

M/s. Sanjeev Woolen Mills v. Commissioner of Income Tax, Mumbai

Civil Appeal Nos. 6735–6736 of 2003

[2005] Supp. 5 SCR 459 | 2005-11-24

Whether the AO could reject a consistently followed method of valuing unsold finished goods at market value above cost when it produced notional profit and distorted the income of two assessment years.

145 (historical text) | 144 (context) | 80HHC (deduction context)

Two-judge bench | Dr. AR. Lakshmanan, J. | P.P. Naolekar, J.

Assessment years: 1992-93, 1993-94

Historical stock-valuation ruling; printed figures conflict

The Court upheld rejection of finished-stock valuation above cost because it recognised notional profit. Neither consistent use nor an abnormal margin alone decides every section 145 case. The report conflicts on Rs 90/Rs 98, exchange-rate arithmetic and commencement-year labels, and prints Rs.2054.60% and section 80HH(C); those are not silently corrected. Both appeals were dismissed, with no costs order in favour of either party. There is no separate fraud or penalty holding, and later treatment/current-law mapping remain unverified.

01 FACTS OF THE CASE

The assessee firm imported synthetic waste and manufactured and exported woollen blankets. It kept mercantile accounts, valuing raw materials and semi-finished goods at cost and finished goods at market value, with dollar prices translated into rupees. In AY 1992–93, it showed finished-goods opening stock at Rs 90 per kg and closing stock at Rs 130 per kg and claimed section 80HHC relief. In AY 1993–94, it carried Rs 130 per kg into opening stock, reported no closing stock and returned a loss of Rs 54,420. These are the principal figures stated in the judicial narrative; a later Rs 98 reference and other numerical inconsistencies are retained as cautions below (physical pages 3–4/SCR 461–462).

The AO considered the higher-market-value method to distort the trading result, inflate the first year's profit and suppress the second year's profit. He substituted inventory valuation on a cost basis and added Rs 2,67,38,280 to total income for the second year. CIT(A) dismissed both appeals. The Tribunal accepted the consistently followed market-value method and the corresponding next-year opening stock. The Bombay High Court allowed both Revenue appeals on 11 December 2002. The assessee brought Civil Appeal Nos. 6735–6736 of 2003 (physical pages 3–6/SCR 461–464).

Source: See the proposition-specific paragraph and PDF-page references below.

02 DISCUSSION BY THE HON'BLE COURT

The Court construed the section 145 text applicable to the years in issue. Regular use of a method mattered: the AO could not replace it merely because it benefited the assessee in a particular year or because a different method seemed preferable. Rejection required cogent evidence that the method did not permit a proper deduction of true income, with the power exercised cautiously, judicially and reasonably. An unusually high profit or a loss could justify closer inquiry, but alone was not enough to reject the accounts (physical pages 7–10/SCR 465–468).

The Court's review of stock-valuation authorities, including Chainrup Sampatram, A.L.A. Firm and Shakti Trading, explained why closing inventory cancels the cost of unsold goods in the trading account. Valuation at market value below cost recognises the accepted prudential exception for anticipated loss. Appreciation above cost creates unrealised profit from stock that remains with the taxpayer; mere carry-forward into next year's opening stock does not make that profit real. The extended quotations are precedent reasoning adopted or discussed by this judgment, not additional transactions of Sanjeev Woolen Mills (physical pages 10–14/SCR 468–472).

Here the method valued finished stock above cost at its higher market price and thereby produced notional income. The Court held that the AO's rejection of that method under historical section 145, as sustained by the High Court, accorded with the governing principles (physical pages 14–15/SCR 472D–473E).

Source: See the proposition-specific paragraph and PDF-page references below.

03 JUDICIAL DECISION

Both assessee appeals were dismissed without any order as to costs. The High Court's result upholding the AO's rejection of the stock-valuation method remained in place. The Supreme Court did not provide a fresh numerical recomputation or a separate penalty determination (physical page 15/SCR 473B–E).

Source: See the proposition-specific paragraph and PDF-page references below.

04 OUTCOME / IN WHOSE FAVOUR

In whose favour: Revenue

Civil Appeal Nos. 6735–6736 of 2003 dismissed; no order as to costs

Final merits decision upholding rejection of the higher-market-value closing-stock method for the two years

Abnormal profit or a tax benefit alone does not authorise rejection; the defect was failure to deduce real income from valuation above cost. The judgment is not a free-standing foreign-exchange-gain rule, a penalty finding or a current ICDS/section 145A ruling.

Source: See the proposition-specific paragraph and PDF-page references below.

