

आयकर अपीलिय अधिकरण, 'डी' न्यायपीठ, चेन्नई
**IN THE INCOME TAX APPELLATE TRIBUNAL
'D' BENCH, CHENNAI**

श्री महावीर सिंह, उपाध्यक्ष एवं श्री एस. आर. रघुनाथा, लेखा सदस्य के समक्ष
**BEFORE SHRI MAHAVIR SINGH, HON'BLE VICE PRESIDENT AND
SHRI S. R. RAGHUNATHA, HON'BLE ACCOUNTANT MEMBER**

आयकर अपीलसं./ITA No.: **1363/Chny/2023**
निर्धारणवर्ष / Assessment Year: 2008-09

Assistant Commissioner of
Income Tax, Central Circle -1(1) v.
No.46, M.G. Road,
Nungambakkam,
Chennai – 600 034.

Coastal Energy Private Limited
(under Official Liquidator),
Old No.22, New No.28, Menod
Street, Purasawakkam,
Chennai – 600 007.

[PAN: AAACC-4160-A]

(अपीलार्थी/Appellant)

(प्रत्यर्थी/Respondent)

आयकर अपीलसं./ITA Nos.: **1364, 1365 & 1366/Chny/2023**

निर्धारणवर्ष / Assessment Years: 2011-12, 2012-13 & 2013-14

Coastal Energy Private Limited
(under Official Liquidator),
Old No.22, New No.28, Menod
Street, Purasawakkam,
Chennai – 600 007.

[PAN: AAACC-4160-A]

(अपीलार्थी/Appellant)

Deputy Commissioner of Income
Tax,
Corporate Circle -1(2), Chennai.
(Now assessed by Assistant
Commissioner of Income,
Central Circle -1(1), Chennai.

(प्रत्यर्थी/Respondent)

Assessee by : Shri. B. Ramakrishnan, FCA

Department by : Shri. A. Sasikumar, CIT

सुनवाई की तारीख/Date of Hearing : 11.09.2024

घोषणा की तारीख/Date of Pronouncement : 25.10.2024

आदेश / O R D E R

PER S. R. RAGHUNATHA, ACCOUNTANT MEMBER:

These appeals are filed by both revenue and the assessee
against the separate order of the Commissioner of Income Tax

(Appeals)-18, Chennai for all the four assessment years dated 29.09.2023. Since, facts are identical and issues are common in all the appeals, for the sake of convenience we adjudicate the appeal filed by the revenue for the assessment year 2008-09 as lead case and the result of the same will be applicable to all other assessment years as well.

ITA 1363/CHNY/2023 - AY 2008-09:

2. The revenue has raised the following grounds of appeal:

"1. The order of the Id. CIT(A) is opposed to law and facts of the case.

2. The Id. CIT(A) erred in deleting the disallowance of Provision for Forex loss amounting to Rs,4,09,91,273/-

2.1 The Id. CIT(A) has erred in stating that the loss is allowable as per the Hon'ble Supreme Court decision in the case of CIT vs. Woodward Governor India (P) Ltd. 312 ITR 254 without appreciating that the said decision is not applicable to the facts of the instant case as the assessee has only a provision for forex loss which has not been computed on scientific basis.

2.2 The Id. CIT(A) has failed to appreciate that in terms of the CBDT Instruction No.03/2010, Marked to Market losses where there is no actual settlement cannot be allowed and in the instance case, the assessee has only made a journal entry at the year end and as such the said provision made by the assessee is not allowable business loss.

3. The Id. CIT(A) has erred in deleting the disallowance on account of Forex loss on Forward contract amounting to Rs.1,10,81,279/-.

3.1 The Id. CIT(A) has failed to appreciate that in the instant case the loss has occurred only due to premature cancellation of forward contracts and as such as held by

the Hon'ble ITAT Chennai in the cases of DCIT vs. Aswini Fisheries P.Ltd, ITA No.2246/Mds/2014 dated 18.12.2015 and Cotton Blossom India P Ltd vs JCIT (2016) 68 taxmann.com 38, such loss cannot be considered as business loss.

4. For these grounds and any other ground including amendment of grounds that may be raised during the course of the appeal proceedings, the order of the Id.CIT(A) may be set aside and the additions/disallowances made by the Assessing Officer be restored.”

3. The brief facts of the case are that the assessee is a private limited company incorporated under the Companies Act, 1956 and is engaged in providing Fuel Management Solutions for Fossil Fuel Users and supply of Fossil Fuel. The assessee being a trader in imported coal has entered into forward contracts with banks in order to cover itself against the risk of foreign exchange fluctuation. This has been undertaken by the assessee only to mitigate the loss arising on settlement made for the imports made by the Company. The assessee filed its return of Income u/s.139(1) of the act on 29.09.2008 admitting a total income of Rs.16,09,22,079/-. The assessment was completed u/s.143(3) of the Act on 19.10.2012. Subsequently, the case was reopened u/s.148, since the AO is of the opinion that the income to the extent of Rs.5,20,72,552/- has escaped assessment stating that the assessee did not disallow the year end provision on foreign exchange fluctuations and loss on

forward contract. The re-assessment was completed vide order u/s 143(3) r.w.s 147 of the Act for AY 2008-09 on 30.03.2016, by disallowing the provision for foreign exchange fluctuations of Rs.4,09,91,273/- and loss on forward contract of Rs.1,10,81,279/-. Aggrieved by the reassessment order of the AO, the assessee preferred an appeal before the Ld.CIT(A) – 18, Chennai.

