

**IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH: 'I-1', NEW DELHI**

**BEFORE SHRI H.S. SIDHU, JUDICIAL MEMBER
AND
SHRI O.P. KANT, ACCOUNTANT MEMBER**

ITA No.6979/Del/2017
Assessment Year: 2013-14

M/s. Alcatel-Lucent India Ltd., DLF Cyber Greens, 14 & 15 th Floor, Tower C, Phase-III, DLF City, Gurgaon	Vs.	Addl. CIT, Special Range-1, New Delhi
PAN :AACCA8667N		
(Appellant)		(Respondent)

Appellant by	Shri Deepak Chopra, Adv.; Ms. Manasvini Bajpai, Adv.; & Shri. Ankul Goyal, Adv.
Respondent by	Shri Sanjay I. Bara, CIT(DR)

Date of hearing	03.04.2019
Date of pronouncement	09.05.2019

ORDER

PER O.P. KANT, A.M.:

This is an appeal by the assessee and directed against final assessment order dated 26/10/2017 passed by the Joint Commissioner of Income Tax, Special Range-1, New Delhi [hereinafter referred to as "the Assessing Officer"] for assessment year 2013-14, in conformity with the direction of the Ld. Dispute Resolution Panel (DRP). The grounds of appeal raised by the assessee are reproduced as under:

1. *That on the facts and circumstances of the case and in law, the Ld. AO, has erred in determining the taxable income of the appellant for*

the subject assessment year at Rs. 2,52,89,95,210/- as against the returned income of Rs. 1,11,54,93,650/-.

- 1.1 That on the facts and circumstances of the case and in law, the Ld. AO has erred in proposing several additions based on mere conjunctures and surmises, ignoring the factual matrix of the company as well as the nature of the transactions undertaken by the appellant.
- 1.2 That the Ld. AO failed to appreciate the submissions made/ contentions raised by the appellant and further erred in making several observations and inferences in the impugned assessment order which are factually incorrect and legally untenable.

Transfer Pricing (“TP”) Grounds

2. That, in framing the impugned assessment order, the reference made by the Ld. AO under section 92CA(1) of the Act suffers from jurisdictional error, as the Ld. AO had not recorded any reasons nor he had any material whatsoever on the basis of which he could even reach a prima-facie opinion, that it was ‘necessary or expedient’ to refer the matter to the learned Deputy Commissioner of Income Tax, Transfer Pricing Officer - I(1)(1), New Delhi (hereinafter referred to as “Ld. TPO”) for computation of a m’s length price (“ALP”)
3. That on the fact of the case and in law, the Ld. AO/ Ld. TPO / Hon’ble Dispute Resolution Panel (“Hon’ble DRP”) has erred by not accepting the economic analysis undertaken by the Appellant in accordance with the provisions of the Act read with the Income Tax Rules, 1962 (“the Rules”), and conducting a fresh comparability analysis for the determination of the ALP of the Appellant’s international transactions pertaining to provision of contract software development (“CSD”) services and technical support services (“TSS”) by the Appellant to its associated enterprises (“AEs”) and holding that the said international transactions are not at arm’s length
4. That on the facts and circumstances of the case and in law, the order passed by Ld. AO in pursuance to the directions of the Hon’ble DRP under section 143(3) read with section 144C of the Act, is bad in law and void ab-initio, as it violates the provisions of section 144C(10) r.w.s. 144C(13) of the Act, as the same has been passed in contravention of specific direction of Hon’ble DRP.
 - 4.1 That on the facts and circumstances of the case and in law, the Ld. AO/ Ld. TPO erred in including Allcargo Logistics Limited, HSCC (India) Limited and Certification Engineering International Limited as comparable for the purpose of determining the ALP of the international transaction in relation to provision of TSS since they fail

to qualify the filters applied by Hon'ble DRP and thus should have been rejected in conformity with the directions of Hon'ble DRP;

- 4.2 That on fact and circumstances of the case and in law, the Ld. AO/ Ld. TPO erred in not granting the benefit of working capital adjustment while computing the ALP of the international transaction pertaining to provision of TSS despite the fact that Hon'ble DRP directed the Ld. AO/ Ld. TPO to provide such benefit and the Ld. AO/ Ld. TPO granted such benefit in relation to the international transaction of provision of CSD services;*
- 4.3 That on fact and circumstances of the case and in law, the Ld. AO/ Ld. TPO erred in rejecting Microland Ltd and Desein Private Limited as comparable companies and in not passing a speaking order ,giving reasons, for exclusion of these companies for the purpose of determination of ALP of international transaction of provision of TSS despite specific directions of Hon'ble DRP o that effect;*
- 4.4 That on fact and circumstances of the case and in law, the Ld. AO/ Ld. TPO erred in rejecting Infomile Technologies Limited, Silverline Technologies Limited and Lucid Technologies Limited as comparable companies and in not passing a speaking order, giving reasons, for exclusion of these companies for the purpose of determination of ALP of international transaction of provision of CSD services despite specific directions of Hon'ble DRP to that effect.*
- 5. That on the facts and circumstances of the case and in law, the direction issued by Hon'ble DRP under section 144C (5) of the Act is bad in law and void ab initio since the subject directions direct the Ld. TPO/ Ld. AO to make further enquiuy by requiring the Ld. AO/ Ld. TPO to pass a speaking order in relation to inclusion/ exclusion of companies such as Microland Ltd., Desein Private Ltd, Infomile Te hnologies Ltd, Silverline Technologies Ltd. and Lucid Technologies Limited as comparable, which is in contravention to the provisions Section 144C(8) of the Act.*
- 6. That on the facts of the case and in law, the Ld. TPO / Hon'ble DRP has erred in rejecting the Appellant's claim to use multiple year data for computing the arm's length price and, instead, has adhered to the use of single year updated data to conclude the ALP of the international transaction which was not available to the Appellant at the time of undertaking transfer pricing study required to be maintained under Section 92D of the Act.*
- 7. That on fact of the case and in law, the Ld. TPO/ Hon'ble DRP has erred in application of inappropriate filters based on turnover, different financial year end, service income, export sales and employee cost for identifying companies comparable to the Appellant.*

