

आयकर अपीलीय अधिकरण, 'डी' न्यायपीठ, चेन्नई।
IN THE INCOME TAX APPELLATE TRIBUNAL
'D' BENCH: CHENNAI

श्री वी. दुर्गा राव, माननीय न्यायिक सदस्य एवं
श्री जी. मंजूनाथा, माननीय लेखा सदस्य के समक्ष
BEFORE SHRI V. DURGA RAO, HON'BLE JUDICIAL MEMBER AND
SHRI G. MANJUNATHA, HON'BLE ACCOUNTANT MEMBER

आयकर अपील सं./ITA No.733/Chny/2017
निर्धारण वर्ष /Assessment Year: 2012-13

M/s.Mega Soft Ltd.,
No.85, Kutchery Road,
Mylapore, Chennai-600 004.

[PAN: AABCM 8933 A]
(अपीलार्थी/Appellant)

v. The Dy. Commissioner –
of Income Tax,
Corporate Circle-4(1),
Chennai.

(प्रत्यर्थी/Respondent)

अपीलार्थी की ओर से/ Appellant by : Mr.M.Muraleedhara Reddy,CA
&
Mr.Nagaprasad, CA
प्रत्यर्थी की ओर से /Respondent by : Dr.S.Palani Kumar, CIT
सुनवाई की तारीख/Date of Hearing : 28.07.2022
घोषणा की तारीख /Date of Pronouncement : 21.09.2022

आदेश / ORDER

PER G. MANJUNATHA, ACCOUNTANT MEMBER:

This appeal filed by the assessee is directed against final Assessment Order passed by the AO u/s.144C(13) of the Income Tax Act, 1961 dated 31.01.2017, in pursuant to directions of the Dispute Resolution Panel-2, Bengaluru, u/s.144(5) of the Income Tax Act, 1961 dated 26.12.2016 and pertains to assessment year 2012-13.

2. The assessee has raised the following grounds of appeal:

1. The Assessing Officer (AO) ' Dispute Resolution Panel (DRP) erred in making upward adjustment in Arm's Length Price (ALP).

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- 2. The AO/DRP erred in rejecting the Comparable Uncontrolled Price (CUP) method in the current year without passing a reasoned order, even when there is no change in facts of the case and ignoring the fact that for the earlier years the same methodology was followed and accepted by the department consistently.*
- 3. The AO/DRP erred in applying the generalized literature on application of CUP without discussing as its applicability to facts of the Appellant's case?*
- 4. The AO/DRP erred in choosing Transaction Net Margin Method (TNMM) as the most appropriate method without any reasoned order and choosing the same by default on rejection of CUP method?*
- 5. The DRP erred in substituting TNMM over CUP method as the most appropriate method?*
- 6. The DRP/AO failed to see that they cannot take different stand on same set of facts on the applicability of quantum of services provided, quality and nature of services provided, geographical location of the customers, credit, market risk when applying CUP method and when applying TNMM?*
- 7. Without prejudice to the ground that TNMM is not the most appropriate method, the DRP/AO erred in making a separate upward adjustment on Corporate guarantee provided to the Associated Enterprise (AE) when adopting TNMM as most appropriate method.*
- 8. The AO/DRP erred in not disclosing the standard filters used by him/them for choosing comparables under TNMM?*
- 9. The AO/DRP erred in not disclosing the arithmetical computation of determining the PLI (Operating Profit/Operating Cost) of the Appellant under TNMM.*
- 10. Whether the AO/DRP is right in arbitrarily rejecting the CUP method and choosing TNMM without justifying it as Most Appropriate Method randomly picking their choice comparables without disclosing the filters used for choosing such comparables?*
- 11. Whether the AO/DRP is right in choosing companies such as Larsen & Toubro Infotech Ltd and Mindtree Ltd and Persistent Systems Ltd having turnover of Rs 2959.56 crores, 1915.2 crores and 810.36 crores respectively when the Appellant's turnover is less than 50 crore?*
- 12. Whether the AO/DRP is right in not providing the Appellant the data of the Comparable Companies and further without any discussion on such data of the comparable companies?*
- 13. Whether the AO/DRP is right in enhancing the adjustment without any basis and reasoning?*
- 14. Whether the PLI adopted by the AO/DRP in respect of comparables is arbitrary or not. More so, when no data of the comparable is not provided to the Appellant.*
- 15. Whether the AO/DRP is right in making upward adjustment on account of corporate guarantee provided by the Appellant to its Associated Enterprises?*

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16. Whether the AO/DRP is right in not disclosing the most appropriate method for determining Arm's Length Price on provision of corporate guarantee?

17. Whether the AO/DRP is right in fixing the arm's length price for providing corporate guarantee @ 1% on the guarantee provided?

18. Whether the AO/DRP is right in ignoring the basic condition of section 92B, which describes that to attract the provisions of transfer pricing, it should have a bearing on the profits, income, losses or assets of such enterprises.

19. The AO/DRP failed to appreciate that the Appellant in providing the corporate guarantee without incurring any cost and that notional income cannot be imputed on the Appellant arbitrarily.

