**IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "K" MUMBAI**

**BEFORE SHRI S. RIFAUR RAHMAN (ACCOUNTANT MEMBER)
AND
SHRI RAVISH SOOD (JUDICIAL MEMBER)**

**ITA No.3109/MUM/2019
(Assessment Year: 2013-14)**

Dy. Commissioner of Income-tax 5(1)(2), Room No. 568, 5th Floor, Aayakar Bhavan, M.K. Road, Mumbai – 400 020	Vs.	M/s Hari Krishna Exports Pvt. Ltd., 1701, B-Wing, The Capital Bandra Kurla Complex, Bandra (E), Mumbai - 400 051
PAN No. AACCH8430N		
(Revenue)		**(Assessee)**

Assessee by	:	Shri Nitesh Joshi, A.R
Revenue by	:	Shri Sunil Despande, D.R
Date of Hearing	:	28/05/2021
Date of pronouncement	:	25/06/2021

ORDER

PER RAVISH SOOD, J.M:

The present appeal filed by the revenue is directed against the order passed by the CIT(A)-56, Mumbai, dated 14.03.2019, which in turn arises from the order passed by the Dy. CIT, Transfer Pricing-2(2)(2), Mumbai (for short "TPO") u/s 271G of the Income Tax Act, 1961 (for short 'Act'), dated 28.04.2017 for A.Y. 2013-14. The revenue has assailed the impugned order on the following effective grounds of appeal before us:

"(1) Whether on the facts and in circumstances of the case the Ld. CIT(A) was correct in deleting the penalty levied u/s. 271G of the Act, by holding that the assessee had made substantial compliance, failing to

note that under TNMM adopted by the assessee, the profit of the international transaction has to be furnished, whereas the assessee has only furnished the entity level margins which consists of overall profits on AE and significant non-AE transactions.

(2) Whether on the facts and in circumstances of the case the decision of the Ld. CIT(A) is not vitiated for the reason that the CIT(A) has not given any finding on how the assessee has complied with clause (d), (g), (h) and (m) of Rule 10D (1), that have been specifically invoked by the TPO.

(3) Whether on the facts and in circumstances of the case the Id. CIT(A) erred in holding that there was reasonable cause for non-compliance of sec.92D read with Rule 10D(1) without specifying the cause of such non-compliance or demonstrating how the same was reasonable.

(4) Whether on the facts and in circumstances of the case the Id. CIT(A) was correct in ignoring the ratio laid down in the decision of Hon'ble Bombay High Court in the case of M/s. Shatrunjay Diamonds (261 ITR 258) holding that the initial burden was cast upon the assessee?

(5) Whether on the facts and in circumstances of the case the Id. CIT(A) erred in deleting the penalty for the reason that non adjustment was made to the ALP, failing to note that by not producing the material documents necessary to determine the ALP under any of the prescribed methods u/s. 92 C (1) of the Act, the assessee effectively prevented the TPO to make any determination as recorded by the TPO in the order u/s. 92CA (3) of the Act."

2. Briefly stated, the assessee company is engaged in the business of manufacturing and export of cut and polished diamonds. Reference u/s 92CA(1) of the Act, dated 18.12.2015 was made in the course of the assessment proceedings to the Dy.CIT, Transfer Pricing -2(2)(2), Mumbai, for computing the Arm's Length Price (for short 'ALP') of the specified domestic transactions entered into by the assessee with its AE's during the year under consideration.

3. Notice u/s 92CA(2) along with a questionnaire was issued to the assessee on 17.02.2016, whereby it was directed to submit details/explanations to support the ALP of the specified domestic transactions as was computed in its audit report in Form 3CEB. Another notice u/s 92CA(2) along with a questionnaire was issued to the assessee on 10.08.2016, whereby it was once again called upon to submit details/explanations to support the ALP of its transactions

with its AEs. On a perusal of the Form 3CEB, it was observed by the TPO that the assessee during the year under consideration had entered into the following specified domestic transactions :

Sr. No.	Description of transaction	Name of the AE	Amount (in Rs.)	Method by taxpayer
1.	Purchase of Rough Diamonds	H.K. Diam B.V.B.A	4,058,366,764	TNMM
2.	Labour Charges paid for cutting and polishing rough diamonds	H.K. Diamonds Polishing LLP	214,304,481	TNMM
3.	Rent paid	Hari Krishna Leasing Private Ltd.	4,719,120	TNMM
4.	Remuneration	Savjibhai D. Dholakia Ghanshyambhai D. Dholakia Tulsibhai D. Dholkia Bharat A. Patel Naresh V. Lungaria Hasmukbhai T. Dholakia	27,600,000	TNMM
5.	Salary Paid	Rajesh Himmatbhai Dholakia Brijesh Tulsibhai Dholakia Pintu Tulsibhai Dholakia Dholakia Ankit Bharatbhai Patel	4,300,000	TNMM