4. The Id.CIT(A) after careful consideration of the findings of the AO in his order and the submissions made by the assessee, deleted the additions made in the reassessment order by relying on the decision of the Hon'ble Supreme Court in the of CIT, Delhi Vs. Woodward Governor India (P) Ltd 312 ITR 254(SC) by holding as under :

"10. Decision along with the Reasons:

10.1 In this case, the original assessment was completed u/s 143(3) on 19.10.2012 and the proceedings for re-assessment was initiated by issue of notice u/s 148 on 19.03.2015. One of the main reasons recorded by the Assessing Officer is that

"At the time of making year end provision, the opening balance of the provisions made in the earlier years, its withdrawal / utilization during the current year, the closing balance in the current year have not been disclosed. No foreign exchange gain/loss reserve/ provisions the balance sheet. Thus, it is clear that only restatement in respect of the outstanding at the yearend are only made year after year by debit the P&L account, without any adjustments in the subsequent year(s). In view of the above, the assessee's claim of forex loss, both at the time of

remittances through banks and for the provisions made in the year end restatements is not in order."

10.2 It is seen that the two additions made in the assessment order under challenge in this appeal are inter-connected: i) Disallowance of provision for forex loss of Rs.4,09,91,273/- and ii) disallowance of forex loss on forward Contract of Rs. 1,10,81,279/-. These amounts were shown together in Schedule 23-Financial Expenses as Exchange Fluctuation'.

10.3 In respect of the disallowance with regard to foreign exchange loss of Rs.4,09,91,273/-, the AO has made the disallowance observing that (i) the assessee has not proved with any evidence that the year-end provision made was not for the purpose of reducing the tax liability and ii) the assessee also not proved that provision is ascertained one and ii) the assessee has not proved that the same was computed on scientific basis.

10.4 In respect of the addition of Rs.1,10,81,279/- as forex loss on forward contracts, the AO has observed that the transactions entered into by the assessee were not hedging transactions but the same were speculative and therefore the assessee's case is not covered by proviso to (a) to section 43(5) of the Act. The AO has further held that the finding rendered in the decision of the Bombay High Court in the case of Bharat R Ruia (HUF) INCOME TAX APPEAL NO. 1539 OF 2010 dated 18th April, 2011 where the Court has held that future contracts for purchase / sale of an underlying security permitted to be traded on the stock exchange and settled otherwise than by actual delivery would be speculative transactions under Section 43(5) of the Act, would be apply to the facts of assessee's case and disallowed the same.

10.5 On the other hand, the assessee submitted that the total foreign exchange fluctuation loss claimed is actually Rs.8,02,49,839/- consisting of year-end translation loss of Rs.4,09,91,273/- (restatement of foreign Currency) and remittance loss of Rs.3,92,58,566/- on transactions during the year.

10.6 The assessee also claimed that the year-end provision is made in compliance with Accounting Standard AS11 and in the subsequent year, the difference between the reinstated rate and payment rate has been captured under exchange fluctuation remittance ledger account. The break-up of exchange loss claimed as given by the assessee is as under:

Details	Remittance	YE Provision	Exchange Loss	Total

CHENNAI	-33,13,097	2,81,77,287	75,86,272	3,24,50,462
MUMBAI	3,49,80,697	1,28,13,986	4,695	4,77,99,377
Total as per Tally	3,16,67,599	4,09,91,273	75,90,967	8,02,49,838

Note

Total as above	8,02,49,839	
Provision	4,9,91,273	Classified under exchange fluctuation and disallowed (by Assessing Officer)
Classified in purchases	2,81,77,287	Classified in purchases
Balance	1,10,81,279	Classified under exchange fluctuation and disallowed (by the AO)

10.7 In other words, the total amount of exchange loss of Rs.8,02,72,552/- in Sch.23 of the P&L a/c and the balance Rs.2,81,77,287 is shown as part of purchases of Rs.1087,79,37,8417/-.

10.8 In respect of the exchange loss on forward contracts, the assessee submitted that sometimes due to fund constraints, the company may in a position to honour the vendor payments and under such circumstances if the same is under forward cover, the company will have to cancel the forward Contracts and rebook the same. This difference as a result of cancellation (Gain/loss) is also booked in Forex loss or gain on settlement.

10.9 The assessee also submitted that these are purely commercial transaction based on underlying purchase invoices and with a genuine intention to cover exchange risks and not speculative as suggested in the Assessment Order.

