

आयकर अपीलीय अधिकरण "E" न्यायपीठ मुंबई में।

IN THE INCOME TAX APPELLATE TRIBUNAL "E" BENCH, MUMBAI

**BEFORE SHRI C.N. PRASAD, JUDICIAL MEMBER
AND SHRI RAMIT KOCHAR, ACCOUNTANT MEMBER**

आयकर अपील सं./I.T.A. No. 7311/Mum/2012

(निर्धारण वर्ष / Assessment Year : 2009-10)

M/s Shree Ramkrishna Exports Pvt. Ltd., (earlier Shree Ramkrishna Exports) EE 6011, Bharat Diamond Bourse, G Block, Bandra-Kurla Complex, Bandra East, Mumbai - 400 005.	बनाम/ v.	The Jt. Commissioner of Income Tax - 16(3), Matru Mandir, Mumbai - 400 007.
स्थायी लेखा सं./PAN : Earlier PAN AAASF6758D (now PAN AARCS2442Q)		
(अपीलार्थी /Appellant)	..	(प्रत्यर्थी / Respondent)

आयकर अपील सं./I.T.A. No. 112/Mum/2013

(निर्धारण वर्ष / Assessment Year : 2009-10)

The Jt. Commissioner of Income Tax - 16(3), Matru Mandir, 2 nd Floor, Room No. 206, Tardeo Road Mumbai - 400 007.	बनाम/ v.	M/s Shree Ramkrishna Exports, 214 Prasad Chambers, Opera House, Mumbai - 400 004.
स्थायी लेखा सं./PAN : AAASF6758D		
(अपीलार्थी /Appellant)	..	(प्रत्यर्थी / Respondent)

Assessee by	Dr. K. Shivaram
Revenue by :	Shri Manjunatha Swamy (CIT - D.R.)

सुनवाई की तारीख /Date of Hearing : 10-08-2016

घोषणा की तारीख /Date of Pronouncement : 07-11-2016

आदेश / O R D E R

PER RAMIT KOCHAR, Accountant Member

These are cross appeals filed by the assessee and the Revenue before the Income-tax Appellate Tribunal, Mumbai (Hereinafter called "the Tribunal"). These cross appeals are heard together and are disposed of by this common order for the sake of convenience and brevity. These appeals are directed against the appellate order dated 30th October, 2012 passed by learned Commissioner of Income Tax (Appeals)- 27, Mumbai (hereinafter called "the CIT(A)"), for the assessment year 2009-10, the appellate proceedings before the learned CIT(A) arising from the assessment order dated 26th December, 2011 passed by the learned Assessing Officer (hereinafter called "the AO") u/s 143(3) of the Income-tax Act, 1961 (Hereinafter called "the Act").

2. The following grounds of appeal are raised by the assessee in ITA No. 7311/Mum/2012 for the assessment year 2009-10 in the memo of appeal filed with Tribunal which reads as under:-

"On the facts and circumstances of the case and in law, the learned Comm. of Income Tax (Appeals) erred in partly conforming the action of the learned Assessing Officer for disallowance of business expenditure in the nature of marked - to - market loss on restatement of outstanding forward contracts to the extent of Rs. 9,92,48,752/- by considering the loss as notional and speculative in nature."

3. The following grounds of appeal are raised by the Revenue in ITA No. 112/Mum/2013 for the assessment year 2009-10 in the memo of appeal filed with Tribunal which reads as under:-

"1. Whether on the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in holding that 'Mark to Market' loss

of Rs.22,76,84,554/- arising on valuation of forward exchange contracts on the closing date of accounting year is not a notional loss and, therefore, allowable.”