Notices under Sec. 92D(3) r.w Rule 10D were issued by the TPO, and the assessee was directed to furnish certain specific information, as under :

Date	Particulars
02.08.2016	Notice u/s 92D(3) was issued by the TPO, wherein the assessee was directed to furnish all the information documents as were required to be kept and maintained as per Rule 10D(1)(a to m) r.w.s 92D in respect of its international transactions and specified domestic transaction as referred in Form No. 3CEB and its TP Review Report.
29.08.2016	Notice u/s 92D(3) was again issued to the assessee, wherein the assessee was directed, viz. (i) that the TNMM benchmarking be reworked out at segmental level considering operating profits at segmental level and that with AEs and parties mentioned u/s 40A(a)(b) of the Act; (ii) that in case the benchmarking as mentioned hereinabove could not be carried out then, to put forth an explanation that as to why TNMM method employed for the abovementioned transactions may not be rejected, and a fresh benchmarking be carried out as per any other method out of the methods prescribed under the Act; and (iii) that in case of certain inter unit transfers, if the benchmarking as per 10% mark up as per the excise rule was to be adopted, then, it has to be demonstrated that non-inter

	unit uncontrolled market comparable transactions mark up did also fit to that range as required in its case.
28.10.2016	Notice u/s 92D(3) was again issued by the TPO wherein it was pointed that after rejection of TNMM as MAM, the benchmarking process may alternatively be supported by segregating the transactions into AE & Non-AE segment, whereby the margins of the said respective segments were to be compared.

However, as the assessee did not submit the details in compliance to the aforesaid notice(s) that were issued by the TPO u/s 92D(3), therefore, a 'Show cause' notice (for short 'SCN'), dated 31.10.2016 was issued by him, wherein the assessee was called upon to explain as to why penalty u/s 271G may not be imposed on it. Thereafter, another notice u/s 271G was issued to the assessee on 26.04.2017. In reply, it was submitted by the assessee vide its letter dated 28.04.2017 that all the requisite documents/information required u/r 10D(1) of the Income tax Rules,1962 were submitted during the course of the transfer pricing proceedings. It was further submitted by the assessee that it had during the year under consideration only entered into specified domestic transactions and there were no international transactions. Apart from that, the assessee demonstrating the peculiar nature of its business submitted, that as it had a single operating segment comprising of processing of rough diamonds and selling of finished goods, thus, the results at entity level were considered for computing the ALP. Referring to the peculiar nature of its business, it was submitted by the assessee that benchmarking of its transactions with the AEs as against independent comparable transactions under CUP and CPM was not possible. It was the claim of the assessee that TNMM was the most appropriate method to benchmark its transactions of purchase of rough diamonds from its AEs, and the said method was followed by the industry at large. It was further submitted by the assessee that as its transactions

with its AEs were less than 25% of its total transaction, therefore, it had rightly adopted TNMM for benchmarking the specified domestic transactions. It was submitted by the assessee that as per the settled position of law where any other method such as CUP and CPM cannot be effectively applied then, TNMM would be the most appropriate method. Alternatively, the assessee on the basis of the record maintained furnished details of comparable transactions under CUP and CPM.

4. However, the TPO did not find favour with the adoption of TNMM by the assessee for benchmarking its specified domestic transactions. It was observed by the TPO that the assessee remained under an obligation to maintain documents giving various details about the international transactions, viz. nature and terms; FAR analysis; record of forecasts budgets etc.; documents explaining and justifying the selection of the most appropriate method considering the factors specified in Rule 10C; and also the documents related to uncontrolled transactions to establish comparability and ALP of th international transactions [or specified domestic transaction] by applying such most appropriate method. After referring at length to the relevant statutory provisions, it was observed by the TPO that the assessee had not kept and maintained the documents as mandated by Rule 10D. It was further observed by him that the assessee had not maintained proper documents to justify selection of CUP or TNMM as the most appropriate method. It was observed by the TPO that if TNMM was to be considered as the most appropriate method then, as per the mandate of Rule 10C(2)(d), the assessee should have considered the degree of comparability existing between the international transactions [or specified domestic transactions] and uncontrolled transaction, and should have maintained documents in this regard as per the mandate of Rule 10D(1)(i). Also, the TPO was of the view that if

