IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH: 'I-1' NEW DELHI

BEFORE SHRI R. K. PANDA, ACCOUNTANT MEMBER
AND
MS SUCHITRA KAMBLE, JUDICIAL MEMBER

I.T.A .No. 4363/DEL/2010 (A.Y 2006-07)

Calance Software Pvt. Ltd. C/o Ravi Gupta, Advocate, D-10, Kailash Colony, New Delhi – 110048 **(APPELLANT)**	Vs	DCIT Circle-3 (1) New Delhi **(RESPONDENT)**

Appellant by	**Sh. P. C. Yadav, Adv.**
Respondent by	**Sh. Kumar Pranav, Sr. DR & Sh. Sanjay Bara, CIT DR**

Date of Hearing	**06.02.2018**
Date of Pronouncement	**23.03.2018**

ORDER

PER SUCHITRA KAMBLE, JM

This appeal is filed by the assessee against order dated 26.07.2010 passed by the Assessing Officer u/s 143(3) read with Section 144C of the Income Tax Act, 1961.

2. The assessee is a company engaged in providing the services such as software development and man power placing and filed its original return of income declaring an income of Rs.11,31,200/- and subsequently revised its return of income on 19/3/2008 and declared a loss of Rs.36,00,046/-. A reference was made to TPO by the Assessing Officer for determining the Arm's Length Price u/s 92CA(3) in respect of international transactions entered into by the assessee during F.Y. 2005-06. The Assessee has undertaken following international transaction:

S.No.	Description of transaction	Method	Value (in Rs.)
1	Software Development	CUP	2,15,04,878

The TPO determined the Arm's Length Price of the International Transactions at Rs. 2,95,01,518/-. The TPO further held that since the difference between the ALP and the value of international transaction booked is more than 5% of the international transaction, no benefit of the amended proviso to Sec. 92C(2) is available to the assessee. The TPO directed the Assessing Officer to enhance the taxable income of the assessee by Rs.79,96,640/-. The Assessee filed objection before the DRP. The DRP issued direction to the Assessing Officer regarding the depreciation on the computer accessories to segregate details relating to accessories and peripherals which can work only in connection with or with the aid of computer and assets which can work independently and accordingly allow admissible depreciation on these assets @60% or @15% as the case may be. Relating to transfer pricing issues, the DRP upheld the TPO's findings. As relating to 10A issue the DRP upheld the directions of the TPO/AO. The Assessing Officer disallowed the claim of the assessee u/s 10A as well as disallowed an amount of Rs.79,96,640 made on account of ALP and added back the same to the income of the Assessee. The Assessing Officer also made addition of Rs.22,230/- in respect of depreciation claimed on computer.

3. Being aggrieved by the said Assessment Order, the assessee filed appeal before us.

4. The Ld. AR submitted that the assessee has filed additional legal ground which was admitted on 16/1/2013 and the same was prayed to be adjudicated first. The additional legal ground is as follows:-

> "*The reference to the Transfer Pricing Officer u/s 92CA of the Income Tax Act, 1961 by the Assessing Officer was illegal being contrary to (i) the binding Instruction No. 3/2003, (ii) the provisions of Section 92CA and the*

binding decision of the Special Bench in the case of Aztec Software and Technology Services Ltd. 107 ITD 141 (Bang) (SB). Consequently, the impugned assessment is time barred and, therefore, bad in law."

5. The Ld. AR submits that as regards the legal ground, the reference made to the TPO is bad in law. There are two limbs of this ground. Firstly, the Assessing Officer has not taken any approval from the Commissioner in this regard and secondly, as the quantum of the international transaction is below Rs. 5 crore the Assessing Officer ought to have determined the ALP himself and not referred to the TPO. The order of the TPO makes it clear that quantum of international transaction is Rs.2,15,04,878/- which means the same is below the monetary limit of Rs. 5 crore. The Ld. AR submitted that limit of Rs. 5 crore is not mentioned anywhere in the provisions of Transfer Pricing, however, CBDT vide its Instruction dated 20.03.2003 being Instruction No. 03 of 2003 categorically provided that only those cases where the quantum of international transaction is above Rs. 5 crore would be referred to the TPO. The Ld. AR submitted that the CBDT made it clear that "it would be appropriate if a small number of cases are selected for scrutiny of transfer price and these are dealt with effectively." Therefore, it can be said that the reference made to the TPO was bad in law and hence the adjustment made by the TPO was also bad in law. This argument further finds support from the Instruction No. 3 of 2016 wherein it has been categorically mentioned that all references made to TPO, which are not in consonance with the instruction of Board, should be withdrawn. The Ld. AR relied upon the decision of the Jurisdictional High Court in case of CIT vs. SPL's Siddhartha Ltd. (2012) 345 ITR 223 and also relied upon the decision of Special Bench of this Tribunal in case of Aztec Software & Technology Services Ltd. vs. ACIT (2007) 107 ITD 0141 (SB).

