

**IN THE HIGH COURT OF DELHI AT NEW DELHI**

% Judgment delivered on: 14.10.2024

+ **ITA 220/2022**

ALCATEL LUCENT INDIA LIMITEDAppellant

Versus

**DEPUTY COMMISSIONER OF INCOME TAX
& ANR** Respondents

AND

+ **ITA 221/2022**

ALCATEL LUCENT INDIA LIMITED Appellant

Versus

**DEPUTY COMMISSIONER OF INCOME TAX
& ANR** Respondents

Advocates who appeared in this case:

For the Appellant : Mr. Nageshwar Rao and Mr. Parth, Advs.

For the Respondent : Mr. Indruj Singh Rai, SSC, Mr. Sanjeev Menon, JSC, Mr. Rahul Singh, JSC and Mr. Anmol Jagga, Advs.

CORAM

HON'BLE MR JUSTICE VIBHU BAKHRU

HON'BLE MS. JUSTICE SWARANA KANTA SHARMA

JUDGMENT

VIBHU BAKHRU, J

1. The appellant has filed these appeals under Section 260A of the Income Tax Act, 1961 (hereafter *the Act*) impugning a common order



dated 16.08.2021 (hereafter *the impugned order*) passed by the Income Tax Appellate Tribunal (hereafter *the Tribunal*) in ITA No.5553/Del/2011 and ITA No.5554/Del/2011. The appellant had preferred the said two appeals in respect of assessment year (hereafter AY) 2007-08 against two separate orders, both dated 31.10.2011, passed by the Assessing Officer (hereafter *the AO*) under Section 143(3) read with Section 144C of the Act.

2. ITA No. 5553/Del/2011 was preferred by the appellant impugning the assessment of income of Alcatel Lucent Technologies India Pvt. Ltd. (hereafter *ALTIPL*) for the AY 2007-08.

3. The appellant preferred ITA No.5554/Del/2011 impugning the assessment of income of Alcatel Development India Pvt. Ltd. (hereafter *ADIPL*) for the AY 2007-08. Both the aforementioned companies – *ALTIPL* and *ADIPL* have since merged with the appellant.

4. The controversy involved in these appeals relates to the enhancement of total income chargeable to tax on the basis of orders passed by the Transfer Pricing Officer (hereafter *the TPO*). *ALTIPL* and *ADIPL* [hereafter also referred to as *the assessee(s)*] adopted the Transactional Net Margin Method (hereafter *TNMM*) with the ratio of operating profit (OP) to costs as the Profit Level Indicator (PLI) for determining the arm's length price (ALP) in respect of transactions of the assesseees with their associate enterprises (hereafter also referred to as *AEs*). The TPO rejected the Transfer Pricing Studies furnished by the assesseees and determined the ALP on the basis of filters selected certain



uncontrolled comparable entities for determining the PLI on arm's length basis. In the case of ALTIPL, the TPO determined its operating profit margin to costs at 25.44%, which was significantly higher than ADIPL's operating profit margin to cost of 10.57%.

5. Accordingly, the TPO passed an order dated 28.10.2010 under Section 92CA(3) of the Act proposing an upward adjustment of ₹27,91,55,906/- in respect of the ADIPL's software development segment.

6. In view of the said order of the TPO, the AO passed a draft assessment order dated 30.12.2010 assessing ADIPL's total income as ₹29,46,35,755/-.

7. Similarly, in case of ALTIPL, the TPO determined the operating profit margin at 25% (27.11% less working capital adjustment of 2.11%) for determining the ALP. This was significantly higher than ALTIPL's operating profit margin of 9.7%. Accordingly, the TPO passed an order dated 26.10.2010 proposing an enhancement of ₹57,29,49,678/- in respect of the software development segment of ALTIPL.

8. The AO passed a draft assessment order dated 03.12.2010 assessing ALTIPL's total income as ₹64,31,25,560/-.

9. The appellant objected to the aforementioned draft assessment orders before the Dispute Resolution Panel (hereafter *DRP*). In case of ALTIPL, the *DRP* upheld the adjustment proposed by the TPO and



accordingly, ALTIPL's income was enhanced by ₹57,29,49,678/-. Thereafter, the AO passed a final assessment order dated 31.10.2011.

10. Insofar as ADIPL is concerned, the DRP, upheld the action of the TPO but directed the TPO to grant the benefit of working capital adjustment. Accordingly, the ADIPL's enhanced income in the software development segment as proposed to be assessed was marginally reduced to ₹24,34,79,416/-.

11. The AO's final assessment orders dated 31.10.2011 in respect of ALTIPL and ADIPL were the subject matter of appeals before the Tribunal.

12. The appellant's challenge in the present appeals is confined to including certain uncontrolled entities as comparables for determining the ALP and excluding certain uncontrolled entities as comparables as suggested by the appellant.

13. On 01.02.2023, this Court framed the following common questions for consideration in the present appeals:

“(i) Whether the Tribunal misdirected itself on facts and in law, in not excluding the comparables Avani Cincom Technologies Ltd. and Ishir Infotech Ltd. in determining the Arm's Length Price concerning the international transactions undertaken by the appellant/assessee with an Associated Enterprise?

(ii) Whether the Tribunal misdirected itself both on facts and in law in not including the comparable Akshay Software Technologies Limited in determining the Arm's Length Price concerning the international transaction undertaken by the appellant/assessee with an Associated Enterprise?



(iii) Whether the Tribunal misdirected itself on facts and in law in failing to adjudicate the contentions of the appellant/assessee with regard to the exclusion of the following comparable companies: Tata Elxsi Limited and Sasken Communication Technologies Limited?”

QUESTION NO.(I)

AVANI CINCOM TECHNOLOGIES LIMITED

14. According to the appellant, the TPO had erred in including Avani Cincom Technologies Ltd. (hereafter *Avani*) as a comparable for the purpose of determining the operating profit margin for determining the ALP adjustment. It is the appellant’s case that Avani is not functionally comparable to ADIPL/ALTIPL.

15. ADIPL was originally incorporated as a private limited company on 03.03.1998. At the time of incorporation it was named as Alcatel Development Center Chennai Private Limited till the financial year 2002-03. ADIPL is a software development company and is engaged solely for the development of software for the Alcatel Lucent group of companies. ADIPL provides services in respect of software implementation, customization and maintenance. ALTIPL is also a software development company and is engaged in providing contract software development services for developing software applications.

