# M/S Harman Connected Services ... vs Additional Commissioner Of Income Tax ... on 12 January, 2023

ITA Nos.1980 to 1982/Bang/2018
M/s. Harman Connected Services
Corporation India Pvt. Ltd., Bangalore

IN THE INCOME TAX APPELLATE TRIBUNAL
"C'' BENCH: BANGALORE

BEFORE SHRI N.V. VASUDEVAN, VICE PRESIDENT
AND
SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER

ITA Nos.1980 to 1982/Bang/2018
Assessment Years: 2009-10, 2010-11 & 2012-13

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| M/s. Harman Connected Services<br>Corporation India Pvt. Ltd.<br>(formerly known as Symphony Teleca<br>Corporation India Private Ltd.)<br>No.3 & 3A, EOIZ Industrial Area<br>Survey No.85 & 86, Sadarmangala<br>Village<br>Krishnarajapuram Hobli<br>Bangalore 560 066<br><br>PAN NO : AABCG5658E<br>APPELLANT | Vs. | Addl. CIT<br>Range-12<br>(currently with ACIT<br>Circle-3(1)(2))<br>Bangalore<br><br><br><br><br>RESPONDENT |

Appellant by : Shri T. Suryanarayana, Sr. A.R.
Respondent by : Shri Sreenivas T. Bidari, D.R.

Date of Hearing : 04.01.2023
Date of Pronouncement : 12.01.2023

ORDER

PER CHANDRA POOJARI, ACCOUNTANT MEMBER:

All these appeals by assessee are directed against different orders dated 9.4.2018, 10.4.2018 & 10.4.2018 passed u/s 143(3) of the Income-tax Act,1961 ['the Act' for short] by the CIT(A), Bangalore for the assessment years 2009-10, 2010-11 & 2012-13.

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2. The first common ground in all these appeals in ITA Nos.1980 to 1982/Bang/2018 is with regard

to disallowance of MTM losses on forex derivatives (unrealised) and hedging losses (realised) and with regard to non-adjudicating of the ground relating to the hedging losses amounting to Rs.50,49,94,175/- of Bangalore unit and Rs.74,74,205/- of Pune Unit. We consider the facts on this issue as narrated in ITA No.1980/Bang/2018 for the AY 2009-10.

3. This ground of appeal relates to adjustment of marked to market losses. In brief, during the assessment proceedings, the AO observed that the assessee has debited the profit and loss account by an amount of Rs.78,69,47,279/- on account of unrealised marked to market losses. Of this an amount of Rs.77,78,98,324/- was debited under the head 'unrealised marked to market losses' and the balance amount of Rs.90,48,955/- was included in foreign exchange loss of Rs.12,85,52,937/-. After taking into consideration the replies of the assessee on the issue, the AO concluded that the marked market losses (MTM) claimed by the assessee on account of restatement of forex derivatives at the end of the financial year are not allowable as revenue expenditure. Accordingly, an amount of Rs.78,69,47,279/- was disallowed and added back to the income of the respective undertakings/units of the assessee company.

4. The ld. A.R. submitted that during the assessment year 2009- 10, the assessee incurred an aggregate loss of Rs. 129,94,15,659/- (comprising of loss of Rs. 78,69,47,279/- arising on restatement of forward contracts, and realised loss of Rs. 51,24,68,380/-), in respect of the forward contracts entered into by it, on account of fluctuation of foreign currency. The assessee claimed the loss as a deduction.

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5. The ld. CIT(A) has observed that a perusal of the details filed by the assessee shows that during the year under consideration, the assessee company had made certain exports and raised invoices from time to time. To safeguard any losses in sales, invoices raised on account of exchange fluctuation in foreign currency, the assessee used to enter into Forward Contracts with Banks in relation to some of these sales. Some of these forward contracts matured during the year and some of them had the maturity date beyond 31.03.2009. The contracted rate of currency exchange varied depending upon the time of entering into such contract and the rate offered by the bank at that time. According to the assessee, it re-measured its forward contract pending as on 31/03/2009 at prevalent forward market exchange rate and computed total loss of Rs,78,69.47,279/-, which was debited to the profit and loss account and claimed in the return of income. However, the assessee expressed its inability before the ld. CIT(A) to link various sale invoices with the forward contracts. In addition to above, the assessee also restated the foreign exchange trade receivables as on 31.03.2009 as per the prevailing market exchange rate on that date.

5.1 During the appellate proceedings, the assessee has placed reliance on the judgment of the Hon'ble Supreme Court in the case of CIT Vs Woodward Governor India (I) Ltd. [2009] 312 ITR 254/179 Taxman 326. Therefore, it is important to look into-the ratio of the said case. In this case, questions of law related to the impact of variation in foreign currency exchange rate on the balance sheet date both on the expenditure on account of capital as well as revenue. The questions of law

framed in the case of Woodward Governor (supra) are as under:

> "(i) Whether, on the facts and circumstances of the case and in law, the additional liability arising on account of fluctuation in the rate of exchange ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore in respect of loans taken for revenue purposes could be allowed as deduction under s. 37(1) in the year of fluctuation in the rate of exchange or whether the same could only be allowed in the year of repayment of such loans?
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> ii) Whether the assessee is entitled to adjust the actual cost of imported assets acquired in foreign currency on account of: fluctuation in the rate of exchange at each balance sheet date, pending actual payment of the varied liability?"

