

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

**BEFORE SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER
AND
SMT. BEENA PILLAI, JUDICIAL MEMBER**

IT(TP)A No.2506/Bang/2019
Assessment Year: 2015-16

M/s. SAP Labs India Pvt. Ltd. No.138, Export Promotion Industrial Park Whitefield Bangalore 560 066 PAN NO : AAFCS3649P	Vs.	JCIT Special Range-6 Bangalore
APPELLANT		RESPONDENT

Appellant by	:	Shri Aliasgar Rampurawala, A.R.
Respondent by	:	Shri Sankar Ganesh K., D.R.

Date of Hearing	:	23.05.2023
Date of Pronouncement	:	25.05.2023

O R D E R

PER CHANDRA POOJARI, ACCOUNTANT MEMBER:

This appeal by assessee is directed against final assessment order passed by JCIT Special Range-6, Bangalore for the assessment year 2015-16 u/s 143(3) r.w.s. 144C(13) of the Income-tax Act, 1961 [‘the Act’ for short] dated 10.10.2019. The assessee has raised following grounds:

“The grounds mentioned herein by the Appellant are without prejudice to one another.

- 1. On the facts and in circumstances of the case and in law, the order of the Joint Commissioner of Income- Tax Special Range-6, Bengaluru (‘learned*

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AO') to the extent prejudicial to the Appellant, is bad in law, contrary to the facts and circumstances of the case and is liable to be quashed.

2. On the facts and in circumstances of the case and in law, the Dispute Resolution Panel (learned DRP) erred in not appreciating that the order of the learned Assistant Commissioner of Income-tax (Transfer Pricing) — 1(3)(1), Bangalore (learned TPO) passed under Section 92CAA of the Income-tax Act, 1961 ('the Act') is contrary to law and thus liable to be quashed.
3. On facts and in the circumstances of the case and in law, the learned DRP/AO/TPO erred in making an upward adjustment of INR 1,774,850,318 to the transfer price of the Appellant's international transactions in respect of software development services.

Grounds for software development services

4. On the fact and in the circumstances of the case and in law, with respect to adjustment to the transfer price of the software development services, the learned DRP/AO/TPO erred in:
 - 4.1. Rejecting the Transfer Pricing ('TP') documentation maintained by the Appellant under Section 92D of the Act, in good faith and with due diligence.
 - 4.2. Rejecting the comparability analysis carried out by the Appellant in the TP documentation and in conducting a fresh comparability analysis for the software development services based on the application of additional filters in determining the arm's length price.
 - 4.3. Using data, which was not contemporaneous and which was not available in the public domain at the time of preparing the TP documentation.
 - 4.4. Not considering the multiple year/prior year data of comparable companies while determining the arm's length price in relation to the Appellant's international transactions with its AEs.
 - 4.5. Using information under section 133(6) of the Act, which tantamount to choosing secret comparable companies whose information was not available in public domain while preparing the transfer pricing documentation for the relevant financial year.
 - 4.6. Disregarding certain filters applied by the Appellant in selection of the comparable companies at the time of TP documentation.

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- a) *Rejection of companies whose employee cost is less than 25% of operating revenue;*
- b) *Rejection of companies having income from core services less than 75% of the total sales;*
- c) *Rejection of companies having export sales less than 75% of the total sales; and*
- d) *Rejection of companies having different financial year ending or data of the company do not fall within 12 month period.*

4.8. *Including the following companies even though they are functionally different from operational profile of the Appellant:*

- a) *Tata Elxsi Limited (Seg);*
- b) *Rheal Software Private Limited;*
- c) *Mindtree Limited*
-) *..Larsen & Tubro Infotech Limited;*
- d) *R S Software (India) Limited*
- e) *Infolvans Technologies Limited*
- f) *Persistent Systems Limited;*
- g) *Nihilent Technologies Limited;*
- h) *Aspire Systems (India) Private Limited;.*
- i) *Inteq Software Private Limited;*

4.9. *Excluding the following companies even though they are functionally comparable to the Appellant and passes all the filters applied by the learned TPO in its order:*

- a) *Akshay Software Technologies Limited;*
- b) *Celstream Technologies Limite*
- c) *I2T2 India Limited; and*
- d) *Infomile Technologies Limited.*

4.10 *Not considering certain expenses such as provision for doubtful debts/bad debts/expenses and liabilities written back, as operating in nature on the premise that these are not the routine operating costs in determining the operating mark-up of the comparable companies.*

4.11. *Not providing an adjustment for the differences in working capital of the Appellant and the comparable companies.*

4.12. *Not providing suitable adjustment to account for differences in the risk profile of the Appellant*

4.13 *Computing incorrect operating mark-up of certain comparable companies:*

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- a) *Kals Information Systems Ltd.;*
- b) *E-Zest Solutions Limited;*
- c) *CG-VAK Software & Exports Limited; and*
- d) *Tata Elxsi Limited (Seg)*

4.14 *Computing incorrect operating mark-up of the Appellant.*

Other than Transfer Pricing Related

5. *That the learned AO erred in levying interest under section 234B of the Act of INR 321,000,259.”*

2. At the time of hearing, the assessee pressed only following grounds and not pressed other grounds for which the Id. A.R. made an endorsement. Accordingly, only the following grounds are adjudicated and other issues are dismissed as not pressed.

