IN THE INCOME TAX APPELLATE TRIBUNAL, DELHI 'I-2' BENCH, NEW DELHI

BEFORE SHRI N.K. BILLAIYA, ACCOUNTANT MEMBER, AND SHRI SANDEEP GOSAIN, JUDICIAL MEMBER

ITA No. 2461/DEL/2011
Assessment Year: 2005-06

The AC.I.T Circle - 1, Gurgaon	Vs.	M/s. Comverse Kenan India Pvt. Ltd. [Known as CSG Systems India Pvt Ltd] 2nd Floor DLF Cyber City, Phase – II Gurgaon PAN No.: AABCC 9425 F
(APPELLANT)		(RESPONDENT)

Cross Objection No.213/DEL/2011
(A/o In ITA No.2461/Del/2011)
Assessment Year : 2005-06

M/s. Comverse Kenan India Pvt. Ltd. [Known as CSG Systems India Pvt Ltd] 2nd Floor, DLF Cyber C ty, Phase – II, Gurgaon PAN No.: AABCC 9425 F	Vs.	The A.C.I.T Circle - 1 Gurgaon
(APPELLANT)		(RESPONDENT)

Assessee by : Shri G.C. Srivastava
Shri Parichay Solanki, CA
Shri Suvinay Kumar Dash, Adv

Revenue by : Shri Sandeep Kumar Mishra, Sr DR

Date of hearing : 05/03/2019
Date of Pronouncement : 11/03/2019

ORDER

PER N. K. BILLAIYA, AM:

This appeal by the Revenue and Cross Objection by the assessee are preferred against the order of the Commissioner of Income Tax [Appeals], Panchkula dated 28/02/2011 pertaining to A.Y. 2005-06. The appeal and the cross objection were heard together and are being disposed of by this common order for the sake of convenience and brevity.

2. The substantive grounds of appeal raised by the Revenue are as under:

1. *On the facts and in the circumstances of the case, the Ld. Commissioner of Income Tax (Appeals) has erred in facts and law in deleting the addition of Rs. 1,27,01,985/- made by AO on account of transfer pricing adjustment when the TPO has rightly determined the arm's length price u/s 92CA(3) in respect of international transaction entered into by the assessee during the Financial Year 2004-05. The reliance is placed on the decision of the Ld. ITAT in the case of Serdia Pharmaceuticals (I) Pvt. Ltd. vs ACIT (ITAT - Mumbai).*

2. *On the facts and in the circumstances of the case, the Ld. Commissioner of Income Tax (Appeals) has erred in facts and law in directing the TPO to exclude the two companies, namely (i) L&T Infotech (ii) M/s Thirdware Solution Ltd from the final set of comparables, when TPO has rightly drawn the conclusion that in view of the peculiarity of this case and also keeping in view of the unique nature of transactions involved, the comparables selected are justified and appropriate.*

3. *On the facts and in the circumstances of the case, the Ld. Commissioner of Income Tax (Appeals) has erred in facts and law in holding that working capital adjustment should be allowed on the same lines as given in the Assessment Year 2007-08, when the TPO has rightly drawn the conclusion that the biggest problem about this adjustment is the inability to find out the position of the payables and receivables at the beginning and end of the year. Moreover, the credit terms offered by the comparables are not known. The debtors and creditors shown in the balance sheet of the comparables contain both trade and non-trade creditors. In the absence of a break up, such adjustment cannot be reliable and justified. Similarly, the assumption of prime lending rate as the interest rate applicable for making the working capital adjustment suffers from risks of inaccuracy. There is no scientific way making risk adjustments which is much more difficult and involves more approximation than working capital adjustment"*

3. The Revenue has also raised one additional ground and the same reads as under:

> "On the facts and circumstances of the case, the Ld. CIT(A) erred in not including M/s Infosys as one of the comparable, which was left out by the TPO due to inadvertence, as the above comparable was selected by the assessee itself in the TP Study Report and the assessee never objected to inclusion of the above comparable on ground of functional dissimilarity".

