

**IN THE INCOME TAX APPELLATE TRIBUNAL "D" BENCH, MUMBAI
BEFORE SHRI SHAMIM YAHYA, AM AND SHRI AMARJIT SINGH, JM**

ITA No.6102/Mum/2017
(Assessment Year: 2007-08)

ITO-19(1)(4) Matru Mandir, 2 nd Floor, R. No. 222, Tardeo Road, Mumbai-400 007	Vs.	M/s. Dinal Diamonds Office No. JW4190 J Tower, West Wing, 4 th Floor, Bharat Diamond Bourse, BKC, Bandra (E), Mumbai-400 004
PAN/GIR No. AACPN 2962 L		
(Appellant)	:	(Respondent)
Appellant by	:	Shri D. G. Pansari
Respondent by	:	None
Date of Hearing	:	04.02.2019
Date of Pronouncement	:	05.03.2019

ORDER

Per Shamim Yahya, A. M.:

This appeal by the Revenue is directed against the order of the learned Commissioner of Income Tax (Appeals)-30, Mumbai ('Id.CIT(A) for short) dated 03.07.2017 and pertains to the assessment year (A.Y.) 2007.08.

2. The grounds of appeal read as under:

1. "Whether on the facts and in the circumstance of the case and in law, the Learned. CTT(A) order Is not perverse for not considering the order of Hon" ble Supreme Court in the case of N K Protein Ltd dated 16.01.2017, which is on the similar issue of bogus purchases and when the apex court order was already the law of the land when the Ld. CIT(A) has given his decision vide order dated 03.07.2017 ?"
2. "Whether on the facts and in the circumstance of the case and in law, the Learned. CIT(A) has erred in directing the A.O. to restrict the estimation of the profit at 3% instead of 100% of the total non-genuine purchases when he himself has accepted that these purchases are non genuine as held by A.O.?"
3. "Whether on the facts and in the circumstance of the case and in law, the Learned. CIT(A) is justified in confirming the addition of only 3% in view of the deicison of Hon'ble Calcutta High Court in case of Precision Finance Pvt. Lts. Which stated that mere payment

sustaining only an addition @ 3% profit rate on total purchases of Rs.5.57,61,124/- made from 4 parties when in fact the assessee had failed to prove the genuineness of the said purchases ?

3. "Whether on the facts and in the circumstance of the case and in law, the Learned. CIT(A) has erred in directing the AO to restrict the estimation of the profit at 3% instead of 100% of the total non-genuine purchases when he himself has accepted that these purchases are non genuine as held by AO ?

4. The appellant prays that the order of the Ld.CIT(A) on the above grounds be set aside and that of the AO be restored.

3. Brief facts of the case are as under:

The assessee is a Partnership Firm, engaged in the business of 'import, manufacturing and trading of cut and polished diamonds. The return of income for the year under appeal was filed on 27-10-2007, declaring total income of Rs.15,93,584/-. The case was reopened u/s 147 of the Act, by issuing notice u/s 148 of the Act on 28-03-2014. In response to the notice u/s 148 of the Act, the assessee filed various details in response to the questionnaire sent by the office. Assessment u/s. 143(3) r.w.s. 147 of the I.T. Act, 1961 was completed by the Ld. AO, on 30-03-2015 determining the total income at Rs.1,02,68,130/-.

4. The reasons for reopening of the assessment is based on the information that Search & Seizure operations as well as Survey operations were conducted on 03-10-2013 by the DGIT, Investigation Wing, Mumbai, in the case of Shri Praveen Kumar Jain and also in the group cases of Shri Gautam Jain and others. During the course of the operation, it was found that several name lending dummy directors, partners/ proprietors of various concerns which were literally controlled, operated and managed by Shri Rajendra Kumar Jain, Sanjay Choudhary and Dharmichand and the persons-in-charge belongs to their native place. This was "admitted by those persons in the sworn

