IN THE HIGH COURT OF JUDICATURE AT BOMBAY

ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.1753 OF 2018
AND
INCOME TAX APPEAL NO.1759 OF 2018
AND
INCOME TAX APPEAL NO.2780 OF 2018

Ashok Kumar Rungta

Red Wood 'A', Flat No.404,
Evershine Greens, Adhori Link road,
Adarsh Nagar, Oshiwara, Jogeshwari (West),
Mumbai- 400102 .... **Appellant**

Versus

1. Income Tax Officer 24(1)(1)

Pratyakshkar Bhavan, Bandra Kurla Complex,
Bandra (East), Mumbai-400051

2. Commissioner of Income Tax-30, Mumbai

3. Union of India

Through Ministry of Law
Aaykar Bhavan, M.K. Road,
Mumbai-400020 .... **Respondents**

Mr. N.M. Porwal, *Advocate for the Appellant.*
***Ms. Swapna Gokhale**, Advocate for the Respondents.*

CORAM : G. S. KULKARNI &
SOMASEKHAR SUNDARESAN, JJ.

RESERVED ON : SEPTEMBER 26, 2024

PRONOUNCED ON : OCTOBER 15, 2024

Judgment (*Per. Somasekhar Sundaresan J*):

1. This batch of Appeals challenge an Order and Judgment of the Income Tax Appellate Tribunal (***"ITAT"***) dated August 9, 2017 (***"Impugned Order"***) upholding an Order dated April 27, 2015 passed by the Commissioner of Income Tax - Appeal (***"CIT-A"***), disallowing 10% of certain suspect purchases on the premise that they are bogus purchases. Originally, the Assessing Officer had passed an order dated March 21, 2014 ("***AO Order***") on reassessment of returns for three Assessment Years, disallowing all the expenses incurred towards purchase from certain entities, and thereby adding such expenses to the income of the Appellant-Assessee.

2. Income Tax Appeal No.1753 of 2018 relates to Assessment Year 2009-10; Income Tax Appeal No.2780 of 2018 relates to Assessment Year 2010-11; and Income Tax Appeal No.1759 of 2018 relates to Assessment Year 2011-12.

3. The questions of law raised by the Appellant-Assessee are manifold. Mr. N.M. Porwal, Learned Counsel appearing on behalf of the Appellant-Assessee submitted that he would only be pressing four out of the seven questions raised in these Appeals. However, at the heart of these questions, lies a single issue, namely, whether the ITAT

was right in upholding the findings of the CIT-A, by disallowing 10% of the total purchases alleged to have been bogus, and adding such sum to the income of the Appellant-Assessee for the relevant Assessment Years.

4. The Appellant-Assessee wants this Court to hold that all the purchases were genuine and must be allowed as legitimate expenses. The Respondent-Revenue had wanted this Court to hold that all the expenses ought to have been treated as bogus and that the ITAT was wrong in disallowing only 10% of such expenses. It is a matter of record that Income Tax Appeal No. 1349 of 2018, filed by the Revenue against the very same Impugned Order, was not entertained by a Division Bench of this Court by an order dated April 24, 2024.

5. The grievances of the Revenue being different from the grievances of the Assessee, the dismissal of the Revenue's appeal is not conclusively determinative of the status of the Assessee's grievances. We have heard the parties at length with this specific perspective in mind.

