

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

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

IT(TP)A No.678/Bang/2016
Assessment Year: 2011-12

M/s. Textron India Pvt. Ltd., 1 st & 2 nd Floors, B Block (Tower 2) SEZ Campus, Global Village RVCE Post, Myslasandra, Off Mysore Road Bangalore 560 059 PAN NO :AACCT0118M	Vs.	Deputy Commissioner of Income-tax Circle-7(1)(1) Bangalore
APPELLANT		RESPONDENT

IT(TP)A No.594/Bang/2016
Assessment Year: 2011-12

Deputy Commissioner of Income-tax Circle-7(1)(1) Bangalore	Vs.	M/s. Textron India Pvt. Ltd., Bangalore 560 059
APPELLANT		RESPONDENT

C.O. No.22/Bang/2017 (Arising out of IT(TP)A No.594/Bang/2016)
Assessment Year: 2011-12

M/s. Textron India Pvt. Ltd., Bangalore 560 059	Vs.	Deputy Commissioner of Income- tax Circle-7(1)(1) Bangalore
APPELLANT		RESPONDENT

Assessee by	:	Shri Sumeeth Khurana, A.R.
Revenue by	:	Shri Sumer Singh Meena, D.R (OSD)

Date of Hearing	:	15.11.2021
Date of Pronouncement	:	04.01.2022

ORDER

PERB.R. BASKARAN, ACCOUNTANT MEMBER:

The cross appeals filed by the parties and the cross objection filed by the assessee are directed against the assessment order dated 16-03-2015 passed by the assessing officer u/s 143(3) r.w.s 144C(13) of the Income-tax Act,1961 [the Act' for short] in pursuance of directions given by Ld Dispute Resolution Panel (DRP).

2. The appeal filed by the assessee give rise to the following issues:-

- (a) Transfer pricing adjustment made in respect of "Engineering Design Segment".
- (b) Transfer Pricing adjustment made in respect of "Marketing Support Services"
- (c) Disallowance u/s 40(a)(ia) in respect of broad band connectivity charges.
- (d) Disallowance u/s 40(a)(ia) of depreciation claimed on software purchases for non-deduction of tax at source.
- (e) In the alternative, the above disallowances will go to increase business profits eligible for deduction u/s 10A of the Act.

3. The revenue is in appeal in respect of following issues:-

- (a) Granting of risk adjustment @ 1% arbitrarily without appreciating the facts of the case and its comparables.

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(b) Allowing deduction of expenditure 'deducted from Export turnover' from the Total turnover also while computing deduction u/s 10A of the Act.

4. In the Cross objection, the assessee has only raised many general grounds relating to Transfer pricing adjustment. Hence, the Cross objection does not require any specific adjudication.

5. The facts relating to the case are set out in brief. The assessee is a subsidiary of Textron Atlantic Inc., USA (Textron US) and Textron Inc., USA. The assessee undertakes contract engineering design services (EDS) for its Associated Enterprises (AEs). The assessee also renders Marketing Support Services (MSS) to its AEs. During the year under consideration, the assessee had entered into four types of international transactions with its AEs. In respect of Engineering Design Services (EDS), the TPO made transfer pricing adjustment of Rs.4,80,86,713/- and in respect of Marketing Support services (MSS), the TPO made transfer pricing adjustment of Rs.70,71,129/- Other two international transactions were accepted to be at arm's length by TPO.

6. The AO issued draft assessment order proposing addition of transfer pricing adjustments in both EDS and MSS services. Besides the above, the AO also proposed addition u/s 40(a)(ia) of the Act in respect of payment of broadband connectivity charges and the depreciation claimed on software purchases, whose payments were made without deduction of tax at source. The AO also took the view that the expenditure deducted from Export turnover cannot be deducted from the Total turnover also while computing deduction u/s 10A of the Act. The deduction u/s 10A was recomputed by AO accordingly.

