

**IN THE INCOME TAX APPELLATE TRIBUNAL
BANGALORE BENCHES "B", BANGALORE**

Before Shri George George K, JM and Shri B.R.Baskaran, AM

IT(TP)A No.2440/Bang/2019 : Asst.Year 2015-2016

M/s.Arista Networks India Private Limited, Global Technology Park Tower A & B, 11 th Floor Marathahalli Outer Ring Road Devarabessanhalli, Varthur Hobli Bengaluru – 560 103. PAN : AAICA9663J.	v.	The Dy.Commissioner of Income-tax, Circle 1(1)(1) Bangalore.
(Appellant)		(Respondent)

Appellant by : Sri.Padamchand Khincha
Respondent by : Sri.B.K.Panda, CIT-DR

Date of Hearing : 30.09.2021	Date of Pronouncement : 05.10.2021
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ORDER

Per George George K, JM

This appeal at the instance of the assessee is directed against the final assessment order dated 01.10.2019 passed u/s 143(3) r.w.s. 144C of the I.T.Act. The relevant assessment year is 2015-2016.

2. All the issues raised in this appeal relate to transfer pricing adjustment.

3. The brief facts of the case are as follows:

The assessee is a private limited company. It is primarily engaged in software development services (SWD) to its Associate Enterprises (AEs). The assessee also provides pre sales and marketing support services to its AEs for the products sold in India. For the services rendered to its AEs,

the assessee is remunerated on a cost plus mark-up basis (capital service provider). For the assessment year 2015-2016, the return of income was filed on 27th November, 2015, declaring total income of Rs.8,02,38,163. The assessment was selected for scrutiny and notice u/s 143(2) of the I.T.Act was issued. During the course of assessment proceedings, the A.O. referred the case to the Transfer Pricing Officer (TPO) to determine the Arm's Length Price (ALP) of the international transactions undertaken by the assessee with its AEs (In this case transfer pricing adjustment was made by TPO only with regard to software development segment). In the transfer pricing study, the assessee had selected Transactional Net Margin Method (TNMM) as the most appropriate method. The assessee had selected fourteen companies as comparable companies in its transfer pricing study. For the companies identified as comparable by the assessee, the weighted average operating profit earned on cost was computed using the financial data pertaining to financial year 2012-2013, financial year 2013-2014 and financial year 2014-2015. The weighted average profit margin of the comparable companies was determined from 7.56% to 19.99% with a median of 12.05%. Since operating profit on cost of assessee was 15.07%, the ALP of international transaction was sought to be justified in TP study. The details of financial result of the assessee as per P & L account, the comparable companies selected by the assessee and margin of comparable are as follows:-

Financial results of the assessee as per Profit & Loss account

Revenue from software exports	Rs.38,82,93,951
Total operating income – SWD	Rs.38,82,93,951
Operating expenses – SWD	Rs.33,74,48,924
Operating profit	Rs.5,08,45,027
Operating profit on cost of the assessee for the year.	15.07% (as per TP order 15.01%)

Comparable companies selected by the assessee

Sl. No.	Comparable companies	Weighted Average (unadjusted)
1.	Sagar Soft India Limited	-1.28%
2.	TVS Infotech Limited	3.25%
3.	Kals Information Systems Ltd.	11.25%
4.	Caliber Point Business Solutions Limited (Segment)	3.38%
5.	Akshay Software Technologies Limited	4.68%
6.	Sasken Communication Technologies Limited	7.56%
7.	Cigniti Technologies Limited	11.61%
8.	CG-VAK Software & Exports Limited	12.58%
9.	Helios & Matheson Information Technology Limited	19.70%
10	R Systems International Limited (Segment)	20.00%
11	SQS India BFSILimited (formerly Thinksoft Global Services Ltd. (Consolidated)	21.23%
12	Larsen & Toubro Infotech Limited	24.89%
13	R S Software (India) Limited	25.29%
14	InfoBeans Technologies Limited	41.85%
	35 th Percentile	7.56%
	Median	12.09%
	65 th Percentile	20.00%
Note: Margins of certain comparables have been updated based on the information available at the time of the show cause notice issued by the TPO.		