Ground No.4.8:

3. The assessee sought the exclusion of following comparables:

- (c) Mind Tree Ltd.
- (d) L&T Infotech Ltd.
- (f) Infobeans Technologies Ltd.
- (g) Persistent Systems Ltd.
- (k) Infosys Ltd.

(c) Mind Tree Ltd.:

4. The assessee has following objections:-

- *Diversified operation and lack of segmental data*
- *Significant R&D activity*
- *Presence of intangibles*
- *Significant onsite activity*

4.1 The Id. D.R. submitted that this company is not functionally comparable as it is engaged in providing services in diverse areas such as analytics, information management, application development, business process management, business technology consulting, infrastructure management services, product

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engineering and SAP services. It was also contended that this company is engaged in sale of products and also engaged in out sourcing IT services in banking and financial services and insurance sector, and also has R&D operations and patents and hence not functionally comparable.

4.2 He submitted that on perusal of the annual report of this company it was observed by the Id. DRP that this company is engaged in rendering of software development services in different verticals and not engaged in product sales as contended. As seen from the annual report of this company, it is engaged in international information technology consulting and implementation delivering business solutions through global software development. Its software development is structured into five verticals. As per Note 2.8.1, it is stated, that the company derives its revenue primarily from software services'. Again, as per Note 3.9 of the annual report 'the company is engaged in software development services'. Further, as per Note 3.1.2 of the annual report, the company's earnings in foreign currency from software development services was Rs.34.45 millions. As per the Note on Revenue Recognition, it has stated the principles adopted in recognizing revenue from software development services and there is no reference to product sales.

4.3 The Id. D.R. submitted that all this information clearly indicate that this company is engaged in software development. Besides, it is also relevant to note that the IP led revenue constituted meagre 2% of the consolidated revenue of the company for the F.Y. 2014-15 & 1% for F.Y. 2013-14. Considering this information in the annual report, the Id. DRP observed that this company is predominantly (i.e., 98%) engaged in software

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development activity and is functionally comparable to the assessee. The different services activities, in the form of consulting, maintenance, testing, management support services etc. clearly fall within the gamut of software development services, though it pertains to different verticals. That is the reason, the company has recognised a single business segment i.e., software development services, and which are categorized into five verticals. Besides, page 39, Annexure 4 of the annual report, the nature of the various services activities are given as under: -

Sl. No	Name and Description of main products / services	NIC Code of the Product / service	% total turnover of the company
1	Writing, modifying, testing of computer program to meet	62011	15.6
2	Web-page designing	62012	0.0
3	Providing software support and maintenance to the clients	62013	21.1
4	Computer consultancy and computer facilities management activities	62020	4.0
5	Software installation	62091	5.6
6	Other information technology and computer service activities n.e.c	62099	53.7
	Total		100

4.4 The ld. D.R. submitted that the above information clearly show that this company is engaged only in software development and related services. Therefore, the pleas that the company performs different and diverse activities and hence functionally different was rejected by the ld. D.R.P. The ld. DRP also rejected that plea that this company is product based company.

A plea was raised that this company also provides data analytic services which is high end and hence, cannot be compared to the

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assessee. The Id. DRP did not find merit in the plea, as undoubtedly, provision of data analytic services is not functionally different from software development activity. The data analytic services also use only certain software and tools, write codes to perform certain tasks. Like any other software application, these tools also facilitate and enables business enterprises for informed management and decision. Therefore, the Id. DRP did not find merit in the plea. Further, there cannot be any distinction between high end software activity and low end activity, so long as it falls within the purview of software development services. Besides, under the TNMM, such differences are tolerable and there is no requirement that the services / activities performed are identical. It is enough that the services are similar and fall within the same domain of software development. Accordingly, the pleas raised were rejected by the Id. DRP.

4.5 The Id. D.R. contended that this company has brand identity and earns significant brand profit on account of the same. He stated that the Id. DRP observed that the plea of assessee is purely based on conjectures as the assessee could not point to any information in the annual report to indicate that brand has contributed to the revenue growth or profitability of the company. Further, a careful perusal of the annual report for FY 2014-15 that there is no information as to brand promotion or as to impact of brand on its revenue growth. On the other hand, the Id DRP found various references in the annual report that their agile development practice have led to their revenue growth and sustainability in the market.

