**IN INCOME TAX APPELLATE TRIBUNAL,**
**MUMBAI BENCH "E" MUMBAI.**

**BEFORE SH. A.D. JAIN, JUDICIAL MEMBER**
**AND SH. RAJENDRA, ACCOUNTANT MEMBER**

ITA No.7513/M/2010
Assessment year : 2005-06

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| Deputy Commissioner of Income Tax<br>Centre-1, World Trade Centre,<br>28th Floor, CUFFE Parade,<br>Mumbai.<br>(Appellant) | vs. | M/s. Tata Consultancy Services<br>Ltd. 9th Floor Nirmal Building,<br>Nariman Point,<br>Mumbai.<br>(Rspondent) |

C.O. No.216/M/2010
(Arising out of ITA No.7513/M/2010)
Assessment year : 2005-06

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| M/s. Tata Consultancy Services Ltd.<br>9th Floor Nirmal Building,<br>Nariman Point, Mumbai.<br>(Appellant) | vs. | Dy. Commr. of Income Tax,<br>Cenre-1,<br>Mumbai,<br>(Respondent) |

Department by::Sh. N.K. Chand, CIT(DR)
Assesseeby by: Sh. Dinesh Vyas, Sr. Advocate

Date of hearing : 30/07/2015
Date of pronouncement: 04/11/2015

**ORDER**

**PER A.D. JAIN, JM**

This is Department's appeal for the assessment year 2005-06, taking the following grounds:

"1. On the facts and in the circumstances of the case and in law, the ld. CIT(A) erred in allowing overseas taxes paid of Rs.216,27,28,177/-.

2. On the facts and in the circumstances of the case and in law, the ld. CIT(A) erred in allowing penal interest paid in USA towards late payment of taxes paid of Rs.4,61,683/-.

3. On the facts and in the circumstances of the case and in law, the ld. CIT(A) erred in allowing software expenses u/s 40a(i) on account of non-deduction of TDS amounting Rs.25,11,88,831/-.

4. On the facts and in the circumstances of the case and in law, the ld. CIT(A) erred in allowing claim u/s 10A on units on which deduction u/s 80HHE was passed and method of computation of deduction u/s 10A of the I.T. Act.

5. On the facts and in the circumstances of the case and in law, the ld. CIT(A) erred in deleting the additions on account of Transfer Pricing adjustment in relation to transaction with Associated Enterprises M/s. Tata America International Corporation Inc. (TAIC)."

2. Apropos Ground No.1, it states that the ld. CIT(A) has erred in allowing overseas taxes paid of Rs.216,27,28,177/-. As per the record, the assessee has paid the following Federal taxes in the USA, Canada and other Overseas branches and State taxes in the USA and Canada, which were claimed as deduction in the return of income:

Federal tax of Rs.19,99,80,754/-

State taxes of Rs.16,28,38,423/-

Total Overseas tax Rs.216,27,28,177/-.

The AO disallowed deduction for Rs.2162728177/- holding that such taxes are covered by the provisions of section 40(a)(ii) of the Income tax Act, 1961.

3. The Ld. CIT(A) confirmed the disallowance of Federal tax of Rs.199.99 crores. However, deduction of State Taxes of Rs.16.28 crores was allowed. It was held that since the amended provisions of section 40(a)(ii), by way of insertion of Explanation-1, is clarificatory in nature, the AO was correct in holding that the amended provisions of the section are retrospective in effect. It was also held that the Federal tax was eligible for relief u/s 90 of the I.T. Act. It was held that however, State taxes paid in the USA and Canada are ineligible for relief u/s 90 of the I.T. Act, read with the provisions of Article 1(3) of the Indo- Canada Treaty and Article 2(a) of the Indo-USA Treaty and that accordingly, the provisions of section 40(a)(ii) of the Act do not apply to the State Taxes.

4. At the outset, the ld. counsel for the assessee has contended that on this issue, the decision of the Mumbai Bench of the Tribunal in the case of "Tata Sons Limited.", reported as 9 ITR 154 (Mumbai) is against the assessee and an appeal against the same is pending before the Hon'ble High Court, having been admitted.

5. On the other hand, the ld. DR has placed strong reliance on the impugned order.

6. Since admittedly, the Tribunal has decided this issue against the assessee in the case of "Tata Sons Ltd." (supra), and the said decision has not been stated to have been stayed on appeal, respectfully following the same, this issue is decided against the assessee. Ground No.1 stands dismissed.

7. As per Ground No. 2, the ld. CIT(A) erred in allowing penal interest paid in the USA towards late payment of taxes paid of Rs.4,61,683/-.

8. This issue is relatable to Ground No.1 (supra). In view of our observations made with regard to that ground, Ground No.2 also stands rejected.

9. According to Ground No.3, the ld. CIT(A) has erred in allowing software expenses under section 40(a)(i) of the Act on account of non-deduction of TDS amounting to Rs.25,11,88,831/-. The assessee imported certain software products for its business. The software products imported were both for use in its own business as well as for the purpose of trading. Such expenditure was claimed as a deduction in the return of income, as follows:

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| Software for internal use | : | Rs.19,52,33,849/- |
| Software for trading purpose | : | Rs.5,59,54,982/- |
| Total: | : | Rs.25,11,88,831/- |

The AO disallowed the expenditure claimed, applying the provisions of section 40(a)(i) of the Act on the ground that the tax was required to be deducted at source u/s 195 of the Act.