8. *That on the facts of the case and in law, the Ld. TPO/ Hon'ble DRP has erred in selection of functionally non-comparable companies and rejection of comparable companies, as per provisions of Rule 10B(2), for the purpose of determination of ALP of the international transactions pertaining to provision of CSD services and TSS by the Appellant.*
9. *That on the facts of the case and in law, the Ld. TPO/ Hon'ble DRP has erred in cherry-picking of companies as comparable by selecting those companies as comparable which fail the quantitative filters applied by the Ld. TPO.*
10. *That on facts of the case and in law, the Ld. TPO/ Hon'ble DRP has erred in selecting certain companies which are earning super normal profits as compared to the Appellant.*
11. *That on the facts of the case and in law, the Ld. TPO / Hon'ble DRP has erred in committing certain computational errors while computing operating margin of comparable companies.*
12. *That on the facts of the case and in law, the Ld. TPO has followed an inconsistent approach in not providing for benefit of working capital adjustment while determining ALP of the international transaction in relation to provision of TSS despite the fact that the said benefit had been granted by the Hon'ble DRP in relation to the international transaction of provision of CSD services and TSS.*
13. *That on the fact of the case and in law, the Ld. TPO / Hon'ble DRP has erred in not allowing a risk adjustment to the Assessee on account of the fact that the Appellant is a captive service provider for its associated enterprises and is remunerated on a cost plus basis irrespective of the outcome of the services provided and hence undertakes no market risk, product/ service liability risk, credit risk, capacity utilization risk etc. as against comparable companies that are the full-fledged risk taking entrepreneurs.*

Corporate Tax Grounds

14. *That on the facts and circumstances of the case and in law, the Ld. AO has erred in disallowing the liquidated damages of INR 1,64,00,000/- incurred by the Appellant pursuant to breach of its contractual arrangements on the grounds that the same could not be verified.*
- 14.1 *That the Ld. AO failed to follow the spirit and intent of the directions of the Hon'ble DRP as he failed to appreciate the correct facts and evidences brought on record for verification in accordance with the directions of Hon'ble DRP and further erred in making several allegations, observations and inferences in the assessment order which are both factually incorrect as well as legally untenable.*
15. *That on the facts and circumstances of the case and in law, the Ld. AO has erred in proposing to disallow an amount of Rs. 6,17,20,463/- under Section 37(1) of the Act on account of prior period expenditure.*

- 15.1 That on the facts and circumstances of the case and in law the Ld. AO has erred in summarily rejecting the appellant's contentions and not considering the binding judicial precedents which squarely applies to the facts of the appellant's case.
16. That on the facts and circumstances of the case and in law, the Ld. AO is not justified in making a disallowance of Rs. 28,61,300/- by applying Rule 8D read with Section 14A of the Act, having regard to the accounts of the appellant, without recording his dissatisfaction with respect to correctness of claim made by the appellant that no expenditure has been incurred in relation to earning exempt income during the subject assessment year.
- 16.1 That on the facts and circumstances of the case and in law, the Ld. AO has grossly erred on facts in concluding that the said disallowance be made under section 14A of the Act where own funds have been used by the appellant or making strategic investments in group companies. That the Ld. AO has failed to appreciate that the investments were driven by business rationale and not with an intent of earning dividend income.
- 16.2 That on the facts and circumstances of the case and in law, the Ld. AO grossly erred in making addition under section 14A of the Act without considering the fact that no exempt income has been earned by the appellant during the relevant assessment year.
17. That on the facts and circumstances of the case and in law, the Ld. AO has erred in disallowing an amount of Rs. 44,67,442/- on account of interest expenses under Section 36(l)(iii) of the Act
- 17.4 That on the facts and circumstances of the case and in law, the Ld. AO has erred on the facts and circumstances of the case and in law in summarily rejecting the appellant's arguments, factual submissions and not considering the binding judicial precedents applicable to the facts of the appellant's case.
18. That on the fact and circumstances of the case and in law, the Ld. AO has grossly erred in disallowing an amount of Rs. 76,446/- on account of contribution to labour welfare fund deposited by the appellant after the respective statutory due date but before the filing of return of income for j AY 2013-14, particularly in view of the directions of the Hon'ble DRP directing deletion of the/r said addition.
19. That on the facts and circumstances of the case and in law, the Ld. AO has erred in not allowing set off of brought forward business losses of previous assessment years from the current year's income.
20. That on facts in the circumstances of the case and in law, the Ld. AO has erred in initiating penalty proceedings under section 271(l)(c) of the Act mechanically and without recording any adequate satisfaction for its initiation.
- The Appellant craves leave to add, amend, alter, delete, rescind, forgo or withdraw any of the above grounds of appeal either before or during the hearing before the Hon'ble Tribunal. Further, the aforesaid grounds are mutually exclusive and without prejudice to each other.

2. Briefly stated facts of the case are that the assessee was engaged primarily in distribution and sale of digital switching equipments, cellular exchange equipment and other telecommunication equipment and provision of related services. During the year under consideration, it also provided intra-group marketing, technical support and contract software development services. The assessee filed return of income for the year under consideration on 29/11/2013, declaring total income of Rs.178,69,64,430/-, which was further revised to Rs.111,54,93,650/-, in the revised return of income filed on 12/11/2014. The case was selected for scrutiny and statutory notices were issued and complied with. The Assessing Officer noted the International Transactions carried out by the assessee with Associated Enterprises and accordingly, referred the matter to the learned Transfer Pricing Officer (TPO) for determination of arm's length price of those international transactions. The learned TPO in his order under section 92CA(3) of the Act proposed adjustment of Rs.91,24,40,290/- to the value of the International Transaction. The Assessing Officer in the draft assessment order dated 30/12/2016 included that adjustment proposed by the learned TPO and other additions. Against the draft assessment order, the assessee filed objections before the learned DRP. The learned DRP after considering the objections of the assessee, issued certain directions on 26/09/2017, which resulted in modification of the transfer pricing adjustment to Rs.65,65,05,130/-. The learned DRP also issued directions in respect of the other additions. Pursuant to the direction of the learned DRP, the Assessing Officer passed the final assessment

order in which, he computed the total income of the assessee at Rs.252,89,95,210/-as under:

	<i>Revised return as declared by the assessee</i>	Rs.	111,54,93,650
Add	<i>On account of TPO order in relation to Arm's Length Price of International Transactions (As discussed above)</i>	Rs.	65,65,05,130
Add:	<i>On account of 'Liquidate damages' as per para '7' above</i>	Rs.	1,64,00,000
Add:	<i>On account of "Losses brought forward" as per para '8' above</i>	Rs.	67,14,70,783
Add:	<i>On account of "Prior period expenses" as per para '9' above</i>	Rs.	6,17,20,463
Add:	<i>On account of 'Disallowance u/s 14A r.w.r 8D" as per point 11</i>	Rs.	28,61,300
Add:	<i>On account of "late deposited of Labor Fund" as per point 10</i>	Rs.	76,446
Add:	<i>On account of "Disallowance of proportionate Interest" as per point 12</i>	Rs.	44,67,442
	<i>Total Income</i>	Rs.	2,52,89,95,214
	<i>Rounded off u/s 288</i>	Rs.	2,52,89,95,210

2.1 Aggrieved with the above additions, the assessee is in appeal before the Tribunal raising the grounds as reproduced above. The assessee also filed supplementary grounds on 26/04/2018. In the supplementary grounds, the assessee has actually elaborated ground No.8, specifying the name of comparables sought to be excluded/included as under:

8.1 *The learned AO/ TPO and Hon'ble Dispute Resolution Panel ("DRP"), in particular, erred in selecting Infosys Limited, Larsen and Toubro Infotech Limited (Segmental), Persistent Systems Limited and Mindtree Limited as comparables without appreciating that these companies are not functionally comparable to the Appellant in relation to the international transaction pertaining to provision of contract software development ("CSD") services.*

- 8.2 *The learned AO/ TPO and Hon'ble DRP, in particular, erred in rejecting Cat Technologies Limited, Maveric Systems Limited, Infomile Technologies Limited and Silverline Technologies Limited as comparables selected by the Appellant on account of functional dissimilarity for the purpose of determination of arm's length price ("ALP") of international transaction pertaining to provision of CSD services, KIA.*
- 8.3 *The learned AO/ TPO and Hon'ble DRP, in particular, erred in selecting Allcargo Logistics Limited, HSCC (India) Limited, Mitcon Consultancy & Engineering Services Limited, Holtec Consulting Private Limited, Certification Engineers International Limited and Acropetal Technologies Limited (Segmental) as comparables without appreciating that these companies are not functionally comparable to the Appellant in relation to the international transaction pertaining to provision of technical support services ("TSS").*
- 8.4 *The learned AO/ TPO and Hon'ble DRP, in particular, erred in rejecting Microland Limited (Segmental) and Desein Private Limited as comparables selected by the Appellant for the purpose of determination of ALP of international transaction pertaining to provision of TSS.*

2.2 The supplementary grounds, being extension of the original ground only, the same were admitted.

3. The ground No. 1 of the appeal, being general in nature, was not argued specifically and thus, we are not required to adjudicate upon the same specifically.

4. The grounds no. 2 to 13 including supplementary ground No. 8.1 to 8.4 relates to transfer pricing adjustment of Rs.65,65,05,130/-. In respect of the addition, the Ld. counsel of the assessee before us only raised the issue of exclusion/inclusion of certain comparables specifically raised in supplementary grounds No. 8.1 to 8.4 of the appeal.

4.1 Brief facts qua the addition are that the assessee reported following International transactions:

<i>S. No.</i>	<i>Description of the transactions</i>	<i>Amount (In Rupees)</i>
1.	<i>Provision of services</i>	287735285
2	<i>Provision of software development services</i>	5910299598
8	<i>Other operating revenue</i>	2657900880
4	<i>Reimbursement of expenses</i>	5753365
5	<i>Trade receivable</i>	885415038
6	<i>Purchase of material</i>	1112710682
7	<i>Purchase of fixed assets</i>	323303078
8	<i>Receipt of services</i>	184830
9	<i>Receipt of technical services</i>	281561375
10	<i>Interest paid on ECB loan</i>	4823656
11	<i>Deputation of employee</i>	175987570
12	<i>Trade payables</i>	3765569001

4.2 The Assessing Officer accepted the arm's length price of the transactions except transaction of provision of "Software Development Services" and "Technical Support Services". Under the Software Development service segment, the assessee provided contract software development services to its associated Enterprises. The functions performed were stated to be development/coding, testing, maintenance of support for software development. The AEs provided specifications relating to the assignment to be undertaken by the assessee. The assessee in its transfer pricing study for contract software development (CSD) services provided to the Associated Enterprises (AEs) determine the arm's length price applying Transactional Net Margin Method (TNMM). The Operating Profit to Total Cost (OP/TC) was taken as profit level indicator (PLI) in the TNMM analysis. The "PLI" of the

assessee company was arrived at 7.98 percent, whereas the average PLI of the comparables was arrived at 8.20%. As the average margin of the comparable companies was within the plus minus ($\pm 5\%$) range, the assessee found the price of International transaction declared by it at arm's length price. The assessee after applying various filters over the database like exclusion of companies having software development service income less than rupees one crore, exclusion of companies having revenue from service less than 75% of the total operating revenue, exclusion of the companies having insufficient financial data etc, selected 10 companies as comparable. The Ld. TPO however, rejected certain comparables due to functional dissimilarity etc. reasons and included few comparables to the final list of 14 comparables having average margin of 18.47%. Accordingly, the learned TPO computed adjustment of Rs.57,34,68,890/- to the software development services segment.

4.3 Under the Technical Support Service (TSS) segment, the taxpayer provided support services to its Associated Enterprises (AEs). The services included technical services in the nature of fault ticket generation support with regard to integration, installation, Inter-operator ability testing, on-site installation and development support, service migration etc. Apart from technical services, the taxpayer also provided welcome Centre Service, network engineering and integration services in the technical support service transaction. The assessee shown OP/TC margin of 5.17% and selected 3 comparables. The comparables selected by the assessee were rejected by the learned TPO as being different functional data and proposed 10 comparables having average margin of 27.22%. Accordingly, the learned TPO proposed

adjustment of Rs. 33, 89, 71, 400/-to the transaction of technical support services.

4.4 The learned DRP considered objection of the assessee in respect of the various filters and exclusion inclusion of comparables. The learned DRP under CSD segment retained 12 comparables, the average margins of whom , has been worked out to 13.79% and thus the transfer pricing adjustment under the CSD segment has been accordingly modified to Rs.31,75,33,730/- . Under the TSS segment, the learned DRP directed for retaining of certain comparables and for the remaining comparables directed to verify whether they fails on any of the filters approved by the DRP. In the effect giving order of the learned DRP, the learned TPO retained all the comparables, which were proposed in the draft assessment order.