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4.6 The Id. D.R. submitted that the CFO in his message in the annual report has highlighted that the 'net profits grew over the previous year due to our efforts to drive higher operational efficiencies and aided by favourable currency movements'. Further at page 95 of the annual report, it was stated, 'our relentless focus on customer centricity has enabled us to become the partner of choice for our clients', and 'this reflects in our growth in high revenue clients'; 'our senior management comprises some of the seasoned global leaders from diverse backgrounds, geographies and with different arrears of specialization; and their leadership and governance helped us deliver consistent performance'. It is also pertinent to refer to the discussion on the risks faced by the company, wherein it is stated, 'we may face margin pressures due to customers having tough expectations on pricing or due to tactical movements on the part of our competitors to gain market shares. `Mindtree risks losing business to larger players in the industry, as our competitors may come up, with new offerings to challenge one market share and growth'. This information clearly indicates that brand has not leveraged business growth or sustenance in the market. Thus, the information in the annual report, clearly indicate that the company's customer centricity approach, technology, capability, skilled employees, delivery excellence have contributed to its revenue growth. Therefore, the Id. DRP did not find merit in the plea that brand has contributed to the revenue growth.

4.7 It was also argued that this company has significant intangibles and undertakes R & D activity. On careful perusal of the information in the annual report, the Id. DRP observed that the R&D activities are mainly towards remaining abreast with the

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technological development so as to remain competitive in the business and improve delivery excellence. Further we also note that there is no specific debit in the P&L a/c towards R&D activity, which only indicates that the R&D activities are routine and carried in the normal course of business. Besides, the Id. DRP observed that as per the information in the Asset Schedule (at page 11 of Annual report), the intangible assets comprised of Intellectual Property and computer software. The value of Intellectual Property as on 31.03.2013 was Rs.67 million, as on 31.03.2014 Rs.15 million and as on 31.03.2015 Rs.2 million which is insignificant and meagre in regard to its Asset Portfolio of Rs.6407 million; Rs.3436 million & Rs.4626 million in the corresponding period. The computer software refer to routine computer licences & not Intellectual Property generated by the company. Besides, the Id. DRP also observed that as per information in the annual report at page 90, the IP led revenue was only 2% during the year and meagre 1% in the earlier year. Thus, it is evident the intangibles have no material impact on the revenue growth or profitability of the company. Besides, the assessee has failed to establish that such differences have material effect on the margin of the above company, in terms of clause (i) of sub-rule (3) of Rule 10B, which provides that an uncontrolled transaction shall be comparable to an international transaction if none of the differences, if any, between enterprises entering into business transactions or likely to materially affect the profit arising from such transactions in the open market. The assessee is also engaged in R&D activities and hence this argument fails. Further, the assessee's R&D functions generate significant intangibles. Hence, this argument of the assessee was not accepted and the pleas were rejected by the Id. DRP.

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4.8 As to onsite expenses, the Id. DRP observed that the assessee has assumed that the entire expenditure incurred in foreign currency would be onsite expenses, which is incorrect, as there may be requirement to incur expenditure in foreign currency for offshore transactions also like payment of professional charges, sales commission etc. onsite activity would not affect adversely comparability when the company is otherwise functionally comparable. Therefore, the Id DRP considered it appropriate to reject these pleas.

5. We have heard the rival submissions and perused the materials available on record. This comparable has been considered in the case of M/s. SAP Labs India Pvt. Ltd. Vs. JCIT in IT(TP)A No.2519/Bang/2019 in assessment year 2015-16 dated 21.7.2022, wherein they placed reliance on the earlier order of the Tribunal in the case of LG Soft India Pvt. Ltd. in IT(TP)A No.2412/Bang/2019 dated 31.5.2022 wherein held as under:

“12.2 Further we note that Coordinate Bench of this Tribunal in case of LG Soft India Pvt. Ltd. vs. DCIT in IT(TP)A No. 2412/Bang/2019 dated 31/05/2022 observed as under:

“I. Mind Tree Limited:

5. The Ld. A.R. submitted that this company is not functionally comparable as it is engaged in providing service in diverse areas such as analytics, information management, application development business process management, business technology consulting, infrastructure management services, product engineering & SAP services. It was also contended that this company is engaged in sale of product and also engaged in outsourcing IT services in banking and financial services and insurance sector and also as R&D operations and patents and hence not functionally comparable. However, Ld. Dispute Resolution Panel (“DRP”) observed that this company is only engaged in software development and related services as seen from its financials. Therefore, the plea of the assessee that company performs different and diverse activities and hence functionally different was rejected by Ld.

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DRP. Further, it was observed by Ld. DRP that provision of data analytic services is not functionally different from software development activity. Data analytic services also used only in certain software and tools, writes codes task. Like in other software application, these tools also facilitate and enable business of enterprises for enough management and decisions. Therefore, the Ld. DRP observed that there cannot be any distinction between high end software activity and low-end activity so long as it falls within the purview of software development services. It was observed that under TNMM, such differences are tolerable and there is no requirement that services for activities performed are identical. It is informed that the services are similar and fall within the same domain of software development. Accordingly, Mind Tree Ltd. was included in the list of comparables while determining the ALP of international transactions with A.Es. Against this assessee is in appeal before us.

