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IN THE INCOME TAX APPELLATE TRIBUNAL
(DELHI BENCH 'D' : NEW DELHI)

BEFORE SHRI U.B.S. BEDI, JUDICIAL MEMBER
and
SHRI B.C. MEENA, ACCOUNTANT MEMBER

ITA No.3816/Del./2011
(ASSESSMENT YEAR : 2008-09)

Luxor Writing Instruments Pvt. Ltd., 5, Okhal Industrial Estate, Phase – III, New Delhi. **(PAN : AAACL1980D)**	vs.	DCIT, Circle 4 (1), New Delhi.
(APPELLANT)		(RESPONDENT)

ASSESSEE BY : Shri Sanjay Kalra, CA
REVENUE BY : Ms. Y. Kakkar, DR

ORDER

PER B.C. MEENA, ACCOUNTANT MEMBER :

This appeal filed by the assessee emanates from the order of CIT (Appeals)-VII, New Delhi dated 14.06.2011 for the assessment year 2008-09.

2. The assessee company is engaged in the business of manufacture and sale of writing instruments. During the relevant assessment year, the assessee has changed the method of valuation of stock. Due to the change in the method of valuation of stock, the income of the assessee has been returned lesser by Rs.11,60,494/-. The Assessing Officer asked the explanation of the assessee and found it unacceptable and held that according to the provisions of section 145A of the Income-tax Act, 1961, for valuation of inventory, the method to be adopted is the method of accounting regularly employed by the

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assessee. The assessee company had changed its method of valuation of inventory which is not allowed under the provisions of section 145A and he made an upward adjustment in the income of the assessee of Rs.11,60,494/-.

3. The assessee filed the appeal on this issue before the CIT (A) and the CIT (A) has confirmed the addition by holding as under :-

> "4.2 In view of these circumstances, I am of the considered view that the addition of Rs.11,60,494/- on account of valuation of closing stock in terms of section 145A of the Act was rightly made by the Assessing Officer. As a result, Ground of appeal No.2 is dismissed."

4. The grounds of appeal read as under :-

> "1. That the order of Commissioner of (Appeals) is contrary to law and the facts of the appellant's case insofar as it relates to method of accounting.
>
> 2. That CIT (Appeals) erred in ignoring the facts that the assessee Company continues to value the Stock at cost or net realizable value whichever is less, as was being done earlier. Shifting to a new ERP package i.e. SAP for improvement in working in a more scientific method which values the stock at cost but takes moving average method to arrive at cost does not amount to change in method of valuation of stock of change in accounting not allowable U/s 145A of the Income Tax Act. The same basis has been adopted in subsequent years as well. The Ld. CIT is incorrect in holding that once a method is taken it can't be changed at all. 'Regular' doest not mean permanent. 'Relied on – CIT v. Punjab State Industrial Development Corpn. Ltd. [2002] 255 ITR 351 (Punj. & Har.). He has tried to limit adaptation of innovative and Scientific method in accounting which is never the intention of law.
>
> 3. The AO has incorrectly disallowed Rs.11,60,494/- and CIT (Appeal) has wrongly confirmed the disallowance.
>
> The appellant craves leave to add to or amend the aforesaid grounds before disposal of the appeal."

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5. The only issue involved in the appeal is sustaining the addition on account of change in accounting method of valuation of stock.

6. Ld. AR submitted that as per the provisions of section 145A (a)(i) of Income-tax Act, the inventory valuation has to be done as per method of accounting regularly employed by the assessee. Assessee company continues to value the stock at cost or net realizable value whichever is less. The assessee has followed this method of valuation regularly. The provisions of section 145A nowhere bars the assessee from changing the method of valuation it only lays down the criteria that it has to be followed regularly, for example, in subsequent years as well. The assessee should not make it a practice to change in the method of valuation of and on. It has to be bonafide and frequently followed. Assessee had shifted to new EPR Package : SAP for improving the working in more scientific method. In a sense, the assessee has changed its method of valuation of finished goods from historical (Direct) cost to weighted moving average basis as it installed a better or more scientific ERP package of accounting known as SAP which is more precise, accurate and scientific . SAP follows Weighted Moving Average Basis of valuation of inventory than Historical Cost (Direct Cost) or FIFO method. Both the cost are prescribed method for valuation of stock, as held in CIT vs. Amrithalakshmi – 163 Taxman 467 (HC). He further pleaded that both Direct Cost (FIFO) or weighted moving average method are recognized in

