

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

**BEFORE SHRI GEORGE GEORGE K., JUDICIAL MEMBER
AND
SHRI B.R. BASKARAN, ACCOUNTANT MEMBER**

IT(TP)A No.1824/Bang/2017
Assessment Year: 2013-14

ARM Embedded Technologies Pvt. Ltd. Bagmane World Technology Pvt. Ltd., SEZ Citrine Block, 5 th Floor, Marathahalli Outer Ring Road, Doddanakundi Village Mahadevapura Bangalore 560 048 PAN NO : AAECA1582E	Vs.	DCIT Circle-1(1)(1) Bangalore
APPELLANT		RESPONDENT

Appellant by	:	Shri T. Suryanarayana, A.R.
Respondent by	:	Shri Muzaffar Hussain, D.R.

Date of Hearing	:	15.06.2021
Date of Pronouncement	:	12.07.2021

ORDER

PER B.R. BASKARAN, ACCOUNTANT MEMBER:

The assessee has filed this appeal challenging the assessment order dated 7.7.2017 passed by the Assessing Officer for assessment year 2013-14 u/s 143(3) r.w.s 144C of the Act in pursuance of directions given by Ld. Dispute Resolution Panel (DRP).

2. Though the assessee has raised many grounds in this appeal, they relate to the following issues: -

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- a) Transfer pricing adjustment made in respect of provision of software development services.
- b) Addition made u/s 28(iv) of the Act treating the assets received free of cost as benefit received by the assessee.
- c) Non-granting of MAT credit.

The grounds relating to charging of interest u/s 234B and 234C are consequential in nature.

3. The assessee is a subsidiary of M/s. ARM Ltd., UK. The assessee is engaged in the business of providing software development services and marketing support services to its Associated Enterprises. The assessee is contesting the transfer pricing adjustments made in respect of software development services. The revenue from software development services was Rs.131.22 crores. The TPO made TP adjustment of Rs.4.93 crores, which stood enhanced to Rs.5.42 crores on giving effect to the directions of Ld. DRP.

4. The assessee adopted TNM method as most appropriate method and OP/OC as profit level indicator. The assessee declared profit margin of 14.91% for the year under consideration. The assessee selected 9 comparable companies, whose average arithmetic mean of margin was 10.28%. Accordingly, the assessee contended that its international transaction in providing software development services was at arm's length.

5. The TPO did not accept the TP study of the assessee. He selected following 7 comparable companies whose average margin was 20.90%. After giving working capital adjustment of 1.69% the average margin was arrived at 19.21% by TPO. Accordingly, he made transfer pricing adjustment of Rs.4.93 crores. The comparable selected by TPO are given below:

<i>Sl.No.</i>	<i>Name of the company</i>	<i>Mark-up on Total Costs (WC-Unadjusted) (in %)</i>	<i>Mark-up on Total Costs (WC-adjusted) (in %)</i>
1.	<i>CG-VAK Software Exports Ltd.</i>	20.54	19.32
2.	<i>ICRA Techno Analytics Ltd.</i>	17.10	12.25
3.	<i>Larsen and Toubro Infotech Ltd.</i>	26.06	24.93
4.	<i>Mindtree Ltd. (seg.)</i>	18.19	16.65
5.	<i>Persistent Systems Ltd.</i>	28.27	26.28
6.	<i>RS Software (India) Pvt. Ltd.</i>	17.41	17.67
7.	<i>Tech Mahindra Ltd. (seg)</i>	18.72	17.38
	AVERAGE MARK-UP	20.90	19.21

6. The Ld. DRP directed exclusion of 3 companies namely ICRA Techno Analytics Ltd., Persistent Systems Ltd. and Tech Mahindra Ltd. Accordingly, the ld. DRP confirmed selection of remaining 4 comparable companies. The order passed by Ld. DRP resulted in enhancement of TP adjustment to Rs.5.42 crores.

