

Reassessment rightly made as AO had reasons to believe that taxpayer had made bogus purchases

Summary – The High Court of Gujarat in a recent case of Sajani Jewels, (the Assessee) held that In view of sufficient prima facie material on record to show that assessee had made bogus purchases through web of entities created by B initiation of reassessment by Assessing Officer was justified

Facts

- The assessee (Special Economic Zone) was engaged in business of manufacturing and export of diamond studded jewellery. It claimed exemption under section 10AA which was granted by Tribunal as well as High Court.
- Thereafter, on basis of search operation at premises of one 'B' wherein it was revealed that assessee had accommodated bogus entries to inflate purchases, the Assessing Officer noted that assessee had itself accepted bogus accommodation entries for purchase from Meridian Gems and concluded that income chargeable to tax had escaped assessment within the meaning of section 147.
- The assessee objected to process of reopening of assessment but such objections were however, rejected by the Assessing Officer.
- The assessee submitted that the reasons recorded by the Assessing Officer did not demonstrate any independent application of mind by Assessing Officer. There was no failure on the part of the assessee to disclose truly and fully all material facts and in any case, there was no escapement of income as the assessee enjoyed 100 per cent exemption under section 10A.

Held

- Regarding the first contention of the assessee, the Assessing Officer has noted that search and seizure action was initiated in the premises of one 'B' and other family members on 11-10-2013, during which, statement on oath of 'B' was recorded. In such statement, he had disclosed elaborative method of providing recognition entries to various individuals and entities through number of bogus concerns. Such concerns would provide bogus sale entries to the so-called purchasers. The sale consideration would be received in cheque. The seller would return the cash amount to the purchaser after retaining commission. 'B' had also provided list of such bogus entities, one of them being Meridian Gems. The reasons further record that the assessee had also accepted bogus accommodation entries for purchase of goods worth Rs. 90.17 lakhs from said Meridian Gems in order to inflate the purchases.
- The investigation wing of the income tax department had placed the entire report of said investigation along with important documents such as the statement of B and other witnesses whose statements were recorded. If after perusal of such documents, the Assessing Officer recorded the reasons, it cannot be stated that these reasons were not those of the Assessing Officer and merely amounted to mechanical reproduction of the exercise undertaken by the investigation wing

of the Income tax department. It is undoubtedly true that the reasons to be recorded before issuance of notice of reopening have to be those of the Assessing Officer alone. This however, does not mean that the Assessing Officer cannot rely on the exercise undertaken by other wings of the Government departments, if the material so collected through inquiry or investigation provides *prima facie* information, a tangible material; which enables the Assessing Officer to form a belief that income chargeable to tax has escaped assessment. There is nothing to prevent the Assessing Officer from recording such satisfaction and to proceed to issue notice for reopening. An independent decision by the Assessing Officer to enable her to come to the conclusion that income chargeable to tax has escaped assessment is *sine qua non* for reopening an assessment. This would undoubtedly require application of mind on her part when certain materials collected by some other wing of the department is placed before her. There can however be no straight jacket formula of the manner in which, mind can be applied or shown to have been applied. The same may be gathered from the reasons recorded and other contemporaneous material on record. In this context, it was the decision of the Assessing Officer, based on the materials collected by the investigation wing that she recorded the reasons to form a belief that income chargeable to tax had escaped assessment, which led her to issue notice of reopening.

- The second contention of assessee that there was no failure on the part of the assessee to disclose truly and fully all material facts, must meet with summary rejection. There was sufficient *prima facie* material on record that the assessee had made bogus purchases through the web of entities created by B. Obviously such facts were not on record during the original assessment proceedings.
- The argument of the assessee that in any case, the entire income of the assessee being tax exempt, even if the stand of the department as reflected in the reasons recorded is correct and ultimately established, there would be no additional tax burden on the petitioner. To put it simply, the question being posed is where is the escapement of income chargeable to tax ?
- According to the department, the petitioner had shown purchases of goods from one of the bogus entities created by B. There was no genuine purchase. All that was done was that the assessee had paid such amount in cheque without making any purchases. The seller after receiving such amount, would return substantial portion thereof in cash retaining his commission. This circuitous route would ensure that cost of purchases made by the assessee would be artificially inflated, thereby deflating the profit. In that view of the matter, even if the department is correct, all that would be done even if the assessment is permitted, is to disallow the expenditure of Rs. 90.17 lakhs. Correspondingly, the income of the assessee would increase by the said sum of Rs. 90.17 lakhs. However, if the entire income is exempt under section 10AA of the Act, there would be still no tax implication.
- The result of this exercise would be that even if the expenditure of the so called bogus purchases is disallowed, the only effect it could have is to increase the profit of the assessee which in any case is exempt under section 10AA. Section 147 would be applicable where the Assessing Officer has reason to believe that income chargeable to tax has escaped assessment. When this fundamental

requirement fails, power of reopening cannot be exercised. The argument of the revenue cannot be appreciated that such income would not qualify as business income and that it should be treated as income from other sources by applying section 69C. This section pertains to unexplained expenditure and provides that where, in any financial year, an assessee has incurred any expenditure and he offers no explanation about the sources of such explanation or part thereof or the explanation offered is not satisfactory, the amount covered by such expenditure or the part, as the case may be, would be deemed to be the income of the assessee for such financial year. The present is not a case where the assessee has incurred expenditure, but failed to offer explanation about the source of such expenditure. The source of expenditure was very much available since in the reasons recorded itself, the Assessing Officer points out that the purchases were made by making cheque payments. Section 69C therefore has no applicability.