TNMM was to be considered as the most appropriate method then, the assessee should have worked out the net profit margin realised from the international transactions [or specified domestic transactions] as per the mandate of Rule 10B(1)(e) and should have maintained a record of detailed workings in this regard as require by Rule 10(1)(j). It was further observed by him that as the assessee had claimed that TNMM was the most appropriate method for determination of the ALP of its specified domestic transactions, then, as per Rule 10B(1)(e) r.w. Rule 10D(1)(j) it was required to have filed the audited segmental profitability of the AE & non-AE segments in the course of the TP proceedings, so that the actual profits earned by the assessee from the specified domestic transactions could be ascertained. It was observed by the TPO that the assessee had failed to furnish the segmental profitability of its AE & non-AE segments, for the reason, that it was not possible to differentiate the profitability between its transactions with the AEs and those with the non-AEs. In the backdrop of the aforesaid facts, the TPO was of the view that the assessee by considering the entity level profitability for application of TNMM had violated the provisions of Rule 10D(1)(g) & (h) r.w Rule 10C(2)(d) r.w. 10B(1)(e) because each of the clause contemplated comparability between international transaction [or specified domestic transaction] and uncontrolled transaction. It was observed by the TPO that though the assessee had considered the profitability at entity level, however, it had failed to furnish the record of uncontrolled transactions as per Rule 10D(1)(g) and also, the record analysis as mandated by Rule 10D(1)(h). Also, he was of the view that the assessee by considering the profitability at entity level had failed to comply with the provisions of Rule 10C(2)(d) for selection of the most appropriate method, and thus, violated the requirements of Rule 10D(1)(i). It was further observed by him that as the assessee had not worked out the net

profit margin realised from its specified domestic transactions as per Rule 10B(1)(e), it had, thus, also violated the requirements of Rule 10D(1)(j).

5. Backed by his aforesaid deliberations, the TPO was of the view that as the assessee had not complied with the provisions of Rule 10D(1), and not furnished the documents before the TPO, therefore, it had rendered itself exigible for levy of penalty u/s 271G of the Act. As regards the claim of the assessee that it was not practically possible to provide the separate profitability for its transactions with AE & non-AE, the same was rejected by the TPO, for the reason, that the said contention clearly militated against the provision of Rule 10B(1)(e) that prescribed the manner for determination of net profit margin from the international transactions [or specified domestic transactions]. In fact, it was observed by the TPO that if there was a practical difficulty in working out the profit from international transaction [or specified domestic transaction], then TNMM should not have been considered as the most appropriate method at all. Being of the view, that having considered TNMM as the most appropriate method, the TPO was of the view that the assessee could not be allowed to change the manner of determination of ALP under TNMM as was prescribed under Rule 10B(1)(e). Also, the plea of the assessee that considering the peculiar nature of its trade it was practically not possible to provide separate profitability for transactions with AE & non-AE, the same was rejected by the TPO on the ground that every businessman while working out the sale price of any item would necessarily take into consideration the cost incurred by him for the same. Adverting to the business of the assessee, it was observed by the TPO that even if there was mixing of various diamonds during the manufacturing process, the assessee would still have the relevant cost details for the final output, which however, it had not produced. It was, thus, observed by the TPO that

the assessee by not maintaining or producing the requisite data as was called for by the TPO under rule 10D, had thus, intentionally prohibited the TPO from determining the ALP of its specified domestic transactions. Observing, that the assessee had clearly violated the lawful requirement U/rule 10D r.w.s 92D to maintain as well as to produce documents as called for by him in the course of the transfer pricing proceedings, the TPO imposed penalty on the assessee u/s 271G of the Act i.e @ 2% of its specified domestic transactions of Rs.405,83,66,764/-, which therein worked out at an amount of Rs.8,11,67,335/-.