5.2 As far as second question of law is concerned, the ld. CIT(A) observed that the effect of fluctuation in exchange rate of foreign currency on capital expenditure is governed by the Section 43A of the Act. Since in the above batch of the appeals, the assessment year involved was 1998-99, the SC decided the issue in view of Section 43A (pre-amended w.e.f. 01/04/2003) of the Act. After 1-4-2003, the issue is governed by the amended Section 43A of the Act.

5.3 As regards the first question of law in above case, it was observed by the ld. CIT(A) that there was a loan liability in the books of accounts of the assessee on revenue account as a monetary transaction appearing in the balance sheet and was raised in foreign currency. Due to fluctuation in foreign currency exchange as on 31st March of the accounting year, the liability had increased. The assessee debited the increase in liability due to fluctuation as loss in the profit and loss account. The Hon'ble Supreme Court held that the loss suffered by the assessee on revenue account, maintaining accounts regularly on Mercantile system and following accounting standards prescribed by the Institute of Chartered Accountants of India, on account of fluctuation in rate of foreign exchange as on the date of balance sheet, was an item of expenditure under section 37(1) of the Act notwithstanding that the liability had not been discharged in the ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore year in which the fluctuation in the rate of foreign currency occurred. While allowing the loss due to fluctuation in the rate of exchange on the balance sheet date, the Hon'ble Supreme Court explained the position through following example:

> "19. A company imports raw material worth US $250000 on 15th Jan, 2002 when the exchange rate was Rs.46 per US$. The company records the transaction at that rate. The payment for the imports is made on 15th April, 2002 when the exchange rate is Rs.49 per U$. However, on the balance sheet date, 31st March, 2002, the rate of exchange is Rs.50 per US $. In such a case, in terms of AS-11, the effect of the exchange difference has to be taken into P&L account. Sundry creditors is a monetary item and hence such item has to be valued at the closing rate, i.e. Rs.50 at 31st March, 2002, irrespective of the payment for the sale subsequently at a lower rate. The difference of Rs.4 (50-46) per US$ is to be shown as an exchange loss in the P&L account and is not to be adjusted against the cost of raw materials."

5.4 The ld. CIT(A) noted that in the case of Bechtel India (P.) Ltd. vs. Assistant Commissioner of Income-tax, Circle -4(2), [2017] 82 taxmcwo.com 301 (Delhi - Trib.), wherein held that 5.5 Considering above judgement, the ld. CIT(A) concluded that the claim of the assessee needs to be rejected. The loss claimed by the assessee is wholly unwarranted. Further the ld. CIT(A) observe that the claim of the assessee is also in nature of a provision for a liability which would never arise. So the claim needs to be treated to be in nature of an unascertained liability. The assessee has relied upon the decision of jurisdictional ITAT in the case of Quality Engineering & Software Technologies (P) Ltd (Supra). However it is noted that the same was rendered on different facts and the facts as discussed above were never before the ITAT. As regards argument of the assessee to allow this loss to be carried forward to be set off in future years against MTM gain, the same is also without merit as the loss itself is found to be wrongly claimed. Considering above, the ld. CIT(A) noted that the ground of appeal of the assessee needs to be dismissed.

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6. The ld. A.R. submitted that with respect to the export sales of the assessee, invoices are raised in foreign currency on a particular date, whereas they are realised on different dates in the future. Since the assessee's expenditure is in Indian currency, in order to secure a steady flow of INR to meet its operating expenses, the assessee entered into hedging contracts with banks.

6.1 The ld. A.R. further submitted that undisputedly, the forwards contracts entered into are in respect of the export sales of the assessee. This is in fact acknowledged by the CIT(A) in para 5.8 of his order. Therefore, any loss arising therefrom ought to be allowed as a revenue expenditure. Moreover, the assessee has now filed additional evidence before this Tribunal, to demonstrate that the forward contracts entered into are in respect of the export sales. In any event, the ld. A.R. submitted that the realised loss of Rs. 51,24,68,380/- ought to be allowed as a deduction, in view of the settled position of law. He relied on following judgements:

- CIT v. D. Chetan & Co. (reported in [2016] 75 taxmann.com 300 (Bombay)- para 7);

- PCIT v. Mphasis Ltd. (reported in [2021] 128 taxmann.com 138 (Karnataka)-paras 14-20);

- Quality Engineering & Software Technologies (P.) Ltd. v. DCIT (reported in [2014] 52 taxmann.com 515 (Bangalore-Trib.)- para 4.5.8); and

- CIT v. Woodward Governor India (P.) Ltd. (reported in [2009] 179 Taxman 326 (SC)- paras 12-21).

