

**IN THE INCOME TAX APPELLATE TRIBUNAL  
"F" Bench, Mumbai**

**Before Shri Jason P. Boaz, Accountant Member  
and Shri Amarjit Singh , Judicial Member**

**ITA No. 6821/Mum/2014**  
(Assessment Year: 2010-11)

A C I T – 17(3) Room No. 614, 6 <sup>th</sup> Floor Piramal Chambers, Parel Mumbai 400012	Vs.	Shri Vipin B. Shah 206, Amit Industrial Premises Co.op Society Ltd. 61 Dr. S.S. Road, Parel (E) Mumbai 400012 PAN – ALIPS2377R
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**Appellant**

**Respondent**

**ITA No. 6381/Mum/2014**  
(Assessment Year: 2010-11)

Shri Vipin B. Shah 206, Amit Industrial Premises Co.op Society Ltd. 61 Dr. S.S. Road, Parel (E) Mumbai 400012	Vs.	A C I T – 17(3) Room No. 614, 6 <sup>th</sup> Floor Piramal Chambers, Parel Mumbai 400012 PAN – ALIPS2377R
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**Appellant**

**Respondent**

Revenue by: Shri Ranatir Gupta  
Assessee by: Shri Sanjay Parikh

Date of Hearing: 02.11.2016  
Date of Pronouncement: 16.11.2016

**ORDER**

**Per Jason P. Boaz, A.M.**

These are cross appeals, one by Revenue and the other by the assessee, directed against the order of the CIT(A)-29, Mumbai dated 22.08.2014 for A.Y. 2010-11.

2. The facts of the case, briefly, are as under: -

2.1 The assessee, proprietor of Vipin Shah and Associates, engaged in business as civil contractors, filed the return of income for A.Y. 2010-11 on 15.10.2010 declaring total income of ₹62,40,310/-. The return was

processed under section 143(1) of the Income Tax Act, 1961 (in short 'the Act') and the case was subsequently taken up for scrutiny. The assessment was completed under section 143(3) of the Act vide order dated 25.03.2013; wherein the income of the assessee was determined at ₹2,02,24,470/- in view of the following additions/disallowances: -

(i)	20% disallowance out of motor car expenses	₹79,063/-
(ii)	Disallowance out of telephone expenses (15%)	₹36,663/-
(iii)	Disallowance out of labour charges	₹1,05,58,905/-
(iv)	Bogus purchase under section 69C	₹33,09,526/-

2.2 Aggrieved by the order of assessment for A.Y. 2010-11 dated 25.03.2013, the assessee preferred an appeal before the CIT(A)-29, Mumbai. The appeal was disposed off by the learned CIT(A) vide order dated 22.08.2014 allowing the assessee partial relief. The learned CIT(A):

- (i) sustained the disallowance out of motor car expenses and telephone expenses to the extent of 5% thereof;
- (ii) sustained 25% disallowance under section 40A(2)(b) out of total labour charges paid to three sister concerns; i.e. disallowance to the extent of ₹26,39,726/- was sustained.
- (iii) Profit @12.64% on bogus purchases.

3. Both Revenue and the assessee, being aggrieved by the impugned order of the learned CIT(A)-29, Mumbai dated 22.08.2014 for A.Y. 2010-11, have preferred cross appeals in respect of issues held against them.

3.1 The grounds raised by the assessee in its appeal are as under: -

*“The Honourable Commissioner of Income Tax (Appeals) has erred in confirming ad-hoc 25% addition of the disallowed labour charges of Rs. 1,05,58,905/- by the learned assessing officer without considering the fact and merits of the case.*

*The Hon'ble CIT (Appeals) has also erred in confirming ad-hoc 12.64% addition of the disallowed alleged bogus purchases of Rs. 33,09,526/- by the learned assessing officer without considering the fact and merits of the case.*

*The Hon'ble CIT (Appeals) has also erred in not considering the fact that purchases to the extent of Rs. 29,90,240/- out of the above alleged*

