

IN THE HIGH COURT OF JUDICATURE AT MADRAS

CORAM:

THE HONOURABLE MR.JUSTICE T.S.SIVAGNANAM
and
THE HONOURABLE MR.JUSTICE N.SATHISH KUMAR

Tax Case (Appeal) No.979 of 2008

Judgment reserved on 09.11.2018	Judgment pronounced on 19.11.2018
------------------------------------	--------------------------------------

Shri P.Amarnath Reddy,
No.1/1, Kothari Road,
Nungambakkam,
Chennai-600 034.

... Appellant

-vs-

The Deputy Commissioner of Income-tax,
Central Circle-III (3),
121, Mahatma Gandhi Road,
Chennai-600 034.

... Respondent

Tax Case Appeal filed under Section 260A of the Income Tax Act, 1961 against the order of the Income-tax Appellate Tribunal Chennai Bench "B", dated 11.03.2008 in I.T.A.No.684/Mds/2007 for the assessment year 2000-01 against the order of the Commissioner of the Income Tax (Appeals)-II, Chennai, Nungambakkam, Chennai-34, dated 15.12.2006 made in Appeal No.CIT(A)/CHE/171/06-07 and against the order in the Joint Commissioner of Income Tax, Central Circle-III (3), Chennai, dated 31.3.2006 made in PANo/GI NO.AABR9639K, for the Assessment year 2000-01.

For Appellant : Ms.Sree Lakshmi Valli

For Respondent : Mr.T.Ravi Kumar,
Senior Standing Counsel

JUDGMENT

T.S.Sivagnanam, J.

This appeal, by the appellant/assessee under Section 260A of the Income-tax Act, 1961 (hereinafter referred to as "the Act"), is directed against the order passed by the Income-tax Appellate Tribunal Chennai 'B' Bench ("the Tribunal" for brevity) in I.T.A.No.684/Mds/2007, dated 11.03.2008, for the assessment year 2000-01.

2. The appeal was admitted, by order dated 29.07.2008, on the following substantial questions of law:-

"(i) Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in law in rejecting the appellant's valuation of the closing stock of shares on the basis of "since realized value"?

(ii) Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in law in confirming the value of the closing stock determined by the Commissioner of Income Tax (Appeals)?"

3. The assessee is an individual, running a proprietorship concern, engaged in the manufacture and export of leather products. On 22.01.2004, a search was conducted in the residential premises of the assessee, pursuant to which, a notice under Section 153A of the Act was issued. In response to such notice, the assessee filed return of income declaring a loss of Rs.3,39,93,012/-, apart from the agricultural income of Rs.2,31,203/-.

4. The assessee's case is that during the previous year, relevant to the assessment year 2000-01, he had commenced business of trading in shares, and throughout the year, there was tremendous fluctuation in the value of shares due to hawala transaction, and only towards the end of the year, the value of shares stabilized.

5. The assessee would state that he was advised that the valuation of closing stock of shares would have to reflect a realistic value and accordingly, the assessee valued the closing stock of shares on the basis of "since realised price". According to the assessee, if any other method of valuation is adopted, it would reflect a distorted or unreal value.

6. The assessee would further state that the 'since realised price' method of valuation is an accepted method, in accordance with the Accounting Standard (AS) prescribed by the Institute of Chartered Accountants of India (ICAI), and accordingly, valued his shares at Rs.6,46,36,684/-.

7. The Assessing Officer, by order dated 31.03.2006, completed the assessment under Section 153A read with Section 143(3) of the Act and while doing so, raised a query as to why the valuation of the closing stock adopted by the assessee, was lower than the cost of the stock. The assessee explained stating that on account of a scandal that had occurred during the relevant time, the prices of the shares had been fluctuating inordinately and on account of difficulty in ascertaining the true value of the share with the stock market crashing day by day, the assessee resorted to adopt the price at which the stock was sold in the first month of the

subsequent financial year. The Assessing Officer rejected the contention raised by the assessee as regards the method of valuation and ascertained the market value of the stock as on 31.03.2000 from the website of the National Stock Exchange and determined the market value of the closing stock at Rs.13,43,22,426/-.

