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IN THE HIGH COURT OF DELHI AT NEW DELHI

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ITA 913/2016, CM APPL.46519/2016

PR. COMMISSIONER OF INCOME TAX-6 Appellant
Through: Mr. Rahul Chaudhary, Sr. Standing
Counsel.

Versus

MITSUI PRIME ADVANCED COMPOSITES INDIA PVT. LTD.
..... Respondent
Through: Mr. Mayank Nagi, Advocate.

CORAM:

HON'BLE MR. JUSTICE S. RAVINDRA BHAT

HON'BLE MR. JUSTICE NAJMI WAZIRI

ORDER

17.01.2017

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The Revenue argues that the Income Tax Appellate Authority's (ITAT's) order deleting the penalty imposed upon the assessee in the facts and circumstances of the case is untenable and urges this Court to frame the question of law.

The Assessing Officer ('AO') had - based upon the TPO's Arm's Length Price (ALP) determination - rejected the assessee's claim that the TNMM method was applicable and rather imposed the CUP method under Section 92CA of the Income Tax Act, 1961. The assessee did not appeal as apparently it had consistently incurred losses. The difference in method led to rejection of losses of about ₹3 Crores. The AO initiated penalty proceedings premised upon the

understanding that an adverse order under Section 92C attracted the 7th Explanation to Section 271(1)(C). After discussing the submissions he was of the opinion that the explanation offered by the assessee was not satisfactory and did not display good faith - a pre-requisite under the 7th Explanation. The ITAT discussed this by the impugned order in detail and *inter alia* held as follows: -

“11. To find an answer to this question, we need to briefly revisit the vital facts. The TPO has determined Nil ALP of the three international transactions by holding that the assessee did not avail any services for which the payment was made to its AEs as no benefit was shown to have been received, and, in any case, it was a case of duplication of services.

12. We do not find any force in the view point of the TPO that it was a case of duplication of services. It is for the reason that the assessee was incorporated in the Financial year 2007-08 and its Annual accounts for the year under consideration show that the manufacturing activity was undertaken for the first time during this year, as against the only trading activity in the preceding year. Manufacturing activity was undertaken as a consequence of the assessee entering into ‘Project consultancy and Business transfer agreement’ dated 1.8.2009 with GSC which is engaged in the business, inter alia, of manufacture and supply of poly propylene compounds and was hitherto an established supplier of poly propylene compounds to Maruti Suzuki India Ltd. Under this Agreement, the assessee acquired ‘Specified business’ and consultancy services from GSC for a consideration of Rs.3.14 crore. The ‘Specified business’ of GSC with Maruti Suzuki Ltd. was transferred to the assessee with all business activities, transactions, contracts, orders, inquiries and the consultancy services in relation to the transition of such business. In addition to that, GSC also

agreed to provide all technical information, know-how, data, formulae and knowledge relating to the products manufactured and sold to Maruti Suzuki, which stood transferred to the assessee by means of this Agreement. It appears that the TPO misdirected himself in evaluating the international transaction of payment of Rs.3.15 crore to GSC as a mere rendering of services alone in disregard to the fact that this payment was mainly for acquiring business of Maruti Suzuki Ltd. and receipt of technical know-how, etc. for the manufacture of desired products to be sold to Maruti Suzuki Ltd. A crucial factor which ought to have been considered by the AO was if such payment falls in capital or revenue field. Since the AO has imposed penalty by considering the transfer pricing adjustment made by the TPO on the premise of 'non-availing of services', which position is contrary to the actual factual matrix of having also received the entire business with Maruti Suzuki Ltd., for the stated consideration, we cannot improve the assessment order or the consequential penalty order to rope in another new reason for confirming the penalty. Fate of the penalty could have been different if a proper analysis of the Business transfer Agreement had been made by the authorities to ascertain if such payment of Rs.3.14 crore (out of total addition of Rs.3.31 crore) was a capital or a revenue expenditure. Back to our context, it is found that the assessee did receive business from GSC and technical know-how as a quid pro quo for the payment of Rs.3.14 crore.

13. The second transaction of availing Engineering support services was entered into pursuant to Agreement dated 1.10.2007 with its AE, a copy of which is available at page 551 to 568 of the paper book. This Agreement divulges that the assessee was planning to build a new plant and desired to receive certain engineering services through the employees of its AE. This demonstrates that whereas consideration of Rs.3.14 crore was mainly for acquiring 'Business' of supply of goods to Maruti Suzuki, for which it was to set up its own plant

and the second amount of Rs.13.03 lac was paid for availing the engineering services in installing such plant and machinery. The third international transaction is payment of a small amount of Rs.3.91 lac paid to AE for availing management support services. These services were received pursuant to an Agreement with Prime Polymer Co. Ltd., Japan, a copy of which is available at page 569 of the paper book. The services provided under such Agreement have been set out in clause 1.2, which states that the AE shall assist in business operations of the assessee and in market development in India apart from rendering engineering and technical support services in India. A brief description of the above Agreements amply shows that the assessee paid under these international transactions for acquiring the 'Business' of supply to Maruti Suzuki Ltd., and availing engineering services for setting up of plant required for manufacturing of the products to be supplied to Maruti Suzuki. Since no manufacturing activity was done by the assessee in past as it was simply a trader, acquiring of 'Business' and availing of the services under these three Agreements cannot be characterized as duplication of services."

The ITAT also held that to say that the assessee did not avail any services at all, is incorrect. The assessee had acquired business from GSC for supply of products as well as availing engineering services to set up a plant for manufacturing the designated products. This included manufacturing facility which resulted in sale of goods in the sum of ₹30.43 Crores which according to the ITAT indicated the benefit derived by it from payments under three international transactions. The ITAT also held that this was because the assessee not only acquired new business but also availed services to set up a plant, the details of which were disclosed to the TPO by a letter. This

according to the ITAT was sufficient elaboration of the nature of services availed of under the three international transactions which were improperly dealt with by the TPO and consequently the AO. The Tribunal thereafter took note of the decisions of the Punjab and Haryana High Court in *Knorr-Bremse India P. Ltd. vs. ACIT* (2016) 380 ITR 307 (P&H) and then observed as follows: -

“The only question is whether the transaction was entered into bona fide or not or whether it was sham and only for the purpose of diverting the profits. Reverting to the facts of the extant case, we have found out above that the three international transactions entered in to by the assessee with its AEs were not only genuine and bona fide but were also given effect to.”

The Revenue argues that the assessee was obliged to disclose the benefits and advantages they had derived from the services and also describe the nature of the services and that its failure resulted not only in rejection of TNMM method but also reduction of losses - which meant that the application of Section 271 (1) (c), 7th Explanation was warranted.

This Court has considered the submissions. As is evident, the ITAT's impugned order has elaborately dealt with the rationale in rejecting the AO's imposition of penalty. This Court is of the opinion that the view taken by the ITAT does not in any manner deviate against the 7th Explanation of Section 271 (1) (c). Furthermore, having regard to the fact that the assessee's claim was in respect of a new line of business of manufacturing, introduced for the first time in

the given year, its failure *per se* could not have triggered the automatic presumptive application of 7th Explanation of Section 271 (1) (c) as perceived by the revenue authorities in this regard.

Undoubtedly, the application of the exception has to be based upon the facts of each case and no generalisation can be made. Given this reality, the Court is satisfied that in the present instance, the ITAT did not commit any error of law. No substantial question of law arises. The appeal is consequently dismissed.

S. RAVINDRA BHAT, J.

NAJMI WAZIRI, J.

JANUARY 17, 2017
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