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Accounting Standard 2 (AS-2) prescribed by ICAI and accepted by Income-tax Act in Section 145 in Method of Accounting. AS-2 in para 16 states as under :-

> "16. The cost of inventories, other than those dealt with in paragraph 14, should be assigned by using the first-in, first-out (FIFO), or weighted average cost formula. The formula used should reflect the fairest possible approximation to the cost incurred in bringing the items of inventory to their present location and condition."

He pleaded that as per this, the assessee has a choice to value the stock at cost either by following FIFO or weighted average cost formula. To arrive at the valuation with both these methods is known as cost. Therefore, the basic fundamental of accounting, i.e. the valuation of inventory should be at cost or net realizable value whichever is lower is met and if one follows either of these there is no change in method of valuation. Therefore, the basic fundamental of accounting for valuing inventory at cost or net realizable value whichever is less is met if anyone of either is followed. There will be no change in the method of valuation. He pleaded that various courts had held that bonafide change of method is permissible. He pleaded that the assessee must alter his regular method, he must abandon what up to that time was his regular method and start a new regular method and not merely a new method for a casual period. For this proposition, he relied on the decision of Sarupchand vs. CIT – (1936) 4 ITR 420 (Bom.). He pleaded that once the assessee changed the method of accounting and satisfies the department that

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he intends to adopt changed method of accounting thereafter and he has in fact adopted it thereafter, that will satisfy the requirement of section 145. Neither principle nor authority bars an assessee from substituting one method of accounting for another. A change in the method of valuing closing stock under such circumstances does not entail a rejection of the method of the assessee's choice or the application of the First Proviso to Section 145 (1) and learned AR relied on the following case laws :-

(i) Indo-Commercial Bank Ltd. vs. CIT - (1962) 44 ITR 22;
(ii) Forest Industries Travancore Ltd. v CIT - (1964) 51 ITR 329 (Ker);
(iii) New Victoria Mills Co. Ltd. vs. CIT - (1966) 61 ITR 395 (All);
(iv) Dr. Ishwari Prasad vs. CIT - (1983) 143 ITR 789 (All);
(v) CIT vs. Shriram Associated Bearing (P) Ltd. - (1984) 150 ITR (St.) 77 (SC);
(vi) CIT vs. Hind Lamps Ltd. - (1987) Taxation 85 (3)- 225 (All);
(vii) CIT vs. Mopeds India Ltd. - (1988) 173 ITR 347, 350 (AP);
(viii) CIT vs. Bikaner Trading Co. - (1989) 180 ITR 286 (Cal)
(ix) Hollungooree Tea Co. - (1991) 192 ITR 126 (Cal)

He also submitted that in respect of the basis adopted for valuation in the earlier years, the assessee has the option to change the method of valuation of the closing stock at cost or market price, whichever is lower, at any time provided the change was bonafide and followed regularly thereafter. For this, he relied on the following case laws :-

(i) CIT vs. Corporation Bank Ltd. - (1988) 174 ITR 616, 620 (Karan);
(ii) CIT vs. Dalmla Cement (Bharat) Ltd. - (1995) 215 ITR 441, 445 (Del.), Page 89-91.

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Once having so changed the method of accounting, if the assessee continued with the changed method, it becomes his regularly employed method within the meaning of section 145 (1) and the Assessing Officer is bound to base his assessment on the changed method provided that income can properly be deducted from such method. If, however, the changed method is not followed regularly by the assessee, the taxing authority cannot fall back upon the earlier method of accounting. This is so because in such a case it cannot be said that the assessee had followed the earlier method regularly in view of the intermediary changed method of accounting. Such a case will be a case falling under section 145 (2) where no method of accounting has been regularly employed by the assessee, entitling the assessing authority to make an assessment in the manner provided in section 144. For this proposition, he relied on the decision of Reform Flour Mills (P) Ltd. vs. CIT – 114 ITR 227 (Cal.). Learned AR further pleaded that in view of this, where it is found that an assessee has changed his regular method of accounting by another recognized method and has followed the latter method regularly, thereafter, it is not open to the revenue authorities to go into the question of bonafides of the introduction and continuance of the change. For this, he relied on the decision of Snow White Food Products Co. Ltd. vs. CIT – 141 ITR 861 (Cal.). Learned AR also pleaded that in other words, it cannot be contended that a change has to be supported by cogent reasons showing the bonafides of

