

आयकर अपीलीय अधिकरण, 'बी' न्यायपीठ, चेन्नई।
IN THE INCOME TAX APPELLATE TRIBUNAL
'B' BENCH: CHENNAI

श्री रमित कोचर, लेखा सदस्य एवं
श्री धुव्वुरु आर.एल. रेड्डी, न्यायिक सदस्य के समक्ष
BEFORE SHRI RAMIT KOCHAR, ACCOUNTANT MEMBER AND
SHRI DUVVURU R.L.REDDY, JUDICIAL MEMBER

ITA No.984/Chny/2007
निर्धारण वर्ष / **Assessment Year: 2004-05**

The Asst. Commissioner of -
Income Tax,
Company Circle-I,
Madurai.

v. M/s.Thiagarajar Mills Ltd.,
Kappalur,
Madurai-625 008.

(अपीलार्थी/**Appellant**)

[PAN: AACT 4304 R]
(प्रत्यर्थी/**Respondent**)

Department by
Assessee by

: Mr.A.Sundararajan, Addl.CIT
: Mr.R.Sreenivasan, AR

सुनवाई की तारीख/Date of Hearing

: 18.11.2019

घोषणा की तारीख /Date of Pronouncement

: 05.02.2020

आदेश / ORDER

PER RAMIT KOCHAR, ACCOUNTANT MEMBER:

Briefly stated that the assessee is in business of manufacture and sale of cotton yarn. This is second round of litigation before Income-tax Appellate Tribunal, Chennai (hereinafter called " the tribunal") . In the first round of litigation before tribunal, this appeal filed by Revenue for assessment year 2004-05 was adjudicated by tribunal vide order dated 03.04.2009, which is a common order passed by tribunal for ay: 2002-03 to 2004-05. The assessee being aggrieved by an appellate order passed by tribunal in ITA No. 984/Mds/2007 for ay: 2004-05 filed an appeal u/s 260A of the 1961 Act with Hon'ble Madras High Court admitted as an TCA

No. 1128 of 2009. The Hon'ble Madras High Court was pleased to pass an judgment dated 04.09.2019 , wherein it was held by Hon'ble Madras High Court as under:

"TCA.No.1128 of 2007:

1. *Whether the Appellate Tribunal was right in reversing the order of the first appellate authority and restoring that of the Assessing Officer for excluding receipts arising in the core business and not specified in Explanation (baa) to section 80 HHC?*

2. *Whether the Tribunal was right in directing the Assessing Officer to value the opening stock also on the basis as the closing stock in a case of change in valuation of closing stock which was accepted as bonafide and contrary to the decision of the jurisdictional High Court?*

3. *As far as question arising out of Section 80 HHC(baa) of IT Act, 1961 in the respective appeal is concerned, we are of the view that the issue is pending before the Special Bench of the Tribunal and therefore there is no substantial questions of law to be decided now by us for the present. We therefore, do not find any reason to answer this issue at present.*

4. *As far as variance in valuation of the opening stock and closing stock is concerned, the learned Standing Counsel submitted that while remanding the case back to the Assessing Officer directed adoption of valuation of cost price method with regard to valuation of opening stock on the same manner as the closing stock. He relied on the Judgment by the Division Bench of this Court in M/s.Kadari Ambal Mills Limited Super B-3, Industrial Estate, Madurai vs. Joint Commissioner of Income Tax and another in TCA.No.430 of 2005 dated 20.06.2001 wherein it is stated that the Tribunal is wrong in holding that there must be uniformity in the method of valuation of opening stock as well as the closing stock and further submitted that in a case remand back to the Appellate Tribunal.*

5. *The learned counsel for the Revenue submitted that the relevant Paragraphs 24 and 32 of the order of the Appellate Tribunal, dated 03.04.2009, are quoted below for ready reference :*

