IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "I-2", NEW DELHI
BEFORE SHRI N.K. SAINI, ACCOUNTANT MEMBER
AND
SHRI KUL BHARAT, JUDICIAL MEMBER
I.T.A. Nos. 1028 & 7180/Del//2017
A.Yrs. : 2012-13 & 2013-14

M/S BIRLASOFT (INDIA) LTD., BIRLA TOWER, 8TH FLOOR, 25, BARAKHAMBA ROAD, NEW DELHI – 110 001 (PAN: AAACB2769E) **(Appellant)**	vs.	ASSTT. COMMISSIONER OF INCOME TAX, Circle-5(1), New Delhi **(Respondent)**

Assessee by	:	Sh. Ajay Vohra, Sr. Adv., Sh. Neeraj Jain, Adv., Sh. Abhishek Aggarwal, CA
Department by	:	Sh. H.K. Choudhary, CIT(DR)

ORDER

PER KUL BHARAT : JM

These two appeals by the Assessee are directed against the impugned Orders dated 16.01.2017 & 26.10.2017 passed by the AO u/s. 143(3) read with section 144C of the Income-tax Act, 1961 (for short 'the Act') in consonance with the orders passed by the Ld. DRP/TPO qua the assessment years 2012-13 & 2013-14 respectively. Since the issues are common and connected, these are being

consolidated and disposed of by this common order for the sake of convenience, by first dealing with assessment year 2012-13.

2. The Assessee has raised the following grounds in respect of assessment year 2012-13:-

> *1. That the assessing officer erred on facts and in law in completing the assessment under section 144C read with section 143(3) of the Income-tax Act (the Act) at income of Rs. Nil after adjusting brought forward business losses of Rs. 54,37,55,822, as against returned income of Rs. Nil after setting off of brought forward losses of Rs. 4,87,99,289.*
>
> *2. That the assessing officer erred on facts and in law in making adjustment of Rs. 48,29,39,813 to the income of the appellant on account of the alleged difference in the arm's length price of the international transaction of provision of software development services undertaken during the previous year on the basis of order passed by Transfer Pricing Officer ('TPO') under section 92CA(3) of the Act.*
>
> *2.1 That the Dispute Resolution Panel ('DRP')/TPO erred on facts and in law in disregarding the internal benchmarking undertaken by the appellant for determining the arm's length price of the international transactions, applying TNMM, holding that:*

(i) the appellant did not maintain segmental accounts for the related and non-related transactions and there was no segregation of these activities in the audited financials.

(ii) in the segmental accounts prepared by the appellant, expenses which cannot be directly allocated are apportioned on the basis of respective turnover and is not reliable at all.

(iii) The segmental accounts were created by the assessee artificially.

(iv) that the characteristics of services transferred, functions performed, asset employed and risk assumed by assessee in providing services to related and unrelated party are different.

2.2 That the DRP/ TPO erred on facts and in law in holding that the internal comparability does not provide meaningful benchmarking, even after accepting that, FAR of the segments are identical and concurrent transactions of both the segments are homogeneous.

2.3 That the DRP/ TPO erred on facts and in law in disregarding the internal benchmarking analysis applying TNMM undertaken by the appellant, without pointing out any error or mistake in the segmental profitability in relation to revenue earned from AE

and non AEs transactions worked out by the appellant and also certified by independent Chartered Accountants.

2.4 Without prejudice, while benchmarking the international transaction of provision of software development services with external comparables, the DRP/ TPO erred on facts and in law in considering the following companies which does not pass comparability criteria provided under Rule 10B(2) of the Income Tax Rules:

i. Acropetal Technologies Limited

ii. Infosys Ltd.

iii. Larsen & Toubro Infotech Limited

iv. Minditree Limited

v. Persistent Systems & Solutions Limited

vi. Spry Resources Pvt. Limited

vii. Zylog System Limited.

2.5 That on the facts and in the circumstances of the case and in law, the DRP/ TPO erred in rejecting the contention of the appellant regarding risk adjustment, allegedly holding that in absence of robust and reliable data, both for the assessee and for the comparables,

risk adjustment cannot be considered for enhancing comparability.

2.6 Without prejudice, that the assessing officer/TPO erred on facts and in law in not giving effect to the direction of the DRP to restrict adjustment in the arm's length price of international transaction of software development services only to the international transaction undertaken with the associated enterprise and not to the entire turnover of the appellant.

