IN THE INCOME TAX APPELLATE TRIBUNAL
PUNE BENCH "C", PUNE – VIRTUAL COURT

BEFORE SHRI R.S. SYAL, VICE PRESIDENT AND
SHRI S.S. VISWANETHRA RAVI, JUDICIAL MEMBER

आयकर अपील सं. / ITA No.601/PUN/2017
Assessment Year : 2012-13

DCIT, Circle-1(1), Pune	Vs.	M/s. Barclays Technology Centre India Pvt. Ltd., 3rd Floor, Block-C, Panchashil Tech Park, Off Airport Road, Yerawada, Pune 411 006 PAN : AADCB1173D
Appellant		Respondent

आयकर अपील सं. / ITA No.700/PUN/2017
Assessment Year : 2012-13

Barclays Global Service Centre Private Limited (earlier known as Barclays Technology Centre India Private Limited, Ground to 7th Floor, Wing-3, Cluster A, EON Free Zone, MIDC Knowledge Park, Kharadi, Pune 411 014 PAN : AADCB1173D	Vs.	DCIT, Circle-1(1), Pune
Appellant		Respondent

Assessee by	Shri Rajendra Agiwal
Revenue by	Shri Mahadevan A.M. Krishnan
Date of hearing	12-01-2021
Date of pronouncement	12-01-2021

आदेश/ ORDER

PER R.S.SYAL, VP :

These two cross appeals - one by the assessee and other by the Revenue – emanate from the order dated 29-12-2016 passed by the ld. CIT(A) in relation to the assessment year 2012-13.

2. The first issue raised by the assessee in its appeal is against the confirmation of disallowance of leased line charges (link service cost) on account of non-deduction of tax at source. First ground of the Revenue's appeal is also interconnected with the same.

3. Briefly stated, the facts of the case are that the assessee is an Indian Private limited company engaged in providing Software Solution services to Barclays group worldwide. It has one undertaking approved as a 100% Export Oriented unit eligible for deduction u/s.10B of the Income-tax Act, 1961 (hereinafter also called `the Act'); another unit within the area of Special Economic Zone (SEZ) entitled to deduction u/s.10AA of the Act; and still another unit in Domestic Tariff Area (DTA) in Mumbai. During the course of assessment proceedings, the Assessing Officer (AO) observed that the assessee paid a sum of Rs.2,41,82,749/- as leased line charges to various vendors in India, which were claimed as deduction. On being called upon to explain as to why no deduction of tax at source was made in terms of section 194J of the Act, it was submitted that the amount paid was not in the nature of fees for Professional or technical services or royalty etc. in the hands of recipient warranting any deduction

of tax at source. The AO found that the assessee was engaged in software development and production of software products. Internet with high bandwidth was required for such work. A dedicated lease line for internet service was taken from supplier. The payment was held by the AO to be in the nature of fees for technical services requiring deduction of tax at source u/s 194J of the Act. Having not done so, the AO invoked section 40(a)(ia) of the Act. He noticed that out of such sum of Rs.2.41 crore, an amount of Rs.55,46,411/- was incurred against SEZ unit. The AO opined that the enhanced claim of deduction u/s.10AA due to disallowance u/s 40(a)(ia) on this count will not be available to the assessee despite the judgment of Hon'ble Bombay High Court in the case of *CIT Vs. Gem Plus Jewellery India Ltd. (2011) 330 ITR 175 (Bom.)*. The ld. CIT(A) approved the stand of the AO, in principle, by holding the amount paid by the assessee was in the nature of `Royalty' under the terms of Explanation 6 to section 9(1)(vi) of the Act, inserted by the Finance Act, 2012 w.r.e.f. 01-06-1976. That is how, he held that the assessee was obliged to deduct tax at source on payment of Rs.2.41 crore. He, however, held that the disallowance of the leased line charges for a sum of Rs.55,46,411/-, pertaining to the SEZ unit of the assessee, would

make the assessee eligible for deduction u/s.10AA at the enhanced income. Whereas, the assessee is aggrieved by the sustenance of disallowance u/s.40(a)(ia) to the tune of Rs.2.41 crore, the Revenue has challenged the succour provided by the ld. CIT(A) in allowing deduction u/s.10AA at the enhanced profit because of the disallowance of Rs.55.46 lakh pertaining to the eligible unit.