" 24. After considering the rival contentions and the materials on record, we note that the assessee has changed the method of valuation of closing stock from the market price to the cost which has reduced the value of the closing stock. As per the accounting standards, the valuation of the stock should be at the cost market price, whichever is less. Therefore, there is no dispute that by adopting the cost price method for valuation of the closing stock, the assessee has followed the principle of accounting standards but at the same time the assessee should have also valued the opening stock on the same basis to maintain the uniformity and to avoid distortion of results. There is no bar in adopting the method of valuation which is bonafide but the method should be adopted for both, opening stock as well as closing stock. We note that the Assessing Officer has not discussed this issue in detail and in our view when the assessee has adopted the cost price method for valuation of the closing stock, then the same method should be adopted for valuation of the opening stock also for the accounting year under consideration. Accordingly, we set aside the orders of the lower authorities, qua this issue and remit the same to the record of the Assessing Officer to decide this issue fresh by doing the valuation of opening stock as well as the closing stock at the cost price method.

32. After considering the rival contentions and the materials on record, we note that sub-section (2) and (3) of Section 14A have been inserted in the statute by the Finance Act, 2006 w.e.f.01.04.2007. These subsections have provided that if the Assessing Officer is not satisfied with the correctness of the claim of the assessee in respect of the expenditure, he shall determine the amount of expenditure incurred in relation to such income in accordance with such method as prescribed. We further note that in the case of *Income Tax Officer vs. Daga Capital Management (P) Ltd.*, supra the Mumbai Special Bench of this Tribunal has held that "subsection (2) and (3) of section 14A are procedural in nature and hence retrospective. Therefore, if the Assessing Officer is not satisfied with the claim of the assessee, he has to determine the expenditure as per the rule 8D of the Income Tax Rules. Accordingly, we set aside the orders of the lower authorities, quash this issue and remit the same to the record of the Assessing Officer to ascertain the expenditure incurred in respect of the dividend income according to the Rules and decide this issue after hearing the assessee."

6. Having considered the submissions made by the learned counsel for the Revenue, we do not find any substantial questions of law arising in respect of the method of valuation and therefore all the appeals may be remanded back to the Tribunal and the learned Tribunal may pass final orders about the valuation of closing stock in accordance with law after considering the decision of this Court cited supra while passing the fresh order. The learned Tribunal upon such remand shall pass a fresh order, within a period of six months from today. The Assessee shall appear before the Tribunal at the first instance without any further notice on 17.10.2019.

7. Accordingly, these Appeals are disposed of. No costs."

1.2 Thus, as could be seen from above judgment, the Hon'ble Madras High Court was pleased to remit the matter back to the file of the Tribunal for adjudication of the issue of valuation of closing stock and that is how now we are seized of this matter.

2. The brief background of the issue is that the assessee was earlier valuing finished stock consistently at market price in preceding years which was accepted by Revenue, while in the year under consideration, the assessee changed the method of valuing finished stock at 'cost or market value whichever is lower' as against valuing the finished stock at 'market value' as was done in earlier years. This led to reduction of closing

stock of finished goods as the same was valued to lower of cost or market price , as against method of valuing stock of finished goods at market price in the earlier years. The assessee, however, valued opening of stock of finished goods at 'market price' which was method adopted for valuing stock of finished goods in earlier years. The AO accepted said change of method of valuing stock of finished goods but the AO was of the view, the same changed method be applied to opening stock of finished goods as well which led to additions to the tune of Rs. 47,45,000/- being made by AO while framing assessment u/s 143(3) of the 1961 Act , vide assessment order dated 29.12.2006 . The matter travelled to learned CIT(A) who was pleased to delete the additions made by the AO vide appellate order dated 23.01.2007 passed by learned CIT(A), by holding as under:

7.3. I have carefully considered the facts and circumstances. The appellant was obliged to make change in its method of valuation of stock as per the Accounting Standard of the Institute of Chartered Accountants of India and section 145 of the Income Tax Act, which makes it mandatory for companies to follow the Accounting Standards. The change was bona fide. Moreover the reduction profit during this year will be made good in the following year. Therefore, following the principles laid out by the Supreme Court in the case referred supra, I find that the appellant is entitled to re-compute his profit by following the changed method of valuation of closing stock. The addition of Rs. 47,45,000 is hereby deleted. This ground is allowed.