16. As noted above, the TPO had rejected the Transfer Pricing Studies furnished by the assessee. It adopted the TNMM as the most appropriate method for determining the ALP. The TPO thereafter finalized the following filters to be applied in the specified order for ascertaining functional entities, which are similar to the assessee:



“10.1 Application of the above filters by the TPO

The filters have been applied in the following order.

- *Companies whose data is not available for the FY 2006-07 were excluded.*
- *Companies whose Software Development Service revenue is less than 75% of the total operating revenues were excluded.*
- *Companies whose software development service revenue <Rs.1 cr. were excluded*
- *Companies who have less than 25% of the revenues as export sales were excluded.*
- *Companies who have more than 25% related party transactions (sales as well as expenditure combined) of the operating revenues were excluded.*
- *Companies whose employee cost to revenues is less than 25% of the revenues were excluded.*
- *Companies having different financial year ending (i.e. not March 31, 2007) or data of the company does not fall within 12 month period i.e., 01-04-2006 to 31-03-2007, were rejected.*
- *Companies who have diminishing revenues / persistent losses for the period under consideration were excluded.*
- *Companies whose onsite income is more than 75% of the export revenues were excluded.*
- *Companies that are functionally different from that of taxpayer.”*

17. One of the comparable entities found by the TPO to be conforming to the above-mentioned filters is Avani. The said entity had reported sales of ₹3.55 crores and operating profit to total costs at 52.59% during the financial year 2006-07. The TPO found, on the basis of information available in the public domain, that Avani is a software development and consulting company. A notice under Section 133(6)



of the Act was issued to Avani. Avani replied to the said notice and the TPO found that it qualified the filters as applicable and therefore proposed its name as a comparable entity. The assessee objected to the same on the ground that Avani's functional and risk profile was not similar to their profiles. The assessee claimed that Avani is a product company and owned products like DXchange, Travel Solutions, Insurance Solution, Customer Appreciation and Relationship Management Application (CARMA), Content Management Systems etc. According to the assessee, Avani had not provided the details of its revenue and profit, segment wise. Therefore, on the basis of its annual reports, it was not possible to determine the quantum of revenue and its profit margin relating to the software development business to the exclusion of the revenues from products developed by the company. The appellant relied on the information that was available on the website of Avani. The relevant extract of the objections furnished by the appellant in respect of Avani, as set out in the order dated 26.10.2010 passed by the TPO under Section 92CA(3) of the Act, is reproduced below:

“1. Avani Cimcon. Technologies Ltd (‘Avani Technologies’)

In the Notice, your good self has proposed to include Avani Technologies as a comparable to the software development services provided by the Assessee. The argument of the Assessee in this connection is as below,

Functionally different – Product company: *Based on the details available on the website of Avani Technologies, the Assessee observes that the company is involved in provision of software development and IT services. Further, Avani Technologies own products like DXchange, Travel Solutions.*



Insurance Solution, Customer Appreciation and Relationship Management Application (CARMA), Content Management Systems etc. For your good self's ready reference the relevant extract from the website is provided as Exhibit II to the submission. As your good self would note, the existence of above product profile goes against the statement of Avani Technologies in its response to notice under section 133(6) wherein the company has claimed that it is a pure software services provider not owning any product.

Non availability of segmental details: *As your good self would note, the annual report of Avani Technologies does not provide the segmental details relating to operating income from IT services and sale of software products. Further, response provided by the company under section 133(6) also does not provide the classification as to income from IT services and products. In the absence of the same, the entire operation result of Avani Technologies cannot be considered as comparable to the software development services provided by the Assessee.*

Thus, based on the above argument, the Assessee is not in agreement with selection of Avani Technologies as comparable to the software development services of the Assessee.”

18. Similar objections were also raised by the appellant in the case of ADIPL and the same were noted in paragraph 30 of the order dated 28.10.2010 passed by the TPO. The same is reproduced below:

“30. Avani Cimcon Technologies Limited: the two arguments put forth by the assessee is that the company is functionally not comparable and data is not contemporaneously available. Apart from that assessee has also raised the issue that the company is actively into R&D whereas the assessee company does not indulge in any R&D.”

19. The TPO rejected the objections raised by the appellant regarding inclusion of Avani as a functionally comparable entity.



20. The TPO relied solely on the information as available on the website of Avani; information and data available in its annual report; and the response of Avani to the notice issued under Section 133(6) of the Act. The relevant extract of the order dated 26.10.2010 passed by the TPO is set out below:

“The company's main argument is that the company is into software products and segmental results are not available. In this regard, the taxpayer tried to rely upon the content available in the website. It is very pertinent to mention here that the TPO did not rely on the information available in websites as the information contained in the websites may not contain information relevant to the FY 2006-07 and may also contain many forward looking statements. Thus, the TPO relied only on the information / data available in the annual report combined with the information collected, if any, from the company. So, the TPO need not comment on what is available on the website of the company.

In regard to software products, the company in its reply as under categorically stated that the company is a purely software development company.

2. Software Development Process: We are Pure Software Development Service provider and Software Description is attached as per Exhibit-3.

3. Description of Business Activity: Avani Cimcon Technologies is in providing software development and consulting IT services to our international clients. We utilize proven technologies to enable customer's business systems. This technology focus has given us the opportunity to become proficient on a wide variety of industry leading tools as well as gaining experience with most database platforms. We are concentrating on Internet enabled business information systems in a wide range of industries.

Further, the following portions of annual report of the company for the FY 2006-07 do not indicate any presence of software products.



PROFIT & LOSS ACCOUNT FOR THE YEAR ENDED
31.03.2007

Schedule	Year Ended	Year Ended
	31.03.2007	31.03.2006
	Amount Rs.	Amount Rs.
<u>INCOME</u>		
Earnings from Software Exports in Foreign currencies	35,477,523	21,761,611
Interest on Deposit with Banks (TDS 1,74,490 F.Y. 1,06,353)	770,376	463,270
Interest on Income Tax Refund	106,064	7,907
Turnover & Connectivity Subsidy	64,343	22,232,788
Profit on Sale of Investment (Net)	36,427,306	22,232,788
TOTAL		

EXPENDITURE:

“c. REVENUE RECOGNITION

Revenue from software development contracts is generally recognised on successful completion of the project or in case of specific contract the same is accounted as per the terms of contracts.”