4.5 Before us, the learned counsel filed a paper-book along with Annual Reports of the companies under comparison and sought to exclude 4 comparables under the CSD segment and 6 comparables under the TSS segment. The arguments of the parties and our decision on the each comparable is discussed as under:

Contract Software Development Segment(CSD)

1. Infosys Ltd

(i) The Ld. counsel of the assessee submitted that the company is functionally dissimilar to the assessee and engaged in providing a wide array of end-to-end services. He submitted that the company is engaged in research and development activities and owns significant intangible assets

and undertakes significant brand building activities. He also submitted that the turnover of the company is 62 times the turnover of the assessee from provision of CSD services. The Ld. counsel submitted that the company earns from dealing in software products and earns income from software licensing as well. The learned counsel also submitted that the company has been rejected in assessee's own case by the Tribunal in assessment year 2011-12 and 2012-13 and the decision of the Tribunal in assessment year 2011-12 has been upheld by the Hon'ble Delhi High Court. He submitted that the DRP in its direction for assessment year 2014-15 has rejected the company is comparable. The learned counsel also relied on number of decisions including decision of the Hon'ble Delhi High Court in the case of Agnity India Technologies Private Limited.(ITA 1204/2011).

(ii) The Ld. DR on the other hand relied on the order of the lower authorities and submitted that the company is functionally similar to the assessee.

(iii) We have heard the rival submissions and perused the relevant material on record. The learned DRP retained the company is comparable holding that research and development activity, owning of intellectual property right and brand building does not effect on the margin of a company. The contention of the Ld. DRP is that when the PLI as OP/TC is taken under TNMM, the effect of brand assets owned will not have impact on margins and the margins will be affected if a PLI like OP/capital employed had been used for comparability. The learned DRP has further relied on the its direction for assessment year 2012-

13. However, the functional dissimilarity has not been examined properly by the learned TPO as well as by the learned DRP. On perusal of page 24, 25,33 42, 57,60,67 and 69 of the paper book of the annual report compendium, we find that company was engaged in dealing software products and earning income from software licensing. Further on perusal of page 63, 81 of the Annual Report we find that there are no segmental result for income from service and sale of products. In absence of any segmental result of service of software development available in the Annual Report of the company, the company cannot be compared at entity level with the contract software development segment of the assessee. Thus, company being functionally dissimilar to the CSD Segment of the assessee, we direct the Ld. AO/TPO to exclude it from the final set of comparables.

2. Larson and Toubro (Infotech) Ltd

(i) The learned counsel submitted that company is engaged in sale of services and products and segment information in relation to service is not available and thus being functionally dissimilar, the company might be excluded. The Ld. counsel also submitted that TPO himself has accepted that the company deals in products. The learned counsel also submitted that the company owns significant intangibles, incurs substantial effort in building and maintaining brand "L & T" and has earned supernormal profit during the year. The learned counsel submitted that company has been rejected by the Tribunal in assessee's own case for assessment year 2011-12 and 2012-13. In

assessment year 2011-12 the decision of the Tribunal has been upheld by the Hon'ble Delhi High Court. Further, the learned counsel submitted that the company has been rejected by the learned DRP in assessment year 2014-15.

(ii) The learned DR, on the other hand, relied on the finding of the lower authorities and submitted that the assessee has not demonstrated as how the ownership of intangibles will impact the profit margin.

(iii) We have heard the rival submissions of the parties. The learned DRP retained the comparable on the ground that the assessee failed to demonstrate or adduce evidence to show that how objections raised regarding the research and development, IP/intangibles ownership has impacted the margins and how it can automatically become the basis for adjustment. The learned DRP also relied on the direction of the DRP for assessment year 2012-13, where the company has been accepted as a valid comparable. But, we find that the lower authorities have not examined properly the functional dissimilarity of the company. The learned DR could not controvert what that the company is engaged in sale of products along with the services. We find that on page 44 of the learned TPO's order, he himself has mentioned that the company was engaged in sales of the the products namely "AccuRUSI" and " Unitrax". Further on perusal of the profit and loss account, we find that operating expenses includes cost of bought out items for resale which amounts to Rs.27,10,89,274/-and there is no separate bifurcations of the revenue from sale of these bought out items. In view of these observations, it is evident that the

revenue of the company declared during the year under consideration include sale of products. As no separate segment of software development being available, the company at entity level, cannot be considered as functionally similar to the CSD Segment of assessee. In view of the functional dissimilarity of the company with the CSD Segment of assessee, we direct the Ld. AO/TPO to exclude the company from the set of the final comparables.

3. Minded Tree Ltd.

(i) The learned counsel submitted that the company is engaged in diverse business activities like IT consulting, data warehousing, product architecture design engineering embedded software, technical support testing and infrastructure management services. He submitted that company is also engaged in providing software delivery platform. He submitted that the company was engaged in research and development activities and owns significant intangibles and has applied for several patents, whereas the assessee is engaged in contract software development at low-level. Accordingly, he submitted that company might be excluded from the set of the final comparables.

(ii) The learned DR, on the other hand, relied on the order of the learned DRP and submitted that under TNMM, broad functional similarity should be seen and a small variation should be ignored as it is difficult to find exact replica of the assessee as comparable. He also submitted that the assessee failed to demonstrate effect of the intangibles on the net margin of the comparable.

(iii) We have heard the rival submissions and perused the relevant material on record. Inclusion of the comparable was not challenged by the assessee before the learned TPO. The assessee first time challenged the inclusion of the company before the learned DRP. The learned DRP on the grounds, firstly, that there is no effect of intangibles and R&D expenses on the margins of the company, secondly, that the broad nature of TNMM would cover a small variation of functions and, thirdly, that not disputed before the TPO, approved the company as one of the valid comparable. However, we find from the pages 434 of the Annual Report compendium that the company offers services which includes IT strategy consulting, data warehousing, business intelligence, technical support, infrastructure management services etc. The relevant part of the director's report is reproduced as under:

"We have developed a comprehensive range of services allowing us to offer end-to-end IT Services to our clients. With delivery centers in India and overseas, we offer IT strategy consulting, application development and maintenance, data warehousing and business intelligence, package implementation, product architecture, design and engineering, embedded software, technical support, testing infrastructure management services etc. to our customers. We believe that our comprehensive portfolio of service offerings helps our customers achieve their key business objectives."

