IN THE HIGH COURT OF PUNJAB AND HARYANA AT CHANDIGARH

ITA No.551 of 2017 (O&M)
Date of Decision : 05.02.2020

The Pr. Commissioner of Income Tax, Gurgaon ...... Appellant

versus

M/s Comverse Network Systems India Pvt Ltd. ...... Respondent

CORAM : HON'BLE MR.JUSTICE AJAY TEWARI
HON'BLE MR.JUSTICE AVNEESH JHINGAN

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Present: Mr. Tajender K. Joshi, Sr. Standing Counsel for the appellant.

Shri Deepak Chopra, Advocate
Shri Deepak Agrawal, Advocate
with Shri Rohan Khare, Advocate for the respondent

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AJAY TEWARI, J. (Oral)

1. The present appeal is directed against the order of the Income Tax Appellate Tribunal ('ITAT'), I-2 Bench, New Delhi dated 31.05.2017 for the assessment year 2010-11. The Revenue has raised the following question of law:-

> *"Whether in the facts and circumstances of the case and in law, the Hon'ble ITAT was correct in excluding M/s e-Infochips Bangalore Ltd, M/s In-finite Data Systems Pvt Ltd, M/s Engineers India Ltd, M/s IBI Chematur Ltd, M/s Riets Ltd (Consultancy Service Segment) and M/s TCE Consulting Engineers Ltd used as a comparable for determining the ALP in the case of the assessee company, since the TPO has made detailed findings by analyzing functionality, turnover and profile of various comparables considered in his order. Further the ITAT was not justified to consider issues pertaining to earlier years, since each year is a separate assessment year and should be considered independently. The comparables had been selected by the TPO by applying suitable and relevant parameters."*

2. The Respondent assessee M/s Comverse Network Systems India

Pvt. Ltd. is a wholly owned subsidiary of Comverse Network Systems Inc., USA. The assessee is engaged in the provision of sales and post-sales support services, software development services, professional and maintenance services to its Associated Enterprises ('AEs').

3. For assessment year 2010-11, the Respondent assessee filed its return of income on 13.10.2010, declaring an income of Rs.1,43,77,210. The case of the assessee was selected for scrutiny and statutory notices under section 142(1) and 143(2) of the Income Tax Act, 1961 ('Act') along with detailed questionnaire was issued upon assessee. In response to these notices representative of assessee attended assessment proceedings from time to time and submitted information as called for by assessing officer. A reference under section 92C(A)(1) of the Act was made to Transfer Pricing Officer ('TPO') New Delhi, for determining arms length price in respect of international transaction entered into by the assessee during financial year 2009-10 to assessment year under consideration.

4. Before Ld. TPO the assessee filed its documentation under Rule 10D of the Income Tax Rules and other details as asked for. Ld. TPO observed that assessee had entered into following international transactions with its associated enterprises ('AE'):

1.	Comverse Limited, Israel	Provision of sales and post sales support service	13,35,70,439	TNMM
2.	Comverse Inc., USA	Provision of software development services	2,28,09,311	TNMM
3.	Comverse Limited, Israel	Provision of professional services	19,51,93,699	TNMM
4.	Comverse Limited, Israel	Provision of maintenance services	2,03,35,591	TNMM

5.	Comverse Limited, Israel	Availing of Support Services	2,89,19,906	TNMM
6.	Comverse Australia Pty. Ltd., Australia	Reimbursement of expenses (Reed.)	1,05,96,927	
7.	Comverse Malaysia Sd. Bhd., Malaysia	Reimbursement of expenses (Reed.)	23,47,408	
8.	Comverse Limited, Israel	Reimbursement of expenses (Paid) to AE	10,47,834	
9.	Comverse Inc., USA	Reimbursement of expenses (Paid) to AE	53,90,382	
10.	Comverse Kenan UK	Reimbursement of expenses (Paid) to AE	13,34,541	
11.	Comverse Australia Pty. Limited	Reimbursement of expenses (Paid) to AE	1,97,921	

5. On the basis of functional profile of the taxpayer under Software Development, Provision of professional (Customization, configuration etc.) Services and Provision of maintenance (trouble shooting) Services segment, these three international transactions were benchmarked using a single set of comparables which are from the Software Industry. TNMM was considered as the 'MAM' & OP/OC was the PLI. The OP/OC of the taxpayer was calculated at 10%, 9% & 7% respectively for these 3 segments against average OP/OC of the 18 comparables at 9.13%. Thus, the transactions were stated to be at arm's length.