3. The Revenue being aggrieved filed appeal with the tribunal, which in the first round of litigation was allowed by the tribunal and the issue was decided in favor of the Revenue, vide order in ITA No.984/Mds/2007 dated 03.04.2009 passed by tribunal wherein it was held that change in method of valuing closing stock is to be applied both to the opening stock and also to closing stock, by holding as under:

:24. After considering the rival contentions and the materials on record, we note that the assessee has changed the method of valuation of closing stock from the market price to the cost price which has reduced the value of the closing stock. As per the accounting standards, the valuation of the stock should be at the cost market price, whichever is less. Therefore, there is no dispute that by adopting the cost price method for valuation of the closing stock, the assessee has followed the principle of accounting standards but at the same time assessee should have also valued the opening stock on the same basis to maintain the uniformity and to avoid distortion of results. There is no bar in adopting the method of valuation which is bonafide but the method should be accepted for both, opening stock as well as closing stock. We note that the Assessing Officer has not discussed this Issue in detail and in our view when the assessee has adopted the cost price method for valuation of the closing stock, then the same method should be adopted for valuation of the opening stock also for the accounting year under consideration. Accordingly, we set aside the orders of the lower authorities, qua this issue and remit the same to the record of the Assessing Officer to decide this issue afresh by doing the valuation of opening stock as well as the closing stock at the cost price method."

We have already seen that Hon'ble Madras High Court was pleased to remit this issue back to the tribunal for fresh adjudication. Now, we are seized of this matter under directions of the Hon'ble Madras High Court. While remitting matter back to the tribunal for fresh adjudication , the Hon'ble Madras High Court referred to judgment of Division Bench in the case of M/s Kadari Ambal Mills Limited v. JCIT in TCA no. 430 of 2005 , judgment dated 20.06.2001. We have heard both the rival parties. The learned counsel for the assessee drew our attention to the orders passed by various authorities including tribunal in the first round of litigation. It was submitted by learned counsel for the assessee that only one issue is presently before tribunal for adjudication vide directions of Hon'ble Madras High Court which concerns itself with change in method adopted for valuing finished stock in this year and whether the same is also to be applied to opening stock of finished goods. The main bone of contention of learned counsel for the assessee is that the said change in method of valuation of finished goods was bonafide and is in conformity with Accountant Standard issued by ICAI. It is submitted by learned counsel for

the assessee that the assessee was earlier following market value method for valuing finished goods consistently in earlier years and it is in this year only , the method of valuing finished goods was changed to cost or market value whichever is lower, which method of valuing finished goods is in consistency with Accounting Standard issued by ICAI. It was submitted that auditors suggested to follow cost or market value method whichever is lower for valuing finished goods. It was submitted that the AO has accepted this change of method of valuing finished goods while framing scrutiny assessment but only that the AO held that this method of valuing finished stock is to be applied to both opening and closing stock of finished goods in the year of change which has caused prejudice to the assessee. It was submitted that the said changed method was applied to closing stock and the same was not applied to opening stock , as otherwise there would have been chain effect for earlier years also. The learned counsel for the assessee would rely on judgment of Hon'ble Madras High Court in the case of M/s Kadari Ambal Mills Limited v. JCIT in TCA no. 430 of 2005 , dated 20.06.2001 . The learned DR would rely on the assessment order passed by the AO.