3. That the assessing officer/ DRP erred on facts and in law in making an ad-hoc disallowance of interest expenses of Rs. 1,20,16,720 allegedly holding that the interest paid on short term loans which are invested in acquisition of fixed assets shall be capitalized along with the fixed assets.

3.1 That the assessing officer/ DRP erred on facts and in law in not appreciating that the fixed assets were acquired by the assessee out of its own funds and accordingly, no interest expenses shall be aggregated with the value of fixed assets.

3.2 That the assessing officer erred on facts and in law in not appreciating that interest on amounts borrowed in connection with acquisition of an asset to the extent relatable to the period after such asset is

first put to use, cannot be capitalized and treated as part of actual cost of such asset.

3.3 Without prejudice, the assessing officer/ DRP erred on facts and in law in allegedly considering the interest rate at 15% on the short term loans for the purpose of computing the interest to be capitalized.

3.4 Without prejudice the assessing officer/ DRP erred on facts and in law in not allowing depreciation on the increased cost of acquisition / written down value of such asset after including interest expenses of Rs. 1,20,16,720.

4 That the assessing officer erred on facts and in law in levying interest under Section 234B and Section 234C of the Act.

The appellant craves leave to add, alter, appeal before or at the time of hearing.

3. Ground no. 1 is general in nature, hence, needs no separate adjudication.

4. Apropos ground nos. 2 to 2.6 relating to TP adjustment amounting to Rs. 48,29,39,813/- in respect of international transaction of provision of software development services.

4.1 At the threshold, Ld. Counsel for the Assessee reiterated the submissions made before the Ld. DRP/TPO and submitted that identical issue came up before the Tribunal in the assessment year

2007-08 in assessee's own case and the Tribunal has set aside the matter to the TPO and the TPO has accepted the segmental profitability by deleting the adjustment made in the original transfer pricing order. He drew our attention towards TPO's order placed in File at page no. 115 & 121 and submitted that in the present year i.e. 2012-13, the AO/TPO has adopted the wrong margin i.e. OP/OC at -8.08% whereas the margin in the above segment has been computed at -7.80%. He further submitted that there is no reason assigned for rejecting the internal TNMM method. He further submitted that the method of TNMM has been accepted in earlier years by this Tribunal. Even the TPO itself has observed that the internal comparables are preferable over use of external comparables however their usage is also subject to restrictions. Ld. Counsel of the assessee has taken us through the earlier order of the Tribunal pertaining to assessment year 2007-08 and submitted that similar issue travelled upto the stage of Hon'ble Delhi High Court and the Hon'ble Delhi High Court in ITA No. 44/2018 (Page no. 45-46 PB) vide order dated 15.04.2015 has ruled that ITAT's reasoning is in accord with Rule 10B(1)(e)(ii) of the Income Tax Rules. Ld. Counsel of the assessee further taken us through the Tribunal's order in assessee's own case passed in ITA No. 4776/Del/2011 (AY 2007-08) (Page no. 47 – 66 PB) and further decision of the Tribunal in Assessment Year (2008-09) passed in ITA No. 284/Del/2013 (Page No. 70-98 PB) and stated that similar issue has been restored to the AO for fresh computation.

4.2 On the other hand, Ld. CIT(DR) supported the order of the AO/TPO.

4.3 We have heard the rival contentions and perused the records. We find that the TPO/AO has rejected the internal TNMM Method, but the Hon'ble Delhi High Court vide its order dated 15.04.2015 passed in ITA No. 44/2015 has affirmed the view of the Tribunal in Assessment Year 2009-10 by observing as under:-

> *"The second question is whether the adjustment directed by the AO/TPO ultimately set aside by the ITAT, with respect to the profits margin derived by the assessee in regard to its transactions with the associated enterprise could have been subjected to adjustment. The ITAT was of the opinion that since the assessee was a service provider to its associated enterprise (AE) as well as other foreign customers or non-AEs, the suggestion that the non-AE transactions which reported lower margins and to be used for bench marking the AE transactions were acceptable. The adjustment was not called for. This Court sees no reason to interfere firstly because the ITAT's order has become final. Furthermore, the ITAT's reasoning is in accord with Rule 10B(1)(e)(ii) of the Income Tax Rules. This question does not arise for consideration."*

4.3.1 We further note that the Tribunal in assessee's own case for the assessment year 2008-09 has given the directions to the AO/TPO as under:-