6. Aggrieved, the assessee carried the matter in appeal before the CIT(A). After deliberating on the contentions advanced by the assessee, the CIT(A) found favour with the same for two fold reasons, viz. (i) as at the time of initiation of the penalty proceedings u/s 271G i.e on 31.10.2016 the statutory time period of 30 days for furnishing the requisite information contemplated in Sec. 92D(3) had yet not expired, thus, no penalty under the aforesaid statutory provision could have validly been imposed; and (ii) on merits, it was observed that as the assessee could not have possibly complied with the obligations for which it had been subjected to penalty u/s 271G was squarely covered by the order passed by the Tribunal in the case of certain other assesses belonging to the trade line of the assessee in , viz. ITA No. 6303-6304/M/2016, ITA No. 6293/Mum/2016 and ITA No. 6310/Mum/2016. Backed by his aforesaid observations, the CIT(A) vide his order dated 14.03.2019 vacated the penalty imposed by the TPO u/s 271G and allowed the assessee's appeal.

7. The revenue being aggrieved with the order of the CIT(A) has carried the matter in appeal before us. The ld. Departmental Representative (for short 'D.R') relied on the order of A.O vide which

penalty was imposed on the assessee u/s 271G of the Act. It was submitted by the ld. D.R that as the assessee had failed in its statutory obligation to maintain or furnish the requisite information as per the mandate of Sec. 92D r.w. Rule 10D, therefore, the TPO had rightly imposed penalty u/s 271G of the Act. It was submitted by the ld. D.R that as the CIT(A) had wrongly vacated the penalty imposed by the TPO u/s 271G, therefore, his order be set aside and that of the A.O be restored.

8. Per contra, the ld. Authorized Representative (for short 'A.R') for the assessee relied on the order of the CIT(A). It was submitted by the ld. A.R that the ITAT, 'K' bench, Mumbai in the case of ACIT-5(1)(2), Mumbai, Vs. M/s D. Navinchandra Exports Pvt. ltd., Mumbai, ITA No. 6304/Mum/2016 had concluded that no penalty u/s 271G could validly be imposed in the case of an assessee engaged in the business of manufacturing and export of cut & polished diamonds. It was, thus, submitted by the ld. A.R that the issue herein involved was squarely covered by the order of the ITAT, 'K' bench, Mumbai, in the case of ACIT-5(1)(2), Mumbai, Vs. M/s D. Navinchandra Exports Pvt. ltd., Mumbai, ITA No. 6304/Mum/2016. It was submitted by the ld. A.R that the Tribunal in its aforesaid order had after exhaustively deliberating on the peculiar nature of the business of manufacturing and trading of diamonds, had upheld the order of the CIT(A) who had vacated the penalty that was imposed by the A.O u/s 271G of the Act. It was submitted by the ld. A.R that the aforesaid order of the Tribunal in the case of D. Navinchandra Exports Pvt. Ltd. (supra) had been upheld by the Hon'ble High Court of Gujarat in CIT (Central), Surat Vs. D Navinchandra Exports Pvt. Ltd., Tax appeal No. 788 of 2018, dated 09.07.2018. Apart from that, the ld. A.R also relied on the following judicial pronouncements to drive home his claim that no penalty u/s 271G could validly be imposed in case of an assessee who

was engaged in the business of manufacturing and trading of diamonds:

(i) Dilipkumar V. Lakhi. ITAT, Mumbai, IT(TP)A No. 2142/Mum/2017; dated 14.06.2018.

(ii) Interjewel Pvt. ltd. and Three Others. ITAT, Mumbai, ITA No. 5626 – 5628/Mum/2016, dated 01.11.2018

(iii) Laxmi Diamond Pvt. Ltd. ITAT, Mumbai, ITA No. 2643/Mum/2017, dated 27.12.2018.

(iv) Ankit Gems Pvt. Ltd. ITAT, Mumbai, ITA No. 4840/Mum/2017, dated 15.04.2019.

(v) Arjav Diamond India Pvt. Ltd. ITAT, Mumbai, ITA No. 1569/Mum/2019, dated 25.11.2019.

(vi) Decent Dia Jewels Pvt. Ltd. ITAT, Mumbai, IT(TP)A No. 2608/Mum/2017, dated 13.03.2020.

In the backdrop of his aforesaid contentions it was submitted by the ld. A.R that as the CIT(A) had rightly vacated the penalty imposed by the TPO under Sec. 271G of the Act, therefore, the appeal filed by the revenue being devoid and bereft of any merit did not merit acceptance and was liable to be dismissed.