3. The Brief facts of the case are that the assessee is engaged in the business of manufacture and export of cut and polished diamonds. It was observed by the A.O. during the course of assessment proceedings u/s 143(3) read with Section 143(2) of the Act from the details furnished by the assessee that it has entered into forward foreign exchange contracts which have been revalued by the assessee on the closing day of the accounting year based on prevailing exchange rate as at year end . On revaluation of forward foreign exchange contracts, the assessee has claimed ‘marked to market’ loss on these outstanding forward foreign exchange contracts amounting to Rs. 32,69,33,306/- and since these contracts have not been settled the assessee was asked to explain why this loss be not disallowed being notional loss. The assessee submitted before the AO that it is engaged in the business of import of rough diamonds, cutting and polishing the same and export of polished diamonds , whereby the assessee has exposure to foreign exchange due to transactions of imports and exports in foreign currency . Further, the assessee submitted that it had availed substantial bank finance in foreign currency, which is required to be settled in foreign currency only. In view of the same, it was submitted by the assessee that it has substantial exposure on account of fluctuation in foreign currency rates. Further the assessee submitted that it had entered into the forward contracts to hedge against the risk of fluctuation in foreign currency rates in respect of its exports and imports transactions. It was submitted that the contract for purchase and sale of foreign currency was also monitored under various regulations issued by the Reserve Bank of India and the assessee was permitted to enter into forward exchange contracts because of its export activity. The assessee submitted that in the assessee’s case, the assessee has entered into forward

exchange contracts to hedge against the risk of fluctuation in foreign currency rates in respect of its exports and imports transactions. It was submitted that assessee is revaluing all the monetary assets and liabilities outstanding at the end of the year by following AS-11 issued by ICAI and recognizing profit/loss during the year . It was submitted that it is recognizing 'mark to market' gain or loss in respect of outstanding forward foreign exchange contracts by revaluing these contracts as per AS-11 issued by ICAI, at year end at the prevailing exchange rates as on year end. The assessee submitted that the assessee is following this accounting practice consistently . The assessee has relied upon the following decisions :

- (i) DCIT vs. Bank of Bahrain & Kuwait 132 TTJ 505 (Mumbai)(SB)
- (ii) Woodward Governor India (P) Ltd. 312 ITR 254(SC)
- (iii) ONGC 322 ITR 180(SC)
- (iv) Badridas Gauridu (P) Ltd. 261 ITR 256
- (v) Soorajmul Nagarmull 129 ITR 169 (Cal.)

The A.O. considered the submissions of the assessee and observed that the assessee has entered into forward foreign exchange contracts , which are outstanding as at the end of the previous year which has been valued by the assessee on the basis of rates applicable on the closing day of the previous year , though the contracts were still outstanding and accordingly, such unrealized losses are recorded by the assessee. It was observed by the AO that these losses have not been actually incurred but are only due to variation in the value of the contracts as on reporting date. It was also observed by the AO that the actual loss or gain will be determined only after the expiry of period of the contracts or their termination and at that time there might not be any loss and such losses are notional and not allowable. It was also observed that these forward contracts in foreign exchange are

different from the actual business liabilities and assets of the assessee like debtors and creditors, which are arising from the business activities of the assessee and which are ascertained at the year end. So far as the pending forward contracts are concerned, it was observed by the AO these are neither assets nor liabilities having any value. Thus it was observed by the AO that forward contracts are not the ascertained asset/liability of the assessee and if valued at the reporting date of the financial statements would result only in an unascertained liability, asset and resulting loss or gain would be notional and such notional loss cannot be allowed as deduction. The A.O. further observed that as per the Act there is no provision or treatment for mark to market method of accounting and is governed by general principle of taxation. It was also observed that the Act does not allow deduction of any such notional loss for which the liability has not crystallized and there is no actual loss incurred/sustained by the assessee on account of dealing in forex derivatives until their final values are known. , thus, the A.O. disallowed the said loss vide assessment order dated 26.12.2011 passed by the AO u/s. 143(3) of the Act.

4. Aggrieved by the assessment order dated 26.12.2011 passed by the A.O. u/s. 143(3) of the Act, the assessee preferred an appeal before the Id. CIT(A).