6. The Ld. AR further submitted that the DRP vide order dated 2/7/2010 ignored the revised return filed by the assessee within the period of limitation as prescribed u/s 139 (5) of the Income Tax Act. The Ld. AR further submits

that the assessee has revised its return of income within the time prescribed u/s 139(5) of the Act and one year expires on 31st March 2008. The assessee filed revised return of income on 19/3/2008 which means that the period of limitation will not come in the way of the assessee. The Ld. AR submits that the assessee can revised his/return of income before the expiry of one year for the relevant assessment year after discovering any omission or any wrong statement therein.

7. The Ld. AR submitted that bona-fides of the assessee can be judge from the certificate of CA who had authorized the merger a valid merger, without there being a valid order of the High Court. The Ld. AR submitted that documents such as advice of merger on the basis of CA's certificate were found during the course of survey. Therefore it cannot be alleged that the documents were after thought. The Ld. AR further submitted that these documents would prove beyond doubt that the assessee was under bona-fide belief and has merged the two companies, on the basis of CA Certificate, without there being any order of High Court. The Ld. AR submitted that assessee revised its Return of Income on 19/03/2008, admittedly in the time allowed under section 139(5) of the Income Tax Act. Therefore, the Assessing Officer ought to have considered the revised return instead of original return. The Ld. AR further mentioned that while deciding the appeal of FBT, the ITAT in the case of present assessee, for the same assessment year, has directed the Assessing Officer to accept the revised return instead of original return. Therefore, the Assessing Officer was not correct in ignoring the revised return. The Ld. AR submitted that provisions related to furnishing of FBT return are prescribed under section 115 WD and provisions relating to revised return of FBT are prescribed as under section 115 WD (4). The Ld. AR submitted that the perusal of section 115 WD (4) would make it clear that the language of this sub-section as well as language of section 135 (5) is verbatim. Therefore, interpretation as adopted by the ITAT vis-à-vis FBT return may be adopted here for Income Tax Return. The Ld. AR submitted that in view of the above the revised return of

the assessee may be accepted and the matter may be restored to the AO for fresh adjudication. The Ld. AR submitted that it is settled position of law that revised return would replace the original return and has to be considered for all aspects which means, the original return become non-est a reference was made to the following cases:-

A Bico engineering Ltd Vs, CIT 148 ITR 478 Punjab & Haryana H C B.
B. CIT Vs Rana Polycot 347 ITR 466

8. The Ld. AR further submitted that without prejudice even if we ignore the revised return filed by the assessee then also it is an admitted position of facts that the merger of the assessee with M/S Abridge Info-tech was bad in law, which means assessee was separately assessable entity under the Income Tax and M/s Abridge was separate assessable entity. This factual position has also been accepted by the Assessing Officer as well as by the CA of the assessee Company at the time of survey. Therefore, consolidated Balance Sheet of both companies was non-est per se and therefore, the AO was not correct in taxing the income of Abridge in the hands of assessee, merely because assessee has included the same in its hand. The Ld. AR submitted that it is the settled position of law that correct income has to be taxed in correct hands and merely because an assessee has offered an income in his hands that does not mean the same is taxable in his hands. Reliance was made on the following judgments:

a) ***CIT Vs VMRP 56 ITR 67(SC)(larger Bench) t***he Hon'ble Apex Court held that the doctrine of "approbate and reprobate" is only a species of estoppel; it applies only to the conduct of parties. ***As*** in the case of estoppel, it cannot operate against the provision of a statute. If a particular income is not taxable under the IT Act, it cannot be taxed on the basis of estoppel or any other equitable doctrine Equity is out of place in tax law; a particular income is either eligible to tax under the taxing statute or it is not. If it is not, the ITO has no power to impose tax on the said income"

b) Mayank Podar(HUF) Vs Wealth Tax Officer reported in 262 ITR 633(Call), the Hon'ble Calcutta High Court held that there is no estoppel against the statute a property which is not otherwise taxable cannot become taxable because of misunderstanding or wrong understanding of law by the assessee or because of his admission or his misapprehension'

