

**IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD 'B' BENCH, HYDERABAD.**

**BEFORE SHRI RAMA KANTA PANDA, ACCOUNTANT MEMBER AND
SHRI LALIET KUMAR, JUDICIAL MEMBER**

**ITA No.85/Hyd/2021
(Assessment Year : 2008-09)**

M/s.Sai Life Science Ltd.,
Hyderabad.
PAN AAEC6143F

.....Appellant.

Vs.

Asst. Commissioner of Income Tax,
Central Circle 3(1), Hyderabad.

.....Respondent.

Appellant By : Shri V. Siva Kumar for Shri S. Rama Rao.
Respondent By : Shri Rohit Majumdar. (D.R.)

Date of Hearing : 19.05.2022.

Date of Pronouncement : 31.05.2022.

O R D E R

Per Shri Rama Kanta Panda, A.M. :

This appeal filed by the assessee is directed against the order dt.15.06.2020 of the learned Commissioner of Income Tax (Appeals)-10, Hyderabad relating to Assessment Year 2008-09.

2. There is a delay of 147 days in filing of this appeal by the assessee for which the assessee has filed an application

seeking condonation of delay along with an Affidavit. It is explained in the condonation application that the corporate office was closed due to Covid 19 and after reopening also most of the employees were working from home. Therefore, the order of the CIT (Appeals) could not reach the concerned person and remained with the receiving desk clerk of company unattended. Subsequently, it was traced and the consultant was approached for filing the appeal before the Tribunal. The Consultant office was also functioning partially due to covid 19 and was working with lesser staff for which there was a delay in filing of the appeal before the Tribunal. After hearing both the sides and after perusal of the contents of the condonation application along with an Affidavit filed by the assessee, the delay in filing of the appeal is condoned and appeal is admitted for hearing.

3. The facts of the case, in brief, are that the assessee is a company engaged in the business of export of pharma products as 100% EOU and filed its Return of Income on 30.09.2008 declaring total income of Rs.33,96,798.

Subsequently, a revised return was filed by the assessee declaring a total income of Rs.51,31,934.

3.1 During the course of assessment proceedings, the Assessing Officer noted from the details furnished by the assessee that the assessee company had entered into forward contract, options contracts and derivative contracts equivalent to Rs.1,13,12,44,375. The company recognized a notional loss on Mark to Market losses on the above contracts and made a provision of Rs.1,97,91,087 as exchange fluctuation loss for the forward contracts entered under the head "Gain/Loss on Exchange Fluctuation" in the P&L Account which was not added back to the Book Profit as per provisions of sub-clause (d) of Expln. (1) to Section 115JB of the Income Tax Act, 1961 (in short 'the Act'). The provision for loss/expense is not for an ascertained liability but is a notional entry for loss. The Assessing Officer therefore made an addition of Rs.1,97,91,087 on account of provisional loss on the forward/option/derivative contracts.

4. Aggrieved the assessee filed an appeal before the CIT (Appeals) and furnished various details based on which the

CIT (Appeals) called for a remand report from the Assessing Officer. After considering the remand report submitted by the Assessing Officer and rejoinder of the assessee to such remand report, the CIT (Appeals) upheld the action of the Assessing Officer by observing as under :

7. All the grounds of appeal as well as the additional ground of appeal raised by the appellant are dealt with conjointly both on the facts of the case as well as the law laid down by the Act including the clarificatory instruction as well as the judicial support taken by way of legal precedents.

8. To understand the case, the relevant part of Sec. 115JB of I.T. Act, 1961 is reproduced below: (i.e. explanation (1) to Sec. 115JB)

"Sub-clause (d) of Explanation(1) – for the purposes of this sec. 'Book Profit' means the (profit) as shown in the (statement of profit and loss) for the relevant previous year prepared under Sub-Section(2) as increased by –

- 1. The amount of income tax paid or payable, and the provision therefor; or*
- 1. The amounts carried to any reserves, by whatever name called (other than a reserve Specified under Sec. 33AC); or*

(c) The amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liabilities; or

9. Further CBDT has also given a circular clearly laying down that "Foreign Exchange fluctuation Loss" is not an ascertained liability which is reproduced here for the purpose of clarity :-