(iii) Further, on perusal of the page 442 of the Annual Report compendium, we find that the company has used expertise in research and development to provide technology consulting services to its customers.

(iv) On page, 480 of the Annual Report compendium under significant accounting policies and notes to account for the

year ended 31/03/2013, the company has been treated as consulting and Implementation Company. The relevant part of the notes to account is reproduced as under:

“Mindtree Limited ('Mindtree' or 'the Company') is an international Information Technology consulting and implementation company that delivers business solutions through global software development. The Company is structured into two business units - Information Technology ('IT') Services and Product Engineering ('PE') Services. IT Services offer consulting and implementation and post production support for customers in manufacturing financial services, travel and leisure and other industries, in the areas of e-business, data warehousing and business intelligence, supply chain management, ERR and maintenance and re-engineering of legacy mainframe applications PE Services provides full life cycle product engineering, professional services and sustained engineering services. It also enables faster product realization by leveraging the expertise in the areas of hardware design, embedded software, middleware and testing and through Mindtree's own IP building blocks in the areas of Bluetooth/VOIP, IVP6, iSCSI and others in datacom, telecom, wireless, storage, industrial automation, avionics, consumer products and computing.”

(v) In view of the above observation, it is evident that the services rendered by the company are not limited to software development, but also are in the field of consulting and technical support, management etc. In our opinion the software development services rendered by the assessee cannot be compared with a whole basket of services of consulting, technical support or management services rendered by the company. As there is no separate segment of software development services available in the financial statement of the company, the company at entity level cannot compare functionally with the CSD Segment of assessee and accordingly, we direct the Ld. AO/TPO to exclude the company from final set of the comparables.

4. Persistent Systems Ltd.

(i) The learned counsel submitted that company earns income from royalty fee and is engaged in development of products. He submitted that Hon'ble Andhra Pradesh High Court in the case of CIT Vs Intoto software India Private Limited (ITA 233 of 2014) has held the company as engaged in both product and development of the software development services and therefore cannot be compared to a software development service provider. The learned counsel submitted that the company incurs significant R&D expenditure which resulted in global patents and the company owns significant intangibles which have either been developed or have been acquired from 3rd parties as part of inorganic growth strategy. The learned counsel also submitted that the company has been rejected by the Tribunal in assessee's own case for assessment year 2011-12 and assessment year 2012-13. The decision of the Tribunal of rejecting the company has been upheld by the Hon'ble Delhi High Court in assessment year 2011-12 . In view of the above, the learned counsel submitted that the company might be excluded from the final set of the comparables.

(ii) The learned DR, on the other hand, relied on the order of the lower authorities and submitted that under that TNMM a small variations in vertical activity might be accepted.

(iii) We have heard the rival submission and perused the relevant material on record. The learned TPO observed that the company delivers services across all stage of the product

life-cycle, which enables them to work with a wide range of customers and allow them to develop, enhance and deploy their customer software products. The learned DRP further relied on the its direction for assessment year 2011-12 and 2012-13, where it has been approved as a valid comparable. As far as direction of the DRP for assessment year 2011-12 and 2012-13 is concerned, the Tribunal has already reversed the finding in the order in ITA No.6586/Del/2015 for assessment year 2011-12 and ITA No. 1112/Del./2017 for assessment year 2012-13. The Tribunal in assessment year 2012-13 held the company as functionally different from the assessee. In the year under consideration, also we find from the pages 214, 222, 302, 345 and 347 of the compendium of the Annual Report that the company has earned income from royalty fee and engaged in development of the products. We are of the view that a company engaged in development of the software products cannot be compared with the assessee who is engaged in contract software development services. Accordingly, we direct the Ld. AO/TPO to exclude the company from the final set of the comparables.

4.6 Now, we take up the companies sought to be excluded by the assessee under Technical Support Service (TSS) segment.

1. All cargo logistic limited

(i) The Ld. counsel submitted before us that the company is engaged in providing integrated logistics solutions and services include multimodal transport operations, inland

container depot, container freight station operations, contract logistics operations and project engineering solutions. The Ld. counsel submitted that the Ld. TPO himself has accepted the company as engaged in providing inbound and outbound consolidation, multicity consolidation, FCL forwarding, airfreight forwarding activities, projects cargo handling and transportation etc. Thus, according to the learned counsel, the company is not functionally similar to the assessee, who is engaged in providing technical support services like installation, testing service migration etc under the technical support service segment. The learned counsel submitted that learned DRP in its direction for assessment year 2014-15 has excluded the company from the final set of the comparables by observing that it is not functionally comparable with the TSS segment of the assessee.

(ii) The Ld. DR, on the other hand, relied on the order of the lower authorities.

(iii) We have heard the rival submission and perused the relevant material on record. The learned DRP directed the learned TPO to verify whether company fails any of the filters approved by the learned DRP, however, the functional dissimilarity was not examined properly by the learned DRP. On perusal of the pages 648, 651, 663, 690 and 720 of the compendium of the Annual Reports, we find that the company is engaged in providing logistic and transport solutions as against the assessee, who has provided technical support services. The company being functionally dissimilar with the TSS segment of the

assessee, we direct the Ld. AO/TPO to exclude the company from the final set of the comparables for TSS segment.

2. HSCC (India) Ltd.

(i) The learned counsel submitted that the company fails to qualify the filter of a ratio of service income to total income being more than 75%, because in the case of the company the said ratio is only 57.92%. Further the learned counsel submitted that learned DRP in its direction for assessment year 2014-15 has excluded the company from final set of the comparables by observing that it is a government undertaking and FAR profile of the company is different from the FAR profile of the TSS segment of the assessee. The learned counsel submitted that 99% of the shares of the company are held in the name of President of India. He further submitted that the company is engaged in providing consultancy services for design and engineering, construction contracts(project management) procurement of medical equipment, drug and pharmaceutical etc for various projects.

(ii) The learned DR, on the other hand, relied on the order of the lower authorities.

