ITAT allows film distributor to follow conservative method for valuation of closing stock instead of Rule 9B

Summary – The Mumbai ITAT in a recent case of Universal Arts Ltd., (the Assessee) held that where assessee-distributor of rights of feature films followed conservative method of accounting for valuation of closing stock being cash method and arrived at lesser amount of business loss than that which would be by adopting rule 9B, of assessee's method was to be endorsed and addition to be deleted

Facts

- The assessee was engaged in sale of television serial, editing and film software development. The assessee was following conservative method of accounting for valuation of closing stock.
- The Assessing Officer observed that as the assessee was engaged in the business of distribution of rights of feature films, rule 9B was attracted in this case. He referred to sub-rules (4) and (5) of rule 9B and, accordingly, disallowed the excess cost for acquisition of films.
- The Commissioner (Appeals) granted relief to the assessee.
- On appeal:

Held

- It is not in dispute that the assessee has been valuing the closing stock of movies at cost for past many years and in assessment years 2007-08 and 2008-09, the valuation method has been challenged by the concerned Assessing Officer. If the method followed by the assessee is accepted, the loss claimed in assessment years 2007-08 and 2008-09 would be Rs. 10.17 lakh and 18.22 lakh.
- In case the rule 9B is applicable, the following position in respect of valuation of closing stock would emerge: In terms of sub-rule (2) to rule 9B, if the film is released at least 90 days before the end of previous year, entire cost of acquisition is to be allowed in that year. In terms of sub-rule (3) to rule 9B if the film purchased is not released least 90 days before the end of previous year but amount realized on sale of rights during previous year, is less than cost price, the amount realized would be allowed as reduction and the balance cost of acquisition is to be carried forward to next year. In terms of sub-rule (4) to rule 9B if the film purchased is not released or sold during previous year, entire cost of acquisition is to be carried forward in next year. In terms of sub-rule (5) to rule 9B the amount realized on sale during previous year, should be credited in the books of account. From above, it is clear that the cost to be allowed during the year depends upon the closing stock of the previous year, purchases during the year and the valuation of the closing stock would be dictated by sub-rules (2) and (3). From the assessment order, it appears that the Assessing Officer has misconstrued the provisions of rule 9B and has not applied sub-rules (2) and (3) properly. In fact he had ignored sub-rule (4) completely and did not allow the closing stock of the previous year of

unsold films which is to be allowed as deduction irrespective of sale or not. In case, the correct adjustments are made to opening and closing stock as per rule 9B, instead of loss claimed by the assessee in the return, loss have to be allowed as per rule 9B. As per the cost of acquisition, closing stock adjustment in past year's closing stock may lead to allowing higher losses in the instant assessment year. The method followed by the assessee is endorsed and the addition made by the Assessing Officer was rightly deleted by the Commissioner (Appeals) in the assessment year, *i.e.,* 2007-08. This factual legal finding needs no interference and uphold the same.

- In the result, appeals are dismissed.