Some services were also availed from the AE and for this segment OPM of the taxpayer was calculated at 26.89% against average OPM of the comparables at 5.58%. The taxpayer had also provided some Sales and Post Sales Support Services to its AE and for this segment OP/OC of the taxpayer was calculated at 7% against average OP/OC of the comparables at 6.58%.

Thus, these transactions were stated to be at Arm's Length.

6. The TPO, however, vide its order dated 27.01.2014 determined an adjustment of Rs.5,78,66,602 as under:

a.	Software Development Services	Rs.3,45,49,016/-
b.	Technical Support Service Segment	Rs.2,33,17,586
Total (a + b)		Rs.5,78,66,602/-

7. The said adjustment was incorporated by the Assessing Officer ('AO') in the draft assessment order. Against the draft assessment order, the assessee filed its objections before the Dispute Resolution Panel ('DRP'). The DRP vide its direction dated 18.12.2014 confirmed the adjustment as made by the TPO/AO.

8. After taking into account the adjustment to ALP, as directed by the DRP, the AO passed the Final Assessment order under section 144C read with section 143(3) of the Act on 24.02.2015.

9. Aggrieved by such final assessment order dated 24.02.2015, the assessee preferred an appeal before the Hon'ble ITAT. The Hon'ble ITAT accepted the submissions of the assessee that the comparables chosen by the TPO were functionally dissimilar and were liable to be rejected vide its order dated 31.05.2017.

10. Being aggrieved by the impugned order dated 31.05.2017 of the Hon'ble ITAT, the Revenue has preferred the present appeal for consideration.

11. Only one question has been proposed by the Revenue which encompass all the comparables rejected by the Tribunal by analyzing the functionality, turnover and profile of the various comparables now being impugned before us. We propose to deal with the same sequentially as under:

SOFTWARE DEVELOPMENT SEGMENT

E-Infochips Bangalore Limited

12. The TPO had adopted E-Infochips whilst stating that the said comparable is primarily engaged in software development services and does not

provide IT enabled services. The TPO also alleged that even though the said company treats IT and ITES as one industry i.e., one segment, however, the Annual Report does not have any reference to any ITES services being performed by the company. The DRP had rejected the claim of the assessee for its exclusion. Before the ITAT, the assessee submitted that E-Infochips was functionally dissimilar to the profile of the assessee owing to the fact that E-Infochips was engaged in hardware designing, product reengineering, product life cycle management enterprises, IT consulting and IT enabled services. Further, it was also submitted by the assessee that the said company had insufficient segmental information as it reported only one segment. The finding the ITAT for its exclusion is as under:

> "*56. On perusal of relevant material on record, we find from annual report of this company is placed at 1-19 of the paper book that profit and loss account shows income from software services at Rs.43,04,66,481/-. Schedule 7 gives breakup of this income is as under:*
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> | | |
> |---|---|
> | *Income from software services* | *Rs.37,13,88,107* |
> | *Consultancy charges* | *Rs.5,90,78,374* |
>
> *57. In the directors report this company has been characterized as to be engaged in development of software as per specific requirement of clients. The reported segment of this comparable indicates that revenue from software development services includes revenue from IT enabled services also. And more so, this comparable has been characterized as having both software development and ITES segment into overall segment designated as software development division.*
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> *58. In the facts of the present assesse, the functions are only relating to software development to its AEs. No where functional profile indicates there has been an inclusion of IT enabled services into software development division. Therefore, in our considered opinion functions of this company cannot be held to be comparable with that of assessee.*

> *We, therefore, direct exclusion of this company from the list of comparables."*

13. The counsel for the revenue relies upon the order passed by the TPO and argued that the ITAT failed to appreciate the findings and observations given by the TPO. The ITAT has noted that in the directors report the comparable company has been characterized as to be engaged in development of software as per specific requirement of clients revenue from software development services includes revenue from IT enabled services also. The ITAT has also noted that no where functional profile indicates that there has been an inclusion of IT enabled services into software development division and both the companies are having different functional profile. Said finding of fact that the comparable is functionally dissimilar has not been shown to be perverse by the Revenue and thus, the comparable has rightly been excluded by the ITAT.