4. The TPO vide his order dated 29.10.2018 rejected the TP study of the assessee. The TPO held that the transfer pricing documentation prepared by the assessee by using data in computation of ALP in respect of provision for software

development services is not reliable / correct. Accordingly, the TPO undertook fresh search and thirteen comparables were selected by the TPO (some comparables are common in TP study of assessee and in the TPO's order). The TPO computed the operating margin of the comparable companies with respect to the software development segment with a median of 31.69% and accordingly, an adjustment was made on the account of ALP Rs.4,18,31,197 in the software development segment. The details of comparable companies selected by the TPO, the computation of ALP and the adjustment made by the TPO are as follows:-

The final set of comparable companies selected by the TPO in TP Order.

Sl. No.	Company Name	Financial Year wise OP/OC (%)			
		2014-15	2013-14	2012-13	Average
1.	Tata Elxsi Ltd (Seg.)	23.33	22.02	11.24	19.34
2.	Rheal Software Pvt. Ltd.	2.76	36.64	No data in public domain	19.88
3.	Mindtree Ltd.	20.55	21.18	19.75	20.55
4.	Larsen & Toubro Infotech Ltd.	24.22	23.54	17.44	24.82
5.	R S Software (India) Ltd.	32.66	24.14	17.44	24.82
6.	Infobeans Technologies Ltd.	20.7	41.95	29.22	29.91
7.	Persistent Systems Ltd.	31.11	35.44	28.2	31.69
8.	Nihilent Technologies Ltd.	29.19	35.72	No data in public domain	32.21
9.	Aspire Systems (India) Pvt. Ltd.	30.98	38.04	No data in public domain	34.18
10	Inteq Software Pvt.Ltd.	31.16	45	Fails employee cost filter	37.9
11	Infosys Ltd.	40.29	36.28	39.25	38.59
12	Thirdware Solutions Ltd.	43.69	44.68	32.65	41.12
13	Cybage Software Pvt.Ltd.	68.17	68.82	60.81	66.27
	35th Percentile				24.82%
	Median				31.69%
	65th Percentile				34.18%

Computation of ALP and TP adjustment in SWD segment:

Particulars	Formula	Amount
Taxpayers operating revenue	OR	3890,92,615
Taxpayers operating cost	OC	3383,24,419
Taxpayers operating profit	OP	507,68,196
Taxpayers PLI	PLI=OP/OC	15.01%
35 th Percentile Margin of comparable set		24.82%
Adjustment required (if PLI <35 th Percentile)		Yes
Median Margin of comparable set	M	27.37%
Arm's length price	ALP=(1+M) *OC	430923812.5
Price Received	Or	389092615
Shortfall being adjustment	ALP-OR	41831197

5. On receipt of the TPO's order dated 29.10.2018 passed u/s 92CA of the I.T.Act, the A.O. passed draft assessment order on 05.12.2018. Against the draft assessment order, the assessee filed objections before the DRP. The final list of comparables selected by the DRP was twelve in number. The DRP excluded Thirdware Solutions Limited from the list of comparables. The TPO gave effect to the order of the DRP and TP adjustment of Rs.4,18,31,190 was retained by the TPO. Thereafter, the final assessment order was passed on 01.10.2019 incorporating the TP adjustment.

6. Aggrieved, the assessee has filed this appeal before the ITAT. The assessee has raised several grounds. However, during the course of hearing, the learned AR limited his submission that out of the final list of comparables, the assessee is seeking to exclude twelve companies. It was also argued that 3 companies need to be included in the final list of comparables. The list of 12 companies, the assessee is

seeking to exclude from the final list of comparables are as follows:-

- (i) Sasken Communication Technologies Limited
- (ii) Tata Elxsi Limited
- (iii) Mindtree Limited
- (iv) Larsen and Toubro Infotech Limited
- (v) R S Software (India) Limited
- (vi) Persistent Systems Limited
- (vii) Nihilent Technologies Limited
- (viii) Infosys Limited
- (ix) Cybage Software Private Limited
- (x) Aspire Systems (India) Private Limited
- (xi) Inteq Software Private Limited
- (xii) Infobeans Technologies Limited.

