

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

**BEFORE SHRI N.V. VASUDEVAN, VICE PRESEIDENT
AND
SHRI PADMAVATHY S, ACCOUNTANT MEMBER**

IT(TP)A No.35/Bang/2020
Assessment year : 2015-16

Outsourcepartners International Pvt. Ltd., Tower 2D, Embassy Tech Village, Devarabeesanahalli Outer Ring Road, Bangalore – 560 037. PAN : AAACO 5734C	Vs.	The Assistant Commissioner of Income Tax, Circle 5(1)(2), Bangalore.
APPELLANT		RESPONDENT

Appellant by	:	Shri K.R. Vasudevan, Advocate
Respondent by	:	Shri V.S. Chakrapani, CIT(DR)(ITAT), Bengaluru.

Date of hearing	:	20.06.2022
Date of Pronouncement	:	24.06.2022

ORDER

Per Padmavathy S., Accountant Member

This appeal is against the final assessment order of the ACIT, Circle 5(1)(2), Bangalore dated 24.10.2019 for the AY 2015-16.

2. The assessee has raised 9 grounds of appeal, out of which Ground No.1 is general and does not require any separate adjudication. Ground Nos.8 & 9 are consequential in nature. Accordingly, these grounds are dismissed.

3. The only issue that arises for consideration vide ground Nos.2 to 7 is with regard to calculation of interest on delayed receivables, which we will adjudicate in the ensuing paragraphs.

4. The assessee has also raised an additional ground pertaining to Education Cess, but did not press for the same during the course of hearing in view of the recent amendments to statute. Therefore, the additional ground is dismissed as not pressed.

5. The assessee is engaged in the business of providing Information Technology enabled Services [ITeS] to its Associates Enterprises [AE]. In terms of Sec.92B(1) of the Act, the transaction of providing IT enabled services (ITES) to its AE were “international transaction” i.e., a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises. In terms of Sec.92(1) of the Act, the any income arising from an international transaction shall be computed having regard to the arm’s length price.

6. The assessee adopted Transactional Net Margin Method (TNMM) as the Most Appropriate Method [MAM]. The Operating Profit to Operating Cost ratio has been taken as the Profit Level Indicator [PLI] in TNMM analysis.

7. The assessee filed return of income for AY 2015-16 on 30.9.2016 admitting an income of Rs.16,43,89,350. The case was selected for scrutiny and referred to the Transfer Pricing Officer [TPO]. The assessee's comparables were not accepted by the TPO during the TP proceedings. The TPO on a fresh set of comparables chosen made a TP adjustment of Rs.17,28,28,717 and also calculated interest on outstanding receivables at Rs.7,62,860.

8. The assessee raised objections before the DRP. The DRP granted relief to the assessee on exclusion of various comparables and therefore the TP adjustment was reduced to NIL and the margin of the assessee was determined to be within the arm's length. However, the DRP upheld the adjustment of the TPO with respect to interest on receivables with a direction to reduce the credit period from 90 days to 30 days. The interest was therefore enhanced to Rs.1,00,78,319 and the final order of assessment was passed by the AO giving effect to the same. Aggrieved, the assessee is in appeal before the Tribunal.

9. The Id. AR submitted that no benchmarking was done by the TPO while treating the interest on receivables as a separate international transaction with respect to whether interest has been charged on receivables from non-AEs or whether there is any payable

outstanding from AE in which the same needs to be netted against receivables for the purpose of interest. The Id. AR also submitted that no separate adjustment for interest on receivables is warranted, if working capital adjustment is done. He further submitted that the assessee is a debt free company and hence there is no requirement for interest on receivables. He contended that the DRP has reduced the credit period from 90 days to 30 days without taking cognizance of the amendment to the agreement entered into with the AEs enhancing the credit period.