5.1. We have heard the rival submissions and perused the materials available on record. This company Mind Tree Ltd. was considered as not comparable in the case of Yahoo Software Development India Pvt. Ltd. in IT(TP)A No.2657/Bang/2018 & 2365/Bang/2019 dated 28.2.2020 by Bangalore Bench of Tribunal, wherein it was held as under:-

“41. The next company sought to be excluded is Mindtree Ltd. The submissions made before us were as follows:-

“Functionally dissimilar, diversified operation, significant R&D

spend, ownership of intangibles.

- Also engaged in business of rendering IP-Led revenue, infrastructure management, package implementation, consultancy services, etc. constituting 45% of overall revenue during FY 2014- 15.

- Diversified operation i.e. engaged in infrastructure management services, business process management, technology consulting, product engineering and SAP services. Also lacks segmental data

- Significant research & development activity. By incurring R&D expenses, it was able to deliver IP based video surveillance management, recording and analytic products and solutions. It has filed 4 patents in India and US so far in the area of Video analysis.

- Ownership of intangibles in the form of intangible property. Significant onsite activity:

- 46% of revenue earned under Onsite model.

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- Incurred overseas branch office expenses amounting to INR 1582 crores - Receives incentives from State of Florida in relation to the development center located overseas. Lack of segmental data

- Does not maintain segmental information in respect of profitability reported from business activities in the nature of infrastructure management services, technology consulting and SAP services. -

Acquisition of subsidiary – Discoverture Solutions LLC 42. The DRP while dealing with the aforesaid objections has merely taken the view that the presence of IPR revenue was insignificant and so also expenses of brand value, R&D & intangibles. More importantly, the DRP did not dispute the presence of 46% of revenue from onsite model, but went on to hold that the presence of revenue is not sufficient to exclude a company, when it is otherwise functionally comparable. On this aspect, we have already referred to the decision of the ITAT Bangalore Bench in the case of Trilogy e-business Software India P. Ltd. (supra) and in the light of this decision and the admitted factual position regarding presence of onsite revenue over and above the threshold limit of 25% of total revenue, we are of the view that this company should be excluded from the list of comparable companies. We hold and direct accordingly.”

5.2. In view of the above order of the Tribunal, we are inclined to direct the AO/TPO to exclude this company from the list of comparables. Directed accordingly.”

Respectfully following the same, we direct the Ld.AO to exclude this comparable.”

5.1 In view of the above order of the Tribunal, we are inclined to direct the AO/TPO to exclude Mind Tree Ltd. from the list of comparables to determine the ALP of international transactions.

(d) L&T Infotech Ltd.:

6. The ld. A.R. raised the following objections:

- Functionally dissimilar
- Presence of Brand value
- Significant onsite activity

6.1 The ld. D.R. relied on the order of ld. DRP and supported the inclusion of this comparable.

6.2 We have heard the rival submissions and perused the materials available on record. This comparable has been considered in the case of M/s. SAP Labs India Ltd. in ITA No.2510/Bang/2019 wherein they placed reliance on the earlier decision in the case of M/s. SAP Labs India Pvt. Ltd. in IT(TP)A No.684/Bang/2017 dated 23.7.2021 and held as under:

“LARSEN & TOUBRO INFOTECH LIMITED

7. The learned AR relied on the order of the ITAT Bangalore Benches in the case of CGI Information Systems and Management Consultants Private Limited in IT(TP)A No.586/Bang/2015 - order dated 11.04.2018 and submitted that it was excluded from the list of comparables for the reason that Larsen & Toubro Infotech Limited was a software product company and segmental information on SWD services was not available. In the present case, Larsen & Toubro Infotech Limited engaged in development of software onsite and its overseas revenue for the financial year 2011/2012 was Rs.27,838,752,995 and domestic revenue was Rs.1,756,792,454. Further in the case of Huawei Technologies India Pvt. Ltd. in IT(TP)A No.1939/Bang/2017 for assessment year 2012-2013 — order dated 31.10.2018 has taken the same view that it cannot be a comparable with that of the assessee. Being so, we direct the TPO to exclude the same from the list of comparables.”

6.3 In view of the above order of the Tribunal, we are inclined to direct the AO/TPO to exclude L&T Infrastructure Ltd. from the list of comparables.