statements' recorded during the course of search operation and they have also admitted that they were made to the position by Shri Rajendra Kumar Jain and others. It was found that the group concerns are .all paper companies/firms, proprietorship concern with no real business activities, "operating solely with the purpose of facilitating fraudulent financial transactions which includes, among others, providing accommodation entries in the form of unsecured loans to interested parties, issuing of bogus sale bills to various parties and providing a bogus front to concerns which do not want to import diamonds in their own hands/books of accounts. Post search investigation reveals that the assessee has taken accommodation entries in the form of bogus purchases from M/s Vitrag Jewels amounting to Rs. 86,74,541/-.

5. After obtaining the explanations from the appellant, AO concluded that the appellant adopted a modus operand! to reduce its true profits by inflating its expenses including purchase by taking accommodation entries. It was held that the purchases remained unverifiable in the books of accounts of the assessee and were inflated to suppress the true profits. Mere filing of evidences in support of purchases and payment through account payee cheques cannot be conclusive proof in a case where genuineness of the transaction itself is in doubt. Therefore, based on the statements recorded on oath during the search operations from Shri Rajendra Kumar Jain Sanjay Choudhary and Dharimchand Jain and ethers, the purchases made from the M/s. Vitrag Jewels is treated by the AC as unverifiable. For this reason, AO rejected the books of accounts as provided in section 145 (3) of the Act. The AO also stated that in the given facts and circumstances of the case, the assessee have indulged in non-genuine transactions and the intention of

indulging in such activity is to suppress the true profits and to reduce the tax liability. Therefore the total purchases from the party amounting to Rs. 86,74,541/- is treated as non-genuine purchases and is added to the total income of the assessee.

6. Upon the assessee's appeal, the Id. CIT(A) noted that he was in agreement with the findings of the A.O. that the purchases are not made from the party. However, he noted that the A.O. has added the entire amount of purchases from the party. But at the same time, the A.O. did not disturb the sale, ignoring the fact that there will not be any sale without the purchases. He opined that there are every change that the assessee might have purchased the goods through grey market. He further observed as under:

6.8 From the above discussion, one can safely conclude that the appellant had obtained only the bills from the above-mentioned parties without actually getting the material. However, it is also a matter of fact that the purchases from these concerns have been entered into the stock register and the assessee has shown corresponding sales against the said purchases. This could only mean that the diamonds were bought by the assessee, from grey market without bills and to adjust these transactions into the books of accounts, the appellant obtained bills from Rajendra Jain Group Concerns. In such scenario, on one hand the genuineness of the purchase party is doubted but the genuineness of purchase on a whole cannot be doubted.

6.9 In this case, I find that quantitative details were maintained, Ld. AO not doubted the genuineness of sales, however, held that the appellant indulged in non-genuine purchases to suppress the profits and rejected the books of accounts under section 145 (3) of the I T Act and proceeded to add the entire amount of such purchases made from the three parties, instead of making the profit element embedded in such bogus purchase. As stated earlier when the sales are genuine, it is not possible to sell the goods without making any purchases. If the purchases are not made from those parties, the appellant must have purchased from some other parties. In such a situation, adding the entire amount of purchase to the total income is not correct because it will give a distorted picture of the profit margin. In my considered opinion, which is supported by several judicial forums, estimating the profit percentage on such purchases is the correct way to bring the income to tax. Thus, the issue would boil down to finding out what is the correct element of profit embedded in bogus purchases which the appellant would have made from such unknown entities.

7. Thereafter, the Id. CIT(A) quoted several case laws. He proceeded to disallow 3% on the total purchases by holding as under:

6.13 Taking into consideration the above facts, the issue arrives at, is to what would be the margin, one can expect while buying the material from grey market instead of normal course of business from regular dealers. Two aspects need to be taken into consideration in such circumstances. First, these diamonds in the grey market are always cheaper than the diamonds sourced from the genuine dealer. This is because, the genuine dealer would charge his incidental cost including the whole administrative cost while selling the diamond in the market, whereas the petty dealers in the grey market do not carry such incidental charges on such sales, wherein they are only looking for a quick profit. Secondly, there is always an element of discount in the case of instant cash purchase.

