आयकर अपीलीय अधिकरण, इंदौर न्यायपीठ, इंदौर

IN THE INCOME TAX APPELLATE TRIBUNAL, INDORE BENCH, INDORE

BEFORE SHRI KUL BHARAT, JUDICIAL MEMBER AND SHRI MANISH BORAD, ACCOUNTANT MEMBER

ITA No583/Ind/2012

Assessment Year: 2009-2010

M/s. HEG Limited, Mandideep, Dist. Raisen		ACIT- 1(1) Bhopal
(Appellant)		(Respondent)
PAN No.AAACH6184K		

Revenue by	Shri Lal Chand, CIT
Assessee by	Mr. Sumit Neema, Sr.Adv & Shri Ayush Gupta, Adv
Date of Hearing	19.09.2018
Date of Pronouncement	28.09.2018

O R D E R

PER MANISH BORAD, AM.

This appeal filed at the instance of assessee pertaining to A.Y. 2009-2010 is directed against the order of Ld. Commissioner of Income Tax(Appeals)-I, Bhopal (in short 'CIT(A)'), vide appeal No. CIT(A)-I/BPL/IT-256/11-12 order dated 11.10.2012 which is arising out of the order u/s 143(3) of the Income Tax Act 1961(hereinafter called as the 'Act') framed on 28.12.2011 by ACIT-1(1), Bhopal.

2. Briefly stated facts as culled out from the records are that the assessee is a public limited company engaged in the business of manufacture of graphite electrodes, steel, activated carbon cloth, power generation and 100% export oriented unit of technology centre. Income of Rs.141,32,99,510/- disclosed in the income Tax return filed on 27.9.2009. The case was selected for scrutiny and notice u/s 143(2) dated 23.8.2010 was duly served upon the assessee. Assessment was completed u/s 143(3) of the Act at total income of Rs.168,51,36,442/-. by making various additions. Aggrieved assessee preferred appeal before Ld.CIT(A) and partly succeeded.

3. Now the assessee is in appeal before the Tribunal raising following grounds of appeal;

> *"1. That there is no justification either in law or on facts for the AO and CIT(A) in rejecting the claim of set off of loss of Rs.53,26,361/- incurred by the appellant in 100% EOU Technology Division.*
>
> *2. That the learned CIT(A) failed to appreciate the provisions of section 10B of Income Tax Act 1961 as amended by Finance Act 2000 whereby section 10B was amended and consequently the said section provide for deduction of profits/losses and the said section is not an exemption section.*

3. That the learned AO was not justified in law or on facts by holding that the aforesaid claim of loss of Rs.53,26,361/- is not allowable in the course of assessment proceedings as claimed by the appellant.

4. That there is no justification either in law or on facts for the AO and CIT(A) in making disallowance of foreign currency fluctuation loss of Rs.2,82,42,778/-."

4. We will first take up first Ground No. 1, 2 & 3 through which the assessee has raised the issue relating to rejection of claim of set off of Rs.53,26,361/- incurred by the appellant in 100% Export Oriented Unit.

5. At the outset Ld. Counsel for the assessee submitted that the issues stands squarely covered in favour of the assessee by CBDT Circular No.7/DV/2013 dated 16.7.2013 as well as the following judgments;

(a) Bombay High Court in the case of CIT V Galaxy Surfactants (2010) 325 ITR 102 (Bom)

(b) Bombay High Court in the case of DCIT V Hindustan Unilever (2012) 343 ITR 108 (Bom)

(c) Delhi High Court in the case of DCIT V Honey Well International (2008) 26 SOT 503 (Del)

(d) Ahmedabad I.T.A.T. in the case of ACIT V Bharat Ltd (2012) 50 SOT 298 (Ahd)

6. Per contra Ld. Departmental Representative supported the orders of Ld. Assessing Officer.

7. We have heard rival contentions and perused the records placed before us and carefully gone through the judgments placed and relied by the Ld. Counsel for the assessee.

8. The issue raised before us is that the assessee incurred loss of Rs.53,26,361/- in its 100% Export Oriented Unit of Technology Centre which was eligible for exemption u/s 10B of the Act. The alleged loss was claimed as set off against the profit of other Division of the assessee. This claim was rejected by the both lower authorities.