7. The ld. D.R. submitted that the ld. CIT(A) has observed that the assessee made certain exports and part of the export receipts were pending as on the balance sheet date i.e. 31-3-2009 and were thus shown as receivables in the balance sheet. The receivables in the case of the assessee are items of balance sheet and arisen due to trading transactions. In view of the ratio of the Woodward

Governor (P) Ltd (Supra), the assessee was having option of ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore measuring its exports receivables at exchange rate of US dollar on the balance sheet date. Admittedly the assessee has already done so. The AO has not disputed the same and such gain or loss has been allowed to the assessee. But the assessee has gone a step further and made additional claim in relation to same receivables on the basis of forward contracts and claimed loss on the basis of revaluation of the forward contracts. The assessee entered into forward contracts with banks at predetermined exchange rate of foreign currency to safeguard its receivables from any fluctuation in foreign exchange. By entering into such forward contracts, the assessee hedged its receivables and immuned itself from effect of any change in exchange, rate of foreign currency. Whatever may be the foreign change rate on the date of receipt of exports, whether it is higher or lower than the contracted rate, the assessee was certain of receiving the contracted rate under the forward contract. However, by revaluing these forward contracts on 31.03.2009, the assessee has made claim of loss not only on the basis of revaluation of its foreign exchange receivables but also on the basis of forward contracts. The ld. CIT(A) opined that such an additional loss cannot be allowed to the assessee. The ld. CIT(A) noted that in the case of Bechtel India (P.) Ltd. vs. Assistant Commissioner of Income-tax, Circle -4(2), [2017] 82 taxmcwo.com 301 (Delhi - Trib.),under similar facts the ITAT held as follows:

> "4.5. We have heard the rival submission and perused the relevant material on record. The Ld. counsel has placed reliance on the judgment of the Hon'ble Supreme Court in the case of Woodward Governor Private Limited (supra). In assessment year 2008-09, the forex fluctuation loss on unexpired forward contracts was allowed by the Tribunal following the Hon'ble Supreme Court in the case of Woodward Governer (312 ITR 254).Therefore, it is relevant to refer the ratio of the Hon'ble Supreme Court in the case. In the said case, questions of law were raised in respect of impact of variation in foreign currency exchange rate on the balance sheet date both on the expenditure on account of capital as well as revenue. The questions of law framed in the case of Woodward Governor (supra) are as under:
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> ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore "(i) Whether, on the facts and circumstances of the case and in law, the additional liability arising on account of fluctuation in the rate of exchange in respect of loans taken for revenue purposes could be allowed as deduction under s. 37(1) in the year of fluctuation in the rate of exchange or whether the same could only be allowed in the year of repayment of such loans?
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> (ii) Whether the assessee is entitled to adjust the actual cost of imported assets acquired in foreign currency on account of fluctuation in the rate of exchange at each balance sheet date, pending actual payment of the varied liability?"

4.5.1. As far as second question of law is concerned, the effect of fluctuation in exchange rate of foreign currency on capital expenditure is governed by the Section 43A of the Act. Since in the above batch of the appeals, the assessment year involved was 1998-99, the Hon'ble Supreme Court decided the issue raised in second question of law in view of section 43A (pre-amended w.e.f. 01/04/2003)

of the Act and held that it became possible to adjust the increase/decrease in liability relating to acquisition of capital assets on account of exchange rate fluctuation, in the actual cost of the assets acquired in foreign currency and for, inter alia, depreciation to be allowed with reference to such increased/decreased cost. After 1-4-2003, the issue is governed by the amended section 43A of the Act.

4.5.2. As regards the first question of law in the case of Woodward Governor (supra), we find that there was a loan liability in the books of accounts of the assessee on revenue account as a monetary transaction appearing in the balance sheet and was raised in foreign currency. Due to fluctuation in foreign currency exchange as on 31st March of the accounting year, the liability had increased. The assessee debited the increase in liability due to fluctuation as loss in the profit and loss account. The Hon'ble Supreme Court held that the loss suffered by the assessee on revenue account, maintaining accounts regularly on Mercantile system and following accounting standards prescribed by the Institute of chartered accountant of India (ICAI), on account of fluctuation in rate of foreign exchange as on the date of balance sheet, was an item of expenditure under section 37(1) of the Act notwithstanding that the liability had not been discharged in the year in which the fluctuation in the rate of foreign currency occurred. While allowing the loss due to fluctuation in the rate of exchange on the balance sheet date, the Hon'ble Supreme Court explained the position through following example:

> "19. A company imports raw material worth US $ 250000 on 15th Jan., 2002 when the exchange rate was Rs. 46 per US $. The company records the transaction at that rate. The payment for the imports is made on 15th April, 2002 when the exchange rate is Rs. 49 per US $. However, on the balance sheet date, 31st March, 2002, the rate of exchange is Rs. 50 per US $. In such a case, in terms of AS-11, the effect of the exchange difference has to be taken into P&L account. Sundry creditors is a ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore monetary item and hence such item has to be valued at the closing rate, i.e. Rs. 50 at 31st March, 2002, irrespective of the payment for the sale subsequently at a lower rate. The difference of Rs. 4 (50-46) per US $ is to be shown as an exchange loss in the P&L account and is not to be adjusted against the cost of raw materials."

