

Excess stock can't be treated as undisclosed income if assessee identified diff. much prior to commencement of search

Facts of the case - PCIT vs. Industrial Safety Products (P.) Ltd. - [2023] (Calcutta)

A search was conducted on the premises of the assessee's group companies. Assessing Officer (AO), while completing the assessment for the relevant assessment year, issued a show cause notice to the assessee, calling upon it to explain the under-valuation of physical stock.

In response, the assessee stated that the excess stock of leather found during the physical verification of inventory from January to February 2014 had been properly accounted for in the books for the financial year 2014-15, and the same had also been disclosed.

Rejecting the explanation offered, AO treated under-valued stock as undisclosed income.

On appeal, the CIT(A) deleted the additions made by AO. Aggrieved-AO filed an appeal to Calcutta High Court.

Decision of the case :

- The High Court held that no material had been brought on record by the AO to show that during the search, the authorized officer had conducted a physical inspection of the stock, because of which excess quantities of raw leather were detected. Consequently, additions were made towards undisclosed stock.
- It was found that well before the search, the assessee had internally conducted a stock-taking exercise and detected the discrepancy in stock, and the same was reported. Before the commencement of the search, the managing director had instructed the respective unit heads to reconcile the stocks and records and incorporate differences in the books for the said financial year.
- Further, the assessee is a corporate body that is required to maintain and prepare its accounts in conformity with the provisions of the Companies Act. The accounts must be audited, and the auditor must furnish his report in the manner prescribed. After taking note of the auditor's report as well as the stock inspection report, it was found that such an inspection report was prepared at the instance of the assessee as a matter of internal control, and the same was drawn up much before the date of search.
- Therefore, the difference in stocks had been identified by the internal team of the assessee itself much prior to the commencement of the search. Accordingly, the action taken by AO wasn't correct.