9. From perusal of the CBDT Circular No.7/DV/2013 dated 16.7.2013 as well as the judgments referred and relied by the Ld. Counsel for the assessee, we find force in the contention of the

assessee. Hon'ble Bombay High Court in the case of DCIT V Hindustan Unilever (2012) 343 ITR 108 (Bom) (supra) dealing with the same issue has allowed the claim of set off of loss incurred in one of the EOU units eligible for exemption u/s 10B of the Act against the profits of other units run by the same assessee. Hon'ble Court decided in favour of the assessee observing as follows;

(iv') The loss incurred by the eligible unit under section 10B:.'

23. The fourth and final ground which has weighed with the Assessing Officer in re-opening the assessment is that the assessee claimed a deduction of Rs. 14.53 crores under section 1OB. The deduction was restricted to Rs. 11.11 crores in the order. While reopening the assessment, the Assessing Officer has proceeded on the basis that section 1OB provides an exemption and that in respect of the Crab Stick Unit the assessee had suffered a loss of Rs. 1.33 crores. The Assessing Officer has observed that since the income of the unit was exempt from taxation, the loss of the unit could not have been set off against the normal business income. However, this was allowed by the assessment order and it is opined that the assessee's income to the extent of Rs. 1.33 crores has escaped assessment.

24. There is merit in the submission which has been urged on behalf of the assessee that the Assessing Officer has while re-opening the assessment exfacie proceeded on the erroneous premise that section 1OB is a provision in the nature of an exemption. Plainly, sect ion lOB as it stands is not a provision in the nature of an exemption but provides for a deduction. Section 1OB was substituted by the Finance Act of2000 with effect from 1-

4-2001. Prior to the substitution of the provision, the earlier provision stipulated that any profits and gains derived by an assessee from a hundred per cent Export Oriented Undertaking, to which the section applies "shall not be included in the total income of the assessee". The provision, therefore, as it earlier stood was in the nature of an exemption. After the substitution of section 1OB by the Finance Act of 2000, the provision as it now stands provides for a deduction of such profits and gains as are derived by a hundred per cent Export Oriented Undertaking from the export of articles or things or computer software for ten consecutive assessment years beginning with the assessment y.ear relevant to the previous year in which the undertaking begins to manufacture or produce . Consequently, it is evident that the basis on which the assessment has sought to be re-opened is belied by a plain reading of the provision. The Assessing Officer was plainly in error in proceeding on the basis that because the income is exempted, the loss was not allowable. All the four units of the assessee were eligible under section 10B. Three units had returned a profit during the course of the assessment year, while the Crab Stick Unit had returned a loss. The assessee was entitled to a deduction in respect of the profits of the three eligible units while the loss sustained by the fourth unit could be set off against the normal business income. In these circumstances, the basis on which the assessment is sought to be reopened is contrary to the plain language of section10B.

25. For all the aforesaid reasons, we are of the view that the Assessing Officer could not possibly have formed a belief that income chargeable to tax had cap assessment within the meaning of section 147. The petition would have to be allowed and is accordingly allowed by setting aside the impugned notice dated 31-3-2008 issued under section 148 of the Income-tax Act, 1961.

26. Rule is made absolute in the aforesaid terms. There shall be no order as to costs".

10. We therefore respectfully following the judgment of Hon'ble Bombay High Court are of the considered view that both the lower authorities erred in denying the benefit of set off of loss incurred by the assessee in the 100% EOU unit at Rs.53,26,361/. against the profits of other units run by the assessee. We therefore set aside the findings of Ld.CIT(A) and allow Ground No. 1,2 & 3 raised by the assessee.