“10 The Company is into software development and as such is in services sector hence, additional information regarding Quantitative details and other information as required under clause 4-C & 4-D is either Nil or not applicable to the company.””

21. The TPO rejected the assessee’s objections in the case of ADIPL as well. The relevant extract of the order dated 28.10.2010 passed by the TPO rejecting the assessee’s contentions is set out below:

“31. The assessee’s argument that this company is not functionally comparable was not found to be correct. The company provides state of the art technology solutions and services to organizations in different verticals like financial



services, insurance solutions, etc. Simply because the company does not have any operations in the telecommunication space does not make it non comparable with the assessee. TNMM as a method allows broad product comparability and significant functional comparability. In fact among all the methods TNMM is the method which allows more liberty in choosing the comparables in that significant product diversity and functional diversity is allowed under TNMM. TPO also verified R&D expenses as a percentage of sale of the company in Prowess database. It was found that the company has no expenditure on R&D activity during the year. The TPO also went into the income and expenditure statement in Prowess, no expenditure on account of R&D or product development activity is debited in the profit and loss account. Hence this company can be considered as a functionally comparable company for comparability analysis.”

22. The DRP *vide* its order dated 23.09.2011 in the case of ADIPL also rejected the assessee’s objection in regard to inclusion of Avani, solely by referring to the reply furnished by Avani to the notice issued under Section 133(6) of the Act. The relevant extract of the observations of the DRP in respect of the appellant’s objections reads as under:

“S.No.	Name of the company	Reasons given by TPO	Assessee's Comments	OP/TC (%)	Comments
**	**	**	**	**	**
2.	Avani Cimcon Technologies Ltd	This company does not develop any product.	Does not agree with TPO	50.29%	Company in reply u/s 133(6) stated that it is pure software development company. Assessee confronted with above information. Satisfies all other filters.”



23. The DRP's observations in the case of ALTIPL were also in similar terms as noted in the order dated 01.08.2011.

24. The assessee's objections regarding inclusion of Avani were also rejected by the Tribunal. The Tribunal held that 97% of the revenue of Avani was from software development, which was similar to the functions performed by the assessee. The relevant extract of the impugned order is set out below:

“11. The TPO held that the comparable is engaged in provision of software development services and clears all the filters. The Id. DRP agreed to observation of the TPO and found that the company has stated that it is dealing purely in software development. The Id. AR argued that the comparable is functionally different and there was no segmental data available for the revenue from the sale of software development services and the software products. We find that this was not allowed as a comparable for the similarly placed companies owing to high operating margins and different asset base with regard to Motorola Solutions India Pvt. Ltd. During the year with regard to the assessee, we find that the comparable has replied that they are into software development only. We find that 97% of the revenue of the comparable is from software development which is similar to the functions of the assessee who is also having a software development facility centre. Hence, the contention of the Id. AR that in the absence of segmental data, the Avani CT Ltd. is not a right comparable, cannot be accepted.”

25. The learned counsel for the assessee has assailed the impugned order on, essentially, two fronts. First, he submitted that the conclusion that Avani is functionally comparable to the assessee is *ex facie* erroneous. According to the learned counsel for the assessee, the Tribunal proceeded on the assumption that Avani is not a product company but is engaged in software development for its clients /



customers. He referred to the images taken from the website of Avani, which indicated to the contrary.

26. The learned counsel for the assessee also referred to the earlier decision of the Tribunal in *Infogain India (P.) Ltd. v. Deputy Commissioner of Income Tax, Circle 11(1), New Delhi: [2020] 116 taxmann.com 386 (Delhi – Trib.)*. However, the said decision was completely overlooked as is apparent from the plain reading of the orders dated 26.10.2010 and 28.10.2010 passed by the TPO in respect of ALTIPL and ADIPL respectively. The TPO had not accepted that Avani was functionally dissimilar to the appellant on the assumption that Avani is engaged in software development for its clients. In its order dated 26.10.2010 (in the case of ALTIPL), the TPO had referred to the profit and loss account of Avani and noted that it did not “indicate any presence of software products”. It had noted that the income of Avani for the financial year ended 31.03.2007 was ₹3,64,27,306/- which included earnings from software exports in foreign currency of ₹3,54,77,523/-. Accordingly, the TPO had concluded that 97% income of Avani was from software development and not from sale of software products.

27. It is clear from the profit and loss account of Avani that its entire income from operations was ₹3,54,77,523/-(which included income from its software products). In addition to this income, Avani had also earned interest on deposit with banks amounting to ₹7,70,376/-; subsidy of ₹1,06,064/-; and, profit on sale of investment of ₹64,343/-. Concededly, the Tribunal had not bifurcated Avani’s income, segment



wise. As noted, the TPO proceeded on the basis that no part of the income of Avani was from product export. However, this assumption is not supported by the information as available on the website of Avani. The information available on the website of Avani indicates that it does provide “plug and play solutions” and it has developed various products including products named “DXchange, CARMA, Content Management System, Business Rules Engine etc. The relevant extract from the said website is set out below:

“On-Demand Software Solutions for Travel Industry

In the dynamic and highly competitive environment of the Travel Industry, our plug n play solutions allow organizations to expand the direct distribution opportunities, control relationships, lower technology costs enhance marketing communication with customers and prospects. Our ready to deploy solutions offers the marketing and management team with real-time analytics and dashboards to better help compete in today cutthroat environment.

Our solutions cater to the IT needs of Travel Vendors/Providers, Destinations, Associations, Agents, Online Travel Portals, Aggregators and Consolidators.