6. We are conscious that our jurisdiction relates to answering substantial questions of law. Having heard Mr. N.M. Porwal, Learned Counsel on behalf of the Appellant-Assessee and Ms. Swapna Gokhale, Learned Counsel on behalf of the Respondent-Revenue, we find that the

ITAT had been faced with cross appeals from the decision of the CIT-A. The Assessee had been aggrieved by 10% of his purchases being disallowed while the Revenue was aggrieved by only 10% the purchases being disallowed. Examining the flow of the findings in the AO Order and the CIT-A's order, the ITAT expressed the following view:-

> *"13. We notice that the AO has treated the entire purchases of Rs 2,37,63,659/- made from the 12 parties mentioned the assessment order without rejecting the transacting of sale.* ***Once the sale is accepted then it cannot be said that the assessee has sold the goods without making any purchase. So, the findings of the AO are not based on any cogent and convincing evidence.*** *On the other hand* ***the assessee has also failed to produce the parties, from whom the alleged purchases were made and other documents to prove the movement of goods****. The said* ***facts however, suggest that the assessee has purchased the goods from gray market in order to evade taxes****. The Hon'ble Bombay High Court in CIT vs. Nikunj Eximp Enterprises 372 ITR 619(Bom) has held that* ***merely because the suppliers had not appeared before the AO or the CIT, one could not conclude that the purchases were not made****. In our considered opinion the findings of the Ld. CIT(A) is in accordance with the ratio laid down by the jurisdictional High Court in CIT vs. Nikunj Eximp Enterprises (supra) as the facts of both the case are almost similar.* ***The Ld. CIT(A) has restricted the addition to 10% of the total purchases in question taking into consideration the fact that the assessee has filed the sales tax return and VAT audit report apart from other documents, which establish the genuineness of the transaction of sale****. In our considered opinion the facts of the case relied upon by the revenue are different from the facts of the present case.* ***Under these circumstances we uphold the findings of the Ld. CIT(A) and sustain the addition to the extent of 10% of the total bogus purchases made by the assessee during the financial year relevant to the assessment year under consideration****."*
>
> ***[Emphasis Supplied]***

7. It is evident that the ITAT has returned firm findings that the

Respondent-Revenue had accepted the sales effected by the Appellant. The ITAT has also returned a finding that the sales are backed by compliance with indirect tax requirements such as sales tax returns and VAT audit reports. The ITAT has also held that it cannot be said that goods have not been sold by the Assessee. Most importantly, the ITAT has returned a firm finding that the adverse findings contained in the AO Order were not based on any cogent and convincing evidence.

8. Once such a view has been arrived at by the ITAT, which is the last forum for finding of fact, namely, that the AO Order disallowing 100% of the purchases under cloud, is not based on any cogent and convincing evidence, it would follow that the AO Order has been judicially found to be untenable. Therefore, the foundation on which these proceedings were based stand completely undermined.

9. However, the ITAT went on to state that the Appellant-Assessee has also failed to produce the parties from whom the alleged purchases were made and documents to prove the movement of goods (such as lorry receipts). The ITAT came to a view that goods would have indeed been purchased in the grey market. On this basis, it appears that the ITAT took an easy way out by simply upholding the order of the CIT-A – by disallowing only 10% of the purchases and adding that amount to

the income of the Assessee.

10. The key driver for the ITAT's approach appears to have been a judgment of a Division Bench of this Court in the case of *The Commissioner of Income Tax-1, Mumbai V/s. M/s. Nikunj Eximp Enterprises Pvt. Ltd.*[1] (***Nikunj***). The ITAT believed that the view taken by the CIT-A was consistent with the position in ***Nikunj***. Therefore, it would be relevant to examine the facts and the law declared in the context of the facts, in ***Nikunj***.

11. Indeed, in ***Nikunj***, a Division Bench of this Court ruled that merely because the suppliers had not appeared before the Assessing Officer or the CIT-A, one cannot conclude that the purchases in question had never been made and that they are bogus. The following extracts would be noteworthy.