In light of the above grounds and such other grounds that may raise at the time of hearing, it is prayed that the Hon'ble Tribunal may allow the appeal and delete the additions made by the AO/DRP and render justice.

3. The brief facts of the case are that the assessee company is engaged in the business of providing IT consulting services to its AEs XIUS Corp, USA, Megasoft Consultants Sudan Bhd and non-AEs like Tata Communications, Canada. The return of income for the AY 2012-13 was filed on 22.12.2012 declaring total income of Rs.1,00,18,450/-. During the year under consideration, the assessee has entered into various international transactions with its AEs. The assessee has selected CUP as most appropriate method and bench marked transactions with its AE and claimed to be a tested party. During the course of assessment proceedings, the TPO rejected the CUP method adopted by the assessee and has adopted TNMM as most appropriate method. The TPO, after conducting fresh TP study, has selected certain comparables and then, compared with operating margin of the assessee and suggested TP adjustment of Rs.4,40,89,432/- towards AE sales and also made upward adjustment on corporate guarantee of Rs.58,80,000/- @ 1% on total corporate guarantee given by the assessee. Pursuant to TP adjustment as suggested by the TPO, the AO

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has passed draft assessment order u/s.144C of the Act, on 30.03.2016 and made downward adjustment of Rs.4,99,69,432/-. The assessee has filed objections before the DPR, Panel-2, Bengaluru, against draft assessment order passed by the AO and challenged TP adjustment as suggested by the TPO. The assessee has challenged rejection of CUP as most appropriate method and selection of TNMM to bench mark international transactions. The assessee had also challenged computation of operating margins by considering two extraordinary items of bad debts written off and forex fluctuation loss. The assessee had also challenged TP adjustment on corporate guarantee and argued that rate at which the TPO benchmarked on corporate guarantee is higher side. The DRP after considering relevant submissions of the assessee and also taken note of various facts, rejected arguments of the assessee on the issue of most appropriate method and upheld the findings of the TPO in selection of TNMM as most appropriate method and then, upheld the computation of operating margin to make TP adjustment towards AE sales. The DRP has also upheld the adjustment proposed for corporate guarantee @1% of total guarantee given by the assessee to its AE. The AO has passed final assessment order in pursuance to the directions of the DRP and has made additions towards AE sales on corporate guarantee as suggested by the TPO. Aggrieved by the final assessment order, the assessee preferred an appeal before us.

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4. The first issue that came up for our consideration from the assessee's appeal is TP adjustment on AE sales amounting to Rs.4,40,89,432/-. The facts with regard to the impugned dispute are that during the year under consideration the assessee has entered into international transactions with its AEs for providing software consultancy services. The assessee has adopted CUP method to bench mark transactions with its AE. The assessee has considered internal CUP on the basis of similar services rendered to non-AE. The AO has rejected CUP method adopted by the assessee on the ground that the assessee could not furnish necessary working details by matching one to one price with quantity and quality of services with non-AE transactions and also third parties and thus, rejected CUP method and has adopted TNMM as most appropriate method. The TPO has selected 9 comparables with average margin of 18.27%. The TPO had also re-worked PLI of the assessee after considering bad debts written off and forex fluctuation loss as operating expenses and has worked out OP/OC @5.01% and then, compared margin of the assessee with comparables and made TP adjustment of Rs.4,40,89,432/- towards AE sales.

5. The Ld.AR for the assessee submitted that the DRP erred in rejecting CUP as most appropriate method without appreciating the fact that for earlier two assessment years, the assessee has adopted CUP as most appropriate method and the TPO has accepted CUP method without any adjustments towards international transactions with its AEs. The Ld.AR for

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the assessee referring to various documents and Paper Books filed by the assessee submitted that the turnover of the assessee consisting of 74% from AE transactions and 26% from non-AE transactions. The assessee has earned margin on sales @18.81% and margin on cost of 24.61%. The assessee has considered internal CUP on the basis of transactions with third party customers and claimed margin earned on AE sales is higher than the third party sales. Therefore, he submitted that when there is no change in facts and circumstances of the case for the impugned assessment year when compare to previous two assessment years, then there is no reason for the TPO/DRP to reject the CUP method adopted by the assessee for bench marking international transactions with its AEs. In this regard, he relied upon the decision of the Hon'ble Supreme Court in the case of Radhasoami Satsang v. CIT reported in [1992] 193 ITR 321 (SC).

6. The Ld.DR, on the other hand, supporting the order of the DRP submitted that in earlier assessment years the margin of the assessee was 23.64% for the AY 2011-12 and 21.88% for the AY 2010-11. Therefore, under those facts, the TPO has accepted CUP method adopted by the assessee for bench marking international transactions with its AEs. However, for the impugned assessment year, the margin has been drastically come down and therefore, the TPO has rejected CUP method adopted by the assessee on the ground that non-furnishing of necessary details and has adopted TNMM as most appropriate method. Therefore, the Ld.DR further submitted that there is no error in the reasons given by

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the TPO/DRP to select TNMM as most appropriate method and their orders should be upheld.