9. We have heard the authorized representatives for both the parties, perused the orders of the lower authorities and the material available on record, as well as the judicial pronouncements that have been pressed into service by them to drive home their respective contentions. As observed by us hereinabove, penalty u/s 271G was imposed on the assessee, for the reason, that it had failed to maintain or produce documents and information prescribed U/rule 10D, as and when the same was called for by the TPO u/s 92D(3) of the Act. As observed by us at length hereinabove, the assessee had selected TNMM on an entity level as the most appropriate method for benchmarking the specified domestic transactions that were entered

into with its AEs during the year under consideration. Observing, that the assessee had failed to submit segmental accounts of profitability for its AE & non-AE transactions, the TPO was of the view that the non-furnishing of the said information had thwarted the department from evaluating the correctness of the ALP of the said specified domestic transactions. It was observed by the TPO that the assessee had wrongly benchmarked the transactions using TNMM at an entity level, for the reason, that the same had given the combined profits of the transactions of the assessee with its AEs and non-AEs. It was observed by the TPO that as the assessee was adopting TNMM as the most appropriate method as per Sec. 92C, therefore, it was obligated to determine the net profit margin of its specified domestic transactions with the AEs for determining the ALP of the said transactions u/s 92C as per rule 10B(1)(e). As observed by us hereinabove, the TPO noticed that the assessee had not maintained and also not furnished the documentation from which the profit margin of the AEs could be determined. It was further observed by him that the qualitative details of the AEs and Non-AEs transactions have also been maintained by the assessee, as a result whereof the CUP method could not be applied. On the basis of his aforesaid observations, we find that the TPO had concluded that the assessee had failed to keep and maintain the documents as were mandated by Rule 10D of the Income Tax Rules, 1962. As observed by us at length hereinabove, it was in the backdrop of his aforesaid deliberations, that the TPO being of the view that the assessee had not complied with the provision of Rule 10D(1) r.w.s 92D to maintain as well as produce the requisite information and documents as were called for by him in the course of the transfer pricing proceedings, thus, had saddled it with penalty u/s 271G of the Act.

10. As is discernible from the order of the CIT(A), we find that he had inter alia vacated the penalty imposed by the TPO u/s 271G of the Act, for the reason, that the same was initiated before the lapse of a period of 30 days, which he was of the view were statutorily to be provided to the assessee to furnish the requisite information as per the mandate of Sec. 92D(3). We have given a thoughtful consideration to the aforesaid observation of the TPO and are unable to persuade ourselves to subscribe to the same. On a perusal of Sec. 92D(3), as was then available on the statute, we find, that the same read as under:

> "92D. Maintenance and keeping of information and document by persons entering into an international transaction or specified domestic transaction.— (1) Every person who has entered into an international transaction or specified domestic transaction shall keep and maintain such information and document in respect thereof, as may be prescribed :
>
> **Provided** that the person, being a constituent entity of an international group, shall also keep and maintain such information and document in respect of an international group as may be prescribed.
>
> Explanation.—For the purposes of this section,—
>
> (A) "constituent entity" shall have the meaning assigned to it in clause (d) of sub-section (9) of section 286;
>
> (B) "international group" shall have the meaning assigned to it in clause (g) of subsection (9) of section 286.
>
> **(3) The Assessing Officer or the Commissioner (Appeals) may, in the course of any proceeding under this Act, <u>require any person</u> who has entered into an international transaction or specified domestic transaction <u>to furnish any information or document</u> in respect thereof, as may be prescribed under sub-section (1), <u>within a period of thirty days from the date of receipt of a notice issued in this regard</u>:**
>
> **Provided that the Assessing Officer or the Commissioner (Appeals) may, on an application made by such person, extend the period of thirty days by a further period not exceeding thirty days."**
>
> (emphasis supplied by us)

On a perusal of the aforesaid statutory provision, we find, that the same therein contemplates that the A.O or CIT(A), in the course of any

proceeding under the Act, require any person who had entered into an international transaction or specified domestic transaction to furnish any information or documents in respect thereof, as may be prescribed under sub-section (1), within a period of 30 days from the date of receipt of a notice issued in this regard. As per the 'proviso' to sub-section (3) of Sec. 92D, on an application made by the assessee, the aforementioned period of thirty days may be extended by a further period not exceeding thirty days. In our considered view, as per Sec. 92D(3) an assessee may be called upon to furnish the requisite information or documents as prescribed in sub-section (1) of Sec. 92D, within a period of 30 days from the date of receipt of the notice. Now, in the case before us, the TPO vide his notice u/s 92D(3), dated 02.08.2016 had called upon the assessee to furnish the requisite information/documents within a period of 15 days. Another notice u/s 92D(3) r.w Rule 10D, dated 29.08.2016 was issued by the TPO, wherein the assessee was called upon to furnish certain documents/information by 07.09.2016. Further, the TPO u/s 92D(3) r.w. Rule 10D, dated 28.10.2016 had directed the assessee to produce supporting documents in order to justify its claim that the segmentation of AEs & non-AEs was verifiable, by 30.10.2016. In the backdrop of the aforesaid facts, we find that it is a matter of fact borne from the records that the last date for filing of the documents/information as were called for by the TPO lapsed on 30.10.2016. As such, the 'SCN' Dated 31.10.2016 was subsequent to the lapse of the time period that was allowed by the TPO for furnishing of the requisite information/documents by the assessee. We, thus, are of the considered view that the CIT(A) had misconceived the factual position, and observed, that as the time period allowed to the assessee for furnishing of the requisite details as were called for by the TPO u/s 92D(3) had not expired on the date on which the SCN u/s 271G was