4. The appellant company is a subsidiary of CSG, Netherlands BV and is engaged in the business of providing liaison, technical support and maintenance services to it Associated Enterprises, namely, CSG International Ltd, UK. The international transactions reported by the assessee company are given below:

	Nature of transaction	Method used by Assessee		Value of transaction
		Method	PL1	
1.	Professional Services	TNMM		108,173,851
	Maintenance Services	TNMM		38,090,177
S).	Liaison Services	TNMM		32,191,397
4-	Payment of interest on foreign currency	CUP		541.550
5.	Cross charges by Group entities	...		27.589,985
6.	Cross charges on Group entities	-		5.462.035

5. The transfer pricing approach adopted by the assessee has categorized itself as a professional service provider in the I.T. industry. The CSG Systems International Inc, USA and its wholly owned subsidiaries serve more than 265 service providers in more than 40 countries. In February 2003, CSG India entered into an independent agreement with Bharti Tele-Ventures Ltd to provide support services to enable Bharti to operate its billing system.

6. CSG renders professional services to CSG, UK. The professional services rendered by CSG India entail analysis, configuration, customization, integration, implementation and deployment of billing solutions of CSG, UK. The said services are provided as per the Inter-Company Service Agreement between CSG UK and CSG India.

7. The functions performed by CSG India and CSG UK in relation to the professional services are as follows:

a) Product development;
b) Integration and implementation; and
c) Billing and collection.

8. CSG India also renders liaison services to CSG UK which includes liaising with potential customers and communicating with them about the services and products of CSG UK in India.

9. CSG India also renders maintenance services to CSG UK, which involves warranty related services on behalf of CSG UK., error verification, bypass, big fix assistance in update and new release implementation and help desk services.

10. During the course of transfer pricing assessment proceedings, on examination of FAR analysis conducted by the assessee, the TPO noticed that the assessee company has not selected appropriate comparables to bench mark the international transactions. According to the TPO, entire selection process of the comparables and the comparability analysis is questionable. The TPO observed that FAR analysis carried out by the assessee was also sketchy and no weights had been allocated to functions performed, assets used and risk assumed by the assessee and its AE. According to the TPO, considering the FAR analysis of the assessee, it would be difficult to select the potential comparables as it would not be clear as to what filters are to be applied.

11. The TPO selected the following 19 comparables:

SI.No.	Company Name	Financial Year	Sales	OP to j Total Cost |
1	Bodhtree consulting ltd	200503	3.87	24.85 ;
2	Akshay Software Technologies Limited	200503	5.89	7.72
3	Lanco Global Systems ltd	200503	6.11	13.78
4	Exensvs Software Solutions ltd	200503	7.3	70.68
5	Sankhya Info tech ltd	200503	12.99	27.35
6	Sasken Network Systems Ltd,	200503	14.44	16.64
7	Gebbs Infotech Limited	200503	14.74	16.52
8	V J I L Consulting Ltd	200503	15.6	6.68
9	Four soft ltd	200503	15.94	24.7
10	Thirdware Solution limited	200503	29.11	66.11
11	Geometric Software Solutions Co.ltd	200503	95.44	20.34 |
12	Tata Elxsi Limited (seg) ,	200503	146.46	24.35
13	Visual soft Technolgies ltd (seg)	200503	185.43	23.52
14	Sasken communication Technologies" ltd (seg)	200503	189.05	14.42
15	Flextronics (seg)	200503	457.45	32.19
	L&T Infotech Ltd.,	200503	562.45	11.72
17	Satyam	200503	3464.22	30.31
18	Infosvs	200503	6859.66	43.49
19.	Compulink Systems Ltd		12.86	43.62

12. The TPO proposed the arms' length ratio for the software segment at 27.31%, which was proposed to be used for bench marking of international transactions in the software segment. The Arm's length price was proposed to be determined as under:

Arm's length ratio	27.31%
Total cost Rs	99372436
Arms Length Profit Rs	27138612
Arm's length revenue Rs.	126511048
Book Value of revenue Rs.	108173851
Difference Rs.	18337197

13. The assessee objected to the proposed transfer pricing adjustment, reiterated and justified its transfer pricing method employed in the transfer pricing report and stated that the FAR analysis conducted by the assessee is adequate.