7. We have heard both the parties, perused the materials available on record and gone through orders of the authorities below. The assessee has adopted CUP as most appropriate method to bench mark international transactions with its AEs and considered internal CUP on the basis of third party export sales to non-AE. The assessee has followed CUP method consistently for last several years including immediately preceding AYs 2010-11 & 2011-12. It is an admitted fact that the TPO has accepted CUP method for the AYs 2010-11 & 2011-12. However, disputed CUP method for the impugned assessment year only on the ground that the assessee could not file necessary details of working of quantity and quality of services rendered to AE with the third party non-AE suppliers. Except this, the TPO never given any credible reasons to reject CUP method selected by the assessee. In fact, the TPO had accepted the fact that there is no change in the facts and circumstances of the case for the impugned assessment year when compared to previous two assessment years. It is also an admitted fact that the assessee has followed internal CUP on the basis of third party export sales to non-AE and further, margin earned from third party non-AE sales is lesser than the margin earned from sales to AE. Therefore, we are of the considered view that under these facts and circumstances, there is no reason for the TPO to reject CUP method selected by the assessee to bench mark international transactions with its AEs when

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the assessee was consistently following said CUP method. Further, the assessee has filed comparable transactions of third party sales and proved that margin earned from AE transactions is higher than the margin earned from non-AE transactions. It is a well settled principle of law by the decision of the Hon'ble Supreme Court in the case of Radhasaomi Satsang (supra) that although, **res judicata** is not applicable to Income Tax proceedings, but rule of consistency needs to be followed unless there is a change in facts and circumstances which requires to be considered a different approach or method for considering any issue. In this case, as pointed out by the Ld.AR for the assessee, there is no change in the facts and circumstances of the case for the impugned assessment year when compared to previous two years and thus, we are of the considered view that the TPO ought to have followed CUP method selected by the assessee for benchmarking international transactions with its AEs. The DRP without appreciating the above facts, has simply upheld TNMM as most appropriate method and upheld the TP adjustment as suggested by the TPO. Hence, we reverse the findings of the DRP and direct the TPO to consider CUP as most appropriate method to bench mark international transactions with its AEs. Accordingly, we direct the TPO to delete the addition made towards TP adjustment made towards AE sales.

8. The next issue that came up for our consideration from the assessee's appeal is TP adjustment towards corporate guarantee given by the assessee

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to its AE. The assessee company has given a corporate guarantee for the foreign currency loan of US from Axis Bank, Hong Kong to its AE XIUS holdings USA. The AO has computed guarantee commission @1% on total corporate guarantee given by the assessee to its AE and has made adjustment of Rs.58,80,000/-.

9. We have considered relevant materials on record. As regards the arguments of the Ld.AR for the assessee that corporate guarantee **per se** itself is not an international transaction, we find that after amendment of definition of international transaction, corporate guarantee given by any entity to its AE falls under the definition of international transactions in terms of sec.92B of the Act and thus, any corporate guarantee given by the assessee to its AE is an international transaction, which needs to be benchmarked. Further, when it comes to rate, at which, such guarantee commission needs to be benchmarked, then bank guarantee given by the commercial banks cannot be a yardstick to apply to corporate guarantees given by an entity. Further, the guarantee commission rate is depending upon the facts of each case and the risk involved in the transactions between the assessee and its AE. The Hon'ble Madras High Court in the case of PCIT v. Redington (India) Ltd., reported in [2021] 430 ITR 298 (Mad) had considered the issue of corporate guarantee given by an entity to AEs and after considering relevant facts held that rate adopted by the TPO on the basis of internal comparable uncontrolled price charged by the bank @ 0.85% is reasonable for benchmarking corporate guarantee. The

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Hon'ble Bombay High Court in the case of CIT v. Everest Kanto Cylinder Ltd. reported in (2015) 378 ITR 57 (Bom.) had considered an identical transaction and held that 0.5% is appropriate rate for bench marking corporate guarantee given by the assessee to its AE. Therefore, considering the facts and circumstances of the case and also by following the decision of the Hon'ble Bombay High Court in the case of Everest Kanto Cylinder Ltd. (supra), we direct the TPO to benchmark corporate guarantee fees @ 0.5% on total corporate guarantee given by the assessee to its AE.

10. In the result, the appeal filed by the assessee is partly allowed.

Order pronounced on the 21st day of September, 2022, in Chennai.

Sd/-

(वी. दुर्गा राव)

(V. DURGA RAO)

न्यायिक सदस्य/**JUDICIAL MEMBER**

Sd/-

(जी. मंजूनाथा)

(G. MANJUNATHA)

लेखा सदस्य/**ACCOUNTANT MEMBER**

चेन्नई/Chennai,

दिनांक/Dated: 21st September, 2022.

TLN

आदेश की प्रतिलिपि अग्रेषित/**Copy to:**

1. अपीलार्थी/Appellant
2. प्रत्यर्थी/Respondent
3. आयकर आयुक्त (अपील)/CIT(A)
4. आयकर आयुक्त/CIT
5. विभागीय प्रतिनिधि/DR
6. गार्ड फाईल/GF