IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCHES "F", MUMBAI

BEFORE SHRI SAKTIJIT DEY, JUDICIAL MEMBER AND

SHRI MANOJ KUMAR AGGARWAL, ACCOUNTANT MEMBER

ITA No. 7834/MUM/2019
Assessment Year: 2016-17

VVF (India) Ltd., Plot 109, Sion Fort Garden, Sion (East), Mumbai - 400022 PAN: AADCV4970G	**Vs.**	ACIT- Circle (3)(2), Aayakar Bhavan, M.K. Road, Churchgate, Mumbai - 400020
(Appellant)		**(Respondent)**

Assessee by : Madhur Aggarwal (AR)
Revenue by : Usha Gaikwad (DR)

Date of Hearing: 20/05/2021
Date of Pronouncement: 26/07/2021

O R D E R

PER SAKTIJIT DEY, JM

Captioned appeal by the assessee is against the order dated 23.10.2019 of learned Commissioner of Income Tax (Appeals)–14, Mumbai for the assessment year 2016-17.

2. The effective grounds raised by the assessee are as under:-

1. *"On the facts and in the circumstances of the case and in law, the Commissioner of Income Tax (Appeal) ("CIT (A)") grossly erred in*

a. *confirming disallowance of mark to market loss of Rs. 4,04,22,903/- claimed by the appellant.*

b. *applying the ratio of the decision of Hon'ble Delhi ITAT in the case of Bachtal India (P) Ltd. Vs. ACIT [2017] 82 taxmann.com*

c. *not giving appellant reasonable opportunity to explain the case and to bring on record facts to show that its case was factually different from the case of Bechtal India (P) Ltd. (supra).*

d. not appreciating that disallowance of Rs. 4,04,22,903/- resulted in double disallowance as appellant had itself reversed the loss on 31.03.2016 in its books of accounts in April, 2016 and hence was doubly hit.

e. ignoring the consistently followed method without any change in facts."

3. Briefly the facts are, the assessee, a resident company, is stated to be engaged in the business of manufacturing of toilet soaps, fatty acids and fatty alcohols. For the assessment year under dispute, assessee filed its return of income on 26.11.2016 declaring total loss of Rs. 119,75,64,719/-. In course of assessment proceedings, the Assessing Officer (AO) while verifying the audit report of the assessee noticed that assessee has claimed unrealized loss in respect of forward contracts due to foreign currency fluctuation. Noticing the above, he called upon the assessee to explain why the loss claimed by the assessee should not be disallowed in view of instruction no. 3 of 2010 dated 23.03.2010 issued by Central Board of Direct Taxes (CBDT). In response to the query raised, the assessee filed a detailed submission on 21.12.2018 justifying its claim. Further, the assessee submitted that CBDT instruction no. 3/2010 would not be applicable to assessee. The AO however did not accept the submissions of the assessee and proceeded to disallow the unrealized foreign exchange loss of Rs. 4,04,22,093/-, following CBDT instruction no. 3/2010. Though, assessee contested the aforesaid disallowance before learned Commissioner (Appeals), however, relying upon the decision of the Tribunal in case of *Bechtal India (P) Ltd.* vs. ACIT (2017) 82 taxmann.com 301 (Delhi), learned Commissioner (Appeals) sustained the disallowance.

4. Learned Counsel for the assessee submitted, assessee imports raw-material, packing material and various other goods from foreign vendors on credit and also sales its finished products to foreign customers. Thus, to safeguard against loss, which may arise due to fluctuation in foreign currency

rates, the assessee had entered into forward contracts in respect of its export/import orders to hedge against the risk of foreign currency fluctuation. He submitted, all the foreign exchange forward contracts are in respect of underlying import or export transaction. He submitted, the assessee had not entered into any financial derivative transaction which is either for trading or for speculation purpose. He submitted, the auditor also has specifically mentioned this fact in note no. 32 of the Audit Report. He submitted, as per the consistent method of accounting followed by the assessee over the years, the outstanding foreign currency to monetary items are converted at the closing rate by following mercantile system of accounting and Accounting Standard (AS)-11. He submitted, applying the same principle of accounting, the debtors, creditors, borrowings and un-settled forward contracts were restated at the year–end applying the closing rate of the foreign currency and gain/loss of such conversion was charged to the profit and loss account. He submitted, as per the consistent method of accounting followed by the assessee, a foreign exchange fluctuation loss of Rs. 5,76,48,932/- was incurred for the year including the foreign exchange fluctuation loss of year end conversion of outstanding forward contracts. Drawing our attention to details of loss on conversion of debtors, creditors, borrowings and unsettled forward contracts, as placed at page 58 of the paper book, learned counsel submitted, the AO has accepted loss in respect of receivables and debtors, whereas, he did not accept loss incurred on year end conversion of outstanding forward contracts. He submitted, following same accounting method, in assessment year 2015-16, the assessee has offered gain on restatement in value of un-settled contracts which was accepted by the Department. In this context, he drew our attention to the assessment order passed for the assessment year 2015-16. Thus, he submitted, when the AO is accepting the gain shown by the assessee, there is no reason to disallow the loss arising out of a similar situation. He submitted, now, it is fairly well settled that loss arising out of unsettled forward contract is allowable. In this regard, he relied upon the following decisions:-