4.5.3. The Hon'ble Supreme Court in the case of Woodward Governor (supra) has followed the decision of the Hon'ble Supreme Court in the case of Sutlej Cotton Mills Ltd. Vs. CIT, (1979) 116 ITR 1 (SC), where it is held that if loss of foreign exchange fluctuation was on account of trading liability, the same would be allowable. Further, Hon'ble Delhi High Court in the case of Eicher Good Earth in ITA No. 7078 of 1992 observed that the mercantile system of accounting made it mandatory to translate the outstanding liability on the basis of fluctuation of foreign currency rate and amount of increase in such liability as allowable. In this respect, it is relevant to refer the decision of Hon'ble Supreme Court in the case of CIT Vs. Dempo and company private limited reported in 206 ITR 291, wherein trading liability has been summarized as under;

• A loss arising in the process of conversion of foreign currency which is part of trading asset of the assessee is a trading loss as any other loss.

• In determining the true nature and character of the loss, the cause which occasions the loss is immaterial; what is material is whether the loss has occurred in the course of carrying on the business or is incidental to it.

• If there is loss in a trading asset, it would be a trading loss, whatever be its cause because it would be a loss in the course of carrying on the business.

• Loss in respect of circulating capital is revenue loss whereas loss in respect of fixed capital is not.

• Loss resulting from depreciation of the foreign currency which is utilized or intended to be utilized in business and is part of the circulating capital, would be a trading loss, but depreciation of fixed capital on account of alteration in exchange rate would be capital loss.

• For determining whether devaluation loss is revenue loss or capital loss what is relevant is the utilization of the amount at the time of devaluation and not the object for which the loan had been obtained. Even if the foreign currency was intended or had originally been utilized for acquisition of fixed asset, if at the time of devaluation it had changed its character and had assumed the new character of stock-in-trade or circulating capital, the loss that occurred on account of devaluation shall be a revenue loss and not a capital loss.

4.5.4. The Hon'ble Supreme Court in the above case has also held that the way in which entries are made by the assessee in the books of accounts is not determinative ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore of the question whether the assessee has earned any profit or suffer any loss and what is necessary to be considered is the true nature of the transaction and whether in fact it has resulted in profit or loss to the assessee.

4.5.5. In the present case, the assessee exported certain services to its associated enterprise and part of those export receipts were pending on the balance sheet date i.e. 31/03/2009 and were shown as receivables of Rs. 71.64 crores in the balance sheet. The receivables in the case of the assessee are items of balance sheet and arisen due to trading transactions. In view of the ratio of the Woodward Governor's Private Limited (supra), the assessee was having option of measuring its exports receivables at exchange rate of US dollar on the balance sheet date, and any gain or loss on the same would have been allowable to the assessee. But the assessee did not do so.

4.5.6. Whereas, according to the submission of the assessee before us, the assessee entered into forward contracts with banks at predetermined exchange rate of foreign currency to safeguard it receivables from any fluctuation in foreign exchange. By entering into such forward contracts, the assessee hedged its receivables and immuned itself from effect of any change in exchange rate of foreign currency. Whatever may be the foreign change rate on the date of receipt of exports, whether it is higher or lower than the contracted rate, the assessee was certain of receiving the contracted

rate under the forward contract. For example, in forward contract No. 146164, which is available on page 78 of the paper book the assessee agreed to sell US dollar 29,00,000 at the rate contacted of Rs. 42.97 per US dollar. The maturity date of the said contract was 03/04/2009 and according to the FIRC issued by the bank, which is available on page 300 of the paper book, the assessee received USD 29,00,000/- from its associated enterprises M/s BECHTEL Capital Management Corporation, which was sold to bank at the rate of Rs. 42.97 per dollar as already contracted. According to the decision in the case of Woodword Governor (supra), the assessee could have re-measured is its receivables on the balance sheet date according to the foreign exchange rate contracted in the forward contracts. For example, the assessee made sales of 632 USD in Oct., 2008 and recorded sales in Indian rupees at Rs.31,640/- in books of account. According to this exchange rate, on the date of sale was Rs. 50.06. The assessee apprehended decline in foreign exchange rate and already entered into a forward contract with the banks having contracted foreign exchange rate of Rs. 42.97 USD. On the date of balance sheet, the forward contract was not matured. In such circumstances, following the Woodward Governor (supra), the assessee could have valued export receivable of 632 USD at the rate of Rs. 42.97 which would be Rs. 27,157/- and in that case the assessee would have a loss of Rs. 31,640 - 27,157 = Rs. 4,483/-, on balance-sheet date as per "marked to market", which would have been allowed as a loss to the assessee.