> *"2. ……..*
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> *We have considered the submission on behalf of the revenue. However, from the order of the Tribunal dated 30.04.2010, **we find that the Tribunal has deleted the additions on account of bogus purchases not only on the basis of stock statement i.e. reconciliation statement, but also in view of the other facts. The Tribunal records that the Books of Accounts of the respondent- assessee have not been rejected. Similarly, the sales have not been doubted** and it is an admitted position that substantial amount of sales have been made to the Government Department i.e. Defence Research and Development Laboratory, Hyderabad. Further, there were confirmation letters filed by the suppliers, copies of invoices*

[1] *[2015] 372 ITR 619 (Bom.)*

> *for purchases as well as copies of bank statement all of which would indicate that the purchases were infact made.* ***In our view, merely because the suppliers have not appeared before the Assessing Officer or the CIT(A), one cannot conclude that the purchases were made not by the respondent-assessee.*** *The Assessing Officer as well as CIT(A) have* ***disallowed the deduction of Rs.1.33 crores on account of purchases merely on the basis of suspicion because the sellers and the canvassing agents have not been produced before them. We find that the order of the Tribunal is well a reasoned order taking into account all the facts before concluding that the purchases of Rs.1.33 crores was not bogus****. No fault can be found with the order dated 30.04.2010 of the Tribunal."*
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> *[**Emphasis Supplied**]*

12. In the case at hand, indeed, the sales are not under cloud. The only ground for suspecting the purchases is that they were from suspect persons on the basis of input from the investigation wing and sales tax authorities. The ground in the instant case too is that the persons from whom the purchases were made had not been produced before the Assessing Officer. The ITAT has endorsed the CIT-A's acceptance of the sales tax returns and the VAT audit report. The ITAT has returned a firm finding that there is no cogent or convincing evidence in the AO Order. Against such backdrop, the ITAT believed that the factual pattern of the matter at hand is similar to the factual context of ***Nikunj***. That being the case, the outcome too ought to have been similar to ***Nikunj***, where the disallowance was entirely rejected by the ITAT. In the instant case, the ITAT appears to have found it convenient that the CIT-A had chosen to disallow 10% of the expenses and it appears to be

an acceptable consolation to strike a balance.

13. However, we have to note that once there is a quasi-judicial finding that there is no cogent and convincing evidence at all on the part of the Revenue in levelling an allegation, it would be wrong to expect that the Assessee would still have to prove its innocence. The ITAT ought to have gone into this facet of the matter and dealt with why the 10% disallowance was plausible, reasonable and necessary in the context of the facts of the case. Such an analysis is totally absent in the Impugned Order.

14. In our opinion, in adopting such an approach, the ITAT has given credence to the proposition that the law can call for proof of the negative. The ad hoc rejection of 10% of the expenses, found in the order of the CIT-A, appears to have been a convenient *via media* that has been endorsed by the ITAT.

15. Ms. Gokhale sought to defend the approach by stating that 10% was the profit margin in the opinion of the CIT-A and that would be a reasonable barometer for disallowance – to remove the benefit of purchasing in the grey market. The Impugned Order has no analysis whatsoever to endorse any disallowance after having found that all the sales are entirely genuine and that there is no cogent or convincing

evidence in the AO Order to disallow the expenses. In these circumstances, we are unable to endorse the mechanical approach, or even the tactically equitable approach of convenience, by disallowing a portion of the expenses.

16. In the instant case, we find that the Revenue in fact viewed the position as warranting a 100% disallowance of the expenses. In the context of the Impugned Order, that is understandable since one could question if there is no cogent and convincing evidence at all. A Division Bench of this Court did not consider that appeal to be worthy of consideration. In ***Nikunj***, the ITAT reversed the entire disallowance on the part of the Assessing Officer and the CIT-A. But purporting to adopt ***Nikunj***, in the instant case, the ITAT fell short of analysing if the disallowance of 10% was reasonable and justifiable.