5. Before the Id. CIT(A) the assessee submitted that the assessee is engaged in the business of import and exports of diamonds and substantial amount of its turnover was denominated in foreign currency. The assessee submitted that the working capital facility from banks were availed and some of which were also denominated in foreign currency. It also carries currency risk in respect of its stock as it is most likely to be sold by way of exports. The assessee submitted that the forward contracts are entered into to hedge these currency risk associated with normal business transaction and these derivative contracts were entered within the guidelines of RBI & FEMA. The

intent of entering into such derivative contracts was to safeguard itself against exchange fluctuation risk on foreign currency receivables or payables. It was submitted that the assessee has been consistently following the accounting method wherein year-end restatement or mark to market gain or loss in respect of all assets or liabilities denominated in foreign currency i.e. debtors, creditors and forward contracts, is being recognized as gain or loss in profit & loss account which is mandatory as per AS 11 issued by ICAI for depicting the effect of currency fluctuations while finalizing the financial results of the assessee as prescribed by ICAI. The assessee submitted that it has recognized gain of Rs.11,61,52,808/- during the year under consideration by restating the receivables at closing rate, however, this gain was not actually realized. The actual gain may be different amount depending on the rate prevalent when it was actually realized.

The ld. CIT(A) after considering the submissions of the assessee observed that the assessee is engaged in the business of import of rough diamonds, manufacturing i.e. cutting & polishing of same in to polished diamonds and exporting the said diamonds. The total sale of Rs. 961.53 crores(US \$ 217,708,068) was denominated in foreign currency. Out of total purchase of Rs. 791.72 crores, import accounts for Rs.690.08 crores (US \$ 161,404,740). At the year end, the creditors for goods were payable in dollar terms at Rs. 94.07 crores (US \$ 43,851,415). Similarly, exports receivable account for Rs. 209.76 crores(US \$ 41,293,418) denominated in dollar terms. The assessee had a bank loan outstanding in PCFC and FCB accounts of US \$ 25,959,035 at the year end. Thus, it was observed that the assessee was exposed to risk arising out of fluctuation in foreign exchange rate and as a prudent businessmen likely to hedge its risk. The ld. CIT(A) noted that assessee has booked all the forward contracts in respect of export receivables only. It was further noted that in addition to the opening outstanding forward contracts of 61,000,000 US dollars during the year under consideration, the assessee has

booked forward contracts of 767,000,000 US dollar, utilized forward contracts of 72,406,591 US dollar, cancelled forward contracts of 6,000,000 US dollar and finally held the forward contracts of 59,293,409 US dollar at the year end. Thus, the assessee has entered into the forward contracts during the normal course of business and utilized the same for business by allowing them to run up to the date of contract. Further, there was a loss of Rs.90,000 incurred on cancellation of forward contracts which is meager as compared to the volume of assessee's business, thus forward contracts were entered and utilized for business, was the observation of learned CIT(A). Thus from the notes to the accounts it was observed by the learned CIT(A) that the assessee was reporting all the monetary items i.e. export receivable , import payable and foreign currency working capital loan appearing in the balance sheet at closing rate and recognizing the exchange rate difference in profit and loss account as expenses or income which is as per AS-11 issued by ICAI being consistently followed and there is no change in this regard. For the assessment year 2010-11, the assessee has offered a gain of Rs. 5,47,30,056/-as income on revaluation of the pending forward contracts. Thus it was observed by the learned CIT(A) that the assessee is consistently following the above accounting method and hence it is not a case of using the accounting practice as a tool to book the losses and reduce the tax liability. Thus, it was observed by learned CIT(A) that such risk of foreign exchange fluctuation risk is integral part of the assessee's business and is associated with such business. Thus the ld. CIT (A) observed that the risk which the assessee has hedged by way of a forward contract has an underlying asset or a liability , by way of debtors or creditors. The profit and loss arising out of forward contracts either on maturity or on cancellation of such contracts forms part of the business income and such forward contracts entered into during the course of business creates a legal liability irrespective of the fact whether it matures during the accounting period or beyond the accounting period. The ld. CIT(A) considered the judgments' of Hon'ble Delhi High Court