"13. We find that in AY 2007-08 Tribunal has observed in para 4 as under:-

4." We have heard both the parties and gone through the facts of the case as also the aforesaid decision dated 20th January, 2011 of the ITAT for the AY 2006-07. We find that the ITAT in the preceding assessment year concluded that the assessee was justified in undertaking internal bench marking analysis on standalone basis by placing on record working of operating profit margin from international transactions with AEs and transactions with unrelated parties undertaken in similar functional and economic scenario, and the same should be the basis for determination of arms's length price in respect of international transactions undertaken with the associated enterprise. It was further concluded that the TPO had no mandate to have recourse to external comparables when in the present case, internal comparables were available, which could be applied for determining the arm's length price of international transactions with AEs. Accordingly, the ITAT directed the AO/TPO to determine arm's length price of international transactions with AEs by making internal comparison of the net margin earned by the assessee from the

international transactions with associated enterprises and the profit earned by the assessee from the international transactions with unrelated parties. For this purpose, the ITAT restored the matter back to the file of the AO/TPO for fresh adjudication and for the purpose of determining the arm's length price in respect of the international transactions undertaken with the associated enterprise by making internal comparison of profitability from the international transactions with unrelated parties after allocating respective revenues and expenses to both the segmental. The AO/TPO were directed to provide reasonable opportunity of being heard to the assessee while the assessee was directed to furnish all the details and particulars to enable the AO/TPO to make internal comparison of the profitability from the internal transactions with associated enterprise and unrelated parties undertaken by the assessee in the similar functional and economic growth."

14. *There is no dispute that the facts and circumstances in the present assessment year are similar to the facts and circumstances as obtaining in the preceding assessment years. The revenue has not placed before us any*

material so as to enable us to take a different view in the matter. In view of these facts and circumstances, respectfully following the order for earlier assessment years noted above, we restore this matter to the file of the AO/TPO with similar directions as have been given by the ITAT in the preceding assessment year."

4.3.2 Since the facts of the year under consideration are similar to the facts involved in the assessment year 2008-09, therefore, respectfully following the precedent as referred above, the ground no. 2 to 2.7 are restored to the file of the AO/TPO with the similar directions as have been given by the ITAT in assessment year 2008-09 (Supra). In the result, the ground is allowed for statistical purposes.

5. Apropos ground nos 3 to 3.4 relating to adhoc disallowance of interest expenses of Rs. 1,20,16,720/-.

5.1 Ld. Counsel for the Assessee submitted that identical issue came up before the Tribunal in the assessment year 2009-10 in assessee's own case passed in ITA No. 1572/Del/2014 and the Tribunal has set aside the matter to the TPO and in this behalf he drew our attention towards Tribunal's order placed at page no. 115 & 116 of the PB and requested that similar directions may also be passed in this year under consideration by following the earlier decision of the Tribunal, as referred above.

5.2 Ld. CIT(DR) conceded the facts that the issue was earlier decided by the Tribunal by restoring the issue to the AO.

5.3 We have heard the rival contentions and perused the records. We find that Tribunal in assessee's own case for the assessment year 2009-10 has given the directions to the AO/TPO as under:-

> *"36. It may be taken note that Interest on capital borrowed even for acquisition of assets is eligible for deduction as per Sect 36{i)(iii) of the Act. Subsequently a proviso has been inserted by the Finance Act 2003. April], 2004 relating to Assessment Year 2004-05 and subsequent years. Hence the said proviso will apply to the present Assessment Year provided the assessee's case falls under it. In terms of section 36(l)(iii) of the Act, deduction is allowed in respect of interest on capital borrowed for the purpose of business or profession. In terms of the proviso to said section, no deduction, however, is allowed in respect of capital borrowed for acquisition of an asset for extension of existing business or profession for the period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first-put to-use. A reading of section 36(1)(iii) mandates that only interest for the period between the date of borrowing to the date of put to use is to be capitalized as part of actual cost of asset. In other words, no interest is required to be capitalized for the period after such assets are put to use. Therefore the interest expenditure on the utilization of borrowed funds for the acquisition of new*

assets, from the date of its acquisition till the date when, the asset is put to use, is to be disallowed. In-other words, the interest paid on the capital borrowed for acquisition of an asset for extension- of-existing business, shall not be allowed, as deduction, from the date on which the capital was borrowed for acquisition of the asset till the date on which the asset was first put to use.