Leveraging our 15 years of experience in software development and our domain expertise in the Travel Industry we offer customizable solutions like:

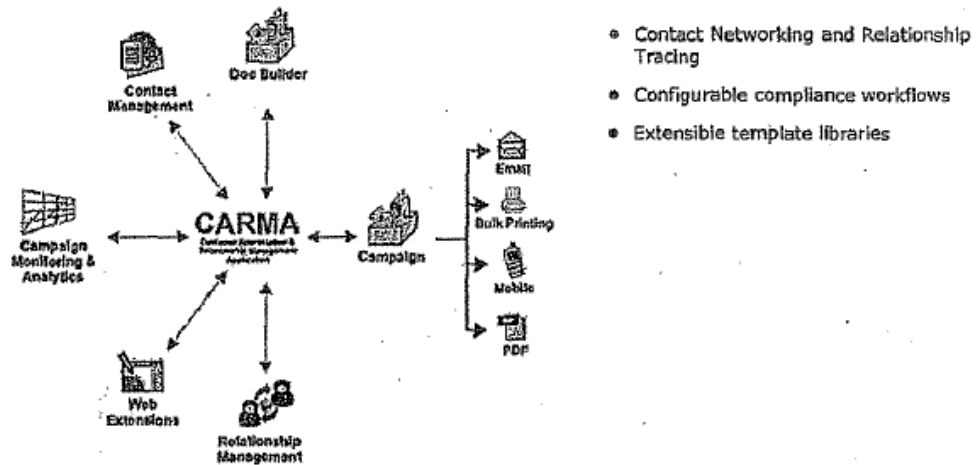
- DXchange – XML Web Services based OTA (Open Travel Alliance) compliant Middleware
- CARMA – Marketing Automation Sulte
- Content Management System
- Social Networking
- Business Rules Engine
- Booking Engine
- Inventory Management System/ eCRS

DXchange



DXchange is an OTA (Open Travel Alliance) compliant XML web services based Data Exchange Middleware Server. It is fully scalable and easily configurable. It provides travel organizations/Web Portals the ability to bundle XML requests to multiple suppliers in a single request, aggregate and consume XML or any form of online data from suppliers. For suppliers, DXchange enables them to expose their Inventory System /CRS as OTA compliant Web Services in a costs effective and secure manner giving them a wider reach. Additionally, it can support other standards with minimal customization.

DXchange is available in three versions: Lite, Professional and Enterprise. It is platform Independent and can connect to heterogeneous systems. It is hosted at the customer’s site and is sold as an annual license fees model, instead of transaction based fees / commissions model, DXchange is available on net and Java platforms.





With CARMA one can create template-based multilingual campaigns with repeated periodic scheduling. These can be sent off in the form of Email, Print (PDF, Bulk print). It is backed up by an ergonomic and well-organized content management system and a full-fledged compliance workflow. It also adds web presence for individual campaigns by adding web-extensions to the campaigns. To sum-up and analyze the outcome of these campaigns there is a powerful comprehensive reporting and analytics module that provides immediate feedback to measure success and improve future marketing initiatives.

Use of our solutions optimizes the effectiveness and cost-efficiency with which a company delivers critical messages to customers and prospects. These, reduces marketing costs, allows users to quickly and effectively identify and target most profitable customers and prospects; allows implementation of customers retention strategies, helps in building relationships and create linked business networks.

Content Management System

A multilingual capable System for Do-it-Yourself web and Social Networking portals

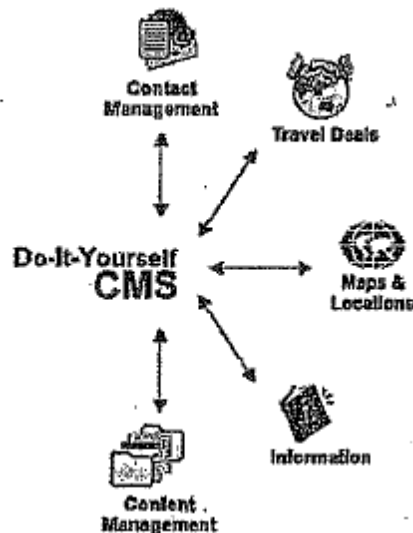
Avani Clmcon Technologies' Content Management System (CMS) is your chance to maintain your website and web content yourself, quickly and cost effectively. It works on the concept of "Do-It-Yourself", i.e., you can yourself create web content like images, text, document, web pages etc, store them for reuse, and Insert them on your website with no knowledge of HTML and without the help of webmasters or web developers. It is available in four versions:

- (a) CMS Lite
- (b) CMS Social Networking
- (c) CMS Travel Portal
- (d) CMS Destination Portal

- Create and Launch Travel Portals/Websites Easily
- Do-It-Yourself: Update, reuse web content as and when needed



- WYSIWYG site builder
- SEO friendly: Crates Search Engine Optimized pages
- Easily submit your site to search engines
- Integration with Booking Engine and Dynamic Packaging
- Domain Specific content: Host the same content with minor modifications for multiple domains
- Newer business modules, RSS etc., can be easily integrated
- Content management allows sharing of content between multiple applications like marketing automation suite
- Linked contract management for storing of site visitors and their information and preferences for marketing campaign.



CMS Lite

CMS Lite is an ideal, out of the box content management solution specially packaged for small companies and professionals who want a presence on the Web and would want to update the content themselves.

CMS Social Networking

Out of the box social networking solution allows implementation of current consumer trends like blog, broadcast, forums, and other means of sharing information.

CMS Travel Portal



It is totally customizable solution for small to large enterprises/portals to launch their web sites as quickly and as cost efficiently as possible. An ideal implementation of this system would be the front-end system to a booking engine. The CMS can be used to update marketing content on a day-to-day or a weekly basis.

CMS Destination Portal

It is a templated solution which allows you to manage your destination content with rich media. It has built-in modules to display complete information about the destination allowing the users to have a more complete view of what destination is, what are the destination's values, easily find places to stay, what to do, what activities are there, property-wise web pages, brochures, tickets and loads of information modules about the destination. It provides a complete travel experience to the users and allows them to navigate and book their entire travel package with the travel products available with for sell, like airlines, hotels, vehicles, restaurants and excursions.

Having a continuously updated website is a mandatory requirement to survive and grow in the dynamic highly competitive environment of the travel industry. But at the same time keeping content continuously updated is expensive and time consuming. CMS not only facilitates content management, but also gives you independent and full control of your website right from the simple ones to the most complicated.