11. Now we take up Ground No.4 wherein both the lower authorities disallowed the claim of foreign currency fluctuation loss of Rs.2,82,42,778/- which was suffered by the assessee on account of forward market contract of forex derivatives outstanding at the year end. The Ld Counsel for the assessee submitted that the issue raised in the appeal is squarely covered in favour of the assessee by various judgments including the Special Bench decision in the case of DCIT V Bank of Bahrain & Kuwait 132 TTJ 505 (Mum) (SB). He also submitted that the actual loss incurred in the forward market contracts for foreign exchange for the transactions squared up

during the year have already been allowed by the revenue authorities but both the lower authorities has denied the claim of loss with regard to pending forward contracts which were due to mature in the subsequent financial year for which notional loss was booked by the assessee in the profit and loss account on the basis of accounting standard (AS) 11 issued by the Chartered Accountants of India. Ld. Counsel for the assessee referred and relied on the following decisions ;

(a) I.T.A.T. Mumbai Bench in the case of ACIT V M/s. D. Dipak & Co I.T.A No.7629/Mum (2011)

(b) Supreme Court in the case of CIT V Woodward Governor India P. Ltd (2009) 312 ITR 254 (SC)

(c) I.T.A.T. Special Bench in the case of DCIT V Bank of Bahrain & Kuwait 132 TTJ 505 (Mum SB) (2010)

(d) I.T.A.T Delhi in the case of M/s. Bechtel India Pvt. Ltd, New Delhi V ACIT ITA No.1224/Del/2017

(e) Bombay High Court in the case of Director of Income Tax (International Taxation) V Citiban N.A. Appeal No.330 of 2013 (2016) 66 rtaxmann.com 373 (Bombay)

(f) Oil & Natural Gas Corpn. Ltd V CIT (2010) 322 ITR 180 (SC)

(g) Perfect Circle India Ltd V Deputy Commissioner of Income Tax (2015) 60 Taxmann.com 424 (Mumbai-Trib)

(h) DCIT Kotak Mahindra Investment Ltd (Mumbai –Trib)

(i) CEE V Ratam Melting & Wires Industries (2008) 13 SCC

12. Per contra Ld. Departmental Representative supported the orders of lower authorities.

13. We have heard rival contentions and perused the records placed before us. We find that the assessee is engaged in the business of manufacture of graphite electrodes, steel, activated carbon cloth, power generation and a 100% export oriented unit of technology centre. Major part of the turnover is from export of graphite which are transported through ships and take long time to reach to the destination and therefore the assessee used to carry out hedging transaction of the foreign currency. A sum of Rs.118.32 crores is claimed as foreign exchange fluctuation expenditure which also includes "marked to market" loss of notional nature at Rs.2,82,42,778/-. Both the lower authorities have allowed the claim of foreign exchange fluctuation expenditure

except for the notional loss of Rs.2,82,42,778/- for the reason that those contracts has not squared up at the close of year and the impugned amount is merely notional loss. Ld. Counsel for the assessee has contended that the impugned notional loss has been shown in the financial statement in order to comply to the Accounting Standard-11 issued by the Chartered Accountants of India for "the effect of changes in Foreign Exchange Rates" which provides that the assessee should show the loss/profit in the profit and loss account arising out of the difference in rate of foreign currency rate at the year end vis-a-vs forward contract rate on the maturity date. It is also contended that in the subsequent year when the alleged "marked to market" forward contract matured/squared, all resultant profit and loss has been booked in the books of accounts after duly adding/reducing the alleged notional loss of Rs.2,82,42,778/-. This plea of the assessee has not been rebutted by the revenue authorities.

14. We find that the Co-ordinate Bench, Mumbai I.T.A No.7629/Mum (2011) in the case of ACIT V M/s. D. Dipak & Co date4d 30.04.2013 dealing with the same issue of "marked to

market" loss of notional nature, allowed the issue in favour of the assessee by relying on the Special Bench decision in the case of DCIT V Bank of Bahrain & Kuwait 132 TTJ 505 (Mum SB) (2010) observing as follows (for sake of convenience we have also mentioned the facts of the case) ;

> "This appeal is preferred by the Revenue against the order of ld. CIT(A) - 27, Mumbai dtd. 28-8-2011 whereby he deleted the addition made by the A.O. on account of "marked to market" loss of Rs. 5,53,02,172/-claimed by the assessee on revaluation of the pending forward contract on the closing day.
>
> 2. The assessee in the present case is a partnership firm which is engaged in the business of manufacturing, trading as well as import and export of diamonds. The return of income for the year under consideration was filed by n 29-9-2008 declaring total income of Rs. 54,44,2'5,595/-. During the o se of assessment proceeding, it was noticed by the A.O. that the assessee had entered into forward exchange contract which were revalued by it on the closing day of the previous year. On such revaluation, the resultant loss amounting to Rs. 5,53,02,172/- was claimed by the assessee as "marked to market" loss. Since the relevant foreign exchange contract had not been settled in the relevant previous year, the assessee was called upon by the A.O. to explain as to why the marked to market loss claimed by it should not be disallowed being a notional loss. In reply, it was submitted by the assessee that it is engaged in the business of export of diamonds and since such exports are made on credit, it is always exposed to foreign currency fluctuation risk. It was submitted that in order to hedge the