in the case of Woodward Governor 294 ITR 451, decision of Hon'ble Supreme Court in the case of CIT v. Woodward Governor India P. Ltd., 312 ITR 254 and the decision of the Special Bench of the Tribunal in the case of DCIT v. Bank of Bahrain and Kuwait, ITA No. 4404 & 1883/Mum/2004 and the decision of Hon'ble Supreme Court in the case of ONGC v. CIT, 322 ITR 180 . The learned CIT(A) observed that as per details placed on record as at 31-03-2009 , the assessee has receivable of US \$ 41,293,417 against which the forward contracts entered for sale of foreign currency and pending as on date were for an amount of US \$ 59,293,409 . Thus, it was observed by learned CIT(A) that the forward contracts were entered for an amount higher than the receivable at the year end and there appears to be no reason for the excess exposure taken by the assessee . The assessee had submitted that the excess contracts were entered into for the export orders pending on hand which were backed by the stocks held by the assessee and actual exports had taken place in the subsequent financial year. The learned CIT(A) allowed the loss on the foreign exchange forward contracts to the tune of US \$ 41,293,417 which were export receivable outstanding as at 31-03-2009 and the loss arising on forward foreign exchange contracts to the tune of excess amount of US \$ 17,999,992 was not allowed by learned CIT(A) as the said foreign exchange forward contracts were not backed by underlying asset receivable in foreign exchange as at 31-03-2009 to back it up and hence it was held by the learned CIT(A) that the aforesaid forward contracts pending as on 31-03-2009 are not for the purposes of business and loss arising on revaluation of such contract is purely notional and speculative in nature and cannot be provided on the prudence principle in computing assessee's income. Thus, the learned CIT(A) confirmed/sustained the disallowance of loss on revaluation of forward contracts amounting to Rs.9,92,48,752 which were not backed by underlying asset receivable in foreign exchange to back it up and the loss incurred by the assessee on restatement of pending forward contract agreement at year end was allowed by learned CIT(A) as business loss to the extent of Rs.

22,76,84,554/- was allowed which were backed by underlying asset being export receivable in foreign exchange, vide learned CIT(A) appellate orders dated 30/10/2012.

6. Aggrieved by the appellate order dated 30/10/2012 passed by the ld. CIT(A), both the assessee and the Revenue are in appeal before the Tribunal.

7. The ld. Counsel for the assessee submitted that the assessee is engaged in the business of import of rough diamonds, cutting and polishing the same and export of polished diamonds. The ld. Counsel submitted that the assessee imports rough diamonds to manufacture cut and polished diamonds and export the same. By importing and exporting the diamonds, the assessee is exposed to foreign currency fluctuation and to hedge against the risk of foreign currency fluctuations, the assessee has entered into foreign exchange forward contracts. The assessee has also availed working capital credit facilities from the banks which are denominated in foreign currency. It is submitted that foreign currency forward contracts were executed to hedge against the possibility of foreign exchange fluctuation loss. There was a marked to market losses incurred in respect of the forward foreign exchange contracts due to adverse movement of foreign exchange rates as at year end. It is submitted by the assessee's counsel that outstanding un-matured foreign currency forward contracts as at year end which were backed by outstanding export receivables as at yearend, the learned CIT(A) allowed the said loss which was to the tune of Rs. 22,76,84,554/-. It is also submitted by the assessee's that with respect to those un-matured outstanding forward foreign exchange contracts as at yearend which are not backed by outstanding export receivables as at yearend are in-fact backed by confirmed export orders and supported by stock purchased for execution of those confirmed export orders and these stocks are held as at yearend by the assessee against those export orders. It is submitted by learned counsel for the assessee that the exports