Booking Engine

Avani Cimcon Technologies offers a complete XML web services based booking engine for Hotels, Vehicles, Restaurants, Airlines and Excursions. It is easy to use, highly scalable and flexible. It can be easily integrated with the website/CMS. It can be integrated with multiple inventory systems through our middleware server DXchange. It can also access inventory of other vendors along with your own inventory and shows aggregated results. It allows multiple currencies and enables users to select and pay in their currency. Rules can be applied on the fly so as to be able to offer variable pricing and incentives to the customers. It allows doing availability search, aggregation and booking of travel products offered by the provides.

Salient Features



- Web based booking engine running off XML
- All elements and pages are customizable to the needs of the customer
- White label sites available
- Provision for display in multiple currencies with base currency
- Allows all currency changes
- Allows rules on the fly so as to be able to offer variable pricing and incentives to the customer
- Can add on editable content pages
- Integration with Website
- Can access inventory of other vendors along with own inventory and show aggregated results. This is in case the vendors have their own system
- Customer registration and management system. Allows capture of customer information which can be used for loyalty programs and incentives
- Over and above the booking engine solution we can have amenities/ facilities / specialty services section in the booking engine. This section would be useful for customers asking for special facilities and services

Business Rules Engine

Business rules engine is a web-based, easy to use application with customizable GUI. This can be integrated with the DXchange server as an add-on. This would provide you with the flexibility to provide data to consumers in accordance with the travel industry's ever-changing business requirements without any programming or code changes. This provides an ability to visually manage and control the flow of information flowing to the customer and the agility to insert complex pricing and markup strategies.”

28. Avani's website clearly indicated that one of its products DXchange is available in three versions. The software is to be hosted on the customers' site and its revenue model is the annual licence fee model. Avani's Content Management System is also available in four



separate versions. The TPO had disregarded the information available on the website of Avani on the assumption that Avani's response was to the contrary. The TPO had reasoned that the information available on the website may not be relevant to the financial year 2006-07 and may contain forward looking statements but Avani's response to the notice under Section 133(6) of the Act was unambiguous.

29. Avani in its response to the notice under Section 133(6) of the Act had stated that it was a "Pure Software Development Service Provider". However, this statement cannot be construed to mean that Avani does not sell software products developed by it. The point is not whether Avani is a software development company but whether it develops customised software for each of its companies or sells/licences software, products, developed by it, to its customers.

30. The response of Avani to the notice under Section 133(6) of the Act is not available on record. However, the relevant extract of the same has been quoted in the order dated 26.10.2010.

31. It is also clear that no specific explanation was sought from Avani regarding the products mentioned on its website. The TPO proceeded only on the basis that the same may not be relevant without ascertaining whether the products as mentioned by Avani on its website were, in fact, sold /licensed during the financial year 2006-07.

32. The DRP also proceeded on the same basis without specifically addressing the appellant's objections in this regard.



33. In *Infogain India (P) Ltd. v. Deputy Commissioner of Income Tax, Circle 11(1), New Delhi* (*supra*), the Tribunal had considered a similar objection based on the assertion that Avani was also engaged in selling software products and its final accounts did not separately reflect the revenues from the said segment. The relevant extract of the said decision is set out below:

“Avani Cimcon Technologies Ltd.

54. The Annual Report of this company shows that this company derives revenue from both software development services and sale of software products [D Exchange] without any segmental details which makes this company functionally dissimilar. For similar reasons, the co-ordinate bench in the case of *Global Logic India (P) Ltd. (supra)* has excluded this company from the final set of comparables. The relevant findings read as under:

“9. The TPO observed on page 89 of his order that this company is also a software development and consulting company. In his opinion, all the filters applied by him were fulfilled and, as such, this company was liable to be considered as comparable. The assessee objected to the inclusion of this company before the DRP by contending that not only the turnover of this company was much lower, but also the profits were extremely high. Rejecting the assessee's contentions, the DRP upheld the TPO's view on the inclusion of this company in the final set of comparables.

10. It can be seen from the Annual accounts of this company, a copy of which is available on record, that albeit it is a pure software development service provider, but, is utilizing its own softwares in rendering such services. The Tribunal in *Motorola Solutions India Pvt. Ltd.*, has held this company to be incomparable by accepting the assessee's contention



that the high operating margins of this company were on account of difference in its asset base. It is further relevant to note that this company, apart from rendering software development services, is also engaged into the sale of software products and the accounts maintained by it are on entity level without there being any segregation for software development segment. As the TPO has considered the entity level figures of this company for making a comparison with the assessee company, such a course of action cannot be permitted because of the inclusion of profit from sale of software products into the overall profitability of this company. Neither separate profits are available, nor there is any measure provided for segregating profit on sale of software products from the overall profit of this company for finding out a comparable segment similar with that of the assessee company. As the profits of the software development portion cannot be ascertained, we hold that it cannot be considered as comparable on entity level. We, therefore, order for the exclusion of this company from the final set of comparables.”

55. Respectfully following the same, we direct the Assessing Officer/TPO for exclusion of this company from the final set of comparables.”

34. As is apparent from the above, in its decision in ***Infogain India (P) Ltd. v. Deputy Commissioner of Income Tax, Circle 11(1), New Delhi*** (*supra*), the Tribunal had referred to its earlier decision in ***Global Logic India (P.) Ltd. v. Asstt. CIT: [2015] 56 taxmann.com 159/69 SOT 57 (URO) (Delhi - Trib.)*** as well.

35. In ***Softbrands India (P) Ltd. v. Deputy Commissioner of Income-tax, Circle 12(3), Bangalore: [2016] 73 taxmann.com 231 (Bangalore-Trib.)*** as well, the Tribunal had accepted similar contention



as advanced by the appellant in this case. The relevant extract of the said decision is set out below:

“(ii) Avani Cincom Ltd.

▪ The comparability of this company has been considered by the co-ordinate bench of this Tribunal in *Trilogy E-Business Software India (P.) Ltd. (supra)* wherein it was found that as far as this company is concerned, the plea of the assessee has been that this company is functionally different from the assessee. Based on the information available in the company's website, which reveals that this company has developed a software product by name 'DXchange', it was submitted that this company would have revenue from software product sales apart from rendering of software services and therefore is functionally different from the assessee. It was further submitted that the Mumbai Bench of the Tribunal in the case of *Telcordia Technologies India (P.) Ltd. v. Asstt. CIT [2012] 22 taxmann.com 96/137 ITD 1* accepted the assessee's contention that this company has revenue from software product and observed that in the absence of segmental details, Avani Cincom cannot be considered as comparable to the assessee who was rendering software development services only. On careful consideration of the submissions made on behalf of the assessee it is viewed that the same deserves to be accepted. The reasons given by the assessee for excluding this company as comparable are found to be acceptable. The decision in the case of *Telcordia Technologies India (P.) Ltd. (supra)* also supports the plea of the assessee. Therefore, the plea of the assessee to reject this company as a comparable is accepted. Following the earlier orders of this Tribunal, the Assessing Officer/TPO is directed to exclude this company from the list of comparable for determining the ALR.