4.5.7. But the assessee has not claimed the loss on the trading liability which was allowable following the case of Woodward Governor (supra). The assessee instead of measuring the receivables on balance sheet date at foreign exchange rate contracted, it measured the pending forward contracts on balance sheet date at a ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore value of foreign currency in the forward market. The assessee has entered into 9 forward contracts. The first forward contract No. 146164 was entered into for sale of 29,00,000 USD at the rate of contracted rate of foreign exchange of Rs.42.97 and the assessee has valued this forward contract on balance sheet date at foreign exchange rate of Rs. 50.78. The assessee has treated the forward contract as its liability to pay and thus according to the assessee its liability to pay to the bank has increased by an amount of rupees 29,00,000 (50.78-42.97) = 2,26,49,000/- . The assessee has claimed this liability as loss. Similarly, the assessee has claimed loss on all the forward contracts, which is amounted to Rs.21,80,46,325/-.

4.5.8. In our opinion, the kind of loss claimed with assessee is not allowable in view of the decision of the Hon'ble Supreme Court in the case of Woodward Governor (supra) and other decisions discussed above, due to following reasons:

> (i) In relevant period, the assessee was evidently not dealing in forward contracts and those forward contracts were not part of a stock in trade of the assessee. Thus, these transactions were in not on account of the trading and, therefore, there was no trading liability.
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> (ii) The assessee, to avoid any unforeseen losses on account of downfall in foreign exchange rate, entered into forward contracts and sealed the amount of foreign exchange rate, which would be receivables to it. In such a situation, the assessee is not affected by any up or down in the foreign change rate of US dollar either on the

> balance sheet date or on the date of actual receipt of foreign currency from buyers till maturity date of the contract. It eliminated effect of any change in the currency exchange fluctuation rate on the receivables. The assessee was certain of receiving US dollar equivalent to what it agreed to sale to the bank in respect of forward contracts. Had the assessee not have the underlying receivables, then on the date of maturity of forward contracts, the assessee would have required to settle the contracts either by the purchasing US dollar from market or paying difference of exchange rate. If the assessee, would have required to buy US dollar for honouring its forward contracts of sale of US dollar, the liability of the assessee would have definitely dependent on the foreign exchange rate on maturity date or balance sheet date. But in the instant case, as the assessee has submitted that it entered into hedging forward contract transactions and settled all the forward contract by way of export receivables, therefore, it was immuned from any such fluctuation in the foreign exchange rate and there was no liability, which could arise on account of such fluctuation in foreign exchange on maturity of contract.

In such circumstances, when it is certain that no additional liability would arise to the assessee on the maturity of the contract, the possibility of such liability on the balance sheet date also cannot arise. The only outgo on account of the forward contracts was premium or discount payments to the banks at the inception of forward exchange contracts ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore and there was no outgo on possible fluctuation in the foreign exchange rate, and thus, there was no liability on revenue account in respect of the forward contracts.

4.5.9. The assessee to immune itself from any losses on account of fluctuation in foreign exchange rate at the time of receipt of payment against the sale invoices, entered into forward contracts with banks. The assessee entered into a contract with the bank to sale US dollar at a predetermined rate on future date. For example, according to forward contract No. 146164 dated 06/08/2008, the assessee agreed to sale 29,00,000 US dollar at the rate of Rs.42.97 per dollar. This forward contract was having maturity date of 03/04/2009. The assessee was expecting receipt of US dollar against sale invoices amounting to USD 632 (October, 2008); USD 1,44,247 (November, 2008) and USD 27,55,121 (December, 2008) before maturity period of the forward contract. By entering into forward contract with banks at predetermined rate of Rs.42.97 per dollar having corresponding export invoices as underlying, the assessee immuned itself from any fluctuation in the foreign exchange rate. From the foreign inward remittance certificate issued by the bank on 02/04/2009, also it is evident that amount of US dollars 29,00,000/- was received against invoices and which was credited at the rate of Rs. 42.97 per US dollor in account of the assessee.

4.6. The Tribunal in assessment year 2008-09 allowed the foreign exchange fluctuation loss with following finding:

> "8. Coming to the corporate additions i.e. disallowance of loss, it clearly emerges from the record that the assessee in respect of foreign exchange realization follows mercantile system of accounting and not case system of accounting. The loss has been

> incurred for hedging of foreign currency fluctuation involved in sales invoices on the basis of forward contracts, which is a business decision to safeguard its interest. The loss has been incurred on the basis of scientific method in the ordinary course of business. The loss being based on a scientific method, on the basis of contractual liability with banks and on mercantile system has to be allowed to the assessee following Hon'ble Supreme Court judgment in the case of Woodward Governor India (P.) Ltd. (supra). Our view is further fortified by the fact that DRP in its own order in subsequent year has itself held that the issue about the loss on mercantile system is pending dispute in A.Y. 2008-09. Therefore, the allowability of the loss on actual payment in A.Y. 2009-10 has been made subject to the allowability of the loss for A.Y. 2008-09. This stand of the DRP itself negates the observations of Assessing Officer that it is a notional loss and establishes that it is a business loss incurred by the assessee on mercantile system which method is consistently followed by the assessee. Under these circumstances, we are inclined to allow the foreign exchange fluctuation loss to assessee in this year. This ground of the assessee is allowed."

ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore 4.7. In our opinion, in the assessment year 2008-09, facts in detail were not brought before the Tribunal, as to whether the foreign-exchange fluctuation liability was in respect of export receivables, which was an item of trading account or in respect of forward contracts, which were not part of trading account of the assessee.

4.8. In view of our discussion above, we are of the opinion that hedging forward contracts of foreign currency cannot be "marked to market" (MTM) on balance sheet date as already there is a underlying asset and there is no extra outgo for settlement of the forward contract other than already determined in the contract and thus there is no additional liability or benefit to the assessee on the settlement date. Once there is no liability or benefit on the settlement date, there is no possibility of liability or benefit to the assessee on balance sheet date also.

4.9. We find that in second round of proceedings, the Ld. DRP in absence of submission /calculation from the assessee, held the forward contract transactions as a speculative transactions and following the decision of the Tribunal in the case of Sh. Vinod Kumar Diamonds Private Limited Vs. Addl. CIT, Range-5(3), Mumbai in was upheld. As the issue was restored to the file of the AO/DRP for afresh adjudication after factual analysis and examination of the impugned transaction following the judgment of the Hon'ble Apex Court in the case of Woodward Governor Private Limited (supra) but no such analysis and examination of all the transactions of forward contract has been carried out by the Ld. DRP due to reasons mentioned in the order of the Ld. DRP. The assessee has filed copy of all the forward contracts before us from page 78 to 87 of the paper book. Bottom portion in all these contracts has been blackened with ink, and therefore the contents are not visible. The assessee has also filed copies of Foreign Inward Remittance Certificates (FIRC) before us, which are available on page 300 to 308 of the paper book. It is contested by the Revenue that in certain forward contracts, there was no underlying asset as on the date of balance sheet and, therefore, it need to be examined whether same were forward contract transaction in the nature of hedging or in the nature of speculation. However, in our opinion, when the contention of the assessee that all the forward

contracts were settled by way of actual delivery through dollars received on export receivables, the assessee cannot be allowed "mark to market" losses on such forward contract and therefore it is not required to examine whether those forward contract transactions were speculative in nature.

4.9.1. In view of above facts and circumstances, we hold that the loss of Rs.21,80,46,325/- claimed by the assessee on account of mark to market losses on account of fluctuation in foreign currency in respect of hedging forward contract is not allowable. The grounds of appeal, raised by the assessee in this respect are accordingly dismissed.

5. In the result, the appeal of the assessee is dismissed."

ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore Keeping in view of the above, the ld. D.R. relied on the order of ld. CIT(A) and submitted that this ground of appeal of the assessee may be dismissed.

8. We have heard the rival submissions and perused the materials available on record. The first issue for our consideration is with regard to disallowance of marked to market losses. The factual matrix of the case are that assessee had made certain exports and raised invoices from time to time. To safeguard any losses in sales invoices raised on account of exchange fluctuation in foreign currency, the assessee used to enter into forward contracts with banks in relation to some of its exports. Some of these forward contracts matured during the year and some of them had matured beyond 31.3.2009. The contract rate of currency exchange varied depending upon the time of entering into such contracts and the rate offered by the bank at that time. Accordingly, the assessee restated this forward contracts pending as on 31.3.2009 at prevalent forward market exchange rate and computed the total loss of Rs.78,69,47,279/-, which is charged to P&L account and claimed it as a deduction in the return of income. However, the assessee failed to link various sale invoices with the forward contracts. In addition to this, the assessee also restated the foreign exchange trade receivables as on 31.3.2009 as per the prevailing market exchange rate on that date. The contention of the assessee's counsel is that the forward contracts are entered into hedge the currency risk associated with normal business transaction i.e. exports. These contracts are entered into within the framework of relevant RBI guidelines. The intention of entering into these contracts was to safeguard interest against exchange rate fluctuation risk on foreign currency receivables and not to carry on separate business activity dealing with currency and these are directly linked to the exports ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore made by the assessee in the assessment year under consideration and have proximate and direct nexus to the business of the assessee though it was difficult to make one to one correlation between forward contracts on its exports invoice in foreign currency and therefore, rightly to be treated as business loss which is to be allowed as a deduction while computing income of the assessee under the head "business" in view of the judgement of Hon'ble Supreme Court in the case of CIT Vs. Woodward Governor (I) Ltd. (2009) (312 ITR