8. Aggrieved by the same, the assessee filed appeal before the Commissioner of Income Tax (Appeals)-II ("the CIT(A)" for brevity) reiterating the stand that the "since realised value" is an approved method of valuation. In this regard, the assessee referred to Accounting Standard No.2, Item No.5 (iv), which defines net realisable value to mean actual/estimated selling price. The CIT(A), by order dated 15.12.2006, rejected the contention advanced by the assessee and held that the valuation of the closing stock would have to be on "cost" or "market" basis and accordingly adopted the cost of the closing of stock at Rs.11,52,00,401/-, which was lower than the market value of the stock as on 31.03.2000, i.e., Rs.13,43,22,426/-. Consequently, the addition was reduced from Rs.6,96,85,741/- to Rs.5,05,63,716/-.

9. Aggrieved by such order, the assessee preferred appeal to the Tribunal. The Tribunal agreed with the findings of the CIT(A) and in doing so, held that the assessee cannot re-write his accounts on the basis of the events that occurred after the finalization of the same. Accordingly, the Tribunal held that the valuation of the closing stock would have to be made on the basis of "cost" or "market" value, whichever is lower. Aggrieved by the same, the assessee is before us by way of this appeal.

10. We have heard Ms.Sree Lakshmi Valli, learned counsel for the appellant/assessee and Mr.T.Ravi Kumar, learned Senior Standing Counsel for the respondent/Revenue.

11. The assessment order dated 31.03.2006, is sort of unique in its narration. We say so because, the Assessing Officer has posed certain questions to the authorized representative of the assessee, culled out answers from him and the assessment order proceeds on a question-answer basis.

12. Be that as it may, we are required to decide the question as to whether the assessee was justified in valuing the closing stock of shares on the basis of "since realised value", which according to the assessee is the value actually realised by the assessee on the sale of the stock during the first month after the end of the financial year.

13. The sum and substance of the finding of the Assessing Officer in his lengthy 24 pages order is that the assessee deliberately valued the closing stock of his stock of shares for the year ending 31.03.2000 by adopting an unconventional method of accounting of valuation only to reduce the value of

closing stock and the profit for the year ending 31.03.2000. According to the Assessing Officer, the method of valuation, adopted by the assessee, is wholly impermissible in the light of the following decisions:-

(i) CIT vs. Kamani Metals and Alloys Ltd., (1994) 208 ITR 1017 (Bom.);

(ii) CIT vs. Tamilnadu Sugar Corpn. Ltd., (2004) 265 ITR 0466 (Madras); and

(iii) K.Mohammed Adam Sahib vs. CIT, (1965) 56 ITR 0360 (Mad.).

14. After referring to the above decisions, the Assessing Officer observed that the assessee is even entitled to valuation of stock at NIL following the principle of "cost price" or "market price", whichever is less, provided that there is no market for the goods/stock as on the date of balance sheet. It further held that it is not the case of the assessee that there was no market for the shares held by him as on 31.03.2000 and the shares were freely traded in the market. Thus, he concluded that for income tax purposes, the Assessing Officer is required to ascertain the profit for a particular financial/assessment year and not for any other period and hence, it is necessary that the value of closing stock needs to be taken as on the date of balance sheet, following the principle of "market price" or "cost price", whichever is less to arrive at the correct profit earned by the assessee in any financial/assessment year. With these observations, the Assessing Officer adopted the market value of the shares and accordingly, made the addition.

15. On appeal before the CIT(A), while agreeing with the assessee that a business man dealing in shares has right to do prudential accounting particularly, in a crashing market, held that the assessee cannot re-write his accounts on the basis of events happening after the date of finalization of accounts and the assessee having adopted the value of the closing stock on the basis of actual sale made in the subsequent year, re-writing his accounts, and this is not permissible as per the principle of accountancy or under taxation law. Thus, the CIT (A) agreed with the Assessing Officer on the above lines but, chose to adopt the cost of the closing stock instead of the market value, as it was lower than the market value. The Tribunal while affirming the order passed by the CIT(A), agreed with the assessee's stand that a business man dealing in shares, does have a right to do prudential accounting but, cannot re-write his accounts.