36. It is not denied that the Tribunal has also followed the same decision in other cases as well.

37. The decision in the case of *Infogain India (P) Ltd. v. Deputy Commissioner of Income Tax, Circle 11(1), New Delhi (supra)* was



cited before the Tribunal. However, it appears that the Tribunal has not considered the same.

38. It is also material to note that in *Infogain India (P) Ltd. v. Deputy Commissioner of Income Tax, Circle 11(1), New Delhi (supra)* the Tribunal had noted that the annual report of Avani shows that the company derives its revenue from both software development services and sale of software products. In view of the above, the TPO and the Tribunal, have erred in not excluding the Avani as a comparable entity for the purpose of determining the ALP.

ISHIR INFOTECH LTD.

39. The assessee objected to the inclusion of Ishir Infotech Ltd. (hereafter *Ishir*) as a comparable entity on two grounds. First, that it had failed the employee cost filter. The TPO issued a notice under Section 133(6) of the Act to the said company and based on the information received in response thereto, had determined that it not only qualified the 25% employee cost filter but other filters as well. The relevant extract of the TPO's order dated 26.10.2010 is set out below:

“14.4.12 Ishir Infotech Ltd

The company was not finding place in the accept/ reject matrix of the taxpayer. But, the company's data was available in the Capitaline database. Based on the data available in Capitaline database, the company failed 25% employee cost filter. Like all other cases, the companies which failed employee cost filter were also examined further. However, as the annual report and other information were not available for the FY 2006-07, notice U/s 133(6) was issued to the company to submit the information. As per the reply submitted by the company, it qualifies 25% employee cost filter and all other filters applied



by the TPO. Thus it is considered as a comparable. The same was communicated to the taxpayer vide this office show cause notice. In its response, taxpayer objected to it as under.

“6. Ishir Infotech Ltd ('Ishir')

Significant related party transaction: Referring to Part IV of the submission, wherein the Assessee has provided his argument on application of related party transaction filter to reject companies having controlled transaction in excess of 15% of revenue, the Assessee would like to submit that during the FY 2006-07, Ishir had transactions with its related parties to the extent of 22% of the total revenue. As such, the Assessee is not in agreement with selection of Ishir as an uncontrolled comparable company in respect of software development services provided by the Assessee.”

The taxpayer's main objection is that the company's related party transactions are more than 15% of revenues. As discussed above, the TPO applied 25% relate party transactions filter. As the RPTs are only to the extent of 22% of the revenues, the same satisfies 25% related party transactions filter applied by the TPO. Hence, the company is retained as a comparable as it is into software development services and qualifies all the filters applied by the TPO.”

40. It is also relevant to refer to the TPO’s order dated 28.10.2010 in the case of ADIPL. The relevant extract of the said order rejecting the appellant’s contention to not include Ishir as a comparable entity is reproduced below:

“45. Ishir Infotech Ltd.: The arguments putforth by the assessee are data contemporaneously not available and functionally not comparable. Regarding contemporaneous availability of data, already the TPO has given detailed submission.

46. The argument that the use of contemporaneous data should be resorted to is correct. The specified date itself is the due date of filing of return of income. The databases would have uploaded all the audited financial statements of the companies



within 31st October every year. The AGM has to be held within 6 months of closing of the financial year. Within 30 days of holding the AGM, the audited financial statements have to be filed before ROC. It is based on the audited financial statements submitted before the ROC, the databases upload the data. Hence the assessee can very well adhere to the Rule of contemporaneous data as prescribed by the Rules. The argument of the assessee may hold good in the earlier years of Transfer Pricing audit conducted by the assessee, since in the earlier years in many instances data was not available for the current year in the case of most of the comparables. Over the years the databases also have been more regular in uploading the data so that financial statements of all listed companies and some of the unlisted companies are available to the general public (people associated with the stock exchanges who use the data frequently and assessee's and TPO's who do TP audit).

47. The company provides application development, software development, product development, software testing etc. According to the web site of the assessee

48. Our software development and outsourcing services offer complete product life cycle solutions as an extension to our clients engineering team. We accelerate the creation of software products, reduce product marketing time and assist in making schedules more predictable. Considering these functions this company is taken to be a comparable company.”

41. It is the assessee's case that the business model followed by Ishir was largely outsourcing its activities and sub-contracting services. The assessee had also referred to the Tribunal's decision in the case of ***Infogain India (P) Ltd. v. Deputy Commissioner of Income Tax, Circle 11(1), New Delhi (supra)*** and submitted that in that case the Tribunal had accepted the objection in this regard. The relevant extract of the said decision is as under:

“Ishir Infotech Ltd.



58. The Annual Report of this company shows that this company is engaged in outsourcing work and is having heavy outsourcing activities as well as having different business model. The Hon'ble High Court of Delhi in the case of *Rampgreen Solutions (P.) Ltd. v. CIT* [2015] 60 taxmann.com 355/234 Taxman 573/377 ITR 533 has held that a company cannot be taken as a comparable which has a different business model. The relevant findings of the Hon'ble High Court read as under:

"38. In our view, even Vishal could not be considered as a comparable, as admittedly, its business model was completely different. Admittedly, Vishal's expenditure on employment cost during the relevant period was a small fraction of the proportionate cost incurred by the Assessee, apparently, for the reason that most of its work was outsourced to other vendors/service providers. The DRP and the Tribunal erred in brushing aside this vital difference by observing that outsourcing was common in ITeS industry and the same would not have a bearing on profitability. Plainly, a business model where services are rendered by employing own employees and using one's own infrastructure would have a different cost structure as compared to a business model where services are outsourced. There was no material for the Tribunal to conclude that the outsourcing of services by Vishal would have no bearing on the profitability of the said entity."