6.1 The companies the assessee is seeking to include are as follows:-

- (i) Kals Information Systems Limited
- (ii) E-Zest Solutions Limited
- (iii) CG-VAK Software & Exports Limited

6.2 The learned AR submitted that out of twelve companies sought to be excluded, nine companies are to be excluded on turnover filter. The list of nine companies sought to be excluded are companies mentioned above in Sl.No.(i) to (ix). As regards exclusion of Aspire Systems (India) Private Limited and Inteq Software Private Limited, it was submitted by

referring to the financials that these companies are not functionally comparable to the assessee. As regards exclusion of Infobeans Technologies Limited, the learned AR relied on the order of the Bangalore Bench of the Tribunal in the case of Zynga Game Networks India Private Limited v. DCIT in ITA No.2573/Bang/2019 (order dated 23.03.2021). As regards the companies which the assessee is seeking to include in the comparable list, the learned AR submitted that the TPO in his order dated 29.10.2018 had held that the above three companies are functionally comparable and is to be included. However, the same was omitted to be included in the list of comparables selected by the TPO. It was further submitted that the assessee has filed rectification application for inclusion of the above three companies in the list of comparables. However, the same is pending adjudication.

6.3 The learned Departmental Representative submitted that out of the nine companies the assessee is seeking to exclude on account of turnover filter, only one company, namely, Infosys Limited alone the assessee had sought to exclude on turnover filter before the Income Tax Authorities. With regard to the exclusion of Aspire Systems (India) Private Limited and Inteq Software Private Limited, the learned DR relied on the order of the TPO and DRP.

6.4 In the rejoinder, the learned AR submitted that the assessee is entitled to raise a fresh plea for exclusion of a company from final list of comparables based on judicial pronouncement rendered subsequently wherein the said

company has been excluded from comparable list. In this context, the learned AR relied on the order of the Tribunal in the case of CIT v. Quark Systems India Private Limited reported in 4 ITR 606 (Tribunal).

7. We have heard rival submissions and perused the material on record. The turnover of the assessee company is Rs.42.56 crore. The assessee is seeking to exclude nine companies from the list of comparables on account of turnover filter. The nine companies sought to be excluded on account of turnover filter are mentioned at paragraph 6 (supra) (Sl.No.1 to 9). The AO / TPO had excluded companies having turnover of less than Rs.1 crore, however, the AO / TPO has not put upper limit to turnover for exclusion of companies having high turnover. The company having very high turnover cannot be compared to the company like the assessee, whose turnover is only Rs.42.56 crore. This proposition has been accepted by the Hon'ble Bombay High Court in the case of CIT v. Pentair Water Private Limited in ITA No.18/2018 (judgment dated 16.09.2015). The recent orders of the Bangalore Bench of the Tribunal in the case of M/s.Zynga Game Network India Private Limited v. DCIT in ITA No.2573/Bang/2018 (order dated 23.03.2021) and Pearson India Support Services Private Limited v. DCIT in ITA No.3171/Bang/2018 (order dated 28.06.2019) had followed the judgement of the Hon'ble Bombay High Court in the case of CIT v. Pentair Water Private Limited (supra) and directed the AO / TPO to exclude from the list of comparables, the

companies having turnover of more than Rs.200 crore. The relevant finding of the ITAT in the case of Zynga Game Network India Private Limited v. DCIT (supra), reads as follows:-

“38. We note that Ld.AO/TPO has applied filter of more than Rs.1 crore, but did not put an upper limit to the filter. This Tribunal in case of Genesis Integrating Systems India Pvt Ltd vs DCIT reported in (2012) 53 SOT 159 and various other decisions have held that, companies having turnover in excess of Rs.200 crores cannot be compared with companies having turnover less than Rs.200 crore. This preposition has been accepted by Hon’ble Bombay High Court in case of CIT vs Pentair Water Pvt.Ltd., by order dated 16/09/2015 in ITA No. 18/2015. Hon’ble Court upheld rejection of companies having turnover holding that turnover is a relevant factor in considering comparability of companies.