4. We have heard the rival submissions through Virtual Court and meticulously scanned the relevant material on record. The moot question is if the assessee was liable to deduct tax at source on the amount of leased line charges paid by it to various vendors in India so as to warrant disallowance u/s 40(a)(ia) of the Act? The AO has invoked this provision in the hue of section 194J of the Act. Section 194J requires deduction of tax at source, *inter alia*, on `royalty'. Explanation to section 194J states through clause (ba) that "royalty" shall have the same meaning as in Explanation 2 to clause (vi) of sub-section (1) of section 9. Explanation 2 to section 9(1)(vi) defines the term "Royalty" to mean consideration for certain things as set out in clauses (i) to (vi). Clauses (i) to (iii) of Explanation 2 refer to the term `process'. Explanation 6 to section 9(1)(vi) inserted by the

Finance Act, 2012, clarifies the ambit of the expression `process' as used in Explanation 2 to section 9(1)(vi). Thus Explanations 5 and 6, in the present context, are just extensions of the Explanation 2 to section 9(1)(vi), which take us to section 194J of the Act.

5. The Finance Act, 2012 has inserted Explanations 4, 5 and 6 to section 9(1)(vi) w.r.e.f. 01-06-1976 defining "income by way of Royalty". Explanation 6 states that the expression `Process' includes and shall be deemed to have always included "*transmission by satellite* (including up-linking, amplification, conversion for down-linking of any signal), *cable, optic fibre or by any other similar technology,* whether or not such process is secret". Thus, with the insertion of Explanation 6 clarifying the scope of the expression "Process" as used in Explanation 2 to section 9(1)(vi), it becomes palpable that if any charge is paid for transmission by cable, optic fibre or by any other similar technology, it will get covered within the definition of "income by way of Royalty". Expression 5 further clarifies that the possession or control of the property with the payer is no more relevant.

6. Leased line is a dedicated communication channel that easily interconnects two or more sites ensuring uninterrupted data flow from one point to another. It is a dedicated, fixed-bandwidth data connection, which allows users to have a reliable, high-quality internet connection. As per the assessee's submission before the ld. CIT(A), as captured on page 9 of the impugned order, it: `entered into an arrangement with third party vendors for providing Digital Subscriber Line facility i.e. broadband communication technology used for connecting to the internet, Ethernet leased line ….. These facilities enables the Appellant to access a standard communication line for highly secured communication. …it is a dedicated line provided to the Appellant…'. Thus the assessee paid for securing a dedicated line for flow of its data, which is nothing but leased line charges. When we consider Explanations 5 and 6 read with Explanation 2 to section 9(1)(vi), it becomes graphically clear that the leased line charges paid for transmission by any technology, get covered within the definition of "Royalty" by the Finance Act 2012 w.r.e.f. 01-06-1976 covering the assessment year under consideration.

7. We have noted above that the assessee is an Indian company and it made payment of leased line charges to various vendors in India, as has also been noted by the AO by reproducing reply of the assessee in para 7.1 of his order. In view of the fact that a resident paid leased line charges to another resident, the matter ends by examining the ambit of the term "Royalty" under the Act itself and there is no need to examine various DTAAs which have been looked into by the Tribunal in certain decisions for holding that leased line charges are not `royalty' in the light of the definition of the term "Royalty" as used in the respective DTAAs.

8. Having held that the payment of leased line charges amounting to Rs.2.41 crore amounted to "Royalty" and the same is covered u/s.194J, the next point requiring consideration is as to whether the assessee could have legally deducted tax at source from the payments made during the F.Y. 2011-12 corresponding to the A.Y. 2012-13 under consideration?