42. The impugned order does not clearly address the challenge raised by the appellant. The Tribunal accepted the contention that Ishir is a comparable entity as it does not fail the employee cost filter as per the annual report. The relevant extract of the impugned decision is as under:

"Ishir Infotech Ltd.



24. The assessee contended that the comparable fails the employee cost filter as per annual report. However, the information provided u/s 133(6) clears the employee filter.”

43. The question whether the business model is different and therefore Ishir would not be an appropriate comparable uncontrolled entity has not been considered by the Tribunal. As noted above, the decision in the case of *Infogain India (P) Ltd. v. Deputy Commissioner of Income Tax, Circle 11(1), New Delhi (supra)* was cited before the Tribunal but the same has not been alluded to by the Tribunal, as well.

44. In view of the above, the impugned order insofar as it rejects the appellant’s challenge to inclusion of Ishir as a comparable entity, is erroneous. In view of the above question no.(i) is answered in favour of the appellant and against the Revenue.

QUESTION NO.(II)

45. The next question to be addressed is whether the Tribunal had misdirected itself in not directing inclusion of M/s Akshay Software Technologies Ltd. (hereafter *Akshay*) as a comparable uncontrolled entity for determining the ALP.

46. It is the assessee’s case that Akshay is compliant with all the filters chosen by the TPO and the decision to exclude the same from consideration was unjustified. The TPO found that Akshay has more than 75% of its revenue from onsite services. The TPO issued a notice under Section 133(6) of the Act and called upon Akshay to submit its onsite revenue details. Apparently, the information submitted by Akshay indicated that it generated 100% of its export revenue from



onsite operations. The appellant objected to the onsite revenue criteria for selection or rejection of companies as comparables. It contended that any taxpayer engaged in software development services is bound to have offshore and onsite revenues. The composition of such revenues would vary from year to year. The appellant submitted that onshore and offshore revenues may yield different profit margins but the profit margin of an enterprise was required to be considered as a whole on the basis of functional similarity. It is the Revenue's case that the assessee had a consistent mark up on costs and therefore its profitability did not undergo any change on account of onsite and offshore mix of operations. In addition, the appellant also submitted that the mix of offshore and onsite revenues was available in the public domain. However, the TPO in the order dated 26.10.2010 rejected the said contention. Paragraph 9.9 of the said order, which sets out the reasons for rejecting the appellant's contentions is set out below:

“9.9 Onsite revenue Filter:-

The TPO has applied onsite revenue filter wherein the companies whose onsite revenues exceed 75% of export revenues are rejected as comparable. The TPO proposed to apply this filter in the show cause notice. In response, the taxpayer objected to this filter on the ground that the information of the off shore and on site income is not available in the public domain. The assessee has also objected to this filter on the ground that the software industry is a mix of onsite and offshore entities. The assessee claims that onsite work is part and parcel of the software industry and this distinction should not be made.

As discussed under the head “*industry overview of software services sector*”, the business dynamics of onsite and offshore varies a lot. For the sake of clarity, the relevant portion of “*industry overview of software services sector*” is summarized as under:-



- a) The Indian software sector provides both on-site and offshore services.
- b) The Indian vendors have succeeded in raising the share of offshore revenue from 44% in 2000-01 to 64% in 2003-04 and to 71 % in 2004-05.
- c) There is a substantial rate difference between the ON SITE and OFFSHORE projects/ contracts.

As per the industry reports (source: Annual report of Mphasis BFL FY 2004-05) in the year 2004-05 average rate per man hour in the case of offshore projects was US\$18, whereas the same was considerably higher in the case of ONSITE projects at about US\$66 per man hour. **The profit margins also accordingly vary significantly; the offshore projects have much higher margins.** 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. The Indian companies have therefore been slowly moving towards the OFFSHORE work more and more.”

47. The Tribunal rejected the appellant’s claim for including Akshay as a comparable entity on the ground that Akshay did not meet the revenue filter or the export turnover filter. The appellant states that the same is factually incorrect as Akshay does comply with the revenue filter as well as the export filter. This is because its export turnover to total sales was 79.23%, which was in excess of 25%. Further, its revenue for the financial year 2006-07 is ₹5.9 crores, which is greater than the revenue filter of ₹1 crore as applied by the TPO.

48. However, it is noticed that the appellant’s objection to the exclusion of Akshay was not on the ground of revenue filter but on account of onsite revenue filter as applied by the TPO. It is noticed that



the assessee's challenge to exclusion of Akshay before the Tribunal is also sketchy. No specific ground in this regard was taken. Copy of written submissions, which were filed before the Tribunal and placed on record also do not indicate that the said challenge was articulated. Notwithstanding the same, it does appear that the contentions regarding exclusion of Akshay were advanced before the Tribunal as the Tribunal has sought to deal with the same. However, there is an apparent error inasmuch as the appellant's basis for challenging the exclusion of the Akshay has not been considered by the Tribunal. Thus, the Tribunal's decision to exclude Akshay as a comparable entity, is unsustainable. In view of the above, it is apposite to remand the appeal to the Tribunal to consider the assessee's challenge to the exclusion of Akshay as a comparable.

QUESTION NO.(III)

49. The appellant had also objected to inclusion of Tata Elxsi Limited (hereafter *Tata*) and Sasken Communication Technologies Limited (hereafter *Sasken*) as comparable entities. According to appellant, its challenge to the inclusion of the said companies as comparable entities has not been adjudicated by the Tribunal. The appellant had also filed miscellaneous applications before the Tribunal praying that its challenge to inclusion of the said companies as comparable entities be adjudicated. It is relevant to refer to the appellant's challenge to inclusion of the said companies as set out in the miscellaneous applications filed by the appellant before the Tribunal. Paragraph 6 of both the applications (which are



similarly worded) filed by the assessee is relevant and is set out below:

“6. Non adjudication of the following grounds of appeal raised by the applicant:

6.1. Ground of appeal no. 1.9: including certain companies that are not comparable to Applicant in terms of functions performed, assets employed and risk assumed:

During the course of hearing, the Applicant contested exclusion of comparables and submitted detailed contentions against each of such companies in comparable chart filed on 13.01.2021 by email and relied upon during the course of hearing on 22nd March 2021 (Copy of comparable chart filed on 13.01.2021 is enclosed as **Annexure B**). Applicant also submitted written submission by email on 31.03.2021, as directed by Hon’ble Members at the time of hearing (Written submission filed by email on 31.03.2021 is enclosed as **Annexure C**) However, in the order, the Hon’ble Tribunal has inadvertently not adjudicated upon exclusion of two comparables, i.e. Tata Elxsi Limited (“Tata Elxsi”) and Sasken Communication Technologies Limited (“Sasken”) on account of functional dissimilarity.

