

BEFORE SHRI R.S. SYAL, VICE PRESIDENT AND
SHRI PARTHA SARATHI CHAUDHURY, JUDICIAL MEMBER

ITA No.845/PUN/2017

ACIT, Circle-11, Pune	Vs.	Honeywell Automation India Limited, Survey No.56 & 57, Hadapsar Industrial Estate, Hadapsar, Pune 411 013 PAN : AA ACT3904F
Appellant		Respondent

Assessee by Shri Siddhesh Chaugule
Revenue by Shri Mahadevan A.M. Krishnan

Date of hearing	17-06-2021
Date of pronouncement	18-06-2021

આદેશ / ORDER

PER R.S.SYAL, VP :

This appeal by the Revenue is directed against the order passed by the Id. CIT(A) on 23-01-2017 deleting penalty of Rs.1,48,40,838/- imposed by the Assessing Officer (AO) by invoking Explanation 7 to section 271 (1)(c) of the Income-tax Act, 1961 (hereinafter referred to as 'the Act') in relation to the assessment year 2005-06.

2. Briefly, the facts of the case are that the assessee has been carrying the business in the automation and control industry.

Certain international transactions were reported in Form No.3CEB. On a reference made by the AO, the Transfer Pricing Officer (TPO) determined the Arm's Length Price (ALP) and accordingly proposed transfer pricing adjustment of Rs.36,47,76,500/-. The first appeal had the effect of reducing the transfer pricing adjustment to Rs.4,13,68,191/-. On the basis of the sustained amount of transfer pricing addition, the AO imposed penalty u/s.271(1)(c) of the Act amounting to Rs.1,48,40,838/-. The Id. CIT(A) deleted the same. The Revenue has come up in appeal against such deletion.

3. We have heard both the sides through Virtual Court and gone through the relevant material on record. The penalty has been imposed u/s 271(1)(c) with reference to Explanation 7, which reads as under :

Explanation 7.—Where in the case of an assessee who has entered into an international transaction or specified domestic transaction defined in section 92B, any amount is added or disallowed in computing the total income under sub-section (4) of section 92C, then, the amount so added or disallowed shall, for the purposes of clause (c) of this sub-section, be deemed to represent the income in respect of which particulars have been concealed or inaccurate particulars have been furnished, unless the assessee proves to the satisfaction of the Assessing Officer or the Commissioner (Appeals) or the Principal Commissioner or Commissioner that the price charged or paid in such transaction was computed in accordance with the provisions contained

in section 92C and in the manner prescribed under that section, in good faith and with due diligence.

4. On circumspection of the Explanation 7, it is manifested that every transfer pricing addition is deemed to represent concealed income etc. warranting imposition of penalty unless the assessee cumulatively satisfies the following three conditions, viz.,

- i) that the ALP was computed as per one of the prescribed methods u/s 92C;
- ii) such ALP determination was in the manner prescribed under the relevant rule; and
- iii) such ALP determination was done in good faith and with due diligence.

5. There is no dispute insofar as the first condition of the Explanation 7 is concerned inasmuch as the assessee computed the ALP in accordance with the provisions contained in Section 92C by applying the Transactional Net Margin Method (TNMM), which is one of the recognized methods. Thus the first condition is not violated.

6. There is also no quarrel that second condition is also not violated as the assessee determined the ALP in the manner prescribed under Rule 10B(1)(e) of the Income-tax Rules, 1962,

which provides mechanism for determining the ALP under the TNMM.

7. The third condition stipulates that the ALP determination should have been done by the assessee in good faith and with due diligence. Two expressions have been used herein: 'good faith' and 'due diligence', both of which have not been defined under the Act. Section 3(22) of the General Clauses Act, 1897 defines 'good faith' as: 'a thing shall be deemed to be done in "good faith" where it is in fact done honestly, whether it is done negligently or not'. As per this definition, the doing of an act honestly is a requisite condition of good faith. An act done honestly does not cease to be done in 'good faith', even if it was done negligently. The second expression used herein is 'due diligence', which is not defined even under the General Clauses Act. In the absence of its any specific definition, we revert to its connotation in common parlance. Ordinarily, the term 'diligence' means 'carefulness' and 'due' means 'adequate'. The expression 'due diligence', on a whole, means doing of a thing with adequate care. In one sense, 'diligence' is an antonym of 'negligence'. When we read both the expressions 'good faith' and 'due diligence' used in juxtaposition to each other in the provision, contextually, they would mean

determining the ALP honestly and with due care and not negligently.

8. Now we proceed to examine the basis of the transfer pricing addition made by the AO for ascertaining if the assessee's ALP computation lacked either good faith or due diligence or both so to warrant the imposition of penalty. In computing the 'Operating costs' base under the TNMM, the assessee treated Bad debts and Provision of bad debts as non-operating costs. The TPO albeit accepted the application of the TNMM as the most appropriate method along with the PLI, but treated Bad debts and Provision for bad debts as operating costs and further went on to exclude certain companies from the list of comparables by introducing a bad debt filter. While upholding bad debts as operating cost, the Tribunal approved the contention of the assessee for treating Provision for bad debts as non-operating as the same was *suo motu* disallowed by the assessee in the computation of its total income. The Tribunal also rejected the Departmental point of view of applying a bad debt filter for excluding certain companies from the list of comparables. On an overview of the above factual scenario, it is palpable that the stand of the assessee on the issues raised by the TPO in the ALP determination cannot be construed as lacking

either good faith or due diligence. It was a genuine difference of opinion between the assessee and the TPO, which got resolved by the Tribunal substantially in favour of the assessee. Thus it is overt that the assessee did not violate even the third condition.

9. In view of the foregoing discussion, we are satisfied that all three necessary ingredients for non-imposition of penalty in terms of Explanation 7 to section 271(1)(c) are satisfied in the extant case. We, therefore, accord our imprimatur to the impugned order deleting the penalty.

10. In the result, the appeal is dismissed.

Order pronounced in the Open Court on 18th June, 2021.

Sd/-
(**PARTHA SARATHI CHAUDHURY**)
JUDICIAL MEMBER

Sd/-
(**R.S.SYAL**)
VICE PRESIDENT

पुणे Pune; दिनांक Dated : 18th June , 2021
Satish

आदेश की प्रतिलिपि अग्रेषित/Copy of the Order is forwarded to:

1. अपीलार्थी / The Appellant;
2. प्रत्यर्थी / The Respondent;
3. The CIT(A)-13, Pune
4. The Pr.CIT-5, Pune
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, पुणे
“C” / DR ‘C’, ITAT, Pune
6. गार्ड फाईल / Guard file

आदेशानुसार/ BY ORDER,

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

		Date	
1.	Draft dictated on	17-06-2021	Sr.PS
2.	Draft placed before author	18-06-2021	Sr.PS
3.	Draft proposed & placed before the second member		JM
4.	Draft discussed/approved by Second Member.		JM
5.	Approved Draft comes to the Sr.PS/PS		Sr.PS
6.	Kept for pronouncement on		Sr.PS
7.	Date of uploading order		Sr.PS
8.	File sent to the Bench Clerk		Sr.PS
9.	Date on which file goes to the Head Clerk		
10.	Date on which file goes to the A.R.		
11.	Date of dispatch of Order.		

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