9. At this juncture, we want to record that taxability of leased line charges in the hands of the payee is one aspect and deduction of tax at source there from by the payer is another. There is no doubt that the retrospective amendment by insertion of

Explanations 4 to 6 to section 9(1)(vi) made by the Finance Act 2012 albeit with retrospective effect form 01-06-1976 have rendered the amount chargeable to tax as `royalty' in the hands of the recipient. But the position regarding deduction of tax at source by the payer is little different. TDS contemplates making deduction before making the payment. Once an amount is paid as per the law prevailing at the relevant time not requiring any deduction of tax at source, any later retrospective amendment covering the amount under a specific taxing provision cannot bring the hands of clock back so as to require the payer to deduct tax at source. Liability to deduct tax at source can be fastened only under the law prevailing at the time of payment. If no liability exists at the time of payment, any subsequent retrospective amendment cannot be enforced against the payer. Once there is no liability to deduct tax at source at the material time, the fortiori is that there can be no question of disallowance u/s 40(a)(ia) of the Act.

10. Reverting back to the factual panorama, it is obvious that the Finance Bill, 2012 became the Finance Act, 2012 somewhere after the close of the F.Y. 2011-12. As opposed to that, the Financial year corresponding to the A.Y. under consideration

came to an end before that. Ergo, it is overt that when the payment of leased line charges was made, no existing provision at that time made the assessee clearly liable to deduct tax at source. Since the leased line charges got the final dressing up as `Royalty' u/s 9(1)(vi) of the Act after the close of the relevant Financial year, we have no hesitation in holding that - even though the amount became chargeable to tax as royalty in the hands of the recipient under the Act for the year under consideration - but the same did not fasten an obligation to deduct tax at source as the assessee could not have activated its sixth sense to ascertain beforehand that an obligation to deduct tax at source was in offing. As the scope of "Royalty" came to be expanded after the close of the financial year when the assessee had already paid lease line charges, we hold that the same could not have triggered deduction of tax at source so as to warrant any disallowance u/s.40(a)(ia) of the Act. Thus, ground No.1 by the assessee is allowed.

11. In view of our decision in allowing deduction of Rs.2.41 crore in entirety, there can be no question of making any separate disallowance in respect of 10AA unit. The finding rendered by the ld. CIT(A) in sustaining the disallowance and simultaneously

allowing deduction u/s 10AA at the resultant enhanced income has, thus, become academic. Thus, the ground of the assessee is allowed and that of Revenue is dismissed as infructuous.

12. Ground No.2 of the assessee's appeal is against the disallowance of expenditure on purchase of RSA tokens amounting to Rs.25,00,344/-.

13. The factual matrix of this ground is that the assessee purchased RSA tokens worth Rs.25.00 lakh and claimed the same as repair expenses in entirety. The AO did not allow the deduction despite the assessee's contention that the RSA tokens were used in rendering services to its Associated Enterprise and were charged at a mark up at 15% along with other costs incurred by it in rendering services. The AO treated the same as capital expenditure. After allowing deduction towards depreciation allowance, the AO made an addition of Rs.22,07,044/-. No relief was allowed by the ld. CIT(A).

14. Having heard both the sides in the backdrop of the relevant material on record, it is seen that the assessee was getting remunerated by its AE at cost plus 15%. The assessee specifically stated before the AO that the cost of RSA tokens was

repaid by its AE with 15% mark up and such amount was considered as part of income of the year under consideration. Once the amount of expenditure, debited to the Profit and loss account, gets specifically credited to the Profit and loss account with a certain mark-up, there can be no question of disallowing the expenditure so charged while continuing to treat the amount credited as income. Notwithstanding that, the ld. AR has placed on record a copy of the order passed by the Tribunal in the case of *Amdocs Development Centre India Pvt. Ltd. Vs. JCIT (ITA No.69/PUN/2018)* dealing with the similar issue. Vide order dated 27-11-2018, the Tribunal has held that RSA tokens are in the nature of revenue expenditure and hence deductible. We, therefore, order to delete the disallowance of Rs.22.07 lakh sustained in the first appeal.

