IN THE INCOME TAX APPELLATE TRIBUNAL
'C' BENCH : BANGALORE

BEFORE SHRI. CHANDRA POOJARI, ACCOUNTANT MEMBER
AND
SMT. BEENA PILLAI, JUDICIAL MEMBER

IT(TP)A No. 2824/Bang/2017
Assessment Year : 2013-14

M/s. Harman Connected Services Corporation India Pvt. Ltd., No. 3 & 3A, EOIZ Industrial Area, Survey No. 85 & 86, Sadarmangala Village, Krishnarajapuram Hobli, Bangalore – 560 066. **PAN: AABCG5658E**	**Vs.**	The Assistant Commissioner of Income Tax, Circle – 3(1)(2), Bengaluru.
APPELLANT		**RESPONDENT**

Assessee by	:	Shri T. Suryanarayana, Advocate
Revenue by	:	Ms. Neera Malhotra, CIT-DR

Date of Hearing	:	21-06-2023
Date of Pronouncement	:	27-06-2023

ORDER

PER BEENA PILLAI, JUDICIAL MEMBER

Present appeal arises out of the final assessment order passed by the Ld.ACIT, Circle – 3(1)(2), Bangalore for A.Y. 2013-14 on 19.10.2016 on following grounds of appeal:

> *"A. Transfer Pricing*
> *1. The learned Assessing Officer ["learned A0"], learned Transfer Pricing Officer ["learned TPO"] and the Honorable Dispute Resolution Panel ["Hon'ble DRP"] have grossly erred in determining an adjustment of INR 271,125,771/-*

to the revenue earned by the Appellant from the Associated Enterprises ["AEs") in its software design services segment under section 92CA read with section 143(3) & 144C of the Act.

2. The learned AO, learned TPO and Hon'ble DRP have erred in rejecting the Transfer Pricing Documentation ["TP documentation"] maintained by the Appellant by invoking provisions of sub-section (3) of 92C of the Act.

3. The learned AO, learned TPO and the Hon'ble DRP have erred in not considering multiple year financial data of the comparable companies while determining the Arm's Length Price ["ALP"] as prescribed under Rule 10B(4) of the Income Tax Rules, 1962 ["the Rules"].

4. The learned AO, learned TPO and the Hon'ble DRP have erred in using data for FY 2012-13 available at the time of assessment proceedings, instead of the data available at the time of preparing the TP documentation as mandated under Rule 10D(4) of the Rules for comparable companies in determining ALP.

5. The learned AO, learned TPO and Hon'ble DRP have erred in rejecting comparability analysis performed by the Appellant in the TP documentation. Also, the learned AO, learned TPO and Hon'ble DRP have erred in conducting a fresh comparability analysis by modifying/ introducing certain quantitative filters in determining the ALP.

6. The learned AO, learned TPO and the Hon'ble DRP have erred in rejecting companies having different financial year ending data and consequently rejected Helios & Matheson Information Technology Limited, that ought to be selected as comparable to the Appellant.

7. The learned AO, learned TPO and Hon'ble DRP have erred in rejecting the filter of accepting companies reporting service income in excess of 50 percent of total operating income and rather have adopted filter of rejecting companies reporting service income lesser than 75 percent of total sales, leading to a narrower set of comparable companies.

8. The learned AO, learned TPO and the Hon'ble DRP have erred in not restricting the threshold of export earnings filter to 25 percent of total sales rather than adopting threshold of 75 percent of total sales, which led to erroneous rejection of Evoke Technologies Private Limited., that ought to be selected as comparable to the Appellant.

9. The learned AO, learned TPO and the Hon'ble DRP have erred in considering the information that are not publicly available using powers under section 133(6) of the Act.

10. The learned AO/learned TPO/Hon'ble DRP erred in not considering upper limit turnover filter for comparability analysis.

11. The learned AO, learned TPO and Hon'ble DRP have erred in considering negative working capital adjustment while determining ALP.

12. The learned AO, learned TPO and Hon'ble DRP have erred in considering foreign exchange gain/loss as operating in nature.