9. The Ld. AR submitted that the AO while making a reference to the TPO has adopted the figure of revised return only. However while computing the income the Assessing Officer has adopted the figures of original return. The Ld. AR submitted that Assessing Officer has referred to TPO the transaction of Rs 2,15,04,878/- which figure matched with order of TPO. The Ld. AR submitted that in revised return assessee has reflected an amount of Rs 2,48,26,091 under the sales receipts, out of this amount an amount of Rs 2,15,04,878/- was related to the AE of assessee and balance amount of Rs 33,21,213/- was related to independent party and that is why the Assessing Officer has only referred the transaction of Rs 2,15,04,878/- to the TPO. The Ld. AR pointed out that belated return of Abridge was filed on 19.03.2008, in which the income pertaining to that firm has been declared. The Ld. AR further submitted that till date no action has been taken by the revenue to assess the income of Abridge and whatever declared over there has been accepted by the revenue as correct. Therefore the entire assessment may be annulled and a direction may be given to AO to reassess the income of the assessee on the basis of revised return.

10. As regards to merit, the Ld. AR submitted that the TPO has wrongly applied the TNMM method instead of CUP method. During the course of TP proceeding as well as in the proceeding before the DRP, the assessee has averted that it had entered into similar transactions with M/s Visiongain Ltd, UK. The Ld. AR further submitted that in this regard assessee had also furnished a comparative chart wherein the assessee has demonstrated the similarity of service provided to AE as well as Independent party. This

comparative chart would prove that the transactions with independent party are similar to the transactions with AE and hence internal CUP is the best method to apply for computing ALP. The above contentions of the assessee were dismissed by the TPO observing that in TP report the assessee admitted that there was some differences in function performed between Calance India and Uncontrolled Comparables. The Ld. AR submitted that this observation is factually incorrect and perverse. No such averment was made in TP report. This allegation of TPO was refuted by the assessee before the DRP, in its submission. It is settled position of law that when internal CUP is available then no other method is preferred. The Ld. AR relied upon the OECD Guidelines and decision of Inter garden (Bangalore).

11. The Ld. AR further submitted that the TPO has also wrongly chosen the comparable namely Bodh Tree Consulting Ltd. and SPI Technologies. The selection criteria of selecting companies with positive net-worth for the year are incorrect. Calance India had a negative net worth excluding the share application money. Negative net worth companies should have been considered. The search parameter should have been made on companies that were in the first, second or third year of operation with revenues between 2-5 Crores. The search parameter of turnover Rs, 1 to Rs 15 crore is totally irrelevant. The search parameter should include independent companies in software development only. Wages/Sales ratio range if 40% - 60% is also not applicable as it stands up for mature companies and not startups. Startups have a higher wages to sales ratio. Therefore, companies which are identified based on these points, should have been further narrowed, based on 80% wages to sales ratio (CALANCE INDIA'S ratio) as that would be a fair comparison. The list should be further short listed based on positive growth companies. Calance India has only 77% of total income as export income (Total revenue Rs 3 22 Crores and Export revenue Rs 2 48 Crores). This list should be further short listed by companies that had an export income of 75% or higher. The Ld. TPO has not elaborated as to why these companies are

comparable with the assessee company. The Ld. AR submitted that these companies cannot at all be compared with the assessee company. The sample set is too small (only 2 companies) to be generically applied to a company like CALANCE INDIA. The relevant sample size had to be hundreds of companies in order to be statistically meaningful.

a) Bodh Tree Consulting was founded in 1999 and has been in business for 7 years and hence probably matured. Comparison of Calance India (18 month old startup company) with Bodhtree is not meaningful Besides Bodh Tree Consulting was in the business of Business Consulting, Business Transformation and Data Management which are not the same as Calance Software business lines. This companies is absolutely meaningless.

b) SIP Technologies was founded in 1996 and again a mature company and should not be compared with Calance India. Also, the line of business pursued by SIP Technologies is very different from Calance India. They are into testing, portability and maintenance and support. None of these business lines were pursued by Calance India in 2005-2006. Calance India was doing Custom Software Development Calance India responded to the show cause notice clearly articulating the reasons for using the CUP method. TNMM was not applicable and therefore the mean margin approach using Bodh Tree and SIP was not appropriate comparison sets and also the data size too small to be statistically meaningful. In a nutshell, TPO has failed to apply FAR test for choosing the correct comparables.