(f) Infobeans Technologies Ltd.:

7. According to the ld. A.R., this is not functionally comparable to the assessee's case and lack of segmental data.

7.1. The ld. D.R. relied on the order of ld. DRP in para 4.7.1 page 38 of ld. DRP order

7.2 We have heard the rival submissions and perused the materials available on record. As discussed earlier, this issue came for consideration before this Tribunal in the case of EIT Services India

Pvt. Ltd. Vs. ACIT in IT(TP)A No.2498/Bang/2019 dated 3.9.2021 for the assessment year 2015-16, wherein held as under:

"8. We notice that M/s. Infobeans Technologies Ltd. have been directed to be excluded by the coordinate bench in the case of Metric Stream Infotech (India) Pvt. Ltd. with the following observations:

"14.3. Infobeans Technologies Ltd., Ld.AR submitted that this comparable was selected by authorities below as it passes all filters, based upon response received from this company under section 133 (6) of the act. He submitted that this observation is contrary to the facts and figures appearing in annual report. Referring to page 1015 Ld.AR submitted that this company is operating at CMMI Level 3 and-is a software service company specialising in business application development for web and mobile. In the company overview this company has been stated to be primarily engaged in providing custom developed services to offshore clients and it provides software engineering services primarily in custom application development, content management systems, enterprise mobility, Big Data analytics. Ld.AR thus submitted that this company is functionally not at all similar with a captive service provider like assessee that this providing Ltd services to its associated enterprises.

14.3.1. On the contrary Ld. CIT DR, referring observations of DRP in para 3.6.1 submitted that the activities of company fall under the gamut of software development has categorised by company itself and that the information obtained under section 133 (6) is sufficient enough to come to such conclusions. However he submitted that this comparable also may be sent back to learnt AO/TPO for verification.

14.3.2. We have perused submissions advanced by both sides in light of records placed before us.

It is observed that the annual report of this company categorises the diversify services provided by this company under software development segment. We also note that this company is basically into application development for web and mobile and provides customised services to its offshore clients comprising. Entire revenue received by this comparable ease under one single segment of sale of software. This company also owns software licenses.

14.3.3. In our considered opinion this comparable cannot be considered to be functioning in 100% risk mitigated environment and is a full-fledged enterprise. Such a comparable cannot be compared with a captive service provider like assessee.

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Accordingly we direct this comparable to be excluded from finalist.”

7.3 In view of above order of the Tribunal, we direct the AO/TPO to exclude this company from the list of comparables.

(g) Persistent Systems Ltd. and Infosys Ltd.

8. The ld. A.R. raised following objections:

- Fails RPT to sales filter of 25%
- Functionally dissimilar
- Engaged in research and development activities
- Significant outsourcing activity

8.1 The ld. D.R. relied on the order of ld. DRP

(h) Infosys Ltd.:

9. The ld. A.R. has raised following objections:

- Diversified operations and Functionally not comparable
- Presence of non-routine intangible
- Significant onsite operations
- Significant research and development activity

9.1 The ld. D.R. relied on the order of lower authorities.

9.2 We have heard the rival submissions and perused the materials available on record. This comparables has been considered in the case of EIT Services India Pvt. Ltd. in IT(TP)A No.2498/Bang/2019 for the assessment year 2015-16 wherein held as under:

7. *We notice that the coordinate bench in the case of Yahoo Software Development India Pvt. Ltd. (supra) has excluded following 3 companies holding them as not good comparable companies.*

(A) Persistent Systems Ltd:-

33. We have considered the rival submissions. We find that on the question of application of RPT filter, the assessee had made the following submission before the DRP:-

4. Fails the Related Party Transaction to Sales filter applied by the learned TPO

In the show-cause notice issued, the learned TPO has excluded companies for which the ratio of RPT to sales exceeds 25% during the current year i.e., during FY 2014-15. The relevant extract from the show-cause notice is reproduced below for ease of reference:

e) Companies who have more than 25% related party transactions of the sales were excluded.

Companies having related party transactions of more than 25% are proposed to be excluded. A threshold of 25% is being applied following the provisions of Section 92A(2)(a) which provides a limit of 26% of the equity capital carrying voting rights for treating an enterprise as Associated Enterprise. If the limit is reduced further it would only result in eliminating more and more companies, on the other hand if the limit is relaxed then companies with predominantly related party transactions would get included which would not represent uncontrolled transactions. Therefore, on a balancing note, 25% is a proper threshold limit for related party transactions. The companies having more than 25% related party transactions should therefore be rejected as comparables.

The Hon'ble ITAT has upheld the application of this filter by the TPO in its order in the case of M/s. Supporisoft India Pvt. Ltd for AY 2005-06 in IT (TP)A 1372/B/11 & 20/2012 dated 28.03.2013 following its own decision in the case of M/s. Actis Advertisers Pvt. Ltd vide ITA No.5277/De1/2011 dated 12.10.2012.

