

IN THE INCOME TAX APPELLATE TRIBUNAL  
DELHI BENCHES : I-1 : NEW DELHI

BEFORE SHRI R.S. SYAL, VICE PRESIDENT  
AND  
MS SUCHITRA KAMBLE, JUDICIAL MEMBER

ITA No.7034/Del/2017  
Assessment Year : 2013-14

Pitney Bowes Software India  
Pvt. Ltd.,  
709-710, Ansal Chambers,  
Bhikaji Cama Place,  
New Delhi.  
PAN: AAECM9134E

Vs. Addl. CIT,  
Special Range-7,  
New Delhi.

(Appellant)

(Respondent)

Assessee By : Shri Neeraj Jain, Advocate,  
Shri Ramit Katyal, CA

Department By : Shri Sanjay I. Bara, CIT, DR

Date of Hearing : 12.03.2018

Date of Pronouncement : 13.03.2018

ORDER

PER R.S. SYAL, VP:

This appeal filed by the assessee is directed against the final assessment order dated 31.10.2017 passed by the Assessing Officer (A.O.)

u/s 143(3) read with section 144C of the Income-tax Act, 1961 (hereinafter also called 'the Act') in relation to the assessment year 2013-14.

2. The first issue raised in this appeal is against the addition on account of transfer pricing adjustment of Rs.104,57,16,656/- in the international transaction of 'Provision of software development services.'

3. Briefly stated, the facts of this issue are that the assessee is a company incorporated in India, which is subsidiary of Pitney Bowes Software Inc., USA. It is engaged in the business of providing end-to-end business solutions in location intelligence which combines technology, data and services with domain expertise to enable an organization to measure, compare, visualize its business data. The assessee reported, *inter alia*, an international transaction of 'Provision of software development services' amounting to Rs.109,01,74,781/-. The Assessing Officer referred the matter of determination of the arm's length price (ALP) of the international transactions to the Transfer Pricing Officer (TPO). The TPO observed that the assessee employed the Transactional Net Margin Method (TNMM) for benchmarking its international transaction of Provision of

software development services. The assessee declared its Profit Level Indicator (PLI) of Operating Profit/Total Cost (OP/TC) at 9.38%, which was compared with the average margin of seven comparables at 13.33%. That is how, the assessee tried to demonstrate that its international transaction was at ALP. The TPO made certain changes in the list of comparables making the number of comparables at 13 and their average PLI was worked out at 19.02%. This led to a transfer pricing adjustment of Rs.13,75,72,821/-. After considering the directions from the Dispute Resolution Panel (DRP), the AO finally made an addition of Rs.10,45,71,656/- on account of transfer pricing adjustment in the international transaction of 'Provision of software development services.' The assessee is aggrieved against the addition of Rs.10.45 crore.

4. We have heard both the sides and perused the relevant material on record. The assessee adopted TNMM as the most appropriate method *qua* the international transaction of 'Provision of software development services', which has not been disturbed by the TPO. Two issues raised before us in this regard are against not allowing working capital

adjustment and inclusion of Larsen & Toubro Infotech Ltd. (Seg.) in the final set of comparables.

5. In so far as the non-granting of working capital adjustment is concerned, it is seen that in the immediately preceding assessment year, the Tribunal had an occasion to consider this argument for grant of working capital adjustment. Vide order dated 18.02.2015 (ITA No.679/Del/2014), a copy of which is placed on record, the Tribunal directed to grant the working capital adjustment and, accordingly, remitted the matter to the file of TPO/A.O. for doing the needful. The Revenue assailed this order before the Hon'ble High Court. Vide judgment dated 28.09.2015, the Hon'ble High Court has decided the issue in favour of the assessee by holding that no substantial question of law arises from the Tribunal order. The ld. DR admitted that the facts and circumstances of the instant year are *mutatis mutandis* similar to those of the preceding year. Respectfully following the precedent, we direct to grant the working capital adjustment and, accordingly, remit the matter to the file of A.O./TPO for granting such adjustment in the light of the directions given

by the Tribunal in the preceding year. Needless to say, the assessee will be allowed a reasonable opportunity of being heard in such proceedings.

6. The only other issue in relation to the international transaction of 'Provision of software development services' is the inclusion of Larsen & Toubro Infotech Ltd.(Seg.). The assessee raised objection against the inclusion of this company before the TPO by contending that it was functionally not comparable and was also having high turnover. The TPO rejected the assessee's contention and proceeded to include 'Industrial cluster segment' of this company for the purpose of comparability. In this regard, it was observed that this company reported three segments viz., Service clusters, Industrial clusters and Telecom clusters. The TPO considered only the Industrial cluster as the relevant segment for the purpose of comparison, whose OP/OC was computed as under :-

Particulars	Industrial Cluster
Revenue	16,380,087,222
Expense	11,384,705,358
Profit	4,995,381,864
OP/OC	43.88%

7. Operating profit rate of L&T Infotech Ltd. (segment) at 43.88% was considered for computing the average margin of comparables for the purpose of making transfer pricing adjustment in this international transaction.