7. The assessee filed objections before Ld DRP objecting to the proposals made by the AO in the draft assessment order. The Transfer pricing adjustments were confirmed by Ld DRP except with regard to the objection relating to error in margin computation and Risk adjustment. The Ld DRP restored both the issues to the file of AO/TPO to examine them. In respect of Risk adjustment, the Ld DRP guided the AO/TPO with the decision rendered in the case of DCIT vs. Hello Soft P Ltd (2013)(32 taxmann.com 101 by ITAT, Hyderabad, wherein risk adjustment of 1% was allowed. The Ld DRP confirmed disallowance of broad band connectivity charges u/s 40(a)(ia) of the Act. In respect of disallowance of depreciation on software purchases u/s 40(a)(i) of the Act for non-deduction of tax at source from the payment made towards purchase of software, the Ld DRP noticed that the AO has accepted capitalization of software expenses by the Assessee. Since the jurisdictional Hon'ble Karnataka High Court has held in the case of Samsung Electronics Co. Ltd (2011)(203 Taxmann 477)(Kar) that the TDS is liable to be deducted from payments made for software purchases, the Ld DRP directed the AO to treat the software purchases as revenue expenditure and accordingly directed the AO to disallow entire software purchase expenses, even though it has been capitalised by the assessee. In respect of deduction u/s 10A altered by the AO, the Ld DRP directed the AO to follow the decision rendered by jurisdictional Karnataka High Court in the case of Tata Elxsi Ltd (2012)(349 ITR 98)(Kar) and deducted the expenses from both export turnover and total turnover while computing deduction u/s 10A of the Act.

8. However, it appears that the TPO has given relief on account of risk adjustment. However, the AO retained the addition towards

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Transfer pricing adjustment made in the draft assessment order by observing that the Ld DRP did not give any relief to the assessee. The AO also retained the addition u/s 40(a)(ia) of the Act in respect of payment of broadband connectivity charges. In respect of addition of depreciation u/s 40(a)(i) and the computation of deduction u/s 10A of the Act, the AO did not follow the directions given by Ld DRP. Accordingly, the assessing officer retained the addition made by him in the draft assessment order on both the issues. Aggrieved, both the parties have filed appeal before us. The assessee has also filed cross objections.

9. Before us, the assessee has filed a letter dated 4.12.2019, wherein it has stated that the assessee has settled the issue relating to transfer pricing adjustment made in respect of "USA related transactions" under Engineering design and software development services (EDS) through Mutual Agreement Procedure (MAP) application filed with competent authority of United States of America and India. The MAP resolution letter Number F.No.480/04/2019-APA-1 dated 4.10.2019 has been attached to the above said letter filed by the assessee. Accordingly, the assessee has stated that it is withdrawing the grounds relating to engineering design and software development services in so far as it is related to USA related transactions. We notice from the letter dated 4.10.2019 issued by CBDT, the margin was determined at 15.85% for USA related transactions under EDS entered during the year relevant to the assessment year 2011-12.

10. The Ld. A.R. submitted that the USA related transactions constituted 96.30% of the total turnover in the engineering design services segment. Accordingly, the Ld. A.R. submitted that the MAP rate of 15.85% agreed for USA related transactions may also be

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applied to non-USA related transactions, since the non-USA related transaction constituted only 3.70% of the turnover. The Ld. A.R. submitted that the similar prayer was made before the Tribunal in the assessee's own case in assessment year 2008-09, wherein the non-USA related transaction constituted 16% of the total turnover. The Tribunal, vide its order dated 25.1.2019, passed in IT(TP)A No.5/Bang/2014 has accepted the claim of the assessee and directed the TPO to adopt the MAP rate adopted for USA related transactions to non-USA related transactions also.

11. We heard the parties on this issue and perused the record. We have noticed that the USA related transactions constituted 96.30% of the total turnover of EDS segment for which margin was agreed to be 15.85% under MAP resolution. The coordinate bench has taken the view that the same rate may be adopted for non-USA related transactions also in the assessee's own case relating to 2008-09 (referred supra). Accordingly, following the decision rendered by the coordinate bench in AY 2008-09, we direct the AO/TPO to adopt the margin of 15.85% to non-USA related transactions also under engineering design services segment.

12. The next issue relates to transfer pricing adjustment made in respect of marketing support services. The Ld. A.R. submitted that the TPO had made transfer pricing adjustment of Rs.70,71,129/- instead of making adjustment of Rs.40,71,129/-. When this mistake was pointed out, the DRP directed the A.O. to verify the claim of the assessee and take necessary action. However, the AO/TPO did not examine the claim of the assessee and accordingly retained the transfer pricing adjustment of Rs.70,71,129/-. The Ld. A.R. explained this arithmetical error further, i.e., he submitted

that the TPO had selected following comparable companies for marketing support services:-