13. The learned AO, learned TPO and Hon'ble DRP have erred in considering the provision for bad and doubtful debts as non-operating in nature.

14. The learned AO, learned TPO and Hon'ble DRP have erred in accepting following companies that ought to be rejected as comparable to the Appellant:

- *CG-VAK Software & Export Services Ltd.*
- *ICRA Techno Analytics Ltd.*
- *Larsen & Toubro Infotech Ltd.*
- *Persistent Systems Ltd.*

15. The learned AO, learned TPO and Hon'ble DRP have erred in rejecting following companies that ought to be accepted as comparable to the Appellant:

- *Akshay Software Technologies Ltd.*
- *Cigniti Technologies Ltd.*
- *KALS Information Systems Ltd.*
- *Helios & Matheson Information Technology Ltd.*
- *Evoke Technologies Pvt. Ltd.*
- *Acropetal Technologies Ltd.*
- *Sasken Communication Technologies Ltd.*
- *Spry Resources India Pvt. Ltd.*
- *CTIL Ltd.*

16. The learned AO, learned TPO and Hon'ble DRP have erred in not allowing appropriate adjustment towards the risk difference between the Appellant vis-a-vis the comparable companies.

B. Corporate Tax

17. Restriction of depreciation on computer servers, software's and networking equipments to the extent of 15%

- *The learned AO and Hon'ble DRP have erred in disallowing depreciation amounting to INR 9,178,532 on the networking equipments and servers by treating the same as "plant and machinery" instead of "computers" which are eligible for depreciation @ 60%.*
- *The learned AO and Hon'ble DRP have erred in not appreciating the facts stated by the Appellant during the course of hearing that why networking equipments and*

servers should be treated as part of block of computers & accessories.

- *The learned AO and Hon'ble DRP have erred in not appreciating that the networking equipments and servers cannot work in isolation and hence partake the character of computers.*

18. Re-computation of deduction under section 10AA of the Act

a. <u>Reduction of expenditure incurred in foreign currency, communication expenses and insurance expenses from export turnover only</u>

- *The learned AO has erred in considering expenses incurred in foreign currency, communication expenses and insurance expenses as attributable to the delivery of computer software outside India and therefore excluding the same from the export turnover for the purposes of computing deduction under section 10AA of the Act.*
- *The learned DRP failed to adjudicate on the above ground of objection raised by the Appellant w.r.t. expenses incurred in foreign currency, communication expenses and insurance expenses from export turnover only.*

b. <u>Corresponding reduction from Total turnover</u>

The learned AO and the Hon'ble DRP have failed to reduce the expenses incurred in foreign currency, communication expenses and insurance expenses from the total turnover in arriving at the deduction under section 10AA of the Act.

19. Non-grant of foreign tax credit ["FTC"]

The learned AO has erred in not granting FTC amounting to INR 523,428 to the Company under section 90 of the Act.

20. MAT credit not granted to the extent of difference between tax under normal computation and MAT computation

The learned AO has erred in not granting relief of MAT credit to the extent of difference between assessed tax computed under normal provisions of the Act and MAT computation, even after having sufficient MAT credit.

21. Levy of interest under section 234B of the Act

The learned AO has erred in levying interest under section 234B of the Act amounting to INR 48,653,328 which is consequential in nature. [i.e., without giving effect of MAT credit and FTC]

The appellant craves leave to add, alter, rescind and modify the grounds herein above or produce further

documents, facts and evidence before or at the time of hearing of this appeal.
For the above and any other grounds which may be raised at the time of hearing, it is prayed that necessary relief may be provided."