said risks, the assessee had entered into forward exchange contract with banks. It was submitted that export receivables were being re-valued by the assessee on the closing day of the accounting year following the Accounting Standard _ 11 issued by the Chartered Accountants of India and the resultant loss/profit on such revaluation was claimed in the relevant year I was submitted that similarly the mal-ked to market gain or loss in respect of outstanding forward exchange contract by revaluing these contract as per AS-II was being claimed by the assessee. It was contended that this method was consistently being followed by the assessee and the marked to market loss claimed by it in respect of outstanding forward exchange contract was allowable as held by the Mumbai Special Bench of the ITAT in the case of DCIT vs. Bank of Bahrain and Kuwait (41 SOT 29(Mum).

3. The submissions made by the assessee on this issue were not found acceptable by the A.O. According to him, the relevant foreign exchange contract were still outstanding on the closing day of the previous ear and therefore the "marked to market" loss claimed by the assessee by revaluing The said contract was not the loss actually incurred by the assessee. He held that the actual toss or gain would be ascertained/determined only after the expiry period of the relevant contract or their termination and at that time there might not be any such loss at all. He held that the marked to marked loss claimed by the assessee thus was only the notional loss which was not allowable, As regards the decision of the Special Bench of the Tribunal in the case of Bank of Bahrain & Kuwait (supra) relied upon by the assessee, the A.O. held that the same was distinguishable on facts inasmuch as the foreign currency in that case was held by the assessee as stock-in-trade and he had entered into foreign exchange contract in order to protect its interest against the wide fluctuation in the foreign currency itself He held that in the case of the assessee, foreign currency was not its stock-in-trade and

therefore the decision of the Special Bench of the Tribunal in the ease of Bank of' Bahrain and Kuwait (supra) was not applicable in the case of the assessee being distinguishable on facts. As regards the reliance placed by the assessee on Accounting Standard - 11, the A.O. held that the reporting of notional losses to adhere to the accounting guidelines would not by itself make it deductible for Income Tax purposes especially when there is no provision in the Income 'I'ax Act to allow the deduction on account of notional loss for which the liability has not crystallized. He therefore disallowed the marked to market loss claimed by the assessee in respect of forward exchange contract claimed by the assessee in the assessment completed u/s 143(3) of the Income Tax Act, 1961 (the Act) vide an order dated 24-12-2010.

4. The order passed by the A.O. u/s 143(3) was challenged by the assessee in an appeal preferred before the Id. CIT(A) and the submission., made before the A.O. in support of its claim for "marked to market ass" as a result of revaluation of foreign exchange contract were reiterated on behalf of the assessee before the ld. CIT(A). The reliance was also placed on behalf of the assessee in support of its case on this issue on the decision of Special Bench of ITAT in the case of Bank of Bahrain and Kuwait (supra).

5. After considering the submissions made on behalf of the assessee and he relevant material available on record, the ld. CIT(A) first took note of the facts involved in the assessee's case relevant to this issue in para 5.1 & 5.2 of his impugned order as under:-

> "5.1 At the outset, appellant is predominantly 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 sales are at Rs.I08S.30 Cr, and the entire sales are by way of exports and local sales in diamond dollar

account, which are also in foreign currency. Similarly, out of total purchase of Rs.877.63 Cr, imports account for Rs476.68 Cr. and part of the local purchases are also in diamond dollar account. Appellant firm also utilize working capital loans from banks, some of which are also denominated in foreign currency. Out of total outstanding loan of Rs.260.17 Cr, loan denominated in foreign currency is Rs.256.40 Cr. Similarly bur of total creditors for goods of Rs 122 Cr, imports payable account for Rs.102 Cr. Thus, it is evident that appellant is exposed to risk arising out of fluctuation in Exchange rate and as a prudent businessmen likely to hedge its risk.