10. The ld. CIT(A) allowed the claim, observing that he agreed with the contention of the assessee that payment towards purchase of software is payment for copy righted articles and hence, it only represented the purchase price of an article and could not be considered as royalty, either under the Act, or under the DATA; that it is purely in the nature of business income and in the absence of a permanent establishment in India of the non-resident payees, the amount so remitted to the non-resident is not chargeable to tax. The ld. CIT(A) relied on the decision in the case of "ACZ India (P) Ltd.", 2010-TIOL-187- Del-IT and that in the case of "Parsad Production Limited", rendered by the Chennai Special Bench of the Tribunal in ITA No.663/Mad/2003. The ld. CIT(A) agreed with the view that withholding tax obligation on the payer applies on payments to non-residents onlys if there is income chargeable to tax in India. It was held that accordingly, there was no obligation of the assessee to deduct tax at source u/s 195 of the Act, from making remittances to non-residents. The ld.

CIT(A) held that he agreed with the assessee's contention that no tax was deductible on the same and accordingly, no disallowance ccould be made u/s 40(a)(i) of the Act.

11. Here, invoking the provisions of Rule 27 of the ITAT Rules, 1963 seeking to support the ld. CIT(A)'s order thereby, the ld. counsel for the assessee has pleaded that other than the issue at hand, the assessee had incurred expenses of Rs.38,59,97,989/- on account of software acquired within India for facilitating the assessee's business operations; that the AO disallowed such expenditure, treated it as a capital expenditure and allowed the depreciation thereon. It has been stated that the ld. CIT(A) has upheld this order of the AO. It has been contended that the assessee wants to finish off the litigation and so, here also, depreciation allowed. It has been contended that it is only a timing issue and the assessee will get it over a period of five years.

12. On the other hand, the ld. DR has contended that depreciation can be allowed only if it is a capital expenditure and that in the present case, it is not so.

13. Considering the rival contentions, we find that the argument of the assessee is correct. The locally acquired software expenses have been treated as capital expenditure, placing reliance on various judicial decisions, which

hold that the expenses on software are in the nature of capital expenditure and depreciation is to be allowed on the same. As such, expenses on imported software are also in the nature of capital expenditure and deprecation needs to be allowed thereon. The AO, therefore, is directed to allow depreciation on the imported software purchased by the assessee. This alternative plea raised by the assessee is, hence, accepted.

14. Ground No.4 challenges the action of the ld. CIT(A) in allowing the claim u/s 10A of the Act on units on which deduction u/s 80HHE was allowed in the past and the method of computation of deduction u/s 10A of the Act. This ground comprises of two limbs. The first issue is as to whether deduction can be claimed u/s 10A of the Act in respect of units on which deduction u/s 80HHE was allowed in the past. The AO did not allow deduction u/s 10A of the Act on the ground that section 80HHC(5) of the Act prohibits the claim under any other section of the Act, once deduction was claimed under this section. The ld. CIT(A) allowed the claim following the first appellate orders passed in the assessee's case in earlier years.

15. The challenge of the ld. DR to the ld. CIT(A)'s action reiterates the findings recorded by the AO. It has been contended that at the time of commencement/inception of the undertaking, deduction u/s 10A of the Act was not available for export of computer software. Section 10A was

substituted w.e.f. 1.4.2001, whereby, for the first time, the profit from the export of computer software was included in section 10A of the Act in respect of the newly established undertakings; that prior to that, even though section 10A was in the statute, the deduction was available only on profits and gains derived by an assessee from an industrial undertaking but was not available to the undertaking engaged in computer software; and that hence, deduction u/s 10A is not allowable to the undertakings which were already in existence and claiming deduction u/s 80HHE of the Act. It has been contended that the assessee-company, upto 1998-99, opted out of the deduction u/s 80-O and section 80HHE, which was more beneficial to the assessee for its units in AY 1999-2000. In AY 1999-2000 & in AY 2000-01, the assessee claimed deduction u/s 80HHE. Section 10A was substituted w.e.f. 1.4.2001, in which, the deduction was allowed for the 10 years beginning with the assessment year in which the undertaking began to produce the computer software. It has been contended that the section nowhere provides that the deduction will be available to the existing undertaking. The second proviso to section 10A can only be referred to in respect of the industrial undertakings, which were already covered u/s 10A prior to its substitution w.e.f. 1.4.2001. It has been submitted that deduction upto assessment year 2000-01 was available for the existing industrial

undertakings. The deduction for the software export was not available in the provision as it existed upto AY 2000-01. Thus, the ld. CIT(A) has erred in upsetting the AO's order. It has been contended that deduction u/s 10A was not available to the units engaged in the export of computer software upto assessment year 2000-01 and hence, no question of allowing the deduction u/s 10A on such units arises. It has been contended that once the deduction is not available u/s 10A to the units qua which the deduction is claimed, the question of unintended benefit does not arise. However, the assessee, by claiming deduction u/s 10A wants to avail benefits, which are not available from AY 2001-02 u/s 80HHE of the Act, in view of the phasing out of the deduction u/s 80HHE of the Act from AY 2001-02. The assessee wants to claim one hundred percent deduction in the nature of profits u/s 10A, whereas there is no deduction available u/s 80HHE during the said year. It has been contended that moreover, section 80HHC(5) of the Act prohibits the claim under any other section of the Act, once deduction was claimed under section 80 HHE.