2. Addl. Grounds of appeal vide application dated 13.03.2023

"Additional Grounds of Appeal — Transfer pricing
For the reasons stated in the accompanying affidavit, it is most humbly prayed that this Hon'ble Tribunal be pleased to permit the Appellant to raise the following additional ground, in the interests of justice and equity.
I. Transfer Pricing
Ground 16a — That in the facts and circumstances of the case, having regard to the similarity of functions performed, assets employed, and risks assumed by the Appellant in rendering the services to its Associated Enterprises ("AEs") situated in the United States of America ("US") and in countries other than in the US, the arm's length price agreed between the Competent Authorities of USA and India in the Mutual Agreement Procedure invoked under the India-US DTAA, ought to be applied to the transactions entered into by the Appellant with its AEs situated in countries other than in the US and to the US AE transactions which were not covered under the MAP resolution period (January 2013 to March 2013) for the SWD segment."

2.1 The Ld. Counsel submitted that no new facts needs to be considered in order to dispose of the additional grounds raised by the assessee. It is submitted that, the additional grounds raised do not require verification of any new facts. The Ld.AR, thus prayed for the admission of additional grounds so raised by assessee.

2.2 On the contrary, the Ld.CIT.DR though opposed admission of the additional ground, could not bring anything on record which would challenge such a right available to assessee under the Act.

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

We note that the additional grounds are directly connected with the main issue of transfer pricing additions and no new facts needs to be investigated for adjudicating the same.

2.4 Considering the submissions and respectfully following the decisions of *Hon'ble Supreme Court* in case of *National Thermal Power Co. Ltd. Vs. CIT* reported in *(1998) 229 ITR 383* and *Jute Corporation of India Ltd. Vs. CIT* reported in 187 ITR 688, we are admitting the additional grounds raised by the assessee. **Accordingly, the additional ground raised by assessee vide application dated 13.03.2023 stands admitted.**

3. Brief facts of the case are as under:

3.1 The assessee filed revised return of income on 30.11.2023 for the Assessment Year 2013-14 showing total income of Rs.91,89,06,080/-. The return was processed u/s. 143(1). The case was selected for scrutiny and a notice u/s. 143(2) dated 03.09.2014 was issued. Notice u/s. 142(1) r.w.s 129 of the Act dated 16.09.2016, was issued calling for various details and documents. In response to the statutory notices, representative of the assessee appeared before the Ld.AO and filed requisite details as called for. As the international transactions with its associated enterprise during the year exceeded Rs. 15 Crores as per 3CEB Report, a reference was made to the Ld.TPO.

3.2 The Ld.TPO after considering various submissions in lieu of the show cause notice issued to the assessee, concluded and proposed an adjustment in an order u/s. 92CA amounting to Rs.26,11,88,092/-.

3.2.1. On receipt of the transfer pricing order by the Ld.AO, the draft assessment order was passed making further disallowance

u/s. 10AA amounting to Rs.40,98,35,261/-, disallowance of depreciation on networking equipments amounting to Rs.97,78,532/-.

3.3 On receipt of the draft assessment order, the assessee filed objections before the DRP.

3.3.1. The DRP issued directions on 07.09.2017.

3.3.2. In conformity with the DRP directions, the Ld.AO made additions in the hands of the assessee in respect of the above TP and Corporate tax additions proposed.

3.4 Aggrieved by the order of the Ld.AO, assessee preferred appeal before this *Tribunal.*

4. The Ld.Counsel submitted that assessee seeks to withdraw **Ground nos. 1-16** pertaining to transfer pricing adjustments in respect of the US transactions pursuant to MAP resolution dated 16.10.2020. The Ld.AR also submitted that the MAP resolution is passed in respect of the US transaction between assessee and the AE that took place during the calendar period for A.Ys. 2010-11, 2011-12, 2012-13 and 2013-14.

5. It is the submission of the assessee in the Additional **Ground no. 16a** that, the rate applied to the transactions from April 2012-December 2012 may be considered for the transactions between assessee and the US-AE, that took place between January 2013 to March 2013. He placed reliance on the decision of *Hon'ble Bombay High Court* in case of *J.P. Morgan Services India (P.) Ltd. reported in [2019] 105 taxmann.com 40 (Bombay).*

5.1. It is thus submitted that the mark-up on cost agreed upon for the transaction with US-AE as agreed in the MAP may be considered for the transaction with US-AE for such period that is

not covered in the MAP which is from January to March for the financial year under consideration.