On perusal of the Annual Report of Persistent, we observe that the company has RPT in excess of 25% of the sales. The calculation of the same has been provided below for your ease of reference:

RPT to Sales ratio for FY 2014-15	Amount
Particulars	(INR Million)
Sale of services	2,410.02
Commission received	10.26
Purchase of software	1.49
Cost of technical professional	1,339.1
Commission paid on sales	111.79
Traveling and conveyance	19.27
Total related party transactions (A)	3,891.93
Total Sales (B)	12,424.98
RPT % of Sales (A/B)	31.32%

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*From the above computation, it is clear that the **controlled transactions of Persistent constitutes 31.32% of sales**. Based on the above, it can be seen that Persistent fails the 'RPT to sales ratio' filter applied by the learned TPO and should therefore not be considered as a comparable."*

34. *This argument has been addressed by the DRP in its order as follows:-*

"4.4.9 We note that the approach of the TPO in treatment of related party transaction into two sets, are for revenue transactions and other for expense transaction is logical and correct. We also note that the RPT filter was adopted by the TPO was with the above conditions and has adopted consistently. Hence, we do not find any infirmity the approach. Hence, we reject the assessee's plea. We hold that onsite expenses do not adversely affect comparability and hence, such plea is rejected."

35. *Further, the assessee had also raised plea with regard to onsite revenue filter by pointing out that onsite revenue is substantial and therefore this company should not be regarded as a comparable company with a company which does not have any onsite revenue. In this regard, the ld. counsel for the assessee placed reliance on the decision of the ITAT Bangalore Bench in the case of Trilogy e-business Software India P. Ltd. v. DCIT, ITA No.1054/Bang/2011 for AY 2007-08 dated 23.11.2012 wherein this Tribunal took the following view:-*

"64. The next objection of the Assessee is that when the most appropriate method selected for determining ALP is the TNMM there is no reason as to why one should look at price difference in offshore software development and onsite software development. It is no doubt true that in TNMM it is only the margins in an uncontrolled transaction that is tested with reference to the controlled transaction but it is not possible to ignore the fact that pricing will have an effect on the margins obtained in a transaction. The argument that if pricing structure were to be considered as criteria, then it will have to be seen as to what is the pricing structure of all the comparable for various projects cannot be accepted because the TPO has not chosen any other onsite software service provider with a revenue composition of more than 75% from onsite software services as comparable. As rightly observed by the TPO, the pricing is different in onsite when compared to offshore operations. The further observations of the TPO that the reasons for the same lie in the fact that while in the case of OFFSHORE projects most of the costs are incurred in India; an ONSITE project has to be carried out abroad significantly increasing the employee cost and other costs.

65. The next objection of the Assessee is with regard to Assets employed. The companies, which predominantly generate revenues from onsite activity, do not have significant assets as most of the work

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is carried on the site of customer outside India. The argument that the TPO has himself observed that software service providers do not require much assets cannot be basis to accept the Assessee's plea. Those observations are made by the TPO in the context of application of turnover filter and have been quoted out of context by the Assessee.

66. The next argument of the Assessee is that TPO has held that margins are lower in onsite software services and that margin is not a criteria to select or reject a comparable under Rule IOB(2) of the I.T. Rules. We are of the view that this argument again ignores the fact that the approach of the TPO has been to highlight the fact that there can be no functional comparability, if the assets employed and risks assumed are taken into consideration. It is in that context the TPO has referred to the margins.

67. The companies who generate more than 75% of the export revenues from onsite operations outside India are effectively companies working outside India having their own geographical markets, cost of labour etc., and also return commensurate with the economic conditions in those countries. Thus assets and risk profile, pricing as well as prevailing market conditions are different in predominantly onsite companies from predominantly offshore companies like the taxpayer. Since, the entire operations of the tax payer are taking place offshore i.e. in India; it is but natural that it should be compared with companies with major operations offshore, due to the reason that the economics and profitability of onsite operations are different from that of offshore business model. As already stated the Assessee has limited its analysis only to functions but not to the assets, risks as well as prevailing market conditions in which both the buyer and seller of services located. Hence, the companies in which more than 75% of their export revenues come from onsite operations are to be excluded from the comparability study as they are not functioning in similar economic circumstances to that of the tax payer. Hence, it is held that this filter is appropriately applied by the TPO.

68. Admittedly the onsite revenue in the case of the following comparable companies identified by the Assessee was more than 75% of its export revenues viz., a) Visu International Ltd. b) Maars Software International Ltd. c) Akshay Software Technologies Ltd. d) VJIL Consulting Ltd. e) Synfosys Business Solutions Ltd. The above companies were therefore rightly not considered as comparable by the TPO. We hold accordingly."

36. It is seen that the TPO in coming to the conclusion that the onsite revenue filter is not applicable has placed reliance on the decision of the ITAT Mumbai Bench in

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the case of Capegemini as quoted in para 16 in para 14 of the TPO's order, but that decision does not deal with a case of onsite revenue filter and the decision was rendered on the facts of its own case.