7. The ld. A.R. submitted that the assessee seeks exclusion of two comparable companies namely, M/ s. CG-VAK Software Exports Ltd and M/s. Larsen & Toubro Infotech Ltd. He submitted that these companies have been held to be not a good comparable by the coordinate bench in the case of NXP India Pvt. Ltd. Vs. DCIT (2020) 116 Taxmann.com 421 in the order passed for assessment year 2013-14. Accordingly, he pleaded for exclusion of these two companies. The Ld. A.R. further submitted that the assessee seeks inclusion of two companies namely M/s. Akshay Software Technologies Ltd. & M/s. R. Systems International Ltd. These two companies have been held to be a good comparable by the coordinate bench in the case of NXP India Pvt. Ltd. (supra).

8. The Ld. D.R. on the contrary submitted that the assessee has included CG-VAK Software Exports Ltd. in its TP study as a

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comparable company. In the case of NXP India Pvt. Ltd., the assessee therein did not consider CG-VAK software Exports Ltd., as its comparable in its TP study. Since the assessee had included CG-VAK software Exports Ltd., there was no occasion for the TPO to examine this company. Accordingly, the ld. A.R. prayed that this comparable company may be restored to the file of TPO for examining it afresh. With regard to M/s R. Systems International Ltd., which the assessee has sought inclusion, the Ld. D.R. submitted that this company has failed in RPT filter of 25%, as observed by TPO in page 11 of order passed by him. Accordingly, the Ld. DR submitted that this company should not be included. With regard to M/s. Akshay Software Technologies Ltd., the Ld. D.R. invited our attention to page 27 of the order passed by TPO, wherein the TPO has held that functional profile of this company is different from that of a software development activity.

9. In the rejoinder, the Ld. A.R. submitted that it is true that the assessee had included M/s. CG-VAK Software Exports Ltd. as its own comparable. However, there is no bar that the assessee cannot challenge the same before the higher forums. In this regard, the Ld. A.R. placed his reliance on the decision rendered by Hon'ble Bombay High Court in the case of CIT Vs. M/s. Tata Power Solar Systems Ltd. (Income Tax Appeal No.1120 of 2014 dated 16.12.2016). In the above said case, the Tribunal had held that merely because the assessee has included certain comparable companies in the list of comparable companies in its TP study, the same would not by itself estop a party from establishing that these companies are not comparable. In the above said case, the assessee had sought exclusion of two companies named M/s. Indo Wind Energy Ltd. And BF Utilities Ltd. The observations made by Hon'ble Bombay High Court upholding the view taken by the Tribunal are extracted below:-

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(c) By the impugned order, the Tribunal allowed the Respondent Assessee's appeal. It held that merely because an Assessee has included M/s. Indowind Energy Ltd. And B.F. Utilities Ltd. in its list of comparables to determine the ALP would not by itself estop a party from establishing that these companies are not comparable. The impugned order found that the two comparables viz. M/s. Indowind Energy Ltd. and B.F. Utilities Ltd., were engaged in completely different line of business i.e. generation of wind energy while the Respondent-Assessee is engaged in generation of solar energy. Thus, not functionally comparable. In the above view, the impugned order on the basis of Function, Assets & Risk (FAR) analysis excluded M/s. Indowind Energy Ltd. and B.F. Utilities Ltd. from the list of final comparables to determine the ALP.

(d) We find that the impugned order of the Tribunal holding that a party is not barred in law from withdrawing from its list of comparables, a company, if the same is found to have been included on account of mistake as on facts, it is not comparable. The Transfer Pricing Mechanism requires comparability analysis to be done between like companies and controlled and un-controlled transactions. This comparison has to be done between like companies and requires carrying out of FAR analysis to find the same. Moreover, the Assessee's submission in arriving at the ALP is not final. It is for the TPO to examine and fine out the companies listed as comparables which are, in fact comparable. The impugned order has on FAR analysis found that M/s. Indowind Energy Ltd. and B.F. Utilities Ltd. are not comparable. They are in a different area i.e. wind energy while the Respondent-Assessee is in the field of solar energy.

(e) In the above view, question (a) as proposed does not give rise to any substantial question of law. Thus, not entertained."

10. The Ld. A.R. further submitted that the TPO has excluded M/s R. Systems International Ltd, only on the reason that the company has a different financial year and the same is evident from page 28 of the order of TPO. With regard to M/s. Akshay Software Technologies Ltd., the Ld. A.R. submitted that it has been held to be functionally comparable in the case of M/s NXP India Pvt Ltd (supra).