6. On the contrary, the Ld.CIT.DR submitted that the principle applied by *Hon'ble Bombay High Court* in case of *J.P. Morgan Services India (P.) Ltd. (supra)* was that the transaction was considered in a consolidated manner by the Ld.TPO, and therefore the same rates were upheld to the non-AE transaction. She therefore submitted that this issue may be verified and hence may be remanded to the Ld.TPO.

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

7. We note that assessee is praying for the rates agreed in the MAP with the US-AE transactions during April to December 2012 to be considered for the transactions between January to March 2013 which is relevant FY to the Assessment Year under consideration which was not considered in MAP. It is obvious that the transaction with an entity is to be considered in a consolidated way, and cannot be bifurcated according to the calendar year prevalent in that contracting state.

7.1 We therefore direct the Ld.AO/TPO to consider the rate applied in the MAP for the transactions that entered by the assessee with US-AE for the period April 2012 to December 2019 to the transactions that the assessee entered with the US-AE during January 2013 to March 2013.

7.2 In respect of non-US transaction, we note that the assessee in the TP study report gave bifurcation of the revenue earned from US-AE and non-AE. The relevant extract is placed at page 2 of the 92CA order. Both the transactions are in respect of SWD segment.

7.3. We note from the order passed u/s. 92CA that the ALP was computed only having regards to the US-AE transaction. In other words, the Ld.TPO treated the non-AE transaction to be at arms length. This we notice from the computation of ALP that is placed at page 31 of the 92CA order wherein the price received considered by the Ld.TPO pertains to the US-AE transaction alone.

However in the event there is any transaction with a non-AE is considered in a consolidated way in the said amount by the Ld.TPO, the same may be considered in accordance with the ratio laid down by *Hon'ble Bombay High Court* in case of *J.P. Morgan Services India (P.) Ltd. (supra).*

Accordingly, the additional ground raised by assessee in 16a stands allowed.

8. **Ground nos. 1-16** raised by assessee is thus allowed to be withdrawn pursuant to MAP order dated 16.10.2020.

9. **Ground no. 17** is in respect of the depreciation on computer servers and software at 15% by considering it as plant and machinery.

9.1 This issue is no longer resintegra as it has been considered in assessee's own case for A.Ys. 2014-15 and 2015-16 in *IT(TP)A Nos. 3401/Bang/2018 and 2243/Bang/2019 respectively by orders dated 13.09.2022 and 16.09.2022 respectively.*

9.2 The Ld.AR submitted that the networking equipment broadly comprises of servers, routers, server hard disk and other network accessories. These form an essential part of computer and function as an input processor, storage and output devices, and cannot operate independent of a computer system. Therefore, it is submitted that the said items are eligible for depreciation at the rate of 60%.

On the contrary, the Ld.DR placed reliance on orders passed by authorities below.

9.3 This issue is also covered by the decision of *Hon'ble Karnataka High Court* in case of

a) *PCIT vs. Mphasis Ltd. reported in (2021) 128 taxmann.com 138*
b) *OnMobile Global Ltd. vs. ACIT reported in (2014) 45 taxmann.com 346 (Bangalore-Trib) which was affirmed by the Hon'ble High Court in (2021) 129 taxmann.com 254 (Karnataka)*
c) *CIT vs. BSES Yamuna Powers Ltd. reported in (2013) 40 taxmann.com 108 (Delhi)*

9.4. We have considered the rival submissions. We find that the issue is no longer res-integra and has been decided by the *Hon'ble Karnataka High Court* in the case of *Mphasis Ltd. (supra)* wherein the *Hon'ble Karnataka High Court* held that computer accessories such as switches and routers form part of peripherals of computer system and hence entitled to depreciation at 60%. Following the same, we allow this ground by the assessee.

9.5. We therefore direct the Ld.AO to grant the depreciation to assessee at 60% on computer servers, software and networking equipments as it falls under the category computers.

Accordingly, this ground raised by the assessee stands allowed.

10. **Ground no. 18** is in respect of computation of deduction u/s. 10AA of the act.