39. Objection raised by Ld.CIT.DR has been dealt with by this Tribunal in case of Autodesk India Pvt.Ltd. vs DCIT in (2018) 96 taxmann.com 263 for assessment year 2005-06. This Tribunal reviewed gamut of case laws to consider, whether companies having turnover more than Rs.200 crores should be regarded as comparable with a company having turnover less than 200 crore. This Tribunal held as under:

“17.7 We have considered the rival submissions. The substantial question of law (Question No.1 to 3) which was framed by the Hon’ble Delhi High Court in the case of Chryscapital Investment Advisors (India) Pvt. Ltd., (supra) was as to whether comparable can be rejected on the ground that they have exceptionally high profit margins or fluctuation profit margins, as compared to the Assessee in transfer pricing analysis. Therefore as rightly submitted by the learned counsel for the Assessee the observations of the Hon’ble High Court, in so far as it refers to turnover, were in the nature of obiter dictum. Judicial discipline requires that the Tribunal should follow the decision of a non-jurisdiction High Court, even though the said decision is of a nonjurisdictional High Court. We however find that the Hon’ble Bombay High Court in the case of Pentair Water India (P.) Ltd. (supra) has taken the view that turnover is a relevant criterion for choosing companies as comparable companies in determination of ALP in transfer pricing cases. There is no decision of the jurisdictional High Court on this issue. In the circumstances, following the principle that where two views are available on an issue, the view favourable to the Assessee has to be adopted, we respectfully follow the view of the Hon’ble Bombay High Court on the issue. Respectfully following the aforesaid decision, we uphold the order of the DRP excluding 5 companies from the list of comparable companies chosen by the

TPO on the basis that the 5 companies turnover was much higher compared to that the Assessee.

17.8 In view of the above conclusion, there may not be any necessity to examine as to whether the decision rendered in the case of Genisys Integrating Systems (I) (P.) Ltd. (supra) by the ITAT Bangalore Bench should continue to be followed. Since arguments were advanced on the correctness of the decisions rendered by the ITAT Mumbai and Bangalore Benches taking a view contrary to that taken in the case of Genisys Integrating Systems (I) (P.) Ltd. (supra), we proceed to examine the said issue also. On this issue, the first aspect which we notice is that the decision rendered in the case of Genisys Integrating Systems (I) (P.) Ltd. (supra) was the earliest decision rendered on the issue of comparability of companies on the basis of turnover in Transfer Pricing cases. The decision was rendered as early as 5.8.2011. The decisions rendered by the ITAT Mumbai Benches cited by the learned DR before us in the case of Willis Processing Services (supra) and Capegemini India (P.) Ltd. (supra) are to be regarded as per incurium as these decisions ignore a binding co-ordinate bench decision. In this regard the decisions referred to by the learned counsel for the Assessee supports the plea of the learned counsel for the Assessee. The decisions rendered in the case of NTT Data (supra), Societe Generale Global Solutions (supra) and LSI Technologies (supra) were rendered later in point of time. Those decisions follow the ratio laid down in Willis Processing Services (supra) and have to be regarded as per incurium. These three decisions also place reliance on the decision of the Hon'ble Delhi High Court in the case of Chriscapital Investment (supra). We have already held that the decision rendered in the case of Chriscapital Investment (supra) is obiter dicta and that the ratio decidendi laid down by the Hon'ble Bombay High Court in the case of Pentair (supra) which is favourable to the Assessee has to be followed. Therefore, the decisions cited by the learned DR before us cannot be the basis to hold that high turnover is not relevant criteria for deciding on comparability of companies in determination of ALP under the Transfer Pricing regulations under the Act. For the reasons given above, we uphold the order of the CIT(A) on the issue of application of turnover filter and his action in excluding companies by following the ratio laid down in the case of Genisys Integrating (supra).”