37. Here admittedly an amount of Rs.11.7 crore was borrowed for acquisition of assets for expansion of existing business; therefore the interest accrued on the borrowed fund from the date on which the capital was borrowed for acquisition of the asset till the date on which the asset was put to use shall be disallowed. Therefore in order to apply the proviso to Section 36(l)(iii) of the Act to the facts of the present case, that is in other words, before disallowing the interest expenditure on the Fund borrowed for procurement of asset for extension of existing business, the AO has to record as a matter of fact the date on which the assessee borrowed the fund for acquisition of asset for extension of business and the date on which the asset thus procured was put to use is absolutely necessary. However in the instant case, we find that no such exercise has been done by the AO to find out the date on which the assessee borrowed the fund for acquisition of asset in the relevant AY and we also find

that no attempt has been made by the AO to find out on which date the asset thus procured with the said borrowed fund have been put to use. Only after the dates as afore-stated has been found out then only one can compute the disallowance as prescribed by the proviso to section 36(1)(ii) of the Act. In the said circumstances we set aside the impugned order on this issue and remand this issue back to the file of AO, with a direction to AO to find out the date on which the assessee borrowed the fund for acquisition of asset and also to find out on which date the asset for extension of business thus procured has been put to use; and thereafter capitalize the interest incurred for the period between the date-of borrowing of the fund to the date on which the asset was put to use and we also clarify that interest deduction needs to be allowed from the date after the asset has been put to use by the Assessee."

5.3.1 Since the facts of the year under consideration are similar to the facts involved in the assessment year 2009-10, therefore, respectfully following the precedent as referred above, the issue in dispute is restored to the file of the AO/TPO with the similar directions as have been given by the ITAT in assessment year 2009-10 (Supra). In the result, the ground is allowed for statistical purposes.

6. Apropos ground no. 4 relating to levying interest u/s. 234B and Section 234C of the Act.

6.1 Ld. Counsel of the assessee submitted that the interest u/s. 234B of the Act is consequential in nature whereas in respect of charging of interest u/s. 234C of the Act is concerned, it should be charged on the tax at returned income.

6.2 Ld. CIT(DR) supported the order of the AO.

6.3 We have heard the rival contentions and perused the records. In our opinion, the interest u/s. 234B of the Act is consequential in nature and interest u/s. 234C of the Act is to be charged on the tax at the returned income. We hold and direct accordingly. This ground is allowed.

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

ASSESSMENT YEAR 2013-14

8. The Assessee has raised the following grounds in respect of assessment year 2013-14:-

> 1. *That the assessing officer erred on facts and in law in completing the assessment under section 144C read with section143(3) of the Income-tax Act (the Act) at income of Rs. 29,46,55,100 as against returned income of Rs. Nil after setting off of brought forward losses of Rs. 25,00,07,902.*

2. That the assessing officer erred on facts and in law in making adjustment of Rs. 9,86,08,398 to the income of the appellant on account of the alleged difference in the arm's length price of the international transaction of provision of software development services undertaken during the previous year on the basis of order passed by Transfer Pricing Officer ('TPO') under section 92CA(3) of the Act.

2.1 That the Dispute Resolution Panel ('DRP')/TPO erred on facts and in law in disregarding the internal benchmarking undertaken by the appellant for determining the arm's length price of the international transactions, applying TNMM, holding that:

(i) the appellant did not maintain segmental accounts for the related and non¬related transactions and there was no segregation of these activities in the audited financials.

(ii) in the segmental accounts prepared by the appellant, expenses which cannot be directly allocated are apportioned on the basis of respective turnover and is not reliable at all.

(iii) The segmental accounts were created by the assessee artificially.

(iv) that the characteristics of services transferred, functions performed, asset employed and risk

assumed by assessee in providing services to related and unrelated party are different.

2.2 That the DRP/ TPO erred on facts and in law in holding that the internal comparability does not provide meaningful benchmarking, even after accepting that, FAR of the segments are identical and concurrent transactions of both the segments are homogeneous.

2.3 That the DRP/ TPO erred on facts and in law in disregarding the internal benchmarking analysis applying TNMM undertaken by the appellant, without pointing out any error or mistake in the segmental profitability in relation to revenue earned from AE and non AEs transactions worked out by the appellant and also certified by independent Chartered Accountants.

2.4 Without prejudice, while benchmarking the international transaction of provision of software development services with external comparables, the DRP/ TPO erred on facts and in law in considering the following companies which does not pass comparability criteria provided under Rule 10B(2) of the Income Tax Rules:

i. Acropetal Technologies Limited

ii. Infosys Ltd.

iii. Larsen & Toubro Infotech Limited

iv. Minditree Limited

v. Persistent Systems & Solutions Limited

2.5 That on the facts and in the circumstances of the case and in law, the DRP/ TPO erred in rejecting the contention of the appellant regarding risk adjustment, allegedly holding that in absence of robust and reliable data, both for the assessee and for the comparables, risk adjustment cannot be considered for enhancing comparability.