5.2 From para 6 of schedule-F to Balance Sheet under the heading " Report on Notified Accounting Standards", it is "evident that appellant is reporting all monetary items i.e. Export Receivable, Import Payable and Foreign Currency Working Capital Loan appearing in balance sheet at closing rate and recognizing the exchange rate difference in Trading Account as expenses or income, as the case may be. Similarly outstanding forward contract are marked to market and resulting loss or gain is being recognized as expenses or income in trading account. It may be mentioned that this method of recording transaction denominated in foreign currency is as per AS-1 I & being consistently followed and there is no change as compared to earlier year.

In the light of the relevant facts as noted by him, the ld. CIT(A) decided this issue by applying the ratio of the decisions laid down in the various judicial pronouncements. In this regard, he referred to the decision of the Hon'ble Delhi High Court in the case of Woodward Governor 294 ITR 451 as affirmed by the Hon'ble Supreme Court (312 ITR 254) wherein it was held that the liability arising out of already concluded contracts stands

accrued the minute the contract is entered into and mere postponement of the payment to different date cannot extinguish the liability and render it notional or contingent. He then referred to the decision of Hon'ble Supreme Court in the case of ONGC vs. CIT (322 ITR 180) wherein it was held that when the assessee maintained its accounts on mercantile system of accounting and the loss suffered by it on account of fluctuation in the rate of foreign exchange as on the date of balance sheet was claimed in compliance with Accounting Standards, the same should be allowed as expenditure u/s 37(1) of the act notwithstanding the fact that the liability had not been actually discharged in the year in which the fluctuation in the rate of foreign exchange had occurred. The ld. CIT(A) noted that the business of ONGC was not that of foreign exchange dealer and the similar loss was still held to be allowable by the Hon'ble Supreme Court. He held that the A.O. therefore was not correct in distinguishing the case of Bank of Bahrain and Kuwait (supra) decided by the Special Bench of ITA T involving similar issue on the ground that foreign currency was held in the said case by the assessee as stock-in-trade. The Ld. CIT{A) also took note of the fact that similar method of restatement of foreign exchange was followed by the assessee consistently in the earlier years and the same was accepted by the A.O. The ld CIT (A) accordingly held that the loss incurred by the assessee on restatement of foreign exchange contract at the year end was allowable and deleted the disallowance made by the A.O. on account of restatement of pending forward contract agreement at the year end. Aggrieved by the order of the ld. CIT(A), the Revenue has preferred his appeal before the Tribunal.

6. At the time of hearing before us, the ld. D.R. relied on the order of the A.O. in support of the Revenue's case on the issue involved in the present appeal while the Id. counsel for the assessee strongly supported the impugned order of the Id. CIT(A) giving relief to the assessee on the

said issue submitting that the case laws relied upon by the ld. CITT(A) in support of his decision are squarely applicable to the issue involved in the present appeal. He also relied on the decision of Mumbai Bench of the ITAT in the case of DCIT vs. Banque Indosuez (Known as Credit Agricole Indosuez) reported in (2013) 55 SOT 38 (Mumbai) and in the case of Societe Generale vs. DDIT (International Taxation) reported in (2013) 21 ITR (Trib) 606 (Mumbai) in support of the assessee's case.

7. We have heard the arguments of both the sides and also perused the relevant material available on record, It is observed that a similar claim for marked to market loss claimed by the assessee in respect of forward foreign exchange contract debited to the P&L account has been allowed by the Special Bench of this Tribunal in the case of Bank of Bahrain & Kuwait (supra) after discussing and considering all the relevant aspects of the matter and the relevant observations of the tribunal recorded in this context are summarized as under:-

> "[i] A binding obligation accrued against the Appellant the minutes it entered into forward foreign exchange contracts,
>
> (ii] A consistent method of accounting followed by the Appellant cannot be disregarded, The Appellant has consistently followed the same method of accounting in regard to recognition of profit or loss both) in respect of forward foreign exchange contract as per the rate prevailing on March, 31,
>
> (iii) A liability is said to have crystallized when a pending obligation on the balance sheet date is determinable with reasonable certainty,
>
> (iv) As per AS-II when the transaction is not settled in the same accounting period as that in which it occurred, the exchange

difference arises over more than one accounting period,

(v) In view of the decision of the Supreme Court " the case 0 Woodward Governor India (I) P. Ltd" the Appellant's claim is allowable.