17. This very bench had occasioned to deal with a similar issue in the case of *Principal Commissioner of Income-tax-1 Vs. SVD Resins & Plastics (P.) Ltd.*[2], where, repelling a challenge by the Revenue, to a decision of the ITAT curtailing the disallowance of allegedly bogus purchases to 12.5%, the following observations were made:-

> *"11. We may observe that in the facts of the present case,* ***the basic premise on the part of the A.O. so as to form an opinion that the disputed purchases were***

[2] *[2024] 166 taxmann.com 242 (Bombay)*

not having nexus with the corresponding sales, appears to be not correct. It is seen that what was available with the department was merely information received by it in pursuance of notices issued under section 133(6) of the Act, as responded by some of the suppliers. However, an unimpeachable situation that such suppliers could be labeled to be not genuine qua the assessee or qua the transaction entered with the assessee by such suppliers, was not available on the record of the assessment proceedings. It is an admitted position that during the assessment proceedings, the assessee filed all necessary documents in support of the returns on which the ledger accounts were prepared, including confirmation of the supplies by the suppliers, purchase bills, delivery bank statements etc. to justify the genuineness of the purchases, however, such documents were doubted by the AO on the basis of general information received by the AO from the Sales Tax Department. In our opinion, to wholly reject these documents merely on a general information received from the Sales Tax Department, would not be a proper approach on the part of the AO, in the absence of strong documentary evidence, including a statement of the Sales Tax Department that qua the actual purchases as undertaken by the assessee from such suppliers the transactions are bogus. Such information, if available, was required to be supplied to the assessee to invite the response on the same and thereafter take an appropriate decision. Unless such specific information was available on record, it is difficult to accept that the AO was correct in his approach to question such purchases, on such general information as may be available from the Sales Tax Department, in making the impugned additions. This for the reason that the same supplier could have acted differently so as to generate bogus purchases qua some parties, whereas this may not be the position qua the others. Thus, unless there is a case to case verification, it would be difficult to paint all transactions of such supplier to all the parties as bogus transactions.

12. In our opinion, a full addition could be made only on the basis of proper proof of bogus purchases being available as the law would recognise before the AO, of a nature which would unequivocally indicate that the transactions were wholly bogus. In the absence of such proof, by no stretch of imagination, a conclusion could be arrived, that the entire expenditure claimed by the petitioner qua such transactions need to be added, to be taxed in the hands of the assessee.

13. In a situation as this, the A.O. would be required to carefully consider all such materials to come to a conclusion that the transactions are found to be bogus. Such investigation or enquiry by the AO also cannot be an enquiry which

would be contrary to the assessments already undertaken by the Sales Tax Authorities on the same transactions. This would create an anomalous situation on the sale-purchase transactions. ***Hence, in our opinion, wherever relevant any conclusion in regard to the transactions being bogus, needs to be arrived only after the A.O. consults the Sales Tax Department and a thorough enquiry in regard to such specific transactions being bogus, is also the conclusion of the Sales Tax Department. In a given case in the absence of a cohesive and coordinated approach of the A.O. with the Sales Tax Authorities, it would be difficult to come to a concrete conclusion in regard to such purchase/sales transactions being bogus merely on the basis of general information so as to discard such expenditure and add the same to the assessee's income****.*

14. ***Any half hearted approach on the part of the AO to make additions on the issue of bogus purchases would not be conducive. It also cannot be on the basis of superficial inquiry being conducted in a manner not known to law in its attempt to weed out any evasion of tax on bogus transactions.*** *The bogus transactions are in the nature of a camouflage and/or a dishonest attempt on the part of the assessee to avoid tax, resulting in addition to the assessee's income. It is for such reason, the approach of the AO is required to be well considered approach and in making such additions, he is expected to adhere to the lawful norms and well settled principles. After such scrutiny, the transactions are found to be bogus as the law would understand, in that event, they are required to be discarded by making an appropriate permissible addition.*

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16. The assessee has happily accepted such finding as this has benefited the assessee, looked from any angle. However, ***in a given case if the Income-tax Authorities are of the view that there are questionable and/or bogus purchases, in that event, it is the solemn obligation and duty of the Income-tax Authorities and more particularly of the A.O. to undertake all necessary enquiry including to procure all the information on such transactions from the other departments/authorities so as to ascertain the correct facts and bring such transactions to tax. If such approach is not adopted, it may also lead to assessee getting away with a bonanza of tax evasion and the real income would remain to be taxed on account of a defective approach being followed by the department.*** *"*