14. In its submissions, the assessee vehemently pointed out that in the fresh analysis carried out by the TPO, the TPO has failed to demonstrate the weight assigned to functions, assets and risks used in the fresh search carried out by the TPO as this seems to be the reason for discarding the comparables chosen by the assessee.

15. It was further pointed out that the turnover filed is not a correct filter in the case of the assessee and objected to the rejection of loss making companies from the set of comparables. It was pointed out that some of the comparables are functionally different and having related party transaction. The use of multiple year data was also objected. The assessee strongly pointed out that working capital adjustments and risk adjustment should be made to the comparables.

16. After considering the submissions of the assessee, the TPO partly accepted the contentions and agreed that the following companies are having related party transactions:

1. Four soft Ltd
2. Geometirid Software Solutions Ltd
3. Tata Elxsi [Seg]
4. Flextroncis [Seg]
5. L & T Infotech Ltd
6. Satyam
7. Compulink Systems Ltd

17. After considering the objections of the assessee, the final set of comparables selected is as follows:

Sl .No.	Company Name	Sales	OP to Total Cost ,
1	Bodhtree consulting ltd	3.87	24.851
9	Akshay Software Technologies Limited	5.89	7.72
3	Lanco Global Systems ltd	6.11	13.78
4	Exensys Software Solutions ltd	7.3	30.36
5	Sankhya Infotech ltd	12.99	27.35
6	Sasken Network Systems ltd	14.44	16.64
7	Gebbs Infotech Limited	14.74	16.52
8	V J 1 L Consulting Ltd	15.6	6.68
9	Thirdware Solution limited	29.11	66.11
10	Visual soft Technologies ltd (seg)	185.43	23.52
11	Sasken communication Technologies ltd(seg)	189.05	14.42
12	L&T Infotech Ltd.,	562.45	11.72
			21.6392 ,

18. Based on the above comparables, the ALP of the international transaction is calculated as under;

Arm's length ratio	*21.64%*
Total cost Rs	*99372436*
Arms Length Profit Rs	*21503400*
Arm's length revenue Rs.	*120875836*
Book Value of revenue Rs.	*108173851*
Difference Rs.	*12701985*

19. The assessee carried the matter before the ld. CIT(A) and strongly objected to the transfer pricing adjustment. It was strongly contended that the TPO has not made working capital adjustments. It was further contended that out of the comparable companies selected by the TPO in his order, one company, namely, Thirdware Solution Ltd has earned operating profit of 66.11% on operating cost and since the company is earning super normal profits, the same should be excluded. In support of this contention, reliance was placed on the following decisions of the Tribunal:

a) Egain Communications Pvt Ltd 118 ITD 243 {Pune]

b) SAP Labs Pvt. Ltd [Bangalore ITAT]

c) Adobe Systems India Pvt Ltd [Delhi ITAT]

20. The assessee pleaded for benefit of working capital adjustment. It was also brought to the notice of the first appellate authority that the TPO has excluded L & T Infotech Ltd being one of the seven

companies having related party transactions and yet in the final set of comparables, the TPO included L & T Infotech as a good comparable.

21. After considering the facts and submissions, the ld. CIT(A) found correctness in the contention of the assessee, in so far as L & T Infotech Ltd is concerned. The ld. CIT(A) accordingly directed to exclude L & T from the list of comparables.

22. In so far as Thirdware Solution Limited is concerned, the ld. CIT(A) was convinced that this company has a super normal profits and following the decision of the co-ordinate bench in the case of Egain Communication Pvt Ltd [supra], directed the TPO for exclusion of Thirdware Solutions Ltd

23. In so far as the benefit of working capital adjustment is concerned, the ld. CIT(A) observed that it is logical to make adjustments on account of working capital of the comparables and found that the only objection of the TPO was with regard to not allowing working capital adjustment is the difficulty in working out such adjustments. However, the ld. CIT(A) found that the working capital adjustment has been made in the case of the assessee for

assessment year 2007-08. Considering this fact, the ld. CIT(A) directed the TPO to give working capital adjustment on the same basis as given in assessment year 2007-08.