were undertaken in the next financial year with respect to these confirmed export orders in hand as at year end . It is submitted by learned counsel that such loss which are not backed with export receivables but backed with confirmed export orders and stock held by the assessee as at year end are not allowed by learned CIT(A) which was to the tune of Rs.9,92,48,752/- . It is submitted that these forward foreign exchange contracts were entered within the frame work of relevant RBI & FEMA guidelines and are monitored by RBI. It is submitted that the assessee is regularly following this method of accounting whereby year-end restatement or marked to market gain or loss in respect of all assets or liabilities denominated in foreign currency are restated at prevailing foreign exchange rates as at year end . The restatement of forward foreign currency contracts is followed strictly as per AS-11 prescribed by ICAI. The ld. Counsel has also invited our attention to the written submissions and paper book whereby all the details of forward foreign exchange contracts were submitted. Our attention was drawn to the orders of authorities below. Our attention was also drawn to the audited financial statements and tax audit report of the assessee which are placed in paper book filed with the Tribunal (page 4-67/PB). The details of foreign exchange difference loss/profit are placed in paper book page 136/137. It was submitted that foreign exchange gains earned on revaluation of forward foreign exchange contract as at year end was offered for tax in assessment year 2010-11 and 2011-12 and details are placed in paper book/page 134-149 and details along with assessment orders framed u/s 143(3) of the Act are placed in paper book. The details of outstanding forward foreign exchange contracts as at 31-03-2009 are placed in paper book/page 79 and prayer is made that the same may be allowed as deduction . It is also submitted that the same method is followed next year and revenue impact is tax-neutral as next year said losses were reversed and actual loss/profit on completion of the forward foreign exchange contract is debited/credited to the profit and loss account. It was submitted that the details of these losses were submitted

before the authorities below (page 109-110, 115 of paper book). The assessee submitted that in preceding years as well succeeding years the assessee consistently followed the said method of accounting, and the Revenue has accepted the said method of accounting followed by the assessee except for the impugned assessment year. The assessee placed reliance on following decisions:-

- a) London Star Diamond v. DCIT in ITA no. 6169/M/2012 vide orders dated 11/10/2013
- b) Jaimin Jewellery Exports Private Limited v. ACIT in (2014) 43 taxmann.com 380 (Mum-Trib.)
- c) Adll. CIT v. Daksh Mineral and Marines Private Limited in ITA no. 76/Mum/2013 dated 20-03-2014
- d) ACIT v. S. Rajiv and Company in ITA no. 7095/Mum/2012 dated 12-02-2014
- e) ACIT v. Monarch Gems in ITA no. 2613/Mum/2013
- f) ACIT v. Vimal Export in ITA no. 6610/Mum/2010
- g) The Paper Products Limited v. Addl. CIT in ITA no. 7761/Mum/2012
- h) CIT v. Friends and Friends Shipping Private Limited (2013) 217 Taxman 267 (Guj. HC)
- i) CIT v. Panchmahal Steel Limited (2013) 215 Taxman 140 (Guj. HC)
- j) ACIT v. Venus Jewel in ITA No. 7328 & 7329/Mum/2013 dated 31/07/2015
- k) S. Jogani Exports Private Limited v. ACIT in ITA No. 7012/Mum/2012 dated 26/02/2016
- l) Inventurus Knowledge Services Private Limited v. ITO (2016) 156 ITD 727 (Mum-Trib.)

8. The ld. D.R. relied on the order of the A.O. and also the order of the Mumbai Bench of the Tribunal in the case of S. Vinodkumar Diamonds Pvt. Ltd. v. Addl. CIT in ITA No. 506/Mum/2013 dated 3rd May, 2013.

9. In the rejoinder, the ld. Counsel for the assessee submitted that the decision of the Tribunal in the case of S. Vinodkumar Diamonds Pvt. Ltd. relied on by the ld. D.R. was duly considered in ACIT v. Venus Jewel in decided on 26/2/2016. The learned counsel for the assessee submitted that the Tribunal has given part relief to the assessee with respect to forward foreign exchange contracts which are backed with outstanding export receivables as at year end. The ld. CIT(A) denied the benefit of loss on account of revaluation of forward foreign exchange contracts as at year end which were backed by confirmed export orders supported by stock in hand held by the assessee towards those export orders , hence, this issue may be verified by the A.O. by considering the factual matrix of the case.