16. Thus, we have to consider as to whether the valuation of the closing stock, based on the realised price disclosed in the P & L account, is permissible; and whether the authorities below and the Tribunal were right in coming to the conclusion that the method of accounting adopted by the assessee, is an unconventional method of accounting and an attempt to re-write his accounts.

17. In terms of Section 145(2) of the Act, the Central Government may notify in the Official Gazette accounting standards to be followed by any class of assessee or in respect of any class of income.

17.1. Section 145A of the Act commences with a non obstante clause stating that notwithstanding anything to the contrary contained in Section 145, the valuation of purchase and sale of goods and inventory for the purposes of determining the income chargeable under the head "Profits and gains of business or profession" shall be in accordance with the method of accounting regularly employed by the assessee.

18. In the case on hand, the Assessing Officer as well as the CIT(A) have faulted the assessee in not adopting a uniform method of accounting. However, one important factor, what has been lost sight of by the Assessing Officer is that the assessment year in question is the first year of the assessee's business in stock.

19. In our considered view, this fact assumes importance and therefore, the authorities were not justified in making an observation that the assessee was adopting different methods of accounting for different assessment years. In this regard, we may note Clause No.31 of Valuation of Inventories (AS-2) issued by the council of Institute of Chartered Accountants of India. The said Clause states that consistency is generally accepted as a fundamental accounting assumption and any change in the accounting policy relating to inventories, which has a material effect in the current period or which is reasonably expected to have a material effect in later periods should be disclosed. It further states that in the case of change in accounting policy, which has material effect in the current period, the amount by which any item in the financial statements is affected by such change should also be disclosed to the extent ascertainable and where such amount is not ascertainable, wholly or in part, the fact should be indicated.

20. As pointed out earlier, the year under question was the first year of business of the assessee trading in shares and stocks and therefore, the question maintaining a consistent accounting standard or that there was any inconsistency, cannot arise. Therefore, such finding by the authorities needs to be eschewed.

21. Accounting Standard-4 (AS-4) issued by the council of Institute of Chartered Accountants of India pertains to contingencies and events occurring after the balance sheet date. Contingency has been defined in sub-Clause 3.1 of AS-4 to mean a condition or situation, the ultimate outcome of which, gain or loss, will be known or determined only on the occurrence, or non-occurrence, of one or more uncertain future events.

21.1. Sub-Clause 3.2 deals with events occurring after the balance sheet date and it states that those are significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are approved by the Board of Directors in the case of a company and two types of events have been identified viz., (a) those that provide future evidence of conditions that existed at the balance sheet date; and (b) those that are indicative of conditions that arose subsequent to the balance sheet date.

22. In the Explanation, Clause 4 explains contingencies and in terms of sub-Clause 4.1, it is stated that the term "contingencies" used in AS-4 is restricted to conditions or situations at the balance sheet date, the financial effect of which is to be determined by future events, which may or may not occur.

23. Sub-Clause 4.2 states that estimates are required for determining the amounts to be stated in the financial statements for many on-going and recurring activities of an enterprise. However, one must distinguish between an event, which is certain and one which is uncertain.

23.1. Sub-Clause 4.3 states that uncertainty relating to future events can be expressed by a range of outcomes.

23.2. Clause 5 deals with accounting treatment of contingent losses.

23.3. Sub-Clause 5.1 states that the accounting treatment of a contingent loss is determined by the expected outcome of the contingency and if it is likely that a contingency will result in a loss to the enterprise, then it is prudent to provide for that loss in the financial statements.

23.4. Clause 8 deals with events occurring after the balance sheet date and it contains six sub-clauses viz., sub-clauses 8.1 to 8.6 and all of other provide for contingencies which may indicate need for adjustments to the assets and liabilities as at the balance sheet date.

23.5. Sub-Clause 8.2 gives an illustration regarding adjustment to be made for a loss on a trade receivable account, which is confirmed by the insolvency of a customer, which occurs after the balance sheet date.

23.6. Sub-Clause 8.3 gives an illustration of decline in market value of investments between the balance sheet date and date on which the financial statements are approved.