16. It has been contended that "profit" referred to in section 80HHE(1) means the profits derived by the assessee from the business of (a) export out of India of computer software, or its transmission from India to a place outside India by any means and (b) providing technical services outside

India in connection with the development or production of computer software. The assessee company has also derived its profit from the business referred to in section 80HHE(1) and deduction under section 80HHE is claimed and allowed in the earlier year and so, no deduction under any provision of this section for the same, or any other assessment year can be allowed. This clearly indicates that if in any year deduction has been claimed, the assessee cannot claim deduction of such profits for the same year, or any other assessment year. "Such profits" does not mean profit of that year alone, but the profit of such nature earned in any assessment year. If the legislative intention was otherwise, there was no need to employ the phrase "for the same or any other assessment year". This clearly indicates that the assessee cannot opt for deduction under any provision of the Act in the subsequent years. Then, section 10BA, inserted w.e.f. 1.2.2004, allows the deduction from the profits and gains derived from an undertaking from the export of eligible articles or things, i.e., hand made articles or things having artistic value, which requires the use of wood as the main raw-material. The undertaking exporting such articles is also covered u/ss 10A & 10B of the Act and, therefore, a restriction has been put in section 10BA, that if deduction has been claimed by an undertaking u/s(s) 10A or section 10B, the undertaking will not be eligible for deduction u/s 10BA. The profits

derived from the undertaking covered u/s(s) 10A, 10B and 10BA are the income which do not form part of the total incomes, whereas the deduction u/s(s) 10A and 80HHE is allowed out of gross total income. Therefore, the assessee does not get any support form the proviso to section 10BA of the Act. It has been contended that since the date of the insertion of section 10A in the Act, the assessee was prohibited from claiming deduction u/s 10A, if it wanted to claim deduction under any other provision of the Act, as is evident from section 10A(7), as it existed upto 2000-2001.

17. On the other hand, placing reliance on the impugned order, on behalf of the assessee, it has been contended that the deduction u/s 10A of the Act, is available for the balance number of years in respect of units where deduction u/s 80HHE of the Act has been claimed in the past. Reliance has been placed on the following case laws:

i) "Legato Systems India (P) Ltd.;" 93 TTJ 828 (Delhi), affirmed by the Hon'ble Delhi High Court in 203 CTR 101.

ii) "CIT vs. Excel Softec Limited", 219 CTR 405

iii) "EDS Electronic Data Systems India Pvt. Ltd.", 211 Taxman 133 (Del.)

iv) "Dempo Solutions Pvt. Ltd.", 200 Taxman 26 (Del.)

v) "Excell software Tech. Limited", 219 CTR 405 (P&H)

vi) "Interra Software India P. Ltd." 112 TTJ 982 (Del.)

vii) "Vidya Tech Solutions Pvt. Ltd.", 8 ITR (AT) 705 ( ITAT Delhi)

It has been contended that there is no attempt to extend the period of the tax holiday, as the claim was made for the residual year remaining in the block of 10 years. Reliance in this regard has been placed on "Excel Software Pvt. Ltd." (supra).

18. Here, we find that in "Legato Systems India (P) Limited" (supra), the Delhi Bench of the Tribunal held that "upon a harmonious reading of the entire provision, i.e., section 80HHE, the expression "such profit" as appearing in clause (v) is found to refer to the profits of a particular assessment year and the section does not place any restriction to shift the claim of deduction or exemption under any other provision in respect of profits for which no deduction has been claimed and allowed in the previous year. Since both the sections, i.e., section 80HHE and section 10A entitle the benefit, the assessee would legitimately be entitled to the benefit of that provision of law, which enables a larger benefit being earned by him. This finds support from the decision of the Hon'ble Supreme Court in "Collector Central Excise vs. Indian Petro Chemicals", (1997) 11 SSC 318 and also from the decision of the Hon'ble Delhi High Court, in the case of "C.S.Mathur vs. CBDT" (supra). We, therefore, do not find any justification in the action of the ld. CIT(A) to hold that the assessee being an old unit and

having once claimed deduction u/s 80HHE, was not entitled to claim deduction u/s 10A from the profits of its units.

19. The Hon'ble Delhi High Court has upheld the aforesaid decision of the Tribunal in the case of "CIT vs. Legato Systems India (P) Ltd.", 203 CTR 101 (Del). A similar view has been taken by the Tribunal in the case of "ITO vs. Dempo Solutions Pvt. Ltd.", 200 Taxman 26 (Del), as also in the case of "DCIT vs. Interra Software India P. Ltd.", 112 TTJ 982 and in the case of "Vidya Tech Solutions Pvt. Ltd." 8 ITR (AT) 705 ( ITAT Delhi). Further, in keeping with "Excell software Tech. Limited" (supra), there is no attempt by the assessee to extend the period of the tax holiday by exercising option to claim deduction u/s 10A instead of u/s 80HHE of the Act. The claim of deduction u/s 10A was supported by the requisite audit certificate. In the said certificate also, the date of commencement of manufacture/production has been taken as the original date and not as the date of commencement of claim u/s 10A of the Act.