2.6 Without prejudice, that the assessing officer/TPO erred on facts and in law in not giving effect to the direction of the DRP to restrict adjustment in the arm's length price of international transaction of software development services only to the international transaction undertaken with the associated enterprise and not to the entire turnover of the appellant.

3. That the assessing officer/ DRP erred on facts and in law in making an disallowance of interest expenses of Rs. 4,18,226 allegedly holding that the interest paid on short term loans which are invested in acquisition of fixed assets shall be capitalized along with the fixed assets.

3.1 That the assessing officer/ DRP erred on facts andin law in not appreciating that the fixed assets were acquired by the assessee out of its own funds and accordingly, no interest expenses shall be aggregated with the value of fixed assets.

3.2 Without prejudice, the assessing officer erred on facts and in law in allegedly considering the interest expense of Rs. 73,91,619 paid on loans aggregating to Rs. 22.50 crores, without appreciating that the total purchases of fixed assets made during the year was only for Rs. 9.89 crores.

4. That the assessing officer erred on facts and in law in allowing set-off of brought forward losses from the assessed income for Rs. 5,43,79,729 as against actual brought forward losses claimed in the return of income of Rs. 25,00,07,902.

5. That the assessing officer erred on facts and in law in levying interest under Section 234B and Section 234C of the Act.

The appellant craves leave to add, alter, amend or vary from the appeal before or at the time of hearing.

9. Ground no. 1 is general in nature, hence, needs no separate adjudication.

10. Apropos ground nos. 2 to 2.6 relating to TP adjustment amounting to Rs. 9,86,08,398/- in respect of international transaction

of provision of software development services is concerned, we find that issue in dispute is exactly similar to the issue raised in assessment year 2012-13 as discussed in para no. 4 to 4.3.2 referred above while deciding the ITA No. 1028/Del/2017 wherein we have set aside the similar issue to the file of the AO/TPO in terms of the earlier directions of the Tribunal. Therefore following the consistent view, this issue is also set aside to the file of the AO/TPO in terms of our directions given in para no. 4.3 to 4.3.2 as referred above. In the result, the ground is allowed for statistical purposes.

11. Apropos ground nos 3 to 3.2 relating to adhoc disallowance of interest expenses of Rs. 4,18,226/- is concerned, we find that issue in dispute is exactly similar to the issue raised in assessment year 2012-13 as discussed in para no. 5 to 5.3.1 referred above while deciding the ITA No. 1028/Del/2017 wherein we have set aside the similar issue to the file of the AO/TPO in terms of the earlier directions of the Tribunal. Therefore following the consistent view, this issue is also set aside to the file of the AO/TPO in terms of our directions given in para no. 5.3 to 5.3.1 as referred above. In the result, the ground is allowed for statistical purposes.

12. Apropos ground no. 4 relating to allowing set off of brought forward losses from the assessed income of Rs. 5,43,79,729/- as against actual brought forward loses claimed in the return of income of Rs. 25,00,07,902/- is concerned. After going through the impugned order passed by the AO, we find that AO has allowed the set off of brought forward losses from the assessed income for Rs. 5,43,79,729/- as against actual brought forward losses claimed in the

return of income of Rs. 25,00,07,902/-, hence, in our considered opinion, this claim of the assessee has to be verified and decided afresh by the AO/TPO in accordance with law. We hold and direct accordingly. This ground is allowed for statistical purposes.

13. Apropos ground no. 5 relating to levying interest u/s. 234B and Section 234C of the Act is concerned, we find that issue in dispute is exactly similar to the issue raised in assessment year 2012-13 as discussed in para no. 6 to 6.3 referred above while deciding the ITA No. 1028/Del/2017 wherein we have decided the issue in favour of the assessee. Therefore following the consistent view, this issue is allowed in terms of our directions given in para no. 6.3 as referred above. In the result, the ground is allowed.

14. In the result, both the Appeals of the assessee are allowed for statistical purposes.

Order pronounced in the Open Court on 09/08/2018.

Sd/-	**Sd/-**
[N.K. SAINI]	**[KUL BHARAT]**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Date 09/08/2018

"SRBHATNAGAR"

Copy forwarded to: -

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

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By Order,

Assistant Registrar,
ITAT, Delhi Benches