<u>Infinite Data Systems Private Limited</u>

14. The TPO has selected this comparable whilst stating that the said company is primarily an IT service provider and hence comparable to the profile of the assessee. The said finding was upheld by the DRP. Before the ITAT, the assessee submitted that Infinite Data Systems was functionally dissimilar to the assessee since the said company was deriving its income from technical support and infrastructure management services. Additionally, it was submitted by the assessee that Infinite Data Systems had only one customer i.e., Fujitsu Services Limited. The ITAT while excluding the said comparable has observed as under:

> "*61. We have perused documents relied upon by both sides, it is observed that this company is engaged in a wide array of services like technical consulting, design and development of software maintenance, system integration, implementation and testing will and infrastructure management services as has been mentioned at page 36 of the paper book. It has also been mentioned therein that, it is not possible to give a quantitative details of sales from these individual sectors. Further, it is observed that this company*

> *enters into direct contract with its customer which is not case with assessee before us. This company is also exposed to a huge customer risk as there is only one sole customer. This company has reported its segment based on location of its customer as a primary segment for reporting. Thus, it has reported revenue based on location of its customer,. In the case of assessee before us there is no risk as far as present services rendered to its AE's are concerned. It is also been observed that assessee receives its payments as has been agreed upon between AE and assessee even though work finally done is unsuccessful or even if any substantial rework is required to be filial product. Thus assessee before us does not face any business risk. This is it is also observed that this company is into various segments for which independent information is not available which makes this company are not comparable with assessee.*
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> *62. On the basis of above discussion we direct exclusion of this company from final list of comparables."*

15. The counsel for the revenue relies upon the order passed by the TPO and argued that the ITAT failed to appreciate the findings and observations given by the TPO. But the finding of fact recorded by the ITAT have not been shown to be perverse and cogent reasons have been given showing the dissimilarity of the comparable to the assessee and thus, the exclusion of the above comparable cannot be faulted with.

SALES AND POST SALES SUPPORT SEGMENT

Engineers India Limited

16. The TPO selected the said comparable as being functionally comparable to the profile of the assessee. The said finding was confirmed by the DRP. Before the ITAT, the assessee contended that Engineers India Limited ('EIL') was functionally dissimilar to the profile of the assessee owing to the fact that the said company provided complete range of project services ranging from conceptualization, planning, designing, engineering and construction activities to meet specific requirements of its clients in various fields like petroleum

refining, petrochemicals, pipeline, offshore oil and gas, onshore oil and gas, terminals and storages, mining and metallurgy and infrastructure. Hence, it was submitted by the assessee that the said company was an end to end engineering service provider and that the said company spent significant amount on research and development. The ITAT while directing its exclusion has observed as under:

> "*77. We have considered arguments of the rival submissions advanced by both sides. It is observed that assessee provides support services to its AE in respect of sale of software by AE. Bug fixing is also a part of post sales support services, which may be treated partly as function of technical nature, but the same cannot be compared with consultancy provided in the field of engineering infrastructure field. We see no similarity in the kinds of services rendered by assessee vis-à-vis this company. We accordingly direct for the exclusion of this company from the list of comparables.*"

17. The said finding of fact that the comparable is functionally dissimilar has not been shown to be perverse by the Revenue and thus, the ITAT has rightly concluded that the said comparable has to be excluded.

<u>IBI Chamatur Engineering and Consultancy Ltd.</u>

18. The said comparable was chosen by the TPO as being functionally comparable to the profile of the assessee which was confirmed by the DRP. Before the ITAT, it was submitted by the assessee that IBI Chematur was not functionally similar owing to the fact that it provided planning and engineering services for the chemical manufacturing industry. It was further submitted by the assessee that the said company provided a wide range of services, detailed engineering, intelligent 3D plant modelling, 2D conversion services, smart plant instrumentation inspection services, project planning and management supervision services. The ITAT while directing exclusion of IBI Chematur as not being functionally comparable to the profile of the assessee has held as

under:

> "*80. We have perused records in the light of submissions advanced by both the sides we agree with Ld. Counsel that this company is involved in huge engineering projects; which are turnkey in nature. Such activities cannot be compared with technical services like bug fixing or provisions of warranty servicers etc. rendered by assessee. From the financial report of company it is observed that this company is also responsible for setting up till performance of work undertaken for a particular client. Therefore, in our considered view services rendered by this company cannot be considered to be merely technical in nature.*"

19. The finding recorded by the ITAT have not been shown to be perverse and cogent reasons have been given showing the dissimilarity of the comparable to the assessee and thus, the exclusion of the above comparable cannot be faulted with.