<i>Sl.No.</i>	<i>Name of the company</i>	<i>OP/Cost (%)</i>
<i>1</i>	<i>Asian Business Exhibition & Conferences Ltd.</i>	<i>19.51</i>
<i>2</i>	<i>Cyber Media Research Ltd.</i>	<i>10.59</i>
<i>3</i>	<i>ICC International Agencies Ltd.</i>	<i>24.66</i>
	<i>Average</i>	<i>18.25%</i>

13. Even though the assessee asked for working capital adjustment, the TPO did not grant working capital adjustment and accordingly determined the ALP margin at 18.25% as mentioned in the table. Accordingly, he determined the arms length price at Rs.5.05 crores. The assessee had received payment of Rs.4.65 crores. However, the TPO deducted a sum of Rs.4.35 crores from the AALP amount instead of Rs.4.65 crores. Accordingly, he made transfer pricing adjustment of Rs.70.71 lakhs instead of Rs.40.71 lakhs. Accordingly he submitted that there is excess TP adjustment by Rs.30.00 lakhs.

14. The Ld. A.R. submitted that out of the 3 comparable companies selected by TPO, following two companies have been held to be under good comparables in the case of Electronic Imaging India Pvt. Ltd. in IT(TP)A No.1506/Bang/2015 relating to assessment year 2011-12:-

- a) Asian Business Exhibition and Conferences Ltd.
- b) ICC International Agencies Ltd.

Accordingly, the Ld. A.R. submitted that the above said two companies should be excluded. The Ld. A.R. also submitted that the assessee may be provided working capital adjustment as held in the case of Huawei Technologies India Pvt. Ltd. IT (TP)A No.1939/Bang/2017.

15. We heard Ld. D.R. and perused the record. We notice that M/s. Asian Business Exhibition & Conferences Ltd. and ICC international Agencies Ltd. have been directed to be excluded by the coordinate bench in the case of Electronic Imaging India Pvt. Ltd. (supra). Following the above decision, we direct exclusion of both these companies.

16. After exclusion of the above said 2 companies, only M/s. Cyber Media Research Ltd. would remain. The TPO may determine the sufficiency or otherwise of one comparable company after considering the facts of the case and after hearing the assessee.

17. Since the claim of working capital adjustment is supported by the decision of coordinate bench in the case of Huawei Technologies India Pvt. Ltd. (supra), we direct the A.O. to allow working capital adjustment on actual basis.

18. Accordingly, this issue is restored to the file of the AO/TPO.

19. The next issue contested by the assessee relates to disallowance of broadband charges paid to M/s. BSNL amounting to Rs.62,459/- u/s 40(a)(ia) of the Act for non-deduction of tax at source. The Ld. A.R. submitted that an identical issue was considered by the coordinate bench in the assessee's own case in assessment year 2008-09 and the disallowance was deleted with the following observation:-

23. In respect of non-deduction of TDS u/s 194J, we found that the CIT(A) has dealt on the disputed issue in para 3.3.2 which is as under and granted relief:

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"3.3.2. It is not disputed that, it was submitted before the AO, that there is no specific contract with the service provider. The AO has considered this in the assessment order. Since there is no specific contractual facility that has been obtained from M/s. Tata Indicom, the character of "service contract" is ruled out. It is evident that the assessee has utilised standard service ordinarily available to all and sundry and it is not a specific one. The assessee relied on CIT Vs. Bharthi Cellular (319 ITR 139)(DeI), Asia Satellite Vs. DIT (332 ITR 340)(DeI) &Skycell Communications Vs. DCIT (251 ITR 53)(Mad). The unanimous decision of the Hon'ble High Courts is that fee for providing internet / broadband facility is not technical services as contemplated under Explanation 2 to section 9(1)(vii) of the Act, and the payment made for interconnection provided, through ports is not liable for deduction of tax at source. The Delhi High Court emphasized that the services do not involve any human interface. Similar view was expressed by the Mumbai Bench of the Hon'ble Tribunal in [14 ITR (Trib) 349] & [3 ITR (Trib) 294]. After examining the facts and circumstances of the instant case, I find that the assessee has simply obtained broadband / Internet facility from the service provider M/s. Tata Indicom. It is not a case where a service contract has been entered into. The facility is open to all and sundry and any member of the public can avail of it. In such circumstances, the view of the AO that the nature of service rendered as an element of implicit contract is struck down and therefore, the addition of Rs.21.49 lakhs cannot be sustained in first appeal. It is ordered accordingly.