20. In view of the above discussion, finding no error therein, this part of the order of the ld. CIT(A) is upheld.

21. Apropos the second limb of Ground No.4, i.e., the department's challenge to the method of computation of deduction u/s 10A of the Act, the ld. CIT(A) followed the Special Bench decision of the Tribunal in the case

of "Sak Soft Limited", reported at 30 SOT 55 (Chennai) (SB), wherein, it was held that for the purpose of applying the formula u/s 10B(4), which is pari materia to section 10A(4), the freight, telecom charges or insurance attributable to the delivery of articles or things or computer software outside India, or the expenses if any, incurred in foreign exchange in providing technical services outside India, are to be excluded from export turnover and from total turnover, which are the numerator and the denominator, respectively, in the formula. The ld. CIT(A) directed the AO to compute the deduction after reducing the expenditure already reduced from the export turnover, from the total turnover as well.

22. Challenging the impugned order, the ld. DR has placed strong reliance on the assessment order. It has been contended that section 10A of the Act has defined the term 'export turnover' and not the term 'total turnover'. It has been submitted that the ITAT, Hyderabad Bench, in the case of "Patni Telecom. Pvt. Ltd. vs. ITO", 22 SOT 26 (Hybd), examined the provisions of section 10A of the Act and it considered the reasoning why such expenditure is being excluded from the computation of benefit u/s 10A; that it has also considered CBDT Circular No.564 dated 05.07.1990, which clarified this aspect in respect of deduction u/s 80HHC, where a deduction of total turnover is provided and exclusion of such expenditure was specifically

provided in that definition; that it is this definition which has been logically brought into the provisions of deduction under section 10A; that there is no specific definition or provision provided in the said section to exclude such expenditure; and that the import of such definition is not correct as per the settled position of law. It has been contended that the various judicial decisions have held that deduction u/s 80HHC of the Act is governed by the provisions of the said section, which is a code in itself; that on a similar analogy, the deduction u/s 10A is to be taken as governed by the provisions of the said section and that the said section, i.e., section 10A, is also a code in itself; that the legislature, in its wisdom, has introduced the section in Chapter III, i.e., Incomes which do not form part of total income and not under Chapter VIA of the Act; that the CBDT, in circular No.694, dated 23.11.1994, clarified the intention of bringing in sections 10A & section 10B in the Act, that the attempt to introduce these sections requires a simple interpretation and the reason as to why the legislature has not given a definition of "total turnover", as given in section 80HHC, in the provisions of section 10A; that it is the discretion of the legislature to frame such a section, by which, a particular category will get a deduction on fulfilling certain conditions; that, however, at the same time, it gives discretion as to how much of that deduction should be given and as to how the deduction is

to be computed; and that therefore, section 10A requires to be read in a holistic manner. It has been contended that the meaning of a word or a phrase has to be adopted by considering the context in which it has been used; that the meaning given to a particular expression in one enactment cannot be bodily fitted into another altogether different enactment. It has been contended that as such, the ld. CIT(A) erred in directing the method of computation of deduction u/s 10A to be adopted by the AO, as has been done.

23. Per contra, supporting the impugned order, the ld. counsel for the assessee has contended that the term "total turnover' is an enlargement of the term of 'export turnover'. The expenditures which are required to be reduced from the export turnover as per the provisions of section 10A of the Act should also be reduced from the total turnover. Reliance has been placed on the decision of the Hon'ble Bombay High Court in the assessee's own case, i.e., "Tata Infotech Limited.", in ITA No.3474 of 2010. Reliance has also been placed on the order in the assessee's own case in ITA Nos. 1311/M/2012 and 2125/M/12, rendered by the Mumbai Tribunal. Further, reliance has been placed on the following case laws:

i) "Tata Elxis Limited", 349 ITR 98 (Kar.)

ii) "ITO vs. Sak Soft Limited", 30 SOT 55 (Chennai)(SB)

iii) "CIT vs. Gem Plus Jewellery India Ltd.", 330 ITR 175 (Bom.)

iv) "CIT vs. Lakshmi Machine Works", 290 ITR 667 (SC)

v) "CIT vs. Catapharma I(India) P. Ltd.", 292 ITR 641 (SC)

vi) "CIT vs. Sudershan Chemical Industries Ltd.", 245 ITR 769 (Bom.)

vii)

24. Here, we find that the decision of the Special Bench in "Sak Soft Limited" (supra), holds the field. It has not been upset on appeal. No decision to the contrary has also been placed on record before us. Therefore, the action of the ld. CIT(A) in following "Sak Soft Limited" (supra), alsocannot be found fault with. The same is confirmed. As such, Ground No.4 is rejected.

25. As per Ground No.5, the ld. CIT(A) has erred in deleting the additions on account of TP adjustments in relation to transaction with AE, M/s. Tata America International Corporation Inc. ( TAIC).