8. The Id. AR contended before us that while computing OP/OC of the relevant segment of L&T Infotech Ltd., the TPO did not consider 'Unallocated expenses' to the relevant segment. We have gone through the Annual report of this company, whose copy is placed at page 73 onwards of the paper book. It can be seen from page 101 of the paper book that this company has reported revenues from three segments and the revenue from Industrial cluster segment is Rs.1638,00,87,222/-, as has been rightly adopted by the TPO. The next item on page 101 under the Industrial Cluster segment is segmental operating profit of Rs.527,75,53,809/-. If we exclude segmental operating profit from the segmental revenue, the amount of the 'Operating costs' comes to Rs.1111 crore and odd. As against this figure, the TPO has taken operating expenses at Rs.1138/- crore and odd. Thus, there is difference of Rs.27 crore and odd between the two figures. In the same Table on page 101 of

the paper book, this company has shown the amount of 'Unallocable expenses' under the head 'Total' at Rs.225.73 crore. In addition, there are items of Depreciation and Amortization of intangible assets. These two items of Depreciation and Amortization of intangible assets when apportioned on the basis of revenue from the Industrial cluster vis-à-vis total revenue, give the figure of Rs.27 crore to match with the figure of total Operating expenses taken by the TPO at Rs.1138 crore. Thus, it is clear that in computing the operating profit from the Industrial cluster segment, the TPO, firstly, allocated Depreciation and Amortization of intangible assets on the basis of gross revenue and not the actuals of this segment and secondly, excluded 'Unallocable expenses' of Rs.225.73 crore altogether.

9. Unallocated expenses obviously comprise several items of expenses of distinct nature and hence there cannot be a uniform key of apportionment. For example, 'Rent' paid by an assessee cannot be bifurcated on the basis of revenue from different segments, such as, Manufacturing, Trading and services. The extent of area used by each business segment varies as per the nature of transaction, which may have

no relation with the gross revenue. For example, a manufacturing unit will need relatively more area than a trading unit. Similarly, a service unit will need still lesser area. In such circumstances, apportioning common Rent expenditure on the basis of gross revenue from such varied divisions, will give skewed results of segment profitability. Similarly, contribution of various segments to other items of expenses varies depending upon the nature of transaction, extent of capital and labour required etc. etc. So all common expenses cannot be apportioned in the ratio of gross revenue from different segments, each having its own separate features and characteristics. One can logically make allocation depending upon the nature of expenditure and appropriate allocation key.

10. Adverting to the facts of the instant case, we find that firstly, the TPO did not allocate 'Unallocable expenses', which are necessary ingredient of 'Operating costs', without which correct amount of operating profits cannot be ascertained. Secondly, neither the nature of common unallocated expenses is known nor the information concerning the appropriate allocation keys is available. Under such circumstances, the very inclusion of Larsen & Toubro Infotech Ltd. (Seg.) in the list of



comparables vitiates the comparability. The Delhi Bench of the Tribunal in CEVA Freight India Private Limited. (ITA No.4956/Del/2013), vide its order dated 18.01.2012, has directed the exclusion of a company in similar circumstances which also had certain unallocable expenses, not capable of proper allocation.

11. Be that as it may, the Id. AR has placed on record a calculation in which 'Unallocable expenses' of Larsen & Toubro Infotech Ltd., have been apportioned on the basis of gross revenue, which gives segmental profit rate of the Industrial cluster segment of L& T at 34.9%. The Id. AR contended that even if the segment of L&T is included with this amended profit rate, its margin will be within the permissible range. Since we have held, in principle, that a company with 'Unallocable expenses', in the absence of the availability of nature of expenses and proper allocation keys, has to be excluded at the threshold, there is no need for examining the apportionment of 'Unallocable expenses' as put forth by the Id. AR. We, therefore, direct to exclude Larsen & Toubro Infotech Ltd. (Seg.) from the list of comparables.

12. The only other issue raised in this appeal is against the transfer pricing adjustment of Rs.11,57,791/- on account of Interest on delay in realization of receivables from the Associated enterprises (AEs).

13. Briefly stated, the facts of this ground are that the TPO noted on page 53 of his order that the invoices from the AEs were realized late. Considering a period of 30 days as a grace period for realization of invoices, he went on to compute a transfer pricing adjustment of Rs.11,57,791/- on account of interest on receivables. No relief was allowed by the DRP, which resulted into an addition of equal amount in the final assessment order.