(iii) We have heard the rival submission and perused the relevant material on record. In case of the company, the learned TPO has noted that it is engaged in rendering comprehensive range of professional consultancy services in the healthcare and other social sectors in India and abroad. The learned DRP directed to verify whether the

company fails any of the filters approved by the learned DRP. The learned DRP has approved the one of the filter applied by the learned TPO is to exclude the companies whose revenue from service is less than 75% of the total operating revenue. The assessee has before us submitted that service income of the company is Rs.33,79,79,511/- as compared to total income of Rs.58,35,30,945/-, resulting into ratio of the service income to total income at 57.92%. In our opinion, this company is liable to be rejected even pursuant to the direction of the learned DRP. Further we find that the company has already been rejected by Tribunal Delhi bench in the case of Granite services International Private Limited [TS-731-ITAT-2017(Del)-TP] on account of it being a government company. Further we also note that the companies engaged in altogether different kind of services including procurement of medical equipment, drug and pharmaceutical etc, and thus cannot be compared functionally with the TSS segment of the assessee. In view of the above discussion, we direct the Ld. AO/TPO to exclude the company from the final set of the comparables.

3. Mitson Consultancy and Engineering Services Ltd.

(i) The Ld. counsel of the assessee submitted that company derived revenue from consultancy services, vocational and training, banking and financial consultancy, environmental management and engineering, laboratory and wind power generation.

Further, the learned counsel submitted that no separate segment for consultancy services was available and the segment in relation to consultancy services and training consist of revenue from sale of printed course material which cannot be compared to the TSS segment of the assessee. Further, the learned counsel submitted that the company has received grants from government of India to support such operation and need to be excluded on the ground of government assisted company. The learned counsel submitted that the learned DRP for its direction for assessment year 2014-15 has excluded the company from the final set of the comparables by observing that it has received government grant and FAR profile of the company being different from the FAR profile of the TSS segment of the assessee.

(ii) The learned DR, on the other hand, relied on the order of the lower authorities.

(iii) We have heard the rival submission and perused the relevant records including the Annual Report of the company. We find from page 820 of the Annual Report compendium that the company has received capital grant from the Department of Science and Technology, Government of India for export facilities and Centre and for setting up Biotechnology Laboratory. The company has also received a grant from Ministry of Food Processing, Government of India and Technology Development Board, Government of India. The receipt of grant has affected the profit margin of the company and therefore comparing the assessee's margin of TSS

segment would not be a fair comparison. Further, functional profile of the company is evidently different from the functions performed by the assessee under TSS segment. We also note that Ld. DRP in assessment year 2014-15 has directed to exclude the company on the ground of receipt of government grants and FAR profile being different from the assessee. We also note that no appeal has been filed by the Revenue against the said finding of the learned DRP. Thus, in view of the govt. assisted company and functional dissimilarity, the company requires to be excluded. In view of the discussion, we direct the Ld. AO/TPO to exclude the company from the final set of the comparables.

4. Holtec Consulting Private Limited.

(i) The learned counsel submitted that the company is engaged in providing engineering consulting services on an integrated basis and is primarily positioned to service the need of global cement industry. The learned counsel submitted that as per the brochure of the company dated June, 2012, it was engaged in providing consulting services in the nature of engineering, project and construction management, plant operation and maintenance etc, which are highly technical and require highly skilled manpower unlike the technical support service rendered by the assessee. The learned counsel further submitted that as per the said brochure the type of assignment which have been handled by the "Holtec" include site identification, feasibility studies, geological

investigations, performance enhancement studies, waste heat recovery Project, use of alternate fuels etc., which are services being highly technical in nature and cannot be compared with the technical support services rendered by the assessee. He also submitted that the company recognizes revenue on the basis of percentage of completion method whereas the assessee gets reimbursed monthly on cost plus mark-up basis. Accordingly, he submitted that the company needs to be excluded from final set of the comparables.

(ii) The learned DR, on the other hand, submitted that the learned TPO and the DRP has found the company functionally similar under the broad definition of TNMM.

(iii) We have heard the submission of the both the parties on the issue of exclusion of the company. We find from page 873 of the compendium of Annual Reports, that the company is primarily engaged in the business of rendering engineering consultancy services to its clients located in India and abroad. Under the consultancy services, the recipient is advised in carrying out the actual project or task whereas under the technical support services, the assessee itself has executed the task on the project and thus the function of providing consultancy is different from the function of providing technical support services. Thus the company being functionally dissimilar to the assessee, it cannot be compared with the TSS segment of the assessee and accordingly, we direct the Ld. AO / TPO to exclude the company from the final set of the comparables.

5. Certification Engineering International Ltd.

(i) The learned counsel submitted that the company is engaged in certification activities and third-party inspection job, which cannot be compared to the TSS segment of the assessee. The Ld. counsel also submitted that the company is a government company and providing services to government companies and government agencies. The learned counsel submitted that DRP in its direction for A.Y. 2014-15 has rejected HSCC and Mitcon on the ground of being government of India undertaking. He further submitted that the company also fails the related party transactions filter of 25%. The learned counsel submitted that in the case of the company related party transactions are of Rs. 99, 125,330, which are 34.86% of the sales and thus as per the direction of the learned DRP the TPO/AO should have excluded the company from the final set of the comparables.

(ii) The learned DR, on the other hand, relied on the order of the lower authorities.

(iii) We have heard the rival submission of the party and perused the relevant material on record including the Annual Report of the company. We find from the pages 882, 885 and 886 of the compendium of the Annual Reports that the company was engaged in certification activities and third-party inspection job. The function of providing services of certification for safety or energy audit cannot be compared with the function of providing technical support services by the assessee. Further, the

assessee is a subsidiary of Engineers India Ltd, which is a government company. We have already excluded the company HSCC (India.) Ltd from the set of the final comparables on the ground of being a government company. Accordingly, we direct the Ld.AO/TPO to exclude this company from the final set of the comparables.

6. Acropetal Technologies Private Limited.

(i) The learned counsel of the assessee submitted that company earned revenue under 3 segments namely engineering design, information technology services and healthcare. The function of engineering design segment, which has been compared by the learned TPO includes offering concept design product design and development, advance analysis, reliability engineering and value engineering. It also include product quality improvement, idea generation, product tear down, material cost output, product redesign, back-office support to accomplish 2-D drawing, Dada conversion and 3-D modelling. In view of the learned counsel, the function of the engineering design segment of the company are different from the function of technical support services rendered by the assessee to its Associated Enterprises, and thus company being functionally dissimilar, need to be excluded.