*37. On the issue of RPT filter, we notice that the TPO in para 16 has accepted that the RPT filter should be @ 25%. In the case of Persistent Systems Ltd., the RPT is at 31.32% as extracted in the earlier part of this order and therefore this company should be excluded by application of RPT filter. In view of the above, we do not wish to go into other grounds on which this company is sought to be excluded viz., that it is a product company and there is no segmental data between product and services segment, presence of onsite activity and the impact of extra-ordinary event of acquisition during the relevant previous year. **Therefore, this company is directed to be excluded from the list of comparable company.***

(B) LARSEN & TOUBRO INFOTECH LTD:-

*38. As far as L&T Infotech Ltd. is concerned, the ld. counsel for the assessee brought to our notice the decision of ITAT Delhi Bench in the case of Saxo India Pvt. Ltd. v. ACIT, ITA No.6148/Del/2015 for AY 2011-12, order dated 5.2.2016, wherein the Tribunal took note of the fact that this company was also trading in software and owned insignificant intangible assets. **The company was excluded from the list of comparable companies with reference to SWD services provider such as the assessee.** The ld. Counsel pointed out that though this decision was rendered with reference to AY 2011-12, the same reasoning would apply to AY 2015-16 also and in this regard, he drew our attention to page 696 of assessee's PB, which gives the details of the revenue generated by this company without any segmental break-up. Our attention was also drawn to page 682 of PB which shows that there is substantial onsite revenue activity as well as cost incurred on onsite software development. We notice from page 676 of assessee's PB that this company as part of its operating profit in Schedule-O of profit & loss account contains expenditure for 'cost of bought out items for resale' and this is a significant part of the operating expenditure. When we see the revenue in Schedule M of the profit & loss account, there is no break-up of the revenue with regard to software services and software product. In our opinion, this distinction is enough to exclude this company from the list of comparable companies as held by the Hon'ble Delhi ITAT in the case of Saxo India Pvt. Ltd. (supra) which decision was also confirmed by the Hon'ble Delhi High Court*

(C) INFOSYS LTD.

39. The next company which the assessee seeks to exclude is Infosys Ltd. As far as this company is concerned, it is seen that the following are the functional dissimilarities brought to our notice:-

“Functionally dissimilar - owns intellectual properties, incurs significant R&D costs & onsite activity.

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- *Engaged in diversified business activities.*
- *Involved in development of software products in addition to software services.*
- *Owns intellectual property rights.*
- *Incurs significant research and development costs.*
- *Carries out significant activities based on onsite business.*
- *Owns products such as Finacle, Edge Verve and other product based solutions.*

Extra-ordinary event of merger with Infosys Consulting India Ltd.

Segmental profit & loss account not available.

Commands substantial brand value.

40. *The DRP, however, has not thought it fit to exclude this company by observing that this company has substantial pre-dominant revenue from software services and the growth was not attributable to any brand value. Presence of onsite activity and the expenses on R&D have all been brushed aside. **In our view, the difference pointed out by the ld. counsel for the assessee before us show that this company cannot be compared with that of the assessee** basically because of its business model, presence of onsite revenue generation and other reasons cited before us. Besides, the reason that turnover of this company is huge and more than 10 times that of the assessee.”*

8. *We notice that M/s. Infobeans Technologies Ltd. have been directed to be excluded by the coordinate bench in the case of Metric Stream Infotech (India) Pvt. Ltd. with the following observations:*

“14.3. Infobeans Technologies Ltd.,

Ld.AR submitted that this comparable was selected by authorities below as it passes all filters, based upon response received from this company under section 133 (6) of the act. He submitted that this observation is contrary to the facts and figures appearing in annual report. Referring to page 1015 Ld.AR submitted that this company is operating at CMMI Level 3 and is a software service company specialising in business application development for web and mobile. In the company overview this company has been stated to be primarily engaged in providing custom developed services to offshore clients and it provides software engineering services primarily in custom application development, content management systems, enterprise mobility, Big Data analytics. Ld.AR thus submitted that this company is functionally not at all

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similar with a captive service provider like assessee that this providing Ltd services to its associated enterprises.

14.3.1. On the contrary Id. CIT DR, referring observations of DRP in para 3.6.1 submitted that the activities of company fall under the gamut of software development has categorised by company itself and that the information obtained under section 133 (6) is sufficient enough to come to such conclusions. However he submitted that this comparable also may be sent back to learnt AO/TPO for verification.

14.3.2. We have perused submissions advanced by both sides in light of records placed before us.

It is observed that the annual report of this company categorises the diversify services provided by this company under software development segment. We also note that this company is basically into application development for web and mobile and provides customised services to its offshore clients comprising. Entire revenue received by this comparable ease under one single segment of sale of software. This company also owns software licenses.

14.3.3. In our considered opinion this comparable cannot be considered to be functioning in 100% risk mitigated environment and is a full-fledged enterprise. Such a comparable cannot be compared with a captive service provider like assessee.

Accordingly we direct this comparable to be excluded from finalist.”