The Ld. AR submitted that all these dissimilarities were pointed out before the DRP. However the DRP has not considered any of the above objections and has just affirmed the order of the TPO in a sketchy manner. Without prejudice to the above even if it is presumed that the TPO has correctly applied TNMM method, then also the calculations made by the TPO are not tenable in law Because it is an admitted position of fact that the agreement was entered on 29/09/2005 and the payments were received from the month of October 2005. Therefore, the TPO ought to have excluded the

expenses of 1st April to 30th September 2005. However, the TPO as well as DRP failed to considered this aspect and has made the adjustment. The Ld. AR submitted that if we exclude the operational cost for the period of 1-04-2005 to 30/09/2005 then profits of the assessee would become 67% of the cost. In more clear terms the assessee wish to demonstrate as under:-

> Total Cost from 1. 10 .2005 to 31 03.2006= 2,06,25,838/
>
> 62 % of the cost can be attributed to AE which is =1,28,56,699/- Now if we apply 23,64% as applied by the TPO then the figure of profits would be 1,58,96,023/- On the other hand assessee has shown an amount of Rs 2,15,04,878 from AE which is 67% of the cost therefore the margin shown by the assessee is much higher than the rate of TPO.

In view of the above the Ld. AR submitted that the order of assessment as well as DRP may be annulled and appeal of the assessee may be allowed.

12. The Ld. DR submitted that the circular / instructions are directive in nature and not mandatory. Therefore, additional ground has to be dismissed. The Ld. DR further submitted that question of limitation should have not been taken into account as the assessee filed revised return during the assessment proceedings which is not permissible. Once the notice received the revised return cannot be filed. The Ld. DR also relied upon the order of the TPO and DRP.

13. We have heard both the parties and perused the material available on record. At the time of hearing the Ld. AR has taken a ground which is on legal point that as per the Instruction No. 3/2003 issued by the CBDT, the Assessing Officer should have decided the issue of international transaction himself instead of referring it to Transfer Pricing Officer as the quantum of International Transaction is below the monetary limit of Rs.5 crore. Prima facie, it appears that the contention of the Ld. AR is supported by the Instruction No.

3/2003. Therefore, we have to verify whether that Instruction has a binding force or it is just an administrative Instruction within the Departments day to day activities. The Circular has been considered by the Andhra Pradesh High Court in case of CIT Vs. Nayana P Dedhia 270 ITR 572 wherein it is held that the authorities responsible for administration of the Act shall observe and follow any such orders, instructions and directions of the board. This is actually reiterated from the decision of the Hon'ble Apex Court in case of UCO Bank Vs. CIT 237 ITR 889. But at the same time the Hon'ble Supreme Court also held that the Circulars can be adverse to the IT Department but still are binding on the authorities of the Income Tax Departments but cannot be binding on the assessee if they are adverse to the assessee. These ratio laid down by the Apex Court has an impact on the argument of the Ld. AR regarding the Board's Instruction to be followed. The Special Bench of this Tribunal also in case of Aztec Software & Technology Services Ltd. vs. ACIT held that CBDT directions are mandatory and binding on the Assessing Officer and CIT. Further the Jurisdictional High Court in case of CIT vs. SPL's Siddhartha Ltd. (supra) held that "*Section 116 of the Act also defines the income-tax authorities as different and distinct authorities. Such different and distinct authorities have to exercise their powers in accordance with law as per the powers given to them in specified circumstances. If powers conferred on a particular authority are arrogated by other authority without mandate of law, it will create chaos in the administration of law and hierarchy of administration will mean nothing. Satisfaction of one authority cannot be substituted by the satisfaction of the other authority. It is trite that when a statue requires, a thing to be done in a certain manner, it shall be done in that manner alone and the court would not expect its being done in some other manner."* Therefore, the additional Ground of the assessee is allowed. At this juncture, the assessment has become time barred as the reference made to TPO itself is not sustainable and the Assessing Officer should have passed Assessment Order at the prescribed time provided under the statute. We are not deciding on the merit of the case as the additional ground is decided in favour of the assesse.

14. In result, appeal of the assessee is allowed.

Order pronounced in the Open Court on 23rd March, 2018.

Sd/- Sd/-

(R. K. PANDA) **(SUCHITRA KAMBLE)**
ACCOUNTANT MEMBER **JUDICIAL MEMBER**

Dated: 23/03/2018
R. Naheed *

Copy forwarded to:

1. Appellant
2. Respondent
3. CIT
4. CIT(Appeals)
5. DR: ITAT

ASSISTANT REGISTRAR

ITAT NEW DELHI

		Date	
1.	Draft dictated on		PS
2.	Draft placed before author		PS
3.	Draft proposed & placed before the second member		JM/AM
4.	Draft discussed/approved by Second Member.		JM/AM
5.	Approved Draft comes to the Sr.PS/PS	23.03.2018	PS/PS
6.	Kept for pronouncement on	23.03.2018	PS
7.	File sent to the Bench Clerk		PS
8.	Date on which file goes to the AR		
9.	Date on which file goes to the Head Clerk.		
10.	Date of dispatch of Order.		