11. We heard rival contentions on this issue and perused the record. We notice that the Ld A.R has convincingly refuted the arguments of Ld D.R on the exclusion of M/s C.G Vak Software Exports Ltd and also on objections raised for inclusion of two comparable companies. In any case, the claim of the assessee for inclusion/exclusion is covered by the decision rendered by the co-ordinate bench in the case of M/s NXP India Pvt Ltd (supra). For the sake of convenience, we extract below the observations made by the co-ordinate bench in respect of the above said four companies in the case of M/s NXP India Pvt Ltd:-

(A) COMPANIES SOUGHT TO BE EXCLUDED:-

I. Larsen & Toubro Infotech Limited

22. The learned AR relied on the order of the co-ordinate Bench in the case of Metric Steam Infotech (India) (P.) Ltd. v. Dy. CIT [IT (TP) Appeal No.1418 & 2735 (Bang.) of 2017, dated 27-2-2019], wherein the Tribunal held as under:—

"11. As far as L&T Infotech Ltd. and Persistent Systems Ltd. are concerned, our attention was drawn to the decision of ITAT Hyderabad Bench in the case of M/s. EPAM Systems (I) P. Ltd. v. ACIT, ITA No.2122/Hyd/2017 for AY 2013-14, order dated 20-11-2017. Vide para 12 of the decision, the Tribunal took the view that Persistent Systems Ltd. was into software products and software solutions and no segmental details were available and therefore the profit margin in the software development services segment could not be compared with the assessee's profit margin. As far as L&T Infotech Ltd. is concerned, the Tribunal vide para 17 of the aforesaid order came to a similar conclusion to hold that L&T Infotech should not be regarded as a comparable company. In the light of judicial precedents which remain uncontroverted, we are of the view that the aforesaid two comparable companies should be excluded from the list of comparable companies. "

22.1 *It was also brought to our notice that in earlier year, Larsen & Toubro Infotech Limited has incurred expenditure on "cost of brought out items for resale at Rs.27,10,89,274 for which he drew our attention to the financial statement of Larsen & Toubro Infotech Limited placed at paper book page No.1081, which is absent in the case of present assessee. He also submitted that it has huge intangible assets and brand value in software at Rs.143,61,95,196 and it has intangible asset in the form of business rights to the tune of Rs.153,42,45,196 as shown in the Fixed Assets as on 31.03.2013 placed at paper book page No.1078. Being so, in our opinion, it cannot be compared with the assessee's case. Accordingly, we direct the TPO to exclude the same from the list of comparables.*

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III. C G Vax Software & Exports Limited

24. The learned AR submitted that this company should be excluded for the reason that C G VAX Software & Exports Limited is engaged in software development and sale of products which involves high degree of R & D expenditure and to demonstrate the same, he drew our attention to the paper book page Nos.1018 and 1034 and submitted that the nature of the business of software development involves inbuilt, constant Research and Development as a part of its process of manufacturing (development). The company is developing applications engines, re-usable codes and libraries as a part of its R & D activities. Further, it has intangible assets as shown in the financial statement as on 31.03.2013 at Rs.3,03,83,536 and it is also engaged in outsource product development, as is evident from the attached notes forming part of the accounts. The learned AR also submitted that C G VAK Software & Exports Limited was not considered as a comparable in the case of EPAM Systems India (P.) Ltd. v. Asstt. CIT [2018] 100 taxmann.com 335 (Hyd. - Trib.), the Tribunal held as under:—

"16. Having regard to the rival contentions and the material on record, we find that the assessee has raised its objections before 10 the TPO but he held that it is functionally similar. We have gone through the annual reports of CGVAK Software & Exports Ltd and find that the said company is having revenue from both software services and BPO services but there is no segmental data with regard to each of these transactions. Therefore, as held by the Coordinate Bench of the Tribunal in a number of cases (cited supra), we hold that this company cannot be taken as a comparable to the assessee-company. Accordingly, we direct the TPO to exclude this company from the final list of comparables. "

24.1 Similarly, in the case of ION Trading India (P.) Ltd. v. ITO [2016] 70 taxmann.com 349 (Delhi - Trib.), held as under:-