issued i.e on 31.10.2016, therefore, the penalty could not have been validly imposed. In our considered view, as the SCN, dated 31.10.2016 was issued by the TPO after the lapse of the time period that was allowed for furnishing of the requisite information/documents that were called for by him vide his aforementioned notices issued u/s 92D(3), therefore, no infirmity does arise therefrom. We thus, not being able to concur with the aforesaid view so arrived at by the CIT(A) therein vacate the same.

11. We shall now advert to the merits of the case, on the basis of which it is averred by the ld. A.R that considering the peculiar nature of the assessee's business of manufacturing and export of cut & polished diamonds, no penalty u/s 271G could have validly been imposed. As observed by us hereinabove, it is the claim of the ld. A.R that the issue is squarely covered by the orders of the co-ordinate benches of the Tribunal wherein it has been held that no penalty u/s 271G considering the nature of the business of manufacturing and export of cut & polished diamonds could validly be imposed. As stated by the ld. A.R, and rightly so, the issue had been deliberated at length by the ITAT, Mumbai 'K' Mumbai in the case of ACIT-5(1)(2), Mumbai Vs. M/s D Navinchandra Exports Pvt. Ltd., ITA No. 6306/Mum/2016, dated 25.10.2017. In its aforesaid order, the Tribunal after exhaustively deliberating on the nature of the business of the assessee before them, viz. manufacturing of diamonds, had concluded that penalty u/s 271G could not have been imposed on the assessee, observing as under:

> "16. We have heard the ld. D.R and perused the orders of the lower authorities. We have given a thoughtful consideration to the facts involved in the case before us and are of the considered view that it remains as a matter of fact borne from the records that the TPO had imposed penalty under Sec. 271G for the reason that the assessee had failed to furnish the information as was called for by him. We find that the TPO held a conviction that the assessee had not only inappropriately applied the TNMM which patently suffered from serious irregularities, as the assessee had merely allocated the

expenses on the basis of sales, in the backdrop of which the working of the margins involved in the transactions of the assessee with its AEs and non-AEs did hardly witness any variance. We have deliberated on the orders of the lower authorities and find that the TPO in the course of the penalty proceedings was driven by the fact that the assessee by not providing the requisite details, had thus not only failed to substantiate the basis for comparing the transactions of the AE with another AE and/or non-AE, but had also failed to provide any other basis for benchmarking its international transactions with the AEs. We find that the TPO had in his penalty order observed that due to the failure of the assessee to provide requisite data/information as was called for by him in the course of the proceedings to facilitate correct benchmarking of the international transactions of the assessee with its AEs, he could not examine and determine the arms length price and had to accept it as reflected by the assessee in its TPSR. We find that the TPO in order to benchmark the international transactions of the assessee, had as a matter of fact required the assessee to furnish separate profit level indicator (PLI), either by furnishing the AE and non-AE segment wise Profit & loss account, and/or some other evidence to show that the international transactions aggregating to Rs. 107,99,26,354/- of the assessee with its AEs, viz. (i). Purchase of rough diamonds; (ii). Export of rough diamonds; (iii). Export of polished diamonds; and (v). Purchase of polished diamonds, were at arms length price.