*bogus purchase were written back / reversed in the subsequent year on defects finding in the material supplied, without considering the fact and merits of the case.*

*The Hon'ble CIT (Appeals) has also erred in not considering the further payments of Rs. 9,31,950/- out of the disallowed bogus purchase, allowable on the ground of paid portion from the alleged bogus purchase were allowed in the assessment u/s. 143(3) without considering the fact and merits of the case.*

*The Appellant craves leave to submit at the time of hearing such further facts, information, clarification, documents etc. as may be necessary for the purpose of deciding the issues in the appeal.”*

3.2 The grounds raised in Revenue's appeal are as under: -

1. *On the fact and in the circumstances of the case and in law the Ld. CIT(A) has erred in reducing the disallowance the motor car expenses from 20% to 5% without appreciating the fact that the assessee was not maintaining any log book for motor car and use of motor car for personal purposes cannot be ruled out.*
2. *On the fact and in the circumstances of the case and in law the Ld. CIT(A) has erred in reducing the disallowance of Telephone expenses from 15% to 5% without appreciating the fact that the use of Telephone expenses for personal purposes cannot be ruled out.*
3. *On the fact and in the circumstances of the case and in law the Ld. CIT(A) has failed to appreciate that the disallowance of Labour charges of Rs. 1,05,58,905/- was made out of payments payable to sister concerns of the assessee which were covered u/s 40A(2)(b) of the I T Act, and major payment of Rs. 90,04,748/- was shown as outstanding at the end of the year and the parties concerned did not have any source to justify the expenditure made as shown in Return Of Income. Further, on the fact and in the circumstances of the case and in law the Ld. CIT(A) has failed to appreciate that the assessee was not able to place any evidence to prove that the sub-contract were carried out by the sister concerns with their own funds.*
4. *On the fact and in the circumstances of the case and in law the Ld. CIT(A) has failed to appreciate that the peak method of disallowance as held in the case of M/s Vijay Proteins Ltd. (1996 58 ITD 428 Ahd) was correct method from making disallowance out of purchases treated as bogus purchases and has erred in directing the AO to treat the GP of 12.64% as disallowance out of bogus purchases.”*

4. **Ground No. 1 of assessee's appeal & Ground No. 3 of Revenue's appeal – Disallowance of Labour Charges**

4.1 The facts of the matter on this issue as per the records are that in the course of assessment proceedings, the Assessing Officer (AO) noticed

that the assessee had debited an amount of ₹2,44,32,298/- in the Profit & Loss account on account of labour charges paid to different sub-contractors on the civil contracts undertaken by him. Out of these, amounts totalling to ₹1,05,58,905/- had been paid to the following related concerns (hereinafter referred to as 'related parities): -

(i)	M/s. Bhairav constructions	₹37,22,876/-
(ii)	Jain Infrastructure	₹34,34,207/-
(iii)	Nakoda Developers	₹34,01,822/-

It was also observed from the schedule of sundry debtors that amounts totalling ₹90,04,748/- was shown as outstanding to these three parties as on 31.03.2010. On being queried to justify the payments made to these related parties as to why no disallowance is attracted in terms of section 40A(2) of the Act, the assessee filed copies of the returns of income of these parties stating that the above amounts have been offered to taxation by the above three parties. The AO observed that the returns of income of the said three parties (supra) were filed under section 44AF of the Act, which pertains to retail trading and does not cover the cases of sub-contractors. The AO also noticed from the returns of income that these three parties had neither received any money from any source or incurred their own funds to justify expenditure upto 95% as claimed therein; more so when the sub-contracts said to be undertaken by them is for labour supply, where payment to labourers is the basic part of expenditure. In the light of the aforesaid observations, the AO was of the view that since the above three parties had not established or shown that they had carried out any sub-contracts business or made payments to labourers; and the assessee had made meagre payments to them in the period under consideration; these transactions by the related parties were bogus and proceeded to disallow the entire amount of ₹1,05,58,905/- shown/debited as payments to these parties.