254) and according to the ld. A.R., it is not a notional loss or a capital loss and it is a business loss allowable u/s 37 of the Act which is in the revenue field. It is also submitted by ld. A.R. that assessee consistently following the accounting policy as prescribed in AS-11 used by ICAI. In our opinion,

first of all, the assessee has to prove that its forward contracts are in the nature of hedge transactions entered into make plausible loss on fluctuation in foreign currency and not speculative transactions entered by the assessee company. Therefore, we are of the view that prima facie the case is covered by the judgement of Hon'ble Supreme Court in the case of Woodward Governor (I) Ltd. cited (supra) because the assessee has profit/loss on fluctuation in respect of forward contracts on the basis of marked to market at the end of the financial year based on the prevailing exchange rate. However, the assessee has to prove the basic test provided for categorizing that its forward contracts are in the nature of hedging transaction covering the export invoices, though it was not able to link to one to one exports, bills receivables. In other words, the total amount of exposure to hedging transaction in the assessment year under consideration shall not exceed the total amount of exports made by the assessee excluding the brought forward opening balance. If the total derivative or forward contract undertaken by the assessee in foreign exchange exceeds exports turnover, then that loss suffered in respect of that portion of the ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore excess transaction cannot be considered as a business loss and the same has to be considered as a speculative loss as that excess derivative transaction have no proximity with export turnover of that to be excluded from the business loss. Further, we make it clear that if the assessee restated the debtors as on the date of balance sheet following Accounting Standard-11 with regard to Forward contracts of foreign currency emanated from the export sales, to that extent assessee's claim to be allowed on account of foreign exchange fluctuation. But the AO shall ensure that there is no double deduction in the form of restatement on the last date of the accounting period and other claim on the basis of actual loss on settlement. Accordingly, this issue is remitted to the file of AO for fresh consideration and the ground of the assessee is partly allowed for statistical purposes.

8.1 Now one more contention of the ld. A.R. is that the issue relating to hedging loss has not been examined by the ld. CIT(A) though there was a ground of appeal before him. However, the ld. D.R. made an argument that the assessee has already restated the receivables as on the date of balance sheet in respect of export transactions and granting further deduction on the basis of exchange fluctuation in respect of same receivables amounting to granting of double deduction, which shall be avoided and relied on the order of the Tribunal in the case of Bechtel India (P) Ltd. Vs. ACIT cited (supra). In our opinion, this issue is akin to the earlier issue discussed above. While examining the first issue afresh, the AO shall ensure that there shall not be double deduction i.e. one on the basis of restatement of export receivables and another on the basis of MTM loss of forward contracts. The assessee is only entitled for MTM loss as prescribed in Accounting Standard AS-11 by ICAI, the total loss cannot be more than ascertained loss in respect of both items and ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore there cannot be double claim by the assessee as there is no extra outgo for settlement of the forward contracts other than already determined in the contract. Accordingly, we direct the AO to re-compute the same in the light of above observation and decide afresh after giving opportunity of hearing to the assessee.

9. Ground No.2 raised only in ITA No.1980/Bang/2018 is with regard to holding that MTM loss being unascertained liability need to be added to book profits u/s 115JB of the Act.

10. The ld. A.R. submitted that the disallowance, if at all, cannot be added back while computing the book profits under section 115JB of the Act as the loss incurred is an ascertained liability. Reliance is placed on the decision of the Hon'ble Supreme Court in the case of Apollo Tyres Ltd. V. CIT reported in (2002) 122 Taxman 562 (SC).

11. The ld. D.R. relied on the order of the ld. CIT(A).

12. We have heard the rival submissions and perused the materials available on record. First of all, we are of the opinion that the MTM loss cannot be considered as an unascertained loss as held in the case of Woodward Governor (I) Ltd. cited (supra) while computing book profit u/s 115 JB of the Act and this cannot be added. Accordingly, this ground of assessee is allowed.

13. Ground No.3 of the appeal raised only in ITA No.1980/Bang/2018 is with regard to disallowance of deferred rent.

14. The ld. A.R. submitted that the assessee had taken certain buildings on lease. Since the assessee did not intend to acquire the ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore premises, they had been classified as operating lease, in line with AS-

19. As per AS-19, lease payments are to be recognized as expense in the profit and loss account on a straight line basis unless another systematic basis is more representative of time pattern of the user's benefit. Accordingly, the assessee distributed the total lease amount over the term of the lease and claimed deduction of the charge so created.

14.1 The Assessing Officer held that the deferred rent merely represents a book entry without there being any cash flow and therefore the same is not allowable as revenue expenditure. The CIT(A) affirmed the disallowance. In this regard, it is submitted that the assessee in line with AS 19 has created deferred rent charges. The total rentals for the period of the lease are equally distributed and written off to the profit and loss account over a period of time. The ld. A.R. submitted that the excess charge over payment in the current year is set right by excess payment over charge in the subsequent years, and therefore the treatment is merely a timing difference. The deferred rent calculated for one of the buildings is produced on page 544 of the paper book, showing the charge created and the payment made across 49 months. Therefore, the ld. A.R. submitted that the deferred rent charges are allowable as a deduction.

Without prejudice, the ld. A.R. submitted that if the charge is disallowed during the year under consideration, the same ought to be allowed in the year of payment.