10. The Id. DR supported the orders of the lower authorities.

11. We have considered the rival submissions and perused the material on record. The assessee is providing ITeS to its AE. The TPO has held that the outstanding receivables from the AE is in the nature of loans and calculated the interest on receivables from AE by following CUP method. The TPO has considered the RBI Master Circular No.8/2010-11 dated 1.7.2010 on External Commercial Borrowing [ECB] which specifies the ceiling of 6 months LIBOR + 300 basis points to cases where the average maturity period is between 3 to 5 years. The TPO added 100 basis points towards currency risk and arrived at the applicable rate of LIBOR + 400 points which worked to 4.836%. He had considered 90 days credit for arriving at the interest adjustments. The DRP relied on the decision of the ITAT, Delhi in the case of *Bechtel India Pvt. Ltd. in ITA No.6530/Del/2016 dated 16.5.2017* and confirmed the interest adjustment on receivables by

reducing the credit period to 30 days. The issue that arises for our consideration with regard to interest on receivables are :-

- (i) Whether interest on receivables is separate international transaction and requires benchmarking separately? and
- (ii) Whether the credit period considered by the DRP at 30 days is correct on the facts of the case and the evidence?

12. We notice that the coordinate Bench of the Tribunal in the case of *Applied Materials India Pvt. Ltd. v. ITO in IT(TP)A No.3403/Bang/2018 dated 08.06.2022* has considered the issue of whether interest on receivables is a separate international transaction and held that :-

“39. We have considered the rival submissions and perused the material on record. In our opinion, the impugned issue is squarely covered by the decision of the coordinate Bench of the Tribunal in the case of *Swiss Re Global Business Solutions India Pvt. Ltd. (supra)* wherein it was held as under:-

“35. The only other issue that remains for adjudication is ground No.15 with regard to re-characterizing certain trade receivables as unsecured loans and computing notional interest on such trade receivables. The main contention of the ld. AR is that deferred receivables would not constitute a separate international transaction and need not be benchmarked while determining the ALP of the international transaction. In our opinion, this issue was considered by the Tribunal in assessee's own case for AY 2014-15 and in para 23 to 23.9 of the order dated 21.5.2020 this Tribunal held as under:-

“23. Ground No. 14-17 alleged by assessee against adjustment of notional interest on outstanding receivables.

From TP study, it is observed that payments to assessee are not contingent upon payment received by AEs from their respective customers. Further Ld.AR submitted that working capital adjustment undertaken by assessee includes the adjustment regarding the receivables and thus receivables arising out of such transaction have already been accounted for. Alternatively, he submitted that working capital subsumes sundry creditors and therefore separate addition is not called for.

23.1. Ld.TPO computed interest on outstanding receivables under weighted average method using LIBOR + 300 basis points applicable for year under consideration that worked out to 3.3758% on receivables that exceeded 30 days. It has been argued by Ld.AR that authorities below disregarded business/commercial arrangement between the assessee and its AE's, by holding outstanding receivables to be an independent international transaction.

23.2. Ld.AR placed reliance on decision of Delhi Tribunal in Kusum Healthcare (P.) Ltd. v. Asstt. CIT [2015] 62 taxmann.com 79, deleted addition by considering the above principle, and subsequently Hon'ble Delhi High Court in Pr. CIT v. Kusum Health Care (P.) Ltd. [2018] 99 taxmann.com 431/[2017] 398 ITR 66, held that no interest could have been charged as it cannot be considered as international transaction. He also placed reliance upon decision of Delhi Tribunal in case of Bechtel India (P.) Ltd. v. Dy. CIT [2016] 66 taxman.com 6 which subsequently upheld by Hon'ble Delhi High Court vide order in Pr. CIT v. Bechtel India (P.) Ltd. [IT Appeal No. 379 of 2016,

dated 21-7-16] also upheld by Hon'ble Supreme Court vide order, in CC No. 4956/2017.

23.3. It has been submitted by Ld.AR that outstanding receivables are closely linked to main transaction and so the same cannot be considered as separate international transaction. He also submitted that into company agreements provides for extending credit period with mutual consent and it does not provide any interest clause in case of delay. He also argued that the working capital adjustment takes into account the factors related to delayed receivables and no separate adjustment is required in such circumstances.