4.2.1 On appeal, the learned CIT(A) observed from the details on record that the assessee had carried out civil contract works for organizations like RBI, M/s. Reliance Infrastructure Ltd., etc. and therefore ruled out the possibility of these concerns making payments for civil contracts without

any work being carried out. It was also noticed that the AO did not cause any independent enquiry to prove that either that no work was carried out by these three related parties or that the expenditure booked on account of labour charges to them was totally bogus. Therefore, in the absence of any evidence being brought on record to substantiate/prove the same, the payments to these parties can't be termed as bogus and the disallowance of the entire payment of entire labour expenditure, since they were incurred through related parties, was held to be unjustified by the learned CIT(A).

4.2.2 The learned CIT(A) observed from the details on record that though the three related parties had not been paid entire amounts due during the period under consideration, substantial payments have been made in the subsequent year and since the labour jobs to complete the contract have been carried out, the expenditure incurred through the three related parties cannot be doubted. After thus concluding, the learned CIT(A) observing that since the assessee has not placed on record comparative evidence to show that payments to the related parties were at par with labour payments to other concerns performing similar jobs, the provisions of section 40A(2) of the Act are attracted and consequently sustained the addition to the extent of 20% of labour charges paid to selected parties, i.e. ₹26,39,726/-.

4.3.1 The learned A.R. of the assessee reiterated the submissions/arguments put forth before the AO and learned CIT(A). According to the AO, no case was made out by the AO to warrant disallowance of the entire expenditure incurred on labour charges paid to the three related parties under section 40A(2) of the Act. It is not disputed that civil contract work were, inter alia, carried out for RBI, Reliance Infrastructure Ltd. etc. The fact that no enquiry was conducted by the AO to prove that either no work was carried out by these related parties or that the expenditure booked was entirely bogus, was noted by the learned CIT(A), who proceeded to hold that the disallowance of the entire expenditure was not called for. The learned A.R. of the assessee further contends that after holding thus, the action of the learned CIT(A) himself to then proceed to invoke the provisions of section

40A(2) of the Act to make an adhoc disallowance of 25% of the expenditure incurred on labour charges to three related parties, without pointing out any particular expenditure which according to him is excessive or unreasonable thereunder is not sustainable. In support of the proposition, that no adhoc disallowance can be made under section 40A(2) of the Act, the learned A.R. of the assessee placed reliance on the following decisions:-

- (i) Cisco Systems Capital (I) Ltd. vs. Addl. CIT (2015) 37 ITR (Trib) 343 (Bangalore)
- (ii) Sayaji Iron and Engg. Co. Vs. CIT (2002) 253 ITR 749 (Guj.)
- (iii) Johnson and Johnson Ltd. vs. ACIT (ITA No. 3289 and 9437/Mum/2014)
- (iv) Goldcrest Exports vs. ITO (ITA No. 442/Mum/2009)

4.3.2 It is also contended that expenditure incurred on labour charges paid to the same three related parties was accepted by the Department and no disallowance under section 40A(2) of the Act was made in scrutiny assessment proceedings for A.Y. 2009-10 (copy placed at pg. 34-38 of paper book).

4.4 The learned D.R. for Revenue was heard in support of the grounds raised and placed reliance on the order of the AO. It was pleaded that the order of the learned CIT(A) on this issue be reversed and that of the so restored.