6.2. Applicant’s contentions for exclusion of Tata and Sasken are provided in the ensuing paragraphs for ready reference

a. **Detailed contentions against inclusion of Tata Elxsi**

Applicant made submissions against inclusion of Tata Elxsi during the course of hearing and also filed contentions as part of written submission (Annexure C) and comparable chart (Annexure B):



- **Functionally non-comparable to the Applicant:** Applicant highlighted functional dissimilarity and drew attention to relevant pages of audited financials in written submission filed on 31.03.2021. Kindly refer page 8 of written submission where pg. 1084, 1086 and 1096 of Annual Report paperbook are highlighted to demonstrate that the company undertakes Embedded Product Design Services, (Design & Development of Hardware and Software). Industrial Design and Engineering (Mechanical Design with a focus on Industrial Design) and Animation and Visual Effects (Animation and Special Effects) under software development & services segment.
- **Company's involvement in R&D activities and development of software tools accepted by the Ld. TPO:** Applicant highlighted Tata Elxsi's involvement in R&D activities and development of software tools accepted by the Ld. TPO and drew attention to relevant pages of audited financials in written submission filed on 31.03.2021. Kindly refer page 9 of written submission filed before Hon'ble Tribunal wherein pg.1098 is highlighted along with pg. 1019 and 1126 of annual report wherein segmental details as provided in the annual report is mentioned. Further, on perusal of pages 129- 130 of appeal set, it may be noted that Ld. TPO has himself accepted that the company incurs in R&D activities which resulted in creation of IP.
- **Reliance on judicial precedents:** The Applicant has placed reliance on the decisions of Infogain India Pvt. Ltd. (ITA No. 5870/ Del/2011) (Kindly refer page 23-25, para 34-36) and Magma Design Automation India Pvt. Ltd (ITA No. 1214/Bang/2011) (Kindly refer page 12) which have been mention in SI. No. 24 of the comparable chart (Annexure B) and also



highlighted in written submission filed on 31.03.2021 (Annexure C):

The Hon'ble Tribunal while passing the order inadvertently did not adjudicate upon inclusion/exclusion of Tata Elxsi in the final set of comparable companies. To this extent there appears to be a mistake apparent from record which deserves to be corrected.

b. Detailed contentions against inclusion of Sasken Communication Technologies Limited

Applicant made submissions against inclusion of Sasken Communication Technologies Ltd. during course of hearing and also filed contentions as part of written submission (Annexure C) and comparable chart (Annexure B):

- **Functionally different:** Applicant highlighted functional dissimilarity in comparable chart as part of Applicant's contention. (Kindly refer SI. No. 22 of Annexure B) wherein it was highlighted that the company was engaged in diverse services including complex IC design, hardware design, board support packages and modem solutions, silicon platform services, handset technology services. network and test lab services etc.
- **Owns significant intangibles:** Applicant highlighted significant intangibles in comparable chart as part of Applicant's contention. Kindly refer SI. No.22 of Annexure B wherein Pg. 985 of Annual Report compilation is also highlighted. Kindly refer Pages 126-127 or appeal set wherein this aspect has been highlighted as part or DRP objections.
- **Extraordinary year of operations:** Applicant highlighted acquisition of 100% stake in Integrated Softtech Solutions Pvt. Ltd. and the said company was merged into Sasken. The second acquisition was that



of Botnia Hightech and its subsidiaries based in Finland in written submission (Pg. 8 of Annexure C) by highlighting 917 of Annual Report Paperbook, in comparable chart (SI. No. 22 of Annexure B), and also as part of DRP objections (Pg. 127 of Appeal set)

- **Reliance on judicial precedents:** The Applicant has placed reliance on the decisions of Infogain India Pvt. Ltd. (ITA No. 5870/Del/2011) (Kindly refer page 28-30, para 42-43) which have been mention in SI. No. 22 of the comparable chart (Annexure B) also highlighted in written submission filed on 31.03.2021 (Annexure C):
- The Hon'ble Tribunal while passing the order inadvertently did not adjudicate upon inclusion/exclusion of Sasken in the final set of comparable companies. To this extent there appears to be a mistake apparent from record which deserves to be corrected.
- In view of the above mistakes apparent on record, the Hon'ble Tribunal may kindly be pleased to appropriately modify the order in the interest of justice and to prevent inadvertent miscarriage of justice.”

50. Undisputedly, the contentions as set out above have not been adjudicated by the Tribunal.

51. The appellant had withdrawn its miscellaneous applications in view of the statement made before this Court on 01.02.2023. The learned counsel for the assessee contended that the said statement was made as the Revenue had objected to the appellant pursuing its remedies before this Court as well as by filing miscellaneous applications before the Tribunal.



52. In view of the above, the question no.(iii) is also decided in favour of the appellant and against the Revenue.

CONCLUSION

53. In the given facts, we set aside the impugned order to the limited extent of rejecting the appellant's challenge to inclusion of Avani Cincom Technologies Limited, Ishir Infotech Limited, Tata Elxsi Limited and Sasken Communication Technologies as comparables for the purpose of determining ALP and excluding Akshay Software Technologies Limited as comparable for the purpose of determining the ALP.

54. The matters are remanded back to the Tribunal for deciding afresh the appellant's objections in regard to inclusion and exclusion of Ishir Infotech Ltd, Tata Elxsi Limited, Sasken Communication Technologies Limited and Akshay Software Technologies Limited for determining the ALP adjustment, if any. It is clarified that all contentions of the parties on the merit whether the said companies are required to be included or excluded, are reserved.

55. The appeal is disposed of in the aforesaid terms.

VIBHU BAKHRU, J

SWARANA KANTA SHARMA, J

OCTOBER 14, 2024

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