17. We find that the TPO pursuant to the notice u/s 92CA(2) along with a questionnaire issued to the assessee had in order to verify as to whether the transactions entered into by the assessee with its AEs were at arms length with that entered into by the third party in comparable situation with independent parties, had therein called upon the assessee to submit documents mentioned as per Rule 10D(1) and 10D(3) of the Income tax Rules, 1962 along with other specific details, and further directed it to furnish the documents specified under Sec. 92D and Sec. 92E of the 'Act'. We find that the TPO after examining the details and documents available on record, had therein called upon the assessee to submit the segmental profitability for AE transactions and non-AE transactions. However, as the assessee had not maintained separate books of accounts for AE and non-AE segments, therefore, it expressed its inability to furnish the details in the manner the same were called for by the TPO. We find that the TPO in the absence of the segmental breakup of the AE and non-AE transactions, therein concluded that it was prevented from benchmarking various transactions, and for the said failure of the assessee to furnish the requisite details had initiated penalty proceedings under Sec. 271G in the hands of the assessee. We find that the TPO not finding favour with the explanation of the assessee that no penalty under Sec. 271G was liable to be imposed, therein proceeded with and imposed a penalty of Rs. 2,15,98,527/- i.e @2% of the aggregate value of the international transactions of Rs. 107,99,26,354/- in the hands of the assessee.

18. We find that the CIT(A) after deliberating at length on the nature of the business of manufacturing and trading of diamonds, therein concluded that in the backdrop of the intricacies involved in the said business it was practically difficult for the assessee to furnish the information in the manner the same was called for by the TPO. We find that the CIT(A) in the backdrop of an indepth study of the nature of activities involved in the business of manufacturing and trading of diamonds, had in a very well reasoned manner

culled out the peculiar nature of the trade of the assessee. We are of the considered view that a careful perusal of the very nature of the business of manufacturing and trading of diamonds therein glaringly reveals that certain information which was called for by the TPO could not be furnished by the assessee. We find that the CIT(A) had observed that as the assessee had purchased a mix of imported rough and polished diamonds from AEs and non-AEs, and had also sold/exported rough and polished diamonds to AEs as well as the non-AEs, therefore, the Profit & loss a/c of the assessee reflected a mixture of purchases and sales both from the AEs and the non-AEs. We are persuaded to be in agreement with the view of the CIT(A) that now when the rough/polished diamonds were traded on lot wise basis, therefore, it was difficult to identify and say whether a polished diamond came out of a particular lot of rough diamonds or the other and/or out of the polished diamonds purchased locally by the assessee. We find that the export bills of the cut and polished diamonds exported to the AEs and the non-AEs revealed that the diamonds of varying size, quality, colour and carat weight were exported as was evident from the price per carat charged in each bill, and similar would have been the position in respect of cut and polished diamonds purchased and sold locally and/or purchased from abroad but sold locally. We are of the considered view that in the backdrop of the aforesaid peculiar nature of the trade of the assessee, it could safely or rather inescapably be concluded that it was extremely difficult to identify which rough diamond got converted into which polished diamond, unless the single piece rough diamond happened to be of exceptionally high carat value , therein making the tracing out and identification of the polished diamond physically possible and convenient. We find that the aforesaid practical difficulties in providing the details being faced by the industry can be well gathered from the letter of the GJEPC to the CIT-Transfer Pricing, Mumbai, wherein the aforesaid aspects involved in the diamond manufacturing business were explained.

19. We find that the assessee had in the backdrop of the very nature of its business, viz. manufacturing of diamonds, had though explained to the TPO the practical difficulty in furnishing segment wise Profit & loss account of the AE segment and the non-AE segment, however, the TPO insisted for the same and invoked Rule 10D of the Income-tax Rules, 1962, and instead of determining the arms length price in respect of the international transactions of the assessee with its AEs, rather went ahead and levied penalty under Sec. 271G in the hands of the assessee. We are not impressed with the manner in which the assessee had proceeded with the matter and imposed penalty under Sec. 271G in the hands of the assessee. We are of the considered view that in light of the aforesaid practical difficulties which were being faced by the diamond industry, the TPO should have exercised the viable option of determining the arms length price of the international transactions of the assessee, either by making some comparison of realisation of prices in respect of export sales to AEs and non-AEs by comparing prices of diamonds of similar size, quality and weight to the best extent possible, or in the alternative could have asked for the copies of the Profit & loss accounts and the Balance sheets of the AEs in order to make an overall comparison with the gross profitability levels of the assessee with its AEs, which would had clearly revealed diversion of profits, if any, by the assessee to its AEs. We are further unable to comprehend that as to on what basis the TPO expected the assessee to have carried out the benchmarking by following CUP method. We are of the considered view that as the