24. Reverting back to valuation of inventories (AS-2), in sub-clause 6.9, net realisable value has been defined to mean the actual/estimated selling price in the ordinary course of business, less cost of completion and cost necessarily to be incurred in order to make the sale.

25. The assessee's case is that what has been shown in their books of accounts is the actual price which the assessee realised on the sale of the stock and the assessee has shown the same as 'since realised price', which is nothing but, net realised value as defined in sub-clause 6.9 of AS-2.

26. In Section 17 of AS-2, which falls under the chapter "valuation of inventories below historical cost", it is stated that the historical cost of inventories may at times not be realised e.g., if their selling prices have significantly declined, or if they become wholly or partially obsolete, or if the quantity of inventories is so large that it is unlikely to be sold/utilized, within the normal turnover period and in such circumstances, it becomes necessary to write down the inventory to 'net realisable value', in accordance with the principle of conservatism which requires that current assets should not be carried in the financial statements in excess of amounts expected to be realised in the ordinary course of business.

27. While discussing about the accounting standard, we may also refer to two notifications issued by the Income Tax Department in Notification Nos.9949 [F.No.132/7/95-TPL]/SO 69 (E) and 31/2018: dated 25.01.1996 and 31.03.2005 respectively, issued in exercise of the powers conferred under sub-Section (2) of Section 145 of the Act notifying the accounting standard to be followed by all assessees operating mercantile system of accounting.

28. Clause 4 of the said notification states that accounting policies adopted by an assessee should be such so as to represent a true and fair view of the state of affairs of the business, profession or vocation in the financial statements prepared and presented on the basis of such accounting policies. It identifies 3 major considerations governing the selection and application of accounting policies, viz., (i) prudence; (ii) substance over form; and (iii) materiality. Thus, in terms of what has been said in sub-Clauses 4(i) and 4(ii) of the notification, provisions should be made for all known liabilities and losses even though the amount cannot be determined with certainty and represents only a best estimate in the light of the available information; and the accounting treatment and presentation in financial statements of transactions and events should be governed by their substance and not merely by the legal form.

29. The Revenue seeks to sustain the orders passed by the authorities as confirmed by the Tribunal by reiterating the observations contained therein and placing strong reliance on the decisions in the case of Kamani Metals and Alloys Ltd., (supra); Tamilnadu Sugar Corpn. Ltd., (supra); and CIT vs. British Paints India Ltd., (1991) 54 Taxman 0499.

30. In Kamani Metals and Alloys Ltd., (supra), one of the questions which came up for consideration, was whether the replacement cost for the purpose of valuing a closing stock for the year ended 31.03.1974 has to be determined with reference to the price announced for the quarter ended 31.03.1974 and not with reference to the price announced for the quarter commencement on 01.01.1973. The Hon'ble High Court of Bombay upheld the order of the Tribunal holding that the closing stock has be valued on the last date of the accounting year which in the said case was 31.12.1974 and the price of the raw material on that date was the same as the price prevailing on the date of purchase and the change took place only after the end of the accounting year i.e., on 01.01.1975 and such change cannot affect the valuation of the closing stock on 31.12.1974.

31. In our considered view, the facts of the case in Kamani Metals and Alloys Ltd., (supra) are entirely different from that of the assessee's case. The assessee's case rests upon the actual sale price realised by him on the sale of his stock in the first month of the next financial year. Therefore, we are of the considered view, the decision in Kamani Metals and Alloys Ltd., (supra) cannot in any manner assist the case of the Revenue.

32. The next decision relied on by the Revenue is the case of Tamilnadu Sugar Corpn. Ltd., (supra). The question, which was considered by the Hon'ble Division Bench of this Court, was whether the assessee was entitled to adopt the value of its closing stock at a rate which was prevalent on 25th October 1983 whereas its previous year ended on 30.09.1983. While answering the question, the Court held that the assessee has not adopted the valuation of closing stock of sugar at the end of the accounting period when it made up its accounts and therefore, the assessee is not entitled to value the closing stock on the date when its accounts are prepared and finalized, and if the assessee is permitted to adopt such a system, then the profit of the accounting year would not be reflected and a portion of the profit, which was earned in one year, would be shifted to next year. This finding cannot be applied to the facts of the assessee's case. However, in paragraph 12 of the same judgment, the Division Bench pointed out that the correct principle of accounting is to enter the stock in the books of account at cost unless the value is required to be reduced by the fall in the market price of the goods at the end of the accounting year. We bear in mind this observation made by the Division Bench.