24. Before us, the ld. DR strongly supported the findings of the TPO. It is the say of the ld. DR that in his grounds of appeal before the first appellate authority, the assessee has never raised any ground for the inclusion/exclusion of any comparable. Therefore, the first appellate authority has erred in excluding one of the comparables. The ld. DR drew our attention to the annual accounts of Thirdware Solutions Ltd and pointed out that the sales of Rs. 29.11 crores includes software services of Rs. 8 crores, export of Rs. 14.74 crores and the Revenue from subscription of Rs. 3.94 crores. It is the say of the ld. DR that about 90% of the total sales are comprised of these three elements and, therefore, there is no question of any segmental account. The ld. DR further pointed out that super profits cannot be acriteria for exclusion of any comparable. For this proposition, reliance was placed on the decision of the Hon'ble Delhi High Court in the case of Chryscapital Investment Advisors [India] Ltd 56 Taxmann.com 417.

25. In so far as the benefit of working capital is concerned, the ld. DR pointed out that though the FAR has referred to a chart in his order, but no such chart is found and, therefore, the basis of working capital adjustment is not known.

26. The ld. counsel for the assessee vehemently stated that when the assessee challenges the TP adjustment, the inclusion/exclusion of comparables is inherent in the grounds so taken. The counsel strongly contended that Thirdware Solutions Pvt Ltd does not have segmental account and therefore, for want of segmental data, the same cannot be used as a good comparable. It is the say of the ld. counsel for the assessee that in respect of other comparables, segmental data is available and therefore, they are good comparables. The ld. counsel for the assessee further pointed out to Exhibit 271 and 272 of the paper book and stated that the assessee has clearly demonstrated the working capital adjustment and it is incorrect to say that the basis of working capital adjustment has not been provided. It is the say of the ld. counsel for the assessee that this analysis was also before the TPO.

27. Rebutting to the contention of the ld. DR that working capital adjustment cannot be allowed as the assessee is in the service industry, the ld. counsel for the assessee drew our attention to the decision of the co-ordinate bench in the case of Sun Life India Service Centre Private Limited ITA No. 1489/DEL/2014 order dated 28.09.2015 and pointed out that on identical objection, the bench has allowed the working capital adjustment.

28. We have heard the rival submissions and have given thoughtful consideration to the orders of the authorities below. In so far as the first objection of the ld. DR that exclusion of Thirdware Solution Pvt Ltd was not in the grounds of appeal before the first appellate authority does not hold any water because once the assessee challenges the TP adjustment, based upon the comparables, inclusion/exclusion is imbibed in the grounds itself.

29. The Annual Report of Thirdware Solution Pvt Ltd has been carefully examined. As mentioned elsewhere, the sales of this company includes :

a) sale of licence

b) software services

c) export

d) revenue from subscription.

30. However, a perusal of the annual report reveals that there is no segmental reporting. In our understanding of the facts, even if the Revenue from the three services mentioned at b), c) and d) above comprises of 90% of the total sales, still segmental reporting is a must to justify the inclusion of this comparable. Though the first appellate authority has excluded this company on the ground that it has supernormal profits, but that is not a good reason for excluding this company, but having no segmental accounts make this company excluded from the final set of comparables. Though we do not agree with the exclusion on the point of super normal profits, but nevertheless, for want of segmental reporting, we direct for exclusion of this company from the final set of comparables.

31. In so far as L & T is concerned, there is no dispute that the same was excluded by the TPO for related party transactions. Therefore, inclusion of the same in the final set of comparables is uncalled for and deserves to be excluded.