[Emphasis Supplied*]*

18. The aforesaid analysis would squarely apply to the facts of the instant case. Not only has the Assessing Officer not conducted the exercise as expected of him, the CIT-A has effected a summary measure of disallowing 10% of the expenses and the ITAT has been happy to endorse the same as an equitable middle ground. Such an approach cannot be endorsed as a process known to law to disallow expenses on the premise of their being bogus.

19. Another decision of a Division Bench of this Court in the case of *Principal Commissioner of Income-tax Vs. Shapoorji Pallonji and Co. Ltd.*[3] is noteworthy. The relevant portions are extracted below:-

> *17. On further appeal before the Tribunal by the respondent - assessee, Tribunal held as under:*
>
> > *"16. Having heard rival submissions, we are of the view that there is merit in the submissions made by the assessee. **We notice that the AO has simply relied upon the Sales Tax Department report about suspicious dealers, without making independent inquiries. On the contrary, the assessee has furnished all the materials to prove the genuineness of purchases and the AO has failed to show that those materials were bogus. Under these set of facts, we are of the view that there is no justification in doubting the genuineness of purchases made by the assessee.** Further, these alleged bogus purchases forms a minor fraction of total volume of the assessee company and it is stated that there is no day to day involvement of the management. It was further submitted that the assessee is having strict internal controls. Hence we are of the view that the AO has not made a proper ground in support of the disallowance. Accordingly we set aside the order passed by Ld. CIT (A) on this issue and direct the AO to delete the addition of Rs.3,23,944/-."*
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> *18. **Thus, we find that according to the Tribunal the assessing officer had merely relied upon information received from the Sales Tax Department, Government of Maharashtra without carrying out any independent enquiry. Tribunal had recorded a finding that assessing officer had failed to show that the purchased materials were bogus and held that there was no justification to doubt genuineness of the purchases made by the respondent – assessee.***

[3] *[2020] 117 taxmann.com 625 (Bom)*

> *19. We are in agreement with the views expressed by the Tribunal.* ***Merely on suspicion based on information received from another authority, the assessing officer ought not to have made the additions without carrying out independent enquiry and without affording due opportunity to the respondent - assessee to controvert the statements made by the sellers before the other authority****. Accordingly, we do not find any good ground to entertain this question for consideration as well."*
>
> *[**Emphasis Supplied**]*

20. The Supreme Court dismissed the Special Leave Petition challenging the aforesaid decision. In the instant case, the onus of bringing the purchases by the Appellant-Assessee under cloud was on the Respondent-Revenue, which has not discharged this burden in the first place. Apart from the inputs being received from the investigation wing, there is nothing concrete in the material on record that was used to confront the Appellant-Assessee. If the counterparties in these purchases could not be produced years later, simply adopting a 10% margin for disallowance, without any cogent or convincing evidence, in our opinion, would be unreasonable and arbitrary. It is repugnant for the ITAT to uphold such an addition of 10% of the allegedly bogus purchases to the income of the Appellant-Assessee, despite returning a firm finding that the AO Order was untenable not being backed by cogent and convincing evidence.

21. Therefore, in our opinion, the substratum of the adverse findings returned in the AO Order having been undermined, we are unable to agree, in the facts and circumstances of the case, with the conclusion of

the ITAT. As a result, the Impugned Order deserves to be set aside and these Appeals are disposed of in favour of the Appellant-Assessee and against the Respondent-Revenue. Consequently, all the three captioned Appeals stand allowed. No costs.

[SOMASEKHAR SUNDARESAN, J.] [G. S. KULKARNI, J.]

Aarti Palkar