26. Apropos Ground No.5, invoking the provisions of Rule 27 of I.T.A.T Rules, the assessee has sought to support the order of the ld. CIT(A) by raising a plea that under section 92C or 92CA of the Act, it is the statutory duty of the AO to decide independently, whether the determination of arm's length price by the assessee should be accepted, or whether or not after applying the provisions of section 92CA, the transfer pricing adjustment should be made. This is a statutory safeguard for the assessee. It has been

contended that similarly, it is only after proper application of mind to all the facts and holding a prima facie belief that the AO can make reference to the TPO, or that the ld. CIT(A) can grant approval to such a reference. This, again, is a statutory safeguard for the taxpayer. It is submitted that CBDT Instruction No. 3 of 2003, dated 20.05.2003 detracts the AO and the ld. CIT(A) from the above obligation in complete violation of the statutory provisions of the principles of natural justice. It has been submitted that in the present case, in compliance of the said CBDT Instruction No.3 of 2003, the AO did not himself examine the issue of transfer pricing and with the approval of the ld. CIT(A), made a reference to the TPO u/s 92CA(1) of the Act. The AO and the ld. CIT(A) did not apply their minds to the Transfer Pricing Report, or to any other material or information or document. The TPO made an adjustment which was incorporated by the AO in the assessment order. On their part, the AO and the ld. CIT(A) did not discharge necessary judicial functions conferred upon them u/s 92C or 92CA of the Act.

27. On the other hand, duly supporting the action of the AO and that of the ld. CIT(A) in this regard, the ld. DR has sought to place reliance on the following case laws:

i) "Coca Cola India Inc vs. ACIT", 309 ITR 194 (P&H)

ii) "Sony India P. Ltd. vs. Central Board of Direct Taxes and Another", 288 ITR 52 (Delhi) and

iii) "Aztec Software and Technology Services Ltd. vs. ACIT", 294 ITR (AT) 32 (Bangalore) [SB]

28. With regard to "Sony India Pvt. Ltd." (Ssupra), the Ld. DR has contended that as per this decision, the AO is not required to form a prior considered opinion before making a reference to the TPO under section 92CA(1) of the Act and that only a prima facie opinion is necessary. It is contended that the AO is not required to follow the steps enlisted in section 92CA(1) of the Act, before making reference to the TPO. Instruction No.3/2003 is not violative of article 14 of the constitution of India. The instruction is not ultravires the Income-tax Act. The classification of International transactions is not inconsistent with, or contrary to, the objectives sought to be achieved by Chapter X of the Act. The Instruction supplements the statutory provision to achieve its objective and does not override it. It is neither arbitrary, nor unreasonable. It was held to be constitutionally valid.

29. So far as regards "Aztec tax software & technology Services Ltd." (supra), it has been contended that the Special Bench of the Tribunal, in the said case, has held that in view of the plain and ambiguous language of the Act, tax avoidance is not required to be proved before invoking the

provisions of Chapter X of the Act. The TP provisions are applicable even if income is exempt u/s 10A & 10B of the Act. No prior hearing is to be given to the assessee by the AO, or the ld. CIT(A) before making reference to the TPO. The conditions in section 92CA(3) of the Act are not required to be fulfilled before making reference to the TPO. CBDT Instruction No.3/2003 is binding on the AO and hence, it becomes necessary or expedient for him to refer the case to the TPO u/s 92CA(1) of the Act, if the international transaction or transactions exceeds, or exceed the limit mentioned therein. The initial burden is on the assessee to select the most appropriate method. It is also the assessee's onus to show that the price was at arm's length. In case the TPO redetermines the ALP, the burden shifts on him. Reference can be made to the OECD Guidelines, US Regulations, etc., subject to the domestic statutory regulations. Industry average (Nasscom) cannot be taken as up. The TNMM requires comparability at a broad functional level. The Special Bench of the Tribunal upheld the use of current year data. With reference to "Coca Cola Pvt. Ltd." (supra), it has been contended that as per this decision, there is no need for hearing to be given to the assessee before making reference to the TPO. Once an International transaction is there, in view of the plain and unambiguous language, ALP has to be determined. There is no requirement of showing shifting of profit, evasion of tax, etc.,

before invoking the provisions of Chapter X of the Act. The mere fact that the assessee has chosen one method does not take away the discretion of the TPO to select any other method. Restriction of payment or remission imposed by the RBI or FERA cannot control the provisions of Chapter X of the Act; ALP has to be determined in such cases also.

30 In this regard, it is seen that in "Sony India Pvt. Limited" (supra), their Lordships of the Hon'ble Delhi High Court were considering CBDT Instruction No.3 dated 20.05.2003, which provides that a compulsory reference has to be made to the TPO to determine arm's length price, where the aggregate value of the international transactions exceeds Rs. 5 crores. The assessee-company in that case challenged the constitutional validity of the said Circular mainly on the ground that by issuance of the Circular, the AO's ultimate decision on computation of ALP is sought to be supplanted by the decision of the TPO for transactions of value over Rs. 5 crores and the TPO is not bound to follow the steps outlined u/s 92C of the Act, which are otherwise mandatory for the AO to follow. The question arose whether there is nothing in section 92CA itself that requires the AO to first form a considered opinion in a manner indicated in section 92CA(3) of the Act before he can make a reference to the TPO. It was held that this is indeed so. Apropos the question whether it is not possible to read such a

requirement u/s 92CA(1) of the Act, this was also held in the affirmative. Their Lordships held that it would suffice if the AO forms a prima facie opinion that it is necessary and expedient to make such a reference. It was also held that one possible reason for absence of such requirement of formation of a prior considered opinion by the AO is that the TPO is expected to perform the same exercise, as envisaged u/s(s) 92C(1) to 92C(3) of the Act, while determining the ALP u/s 92CA(3). It was further held that the AO is not bound to accept the ALP as determined by the TPO and always persuaded by the assessee at that stage to reject the TPO's report and still proceeds to determine the ALP himself and, therefore, the AO is the authority to finalise the assessment and the said power of the AO cannot be usurped. It was also held that therefore, it cannot be said that the AO's decision is supplanted by the decision of the TPO. Still further, it was held that that the Instruction in question, i.e., CBDT Instruction No.3, dated 20.05.2013, is consistent with the statutory objective underlying section 92CA(1) of the Act and acts as guidance to the AO in the exercise of discretion in referring an international transaction to the TPO for determination of its ALP and it is neither arbitrary, nor unreasonable and is not ultravires the act.