4.5 We have heard the rival contentions and perused and carefully considered the material on record, including the judicial pronouncements cited. From the facts of the case on this issue, the observations and findings of the authorities below, as discussed in paras 4.1 to 4.4 (supra) it is seen from a perusal of the impugned order of the learned CIT(A) that after due consideration of the material on record he negated the AO's view that the said transactions with the three related parties involving the incurring of expenditure for labour charges were bogus after observing that the said expenditure was in respect of civil contract works carried out for RBI, Reliance Infrastructure Ltd., who would certainly have not paid the assessee unless the civil contract involved was carried out; a view with which we concur. We also observe that the AO has not caused any enquiry to establish that either no contract work was carried out by the three

related parties or that the expenditure booked on account of labour charges was bogus. In this view of the matter, we concur with and uphold the finding of the learned CIT(A) that in the absence of any material evidence being brought on record by the AO to prove that the payments made to these three related parties as bogus, the said payment of labour charges to him cannot be termed as bogus and the action of the so to discover the entire payment of labour expenditure, since they were incurred through related parties, is unjustified and unsustainable in the facts and circumstances of the case. Consequently, ground No. 3 of Revenue's appeal is dismissed.

4.6 In its appeal in connection with ground No. 1 the assessee's submission is that the learned CIT(A) order sustaining an adhoc disallowance of 25% of the expenditure incurred on labour charges paid to the three related parties was unsustainable as no adhoc disallowance can be made as per the provisions of section 40A(2) of the Act. As rightly pointed out by the learned A.R. of the assessee, the AO/CIT(A) cannot make an adhoc disallowance under section 40A(2) of the Act. Rather, he has to make disallowance of such of that expenditure that is excess or unreasonable having regard to the FMV of goods, services, etc. for which the payment is made. In our considered view, the learned CIT(A) has failed to point out any particular expenditure in respect of labour charges which according to him is excessive or unreasonable but has proceeded to uphold an adhoc disallowance of 25% thereof, which is, in our view, unsustainable. In this view of the matter, we are of the opinion that the adhoc disallowance of 25% of expenditure incurred on labour charges paid to related parties under section 40A(2) of the Act was not warranted in the facts and circumstances of the case on hand as discussed above and therefore direct the AO to delete the same. Consequently, ground No. 1 of the assessee's appeal is allowed.

**5. Ground No. 2 to 4 of Assessee's appeal and ground No. 4 of Revenue's appeal – Bogus purchases under section 69C**

5.1.1 In the order of assessment, the AO observed that information was received from Sales Tax Authorities that certain parties had admitted before them that they had issued bogus bills to various parties without

selling any material and the assessee in the case on hand had made so called purchases amounting to ₹41,60,393/- from some such parties, as per the details hereunder: -

(i)	Ramdev Trading	₹73,433/-
(ii)	Dhruv Sale Corporation	₹1,77,138/-
(iii)	Shubhlaxmi Sales Corporation	₹11,28,491/-
(iv)	Ambika Trade Impex	₹3,42,007/-
(v)	Om Corporation	₹14,34,864/-
(vi)	National Trading Co.	₹1,50,938/-
(vii)	Universal Trading Co.	₹2,38,203/-
(viii)	Balaji Traders	₹1,88,434/-
(ix)	Trichipuram Trading P. Ltd.	₹4,26,885/-
	<b>Total</b>	<b>₹41,60,393/-</b>

5.1.2 To ascertain the genuineness of these purchases (supra) the AO called upon the assessee to furnish details to establish the same. The assessee furnished copies of purchase bills, delivery challens, proof payment through banking channels, etc. The AO further required the assessee to produce the said parties to give evidence in respect of the genuineness of these purchases, which he failed to do. The assessee's failure to do so, and relying on the information of the Sales Tax Authorities that these parties admitted to have given bogus bills, the AO proceeded to conclude that the assessee had made the aforesaid purchases (supra) from the above parties out of his undisclosed income and later on obtained the bogus bills to that extent from these parties. In that view of the matter, the AO proceeded to disallow the peak of the above purchases at ₹33,09,526/- and brought it to tax in the assessee's hands under section 69C of the Act.

