For all the above reasons, the writ petition is allowed and the impugned order is quashed.

Summary – The Delhi ITAT in a recent case of Halcrow Consulting India (P.) Ltd., (the Assessee) held that where assessee had obtained transfer pricing study from an outside expert and objectivity of same was not called into question, in such a case, even though certain adjustment was made to ALP, yet conditions precedent for invoking Explanation 7 to section 271(1)(c) did not exist

Facts

- The assessee company was engaged in providing planning, design and management services in the area of infrastructure consultancy. The return of income was filed declaring loss. The case was selected for scrutiny and reference was made to the Transfer Pricing Officer (TPO).
- The TPO proposed a disallowance in respect of international transactions undertaken by the assessee with respect to arm's length price of business support services. The disallowances were also made in respect of balance written off, advances written off and miscellaneous expenses. Subsequently, penalty proceedings under section 271(1)(c) were also initiated and penalty was imposed for furnishing inaccurate particulars leading to concealment of income.
- The Commissioner (Appeals) confirmed the penalty order.
- On second appeal:

Held

- As far as the penalty levied on transfer pricing adjustment is concerned, it is seen that during the year under consideration, the assessee had entered into following international transactions:-
    1. Provisions of technical services (receivables from Associated Enterprises)
    2. Availing of technical services (payable to Associated Enterprises)
- The assessee selected Cost Plus Method for both these transactions. Further, there was also apportionment of expenses towards business support services payable to the Associated Enterprises (AE), foreign currency component of salary of expatriate employees payable to the foreign AE and reimbursement of various expenses receivable from the AE. All these three were at cost. It was the assessee's view that no benchmarking was required in respect if these three transactions. However, during the transfer pricing proceedings, the TPO was of the view that while computing Profit Level Indicator (PLI) using Cost Plus Method, the assessee had claimed idle capacity adjustment of Rs. 2,46,46,065/- which was reduced from the direct cost was not to be included and, accordingly, the TPO excluded the same.
- The TPO also required the assessee to show cause as to why Cost Plus Method should not be rejected and TNMM should not be applied as the Most Appropriate Method. The TPO also asked the assessee to show cause as to why the intra group services payable to the assessee should not be

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treated as *nil* by applying CUP method. Thereafter, the TPO proceeded to make adjustment with respect to idle capacity amounting to Rs. 2,46,46,065/- and of Rs. 1,56,32,267/- with respect to intra group services by taking the ALP of intra group services at *nil*.

- It is seen that the Assessing Officer, while imposing the penalty, simply relied on the addition/adjustment made by the TPO and did not examine in detail as to whether penalty was imposable on such adjustments or not. On appeal, the Commissioner (Appeals) also noted that the assessee had not acted in good faith while computing the ALP. The Commissioner (Appeals) also took note of the fact that the assessee had not preferred any appeal against the ALP adjustment and, therefore, the assessee had accepted that the ALP had not been computed correctly by him and as such, the penalty was imposable.
- The main argument of the assessee against the levy of penalty on the difference in determination of ALP is that it is a debatable issue and, therefore, the penalty cannot be sustained. The scheme of *Explanation* 7 to section 271(1)(c) makes it clear that the onus on the assessee is only to show that the ALP was computed in accordance with the scheme of section 92C in good faith and due diligence. It is not in dispute here that the ALP was computed in accordance with the scheme of section 92C inasmuch as Cost Plus Method was used. The TPO only substituted Cost Plus Method with TNMM and also computed the ALP of intra group services by taking the ALP as *nil* by applying the CUP Method. Whatever may be the merits in the action of the TPO changing the method of computation of ALP, the same cannot be a fit case for imposition of penalty inasmuch as it cannot be said that the ALP had not been computed by the assessee under the scheme of section 92C.
- The scope of connotations of expressed 'in good faith' and appearing in *Explanation* 7 can be found from section 3(22) of the General Clauses Act which states that "a thing shall be deemed to be done in 'good faith' where it is in fact done honestly. Therefore, it is not even necessary whether in doing that thing the assessee has been negligent or not. Thus, there is no way that the assessee can prove his honesty, because honesty, in practical terms, only implies lack of dishonesty, and proving not being dishonest is essentially proving a negative, which as the Supreme Court has observed in the case of *K.P. Verghese* v. *ITO* [1981] 131 ITR 597/7 Taxman 13 is almost impossible. However, as the expression 'good faith' is used along with 'due diligence' which refers to 'proper care'. It is also essential that not only the action of the assessee should be in good faith but also with proper care. An act done with due diligence would mean the act done with as much as care as a prudent person would take in such circumstances.
- Thus, as long as no dishonesty is found in the conduct of the assessee, as long as he has done what a reasonable man would have done in his circumstances, to ensure that the ALP was determined in accordance with the scheme of section 92C, deeming fiction under *Explanation* 7 to section 271(1)(c) cannot be invoked.
- It is seen that the grounds on which the ALP determined by the assessee has been rejected are reasonably debatable. The assessee had obtained a transfer pricing study from an outside expert and the objectivity of the same was not called into question. Therefore, lack of due diligence in