10. We have considered the rival contentions and also perused the material available on record including the case laws relied upon. We have observed that the assessee is engaged in the business of import of rough diamonds, cutting and polishing the same and export of polished diamonds. The assessee imports rough diamonds whereby the payments are made in foreign currency for such imports and payables are denominated in foreign currency. The assessee also exports diamonds whereby payments are received in foreign currency and receivables are denominated in foreign currency. The assessee availed working capital facility from banks , part of which are denominated in foreign currency. The assessee is stated to have entered into forward foreign exchange contracts to hedge the currency risk associated with the transactions of import and exports of diamonds to safeguard against the exchange fluctuation risk on foreign currency receivables and payables. We have observed that the assessee has entered

into forward foreign exchange contracts which have remained unsettled / un-matured at the year end and loss has occurred on the same due to foreign exchange rate variation as at year end. The loss/gain arising on the said fluctuation in foreign currency rates prevailing as at the year end on forward foreign exchange contracts were recognized and brought to P&L account and offered for taxation in the case of profit , and deductions were claimed in case of losses consistently by the assessee for several years. This policy is consistently followed by the assessee which is supported by AS-11 issued by ICAI and accepted by the Revenue except during the impugned assessment year. The revenue has brought to tax, the income arising on fluctuation in foreign exchange rates as at year end on these forward foreign exchange contracts for the assessment year 2010-11 and 2011-12 as was offered for taxation by the assessee of its own and the assessment orders framed u/s 143(3) of the Act is placed on record in paper book filed with the tribunal. . The co-ordinate Bench of the tribunal in the case of Venus Diamond(supra) has allowed the mark to market loss on outstanding un-matured forward foreign exchange contracts after considering the decision of Vinod Kumar diamonds Private Limited(supra) relied upon by learned DR and by following the decision of Hon'ble Supreme Court in the case of CIT v. Woodward Governor India Private Limited(supra) . The tribunal held that view of the tribunal in the case of Vinod Kumar Diamonds Private Limited is contrary to the view taken by Hon'ble Bombay High court in the case of Badridas Gauridu Private Limited in 261 ITR 256(Bom.). The similar view has been taken by the co-ordinate bench in the case of S.Jogani Exports Private Limited v. ACIT in ITA no. 7012/Mum/2012 vide orders dated 26/02/2016 wherein the mark to market losses on unexpired/un-matured forward foreign exchange contracts as at year end were allowed keeping in view prevailing foreign exchange rates. The Hon'ble Bombay High Court in a recent decision in CIT v. D. Chetan and Company in ITA no. 278 of 2014 vide orders dated 01-10-2016 has held that the activity of entering into foreign exchange

forward contract to cover against variation in foreign exchange rate which would impact its business of import and export of diamonds was in the regular course of business only to safeguard against the loss on account of foreign exchange variation and cannot be categorized as speculative in nature but is a business activity. The Hon'ble Bombay High Court dismissed the appeal of the Revenue in the case of CIT v. D. Chetan and Company (supra) on the grounds that no substantial question of law arises from the appeal and consequently decision of the tribunal in allowing mark to market losses of Rs. 78,10,000/- on forward foreign exchange contracts being not a notional loss was upheld. The AO has disallowed the entire loss on threshold on revaluation of forward foreign exchange contract as at year end based on prevailing foreign exchange rates considering the same to be notional loss and no enquiry to verify whether the same is supported by export receivable/import payables denominated in foreign currency have been made. The learned CIT(A) had made an enquiry and observed that as per details placed on record as at 31-03-2009, the total sale of the assessee was Rs. 961.53 crores (US \$ 217,708,068) which was denominated in foreign currency. Out of total purchase of Rs. 791.72 crores, import accounts for Rs. 690.08 crores (US \$ 161,404,740). At the year end, the creditors for goods were payable in dollar terms at Rs. 94.07 crores (US \$ 43,851,415). Similarly, exports receivable account for Rs. 209.76 crores (US \$ 41,293,418) denominated in dollar terms. The assessee had a bank loan outstanding in PCFC and FCB accounts of US \$ 25,959,035 at the year end. Thus, it was observed by the learned CIT(A) that the assessee was exposed to risk arising out of fluctuation in foreign exchange rate and as a prudent businessmen likely to hedge its risk. The ld. CIT(A) noted that assessee has booked all the forward contracts in respect of export receivables only. It was further noted that in addition to the opening outstanding forward contracts of 61,000,000 US dollars during the year under consideration, the assessee has booked forward contracts of 767,000,000 US dollar, utilized forward contracts