5.1.3 On appeal, the learned CIT(A) was of the view that what is to be disallowed in the case of alleged bogus purchases is only the profit element embedded in such purchases shown to have been made from non-existent parties and not the peak amount of alleged bogus purchases as held by the AO. In that view of the matter, the learned CIT(A) directed the so to assess the gross profit (GP) on such bogus purchases @12.64% which is the G.P. Shown by the assessee in the year under consideration.

5.2 The learned D.R. was heard in support of ground No. 4 raised by Revenue challenging the action of the learned CIT(A) in directing the AO to assess the GP of 12.64% as the disallowance out of bogus purchases. It was prayed that the impugned order of the learned CIT(A) be reversed and that of the AO be restored.

5.3.1 The learned A.R. of the assessee was heard in support of the grounds raised at S. No. 2 to 4. In these grounds, the assessee contends that the learned CIT(A) has also erred in confirming the G.P. addition @12.64% of the alleged bogus purchases of ₹33,09,526/- without considering the fact that for the above, purchases to the extent of ₹29,90,240/- were written back/reversed in the subsequent year on finding defects in the material supplied.

5.3.2 According to the learned A.R., the assessee in order to establish the genuineness of the above purchase transaction (supra) had produced material evidence in the form of copies of purchase bills issued by the parties, proof of payment for such purchases through banking channels, delivery challans, etc. It is contended that, on the contrary, the AO has neither caused any independent enquiry nor brought on record even a shred of evidence to prove that the said purchases were bogus and in coming to an adverse finding merely relied on the information of purchase parties listed by the Sales Tax Department. The learned A.R. of the assessee submitted that on similar facts, the Hon'ble Bombay High Court and the Coordinate Bench of the Tribunal had deleted such additions made under section 69C of the Act in, inter alia, the following cases: -

- (i) CIT vs. Nikunj Eximp Enterprises P. Ltd. (2015) 372 ITR 619 (Bom);
- (ii) DCIT vs. Sri Rajeev G. Kalathil (ITA No. 6727/Mum/2012);
- (iii) Ramesh Kumar & Co. Vs ACIT (ITA No. 2955/Mum/2014);
- (iv) ACIT vs. Vishal P. Mehta (ITA No. 5313/Mum/2013).

5.4.1 We have heard the rival contentions and perused and carefully considered the material on record; including the judicial pronouncements cited. On an appreciation of the material on record, it is evident from the order of the assessment that it is on the basis of information from the

Sales Tax Department that the assessee issued notice to the assessee calling upon him to explain the genuineness of the aforesaid purchases from the said parties (supra). As the assessee was unable to produce the said parties, the AO primarily relying on the information obtained from the Sales Tax Department held the said purchases to be bogus. While it may be true that the said parties from whom the said purchases were made did not appear before the AO; however, Hon'ble Bombay High Court in the case of Nikunj Eximp Enterprises P. Ltd. (2005) 372 ITR 619 (Bom) has held that this by itself cannot be a ground to hold the purchases as bogus. Apart from this, the fact also remains that the assessee itself had filed copies of purchase bills, proof that payment for the same were through banking channels, delivery challans, etc. in order to establish the genuineness of the said purchases. It is a fact on record that the AO has not doubted the corresponding sales effected by the assessee and therefore it is in order to conclude that without corresponding purchases being affected, the assessee could not have made the sales.

5.4.2 We find that the AO has not brought on record any material evidence to conclusively establish that the purchases are bogus. Mere reliance by the AO on information obtained from the Sales Tax Department would not suffice to treat the purchases as bogus and make the addition. If the AO doubted the genuineness of these purchases, it was incumbent upon him to cause enquiries to be caused to ascertain the genuineness of otherwise of the transactions. Without causing any enquiries to be made to establish his suspicions, the AO cannot make the addition under section 69C of the Act by merely relying on information obtained from the Sales Tax Department. In the case on hand, the AO failed to make any enquiry to establish his suspicions. Further, the corresponding sales have not been questioned. We find that the assessee has brought on record documentary evidences to establish the genuineness of the purchase transactions, the action of the AO in ignoring these evidences cannot be accepted. When the copies of purchase bills of these parties, delivery challans, proof of payment through banking channels, etc., and there is no evidence brought on record by the AO to establish that the said payments were routed back