23.4. On the contrary Ld.CIT.DR submitted that interest on receivables is an international transaction and Ld.TPO rightly determined its ALP. In support of the contentions, he placed reliance on decision of Delhi Tribunal order in Ameriprise India (P.) Ltd. v. Asstt. CIT [2015] 62 taxmann.com 237 wherein it is held that, interest on receivables is an international transaction and the transfer pricing adjustment is warranted. He stated that Finance Act, 2012 inserted Explanation to section 92B, with retrospective effect from 1.4.2002 and sub-clause (c) of clause (i) of this Explanation provides that:

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

. (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;. . . . '

23.5. Ld.CIT.DR submitted that expression 'debt arising during the course of business' refers to trading

debt arising from sale of goods or services rendered in course of carrying on business. Once any debt arising during course of business is an international transaction, he submitted that any delay in realization of same needs to be considered within transfer pricing adjustment, on account of interest income short charged or uncharged. It was argued that insertion of Explanation with retrospective effect covers assessment year under consideration and hence under/non-payment of interest by AEs on debt arising during course of business becomes international transactions, calling for computing its ALP. He referred to decision of Delhi Tribunal in Ameriprise (supra), in which this issue has been discussed at length and eventually interest on trade receivables has been held to be an international transaction. Referring to discussion in said order, it was stated that Hon'ble Delhi Bench in this case noted a decision of the Hon'ble Bombay High Court in the case of CIT v. Patni Computer Systems Ltd. [2013] 33 taxmann.com 3/215 Taxman 108 (Bom.), which dealt with 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?'"

23.6. Ld.CIT.DR submitted that, while answering above question, Hon'ble Bombay High Court referred to amendment to section 92B by Finance Act, 2012

with retrospective effect from 1.4.2002. Setting aside view taken by Tribunal, Hon'ble Bombay High Court restored the issue to file of Tribunal for fresh decision in light of legislative amendment. It was thus argued that non/under-charging of interest on excess period of credit allowed to AEs for realization of invoices, amounts to an international transaction and ALP of such international transaction has to be determined by Ld.TPO. Insofar as charging of rate of interest is concerned, he relied on decision of the Hon'ble Delhi High Court in CIT v. Cotton Naturals (I) (P.) Ltd. [2015] 55 taxmann.com 523/231 Taxman 401 holding that currency in which such amount is to be re-paid, determines rate of interest. He, therefore, concluded by summing-up that interest on outstanding trade receivables is an international transaction and its ALP has been correctly determined.

23.7. We have perused the submissions advanced by both the sides in the light of the records placed before us.

This Bench referred to decision of Special Bench of this Tribunal in case of Special Bench of ITAT in case of Instrumentation Corpn. Ltd. v. Asstt. DIT (IT) [2016] 71 taxmann.com 193/160 ITD 1 (Kol. - Trib.), held that outstanding sum of invoices is akin to loan advanced by assessee to foreign AE., hence it is an international transaction as per Explanation to section 92B of the Act. We also perused decision relied upon by Ld.AR. In our considered opinion, these are factually distinguishable and thus, we reject argument advanced by Ld.AR.

23.8. Alternatively, it has been argued that in TNMM, working capital adjustment subsumes sundry creditors. In such situation computing interest on outstanding receivables and loans and advances to associated enterprise would amount to double taxation. Hon'ble

Delhi Tribunal in case of Orange Business Services India Solutions (P.) Ltd. v. Dy. CIT [2018] 91 taxmann.com 286 has observed that:

"There may be a delay in collection of monies for supplies made, even beyond the agreed limit, due to a variety of factors which would have to be investigated on a case to case basis. Importantly, the impact this would have on the working capital of the assessee would have to be studied. It went on to hold that, there has to be a proper inquiry by the TPO by analysing the statistics over a period of time to discern a pattern which would indicate that vis-a-vis the receivables for the supplies made to an AE, the arrangement reflected an international transaction intended to benefit the AE in some way. Similar matter once again came up for consideration before the Hon'ble Delhi High Court in Avenue Asia Advisors Pvt. Ltd v. DCIT [2017] 398 ITR 120 (Del). Following the earlier decision in Kusum Healthcare (supra), it was observed that there are several factors which need to be considered before holding that every receivable is an international transaction and it requires an assessment on the working capital of the assessee. Applying the decision in Kusum Health Care (supra), the Hon'ble High Court directed the TPO to study the impact of the receivables appearing in the accounts of the assessee; looking into the various factors as to the reasons why the same are shown as receivables and also as to whether the said transactions can be characterised as international transactions."