31. It has rightly been contended on behalf of the assessee with regard to "Sony India Pvt. Limited" (supra) that the Hon'ble Bombay High Court, in the case of "Vodafone India Services P. Ltd. vs. Union of India", 361 ITR 531 (Bom.), has held that CBDT Instruction No.3 dated 20.05.2003 is contrary to the decision being taken therein and it is not binding on the AO. It was held that this Instruction departs from the provisions of law. It was held that the decision in "Sony India Limited" (supra), is not applicable after the amendment of 2007 (paras 35 to 37 of the judgment are relevant in this regard).

32. In "Aztec Software & Technology Services Ltd." (supra), the Bangalaore Special Bench) of the Tribunal held that it is not a legal requirement under the provisions contained in Chapter X of the Act, that the AO should prima facie demonstrate that there is tax avoidance, before invoking the relevant provisions. It was held that before the case is referred to the TPO u/s 92CA(1) of the Act for computation of arm's length price, the AO is not required to prima facie demonstrate that any one or more of the circumstances set out in sections 92CA(3)(a),(b),(c) and /or (d) of the Act, are not satisfied. It was held that the AO is not required to record his opinion/reason before seeking the previous approval of the ld. CIT u/s 92CA(1) of the Act. It was held that before making a reference to the TPO

u/s 92CA(1) r.w.s. 92C(3) thereof, it is not a condition precedent that the AO shall provide the assessee an opportunity of being heard. It was held that CBDT Instruction No.3 of 2003, dated 20.05.2003, on transfer pricing matters, is not legal and the same is not binding on the Departmental Authorities. It was also held that prior to the amendment brought in w.e.f. 01.06.2007, though the order of the TPO issued u/s 92CA(3) of the Act, is not binding on the AO, the AO may take the ALP determined by the TPO without making any change under section 92CA(3) of the Act, for making assessment. The issue of determination of quantum of ALP was remanded.

33. In "Vodafone India Services P. Ltd." (supra), the Hon'ble jurisdictional High Court has held the decision of the Special Bench of the Tribunal in "Aztec Software Technology & Services" (supra) to be not applicable in view of the amendment brought in in 2007. It was held that it laid down that there was no requirement to establish tax avoidance before initiation of proceedings. Tax avoidance, in other words, is required to be established thereafter and before the completion of the assessment. It was held that the Instruction detracts from the provisions of law.

34. "Coca Cola India Pvt. Ltd." (supra), rendered by the Hon'ble Punjab & Haryana High Court, was appealed against before the Hon'ble Supreme Court. The Hon'ble Supreme Court, in its judgment, reported in "Coca Cola

India Inc.vs. Addl. CIT", 336 ITR 1 (SC), directed that the authorities below should decide the matter afresh, uninfluenced by any of the observations made in the High Court judgment.

35. The position obtaining with regard to these three judgments sought to be relied on by the Department is, that none of these judgments is applicable. "Sony India Limited" has been held to be not applicable by "Vodafone India" (Supra), rendered by the jurisdictional High Court. "Aztec Software & Technology Services" (supra), has also no application in view of "Vodafone India Services P. Ltd." (supra). "Coca Cola India Inc." (supra) is also inapplicable, the Hon'ble Supreme Court having directed the authorities to decide the matter afresh uninfluenced by the observations made by the Hon'ble High Court. Further, in "Sony Ericsson Mobile Communications Pvt. Limited", 374 ITR 116 (Delhi), the same is the position maintained. This apart, the question raised before us was nowhere argued or adjudicated in any of these judgments. The assessee has contended that the AO has abrogated his obligation under a wrong assumption that CBDT Circular, i.e., CBDT Instruction No.3 of 2003 dated 20.05.2003 mandated him to go ahead without making any reference to the TPO. The AO, thus, in the present case, did not examine the question, whether he should himself accept the transfer pricing report of the assessee or whether he should himself

determine the arms's length price. Therefore also, these judgments are not applicable and they do not help the cause of the Department.

36. The Department has further sought to place reliance on "Interra Information Technology (I) Pvt. Limited vs. DCIT", (2012) 27 Taxman.com.1(Del) (Trib.). In that case, considering assessment years 2006-07 & 2007-08, it was held that it cannot be laid down as a proposition that transfer pricing adjustment cannot exceed total profits earned by the group. It was held that the assessee as well as the Revenue Authorities are bound to determine the ALP by applying the law and rules laid down and cannot be guided by extraneous parameters. It was held that any claim for adjustment on the basis of reason or any other factors has to be based on proper data and sound calculation and ad-hoc adjustment should not be granted. It was held that where material is available with the TPO in the current year, which is vastly different from the material available with the TPO in the earlier year, the principle of consistency does not hold water. It was held that the assessee is required to support its claim for any adjustment with robust data and full details and evidence and the burden of proof is on the assessee, whenever it makes such a claim. However, this decision, we are afraid, also does not further the cause of the department, as it does not address the issue raised by the assessee before us in the present case, as discussed.