1. *"CIT Vs. Woodward Governor India (P) Ltd. (312 ITR 254)-Supreme Court.*
2. *CIT Vs. Badridas Gauridas (P) Ltd. (261 ITR 256)-Bombay HC*
3. *CIT Vs. D. Chetan & Co. (ITA No. 278/2014)-Bombay HC*
4. *Pr. CIT Vs. International Gold Company Ltd. (ITA No. 1827/2016)-Bombay HC*
5. *Pr. CIT Vs. Vishinda Diamonds (ITA No. 1841/2016)-Bombay HC*
6. *Pr. CIT Vs. Osia Gems (ITA No. 1221/2016) Bombay HC*
7. *Essel Propack Ltd. Vs. DCIT (ITA No. 5312/Mum/2015)-Mumbai ITAT*
8. *ACIT Vs. Shree Balkrishna Exports (ITA No. 4185/Mum/2014)-Mumbai ITAT*
9. *S. Vinodkumar Diamonds Pvt. Ltd. Vs. DCIT (ITA No. 79/Mum/2015)-Mumbai ITAT*
10. *DCIT Vs. Bank of Bahrain & Kuwait (41 SOT 290) (SB)-Mumbai ITAT*
11. *Everest Industries Ltd. Vs. JCIT (90 taxmann.com 330)-Mumbai"*

5. He submitted, learned Commissioner (Appeals) has wrongly relied upon the decision in case of Bechtal India (P) Ltd as it is factually distinguishable. Further, he submitted, in case of Bechtal India (P) Ltd., the decisions of Hon'ble Bombay High Court have not been considered. Thus, he submitted, following the ratio laid down in case of CIT vs. Woodward Governor India (P) Ltd. (supra) and the decision of the Hon'ble Bombay High Court, loss claimed by the assessee should be allowed. Further, he submitted, since the loss claimed by the assessee is based on consistent method of accounting followed from earlier assessment years and the AO has all along accepted assessee's method of accounting, a different approach cannot be adopted in the impugned assessment year keeping in view rule of consistency. Finally, he submitted, since the assessee has claimed the loss in the impugned assessment year, it has reversed such loss in the subsequent assessment year, wherein the contracts matured. Thus, he submitted, in case it is disallowed in the

impugned assessment yea, it has to be allowed in the subsequent assessment year, otherwise, there will be double disallowance.

5. The learned Departmental Representative strongly relying upon the observations of the AO and learned Commissioner (Appeals) submitted, the fact on record clearly reveal that the forward contracts have remained outstanding at the end of the year. Therefore, the loss computed by the assessee is purely notional and speculative loss. She submitted, since such loss is not allowable as per CBDT instruction no. 3/2020, which is binding on the departmental authorities, loss claimed by the assessee was correctly disallowed.

6. We have considered rival submissions in the light of the decisions relied upon and perused the materials on record. As far as the factual aspect of the issue is concerned, there is no dispute between the assessee and the revenue that the forward contracts entered by the assessee with banks are in respect of underlying import/export transactions. Thus, they are in the nature of hedging contracts to safeguard against loss, if any, arising on account of fluctuation in foreign currency. It is also a fact that as per the consistent method of accounting followed by assessee and applying Accounting Standard-11, the assessee restates the value of debtors, creditors, borrowings and unsettled forward contracts at the yearend applying closing rate of the foreign currency. It is also uncontroverted fact that on such restatement, if there is any gain, the assessee offers it as income and in case there is a loss, assessee claims it as deduction. The Departmental Authorities have also not disputed that the aforesaid accounting method is consistently followed by the assessee and gain arising on reinstatement of unsettled forward contracts at the yearend have been offered as income in some assessment years and accepted by the Department.

7. A perusal of the impugned assessment order would reveal that simply relying upon the CBDT instruction no. 3/2010, the AO has disallowed the claim of loss. However, on a careful perusal of CBDT Instruction No. 3/2010 (supra), we are of the view that the instruction clearly speaks about foreign exchange derivatives contract and not hedging transactions. Thus, in our view,