40. Ld.AR submitted that though this decision was rendered with reference to AY 2005-06 and 2006-07, same reasoning would apply to AY 2015-16 also and in this regard. Based upon above discussions and the decision relied by Ld.AR herein above. We are of opinion that objection raised by revenue cannot withstand the test of law.

Accordingly we direct Ld. AO/TPO to exclude Tata Elxi Ltd (Seg.), Mindtree Ltd., Larsen and Toubro Infotech Ltd., RS Software (India) Ltd., Persistent Systems Ltd., Nihilent Technologies Ltd., Infosys Ltd., Cybage

software Pvt.Ltd. for having high turnover as compared to a captive service provider like assessee.”

7.1 In this case, before the Income Tax Authorities, the assessee had sought for exclusion of only Infosys Limited based on the turnover filter. We find that the turnover of Infosys Limited is Rs.43,300 crore, which is thousand times more than the turnover of the assessee-company. Therefore Infosys Limited cannot be compared to the assessee, in view of the judicial pronouncements cited supra. Hence, we direct the AO / TPO to exclude Infosys Limited from the list of comparables.

7.2 As regards the eight other comparables, we find that the assessee before the Income Tax Authorities has not sought for exclusion of the same on turnover filter. Therefore, the eight companies sought to be excluded on turnover filter are restored to the files of the AO / TPO. The AO / TPO is directed to verify the turnover of these eight companies and exclude the same from the list of comparables if the turnover of each company had exceeded Rs.200 crore for the relevant assessment year. It is ordered accordingly.

Infobeans Technologies Limited

7.3 The assessee is seeking the exclusion of this company from the comparable list. According to the learned AR, Infobeans Technologies Limited is engaged in providing Custom Application Development (CAD), Content Management Systems (CMS), Enterprise Mobility (EM), Big Data Analytics (BDA). Therefore, it was submitted that

Infobeans Technologies Limited cannot be compared to assessee, who is engaged in providing routine software development services to its AEs.

7.3.1 We have heard rival submissions and perused the material on record. The Tribunal in the case of Zynga Game Network India Private Limited (supra) had excluded Infobeans Technologies Limited from the list of comparables. The Tribunal held that the said company was having multiple segments and cannot be compared with a captive service provider. The relevant finding of the Tribunal in the case of Zynga Game Network India Private Limited (supra), reads as follows:-

“43. 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.

44. 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.”

7.3.2 In the instant case, the assessee is a captive service provider to its AEs and the concerned assessment year is 2015-2016. The Tribunal in the case of Zynga Game Network India Private Limited (supra) was considering a case of an assessee, who is also a capital service provider to its AEs and was concerned with identical assessment year, namely, A.Y.

2015-2016. Therefore, following the order of the Tribunal in the case of Zynga Game Network India Private Limited (supra), we direct the AO / TPO to exclude Infobeans Technologies Limited from the list of comparables. It is ordered accordingly.

Inteq Software Private Limited

7.4 The assessee is seeking to exclude the above company from the list of comparables. According to the assessee, Inteq Software Private Limited provides application services, software testing, data warehousing, EI & EDI, BPO and staffing services. It is stated that Inteq Software Private Limited is also involved in end to end product development with primary focus in healthcare industry and there is no segmental information. The learned AR had referred the abridged balance sheet of Inteq Software Private Limited (refer pages 1356 and 1357 of the paper book filed by the assessee) to support his submission.

7.4.1 The learned Departmental Representative supported the order of the TPO / AO.

7.4.2 We have heard rival submissions and perused the material on record. On perusal of the abridged balance sheet of Inteq Software Private Limited, it is clear Inteq Software Private Limited is involved in multifarious services such as application services, software testing, data warehousing, EDI, BPO, staffing etc. However, we noticed from the AO / TPO and the DRP's order, it is stated that Inteq Software Private

Limited is only involved in software development services and the entire turnover is from such service. It is not clear how DRP had arrived at such a conclusion. The profit and loss account of Inteq Software Private Limited is not on record. Therefore, we are not in a position to verify the veracity of the findings of the AO / TPO and the DRP, which is contrary to the narration in the balance sheet of Inteq Software Private Limited. Therefore, we deem it appropriate to restore this issue to the files of AO / TPO. The AO / TPO is directed to afford a reasonable opportunity of hearing to the assessee and decide whether Inteq Software Private Limited is to be included in the comparable list of companies. It is ordered accordingly.