37. In this regard, the Hon'ble Supreme Court, in the case of "Good year India Ltd. vs. State of Haryana", 188 ITR 402 (SC), has held that a decision on a question which has not been argued cannot be treated as a precedent. Further, when a statute vests certain powers in an authority to be exercised in a certain manner that authority has to exercise those powers only in a manner provided in the statute itself. It has been so held by the Hon'ble Supreme Court in "CIT vs. Anjum Ghaswala", 252 ITR 1 (SC). The Hon'ble Jurisdictional High Court has also taken a similar view in the case of "Ghanshyam K. Kharbani", 346 ITR 443 (Bombay).

38. The Department has, then, also sought to place reliance on "Ranabaxy Laboratories vs. Addl. CIT", 110 ITD 428 (Del.). In that case, it was held, with regard to assessment year 2004-05, that it is not right to contend that in not referring the question of determination of arm's length price to the TPO, as required by CBDT Instruction No.3 of 2003 (supra), the AO merely committed a procedural error. "Vodafone India Services P. Ltd.", (supra) was rendered by the Hon'ble jurisdiction High Court post the decision of the Tribunal in "Ranabaxy Laboratories" (supra) and therefore, the Tribunal, clearly did not have the benefit of "Vodafone India", (supra). To reiterate, in "Vodafone India", (supra). CBDT Instruction No.3/2003 has been held to detract from the provisions of law. In "Vodafone India" (supra), it has been

held that necessary hearing is required to be given to the assessee in accordance with the principles of natural justice before a reference is made to the AO after the amendment in the year 2007.

39. In the case of "Johari Lal vs. CIT", 88 ITR 439 (SC), it has been held that the prima facie belief of the AO that it is necessary or expedient to make a reference to the TPO is the condition precedent to be satisfied upon application of mind to the material or information or document in his possession. Such prima facie belief is a condition precedent and is mandatory and it is the statutory safeguard for the assessee's statutory right. The absence of such a belief vitiates the entire proceedings.

40. Like-wise, the approval of the ld. CIT for the reference to the TPO on a proper application of mind to the relevant facts and circumstances is a condition precedent and a necessary safeguard for the statutory right of the assessee and this has to be performed not in a mechanical manner. This is what has been held by the Hon'ble Supreme Court in the case of "Krishna Pvt. Ltd. vs. ITO", 221 ITR 538 (SC) and by the Hon'ble jurisdictional Bombay High Court in the case of "German Remedies", 287 ITR 494 (Bom.).

41. In "CIT vs. Amedius", 351 ITR 82 (Del.), it has been held that it is primarily the duty of the AO to compute the arm's length price in relation to

an international transactoion in accordance with the most appropriate method specified in section 92C(1) of the Act; and that however, where the AO requires the arm's length price to be computed by specialist, a reference may be made to the TPO.

42. In CBDT Circular No.14 of 2001, in para 55.11 thereof, it has been provided that "under the new provisions the primary onus is on the taxpayer to determine an arm's length price in accordance with the rules and to substantiate the same with the prescribed documentation. Where such onus is discharged by the assessee and the data used for determining the arm's length price is reliable and correct, there cannot be any intervention by the AO. This is made clear by sub section (3) of section 92C, which provides that the AO may intervene only if he is, on the basis of material or information or document in his possession, of the opinion that the price charged in the international transaction has not been determined in accordance with sub-sections (1) & (2), or information and documents relating to the international transaction have not been kept and maintained by the assessee in accordance with the provisions contained in sub-section (1) of section 92D and the rules made thereunder; or the information or data used in computation of the arm's length price is not reliable or correct; or the assessee has failed to furnish, within the specified time, any information

or document which he was required to furnish by a notice issued under sub-section (3) of section 92D. If any one of such circumstances exists, the AO may reject the price adopted by the assessee and determine the arm's length price in accordance with the same rules. However, an opportunity has to be given to the assessee before determining such price. Thereafter, as provided in sub section (4) of sec. 92C, the AO may compute the total income on the basis of the arm's length price so determined by him."

43. In the case of "Sirpur Paper Mills", 237 ITR 41 (SC), it has been held that section 119 of the Act permits the CBDT to specify conditions, but conditions cannot have the effect of curtailing the scope of the deduction granted by the section; that the amplitude of the deduction permitted by the section cannot be cut down under the guise of imposing a condition; that in fact, this is not a condition, but an impermissible attempt to re-write the section. It was held that the CBDT may control the exercise of the powers of the Officers of the Department in matters administrative, but not quasi-judicial.

44. In the following decisions, amongst others, it has been held that the Tribunal can ignore alone invalid Circulars of the CBDT:

(i) "Tata & Iron Steel", 69 ITD 292 (Mumbai)

(ii) "Mahindra & Mahindra", 8 ITD 427 (Mumbai) and

(iii) "Pardeep Agencies vs. ITO", 18 SOT 12 (Delhi) (SB)

45. The assessee has further sought to support the ld. CIT(A)'s order on the contention that Transfer Pricing adjustment cannot be made in a case where the assessee enjoys benefit u/s 10A or section 80HHE of the Act, or where the tax rate in the country of the Associated Enterprise is higher than the Indian rate and where, accordingly, establishment of tax avoidance or manipulation of prices or establishment of shifting of profits is not possible.