10.9 The assessee has also stated that exchange loss booked in the next year represent only the difference between the year-end provision and actual remittance rate which also Confirms the fact that there is no element of speculation involved but is compliance related. The assessee has also relied On various case-laws.

10.10 It is seen that assessee has made year-end provision as per Accounting Standard AS11 and the Hon'ble Supreme Court in the case of CIT, Delhi vs Woodward Governor India (P) Ltd 312 ITR 254 (SC) has held as under:

18. AS-11 deals with giving of accounting treatment for the effects of changes in foreign exchange rates. AS-11 deals with effects of Exchange Differences. Under para 2, reporting currency is defined to mean the currency used in presenting the financial statements. Similarly. The words 'monetary items' are defined to mean money held and assets and liabilities to be received or paid in fixed amounts, e.g. , cash, receivables and payables. The word "paid" is defined under Section 43(2). This has been discussed earlier. Similarly, it is important to note that foreign currency notes, balance in bank accounts denominated in a foreign currency, and receivables/payables and loans denominated in a foreign currency as well as sundry creditors are all monetary items which have to be valued at the closing rate under AS-11 Under para 5, a transaction in a foreign currency has to be recorded in the reporting currency by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the transaction. This is known as recording of transaction on Initial Recognition. Para 7 of AS-11 deals with reporting of the effects of changes in exchange rates subsequent to initial recognition. Para 7(a) inter alia states that on cash balance sheet date monetary items, enumerated above, denominated in a foreign currency should be reported using the closing rate. In case of revenue items falling under Section 37(1), para 9 of AS-11 which deals with recognition of exchange differences, needs to be considered. Under that para, exchange differences arising on foreign currency transactions have to be recognized as income or as expense in the period in which they arise, except as stated in para 10 and para 11 which deals with exchange differences arising on repayment of liabilities incurred for the purpose of acquiring fixed assets, which topic falls under Section 43A of the 1961 Act. At this stage, we are concerned only with para 9 which deals with revenue items. Para 9 of AS-11 recognises exchange differences as income or expense. In cases where, e.g., the rate of dollar rises vis-à-vis the Indian rupee, there is an expense during that period. The important point to be noted is that AS- 11 stipulates effect of changes in exchange rate Vis-à-vis monetary items denominated in a foreign currency to be taken into account for giving accounting treatment on the balance sheet date. Therefore, an enterprise has to report the outstanding liability relating to import of raw materials using closing rate of exchange. Any difference, loss or gain, arising on conversion of the said liability at the closing

rate, should be recognized in the P&L account for the reporting period

10.11 In the Concluding part of the decision, the Hon'ble Supreme Court has observed that

21. In conclusion, we may state that in order to find out if an expenditure is deductible the following have to be taken into account (i) whether the system of accounting followed by the assessee is mercantile System, which brings into debit the expenditure amount for which a legal liability has been incurred before it is actually disbursed and file brings into credit what is due, immediately it becomes due and before it is actually received; (ii) whether the same system is followed by the assessee from the very beginning and if there was a change System, whether the change was bona fide: (iii) whether the assessee has given the same treatment to losses claimed to have accrued and to the gains that may accrue to it: (iv) whether the assessee has been consistent and definite in making entries in the account books respect of losses and gains: (v) whether the method adopted by the assessee for making entries in the books both in respect of losses and gains is as per nationally accepted accounting standards; (vi) whether the system adopted by the assessee is fair and reasonable or is adopted only with a view to reducing the incidence of taxation."

10.12 The case of the assessee is seen from the above principle laid down by the Hon'ble Supreme Court. The AO in his order did not bring any of the above factors mentioned by the Court while disallowing the claim. Therefore, the exchange loss gain claimed by the assessee under AS-11 as year-end provision of transactions in foreign exchange is covered in terms of the above decision of the Honble Supreme Court. In respect of the loss on forward contracts, the AO has relied on the decision of Bombay High Court in the case of Bharat R Ruia (HUF). The case law is related to AY 2003-04 and the provisions of Section 43(5) have been amended w.e.f. 1.4.2006. This aspect has not been taken into account by the AO. Further, the assessee has claimed that the forward contracts were cancelled actually and it is not notional. In this regard also, no contrary facts have been brought on record by the AO.

10.13 Moreover unlike for AY 2010-11 and later assessment years. where the search materials had shown that the assessee was inflating his expenditure through over invoicing and major amount is involved with over invoicing of coal price by M/s. Coal

& Oil Company LLC, Dubai and this over invoicing found and specifically admitted by the assessee on appreciation of the seized material has direct bearing on the foreign exchange loans, foreign exchange transactions of the assessee. However, no such material has been brought to notice for this assessment year 2008-09. Therefore, the additions made in this assessment car have to be considered on the basis of material on record and distinct from the later assessment years which are on different footing as per materials on record.