(ii) The Ld. DR, on the other hand, referred to the finding of the learned TPO who has found the engineering design segment of the company as comparable to the technical support segment of the assessee. He also supported the

finding of the learned DRP that under the TNMM small variation in verticals are tolerated.

(iii) We have heard the rival submission and perused the relevant material on record. The services rendered by the assessee under the technical support service segment include fault ticket generation support with regard to integration, installation, interoperability testing, on-site installation, update/upgrade etc, which cannot be compared functionally with the services of providing designs or product design and development. In our view, the engineering design segment of the company is functionally dissimilar to the technical support service segment of the assessee. Accordingly, we direct the Ld. AO/TPO to exclude the company from the final set of the comparables.

4.7 In view of our above directions regarding excluding of the comparables, the learned AO/TPO is directed to re-compute the average margin of the final set of the comparables and determine the transfer pricing adjustment for both the segment of Contract Software Development (CSD) and Technical Support Service (TSS). The ground Nos. 4.1 and ground No. 8 (including modified grounds) of the appeal are allowed for statistical purposes. Remaining grounds out of grounds no. 2 to 13 have not been pressed before us, accordingly, we are not adjudicating upon the same and hence, dismissed as infructuous.

5. The ground No. 14 on 14.1 of the appeal relates to disallowing of liquidated damages of Rs.1,64,00,000/- and the ground No. 15 to 15.1 of the appeal relate to disallowance of

Rs.6,17,20,463/- under section 37(1) of the Act on account of prior period expenditure

5.1 Before us, the Ld. counsel of the assessee submitted that issues of liquidated damages and prior paid expenses in assessment year 2012-13 have been remitted back by the Tribunal to the file of the Assessing Officer. Accordingly, he submitted that both the issues in the year under consideration may also be remanded back to the file of the Assessing Officer for deciding a fresh. The learned DR did not controvert the submission of the learned counsel of the assessee.

5.2 We have heard the submission of the party. We find that in the immediately preceding assessment year i.e. 2012-13 the Tribunal in ITA No. 1112/Del/2017 has restored these issue to the file of the Assessing Officer for deciding afresh after considering the additional evidence submitted by the assessee. The relevant finding of the Tribunal is reproduced as under:

“8. We have heard both the parties and perused the material available on record. Since, the additional evidence was not considered the matter in that respect is remanded back to the Assessing Officer relating to the Corporate Tax issue. Thus, Ground no. 12 to 18 are remanded back to the AO/Transfer Pricing Officer for fresh adjudication after taking into account the additional evidence. Needless to say, the assessee be given due opportunity of being heard as per law.”

5.3 In view of the identical facts in the year under consideration, both the issues in dispute of liquidated damages and prior paid expenses are remanded back to the file of the Assessing Officer for deciding afresh. The ground nos. 14 to 14.1 and 15 to 15.1 of the appeal are accordingly allowed for statistical purposes.

6. In ground Nos.16 to 16.2, the assessee has raised issue of disallowance of Rs.28,61,300/- under Rule 8D of Income-tax Rules, 1962 read with section 14A of the Act.

6.1 Before us, the learned counsel of the assessee submitted that no exempt income has been earned by the assessee during the relevant assessment year and thus in view of the decision of the Hon'ble Delhi High Court in the case of Cheminvest Limited reported in 378 ITR 33W (Delhi), no disallowance can be made in the hands of the assessee. The Ld. DR also could not controvert the fact that no exempt income has been earned by the assessee during the year under consideration.

6.3 We have heard the rival submission and perused the relevant record. The Hon'ble Delhi High Court in the case of Cheminvest Ltd (supra) has held as under:

“In the context of the facts enumerated hereinbefore the court answers the question framed by holding that the expression “does not form part of the total income” in section 14A of the Act envisages that there should be an actual receipt of income, which is not includible in the total income, during the relevant previous year for the purpose of disallowing any expenditure incurred in relation to the said income. In other words, section 14A will not apply if no exempt income is received or receivable during the relevant previous year.”

6.4 Since in the instant case, the assessee has not earned any exempt income during the year under consideration, no disallowance can be made under section 14A of the Act, respectfully following the decision of Hon'ble Delhi High Court in the case of Cheminvest Ltd. (supra). The disallowance made by the lower authorities is accordingly deleted. The ground no. 16.2 of the appeal is accordingly allowed. Since the disallowance under

section 14A has already been deleted by us, we are not adjudicating grounds No. 16 and 16.1 of the appeal, being rendered academic only.

7. The ground Nos. 17 on 17.1 of the appeal relate to disallowance of Rs.44,67,442/- on account of interest expenses under section 36(1)(iii) of the Act.

7.1 Before us, the learned counsel of the assessee submitted that identical disallowance made by the Assessing Officer in assessment year, 2014-15 under section 36(1)(iii) for interest-free advance to M/s C-Dot Alcatel Lucent Research Centre Private Limited (CARC), which is a related concern, has been deleted by the learned DRP. He also further submitted that during the year under consideration the amount of loan/advance is appearing only as opening balance. He submitted that in the case of Commissioner of Income Tax Vs. DD Industries Limited (2015) 231 Taxman 0784 (Delhi), the Hon'ble Delhi High Court has held that disallowance under section 36(1)(iii) of the Act cannot be extended to advances given in the assessment year, which are opening balance during the year. Accordingly, he submitted that, disallowance in question might be deleted.

7.2 On the other hand, the learned DR relied on the order of the lower authorities and submitted that the assessee has to establish that loan/advance to the related party has been given for commercial expediency and without establishing this requirement, disallowance cannot be deleted.