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the assessee in so changing the method. For this proposition, he relied on the decision of Snow White Foods Products Co. Ltd. vs. CIT – 141 ITR 847 (Cal.). He also relied on the order of the Hon'ble Delhi High Court in the case of CIT vs. Modi Rubber Limited – 230 ITR 820 (Del.) wherein change in method of valuation was upheld where the Tribunal has found that the changed method adopted by the assessee was a recognized and scientific method and the same was followed regularly for the subsequent years and it was not going to cause any loss to the revenue. He further pleaded that even after the introduction of section 145A, the law only requires the method needs to be followed regularly and it no where states that it cannot be changed under any circumstances. It is not permanent. For this, he relied on the decision of CIT vs. Punjab State Industrial Development Corp. Ltd. – 255 ITR 351 (P&H). He pleaded that the only thing is it needs to follow is year after year. He also pleaded that the method of valuation of inventory changed by assessee and such change was in consonance with AS-2 on valuation of inventories and assessee had followed changed method consistently in subsequent years; such change cannot be questioned on the ground that it had resulted in inventory being shown at lower value. For this, he relied on the decision of Indo Rama Synthetics Ltd. – [2009] 180 Taxman 35 (DLH). He finally pleaded that in the assessee's case, there was no change of method of closing stock. The assessee has always followed the method of valuation

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which is known as 'Cost or Net Realizable Value wherever is lower'. The assessee was valuing its inventory at cost by FIFO method earlier and now the assessee is adopting the other method of arriving at cost by method of weighted moving average cost method. Therefore, there was no change in the method of assessee. He also relied on the decision of ITAT, Mumbai Bench in Sahara India Mass Communication Ltd. vs. ACIT in ITA No.522/Mum./2006 dated 28th April, 2011 for the proposition that change in method of stock valuation is permitted provided it is regularly followed. Finally, he pleaded that the decision of ITAT, Delhi Bench in the case of Ajanta Raj Proteins Ltd. – [2009] 124 TTJ 914 (Del.) is not applicable to the assessee's case as in that case Tribunal dealt with the change of method of accounting of closing stock which was earlier valued at cost and subsequently valued at net realizable value. Hence, in that case, the method was changed from 'At cost' to 'Net realizable value'. He pleaded that no such circumstances exist in the present case. The assessee continues to value the inventory at cost only. He pleaded to set aside the orders of the authorities below.

7. On the other hand, the learned DR relied on the order of the authorities below and also pleaded that the assessee's claim that the assessee has not changed the method of valuation is completely misplaced. The assessee's auditor has reported in the auditor's report on the accounts of the assessee for

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the year ending 31.03.2008 which has been made in compliance with section 227(2) of the Companies Act, 1956 that they have audited the balance sheet of the assessee as on 31.03.2008 and profit & loss account for the year ended on 31.03.2008 and they have also reported that in their opinion and to the best of their information and according to the explanations given by them, those accounts were subject to the Note which read as under :-

> "During the year the Company has changed its method of valuation of raw material, components and packing material from FIFO (First in First out) to Weighted Moving Average basis. As a consequence the valuation of inventories is lesser by Rs.11,60,494/- and so is the profit" (Refer item "n" in Schedule XIV – Significant Accounting Policies)"

Thus, there was a change in the significant accounting policy which is resulted into reduction in the profit to the tune of Rs.11,60,494/-. Further, he pleaded that the assessee's reliance that only requirement of section 145A is that the method should be followed regularly and here the regular means to be followed in subsequent years also which is also incorrect interpretation of the statute. Section 145A provides the method of accounting in certain cases where the valuation of purchases and sales 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 which made it amply clear that method of accounting regularly employed in the preceding year has to be

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adopted for complying with the requirement of section 145A and the section starts with non-obstante clause which reads as under :-

> "Notwithstanding anything to the contrary contained in section 145A -
>
> (a) 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 -
>
> (i) in accordance with the method of accounting regularly employed by the assessee; and
>
> (ii) further adjusted to include the amount of any tax, duty, cess or fee (by whatever name called) actually paid or incurred by the assessee to bring the goods to the place of its location and condition as on the date of valuation.
>
> Explanation.—For the purposes of this section, any tax, duty, cess or fee (by whatever name called) under any law for the time being in force, shall include all such payment notwithstanding any right arising as a consequence to such payment.
>
> (b) interest received by an assessee on compensation or on enhanced compensation, as the case may be, shall be deemed to be the income of the year in which it is received."