33. The third decision, relied on by the Revenue is the case of British Paints India Ltd., (supra). Paragraph 10 of the said judgment was referred to, which reads as follows:-

"10. Where the market value has fallen before the date of valuation and, on that date, the market value of the article is less than its actual cost,

the assessee is entitled to value the articles at market value and thus anticipate the loss which he will probably incur at the time of the sale of the goods. Valuation of the stock-in-trade at cost or market value, whichever is the lower, is a matter entirely within the discretion of the assessee. But whichever method he adopts, it should disclose a true picture of his profits and gains. If, on the other hand, he adopts a system which does not disclose the true state of affairs for the determination of tax, even if it is ideally suited for other purposes of the business, such as the creation of reserve, declaration of dividends, planning and the like, it is the duty of the Assessing Officer to adopt any such computation as he deems appropriate for the proper determination of the true income of the assessee. This is not only a right but a duty that is placed on the officer, in terms of the first proviso to s. 145, which concerns a correct and complete account, but which in the opinion of the officer, does not disclose the true and proper income.

34. On a plain reading of the above decision, we are of the view that it supports the case of the assessee. What is required by the assessee to do is to disclose a true picture of his profits and gains and it is the duty of the Assessing Officer to adopt the computation as he deems appropriate for the proper determination of the true income of the assessee. Equally, the observations in paragraph 16 would also enure in favour of the assessee, which is as follows:-

"16.The IT Act does not contain any specific provision for the valuation of stock. Income, profits and gains, must however, be computed in the manner provided by the Act. It is the duty of the officer to determine the profits and gains of a commercial venture according to the correct principle of accounting. In doing so, he might, dependent on the nature of the business and its special character, allow certain adjustments but his primary purpose and duty is to deduce the correct income, profits and gains, and this he cannot do without taking into account the value of the stock-in-trade at the beginning and at the end of the year and by ascertaining the difference between them."

35. Mr.T.Ravi Kumar, learned Senior Standing Counsel placed reliance on the decision of the Hon'ble Supreme Court in CIT vs. Woodward Governor India P. Ltd., [2009] 312 ITR 254 (SC). This decision has been pressed into service to explain that profits and gains of the previous year are required to be computed in accordance with the relevant accounting standard and the basis on which stock-in-trade was valued is part of

the method of accounting and it is well established that, on general principles of commercial accounting, in the profit and loss account, the values of stock-in-trade at the beginning and at the end of the accounting year should be noted at the cost or market value, whichever is lower-the market value being ascertained as on the last date of the accounting year and not as on any intermediate date between the commencement and the closing of the year, failing which it would not be possible to ascertain the true and correct state of affairs. The above decision lays down the legal principle which needs to be adopted not only by the assessee but, also the Revenue as well.

36. Thus, the question, which looms large for consideration is whether the assessee should be precluded from reflecting the actual realised cost of share and should a figure which obviously does not match with the sale price realised, be relied on for the purpose of making the amount addition.

37. In CIT vs. Birla Gwalior (P.) Ltd., (1973) 89 ITR 0266, the assessee had foregone an agency commission, which was claimed as a revenue expenditure. While testing the correctness of the order of the Tribunal, which allowed the same as revenue expenditure under Section 10(2)(xv) of the Act, the Court examined the manner of accounting system adopted by the said assessee. The assessee therein adopted mercantile system of accounting and it gave up the agency commission after the end of the financial year. The Revenue contended that the commission had accrued before it was given up and therefore, the assessee cannot state that they had not earned commission in question. The Revenue's contention was rejected by the Hon'ble Supreme Court holding that the commission receivable could have been ascertained only after the managed company made up its accounts, the assessee had given up the commission even before the managed company made up its accounts and merely because the assessee-company was maintaining its accounts on the basis of mercantile system cannot lead to the conclusion that the commission had accrued to it by the end of the relevant accounting year. In support of such finding, reference was made to the decision of the Bombay High Court in H.M.Kashiparekh & Co. Ltd. vs. CIT reported in (1960) 39 ITR 706 (Bom.). In the said decision, it was pointed out that it was the real income of the assessee-company for the accounting year that was liable to tax and that the real income could not be arrived at without taking into account the amount foregone by the assessee. It was further pointed out that in ascertaining the real income, the fact that the assessee followed the mercantile system of accounting did not have any bearing. Further, the accrual of the commission, the making up of the accounts, the legal obligation to give up part of the commission, and the forgoing of the commission at the time of making up of the accounts were not disjointed facts; they were dovetailing about them