4. We have considered rival contentions and perused the material on record. We have observed that assessee was earlier following the market value method for valuing finished goods consistently in preceding years which was accepted by Revenue. The assessee changed method of valuing finished goods in the previous year relevant to impugned assessment year

from 'market value' method to 'cost or market value whichever is lower' method. Undisputedly, this changed method is consistent with Accountant Standard AS-2 issued by ICAI which is a mandatory standard issued by ICAI. When an expert body like ICAI issues accounting standard which is mandatory in nature, it becomes incumbent on the entities to compulsorily follow the same otherwise their accounts will not reflect true and fair view. Even for computing income chargeable to tax and payment of taxes, the income is to be computed after taking cognizance of AS's prescribed by ICAI, unless the AS's are in variation/conflict with provisions of the 1961 Act and in that scenario, provisions of the 1961 Act will prevail over AS. Thus, undisputedly method of valuing finished goods at 'cost or market value whichever is lower' is as per AS prescribed by ICAI and thus it could be said that change in method of valuing finished stock was bonafide and the assessee has rightly applied the said changed method to closing stock of finished goods. This will also satisfy the mandate of Section 145A as was existing in the statute for relevant period. Once there is a change in method of valuing stock which is held to be genuine and bonafide and there is no intent to defraud revenue by changing method of valuing stock, some inconvenience is likely to take place in the first year as the closing stock of preceding year which has become opening stock of the year under consideration was valued at earlier method and if the changed method is applied also to opening stock, then there will be taxing of the same income twice once in preceding year when stock was valued at old method and in this year when the changed method is applied even

to opening stock of the current year under consideration, unless otherwise the changed method is applied to opening stock of preceding year also and so on , which will lead to chain reaction of opening of assessment for several preceding years which is not desirable as ultimately over all effect is tax neutral. In our considered view, the learned CIT(A) has rightly held that there is no need to apply changed method of valuing stock of finished goods to opening stock of finished goods held by assessee at the beginning of previous year relevant to impugned ay: 2004-05 which can continued to be valued as per old method. The decision of Hon'ble Madras High Court in the case of Kadhuri Ambal Mills Limited v. JCIT in TCA No.430 of 2005 , judgment dated 20.06.2011 is clearly applicable. The decision of Hon'ble Madras High Court is reproduced hereunder:

"5. Heard the learned counsel and perused the documents on record. During the relevant assessment year, the assessee has changed the method of valuation of stock from market price to cost price. The assessee valued the closing stock on the basis of cost price but valued the opening stock on the basis of market price. For the earlier assessment years, the assessee valued the closing stock of finished goods at market price. The Auditor of the assessee objected the same and also advised to value the closing stock at cost or market price, whichever is less. Therefore, the assessee has changed the method of accounting with regard to valuation of closing stock from market price to cost price. The Assessing Officer accepted the method of valuation of the closing stock at cost price without questioning the bonafide of the assessee. So, there is no dispute that the Assessing Officer himself had accepted the valuation of the closing stock as on 31.03.1994 as declared by the appellant/assessee. In respect of the opening stock, the assessee valued the opening stock as on 01.04.1993 at market price. Therefore, the Assessing Officer was of the view that valuation in respect of the opening stock and closing stock should be valued in this uniform method i.e., cost price. The dispute is as to whether different methods could be adopted, one for the opening stock and another for closing stock. The said controversy is already settled by this Court in the case of CIT Vs. Carborandum Universal Limited reported in 149 ITR 759 (Mad) . In that judgment, the issue was as to whether the closing stock is to be valued in the same method as what was applied to the opening stock. The High Court after considering the principles of valuation and also series of case laws held at page 765 as follows:-