10.1 The Ld.AO reduced the expenditure incurred in foreign currency and communication expenses and insurance expenses as not contributable to the delivery of articles or things or computer software outside India. It is submitted that this issue is squarely covered by the decision of *Hon'ble Karnataka High Court* in case of

CIT vs. Mphasis reported in (2016) 74 taxmann.com 274, CIT vs. Tata Elxsi Ltd. reported in (2012) 204 Taxman 321.

10.2 The above decisions have been affirmed by *Hon'ble Supreme Court* in case of *CIT Vs. HCL Technologies Ltd. reported in (2018) 93 taxmann.com 33* by observing as under:

> *"17. The similar nature of controversy, akin this case, arose before the Karnataka High Court in CIT v. Tata Elxsi Ltd. [2012] 204 Taxman 321/17/taxman.com 100/349 ITR 98. The issue before the Karnataka High Court was whether the Tribunal was correct in holding that while computing relief under Section 10A of the IT Act, the amount of communication expenses should be excluded from the total turnover if the same are reduced from the export turnover? While giving the answer to the issue, the High Court, inter-alia, held that when a particular word is not defined by the legislature and an ordinary meaning is to be attributed to it, the said ordinary meaning is to be in conformity with the context in which it is used. Hence, what is excluded from 'export turnover' must also be excluded from 'total turnover', since one of the components of 'total turnover' is export turnover. Any other interpretation would run counter to the legislative intent and would be impermissible.*
>
> *18. XXXXXX*
>
> *19. In the instant case, if the deductions on freight, telecommunication and insurance attributable to the delivery of computer software under Section 10A of the IT Act are allowed only in Export Turnover but not from the Total Turnover then, it would give rise to inadvertent, unlawful, meaningless and illogical result which would cause grave injustice to the Respondent which could have never been the intention of the legislature.*
>
> *20. Even in common parlance, when the object of the formula is to arrive at the profit from export business, expenses excluded from export turnover have to be excluded from total turnover also. Otherwise, any other interpretation makes the formula unworkable and absurd. Hence, we are satisfied that such deduction shall be allowed from the total turnover in same proportion as well".*

On the contrary, the Ld.DR placed reliance on orders passed by authorities below.

10.3 We note that this issue is no longer resintegra by virtue of the decisions passed by *Hon'ble Supreme Court* in case of *CIT vs. Mphasis Ltd.* reported in *(2020) 113 taxmann.com 74* held that since the services rendered were in respect of software development or production of computer software which are technical in nature, the said expenses incurred in foreign currency for providing technical services outside India, cannot be excluded from the export turnover.

Respectfully following the above, we direct the Ld.AO to compute the deduction u/s. 10AA in accordance with the principles laid down by *Hon'ble Supreme Court* hereinabove.

Accordingly, this ground raised by assessee stands partly allowed.

11. **Ground no. 19** is in respect of non-grant of foreign tax credit.

11.1 The Ld.AR submitted that relevant documents in respect of the same were filed before the Ld.AO however the same has not been considered. In the interest of justice, we remand this issue to the Ld.AO to verify the documents and to consider the claim in accordance with law.

Accordingly, this ground raised by the assessee stands partly allowed for statistical purposes.

12. **Ground no. 20** is in respect of non-grant of MAT credit.

12.1 It is submitted that the Ld.AO has not granted the MAT credit to the extent of difference assessed tax computed under normal provisions of the act and MAT computation. We remand this issue to the Ld.AO and direct to compute the MAT credit available to the

assessee in accordance with law. Assessee is directed to file relevant details in respect of the same.

Accordingly, this ground raised by the assessee stands partly allowed.

In the result, the appeal filed by the assessee stands partly allowed.

Order pronounced in the open court on 27th June, 2023.

Sd/-	Sd/-
(CHANDRA POOJARI)	(BEENA PILLAI)
Accountant Member	Judicial Member

Bangalore,
Dated, the 27th June, 2023.
/MS /

Copy to:

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

By order

Assistant Registrar,
ITAT, Bangalore