14. After hearing the rival submissions and perusing the relevant material on record, it is noticed that the assessee argued before the TPO that interest on receivables is not an international transaction. At this stage, it would be apposite to note that the Finance Act, 2012 has inserted Explanation to section 92B with retrospective effect from 1.4.2002. Clause (i) of this Explanation, which is otherwise also for removal of doubts, gives meaning to the expression 'international transaction' in an

inclusive manner. Sub-clause (c) of clause (i) of this Explanation, which is relevant for our purpose, provides as under :-

Explanation.—For the removal of doubts, it is hereby clarified that—

(i) the expression "international transaction" shall include—

(a) .....

(b) .....

(c) *capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;....*'

15. On going through the relevant part of the Explanation inserted with retrospective effect from 1.4.2002, thereby also covering the assessment year under consideration, there remains no doubt that apart from any long-term or short-term lending or borrowing etc. or any type of advance payments or deferred payments, '*any other debt arising during the course of business*' has also been expressly recognized as an international transaction. That being so, the payment/non-payment of interest or receipt/non-receipt of interest on the loans accepted or allowed in the circumstances as mentioned in this clause of the *Explanation*, also become international transaction, requiring the determination of the ALP. If

payment of interest is excessive or there is no or low receipt of interest, then such interest expense/income need to be brought to its ALP. The expression '*debt arising during the course of business*' in common parlance encompasses, *inter alia*, any trading debt arising from the sale of goods or services rendered in the course of carrying on the business. Once any debt arising during the course of business has been ordained by the legislature as an international transaction, it is, but, natural that if there is any delay in the realization of debts arising during the course of business, it is liable to be visited with the TP adjustment on account of interest income short charged or uncharged. Under such circumstances, the contention taken by the assessee before the TPO that it is not an international transaction, turns out to be bereft of any force.

16. The Hon'ble Bombay High Court in the case of *CIT vs. Patni Computer Systems Ltd.*, (2013) 215 Taxmann 108 (Bom.) dealt, *inter alia*, with the following question of law:-

“(c) Whether on the facts and circumstances of the case and in law, the Tribunal did not err in holding that *the loss suffered by the assessee by allowing excess period of credit to the associated enterprises without charging an interest* during such credit period would not amount to international transaction whereas section 92B(1) of the Income-tax Act,

1961 refers to any other transaction having a bearing on the profits, income, losses or assets of such enterprises?”

17. While answering the above question, the Hon’ble High Court noticed that an amendment to section 92B has been carried out by the Finance Act, 2012 with retrospective effect from 1.4.2002. Setting aside the view taken by the Tribunal, the Hon’ble High Court restored this issue to the file of the Tribunal for fresh decision in the light of the legislative amendment.

18. The foregoing discussion divulges that non-charging or under-charging of interest on the excess period of credit allowed to the AE for the realization of invoices amounts to an international transaction and the ALP of such an international transaction is required to be determined.

19. Now, we come to the computation of the ALP of the international transaction of debts arising during the course of business. The TPO has calculated TP adjustment on account of interest on outstanding debts beyond a period of 30 days by noting the number of days after which the relevant invoices were realized. The Id. AR did not dispute the correctness of the period of 30 days allowed by the TPO. He, however, contended that

in none of the cases, the assessee realized invoices beyond 30 days from its AEs. He submitted that the TPO inadvertently considered realization from non-AE transactions for the purpose of determination of transfer pricing adjustment. A chart has been placed on record which shows the dates of realization of invoices. Since such details were not before the TPO who proceeded to compute the amount of transfer pricing adjustment by considering realization beyond 30 days, which is not a correct factual position as per the Id. AR, we deem it fit to set aside the impugned order on this score and remit the matter to the file of A.O./TPO for considering the assessee's contention and then deciding this issue afresh as per law, after allowing a reasonable opportunity of being heard to the assessee.

20. To sum up, the determination of ALP and the consequential addition on account of transfer pricing adjustments in respect of the international transactions of 'Provision of software development services' and 'Interest receivables' is sent back to the file of A.O./TPO for doing it afresh in accordance with our above guidelines after allowing a reasonable opportunity of being heard to the assessee.

21. In the result, the appeal is allowed for statistical purposes.

The order pronounced in the open court on 13.03.2018.

Sd/-

[SUCHITRA KAMBLE]  
JUDICIAL MEMBER

Sd/-

[R.S. SYAL]  
VICE PRESIDENT

Dated, 13<sup>th</sup> March, 2018.

dk

Copy forwarded to:

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

AR, ITAT, NEW DELHI.