which could not be ignored. The Court also referred to the concept of real income, which was expounded in the decision of the Bombay High Court in H.M.Kashiparekh & Co. Ltd. (supra), and explained in the following terms:-

"The principle of real income is not to be so subordinated as to amount virtually to a negation of it when a surrender or concession or rebate in respect of managing agency commission is made, agreed to or given on grounds of commercial expediency, simply because it takes place some time after the close of an accounting year. In examining any transaction and situation of this nature the Court would have more regard to the reality and speciality of the situation rather than the purely theoretical or doctrinaire aspect of it. It will lay greater emphasis on the business aspect of the matter viewed as a whole when that can be done without disregarding statutory language."

38. As could be seen from the facts of the above case, the commission was foregone after the closing of the balance sheet yet the Court pointed out that the reality and speciality of the situation should be given due regard rendering pure theoretical or doctrinaire aspect.

39. In CIT vs. Shoorji Vallabhdas & Co. reported in (1962) 46 ITR 0144 (SC), the question was whether two sums are income of the assessee for the previous year ended 31.03.1948. While answering the said question, it was pointed out that a mere book-keeping entry cannot be income, unless income has actually resulted, and where lesser income is actually received consequent to a subsequent agreement, only that part is taxable and not the entire income accounted in the books. Therefore, in our considered view, if the stand taken by the Revenue before us has to be accepted, it would be fallen foul of the law laid down by the Hon'ble Supreme Court in Shoorji Vallabhdas & Co. (supra).

40. In the case of CIT vs. Mahalaxmi Sugar Mills Co. Ltd. reported in (1993) 200 ITR 0275, the assessee reduced the closing stock in respect of the stock earmarked for export on the ground that it was constrained to earmark for export the sugar at prices lower than the market rate, the value of such closing stock was lesser than the aforesaid amount. The Assessing Officer did not accept the contention of the assessee and added back the said sum to the adjusted value of the closing stock shown by the assessee. The assessee was unsuccessful before the first appellate authority and carried the matter to the Tribunal. The Tribunal allowed the assessee's claim by examining the documents and found that the loss, in fact, was incurred and this is allowable as a deduction. The Tribunal pointed out that the method of valuation of the closing stock, which was adopted by the

assessee, was that it would not take the value of the closing stock on the last date of the accounting year but, it took the estimated realisable market value by adopting the price of sugar subsequently realised or realisable before the balance sheet for the year in question was adopted. The Tribunal found this method to be scientific and accordingly, allowed the assessee's appeal. On appeal by the Revenue before the High Court of Delhi, it was pointed out that the assessee had actually suffered a loss in the sale of sugar in the local market and any loss, which is suffered in connection therewith has necessarily to be recorded as loss, which is incidental to the business. Before the Court, the Revenue placed reliance on the decision in British Paints India Ltd., (supra), and contended that the principle of valuation of stock should be valuation at cost or market value, whichever is lower on the closing date and a different principle like the one followed by the assessee therein cannot be correct method of valuing the closing stock.

41. Referring to the decision in British Paints India Ltd., (supra), it was pointed out that the Court no doubt held that the ITO is not bound to accept a system of accounting merely because it is regularly employed by the assessee. However, the system, which was adopted by the assessee must disclose the true state of affairs for determination of tax, if correct profits and gains could be deduced from the accounts as maintained by the assessee, then the ITO was to accept the same if the said system was being regularly employed. It was held that what was the profit of a trade or business is a question of fact and it must be ascertained, as all facts must be ascertained with reference to the relevant evidence and not on doctrines or theories.