comparison by internal CUP method could only be made if two lots of diamonds were similar in size, colour, shape and clarity, which we are afraid, as observed by us at length hereinabove, in light of the peculiar nature of the trade of the assessee would not be possible. We find ourselves to be in agreement with the CIT(A) that if one lot had diamonds of variety of size, colour, shape and clarity, the prices would vary from diamond to diamond and lot to lot, and further, now when the entire lot of diamonds had a common price tag per carat for the whole lot, therefore, it was not possible to evaluate the price of each diamond. We also cannot be oblivious of the fact that even otherwise in the diamond trade line, unless a diamond would weigh half carat or more or one carat or more, the same would not be priced separately in the bill because it was not practical to price diamonds of weights of lower than half carat or one carat separately weight wise per diamond in the lot. We have deliberated on the aforesaid peculiar facts involved in the business of diamond trading and are of the considered view that the insistence of the TPO that the assessee should have followed CUP method was misconceived and impractical. We are in agreement with the CIT(A) that if the TPO would had carried out a comparison of the Profit & loss account and Balance Sheets of the AEs, the same would had revealed the gross profit margins and levels of profitability earned by the AEs in their businesses, and as such any abnormal variation in their gross profitability would had revealed the aberrations in the international transactions.

20. We further find that as stands gathered from the records, the nature and level of business of the assessee during the year under consideration had increased almost two fold. We find that while for the gross profits of the assessee had also increased from 7.42% for A.Y. 2010-11 to 8.71% for the year under consideration, viz. A.Y. 2011-12, the Net profit had also witnessed a growth from 3.9% in the immediate preceding year to 4.9% during the year under consideration. We further find that as observed by the CIT(A) that in the preceding year, i.e A.Y. 2010-11 the TPO did not propose any adjustment in the ALP. We are not inspired by the fault finding approach adopted by the TPO without understanding the intricacies of the diamond manufacture and trading business, and are of the considered view that he instead of determining the arms length price by asking for the Profit & loss a/c and Balance Sheets of the AEs and comparing the financial ratios in general, had rather hushed through the matter and imposed penalty under Sec. 271G of Rs. 2,15,98,527/- on the assessee. We also find that the assessee to the extent possible in the backdrop of the nature of its trade had furnished several details on several occasions from time to time with the TPO. We thus are of the considered view that the assessee had substantially complied with the directions of the TPO and placed on his record the requisite information, to the extent the same was practically possible in light of the very nature of its trade. We though are not oblivious of the fact that the assessee may not have effected absolute compliance to the directions of the TPO and furnished all the requisite details as were called for by him on account of practical difficulties as had been deliberated by us at length hereinabove, but however, in the backdrop of our aforesaid observations, we are of the considered view that the failure to the said extent on the part of the assessee to comply with the directions of the TPO can safely be held to be backed by a reasonable cause, which thus would bring the case of the assessee with the sweep of Sec. 273B of the 'Act'. We thus in the backdrop of our aforesaid observations find ourselves to be in agreement with the view taken by the CIT(A,) and finding no reason to dislodge his well reasoned

order, therefore, uphold the same. We thus uphold the order of the CIT(A) and the resultant deletion of the penalty of Rs. 2,15,98,527/- imposed by the TPO.

21. The appeal of the revenue is dismissed."

As observed by us hereinabove, the aforesaid order of the Tribunal had thereafter been approved by the Hon'ble High Court of Gujarat in CIT (Central), Surat Vs. M/s D. Naveen Chandra Exports Pvt. Ltd., Tax appeal No. 788 of 2018, dated 09.07.2018. We, thus, concurring with the aforesaid view taken by the Tribunal in its aforesaid order in the case of D. Navinchandra Exports Pvt. Ltd. (supra) which thereafter had been approved by the Hon'ble High Court of Gujarat, respectfully follow the same. Accordingly, we herein, in terms of our aforesaid observations uphold the order of the CIT(A) to the extent he had on merits vacated the penalty of Rs. 8,11,67,335/- imposed by the TPO u/s 271G of the Act.

12. Resultantly, the appeal filed by the revenue is dismissed in terms of our aforesaid observations.

Order pronounced in the open court on 25.06.2021

Sd/-	Sd/-
(S. Rifaur Rahman)	(Ravish Sood)
ACCOUNTANT MEMBER	JUDICIAL MEMBER

Mumbai;
Dated: 25.06.2021
PS: Rohit

Copy of the Order forwarded to :

1. The Appellant
2. The Respondent.
3. The CIT(A)-
4. CIT
5. DR, ITAT, Mumbai
6. Guard file.

BY ORDER,
//True Copy//

(Sr. Private Secretary)
ITAT, Mumbai