10.14 On perusal of the assessment order, it is seen that no such material has been brought on record for this assessment year. As mentioned, the Assessing Officer has also not brought out any contrary facts in relation to the consistency in the claim of gain/loss on foreign exchange as laid down by the Hon'ble Supreme Court in the case of Woodward Governor (supra).

10.15 Therefore, applying the decision of the Hon'ble Supreme Court in case of CIT vs Woodward Governor India P Ltd (supra), I delete the additions made on account of i) disallowance of provision for forex loss of Rs.4,09,9 1,273/- ii) disallowance of forex loss on forward contract of Rs.1,10,81,279/-."

Aggrieved by the order of the Ld.CIT(A), the revenue preferred an appeal before us.

5. The Ld.DR relying on the order of the AO, stated that the Ld.CIT(A) has erred in deleting the additions of provision for foreign exchange fluctuations of Rs.4,09,91,273/- and loss on forward contract of Rs.1,10,81,279/- made by the AO in the reassessment order, though the expenditure are in the nature of contingent and the provision is made on the basis of estimation.

6. Per contra, the Id.AR for the assessee asserting the action of the Ld.CIT(A) stated that there is no error in the order and which is supported by the provisions of the Income Tax Act and hence deleted the disallowance of the expenditure and also supported by the various judicial pronouncements of the hon'ble courts. The Ld. AR also filed a Paper book of 207 pages with the following documents:

<i>Sl.No</i>	<i>Particulars</i>	<i>Pg. Nos.</i>
1	<i>Copy of the Annual Report FY 2007-08</i>	<i>1-28</i>
2	<i>Copy of the Reconciliation of Exchange Gain or Loss for FY 2007-08, Detailed analysis and adjustment of foreign exchange fluctuations impacting financial statements.</i>	<i>29</i>
3	<i>Copy of the Exchange Fluctuation Remittance, Ledger account detailing currency exchange remittances and adjustments for the Chennai branch for FY 2007-08.</i>	<i>30-43</i>
4	<i>Copy of the Foreign Exchange Fluctuation Ledger account tracking exchange losses for the Chennai branch for FY 2007-08.</i>	<i>44</i>
5	<i>Copy of the, Foreign exchange Fluctuation ledger account documenting currency exchange transactions and adjustments for the Mumbai branch for FY 2007-08.</i>	<i>45-54</i>
6	<i>Copy of the Foreign Exchange Fluctuation - Ledger account tracking indirect foreign exchange gains and losses for the Mumbai branch in FY 2007-08.</i>	<i>55</i>
7	<i>Copy of the Ledger account for year-end provisions related to exchange rate fluctuations for the Chennai branch.</i>	<i>56</i>
8	<i>Copy of the Ledger account for year-end provisions related to exchange rate fluctuations for the Mumbai branch.</i>	<i>57-58</i>
9	<i>Copy of the Summary Forex Loss Gain Vessel wise Sample, detailing financial fluctuations per vessel.</i>	<i>59</i>
10	<i>Copy of the MV Giorgos B Invoice 108 foreign currency (FC)</i>	<i>60-77</i>
11	<i>Copy of the forward sales contract with an</i>	<i>78</i>

	<i>Indian Overseas Bank (IOB) booking dated July 17, 2007, providing forward cover for future currency exchange rates.</i>	
12	<i>Copy of the invoice for the import order of MV Orientor2, detailing the financial transactions associated with the purchase FY 2007-08.</i>	79-96
13	<i>Copy of the invoice for the import order of MV Nantor Invoice A, detailing the financial transactions associated with the purchase FY 2007-08</i>	97-114
14	<i>Copy of a forward cover booking for a corporation Bank, dated September 7, 2007, securing future currency exchange rates.</i>	115
15	<i>Copy of the invoice for the import order of MV Nantor Invoice B, detailing the financial transactions associated with the purchase FY 2007-08</i>	116-123
16	<i>Copy of a forward cover booking for a corporation Bank, dated 22.11.2007 securing future currency exchange rates.</i>	124-125
17	<i>Copy of the invoice for the import order of MV Genco Muse Invoice, detailing the financial transactions associated with the purchase FY 2007-08</i>	126-141
18	<i>Copy of a Forward Cover CORPN Booking 2 dated 22-11-2007, securing future currency exchange rates.</i>	142
19	<i>Copy of the invoice for the import order of MV Santana Invoice, detailing the financial transactions associated with the purchase FY 2007-08</i>	143-162
20	<i>Copy of the Forward Cover CORPN booking dated 17-07-2007 detailing the financial transactions associated with the purchase and sales FY 2007-08</i>	163
21	<i>Copy of the Ledger account for year-end provisions related to exchange rate fluctuations for the Chennai branch.</i>	164
22	<i>Copy of the Ledger account for year-end provisions related to exchange rate fluctuations for the Mumbai branch.</i>	165
23	<i>Copy of the Foreign exchange Fluctuation ledger account documenting currency exchange transactions and adjustments for the Chennai branch FY 2007-08</i>	166-197
24	<i>Copy of the Foreign exchange Fluctuation ledger account documenting currency exchange transactions and adjustments for the Mumbai branch FY 2007-08</i>	198-207

6.1 Disallowance of provision for Foreign Exchange loss:

The Id.AR drew our attention to the '**Accounting Standard 11: The Effects of Changes in Foreign Exchange Rates**' which lays down the guidelines for treatment of provision of foreign exchange loss which is as under:

"Exchanges differences arising on the settlement of monetary items or on reporting an enterprise's monetary items at rates different than those at which they were initially recorded during the period, or reported in previous financial statements, should be recognized as income or expenses in the period in which they arise."