42. Referring to the valuation of closing stock adopted by the said assessee, the Court held that the system of valuing the closing stock with reference to selling price, subsequent to the last date of the accounting year has been consistently followed by the assessee and it has not been held by the IT Authorities that correct profits and gains could not be deduced from the accounts so maintained. Approving the finding of the Appellate Authority in the assessee's case for the earlier assessment year, it was held that the method adopted by the assessee is in fact, nearer to the reality of the fact and as such could be treated as a correct and perfect method of valuation.

43. In our considered view, the decision in Mahalaxmi Sugar Mills Co. Ltd. (supra) would squarely apply to the case on hand. The Assessing Officer or the CIT(A) does not dispute the fact with regard to the loss suffered by the assessee. We say so after going through the factual matrix of the case, nor such a contention was advanced before us by the Revenue.

44. The Revenue hinges upon the only issue that the correct method of valuation of closing stock should be the cost or market value, whichever is lower on the closing stock. However, one cannot ignore the fact that the assessee is duty bound to disclose the true state of affairs for determination of the tax and if correct profits and gains could be deduced from the amounts maintained by the assessee, the Assessing Officer cannot accept the same. In doing so, in the instant case, we are required to examine the relevant evidence and not confine ourselves to doctrines or theories.

45. The other contention of the Revenue is that the assessee was not consistent with his accounting standards. We do not agree with the said submission because, the assessee has been maintaining mercantile system of accounting for all the assessment years subsequent to the year under consideration. Noteworthy, the year under consideration is the first year of business of the assessee in trading of stocks and shares. Thus, the Revenue is not justified in rejecting the assessee's stand on the ground of inconsistency. At best, the Revenue can pitch its case on the ground that the closing stock cannot be valued as done by the assessee.

46. From the aforementioned decision, it is clear that what is required to be ascertained is what was the profit of the trade or business which essentially is a question of fact and this has to be decided with reference to the relevant evidence, which was provided by the assessee.

47. In the case of Commissioner of Income Tax vs. Delta Plantation Ltd. reported in (1993) 71 Taxman 0329, the question which fell for consideration, was whether the addition made by the Assessing Officer on account of undervaluing of closing stock was justified. The assessee therein was engaged in the business of cultivation, manufacture and sale of tea. The assessee used to value its closing stock of tea at the end of each year at selling price and from the year 1981, it decided to change its basis of valuation of stock of tea and started valuing it at "since realised price" or the "estimated realisable value". The Assessing Officer did not allow the change in method of valuation of stock of tea at the end of the previous year and added back the resultant loss. Before the CIT(A), the assessee contended that the stock valuation adopted by them was a normal practice followed in the entire tea industry for valuation of stock of tea at the end of the accounting year and there was no reason why the Assessing Officer should refuse to accept the change in method of stock valuation followed by the assessee. The CIT(A), while holding that the assessee was at liberty to change the method of valuation of closing stock, held that it cannot be allowed, if it results in loss of Revenue, and accordingly, confirmed the order of the Assessing Officer.

48. On appeal to the Tribunal, the assessee succeeded, which order was questioned by the Revenue before the High Court of Calcutta. The Court referred to the accounting standard more particularly, AS-2 on valuation of inventories and held that the assessee has changed its method of stock valuation from "selling price" to "since realised price" and/or "estimated realisable value", which is nothing but, "net realisable value". It was pointed out that what is relevant to consider is whether the method adopted is one of the recognised methods and further, whether the changed method of stock valuation is followed consistently year after year. Further, it was pointed out that the change of method must be bona fide and must not be restricted to a particular year.

49. In the instant case, the bona fide of the assessee has not been questioned by the Assessing Officer. No doubt true that such procedure was not followed earlier or later than the assessment year under consideration and this is so because, the assessment year under consideration is the first year of business. The other aspect which the assessee had stated is regarding the fluctuation in the market on account of a scam which had occurred during the relevant time. The figures speak for themselves and they indicate the loss sustained by the assessee.