23.9. In view of the above, we deem it appropriate to set aside this issue to Ld.AO/TPO for deciding it in conformity with the above referred judgment. Needless to say, the assessee will be allowed a reasonable opportunity of being heard in accordance with law.”

36. Accordingly, we are of the opinion that deferred receivables would constitute an independent international transaction and the same is required to be benchmarked independently as held by the Hon’ble Karnataka High Court in *PCIT v. AMD (India) Pl. Ltd.*, ITA No.274/2018 dated 31.8.2018.

37. Once we have held that the transaction between the assessee and AE was in foreign currency with regard to receivables and transaction was international transaction, then transaction would have to be looked upon by applying the commercial principles with regard to international transactions and accordingly proceeded to take into account interest rate in terms of London Inter Bank Offer Rate [LIBOR] and it would be appropriate to take the LIBOR rate + 2%. For this purpose, we place reliance on the judgment of the Bombay High Court in the case of *CIT v. Aurionpro Solutions Ltd.*, 99 CCH 0070 (Mum HC). It is ordered accordingly.”

40. In view of the above discussion and considering the decision of the of the coordinate bench of the Tribunal (supra) and the judgment of the Hon’ble High Court of Karnataka in the case of *AMD (India) Pvt. Ltd. (supra)*, we hold that the treatment of interest on deferred receivables is rightly considered as an independent international transaction and benchmarked separately by the revenue authorities.”

13. Following the above decision, in the present case we hold that interest on receivable is a separate international transaction which has been rightly considered by the TPO/DRP.

14. With regard to determination of ALP in respect of interest on receivables, we notice that the coordinate Bench of the Tribunal in the case of *Barracuda Networks India Pvt. Ltd. in IT(TP)A No.229/Bang/2021 vide order dated 25,10.2021* has held as under:-

“43. Having concluded that deferred trade receivables constitute international transaction, we come to the computation of the ALP of the international transaction of 'debt arising during the course of business.' This has two ingredients, viz., the amount on which interest should be charged and the arm's length rate at which the interest should be charged. On this aspect we can take useful guidance from the decision of the ITAT Delhi Bench in the case of *Techbooks International (P.) Ltd. v. Deputy Commissioner of Income-tax, Circle-3, Noida* [2015] 63 taxmann.com 114 (Delhi - Trib.), wherein the Tribunal laid down guidelines on the manner of determination of ALP, as follows:

“13.11 Now, we come to the computation of the ALP of the international transaction of 'debt arising during the course of business.' This has two ingredients, viz., the amount on which interest should be charged and the arm's length rate at which the interest should be charged.

13.12 In so far as the first aspect is concerned, we find that the TPO has taken normal credit period of 60 days and accordingly made addition on account of transfer pricing adjustment for the period in excess of 60 days. In our considered opinion, transfer pricing adjustment on account of interest for the entire period of delay beyond 60 days cannot be treated as a separate international transaction of trading debt arising during the course of business. It is noticed that the assessee entered into an agreement with its AE for realization of invoices within a period of 150 days. This implies that the interest amount on non-realization of invoices up to 150 days was factored in the price charged for the services rendered. Annexure-1 to the TPO's order gives details of the instances of late realization or non-realization of advances up to the year ending. First three and a half pages of this Annexure indicate number of days for which there was delayed realization. Such delay ranges from 175 days to 217 days.