"Instruction No. 03/2010, dt. 23.03.2010

- 1. Foreign Exchange derivative transactions entered into by the corporate sector in India have witnessed a substantial growth in recent years. This combined with extreme volatility in the foreign exchange market in the last financial year is reported to have resulted in substantial losses to an assessee on account of trading in forex-derivatives.*

A large number of assesseees are said to be reporting such losses on 'market to market' basis either suo motu or in compliance of the Accounting Standard or advisory circular issued by the Institute of Chartered Accountants. The issue whether such losses on account of forex-derivatives can be allowed against the taxable income of an assessee has been considered by the Board. In this connection, I am directed to say that the Assessing Officers may follow the guidelines given below:

"Marked to Market Losses":

2. "Marked to Market" is in substance a methodology of assigning value to a position held in a financial instrument based on its market price on the closing day of the accounting or reporting record. Essentially, 'Marked to Market' is a concept under which financial instruments are valued at market rate so as to report their actual value on the reporting date. This is required from the point of view of transparent accounting practices for the benefit of the shareholders of the company and its other stakeholders. Where companies make such an adjustment through their Trading or Profit/Loss Account, they book a corresponding loss (i.e. the difference between the purchase price and the value as on the valuation date) in their accounts. This loss is a notional loss as no sale/conclusion/settlement of contract has taken place and the asset continues to be owned by the company.

A 'Marked to Market' loss may be given different accounting treatment by different assessees. Some may reflect such loss as balance sheet item without making any corresponding adjustment in the Profit and Loss Account. Other may book the loss in the P&L a/c which may result in the reduction of book profit. In case where no sale or settlement has actually taken place and the loss on Marked to Market basis has resulted in reduction of book profits, such a notional loss would be contingent in nature and cannot be allowed to be set off against the taxable income. The same should therefore be added back for the purpose of computing the taxable income of an assessee.

3. Treatment of loss from actual transactions in forex-derivatives

In a case where a loss on a forex-derivative transaction arises on actual settlement/conclusion of contract and is not a notional or marked to market book entry, a further question will arise as to whether such a loss is on account of a speculative transaction as contemplated in Sec. 43(5) of the I.T. Act. For determining whether loss from a transaction in respect of a forex-derivative is a speculation loss or not, the AO may refer to Proviso (d) below sub-section (5) of Sec. 43 inserted by the Finance Act, 2005, with effect from 01.04.2006. It lays down that any 'eligible transaction' in respect of trading in derivatives referred to in clause (ac) of sec. 2 of the Securities Contracts (Regulation) Act, 1956, that has been carried out in a recognized stock exchange shall not be treated as a speculative transaction. Further, an 'eligible transaction' for this purpose would be one that fulfils the conditions laid down in Explanation to Sec. 43(5)(d). Any loss in a speculative transaction can be set off only against profit from speculative transactions.

As the revenue implications of such transaction are large, the Assessing Officers need to examine the statements of accounts and the notes to accounts with a view to find out any reference to any loss on account of forex-derivatives. In some cases, these losses may be camouflaged under the 'financial charges' 'foreign exchange loss' or some similar head which may make it difficult to detect them. In such cases, the Assessing Officers should make a specific query asking the assessee to give a break

up of any 'Marked to Market' loss on a forex-derivatives included in the profit and loss account and examine whether such transactions are 'eligible transaction' in terms of Sec. 43(5)(d). An adjustment to taxable income may therefore be made, if necessary, keeping in view the provisions of law referred to above."

10. The judicial authorities have, however, taken a different view with respect to the above legal provision as well as the instruction. In fact, ITAT, Hyderabad has laid down, as under, in ITA No 1222 of 2016, DCIT vs. Suven Life Sciences Ltd. Hyderabad, stating that a circular is not binding on the appellate authorities which is reproduced below for the sake of clarity :-