15. Having found that first ground of Revenue's appeal has become infructuous because of our decision on Ground No.1 of the assessee's appeal, the only other issue which survives in the Revenue's appeal is against the inclusion of Infosys Technologies Ltd. in the determination of the Arm's Length Price of the international transaction.

16. Briefly stated, the facts of the case are that the assessee declared an international transaction of "Provision of software services" to Barclays Bank Plc. with transacted value of Rs.580.43 crore. It benchmarked the international transaction under the Transactional Net Margin Method (TNMM). Certain companies were chosen as comparable to demonstrate that the assessee's margin was at the ALP. The TPO made certain inclusions in/exclusions from the list of comparables, which led to the transfer pricing adjustment. The ld. CIT(A) directed, *inter alia,* to exclude Infosys Technologies Ltd. from the list of comparables, against which the Revenue has come up in appeal before the Tribunal.

17. Having heard the rival submissions and gone through the relevant material on record, it is seen that the international transaction is that of `Provision of software services' for which the assessee was compensated at cost plus 15%. The assessee is acting as a captive unit to its AE for rendering software services. In contrast, the Infosys Technologies Ltd. is a giant company rendering on-shore and off-shore services at a very high scale. This company was also included by the TPO in his order for the immediately preceding assessment year 2010-11, which the ld.

CIT(A) directed to exclude. Though the Revenue preferred appeal against the order passed by the ld. CIT(A) for such earlier year but chose not to assail the exclusion of Infosys Technologies Ltd. It is further seen that the Hon'ble Delhi High Court in *CIT Vs. Agnity India Technologies Pvt. Ltd. (2013) 219 Taxman 26 (Delhi)* has ordered to exclude Infosys from the list of comparables of Agnity India Technologies Pvt. Ltd., a captive service provider, like the assessee under consideration. In view of the foregoing discussion, we are satisfied that the ld. CIT(A) was justified in excluding this company from the list of comparables.

18. The ld. AR stated that the assessee has raised additional grounds of appeal for inclusion/exclusion of various companies because of abundant caution. Such grounds were also stated to be not adjudicated by the ld. CIT(A) as relief was allowed on the exclusion of Infosys. The ld. AR stated that if the Departmental ground challenging the exclusion of Infosys is dismissed, then the additional grounds raised by it would lose its significance.

19. In view of our decision upholding the exclusion of Infosys Technologies Ltd., these additional grounds raised by the assessee are dismissed as having become academic in nature.

20. In the result, the appeal of the Revenue is dismissed and that of the assessee is allowed.

Order pronounced in the Open Court on 12th January, 2021.

Sd/-	Sd/-
(S.S.VISWANETHRA RAVI)	**(R.S.SYAL)**
JUDICIAL MEMBER	**VICE PRESIDENT**

□□□□Pune; □□□□□ Dated : 12th January, 2021 □□□□

□□□□□□ □□□□□□ □□□□ /**Copy of the Order is forwarded to:**

1. □□□□□□ / The Appellant;
2. / The Respondent;
3. The CIT(A)-13, Pune
4. The Pr.CIT-V, Pune
5. िवभागीय ितिनिध, आयकर अपीलीय अिधकरण, पुणे"**सी**" / DR 'C', ITAT, Pune;
6. गाडफाईल / Guard file.

□□□□□□□□□□/BY ORDER,

// True Copy //

Senior Private Secretary
आयकर अपीलीय अिधकरण ,पुणे/ITAT, Pune

		Date	
1.	Draft dictated on	12-01-2021	Sr.PS
2.	Draft placed before author	12-01-2021	Sr.PS
3.	Draft proposed & placed before the second member		JM
4.	Draft discussed/approved by Second Member.		JM
5.	Approved Draft comes to the Sr.PS/PS		Sr.PS
6.	Kept for pronouncement on		Sr.PS
7.	Date of uploading order		Sr.PS
8.	File sent to the Bench Clerk		Sr.PS
9.	Date on which file goes to the Head Clerk		
10.	Date on which file goes to the A.R.		
11.	Date of dispatch of Order.		

*