of 72,406,591 US dollar, cancelled forward contracts of 6,000,000 US dollar and finally held the forward contracts of 59,293,409 US dollar at the year end. Thus, the assessee has entered into the forward contracts during the normal course of business and utilized the same for business by allowing them to run up to the date of contract. The assessee has receivable of US \$ 41,293,417 against which the forward contracts entered for sale of foreign currency and pending as on date were for an amount of US \$ 59,293,409 . Thus, it was observed by learned CIT(A) that the forward contracts were entered for an amount higher than the receivable at the year end and there appears to be no reason for the excess exposure taken by the assessee . The assessee had submitted that the excess contracts were entered into for the export orders pending on hand which were backed by the stocks held by the assessee and actual exports had taken place in the subsequent financial year. The learned CIT(A) allowed the loss on the foreign exchange forward contracts to the tune of US \$ 41,293,417 which were backed by export receivable outstanding as at 31-03-2009 and marked to market loss on forward foreign exchange contract of 22,76,84,554/- was allowed by learned CIT(A) as the same were backed by export receivable outstanding as on 31-03-2009. The ld. DR could not show us any perversity in the afore-stated finding of learned CIT(A). In our considered view, such marked to market losses with respect to the unsettled/un-matured foreign currency forward contracts on account of revaluation at the year end on the basis of exchange rates prevailing as at year end should be allowed to the assessee as business loss as the same is supported by export receivables outstanding as at year end arising out of normal trading activities of export-import of diamonds undertaken by the assessee. In our considered view , the said loss of Rs. 22,76,84,554/- arising out of forward foreign exchange contracts entered into to hedge against exchange fluctuations and which are backed by the underlying exposure in foreign currency towards exports of diamonds against

which there are export receivables outstanding as at year end denominated in foreign currency and by entering into forward contracts in foreign exchange and as such, the forward contracts entered were for the purpose of the business to hedge against the forex loss and that the assessee has not entered into the forward contracts with an intention to earn any gain due to fluctuation in foreign currency rate but it is necessary for it to enter into such forward contracts to hedge against foreign exchange rate fluctuation and which are incidental to the export-import business of the assessee as in the absence of such forward contracts, the assessee may sustain huge losses and hence it became essential for the assessee to book such forward contracts as a prudent business practices to safeguard against losses which may be sustained by the assessee towards outstanding receivables as on 31-03-2009 on exports made by the assessee outstanding as at year end. Further, we find that the assessee is engaged in the business of manufacture of import of rough diamonds and export of polished diamonds , and not in the business of foreign exchange. The decision of Hon'ble Supreme Court in the case of Woodward Governor India P. Ltd. (supra) relied upon by the assessee will be applicable as the losses are towards hedging against export receivable in foreign currency outstanding as at year end towards export of polished diamonds undertaken by the assessee and cannot be categorized as notional loss or speculative loss as per provisions of Section 43(5) of the Act. The learned CIT(A) has allowed the loss of Rs. 22,76,84,554/- as deduction while computing income of the assessee being arising out of fluctuation in forward foreign exchange contracts due to adverse movement of foreign currency exchange rate at year end as the said forward foreign exchange contracts are backed by export receivables outstanding as on 31-