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determining the ALP is neither indicated nor can be inferred. In such a situation, it cannot be concluded that the assessee had not determined the ALP in accordance with the scheme of section 92C in good faith and with due diligence and accordingly, the conditions precedent for invoking *Explanation* 7 to section 271(1)(c) did not exist on the facts of the instant case.

- If one accepts the contentions of the department that addition on account of transfer pricing adjustment invariably means absence of good faith and due diligence, then each and every case involving transfer pricing adjustment would call for imposition of penalty under section 271(1)(c) of the Act.
- Further, the High Court of Delhi has held in the case of *Pr. CIT* v *Verizon India Ltd.* [IT Appeal No. 4602 of 2016] that in absence of any overt act, which indicates conscious and material suppression, invocation of *Explanation* 7 in a blanket manner could not only be injurious to the assessee but ultimately would be contrary to the purpose for which it was engrafted in the statute. The High Court further observed that it might lead to a rather peculiar situation where the assessee who might otherwise accept such determination may be forced to litigate further to escape the clutches of *Explanation* 7. Therefore, in view of the factual Circumstances, it is opined that the assessee cannot be visited with penalty under section 271(1)(c) of the Act on this issue and accordingly, the impugned order is set aside and penalty is deleted.
- As far as the second ground on which the penalty has been imposed, it is seen that penalty has been imposed on disallowance of advances/balances written off and disallowance out of miscellaneous expenses. The Commissioner (Appeals) has confirmed the penalty on these additions on the ground that the assessee had accepted these additions and that the assessee did not furnish any evidence in support of the write off of advances. The penalty on miscellaneous expenses has been confirmed on the ground that some personal element in the expenditure could not be ruled out. However, it is clear that in the instant case it cannot be said that the assessee had withheld any relevant information regarding miscellaneous expenses or advances/balances written off. The assessee has duly disclosed these amounts in its profit/loss account and has also submitted details thereof during the assessment proceedings.
- The only reason the penalty was imposed was that the lower authorities did not accept the explanation of the assessee and imposed penalty for concealment of income. Thus, the *bona fides* of the assessee cannot be doubted in such circumstances. With regard to the provisions of section 271(1)(c) pertaining to penalty, the Apex Court has authoritatively laid down that making of a claim by the assessee which is not sustainable will not tantamount to furnishing of inaccurate particulars.
- Although both the lower authorities have held that the assessee has concealed particulars of income, on a consideration on the facts, such a view is not tenable is the present appeal. Therefore, the order of the Commissioner (Appeals) is set aside and the Assessing Officer is directed to delete the penalty.
- In the result, the appeal of the assessee is allowed.

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