"Having heard both the parties and having considered their rival contentions, we find that undisputedly, the assessee had entered into foreign exchange forward contract to hedge against risks of foreign exchange fluctuations and though the contract has not matured during the relevant financial year, in order to arrive at actual profits or loss to the assessee, if followed the Accounting Standard 11 and 31 issued by ICAI as notified by Sec. 211(3C) of the Companies Act and had debited the loss on account of 'mark to market losses' as on the closing day of the accounts and claimed it as allowable as business loss. We find that Instruction No.3 of 2010 of CBDT has been reproduced by the CIT(A) at Para 7.4 of his order. As per this instruction, where no sale or settlement has actually taken place and the loss oil, contract has not matured, the loss on 'marked to market' basis has resulted in reduction of book profits, such a notional loss would be contingent in nature and cannot be allowed to be set off against the taxable income and should, therefore, be added back for the purpose of computing the taxable income of an assessee. No doubt, this instruction is clearly on the point and is binding on the assessing authority. However as rightly pointed out by the CIT(A) and as held by the Hon'ble Supreme Court in the case of Hero Cycle Pvt. Ltd. (cited Supra), such instructions are not binding on the assessee nor on the appellate authority, who are entitled to examine the issue on merits and arrive at their own conclusions. The Hon'ble Supreme Court in the case of Woodward Governor of India Pvt. Ltd., reported in 312 ITR 254, has held that the loss suffered by the assessee on account of fluctuation in the rate of foreign exchange as on the date of the balance sheet is an item of expenditure u/s 37(1) of the I.T. Act, 1961."

Judicial discipline contemplates that the undersigned should follow the law laid down by Honourable ITAT, Hyderabad.

11. However, the facts of the case are different from the above case, as the A.O has clearly stated as under in his remand report dt.15.09.2017. The report of the AO is again being reproduced for the sake of clarity at the cost of repetition. The report reads as under:

"The assessee submitted that the foreign exchange fluctuation loss of Rs. 1,97,91,087/- incurred during the AY 2008-09 was reversed in the books of the

assessee in the AY 2009-10.

In this connection, it is submitted that on verification of the assessment record for AY 2009-10, it is noticed that the assessee claimed 'foreign exchange loss, Net' of Rs. 18,80,61,151/-. It is not clear from the record whether the assessee has actually reversed the amount of Rs. 1,97,91,087/- in the AY 2009-10. Hence, it is requested that the appeal may be decided on merits.

With regard to the admissibility of additional evidence, it is seen that the return for the AY 2009-10 was filed on 29.09.2009 and filed revised return on 15.10.2010, which were well before the completion of assessment for AY 2008-09 i.e., 24.11.2010. The additional evidence was not submitted by the assessee during the assessment proceedings for AY 2008-09. Therefore, the claim of the assessee may not be accepted."

12. At this juncture, it is also necessary to reiterate the additional ground taken up by the A.R of the appellant wherein, in 2009-10, the department itself has passed an order u/s. 154 and deleted the addition to the extent of Rs. 4,34,22,500/-. The learned CIT(A)-3 had dismissed the appeal treating the appeal as infructuous, as the said addition was deleted via the route u/s 154, passed by the A.O.

13. Now, passing this order u/s 154 by the A.O do not prove anything here.

What is relevant for this year is, that the appellant has booked a "Marked to market loss on foreign exchange on certain contracts and booked a "Notional loss" on contracts not expired taking the value of the foreign exchange on the Balance Sheet date i.e. 31.03.2008 via a journal entry. The Book profit so arrived on the Balance Sheet date was taken as the "Book Profits" as arrived u/s 115JB and taxes.were paid accordingly. The same was said to be reversed on 31.08.2008 and on 30.09.2008 for an amount of Rs. 82,46,286/- and Rs.1,15,44,801/- via journal entry and ledger a/c copies of the same were produced before the undersigned.