Aspire Systems (India) Private Limited

7.5 The assessee is seeking the exclusion of the above company from the list of comparables. It is contended that Aspire Systems (India) Private Limited is an outsourced technology service company focused on helping software companies create innovative products through its onsite and offshore model. It is also contended that the said company has also income from power generation. It was stated that bifurcation of revenue from both software and power generation services is not provided in the annual report. The learned AR also had contended that the said company fails RPT filter. The learned AR had took us through the abridged balance sheet of Aspire Systems (India) Private Limited to contend that the said company is not merely into the software

development services, but has multifarious activities and cannot be compared to the assessee.

7.5.1 The learned Departmental Representative supported the findings of the TPO / DRP.

7.5.2 We have heard rival submissions and perused the material on record. On perusal of the balance sheet of Aspire Systems (India) Private Limited, it is seen that the said company is an outsourced technology service company. It is also stated in the balance sheet that there is income from power generation. Since the profit and loss account of the assessee company is not enclosed, we are not in a position to examine the DRP's statement that Aspire Systems (India) Private Limited is a pure software development service provider. Therefore, in the facts of the instant case, we deem it appropriate to restore the issue to the files of the AO / TPO. The AO / TPO is directed to afford a reasonable opportunity of hearing to the assessee and take a decision whether Aspire Systems (India) Private Limited can be a comparable. It is ordered accordingly.

7.6 The assessee had sought to include three companies in the list of comparables. The three companies sought to be included in the list of comparables are – (i) Kals Information Systems Limited, (ii) E-Zest Solutions Limited, and (iii) CG-VAK Software & Exports Limited. It is submitted that the above three companies are primarily engaged in the software development services and is comparable to assessee. It was

further submitted that the TPO in the impugned order had accepted the above three companies as comparable to the assessee. However, omitted the same to include in the comparable list.

7.6.1 The learned Departmental Representative present was duly heard.

7.6.2 We have heard rival submissions and perused the material on record. The TPO in the impugned order, insofar as Kals Information systems Limited, had observed as follows:-

“The company is engaged in provision of software development services. The company passes all TPOs filter FAR similar. Hence accepted.”

7.6.3 As regards CG-VAK Software and Exports Limited, the observation of the TPO reads as follows:-

“CG-VAK Software and Exports Limited provides software products and services in India and internationally. It offers product innovation comprising product realization, modernization, mobile, and testing; digital innovation, including digital market, portals / e-commerce, creative UI/UX, and social; and technology innovation services. The company passes all TPOs filter. FAR similar. Hence accepted.”

7.6.4 The observation of the TPO with regard to E-Zest Solution Limited, reads as follows:-

“E-Zest Solutions Ltd. provides software product engineering and enterprise application development services in India and internationally. It designs, develops, enhances, migrates, tests, and maintains software products and applications. The company offers outsourced product development services, including new product design and development, feature enhancement, product platform migration, software product

testing, software product maintenance and support. FAR similar. Passes all TPO's filters. Hence acceptable."

7.6.5 In view of the above observation of the AO /TPO, it is clear that the above three companies were accepted as comparable, however, in the final list of comparables, the same was omitted to be included. Hence, we direct the AO / TPO to include the same in the final list of comparables for determination of arm's length price of the international transaction. It is ordered accordingly.

8. In the result, the appeal filed by the assessee is partly allowed.

Order pronounced on this 05th day of October, 2021.

Sd/-
(B.R.Baskaran)
ACCOUNTANT MEMBER

Sd/-
(George George K)
JUDICIAL MEMBER

Bangalore; Dated : 05th October, 2021.
Devadas G*

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Asst.Registrar/ITAT, Bangalore