Section 145A was introduced by the Finance (No.2) Act, 1998, w.e.f. 1.4.1999 which has been subsequently amended by Finance (No.2) Act, 2009 w.e.f. 1.4.2010. Learned AR pleaded that the assessee can change the method of valuation but if it reduces the income then the assessee has to compensate for the same in the year in which the method has changed. He also relied on

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the decision of ITAT Delhi Bench in the case of Ajanta Raj Proteins Ltd. – [2009] 124 TTJ 914 (Del.) and pleaded that the facts of case under consideration are similar to the facts of the case of Ajanta Raj Proteins Ltd., cited supra.

8. We have heard both the sides in details. We have also perused the material available on record. The provisions of section 145A were inserted by the Finance (No.2) Act, 1998, w.e.f. 1.4.1999. Prior to the assessment year 1998-99, the entire provisions regarding the method of accounting were contained in section 145 of the Income-tax Act only. As per that section, the income under the head "Profit and gains of business or profession" or "Income from other sources" shall be computed according with either cash or mercantile system of accounting regularly employed by the assessee. In other words, the Act recognizes two system of accounting, cash system of accounting and mercantile system of accounting. The section also provides that the Central Government is authorized to notify from time to time the accounting standard to be followed, particularly in the case of any assessee or in respect of any income. The Central Government has notified certain accounting standards. The Accounting Standard – 2 clause (a) provides that a change in the accounting policy shall be made only if the adaptation of a different policy is required by the statute or if it is considered that the change would result in a mere appropriate preparation or presentation of the financial

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statement of an assessee. The provisions of section 145A start with non-obstante clause. This clause begins with notwithstanding anything contained in section 145. The value of purchase and sale of the goods and inventory for the purpose of determining the income chargeable under the head "Profit and gains of business or profession" shall be in accordance with the method of accounting regularly employed by the assessee. Thus, a non-obstante clause is used as a legislative device to modify the ambit of provision or law mentioned in the non-obstante clause or to override it in the specified circumstances. In view of these, the provisions of section 145A are such provisions which provide that notwithstanding the contrary contention of section 145, the provisions of section 145A will prevail. In other words, there would be some contrary situation when provisions of section 145 could be applied. In case of such contradictions or contrary situations, the provisions of section 145 A will be applied. Thus, the provisions of section 145A will prevail over the provisions of section 145. For the determination of income chargeable under the head "Profits and gains of business or profession", the Act requires assessee to value the stock in accordance with the method of accounting regularly employed by the assessee. Once the method has been chosen it should be employed regularly by the assessee and assessee may not be permitted to change it in the subsequent years. The assessee was regularly employing the method of valuation for valuing the stock at cost or net

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realizable value whichever is less. By shifting to a new ERP package, for example, SAP 2 worked out the value of the stock at cost, any reduction in the valuation of the stock is not permitted in law. The assessee's claim that the regularly employed method means change method should be adopted in subsequent years is also untenable. The regular employed method by the assessee must have been followed in the past years which is continued to be followed in the subsequent years. Considering the totality of the facts of the case and considering the case laws relied upon, we find no fault in the orders of the authorities below.

9. In the result, the appeal of the assessee stands dismissed.

Order pronounced in open court on this 29th day of February, 2012.

Sd/- **(U.B.S. BEDI)** **JUDICIAL MEMBER**	**sd/-** **(B.C. MEENA)** **ACCOUNTANT MEMBER**

Dated the 29th day of February, 2012
TS
Copy forwarded to:
1.Appellant
2.Respondent
3.CIT
4.CIT(A)-III, New Delhi.
5.CIT(ITAT), New Delhi

AR, ITAT
NEW DELHI.