Therefore, an enterprise has to report the outstanding liability relating to import of raw materials using closing rate of exchange. Any difference, loss or gain arising on conversion of the said liability at the closing rate, should be recognized in the profit and loss account for the reporting period.

6.2 In this regard, Ld.AR submitted that the year end provision was created for each AY. Further, a Reconciliation Statement of Exchange (Gain)/Loss between books of accounts and Financial Statements along with their respective ledger extracts were produced before the CIT(A) and AO during the course of assessment proceedings. Hence, the Id.AR prayed

for confirming the deletion of disallowance of provision for Foreign exchange loss made by the Ld.CIT(A).

6.3 Disallowance of loss on forward contracts:

Further, the Ld.AR stated that the assessee had entered into a forward contract not for the purpose of purchase and sale of the foreign currency but for the purpose of hedging against foreign exchange fluctuation risk on its import payables. Hence, it is important to note that the intention of the Company is only to cover itself against the risk of foreign currency fluctuation in the ordinary course of business and not to trade in foreign currency. Further, the assessee, in its normal course of operations, import coal from outside India for which settlement is to be made in foreign currency and it is for this purpose the company has entered into a forward contract with the bank. The purpose for which the forward contract is taken is for a transaction of revenue nature. Hence, the loss accounted with respect to foreign currency fluctuation is not to be treated as speculative transaction and therefore, the provisions of section 43(5) of the Act cannot be made applicable to the assessee.

1. The actual settlement of the contract takes place on actual delivery of the currency for which the contract has been

entered into and is of not the nature where settlement of a transaction takes place otherwise than on account of actual delivery.

2. The method of treatment adopted by the assessee is in line with the requirements of AS-11 which require profit or loss arising on account of the forward contracts the maturity period of which does not fall within the same accounting period to be recognized in the profit and loss account.

6.4 Foreign exchange forward contracts are not 'commodities' and hence, are outside the scope of section 43(5) of the Act:

The term "commodity" has not been defined under the Act. The Forward Contracts (Regulation) Act, 1952 ('FCRA') defines 'goods' as "every kind of movable property other than actionable claims, money and securities."

Since the provisions of section 43(5) of the Act apply only to transactions in 'commodity', it is respectfully submitted that the provisions of the said section are not at all applicable in the present case for the simple reason that foreign currency is not a trading commodity.

6.5 In this regard, Ld.AR drew our attention to the decision of the Delhi Bench of the Tribunal in the case of ***Munjal Showa Ltd. v. DCIT: 94 TTJ 227***, wherein the Tribunal held as under:

"31. Foreign currency or any currency is neither commodity nor shares. The Sale of Goods Act, specifically excludes cash from the definition of goods. Besides, no person other than authoriseddealers and money changers are allowed in India to trade in foreign currency, much less speculate. Sec. 8 of the Foreign Exchange Regulations Act, 1973, provides that except with prior general or special permission of the RBI, no person other than an authorised dealer shall purchase, acquire, borrow or sell foreign currency,

32. In fact, prior to the LERMS, residents in India were not even permitted to cancel forward contracts. The presumption of any speculative transaction is, therefore, directly rebutted in view of the legal impossibility and in view of the fact that foreign currency was neither commodity nor shares."
(Emphasis supplied)

In view of the aforesaid, Id.AR stated that foreign currency forward contracts cannot be regarded as 'commodity' and, therefore, the ingredients required to be present for a transaction to qualify as a 'speculative transaction' under section 43(5) of the Act are not satisfied. Consequently, the provisions of the said section are not applicable in the instant case.

6.6 Transaction settled by way of actual delivery or transfer is not 'speculative' in nature:

Further, the Ld.AR argued that in order to be a 'speculative transaction', there should be a contract for purchase or sale of a commodity, including stocks and shares and such contract

should be settled otherwise than by actual delivery or transfer of the commodity. In other words, the transaction must be settled on a net-net basis, whereby the difference between the price prevailing on the settlement date and the contracted price is paid/ received by the parties to the contract. Given that the contracts are settled by actual delivery and not on a net-to-net basis, the same does not fall within the meaning of 'speculative transaction' as mentioned in section 43(5) of the Act.