" On a due consideration of the matter, we are inclined to agree with the view of the Tribunal. If the assessee is called upon to apply the new method of valuation to the opening stock of the accounting year as well, then, in consequence, the value of the closing stock of the year previous to

the accounting year will also get altered and that will result in the modification of that assessment for the previous year. It is for this reason, the Tribunal has stated that though by adoption of the new method of valuation for the closing stock alone the assesses may, appear to get some unintended benefit, in course of time it will get adjusted and the Revenue will not be a loser. Even apart from this reason, if the Revenue's contention that the new method should be adopted both to opening stock and closing stock-even in the first year of the introduction of the new method is accepted, then it will lead to the position that the assessee cannot at all change the method or the assesses has to revalue the closing stock of the previous year which will be the opening stock of this year, and such a revaluation on the new basis as per the assesses is not ordinarily possible. That when a new method of valuation of stock is adopted in any particular year, the assesses can on that basis leave intact, the valuation of the opening stock on the old method has been laid down in a series of cases-"

6. The above judgment was also considered by the Bombay High Court in the case of *Melmould Corporation Vs. Commissioner of Income Tax* reported in (1993) 202 ITR 789. In page Nos. 792 to 794 it was held as follows:-

" We are not here concerned with whether this is the correct method or an acceptable method for determining cost price. At no stage of the proceedings was the question ever raised as to whether it was permissible for the assessee to revalue its stock by not including in the cost price overhead expenses. The Tribunal has not dealt with this aspect, viz. the manner in which the closing stock has been valued in the present case. Therefore,, the decision of the Supreme Court in the case of CIT Vs. British Paints India Ltd. (1991) 188 ITR 44 is not attracted to the question before us for consideration. The decision of the Tribunal is on the footing that since the closing stock was valued by adopting a certain method, the same method should be adopting in valuing the opening stock. In other words, the change in the method of valuation, according to the Tribunal, should commence with valuing the opening stock of any previous year by the new method which is to be adopted for valuing the closing stock as well. The assumption so made by the Tribunal appears to be contrary to the normally accepted accounting principles. Mr.Bhujale has drawn our attention to a booklet called "Valuation of Stock and Work-in-progress-Normally Accepted Accounting Principles" brought out by Indian Merchants Chamber Economic Research and Training Foundation and written by Shri G.P.Kapedia. At page 4 of this booklet there is a discussion about change from one valid basis to another valid basis. It states :*

" 2. Where a change from one valid basis to another valid basis is accepted, certain consequences normally follow. The opening stock of the base year of change is valued on the same basis as the closing stock- Whether the change is to a higher level or to a lower level, the Revenue normally does not seek to revise the valuation of earlier years. It neither seeks to raise additional assessments, nor does it admit relief under the 'Terror or mistake' provisions.

3. It is not possible to define with precision what amounts to a change of basis. It is a convenience, both to the tax payer and to the Revenue, not to regard every change in the method of valuation as a change of basis. In particular, the Revenue encourages the view that change which involves no more than a greater degree of accuracy, or a refinements- should not be treated as a change of basis whether the change results in a higher or a lower valuation.

In such cases the new valuation is applied at the end of the year without amendment of the opening valuation." (underlining ours)-

The same principle has been adopted by the Karnataka High Court in CIT Vs. Corporation Bank Ltd., (1988) 1T4 ITH 616. It has said (headnote):

"The two principles applicable with regard to the valuation of stock are that the assessee is entitled to value the closing stock either at cost price or market value whichever is lower, and that the closing stock must be the value of the opening stock in the succeeding year. It is thus, clear that irrespective 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, provided the change is bona fide and followed regularly thereafter," Thus, the value of the closing stock of the preceding year must be the value of the opening stock of the next year. The change, therefore, has to be effected by adopting the new method for valuing the closing stock which will, in its turn, become the value of the opening stock of the next year. If, instead, a procedure is adopted for changing the value of the opening stock, it will lead to a chain reaction of changes in the sense that the closing value of the stock of the year preceding will also have to change and correspondingly the value of the opening stock of that year and so on. This was pointed out by the Madras High Court in the case of CIT Vs. Carborandum Universal Ltd., (1984) 149 ITR 759. In the case before the Madras High Court also the valuation of opening stock had been done by the company on the basis of total cost i.e., cost including overheads while it changed its method of valuation for the closing stock to "direct cost" i.e. cost without overheads. This change in method was made bona fide and the assessee said that it would for adopting this method consistently in the future just as in the present case. The court in that case held;

"The change was a bona fide one and was a permanent arrangement which was to be followed year after year the change would have to be accepted notwithstanding the fact that during the assessment year in question, which was the first year when the change of method was brought about a prejudice or detriment might be caused to the revenue, because the opening stock was valued at total cost while closing stock was valued at direct cost."