The remaining pages disclose no realization of invoices up to 31st March, 2010. When we consider the dates of invoices in the remaining pages, it is manifested that in certain cases these invoices have been raised on 31st August, 30th or September or 31st October, 2009. In all such cases, the period of 150 days already stood expired as on 31st March, 2010 and the assessee ought to have charged interest on the delay in realizing such invoices along with the first three and a half pages in which there is an absolute and identified delay in realization of invoices beyond the stipulated period. When the interest for realization of trade advances up to 150 days is part and parcel of the price charged from the AE, then the delay up to this extent cannot give rise to a separate international transaction of interest uncharged. Rather interest for the period in excess of normally realizable period in an uncontrolled situation upto 150 days needs to be considered in the determining the ALP of the international transaction of the 'Provision of IT Enabled data conversion services'. This can be done by increasing the revenue charged by the comparable companies with the amount of interest for the period between that allowed by them in realization of invoices and 150 days as allowed by the assessee, so as to bring such comparables at par with the assessee's international transaction of provision of the ITES. To illustrate, if the comparables have allowed credit period of, say, 60 days and the assessee has realized its invoices in 180 days, then interest for 90 days (150 days minus 60 days) should be added to the price charged by the comparables and the amount of their resultant adjusted operating profit be computed. Rule 10B permits making such an adjustment. Sub-rule (2) to rule 10B stipulates that for the purposes of sub-rule (1), the comparability of an international transaction with an uncontrolled transaction shall be judged, inter alia, with reference to the : '(c) the contractual terms (whether or not such terms are formal or in writing) of the transactions ...' . Then sub-rule (3) mandates that an uncontrolled transaction shall be comparable to an international transaction if 'reasonably accurate adjustments can be made to eliminate the material effects of such differences'. Applying the prescription of rule 10, it becomes vivid that difference on account of the 'contractual terms of the transactions', which also include the credit period allowed, needs to be adjusted in the

profit of comparables. As the TPO has taken the entire delay beyond that normally allowed as a separate international transaction, which position is not correct, we hold that the effect of delay on interest up to 150 days over and above the normal period of realization in an uncontrolled situation, should be considered in the determination of the ALP of the international transaction of 'Provision of IT Enabled data conversion services' and the period of delay above 150 days, namely, 30 days in our above illustration (180 days minus 150 days) should be considered as a separate international transaction in terms of clause (c) of Explanation to section 92B.

13.13 In so far as the question of rate of interest is concerned, we find that this issue is no more res integra in view of the judgment of the Hon'ble jurisdictional High Court in the case of Cotton Naturals (I) (P.) Ltd. (supra), in which it has been held that it is the currency in which the loan is to be repaid which determines the rate of interest and hence the prime lending rate should not be considered for determining the interest rate. Under such circumstances, we set aside the impugned order and remit the matter to the file of TPO/AO for a fresh determination of addition on account of transfer pricing adjustment towards interest not realized from its AE on the debts arising during the course of business in line with our above observations.”

44. We are of the view that the issue with regard to determination of ALP in respect of the international transaction of giving extended credit period for receivables should be directed to be examined afresh by the AO/TPO on the guidelines laid down in the decision referred to in the earlier paragraph, after affording Assessee opportunity of being heard. As held in the aforesaid decision the prime lending rate should not be considered and this reasoning will apply to adopting short term deposit interest rate offered by State Bank of India (SBI) also. The rate of interest would be on the basis of the currency in which the loan is to be repaid. We hold and direct accordingly. All issues on determination of ALP of the transaction are kept open.”

15. Following the above decision of the coordinate Bench of this Tribunal, we are of the view that the issue has to be restored back to the AO/TPO for determination of ALP afresh with appropriate benchmarking. We notice that the assessee has entered into a service agreement with its AE with regard to providing ITeS on 1.10.2009 [page 402 of PB] and later entered into amendment agreement on 26.12.2003 [page 414 of PB] whereby clause 2.3 of the original agreement was amended to increase the credit period to 90 days. This fact has not been taken into consideration by the DRP. We therefore direct the TPO to consider the credit period of 90 days while determining the ALP afresh, after providing reasonable opportunity of being heard to the assessee. The assessee is directed to provide the relevant details for fresh benchmarking of the ALP with regard to interest on receivables. With these observations, we set aside the order of the DRP on this issue and remit it back to the AO/TPO for fresh decision.

16. In the result, the appeal by the assessee is partly allowed.

Pronounced in the open court on this 24th day of June, 2022..

Sd/-

Sd/-

(N V VASUDEVAN)
VICE PRESIDENT

(PADMAVATHY S)
ACCOUNTANT MEMBER

Bangalore,
Dated, the 24th June, 2022.

/Desai S Murthy /

Copy to:

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

By order

Assistant Registrar
ITAT, Bangalore.