24. Before us, learned DR has relied on order of the AO but could not controvert the findings of the CIT(A) with any cogent evidence or new facts. We are in agreement with the decision of the CIT(A) on this ground. Accordingly, we affirm the action of the CIT(A) on this issue and dismiss the revenue's ground of appeal."

20. Following the above said decision, we direct the A.O. to delete the disallowance of broadband charges made u/s 40(a)(ia) of the Act.

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21. The next issue relates to disallowance of depreciation on software capitalized by the assessee. As noticed in earlier paragraphs, the assessee had claimed depreciation on software purchase, which have been capitalized by it. Since the assessee has not deducted tax at source from the payment made for software purchase, the A.O. disallowed the depreciation claimed on the software purchases so capitalized by the assessee. The Ld. DPR however directed the assessee to treat the software purchases as revenue expenditure and disallow the entire software expenses. However, the A.O. did not comply with the said directions and retained the depreciation as disallowed by him in the draft assessment order.

22. The Ld. A.R. submitted that the depreciation cannot be disallowed u/s 40(a)(ia) of the Act as the same is not an item mentioned in that section. With regard to direction of Ld. DRP to treat the software expenses as revenue expenditure and disallow the same, the Ld. A.R. submitted that the Ld. DRP had followed the decision rendered by Hon'ble Karnataka High Court in the case of Samsung Electronics Company Ltd. (supra). However, the above said decision has since been reversed by Hon'ble Supreme Court in the case of Engineering Analysis Centre of Excellence Pvt. Ltd. (TS-106-SC-2021).

23. We heard Ld. D.R. on this issue and perused the record. As submitted by Ld. A.R., depreciation is not an item included u/s 40(a)(ia) of the Act and hence the depreciation cannot be disallowed u/s 40(a)(ia) of the Act. We find support by this proposition on the decision rendered by the coordinate bench in the case of UKN Properties Pvt. Ltd. in ITA No.2012/Bang/2016 dated 2.7.2021. Accordingly, the disallowance of depreciation u/s 40(a)(ia) of the Act

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is liable to be deleted. The Ld. DRP however has directed the A.O. to treat software purchases as revenue expenditure and disallow the same u/s 40(a)(ia) of the Act. In this regard, the Ld. CIT(A) has followed the decision rendered by Hon'ble High Court of Karnataka in the case of Samsung Electronics Company Ltd. (supra) which has since been reversed by Hon'ble Supreme Court in the case of Engineering Analysis Centre of Excellence Pvt. Ltd. (supra). Accordingly, in our view, the disallowance of entire amount of software purchases u/s 40(a)(ia) of the Act treating the same as revenue expenditure requires fresh examination at the end of the A.O. by considering the decision rendered by Hon'ble Supreme Court referred above. Accordingly, we restore this issue to the file of the A.O. for examining it afresh.

24. We shall now take up the appeal filed by the revenue. The first issue relates to the granting of risk adjustment. We notice that the TPO has granted risk adjustment as per direction given by Ld. DRP. Further, the same is supported by the decision rendered by the Coordinate bench in the case of Intellinet Technologies India Pvt. Ltd. in ITA No.1237/Bang/2017 and also the decision rendered by Hyderabad bench of Tribunal in the case of Hellosoft Pvt. Ltd. (2013) 32 Taxmann.com 101. Accordingly, we do not find any infirmity in the order of TPO/AO on this issue.

25. The next issue contested by the revenue relates to computation of deduction u/s 10A of the Act. The A.O. had taken the view that the expenses deducted from export turnover cannot be deducted from the total turnover for the purpose of computation of deduction u/s 10A of the Act. The Ld. DRP however directed the Assessing officer to deduct the expenses from total turnover also following the decision rendered by jurisdictional Hon'ble Karnataka

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High Court in the case of Tata Elxsi Ltd. 349 ITR 98. The above said decision of Hon'ble High Court has since been upheld by Honourable Supreme Court in the case of HCL Technologies Ltd. (2018) 93 Taxmann.com 33. Accordingly, we do not find any infirmity in the direction given by Ld. DRP.

26. In the result, the appeal filed by the assessee is treated as allowed. The appeal of the revenue and the cross objection filed by the assessee are dismissed.

Order pronounced in the open court on 4th Jan, 2022.

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

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

Bangalore,
Dated 4th Jan, 2022.
VG/SPS

Copy to:

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

By order

Asst. Registrar, ITAT, Bangalore.