6.14 Hence, the task is to ascertain the additional GP, which the appellant must have earned by purchasing the diamonds from the grey market, than from the regular dealer. This would be the margin, which the petty trader in the grey market offers over the genuine trader.

6.15 Considering the above facts of the case which are similar for the year and also taking into account the submissions of the AR, adding the entire amount of purchases for the year by the AO, is not based on correct footing. Coming to the profit margin in the trade, the taskforce group for diamond industry constituted by the Government of India, Ministry of Commerce and Industry, after considering the BAP scheme, recommended presumptive tax for net profit calculated @2% of trading activity and @3% for manufacturing activity or @ 2.5% across the board. It is also ascertained that the operating profit in case of diamond trading for computation of ALP by the TP wing is consistently in the region of around 1.75% to 3%. It is also brought to my notice that the AOs are also adopting 3% on the purchases made from Bhanwarlal group concerns, as the profit element embedded, in the subsequent assessments finalized on the similar set of facts. In view of the same and also since the profit margin is lesser in this sector, addition of the amount of entire purchases is not realistic. Considering the lesser profit margin in this sector i.e. around 2 to 3 percent and the taxes saved is around 1% and also on purchases made from places like Surat, there is no levy of tax, I am of the considered opinion that if the addition is sustained to the extent of 3% of the purchases made as the profit element embedded in such purchases from four parties belonging to the Rajendra Jain and others, the same will meet the ends of justice. Accordingly I direct the AO to restrict the addition @3%, on the total purchases of Rs. 5,57,61,124/~ from the four parties as the profit element embedded in such purchases. Grounds raised on this issue are treated as 'Partly Allowed'.

8. Against the above order, the Revenue is in appeal before us.

9. We have heard the Id. Departmental Representative (Id. DR for short) and perused the material available on record. None appeared for and on behalf of the assessee despite

notice sent. The notice sent has returned unserved. Hence, we proceeded to adjudicate the issue by hearing the ld. DR and perusing the records.

10. Upon careful consideration we find that the assessee has provided the documentary evidence for the purchase. Adverse inference has been drawn by the A.O. on the investigation wing action on Gautam Jain group. No independent enquiry has been conducted by the A.O. himself. We find that in this case the sales have not been doubted. It is settled law that when sales are not doubted, 100% disallowance for bogus purchase cannot be done. The rationale being no sales is possible without actual purchases. This proposition is supported from the Hon'ble jurisdictional High Court decision in the case of *Nikunj Eximp Enterprises* (in writ petition no 2860, order dt. 18.6.2014). In this case, the Hon'ble High Court has upheld 100% allowance for the purchases said to be bogus when sales are not doubted. However, in that case all the supplies were to the government agency. In the present case, the facts of the case indicate that assessee has made purchase from the grey market. Making purchases through the grey market gives the assessee savings on account of non-payment of tax and others at the expense of the exchequer. In such situation, in our considered opinion, on the facts and circumstances of the case, 3% disallowance out of the bogus purchases meets the end of justice, as reasoned by the ld. CIT(A) above. The case law quoted by the Revenue in the grounds of appeal is a dismissal of SLP simplicitor by the Hon'ble Apex Court. It does not meagre the order of the Hon'ble Apex Court with that.

11. In the result, this appeal by the Revenue stands dismissed.

Order pronounced in the open court on 05th March, 2019.

Sd/-
(Amarjit Singh)
Judicial Member

Sd/-
(Shamim Yahya)
Accountant Member

Mumbai; Dated : 05.03.2019

Roshani, Sr. PS

Copy of the Order forwarded to :

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

BY ORDER,

(Dy./Asstt. Registrar)
ITAT, Mumbai