32. Benefit of working capital adjustment has to be given to the assessee since the assessee has filed a detailed working of the working capital adjustment the same cannot be dismissed on the ground that the assessee is in the service industry. The co-ordinate bench in the case of Sun Life India Service Centre Private Limited has held as under:

> "28. We are not inclined to accept the view canvassed by the authorities below that the working capital adjustment cannot be allowed as the assessee is in service industry. Such an adjustment is restricted to inventory, trade receivables and trade payables. If a company carries high trade receivables, it would mean that it is allowing its customers relatively longer period to pay their dues, which will result into higher interest cost and the resultant low net profit. Similarly, by carrying high trade payables, a company benefits from a relatively longer period available to it for paying back the dues to its suppliers, which reduces the interest cost and increases profits. In order to neutralize the differences on account of carrying high or low inventory, trade payables and trade receivables, it becomes eminent to allow working capital adjustment so as to bring the case of the assessee at par with the other functionally comparable entities. We, therefore, agree in principle with the grant of working capital adjustment."

33. Respectfully following the findings of the co-ordinate bench, we direct the TPO to grant working capital adjustment. The assessee is

directed to furnish afresh a detailed working of the working capital adjustment. The TPO is directed to examine the same and decide the issue.

34. Coming to the additional ground raised by the Revenue which states that the ld. CIT(A) erred in not including M/s Infosys as one of the comparables, which was left out by the TPO due to inadvertence.

35. Before us, the ld. DR strongly stated that the assessee itself has included M/s Infosys as a good comparable in its TP study and the TPO inadvertently did not include the same in the list of final set of comparables. It is the say of the ld. DR that erroneously the TPO included L & T Infotech which was excluded by him and instead of including M/s Infosys, the TPO has mentioned L & T Infotech. Being a typographical error, Infosys Ltd should be included.

36. Per contra, the ld. counsel for the assessee vehemently opposed to the admission of this additional ground. It is the say of the ld. counsel for the assessee that if it was erroneous on the part of the TPO/Assessing Officer, the error could have been easily rectified u/s 54 of the Act and if such error is prejudicial to the interest of the

revenue, the same could have been rectified u/s 263 of the Act. Therefore, the plea taken by the Revenue cannot be a matter of additional ground.

37. Having heard the rival contentions, we are of the opinion that merely because of provisions of section 154 or section 263 of the Act were available with the revenue, it cannot preclude revenue to raise additional ground before us. Therefore, additional ground is admitted.

38. A perusal of the TP study shows that the assessee did include M/s Infosys in its list of comparables. The TPO made a fresh search during the TP assessment proceedings and from his fresh search, the TPO excluded certain comparables and made a final list of comparables as mentioned elsewhere. The exercise so done by the TPO does not leave any room for assumption that inadvertently he has not included M/s Infosys in the final set of comparables. On the contrary, it appears that non inclusion was intentional.

39. The plea of the Revenue that the ld. CIT(A) erred in not including M/s Infosys as one of the comparable is ill-founded because the assessee was in appeal before the ld. CIT(A) and since the assessee

had no grievance for non inclusion of M/s Infosys how could the ld. CIT(A) have adjudicated on inclusion of Infosys unless he wanted to exercise his powers of enhancement.

40. Considering from all possible angles, we do not find any merit in the additional ground raised by the Revenue.

41. The ld. counsel for the assessee has not pressed the cross objections. Therefore, the same is dismissed as not pressed.

42. In the result, the appeal of the Revenue as well as the cross objections of the assessee stand dismissed.

The order is pronounced in the open court on 11.03.2019.

Sd/- **Sd/-**

[SANDEEP GOSAIN] [N.K. BILLAIYA]
JUDICIAL MEMBER ACCOUNTANT MEMBER

Dated: 11th March, 2019

VL/

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR

Asst. Registrar,
ITAT, New Delhi

Date of dictation	
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Date on which the typed draft is placed before the Other member	
Date on which the approved draft comes to the Sr.PS/PS	
Date on which the fair order is placed before the Dictating Member for Pronouncement	
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