"21. We have considered the submission of the Id. counsel for the assessee and have considered the argument of the Id. DR that the assessee is not producing any product, however, we find that CG-Vak Software and Exports Limited is not only into computer software but it is a product manufacturer too. Since assessee is not into product manufacturing and the segmental details cannot be bifurcated from the financial details, we find that the assessee and the CG-Vak Software and Exports Limited are not comparables. Therefore, we are inclined to uphold the orders of the authorities below in rejecting this company as a comparable. We direct accordingly. "

24.2 In our opinion, there is force in the argument of the learned AR. M/s. C G VAX Software & Exports Limited is not only engaged in the business of computer software development, but also engaged in product manufacturing process,

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whereas the present assessee is not in product manufacture activity. M/s. C G VAX Software & Exports Ltd. owns huge intangible assets and also engaged in outsourced product development. In view of the foregoing reasons, we hold that the said company cannot be considered for inclusion in the list of comparables. We, therefore, direct the TPO to exclude the said company from the list of comparables.

(B) COMPANIES SOUGHT TO BE INCLUDED:-

III. R. Systems International Limited

31. This company has been rejected by the TPO on the reason that this company has different year ending as compared to that of the assessee company. As discussed in earlier paragraph, there is no dispute that R. Systems International Limited is functionally comparable to the assessee. Being so, as held in earlier paragraph, we direct the TPO to consider this company as a comparable.

IV. Akshay Software Technologies Limited

32. It was rejected by the TPO for the reason that the function of this company appears to be more in the nature of support services and I.T. enabled services. However, this company is engaged in providing professional services, implementation, support and maintenance of ERP products and other services. These are nothing but software development services, as is evident from Notes forming part of the financial statement, which is placed at paper book page No.1825. Further, the revenue from software services accounts for 99.45% of the total revenue of the company as evident from the financial statement placed on record at paper book page No.1831. Being so, we direct the TPO to consider this company as comparable to the assessee's case while selecting the comparables.

12. Following above said decision rendered by the co-ordinate bench, we direct exclusion of Larsen & Toubro Infotech Ltd and CG VAK Software Exports Ltd. We also direct inclusion of M/s R systems International Ltd and M/s Akshay Software Technologies Ltd. Accordingly, we direct the AO/TPO to redetermine the ALP of the transactions in terms of discussions made supra.

13. The next issue relates to the addition made u/s 28(iv) of the Act. The AO noticed from the notes given under Fixed Asset Schedule of the Annual Report that the assessee has received tangible assets worth Rs.12,65,000/- free of cost from its holding company (AE), i.e., ARM Limited, UK. The AO proposed to assess

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the above said amount as income of the assessee u/s 28(iv) of the Act as it was a benefit received in exercise of profession.

14. The assessee submitted before the AO that it is providing contract design & development services to its Holding company. Those services, inter alia, includes validation (testing), coding and verification of products developed by the holding company. On the basis of coding services provided by the assessee, the holding company produces products, which are required to be validated. Hence the holding company supplies sample products to the assessee company for testing and validation. The assets received free of cost are only those assets which are given to the assessee for testing and validation. Once the testing is completed, the assets are either returned to the holding company or disposed of. Accordingly, the assessee contended that it has not received any benefits.

15. In the alternative, it was submitted that the cost of these assets shall be NIL in terms of sec.43(1) of the Act and hence depreciation shall be NIL. This treatment prescribed by sec.43(1) and sec.32 would show that the assets received free of cost has already suffered taxation. Accordingly, it was contended that the provisions of sec.28(iv) should not be invoked again, as it will result in double taxation. We understand that the assessee has also submitted that the value of assets is NIL and hence it was not included in fixed assets schedule.

16. The AO did not accept the explanations of the assessee and accordingly assessed the above said amount of Rs.12,65,000/- as income of the assessee u/s 28(iv) of the Act. In this regard, the AO placed his reliance on the decision rendered by Hon'ble Madras

High Court in the case of CIT vs. Ramaniyam Home Private Limited (2016)(384 ITR 530).

