



BOM HC: Reaffirms “Profit Element Only” Principle In Bogus Purchase Cases

Facts of the Case

The assessee, Amcon Construction, was engaged in the business of construction. For Assessment Year 2011–12, the Assessing Officer (AO) received information from the Sales Tax Department indicating that M/s Oriental Enterprises was allegedly functioning as a hawala or accommodation entry provider. Relying on this information, the AO treated the purchases made by the assessee from the said supplier as bogus and added the entire purchase amount to the assessee’s income.

In appeal, the Commissioner of Income Tax (Appeals) [CIT(A)] partly upheld the AO’s action and sustained a disallowance of 25% of the alleged bogus purchases. The assessee thereafter appealed to the Income Tax Appellate Tribunal, Pune Bench (ITAT). By order dated 10 November 2021, the ITAT reduced the disallowance to 10% of the alleged bogus purchases, observing that the corresponding sales had been accepted by the Department and, therefore, only the profit element embedded in such purchases could be brought to tax.

Aggrieved by the reduction granted by the ITAT, the Revenue, through the Principal Commissioner of Income Tax-2, Pune, preferred the present appeal before the Bombay High Court u/s 260A of the Income-tax Act, 1961.

Revenue’s Contentions

The Revenue contended that:

- The assessee had failed to produce primary supporting documents such as delivery challans, weighbridge slips, and octroi receipts.
- There was no legal basis for restricting the disallowance to only a percentage of the purchases.
- The entire purchase amount ought to have been added back in light of the decision of the Supreme Court in *N.K. Proteins Ltd. v. Dy. CIT*, wherein bogus purchases were held liable for full disallowance.

Assessee’s Contentions

The Assessee contended that:

- The allegations were founded solely on information received from the Sales Tax Department, which was neither independently verified by the AO nor furnished to the assessee.
- The non-disclosure of such material amounted to a violation of the principles of natural justice.
- The assessee had produced supporting material, including purchase invoices, ledger accounts, bank statements evidencing payment by cheque, and supplier confirmations.
- Since the Department had accepted the corresponding sales, it was commercially untenable to regard the purchases as entirely fictitious.



Ruling of the Court

The Division Bench dismissed the Revenue's appeal, holding that no substantial question of law arose for consideration. The Court observed that the issue was squarely covered by earlier decisions of coordinate Benches, including *Paramshakti Distributors Pvt. Ltd.*, *SVD Resins & Plastics Pvt. Ltd.*, and *Ramelex Pvt. Ltd.* These authorities consistently affirm the principle that, where corresponding sales are accepted, only the profit element embedded in the alleged bogus purchases may be subjected to tax.

The Court further held that mere reliance on generalized information received from the Sales Tax Department, in the absence of any independent inquiry by the AO, was insufficient to justify a complete disallowance of the purchases. Although the Revenue placed reliance on the Supreme Court's ruling in *N.K. Proteins Ltd.*, the Bombay High Court distinguished that decision on the facts and held that it did not give rise to any substantial question of law in the present case. As a result, the line of authority favouring taxation only of the embedded profit element continued to apply.

The Court also noted that the failure to furnish the underlying material to the assessee, coupled with the denial of an opportunity to cross-examine the alleged hawala dealers, constituted a breach of the principles of natural justice. It concluded that the concurrent findings of fact recorded by the CIT(A) and the ITAT did not warrant interference u/s 260A of the Income-tax Act, 1961.

Citation

PCIT v. Amcon Construction (ITA No. 46 of 2004)

Conclusion

The decision in *Amcon Construction* is a significant taxpayer-friendly ruling that reinforces the judicial position that, in cases involving alleged bogus purchases, additions should ordinarily be confined to the profit element embedded in such purchases where the corresponding sales have been accepted. The judgment also underscores the centrality of procedural fairness and imposes a high evidentiary threshold on the Revenue when seeking a complete disallowance of purchases. Where however the assessee is not able to support the factum of purchase by producing documentary evidence to establish movement and receipt of goods, and on that ground purchases have been disbelieved, there are decisions taking the view that the entire purchases should be disallowed as unproved. It has been held that by only adding the profit percentage would help the assessee to regularise the balance unproved purchases which would defeat the purpose of s 69C of the Income tax Act 1961.