(vi) In the ultimate analysis, there is no revenue effect and the timing of taxation of loss/profit,"

Although the decision of Special Bench ITAt In the case of 'Bank of Bahrain & Kuwait (supra) cited before the A.O. was distinguished by him on the ground that the assessee in the said case was holding foreign currency as stock-in-trade, the distinction so made by the A.O. was irrelevant and immaterial as rightly pointed out by the ld. CIT(A) in his impugned order relying on the decision of Hon'ble Supreme Court in the case of ONGC (supra) wherein a similar issue was decided by the Hon'ble Apex Court in favour of the assessee despite the fact that ONGC was not a dealer in foreign exchange.

8. In the case of Banque Indosuez (supra) cited by the ld. counsel for the assessee, the co-ordinate Bench of this Tribunal had an occasion to consider a similar issue and the same was decided by the Tribunal in favour of the assessee following the decision of Special Bench of ITAT in the case of Bank of Bahrain & Kuwait (supra) as is evident from para 15 of the order of the Tribunal passed in the said case which is reproduced hereunder:-

"After considering the rival submissions and 'perusing the material on record we find that the assessee entered, into forward foreign exchange contract during the year In respect of the ma contracts as at the year end, the assessee valued such unmatured forward

foreign exchange contracts at the rate of exchange prevailing a at the end of the year which resulted into loss of Rs. 7.14 crore. It can be considered by way of simple example. If the assessee undertakes a forward foreign exchange contract as on 18th January, 1998, on which the rate of dollar is Rs. 42. Further suppose that the contract is to mature on 30th April at the price of Rs. 46 per dollar. Suppose at the end of the year 31st March, the rate of dollar has gone up to Rs. 43, the assessee's claim is that the difference of Rs. 1 (Rs. 43 -42) as on 31 st March, 1998 should be taken as loss and allowed deduction accordingly. The Special Bench of the Tribunal in the case of Dv. CIT (International Taxation) v. Bank of Bah rain & Kuwait [201 OJ 41 OT 290 (Mum) has held that the loss incurred by the assessee on account of evaluation of the contract on the last day of the accounting year i.e , before the date of maturity of the forward contract, is allowable as deduction. In that view of the matter this loss of Rs. 7. -4 c:-ore representing difference of Re. 1 (Rs. 43 - 42) is liable to be allowed as deduction".

9. In the latest decision rendered on 9th January, 2013 in the case of Societe Generale (supra) cited by the ld. counsel for the assessee, the co-ordinate Bench of this Tribunal has again allowed a similar claim of the assessee for the loss of Rs. 9.16 crores on foreign exchange contracts outstanding as on 31-3-1998 holding that this issue is squarely covered in favour of the assessee by the decision of the Special Bench of ITAT in the case of Bank of Bahrain & Kuwait (supra). In our opinion, the issue involved in the present case thus is squarely covered in favour of the assessee by various judicial pronouncements discussed above and respectfully following the same, we uphold the impugned order of the ld. CIT(A) allowing the claim of the assessee on account of "marked to

market" loss on revaluation of the pending forward contract for foreign exchange."

15. From the perusal of the above order of the Co-ordinate Bench the issue raised before us are squarely similar to those adjudicated by the Tribunal. We therefore in the given circumstances of the case are of the considered view that the lower authorities erred in not allowing the assessee's claim of notional loss arising on account of "marked to market" loss on the valuation of the pending forward contract of foreign exchange at Rs.2,82,42,778/-. We accordingly allow Ground No.4 raised by the assessee. In the result Ground No.4 of the assessee is allowed.

14. In the result the appeal of the assessee is allowed.

The order pronounced in the open Court on 28.9.2018.

Sd/- Sd/-

(KUL BHARAT) (MANISH BORAD)
JUDICIAL MEMBER ACCOUNTANT MEMBER

दिनांक /Dated : 28 September, 2018

/Dev

Copy to: The Appellant/Respondent/CIT concerned/CIT(A) concerned/ DR, ITAT, Indore/Guard file.

By order

Private Secretary/DDO, Indore