17. The Ld DRP confirmed the order of AO with the following observations:-

*“Having considered the submission, it is not a disputed fact that the above asset (which has been capitalized in the books of account of the assessee) has been received free of cost and it is also an admitted fact that they have been provided by the parent company for testing of products developed for them. Even though it is claimed that “once the testing is completed, the assets are either returned to ARM UK or disposed off”, the assessee failed to substantiate with any evidence. **Further, such assets received, on a year to year basis, has been capitalized in the books of account** and therefore it clearly comes under the purview of clause (iv) of section 28. The contention that the assessee would not be entitled for depreciation on such assets as the actual cost under section 43(1) has to be taken at “NIL”, does not have any connection with the applicability of clause (iv) of section 28. Accordingly the above objection is rejected.”*

18. The Ld A.R submitted that, in order to invoke the provision of section 28(iv) of the Act, a benefit or perquisite ought to arise at the threshold. He submitted that the products received by the assessee from its AE are products which are required to be validated, since they have been developed on the basis of services rendered by the assessee. He submitted that these products were supplied purely on commercial expediency and it does not result in any benefit to the assessee. The Ld A.R also submitted that the capital assets received are not in the nature of “income” and hence it cannot be treated as a trading receipt. The Ld A.R placed his reliance on the following case law for this proposition:-

- (a) Mahindra & Mahindra Ltd vs. CIT (2003)(128 Taxman 394)(Bom)
- (b) Logitronics (P) Ltd vs. CIT (2011)(197 Taxman 394)(Delhi)

19. The Ld D.R, on the contrary, supported the orders passed by Ld DRP and the AO.

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20. We heard rival contentions on this issue and perused the record. We notice that the Ld DRP has observed that the assets received free of cost has been capitalized in the books of account. Accordingly, the Ld DRP has held that the same is liable to be taxed u/s 28(iv) of the Act. In fact, the assessee has shown the assets received free of cost as note under Fixed Assets Schedule, meaning thereby, they have not been included as assessee's own fixed assets. Hence the above said observation of Ld DRP is against the facts.

21. In our view, the benefit liable to be taxed u/s 28(iv) of the Act need not always be "revenue" in nature. Suppose a businessman receives a Car on achieving the sales target, the value of Car is liable to be assessed u/s 28(iv) of the Act, even though it constitutes capital asset in the hands of that businessman. The assessee has furnished the details of some of the assets received free of cost in its written submissions as under:-

- (a) Signigy Key jobs – 50 nos.
- (b) Site Assembly board
- (c) Versatile Express mother boards
- (d) Destream debugs.

The items listed in (a) to (c) are hardware items and item listed in (d) is a standard software. We have noticed earlier that the assessee has stated that the products have been received from its AE for validation purposes and the assets listed out do not support the claim of the assessee.

22. Be that as it may, in our view, the main criteria to be examined about applicability of sec. 28(iv) of the Act is whether the "right of ownership" of the products/assets have been transferred to the assessee herein by its AE or not in respect of the products sent free of cost. If the right of ownership of the products/assets have

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been transferred to the assessee, then their value is liable to be assessed as benefit u/s 28(iv) of the Act. On the other hand, if the right of ownership has been retained by the AE and they have been sent to the assessee for utilizing them in the work executed by the assessee for AE, then the value of assets cannot be assessed as benefit u/s 28(iv) of the Act. We notice that these factual aspects have not been brought on record either by the assessee or by the AO, without which it would not be possible to determine about applicability of provisions of sec.28(iv) of the Act. Accordingly, we are of the view that this issue requires fresh examination at the end of AO in the light of principles discussed supra. Accordingly, we restore this issue to the file of the AO. We also direct the assessee to furnish relevant details to the AO and also clarify to the satisfaction of the AO as to whether the right of ownership of the assets/products received free of cost has been transferred to it or not.

23. The next issue contested by the assessee relates non-granting of MAT credit. As this issue requires factual verification, we restore this issue to the file of the AO.

24. In the result, the appeal of the assessee is treated as allowed for statistical purposes.

Order pronounced in the open court on 12th Jul, 2021.

Sd/-
(George George K.)
Judicial Member

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

Bangalore,
Dated 12th July, 2021.
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.