to the assessee, the addition made by the AO under section 69C of the Act is unsustainable. In coming to this view, we draw support from the decisions, inter alia, of the Hon'ble Bombay High Court in the case of Nikunj Enterprises P. Ltd. (supra) and the Coordinate Bench of the Tribunal in the cases of Rajeev G. Kalathil (supra) and Vishal Mehta (supra). In this factual matrix of the case, we hold that the addition made by the AO under section 69C of the Act on account of peak of alleged bogus purchases of ₹33,09,256/- to be unsustainable. Consequently Revenue's ground raised at S. No. 4 is dismissed.

5.5 In this order at paras 5.4.1 to 5.4.2 (supra) we have held that the AO's action in making the addition u/s. 69C of the Act on account of alleged bogus purchases was factually unsustainable in the legal and factual matrix of the case. Consequently, the finding of the learned CIT(A) in the impugned order that adhoc addition of 12.64% on account of alleged bogus purchases is to be made, would also not be sustainable as the profit on sale thereof would already be embedded in the assessee's income. We, therefore, delete this adhoc addition of 12.64% profit on alleged bogus purchases. Consequently, grounds 2 to 4 of the assessee's appeal are allowed.

6. **Ground No. 5 of the assessee's appeal**

This ground being general in nature, no adjudication is called for thereon.

7. **Ground No. 1 of Revenue's appeal – Disallowance of Motor car expenses**

7.1 In this ground Revenue contends that the learned CIT(A) erred in reducing the disallowance of motor car expenses from 20% to 5%. We have heard the rival contentions and perused and carefully considered the material on record. In the order of assessment, the AO has made an adhoc disallowance of 20% of motor car expenses and depreciation thereof (i.e. ₹79,063/-). On appeal, the learned CIT(A) sustained this disallowance to the extent of 5%. Before us, except for raising this ground, Revenue has not brought on record any material evidence to controvert the finding of the learned CIT(A) and warrant our interference therein on this issue. In

this view of the matter, we uphold the order of the learned CIT(A) on this issue and consequently, ground No. 1 of Revenue's appeal is dismissed.

**8. Ground No. 2 of Revenue's appeal – Disallowance of Telephone Expenses**

8.1 In this ground the Revenue challenges the action of the learned CIT(A) in reducing the disallowance of telephone expenses from 15% to 5%. We have heard the rival contentions perused and carefully considered the material on record. In the order of assessment the AO has made an adhoc disallowance of ₹36,663/-; being 15% of telephone expenses amounting to ₹2,44,423/-. On appeal, the learned CIT(A) has sustained the disallowance to the extent of 5%. Except for raising the ground before us, Revenue has not brought on record any material evidence to controvert the impugned order of the CIT(A) and warrant our interference therein on this issue. In this view of the matter, we uphold the order of the learned CIT(A) on this issue. Consequently, ground No. 2 of Revenue's appeal is dismissed.

9. In the result, Revenue's appeal for A.Y. 2010-11 is dismissed and the assessee's appeal is allowed.

Order pronounced in the open court on 16<sup>th</sup> November, 2016.

Sd/-  
**(Amarjit Singh)**  
**Judicial Member**

Sd/-  
**(Jason P. Boaz)**  
**Accountant Member**

Mumbai, Dated: 16<sup>th</sup> November, 2016

Copy to:

1. *The Appellant*
2. *The Respondent*
3. *The CIT(A) -6, Mumbai*
4. *The CIT - 2, Mumbai*
5. *The DR, "F" Bench, ITAT, Mumbai*

*By Order*

//True Copy//

*Assistant Registrar*  
*ITAT, Mumbai Benches, Mumbai*

n.p.