50. Further, from the assessment order, it is seen that for the subsequent year also, the assessee had generated huge loss from the share business and has settled all such loans from other incomes in various years. Thus, we are of the clear view that the 'since realised price', as adopted by the assessee, is the price realised by the assessee upon its sale and taking note of the law laid down in the aforementioned decisions, we hold that the method of valuation of the closing stock adopted by the assessee cannot be stated to be lacking in bona fides and the value adopted by the assessee is the value realised by the assessee upon sale of the share and such contingencies are clearly covered in Clause 8 of AS-4, which deals with events occurring after the balance sheet date.

51. In the light of the above discussion, we are of the clear view that the order passed by the Tribunal calls for interference. In the result, the appeal, filed by the assessee, is allowed, the orders passed by the Tribunal and the authorities below are set aside and the substantial questions of law, framed for consideration, are answered in favour of the assessee. No costs.

Sd/-
Assistant Registrar (CS-VIII)

//True Copy//

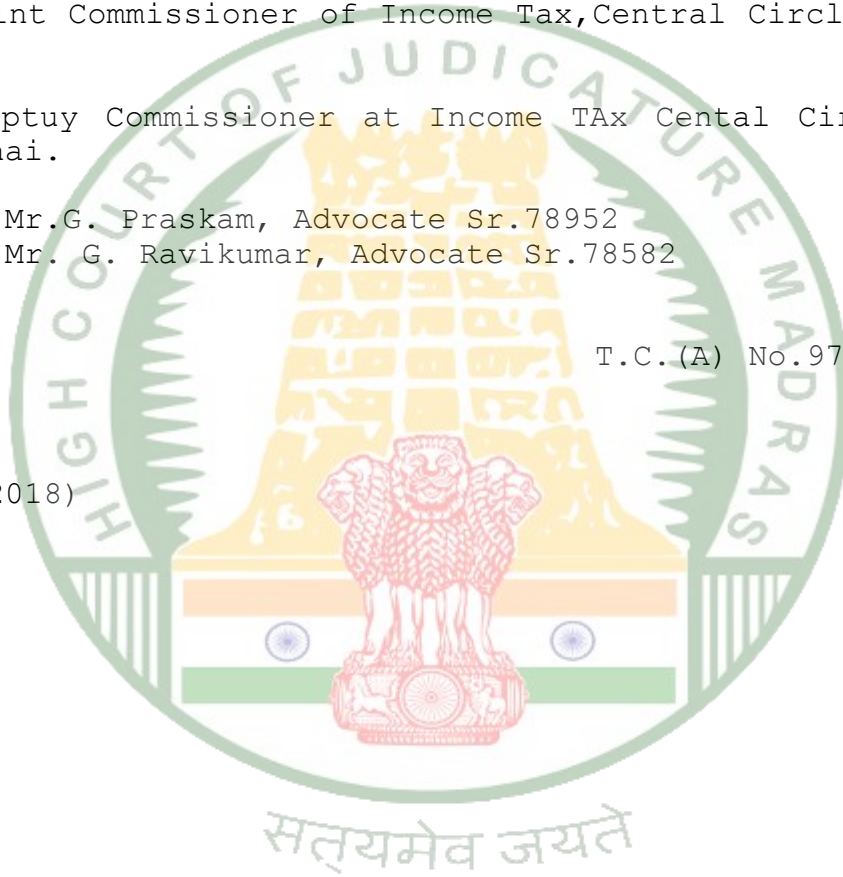
Sub Assistant Registrar

To

1. The Income-tax Appellate Tribunal Chennai Bench "B"., Chennai.
 2. The Commissioner of Income Tax, (Appeals)-II, Chennai.
 3. The Joint Commissioner of Income Tax, Central Circle-III, (B) Chennai.
 4. The Deputy Commissioner at Income Tax Central Circle IIII (A), Chennai.
- + 1 cc to Mr. G. Praskam, Advocate Sr.78952
+ 1 cc to Mr. G. Ravikumar, Advocate Sr.78582

T.C.(A) No.979 of 2008

CP(CO)
EU(06/12/2018)



WEB COPY