14. The fact, however, remains, that the appellant failed to demonstrate, as to which contracts the losses occurred, and on maturity of which contracts, the gain was written back. In short, the basis for "loss-booking" as well as "Reversal Entry" passed on 31.08.2008 for an amount of Rs. 82,46,286/- and on 30.09.2008 for an amount of Rs. 1,15,44,801/- was not evidenced by any proof. Further, the appellant was not clear as to what is the exact amount of MTM loss. That is why the appellant company in its normal computation of tax has added back an amount of Rs. 97,91,087/- to normal income as loss on account of unexpired forward contracts / MTM loss. The basis for the calculation of Rs.97,91,087/- is not there. The appellant added back the amount not only in its original return of income but also while filing its revised return of income. The appellant has requested for this claim as an allowable expenditure as

per Section 37 of the I.T. Act. It is not known as to how the appellant has calculated Rs. 97,91,087/- as MTM loss instead of Rs.1,97,91,087/-. This clearly shows that the appellant company itself is not clear about the exact amount of MTM loss suffered by it. Thus, the appellant's case does not fall under the principles laid down in Woodward Governor as above. The claim by the appellant of loss amounting to Rs. 97,91,087/- in stead of Rs. 1,97,91,087/- goes on to demonstrate that there are strong and sufficient reasons to indicate that the accounts of the appellant company are unreliable.

14.1 In fact, the Hon'ble Supreme Court in its decision in CIT vs. M/s. Woodward Governor India P. Ltd. [312 ITR 254] has lucidly discussed about Sections 28, 29, 37(1) and 145 as well as Sections 43 (1) and 43A and held as under in para No. 14:

"That is why in deciding the question as to whether the word "expenditure" in Section 37(1) includes the word "loss" one has to read Section 37(1) with Section 28, Section 29 and Section 145(1). One more principle needs to be kept in mind. Accounts regularly maintained in the course of business are to be taken as correct unless there are strong and sufficient reasons to indicate that they are unreliable."

15. The accounts of a company are generally running accounts and hence, the time line of an accounting entry extends from one year to another and it is not possible to look at an accounting entry specific assessment year- wise. Hence, the booking of an entry in a particular year and the reversal of an entry in the next year needs to be studied together. The genuineness of an entry is studied from the source year and might continue for next several years each constituting a separate accounting year. In this particular case, there are no doubt journal entries. This is a fact not in dispute. However, what needs to be seen is how reliable are these entries. The appellant had made a claim for MTM loss at Rs. 97,91,087/- and added back the same as disallowable to the normal computation. This was done not only while filing the original return of income but also while filing revised return. The appellant by claiming this amount as disallowable demonstrates that the accounts of the appellant company are somehow unreliable. The point of inquiry starts here. The appellant could not effectively prove why it had claimed Rs. 97,91,087/- as MTM loss for disallowance and why it had adopted Rs. 1,97,91,087/- as MTM loss for booking book profits u/s. 115JB at the time of filing of return.

15.1 No doubt, legal precedents are binding. But facts in each case are distinguishable. On this fact, the present case differs from the case of ITA No. 1222 of 2016, Suven Life Sciences Ltd, Hyderabad, wherein, Hon'ble ITAT has passed the order. The same applies to all other judicial precedents.

16. Further the explanation to Sec. 115JB strengthened by a clarificatory Circular No. 3/2010 meets the Doctrine of legitimate expectation. This case does not call for an occasion for interpretation of a provision in view of non-controversial meaning in plain language.

17. All the grounds of appeal no. 1 to 5 including the additional ground of appeal raised by the appellant are dismissed.

5. Aggrieved with such order of Id. CIT (Appeals), the assessee filed appeal before the Tribunal by making the following grounds :

“ 1. The learned (IT (Appeals) erred in fact and law in considering the amount of Rs.1,97,91,087/-Exchange Fluctuation loss on unexpired forward contracts as notional and unascertained liability and disallowing the same in computing Book profits under section 115JB of Income Tax Act in determining tax under Minimum alternate Tax ignoring the established position of law in this regard.

2. The learned CIT (Appeals) erred in fact and law by making disallowance of Rs.1,97,91,087/in computing the book profits under provisions of section 115JB being Exchange Fluctuation loss on unexpired forward contracts ignoring the fact that the exchange fluctuation loss entry is passed in the books of accounts pursuant to Accounting standard AS-11 under section 311 C of Companies Act 1956 mandatorily to be followed as per companies act and is an allowable expenses under Income tax Act.

3. The (IT (Appeals) erred in fact and law in not considering the fact that the amount of Rs.1,97,91,087/- being Exchange Fluctuation loss on unexpired forward contracts booked on 31st march of 2008 is reversed in the subsequent financial year 2008-09 as per the method of accounting regularly followed by the assessee company and as a result there is no loss of revenue to the Income Tax Department and as a result the amount of Rs.1,97,91,087/- has the effect of getting disallowed twice.