05 AKHB REVIEW POINT

For an inventory dispute, retain the cost build-up, the evidence of market value, the opening/closing-stock bridge and the actual realisation record. Explain exactly how the adopted method affects the year's true trading result. Consistency is relevant evidence but does not cure a method that recognises unsold-stock appreciation as profit; conversely, a high margin is a reason to investigate rather than an automatic ground to reject books.

Do not turn the AO's allegations of tax planning with intent to defraud into a separate Supreme Court fraud or penalty holding. For any modern application, independently examine the applicable statutory and accounting regime. Do not repair this report's conflicting prices, year labels or percentage presentation by silently calculating a replacement figure.

Source: See the proposition-specific paragraph and PDF-page references below.

PROPOSITION-SPECIFIC SOURCE PARAGRAPHS AND PDF PAGES

1.

Topic: Identity, both appeal numbers and judicial opening

Source url: [Open cited source](#)

Pdf pages: 1; 3

Paragraphs: Cover; jurisdiction line; unnumbered judicial opening, SCR 461F–H

Source role: reported metadata and judicial text

2.

Topic: Two assessment years, valuation figures and appellate history

Source url: [Open cited source](#)

Pdf pages: 4; 5; 6

Paragraphs: Unnumbered facts and procedural history, SCR 462–464

Source role: judicial text

3.

Topic: Historical section 145 and constraints on substitution

Source url: [Open cited source](#)

Pdf pages: 7; 8; 9; 10

Paragraphs: Statutory quotation and unnumbered reasoning, SCR 465D–468A

Source role: judicial text with quoted historical statute

4.

Topic: Closing-stock rationale and attributed precedents

Source url: [Open cited source](#)

Pdf pages: 10; 11; 12; 13; 14

Paragraphs: Unnumbered discussion, SCR 468–472

Source role: judicial text with attributed precedent discussion

5.

Topic: Application, dismissal of both appeals and costs

Source url: [Open cited source](#)

Pdf pages: 14; 15

Paragraphs: Final unnumbered reasoning, SCR 472D–473E

Source role: judicial text

JUDICIAL AUTHORSHIP AND SEPARATE OPINIONS

P.P. Naolekar, J.

ACT IDENTIFIED IN THE REVIEWED SOURCE

Income-tax Act, 1961

SOURCE & VERIFICATION

[Hon'ble Supreme Court source PDF \(reported judgment\)](#)

Identified source rendition: 15 PDF pages; SHA-256

7119b1c4645342d936b876727dc7010824dbe48626032381f015f72fcff9dd4b. Original bytes preserved.

Complete unnumbered judicial text from P.P. Naolekar, J., physical page 3/SCR 461 through dismissal of both appeals on physical page 15/SCR 473. Editorial headnote and authorities list on pages 1–3 excluded. Historical section 145 quotation on pages 7–8 and quoted/discussed precedents on pages 10–15 distinguished. No adjacent judgment.

[Open cited source rendition](#)

The principal narrative on physical page 4 gives opening stock at Rs 90 per kg but later on the same page mentions Rs 98 as at 1 April 1991. The quoted US-dollar price and exchange-rate recital also do not transparently reconcile with the stated Rs 90. No corrected valuation or exchange-rate arithmetic is substituted.; The narrative says the method was followed since account year 1986–87, while counsel's submission on page 6 says 1985–86. Neither is treated as an independently verified commencement year.; Physical page 9 prints Rs.2054.60% and gives awkward or overlapping accounting-year labels for the comparator ratios. The note does not convert that into a rupee amount or invent a corrected chronology.; Physical page 9 repeatedly prints section 80HH(C); elsewhere the judgment identifies section 80HHC. The case is indexed to the latter contextual deduction, while preserving the source discrepancy.; The AO's and High Court's adverse descriptions are procedural history. The Supreme Court's operative holding concerns stock valuation and true income; there is no separately adjudicated fraud or penalty charge.; The jurisdiction line contains two appeals. Ingestion metadata showing only Civil Appeal No. 6735 of 2003 is incomplete; both appeal units are retained.; The section 145 text quoted is expressly historical. The judgment does not resolve later statutory changes, section 145A or present accounting standards.

STATUTORY SCOPE

No automatic mapping to the Income-tax Act, 2025 or present-law certification. Apply the statutory text for the relevant year.

LATER TREATMENT

Source checked 2026-10-04. Comprehensive subsequent judicial and statutory treatment has not been verified. No independent later-judgment comparison was conducted for this note; authorities discussed in the judgment are attributed to that source only. No current-law or Income-tax Act, 2025 mapping is certified.

IDENTIFIED SOURCE LINKS

[reported judgment - PDF pages: 15](#)

SHA-256: 7119b1c4645342d936b876727dc7010824dbe48626032381f015f72fcff9dd4b

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