6.7 Judicial precedents supporting that loss on forward contracts entered into in the course of the business of the Assessee are allowable as expenditure:

The Ld.AR further took the support of decision of the Hon'ble Supreme Court of India in the case of **Commissioner of Income-tax, Delhi v. Woodward Governor India (P.) Ltd. [2009] 179 Taxman 326 (SC)** held that:

"The word 'expenditure' is not defined in the Act. The word 'expenditure' is, therefore, required to be understood in the context in which it is used. Section 37 enjoins that any expenditure not being expenditure of the nature described in sections 30 to 36 laid out or expended wholly and exclusively for the purpose of the business, should be allowed in computing the income chargeable under the head 'profits and gains of business'. In sections 30 to 36, the expression 'expenses incurred' as well as 'allowances and depreciation' have also been used. For example, depreciation and allowances are dealt with in section 32. Therefore, the Parliament has used the expression 'any expenditure' in section 37 to cover both. Therefore, the expression 'expenditure' as used in section 37 may, in the circumstances of a particular case, cover an amount which is really a 'loss', even though said amount has not gone out from the pocket of the assessee." [Para 13] "Therefore, in the instant case, the 'loss' suffered by the assessee on account of the exchange difference as on the date of the balance sheet was an item of expenditure under section 37(1). " [Para 15]

The Jurisdictional Chennai Bench of the Tribunal in the following cases has held that losses incurred in the course of business to protect against unfavorable movements in the foreign exchange rate are an allowable expenditure.

1. M/s. Majestic Exports vs JCIT {ITA Nos. 1336 & 3072/Mds/2014}
2. M/s. S P Apparels Ltd vs DCIT (ITA No. 1327/Mds/2014)
3. M/s. SCM Garments (P) Ltd vs DCIT (ITA No. 1645/Mds/2014 & 2275/Mds/2014)

6.8 MTM losses are neither contingent nor notional-unascertained losses:

The Ld.AR also argued that the Section 145(1) of the Act provides that income chargeable under the head 'profits and gains of business or profession' shall be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee. Section 209(3) of the erstwhile Companies Act, 1956 provides for mandatory use of accrual basis and the Double Entry System of Accounting. The term "Mark to Market" is a concept under which the un-matured forward contracts are valued at market rate so as to report their actual value on the reporting date. In such an adjustment, a corresponding loss is booked through the profit and loss account, being the difference between the purchase price and the value as on the valuation date. Further, this issue is

squarely covered by the decision of Supreme Court in the case of CIT vs. Woodward Governor India (P.) Ltd: 312 ITR 254 wherein, the Apex Court dismissed the appeal filed by the Department and affirming the decision of High Court has held that:

loss suffered by the assessee in respect of a revenue liability on account of exchange difference as on the balance sheet would be an item of expenditure allowable under section 37(1) in the year of accrual.

6.9 Therefore, Id.AR submitted that the transaction entered into by the assessee on forward contract with banks cannot be treated as a speculative transaction and it being incidental to the operations of the business, the same should be allowed as a deduction in computing the total income of the assessee.

7. We have heard the rival contentions, perused the materials available on record and gone through the orders of the lower authorities. The AO had reopened the assessee's case u/s.147 for the reason that the income of the assessee has escaped assessment and the AO passed the order U/s.143(3) r.w.s. 147 of the Act, by disallowing the provision for foreign exchange fluctuations of Rs.4,09,91,273/- and loss on forward

contract of Rs.1,10,81,279/-. The Ld.CIT(A) on perusal of the submissions made by the assessee, materials available on record and relying on the decision of the Hon'ble Apex court in the case of CIT vs. Woodward Governor India (P.) Ltd (Supra) deleted the both the disallowances made by the AO. We note that the assessee is a private limited company has maintained books of accounts on mercantile basis as prescribed under the Companies Act. Further, the assessee followed the Accounting Standard 11 - The Effects of Changes in Foreign Exchange Rates and accordingly the provision has been made towards foreign exchange gain or loss (PB page No.29) and claimed as expenditure in Schedule 23 of the audited Financials of the assessee (PB page No.20). The recognizing difference in foreign exchange loss or gain at the year end in the P & L account as per the AS 11 is also upheld by the Hon'ble Apex court in the case of CIT vs. Woodward Governor India (P.) Ltd (Supra) as detailed below:

"18. AS-11 deals with giving of accounting treatment for the effects of changes in foreign exchange rates. AS-11 deals with effects of Exchange Differences. Under para 2, reporting currency is defined to mean the currency used in presenting the financial statements. Similarly. The words 'monetary items' are defined to mean money held and assets and liabilities to be received or paid in fixed amounts, e.g. , cash, receivables and payables. The word "paid" is defined under Section 43(2). This has been discussed earlier. Similarly, it is

important to note that foreign currency notes, balance in bank accounts denominated in a foreign currency, and receivables/payables and loans denominated in a forcing Currency as well as sundry creditors are all monetary items which have to be valued at the closing rate under AS-11 Under para 5, a transaction in a foreign currency has to be recorded in the reporting currency by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the transaction. This is known as recording of transaction on Initial Recognition. Para 7 of AS-11 deals with reporting of the effects of changes in exchange rates subsequent to initial recognition. Para 7(a) inter alia states that on cash balance sheet date monetary items, enumerated above, denominated in a foreign currency should be reported using the closing rate. In case of revenue items falling under Section 37(1), para 9 of AS-11 which deals with recognition of exchange differences, needs to be considered. Under that para, exchange differences arising on foreign currency transactions have to be recognized as income or as expense in the period in which they arise, except as stated in para 10 and para 11 which deals with exchange differences arising on repayment of liabilities incurred for the purpose of acquiring fixed assets, which topic falls under Section 43A of the 1961 Act. At this stage, we are concerned only with para 9 which deals with revenue items. Para 9 of AS-11 recognises exchange differences as income or expense. In cases where, e.g., the rate of dollar rises vis-à-vis the Indian rupee, there is an expense during that period. The important point to be noted is that AS-11 stipulates effect of changes in exchange rate Vis-à-vis monetary items denominated in a foreign currency to be taken into account for giving accounting treatment on the balance sheet date. Therefore, an enterprise has to report the outstanding liability relating to import of raw materials using closing rate of exchange. Any difference, loss or gain, arising on conversion of the said liability at the closing rate, should be recognized in the P&L account for the reporting period 10.11 In the Concluding part of the decision, the Hon'ble Supreme Court has observed that

21. In conclusion, we may state that in order to find out if an expenditure is deductible the following have to be taken into account (i) whether the system of accounting followed by the assessee is mercantile System, which brings into debit the expenditure amount for which a legal liability has been incurred before it is actually disbursed and file brings into

credit what is due, immediately it becomes due and before it is actually received; (ii) whether the same system is followed by the assessee from the very beginning and if there was a change System, whether the change was bona fide: (iii) whether the assessee has given the same treatment to losses claimed to have accrued and to the gains that may accrue to it: (iv) whether the assessee has been consistent and definite in making entries in the account books respect of losses and gains: (v) whether the method adopted by the assessee for making entries in the books both in respect of losses and gains is as per nationally accepted accounting standards; (vi) whether the system adopted by the assessee is fair and reasonable or is adopted only with a view to reducing the incidence of taxation."

As argued by the Id.AR we note that the term "commodity" has not been defined under the Act. The Forward Contracts (Regulation) Act, 1952 ('FCRA') defines 'goods' as "every kind of movable property other than actionable claims, money and securities." Since the provisions of section 43(5) of the Act apply only to transactions in 'commodity', it is respectfully submitted that the provisions of the said section are not at all applicable in the present case for the simple reason that foreign currency is not a trading commodity.

8. We note that in order to be a 'speculative transaction', there should be a contract for purchase or sale of a commodity, including stocks and shares and such contract should be settled otherwise than by actual delivery or transfer of the commodity.

In other words, the transaction must be settled on a net-net basis, whereby the difference between the price prevailing on the settlement date and the contracted price is paid/ received by the parties to the contract. In the instant case of the assessee the contracts are settled by actual delivery and not on a net-to-net basis and hence the same does not fall within the meaning of 'speculative transaction' as mentioned in section 43(5) of the Act. In view of the above discussion and materials placed on records and respectfully following the decision of the Hon'ble Apex Court in the case of CIT vs Woodward Governor India (P.) Ltd (Supra), we do not find fault in the order of the Ld.CIT(A) in deleting the disallowance made by the AO in the reassessment order. Therefore, in the present facts and circumstances of the case, we are of the considered view that both the provision for foreign exchange fluctuations of Rs.4,09,91,273/- and loss on forward contract of Rs.1,10,81,279/- are allowable as expenditure in the impugned year and hence we uphold the order of the Ld.CIT(A) and dismiss the appeal of the revenue.

9. In the result the appeal of the Revenue is dismissed.

10. ITA Nos.: 1364, 1365 & 1366/Chny/2023 for the A.Y. 2011-12, 2012-13 & 2013-14:

The Common grounds raised by the assessee in all the above three appeals are as under:

1. *For that the Order of the Learned Commissioner of Income Tax (Appeals) is contrary to law, facts and circumstances of the case.*
2. *For that the Learned Commissioner of Income Tax (Appeals) erred in confirming the disallowance of provision for loss on account of foreign exchange fluctuation on forward contracts amounting to Rs.14,62,02,308/-.*
3. *For that the Learned Commissioner of Income Tax (Appeals) and Assessing Officer erred in invoking the provisions of section 43(5) of the Act by holding that the forward contracts fall under the term 'Commodities' and thereby grossly erred in treating the transaction as speculative transaction without appreciating the facts and circumstances of the case.*
4. *For that the Learned Commissioner of Income Tax (Appeals) erred in not appreciating the fact that the loss on restatement of forex fluctuation as at the year-end is not contingent in nature and is allowable as deduction u/s 37 of the Act.*
5. *For that the Learned Commissioner of Income Tax (Appeals) erred in upholding the Assessment Order based on the alleged findings emanating out of search conducted on 04.01.2017 which are not part of the records when the Assessment Order was passed u/s 143(3) of the Act.*

For these grounds and such other grounds that may be adduced before or during the hearing of the appeal, it is prayed that the Hon'ble Tribunal may be pleased to delete the addition made and/or grant such other relief as this Hon'ble Tribunal deems fit.