<u>RITES Limited</u>

20. The TPO selected this comparable while stating that only the consultancy services segment has been considered which was similar to the technical services provided by the assessee. The said finding was confirmed by the DRP. Before the ITAT, it was submitted by the assessee that the said comparable was engaged in providing concept to commissioning consultancy, design, engineering and turnkey solutions in the field of transportation, infrastructure and related technologies of the highest professional standards and hence the same ought to be rejected. Additionally, it was submitted by the assessee that the said company had been recognized as a think tank for development of national policies, priorities and strategies in the field of transportation and infrastructure sector. The ITAT while directing its exclusion has observed as under:

> "*We have perused the submissions advanced by both the sides in the light of records placed before us. We find that only*

> *'Consultancy service segment" of this company has been considered by the TPO leaving the other business segments aside. It is also observed that this company is imparting high-end technical services which cannot be compared with the low-end sale and post sale services rendered by assessee. We also find that this company is a Govt. of India Undertaking providing end to end solutions for turn-key project. In the following cases, the Tribunal has held that RITES Ltd. is engaged in providing engineering segments and to end to end solutions and therefore not functionally comparable with marketing support segments.*
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> *(a) Asstt. CIT v. Chemtex Global Engineers (P) Ltd., [2014] 147 ITD 488/[2013] 135 taxmann.com 351 (Mum.-Trib)*
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> *(b) Dy. CIT v. MCI Com India (P) Ltd. [2012] 53 SOT 290 (URO)/25 taxmann.com 520 (Delhi)*
>
> *(c) Yum Restaurants (India) (P) Ltd. v. ITO [2014] 48 taxmann.com 384 (Delhi)*
>
> *(d) Nortel Networks India (P) Ltd. v. Addl. CJT [2014] 44 taxmann.com 26 (Delhi-Trib.)*
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> *Considering the facts discussed herein above in the light of the judicial decisions mentioned herein above, we direct for the exclusion of this company from the final list of comparables."*

21. The said finding of fact that the comparable is functionally dissimilar has not been shown to be perverse by the Revenue and thus, the comparable rightly been excluded by the ITAT.

<u>TCE Consulting Engineers Ltd.</u>

22. The TPO has selected this comparable while stating that the said company is engaged in various project engineering services which are in the nature of technical services and hence comparable to the profile of the assessee. The said finding was confirmed by the DRP. Before the ITAT, it was submitted by the assessee that the said company ought to be rejected owing to the fact that it was engaged in engineering consultancy services in the nature of design engineering, procurement assistances and inspection and expediting, construction and supervision and commissioning support. It was further

submitted by the assessee that the said company had a huge brand value and hence the same was liable to be rejected. The ITAT while directing its exclusion had observed as under:

> "*We have perused the submissions advanced by in the light of the records placed before us. The company is involved in activities beyond engineering design. It is engaged in activities that extend from concept to engineering. Whereas the assessee provides services as a captive unit to its overseas AEs. The diversified functions of this comparable company include pre-project activities, procurement assistance, project management, commissioning and coordination, inspection, construction and supervision. Further, there is no segmental accounting in the annual report of the Company which provides profitability, for the engineering design segment. This, in view of our discussion and also following the precedence in the aforesaid cases, we hold that TCS Consulting cannot be held to be comparable company.*"

23. The counsel for the revenue relies upon the order passed by the TPO and argued that the ITAT failed to appreciate the findings and observations given by the TPO. The finding recorded by the ITAT have not been shown to be perverse and cogent reasons have been given showing the dissimilarity of the comparable to the assessee and thus, the exclusion of the above comparable cannot be faulted with in any manner.

24. The above findings of fact by the ITAT regarding exclusion of the comparables are thus upheld and the same do not merit any interference. The questions of law are answered against the revenue and in favour of the assessee. Similar views have been taken by this Hon'ble Court in the case of **PCIT v Equant Solutions India Pvt. Ltd.** (ITA No. 419/2016), the Bombay High Court in the case of **CIT vs. PTC Software** (395 ITR 176) and in the case of **Principal Commissioner of Income Tax Vs. Barclays Technology Centre India Pvt. Ltd.** (409 ITR 108) and by the Karnataka High Court in **Principal Commissioner of Income Tax vs. Softbrands India Pvt. Ltd.** (406 ITR 513).

25. The appeal stands disposed of in the above terms.

26. Since the main case has been decided, the pending Miscellaneous Application, if any, also stands disposed of.

(AJAY TEWARI)
JUDGE

(AVNEESH JHINGAN)
JUDGE

05.02.2020
pooja sharma-I

Whether speaking/reasoned Yes/No
Whether Reportable : Yes/No