It said (Headnote):

If the assessee is called upon to apply the new method of valuation to the opening stock of the accounting year as well, the value of the closing stock of the year previous to the accounting year will also have to get altered which will result in a modification of the assessment of that previous year."

7. Following the judgment of this Court cited supra and agreeing with the judgment of the Bombay High Court, we are of the view that the Tribunal is wrong in holding that there must be uniformity in the method of valuation of opening stock as well as the closing stock. In the instant case the Assessing Officer has accepted the valuation of the closing stock as on 31.03.1994 at cost price and also bona fide of the assessee is not in dispute. Further, the assessee has followed the new method consistently. Therefore, the order of the Tribunal is wrong in rejecting the contention of

the assessee. Hence, we set aside the order of the Tribunal and restore the order of the Commissioner of income Tax (Appeals). In these circumstances, we answer the above questions of law in favour of the assessee and as against the Revenue. The Tax case (Appeals) stands allowed. No costs."

However, for a limited verification, we are restoring the matter back to the file of the AO for verification of the assessee's contention that the assessee has consistently followed the above new method of valuing inventory in succeeding years also and no attempt is made to suppress income chargeable to tax of the relevant ay . Further, On perusal of the order of the Ld.CIT(A) , it is also observed by us that different methods are applied by assessee for valuing different components of inventory, as under:

<i>Raw Materials and Stores</i>	<i>At cost</i>
<i>Finished goods</i>	<i>At lower of cost and market value</i>
<i>Process stock</i>	<i>At cost</i>
<i>Waste</i>	<i>At net realizable value</i>

If the assessee has to change method of valuing inventory in compliance with AS-2 issued by ICAI, then changed method of valuation has to be applied to all the components of inventory as prescribed under AS-2 and the assessee cannot be allowed to pick and chose method of valuing inventory to apply method to some components of inventory and leaving out other components of inventory. In that scenario, it will lose the character of being a change of method lacking bonafide and genuineness warranting change of method of valuation of inventory. So, also for limited verification by the AO, we are remitting matter back to the file of the AO , wherein the assessee is directed to justify as to why it is adopting

different method for valuing different components of inventories and whether the said differential methods for valuing different components of inventory are consistent with AS prescribed by ICAI. The assessee is directed to give justification before AO for adopting different method of valuing different components of inventory and to prove that these differential methods are consistent with AS-2 prescribed by ICAI and hence accordingly, there was no intent to reduce tax by applying new method of valuing finished goods . We order accordingly.

5. In the result, the appeal filed by the Revenue in ITA No.984/Chny/2007 for ay: 2004-05 is partly allowed for statistical purposes.

Order pronounced on the 05th day of February, 2020 in Chennai.

Sd/-

(धुव्वुरु आर.एल. रेड्डी)

(DUVVURU R.L.REDDY)

न्यायिक सदस्य/**JUDICIAL MEMBER**

Sd/-

(रमित कोचर)

(RAMIT KOCHAR)

लेखा सदस्य/**ACCOUNTANT MEMBER**

चेन्नई/Chennai,

दिनांक/Dated: 05th February, 2020.

TLN

आदेश की प्रतिलिपि अग्रेषित/**Copy to:**

1. अपीलार्थी/Appellant
2. प्रत्यर्थी/Respondent
3. आयकर आयुक्त (अपील)/CIT(A)
4. आयकर आयुक्त/CIT
5. विभागीय प्रतिनिधि/DR
6. गार्ड फाईल/GF