7.3 We have heard the rival submissions and perused the relevant material on the record. The Assessing Officer has observed that no interest has been charged on the loans of Rs.1921 lakhs advanced to M/s CARC whereas the assessee has

paid interest charges of Rs.212 lakhs on borrowed capital. According to the Assessing Officer, the assessee failed to justify that the advance was for any commercial expediency or any business benefit has been accrued to the assessee. Accordingly, he made disallowance of proportionate interest expenses of Rs.44,67,442/-. We find that identical question of disallowance under section 36(1)(iii) was before the learned DRP in assessment year 2014-15. The Ld. DRP, after considering the finding of the Ld. AO in draft assessment order and submission of the assessee, deleted the addition observing as under:

“2.6.3 From the draft assessment order it is observed that the AO has simply disallowed interest by imputing the argument that interest should have been charged on the funds/loan given to other parties without making any effort to bring on record sufficient facts so as to establish the nexus between borrowed funds and funds advanced to CARC In fact there is no finding on fact in the draft assessment order, and the addition proposed is simply ad hoc in nature. The submissions of the assessee that the entire funds raised have been deployed in the business of the appellant company and interest paid thereon is justifiable on the grounds of "commercial expediency" and "used for the purpose of Business" has not been controverted by the AO. The Hon'ble Supreme Court in the case of M/s S A Builders v. Limited v. Commissioner of Income-Tax (Appeals) and Another {(2007) 288 ITR 1 (SC)J has observed as under:

“In order to decide whether interest on funds borrowed by the Appellant to give an interest free loan to a sister concern (e.g. a subsidiary of the Appellant) should be allowed as a deduction under section 36(1) (iii) of the Income Tax Act, 1961 one has to enquire whether the loan was given by the Appellant as a measure of commercial expediency. The expression "commercial expediency" is one of wide import and includes such expenditure as a prudent business man incurs for the purpose of business. The expenditure may not have been incurred under any legal obligation, but yet it is allowable as business expenditure if it was incurred on grounds of commercial expediency.

To consider whether one should allow deduction under section 36(1)(iii) of interest paid by the Appellant on amounts borrowed by it for advancing to a sister concern, the authorities and the courts should examine the purpose for which the Appellant advanced the money and what the sister concern did with the money. That the borrowed amount is not utilized by the Appellant in its own business but had been advanced as interest free loan to its sister concern is not relevant. What is relevant is whether the amount was advanced as a measure of commercial expediency and not from the point of view whether the amount was advanced for earning profits.

Once it is established that there was nexus between the expenditure and purpose of the business (which need not necessarily be the business of the Appellant itself) the Revenue cannot justifiably claim to put itself in the arm-chair of the businessman or in the position of the board of directors and assume the role to decide how much is reasonable expenditure having regard to the circumstances of the case. No businessman can be compelled to maximize his profits."

The Hon'ble Supreme Court in the case of M/s Munjal Sales Corporation v. Commissioner of Income Tax and Another [(2008) 298 HR 298(SC)] held as under:

"Under the income-tax Act, 1961, after amendment of the Act by the Finance Act 1992 in order that interest paid on borrowings can be allowed as a deduction in computing the business profits, every Appellant, including a firm, has to establish, in the first instance, that it was allowable under section 36(1)(iii), and in the case of a firm, further that the amount does not exceed the limit fixed by section 40(b)(iv).

Held, however, on the facts, in this case, that since the Appellant had borrowed the moneys from its partners as early as 1991, and the Appellate Tribunal had held that the loans were given by the partners for business purposes and the interest did not exceed 18 per cent per annum simple interest, the Appellant-firm was entitled to deduction of interest on the borrowings for the assessment years 1993-94 to 1997-98.'

Similar view has been followed in the case of Commissioner of Income Tax v. Motor Sales Limited [(2008) 304 ITR 123 (All)], Commissioner of Income-tax Vs Pudukottai Company Pvt. Ltd. [(1972) 84 ITR 788 (Mad)], Chetan Dass Laxman Dass Vs Income Tax Officer {(2002) 122 Taxman 263 (Delhi) (Mag)}, Gujarat Narmada Valley Fertiliser Co. Ltd. Vs Deputy Commissioner of Income Tax [(2000) 108 Taxman 213 (Ahd)(Mag)], Commissioner of Income-Tax vs. Hotel Savera [(1999) 239 ITR 795 (Mad)], Shree Digvijay Cement Co. Ltd. Vs Commissioner of Income-tax, Gujarat- V [(1982) 138 ITR

45 (Guj)], D & H Secheron Electrodes Pvt. Ltd. Vs Commissioner of Income-tax, Bhopal [(1984) 149 ITR 400 (MP)] wherein it has been held that no addition on account imputed interest attributable to allegedly interest free advances is called for and that a nexus is required to exist and be proved between the borrowing and lending of funds.”

7.4 The learned DR accepted that no appeal has been filed against the said directions of the learned DRP for assessment year 2014-15. Thus, in view of the rule of the consistency, being no change in the facts and circumstances in the year under consideration, the disallowance in dispute is directed to be deleted. The ground of the appeal is accordingly allowed.

8. The ground No. 18 of the appeal relate to disallowance of Rs.76,446/- on account of contribution to labour welfare fund. Before us, the parties have agreed that identical question of disallowance was involved in immediately preceding assessment year 2012-13, which has been restored to the file of the learned Assessing Officer for deciding a fresh in accordance with law. Thus, respectfully following the finding of the Tribunal in ITA No. 1112/Del/2017 for assessment year 2012-13 (which we have already reproduced while deciding the ground No. 14 and 15 of this appeal), we restore this issue to the file of the Ld. Assessing Officer for deciding afresh in accordance with law. The ground of the appeal is accordingly allowed for statistical purposes.

9. The ground no. 19 of the appeal relate to allowing set off of brought forward business losses of the earlier years. We find that this is the issue of the examination of the claim of the assessee and verification of the updated position of the same by the Assessing Officer, thus, we feel it appropriate to restore this issue

also to the file of the Assessing Officer for examining and verification of the claim of the set off of brought forward business losses and allow the same in accordance with law.

10. In ground no. 20 of the appeal, the assessee is aggrieved with initiation of the penalty proceeding under section 271(1)(c) of the Act. As penalty has not been levied in impugned order by the lower authorities, the issue in dispute is premature at this stage and, thus, we dismiss the same as infructuous.

11. In the result, the appeal of the assessee is allowed partly for statistical purposes.

Order is pronounced in the open court on 9th May, 2019.

**Sd/-
[H.S. SIDHU]
JUDICIAL MEMBER**

**Sd/-
[O.P. KANT]
ACCOUNTANT MEMBER**

Dated: 9th May, 2019.

RK/-[d.t.d.s]

Copy forwarded to:

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

Asst. Registrar, ITAT, New Delhi