11. The assessment was completed vide order u/s.143(3) r.w.s 92CA of the Act for AY 2008-09, AY 2011-12 to AY 2013-14, respectively by disallowing the provision for foreign

exchange fluctuations and loss on forward contract as detailed below:

Sl.No.	Date of AO order	A.Y.	Amount in Rs.
1	30.03.2015	2011-12	4,23,17,975/-
2	30.03.2016	2012-13	14,62,02,308/-
3	29.12.2016	2013-14	10,03,79,186/-

Aggrieved by the orders of the AO, the assessee preferred an appeal before the Ld.CIT(A) – 18, Chennai.

12. The Ld.CIT(A) has dismissed the appeals of the assessee for the all the three A.Ys, by upholding the disallowance made by the assessee as shown above by passing a common order on 29.09.2023. Aggrieved by the order of the Ld.CIT(A), the assessee is before us.

13. The Id.AR reiterated the arguments held in the revenue's appeal for the assessment year 2008-09 and further, submitted as below:

"Additionally, it is vital to note that CIT(A), for AY 2008-09, having followed the decision of the Apex Court in the case of M/s. Woodward Governor India (P.) Ltd: 312 ITR 254 had deleted the disallowances made by the AO and allowed the appeal in favour of the appellant, against which the Department is in appeal before this Hon'ble Tribunal.

3. However, it is pertinent to note that the very same CIT(A), for AY 2011-12 to AY 2013-14, has dismissed the appeals merely by

placing reliance on the materials found / sworn statements recorded during the search proceedings conducted on 04.01.2017 without appreciating the fact that the facts of the case for AY 2008-09 were akin to these AYs. Further, it is submitted that the AO, having considered the findings of the search had completed the search assessments u/s 143(3) r.w.s 153A of the Act for AY 2010-11 to AY 2017-18, which are also subject matter of appeals before this Hon'ble Tribunal.

- 4. Based on the above facts, it is submitted that the CIT(A) ought not have formed his opinion based on the subsequent events without appreciating the fact that the present appeals were emanating from the Original Assessments completed u/s 143(3) / 147 of the Act.*
- 5. Considering the facts and circumstances of the case, it is most humbly prayed before Your Authority to direct the Assessing Officer to delete the disallowance of Provision for Foreign exchange loss and loss on Forward contract."*

14. We have heard the rival contentions, perused the materials available on record and gone through the orders of lower authorities. The same issue is adjudicated in favour of the assessee on merits by dismissing the appeal of the revenue for the assessment year 2008-09 (supra). Since, the facts and issues in these appeals are identical and there is no change in the facts and circumstances therefore, following the rule of consistency, the result of the above appeal No. ITA 1363/CHNY/2023 for AY 2008-09 is applicable mutatis mutandis for the assessment years 2011-12, 2012-13 & 2013-14 also.

15. Further, we note that the Ld.CIT(A) for the assessment years 2011-12, 2012-13 & 2013-14 is not entitled to take into

consideration the material, if any, found in search & seizure dated 04.01.2017, for the reason that there is a separate chapter, sections and corresponding procedures are provided in the Act to deal with such issues. Hence, the Ld.CIT(A) cannot usurp the jurisdiction of other officers as enshrined in the search provisions under Chapter XIII of the Act. Any finding based on search material by the Id.CIT(A) in these assessment years is not permissible against the provisions of the Act, hence we reject the findings of the Ld.CIT(A) on those materials which are found in search for adjudication of these appeals. Thus, the appeals of the assessee for all the three assessment years are allowed.

16. In the result, appeal filed by the revenue for the assessment year 2008-09 is dismissed and appeals filed by the assessee for the assessment years 2011-12, 2012-13 & 2013-14 are allowed.

Order pronounced in the court on 25th October, 2024 at Chennai.

Sd/-
(महावीर सिंह)
(MAHAVIR SINGH)
उपाध्यक्ष/**Vice President**

Sd/-
(एस. आर.रघुनाथा)
(S. R. RAGHUNATHA)
लेखा सदस्य/**Accountant Member**

चेन्नई/Chennai,

दिनांक/Dated, the 25th October, 2024

JPV

आदेशकीप्रतिलिपिअग्रेषित/Copy to:

1. अपीलार्थी/Appellant
2. प्रत्यर्थी/Respondent
3. आयकर आयुक्त/CIT - Chennai
4. विभागीय प्रतिनिधि/DR
5. गार्ड फाईल/GF