CBDT instruction no. 3/2010 would not be applicable to the assessee. Having held so, let us examine the reasoning of learned Commissioner (Appeals). As could be seen from the observations of learned Commissioner (Appeals) in paragraph 4.2 of the impugned order, without recording any reasoning of his own, he has simply relied upon a decision of the Tribunal in case of Bechtal India (P) Ltd. vs. ACIT (supra). The Hon'ble Supreme Court in case of CIT vs. Woodward Governor India (P) Ltd. (supra) has held that any gain or loss on outstanding receivables at the year end would be allowable. This ratio laid down by the Hon'ble Supreme Court has been followed by subordinate Courts and Tribunals in a number of decisions. Identical view has been expressed by the Hon'ble jurisdictional High Court in case of CIT vs. Badridas Gauridas(P) Ltd. (supra), Pr. CIT vs. International Gold Company Ltd. (supra). In case of PCIT vs. M/s Osia Gems (supra), the following question came up for consideration before the Hon'ble jurisdictional High Court:

> *"Whether on the facts and circumstances of the case and in law, the Tribunal was justified in allowing 'Mark to Market' loss of Rs. 1,54,83,835/- arising on valuation of forward exchange contracts on the closing date of accounting year?"*

8. While answering the referred question, the Hon'ble jurisdictional High Court following their own decision in case of CIT vs. M/s D Chetan & Co. decided the issue in favour of the assessee. The observations of the Hon'ble High Court are reproduced below for better clarity:

> *"2. Learned counsel for the Revenue pointed out that the issue is squarely covered against the department by virtue of the judgment of this Court in the case of CIT Vs. M/s D. Chetan & Co. dated 1.10.2016 in Income Tax Appeal No. 278 of 2014. Following observations of the Court may be noted:-*
>
> > *"7. The impugned order of the Tribunal has, while upholding the finding of the CIT (Appeals), independently come to the conclusion that the transaction entered into by the Respondent assessee is not in the nature of speculative activities. Further the hedging transactions were entered into so as to cover variation in foreign exchange rate which would impact its business of import and export of diamonds. These*

concurrent finding of facts are not shown to be perverse in any manner. In fact, the Assessing Officer also in the Assessment Order does not find that the transaction entered into by the Respondent assessee was speculative in nature. It further holds that at no point of time did Revenue challenge the assertion of the Respondent assessee that the activity of entering into forward contract was in the regular course of its business only to safeguard against the loss on account of foreign exchange variation. Even before the Tribunal, we find that there was no submission recorded on behalf of the Revenue that the Respondent assessee should be called upon to explain the nature of its transactions. Thus, the submission now being made is without any foundation as the stand of the assessee on facts was never disputed. So far as the reliance on Accounting Standard11 is concerned, it would not by itself determine whether the activity was a part of the Respondent assessee's regular business transaction or it was a speculative transaction. On present facts, it was never the Revenue's contention that the transaction was speculative but only disallowed on the ground that it was notional. Lastly, the reliance placed on the decision in S. Vinodkumar (supra) in the Revenue's favour would not by itself govern the issues arising herein. This is so as every decision is rendered in the context of the facts which arise before the authority for adjudication. Mere conclusion in favour of the Revenue in another case by itself would not entitle a party to have an identical relief in this case. In fact, if the Revenue was of the view that the facts in S. Vinodkumar (supra) are identical / similar to the present facts, then reliance would have been placed by the Revenue upon it at the hearing before the Tribunal. The impugned order does not indicate any such reliance. It appears that in S. Vinodkumar (supra), the Tribunal held the forward contract on facts before it to be speculative in nature in view of Section 43(5) of the Act. However, it appears that the decision of this court in CIT vs. Badridas Gauridas (P) Ltd.1 was not brought to the notice of the Tribunal when it rendered its decision in S. Vinodkumar (supra). In the above case, this court has held that forward contract in foreign exchange when incidental to carrying on

business of cotton exporter and done to cover up losses on account of differences in foreign exchange valuations, would not be speculative activity but a business activity."

9. Thus, the aforesaid observations of the Hon'ble jurisdictional High Court definitely clinches the issue in favour of the assessee.

10. Pertinently, when the AO is accepting the gain offered as income by the assessee following similar accounting method, there is no justifiable reason to disallow the loss. It is also relevant to observe, the contention of the assessee that the loss determined on restatement of forward contract as on 31.03.2016 was reversed on 01.04.2016 i.e. on the first day of the succeeding assessment year, wherein, the forward contracts matured has not been controverted. Thus, any disallowance in the impugned assessment year would be prejudicial to the assessee, as, it would amount to double disallowance of the same amount. Thus, respectfully following the decisions of the Hon'ble Supreme Court and Hon'ble jurisdictional High Court cited before us, we allow assessee's claim of loss. The disallowance is hereby deleted. Grounds are allowed.

11. In the result, appeal is allowed.

Order pronounced in the open court on 26th July, 2021.

Sd/-	*Sd/-*
(MANOJ KUMAR AGGARWAL)	(SAKTIJIT DEY)
ACCOUNTANT MEMBER	JUDICIAL MEMBER

मुंबई Mumbai; दिनांक Dated: 26/07/2021

Alindra, PS

आदेश प्रतिलिपि अग्रेषित/Copy of the Order forwarded to :

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

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