03-2009 and we do not find any perversity in the order of learned CIT(A) as learned DR could not point any defect/mistake in the finding of learned CIT(A), which we confirm/sustain and the grounds raised in the Revenue appeal is dismissed. With respect to the deduction of Rs. 9,92,48,752/- disallowed by the learned CIT(A) arising out of fluctuation in foreign currency rates on forward foreign exchange contracts which are not backed by the export receivables but are stated to be backed with confirmed export orders against which the assessee had stated to have purchased stock and such stock being held by the assessee as on 31-03-2009 with respect to the confirmed export orders in hand, as against which the exports are stated to be made in subsequent financial year, needs verification by the AO of the contentions of the assessee, and hence interest of justice will be best served if the matter is set aside and restored to the file of AO for verification of contentions of the assessee and for fresh determination of the matter on merit in accordance with our directions as contained in this order. If after verification and enquiry it is found by the AO that the said forward foreign exchange contracts are backed by stock purchased and held by the assessee as at year end which are backed by purchased for executing confirmed export orders in hand, which export orders are executed in next financial year, the loss shall stand allowed after such verification and enquiry by the AO as the assessee by holding confirmed export orders denominated in foreign currency and holding stock for execution of those export orders as at year end has definitely exposed itself to foreign currency exchange risk associated with fluctuation in foreign exchange rates as at year end, as the export orders is stated to be executed in the next financial year and such loss is neither notional or speculative loss u/s 43(5) of the Act as it is stated to be backed with stock held by the assessee as at 31-03-2009 and confirmed export orders which are stated to be executed in subsequent financial year. In any case, revenue impact in allowing the said loss is tax-neutral as the said loss is stated to be reversed by the assessee in the subsequent financial year by

way of credit to the profit and loss account, and actual loss is debited to Profit and Loss Account wherein net loss/profit is claimed in the subsequent assessment year in the return of income which contention of the assessee shall also need to be verified by the AO by looking into the return of income for subsequent assessment year(s) to ensure that revenue impact is tax-neutral and there is no loss to Revenue. Thus the matter is set aside and remanded to the file of A.O. for verification of the contentions of the assessee and for redetermination of the issue on merits after necessary verifications and enquiry as directed by us. Needless to say that proper and adequate opportunity of being heard shall be provided by the AO to the assessee in accordance with principles of natural justice in accordance with law and the assessee shall be allowed to place all relevant evidences and material on record to substantiate its contentions. We order accordingly.

11. In the result, the appeal filed by the assessee in ITA No. 7311/Mum/2012 is allowed for statistical purposes and the appeal filed by the Revenue in ITA No. 112/Mum/2013 for the assessment year 2009-10 is dismissed as indicated above.

Order pronounced in the open court on 7th November, 2016.

आदेश की घोषणा खुले न्यायालय में दिनांक: 07-11-2016 को की गई ।

Sd/-
(C.N. PRASAD)
JUDICIAL MEMBER

sd/-
(RAMIT KOCHAR)
ACCOUNTANT MEMBER

मुंबई Mumbai; दिनांक Dated 07-11-2016

I

आदेश की प्रतिलिपि अग्रहित/Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant
2. प्रत्यर्थी / The Respondent.
3. आयकर आयुक्त(अपील) / The CIT(A)- concerned, Mumbai
4. आयकर आयुक्त / CIT- Concerned, Mumbai
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, मुंबई / DR, ITAT, Mumbai "E" Bench
6. गार्ड फाईल / Guard file.

सत्यापित प्रति //True Copy//

आदेशानुसार/ BY ORDER,

उप/सहायक पंजीकार (Dy./Asstt. Registrar)
आयकर अपीलीय अधिकरण, मुंबई / ITAT, Mumbai