4. Any other ground/s may please be allowed at the time of hearing of appeal.”

6. We have heard the rival arguments made by both the sides, perused the orders of authorities below and the paper

book filed on behalf of the assessee. We have also considered the various decisions cited by the learned counsel for the assessee. We find the learned CIT (Appeals) rejected the arguments made by the assessee on the ground that the assessee was not clear as to what is the exact amount of MTM loss and the basis of the calculation of Rs.97,91,087. The assessee was also unable to explain the loss suffered by it on the basis of each contract. It is the submission of the learned counsel for the assessee that the assessee had filed detailed submission furnishing contract-wise loss or profit and that the learned CIT (Appeals) failed to consider the same. From the various details filed by the assessee in the paper book, we find the assessee has filed the following details before the lower authorities which have not been properly appreciated by them.

“ i) Statement showing loss on forward contracts & options contract.

ii) Abstract of forward contract fo the year ended on 31st March, 2008.

iii) Profit and loss account and Balance Sheet for the year ended 31st March, 2009.

- iv) Schedules forming part of P&L account for the year ended 31.03.2009.*
- v) Summary of forex loss for the FY 2008-09 & Ledger statements for the period from 1.4.2008 to 31.3.2009.*
- vi) Ledger extract of Exchange Fluctuation – SBI for the period from 1.4.2008 to 31.3.2009.*
- vii) Ledger extract of Dollar Fluctuation for the period from 1.4.2008 to 31.3.2009.*
- viii) Ledger extract of Exchange Fluctuation (Transaction) for the period from 1.4.2008 to 31.3.2009.*
- ix) Ledger extract of Exchange Fluctuation (Transaction) of Unit-1 & 2 Division B.*
- x) Ledger extract of Exchange Transaction – Unit - 3 for the period from 1.4.2008 to 31.3.2009.*
- xi) Ledger extract of Exchange Transaction – Unit - 4 for the period from 1.4.2008 to 31.3.2009.*
- xii) Ledger extract of Unit – 1 & 2, Division – A.*
- xiii) Ledger extract of Exchange Fluctuation (Transaction) of Unit – 3.*
- ix) Ledger extract of Exchange Fluctuation (Transaction) of Unit – 4.*
- x) Ledger extract of Dollar Fluctuation of Unit – 5 for the period from 1.4.2008 to 31.3.2009.”*

7. On a pointed query raised by the Bench as to whether the assessee has explained the activities carried on by the assessee are related to or linked with the business or not, the learned counsel for the assessee submitted that given an opportunity, the assessee is in a position to substantiate

with evidence to the satisfaction of the Assessing Officer that the activities carried out by the assessee are related to the business of the assessee. Since the lower authorities in the instant case have not appreciated the facts of the case properly as per the details filed by the assessee, therefore, considering the totality of the facts of the case and in the interest of justice we deem it proper to remit the issue to the file of Assessing Officer with a direction to adjudicate the issue afresh and in accordance with law after giving due opportunity of being heard to the assessee. We hold and direct accordingly. The grounds raised by the assessee are allowed for statistical purpose.

8. In the result, the appeal of the assessee is allowed for statistical purposes.

Order pronounced in the open court on 31st May, 2022.

Sd/-

(LALIET KUMAR)
Judicial Member

Sd/-

(RAMA KANTA PANDA)
Accountant Member

Hyderabad, Dt. 31.05.2022.

* Reddy gp

Copy to :

1.	M/s. Sai Life Sciences Ltd., (Formerly known as Sai Advadvantium Pharma Ltd.), SLN Terminus, L4-01 & 02, Survey No.133, Gachibowli-Miyapur Road, Gachibowli, Hyderabad-500 032
2.	ACIT, Central Circle 3(1), Hyderabad.
3.	Pr. C I T-3, Hyderabad.
4.	CIT(Appeals)-10, Hyderabad.
5.	DR, ITAT, Hyderabad.
6.	Guard File.

By Order

Sr. Pvt. Secretary, ITAT, Hyderabad.