46. "Aztec Software & Technology Services" (supra), holds that TP provisions are applicable even if income is exempt u/s(s) 10A/10B of the Act. However, as seen, "Aztec Software & Technology Services", stands overridden by the decision of the Hon'ble jurisdictional High Court in "Vodafone India" (supra).

47. In "Motif India Infotech Pvt. Limited", the decision in ITA No. 3043/Ahd/2010, rendered on 25.03.2013, it has been held that in a case where the income derived from an international transaction is exempt from tax in India because of the provisions of section 10A of the Act, it cannot be held that because of an arrangement between the assessee and the Associated Enterprise, any income taxable in India had been under reported.

48. It has been held that in such circumstances, where the income derived from an international transaction is exempt from tax in India, it cannot be

alleged that the assessee had arranged its affairs in such a manner, so as to show lesser taxable income in India.

49. In "Cotton Naturals (I) Pvt. Ltd. vs. DCIT", 22 ITR (AT) 430 (Del) (Trib.), it was held that the assessee's substantial profits were exempt u/s 10B of the Act and the Associated Enterprises were not situated in tax havens, but in the US, where the tax rates were at par with India, or may be more than that; that the assessee's profits were exempt u/s 10B; and that hence, there was no case that the assessee would benefit by shifting profits outside India.

50. In the case of "Indo-American Jewellery", 41 SOT 1 (Mum), the Mumbai Bench of the Tribunal found merit in the submissions on behalf of the assessee that since the tax rates were higher in the USA compared with those of India, there would not be any incentive to transfer the profits to a higher tax chargeable region, especially when the company enjoyed deduction u/s 80HHE of the Act.

51. In " DCIT vs. Lumax Industries Ltd.", 36 Taxman.com.380, it was observed that the TPO had nowhere made out a case that the profit was shifted from a higher tax jurisdiction to a lower tax jurisdiction; that in fact, there was no motive for any such shifting of profits at the hands of the assessee-company and there could have been any reason for the majority

stake holder in India, i,.e., the assessee, to over pay even a single paise to the minority stake holder in Japan; that the TPO fell in error in ignoring the position that it was if and only if it stood proved that there was manipulation of prices to avoid taxes in India, that the TP provisions of the Act could be invoked; that the TP regulations in India have been brought on the statute book with the intent of preserving the tax base in India and preventing tax evasion through manipulation of pricing of inter-company transactions; that further, application of tax jurisprudence provisions could have been justified, if the rate of tax was lower in Japan as compared to that in India, which was not so; and that it was, therefore, beyond comprehension as to why the assessee would harbour any motive of shifting income.

52. In the case of "Philip Software", 119 TTJ 721 (Bang.), it was held that since the basic intention behind introducing the TP provisions in the Act is to prevent shifting of profits outside India, and the assessee was claiming benefit u/s 10A of the Act, the TP provisions ought not to be applied to the assessee.

53. Similar is the position in the following cases, amongst others:

i) "ITO vs. Zydus Altana Healthcare (P) Limited", 44 SOT 132 (Mumbai)
ii) "ACIT vs. Dufon Laboratories", 39 SOT 59 (Mumbai) and
iii) "IJM (India) Infrastructure", 28 ITR (Trib) 176 (Hyd)

54. For the above discussion, the assessee's support to the impugned order on both counts is found to be correct. The AO erred in not himself examining the issue of TP and with the approval of the ld. CIT, made a reference to the TPO u/s 92CA(1) of the Act; that the AO as well as the ld. CIT(A) failed to apply their mind to the TP Report filed by the assessee, or to any other material or information or document furnished. The TPO made an adjustment which was incorporated by the AO in the assessment order. Thereby, the AO as well as the ld. CIT(A) did not discharge necessary respective judicial functions conferred on them under sections 92C and 92CA of the Act. Further, the assessee is also correct in contending that no TP adjustment can be made in a case like the present one, where the assessee enjoys u/s 10A or 80HHE of the Act, or where the tax rate in the country of the Associated Enterprises is higher than the rate of tax in India and where the establishment of tax avoidance or manipulation of prices or establishment of shifting of profits is not possible.

55. On the basis of the above reasons, qua Ground No.5, accepting the pleas raised by the assessee to support the CIT(A)'s order, without going into the merits of this Ground, the order of the ld. CIT(A) is confirmed. Ground No.5 is rejected.

56. Consequently, the appeal is partly allowed, as indicated.

**C.O. No.216(M/2010**

58. The ld. counsel for the assessee states at the bar that he does not wish to press the C.O. Rejected as not pressed.

59. Accordingly, the cross objections are dismissed as not pressed.

60 In the result, the appeal in ITA No.7513/M/2014 is partly allowed, as indicated above. C.O. No.216/M/2014 is dismissed as not pressed.

Order pronounced in the open court on 4 November, 2015.

Sd/- Sd/-

(RAJENDRA) (A.D. JAIN)
ACCOUNTANT MEMBER JUDICIAL MEMBER
/SKR/
Dated: 04/11/2015

Copy of the order, forwarded to :

1. The Assessee: M/s. Tata Consultancy Services Limited, Mumbai.
2. The DCIT, Circle-1, Mumbai
3. The CIT(A)-15, Mumbai.
4. The CIT, Mumbai
5. The SR DR, ITAT MUMBAI

True copy

By Order

(Assistant Registrar)