9. *Following the above said decisions rendered by co-ordinate benches, we direct exclusion of Persistent Systems Ltd., Larsen & Toubro Infotech Ltd. and Infosys Ltd. & Infobeans Technologies Ltd. from the final list of comparables.”*

9.3 In view of the above order of the Tribunal, we direct the AO/TPO to exclude Persistent Systems Ltd. & Infosys Ltd. from the list of comparables.

Ground No.4.9:

10. The Id. A.R. sought inclusion of following comparables:

- (c) I2T2 India Ltd.
- (d) Infomile Technologies Ltd.

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10.1 The ld. A.R. submitted that it satisfies all the filters adopted by the TPO. Regarding Infomile Technologies Ltd., the ld. A.R. submitted that this is functionally similar and passes all the filters.

10.2 With regard to both the comparables, the ld. D.R. submitted that Annual report of this company do not disclose related party transactions and non-availability of such crucial information make the data unusable for TP analysis and rejected to be upheld.

10.3 After hearing both the parties, we are of the opinion that this comparable is considered as comparable in the case of M/s. SAP India Pvt. Ltd. in IT(TP)A No.2510/Bang/2019 in assessment year 2015-16, wherein held as under:

*“13. In **Ground no. 4.9**, assessee is seeking inclusion of only two comparables viz., I2T2 India Ltd. and Infomile Technologies Ltd. 13.1 We note that these comparables have been remanded by Coordinate Bench of this Tribunal in case of Cypress Semiconductor Technology India Pvt. Ltd. vs. DCIT in IT(TP)A No. 2427/Bang/2019 by order dated 24/03/2022 for A.Y. 2015-16 observed as under:*

“(c) I2T2 India Limited and Infomile Technologies Limited:

(i) The companies came to be rejected by the TPO for the reason that information regarding its related party transactions was not available in the annual report. The DRP further upheld the exclusion.

(ii) It was submitted that if there is no disclosure with respect to the RPT made in the annual report, the presumption out to be that there is no RPT transaction. Further, it was submitted that these companies render SWD services and are functionally comparable to the assessee. This company also passes all the filters applied by the TPO. It was submitted that in cases of similar placed companies, this company is included in the final list of comparables. Reliance in this regard was placed on the decision of this Hon’ble Tribunal in the case of LG Soft India Pvt. Ltd. v. DCIT (Order dated 28.05.2019 passed by this Hon’ble Tribunal in IT(TP)A No. 3122/Bang/2018 for the assessment year 2014-15).

(iii) We have considered the submission. We find that on identical submissions, this Tribunal in the case cited by the learned Counsel for assessee directed inclusion of I2T2

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Company in the list of comparable companies with the following observations:

“12. We find force in the contentions of Ld A.R. If the Annual report of this company does not mention about Related Party transactions, then the assessee cannot be held responsible to prove a fact relating to a third party, which may or may not exist. We notice from the Auditors Report of M/s T2T2 India Ltd that the auditor in para 5(b) of Annexure to the Auditors' report has mentioned as under:-

“There are no transactions that are made at prices exceeding Rs.5 lakhs in respect of any party who is covered under section 301 of the Act during the financial year.”

Hence, in the absence of any specific information, there is merit in the contentions of the assessee that the above said company might not have had related party transactions during the year under consideration. Accordingly we do not agree with the reasoning given by Ld DRP for excluding this company as a comparable. Accordingly we direct the AO/TPO to include this company.”

*20. Following the said decision, we direct inclusion of this company in the list of comparable companies. **As far as Infomile is concerned, the company was rejected for the reason that the RPT details were not available. The reasoning contained in the decision rendered in the case of LG Soft (I) Pvt. Ltd., (supra) will apply and therefore this company should be included as a comparable company as otherwise this company is comparable. We hold and direct accordingly.”***

13.2 The Ld.DR has not brought any contrary decision or facts in order to take a different view in respect of the above comparables. Respectfully following the same, we direct the Ld. TPO to include I2T2 India Ltd. Infomile Technologies Ltd. Accordingly, this ground raised by assessee stands partly allowed.”

10.4 In view of the above order of the Tribunal, we direct the TPO to include I2T2 India Ltd. and Infomile Technologies Ltd. in the list of comparables for determining the ALP of international transactions.

Ground No.4.11:

11. Next ground for our consideration is ground no.4.11 with regard to working capital adjustment.

11.1 After hearing both the parties, we direct the AO/TPO to grant suitable working capital adjustment on actual basis. This issue is remanded back to the AO/TPO for reconsideration.

12. In the result, the appeal of the assessee is partly allowed for statistical purposes.

Order pronounced in the open court on 25th May, 2023

**Sd/-
(Beena Pillai)
Judicial Member**

**Sd/-
(Chandra Poojari)
Accountant Member**

Bangalore,
Dated 25th May, 2023.
VG/SPS

Copy to:

1. The Applicant
2. The Respondent
3. The CIT
4. The CIT(Judicial)
5. The DR, ITAT, Bangalore.
6. Guard file

By order

**Asst. Registrar,
ITAT, Bangalore.**