He relied on the following Case laws:

> ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore

- CIT v. Virtual Soft Systems Ltd. (reported in [2018] 92 taxmann.com 370 (SC)- paras 13-18; and

- CIT v. ICICI Venture Funds Management Co. Ltd. (reported in [2015] 62 taxmann.com 128 (Karnataka)- para 10.

In any event, the ld. A.R. submitted that the rent equalization charges are not 'reserve' or an unascertained liability and therefore cannot be added while computing the book profits under Section 115JB of the Act.

15. The ld. D.R. relied on the order of the ld. CIT(A).

16. We have heard the rival submissions and perused the materials available on record. The assessee has been paying rent for various years at the different rates. In the first few assessment years, rent is lower. However, it was increased in subsequent assessment years. The assessee wants equalized rent from year to year by claiming uniform amount of rent in each assessment year. In our opinion, the actual rent paid by the assessee in the assessment year under consideration is to be allowed in each assessment years. There is no system of equalization of rent though it was increased and incurred in subsequent assessment years. Accordingly, we direct the AO to allow accrued rent as applicable in each assessment year as per terms of rent agreement. Ordered accordingly. This ground of the assessee's appeal is partly allowed.

17. Ground No.4 of the appeal of the assessee raised only in ITA No.1980/Bang/2018 is with regard to disallowance of interest on delayed remittance of TDS.

17.1 The ld. A.R. submitted that the assessee had remitted Rs. 1,43,266/- being interest towards delayed remittance of TDS, which ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore the assessee claimed as a deduction. The Assessing Officer disallowed the claim. The CIT(A) affirmed the disallowance. In this regard, the ld. A.R. submitted that Interest under section 201(1A) is not penal but is compensatory. It also does not represent tax of the assessee as it pertains to the tax liability of a third party.

He relied on the following Case laws:

- Total Environment Building Systems Pvt. Ltd. v. DCIT (Order dated 29.06.2022 passed by this Hon'ble Tribunal in ITA Nos. 45&46/Bang/2017)-

para 16

- Resolve Salvage & Fire India (P.) Ltd. v. DCIT (reported in [2022] 139 taxmann.com 196 (Mumbai-Trib.)- para 5)

18. The ld. D.R. relied on the order of ld. CIT(A).

19. We have heard the rival submissions and perused the materials available on record. This issue came for consideration before Hon'ble Madras High Court in the case of CIT Vs. Chennai Properties & Investment Ltd. (1999) 105 Taxman 346 (Madras) while dealing with the identical issue of allowability of interest on delayed payment of TDS held as follows:

> "The question of law referred to at the instance of the ITIT1114e is as to whether the Tribunal was right in law in holding that the interest under section 201(1A) of the Income-tax Act, 1961 ('the Act') paid by the assessee was an expenditure incidental to business and allowed as a deduction from the profits and gains of the business for the assessment year 1981-82.
>
> 2. The assessee had, in the course of the assessment proceedings for the assessment year 1981-82, claimed the deduction of Rs. 10,542 which amount had heed paid by it to the Income-tax Department as interest under section 201(1A). The claim so made was rejected by the ITO and that rejection was affirmed in appeal by the Commissioner. The Tribunal, however, on a further appeal by the assessee, held that the interest so paid was incidental to the business of the assessee and allowed the amount as deduction under section 37 of the Act.
>
> 3. The learned counsel for the revenue, submitted before us that the deduction so permitted by the Tribunal is contrary to the scheme of. the Income-tax Act.
>
> ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore
>
> 15. The counsel for the assessee in support of his submission that the interest paid by the assessee was compensatory in character besides relying on the ease of Mahalakshmi Sugar Mills Co. (supra) also relied on the decisions of the Apex Court in the cases of Prakash Cotton Mills (P.) Lid, v. CIT [1993] 201 ITR 684 / 67 Taxman 546; Malwa Vanaspati & Chemical Co. v. CIT[1997] 225 ITR 383 and CIT v. Ahmedabad Cotton Mfg. Co. Ltd. V. CIT[1994] 205 ITR 163. In all those cases, the Court was concerned with an indirect tax payable by the assessee in the course of its business and admissible as business expenditure. Further. liability for' interest which had been incurred by the assessee therein was regarded as compensatory in nature and allowable as business expenditure.
>
> 16. The ratio of those cases is not applicable here. Income-tax is not allowable as business expenditure. The amount deducted as tax is not an item of expenditure. The amount not deducted and remitted has the character of tax and has to be remitted to the State and cannot he utilized by the assessee for its own business. The Supreme Court in the case of Bharat Commerce et Industries Ltd. (supra) rejected the argument advanced by the assessee that retention of money payable to the State as tax or income-tax would augment the capital of the assessee and the expenditure incurred, namely. interest paid for the period of such retention, would assume the

> character of business expenditure. The Court held that an assessee could not possibly claim that it was borrowing from the State the amounts payable by it as income-tax and utilizing the same as capitalization in its business, to contend that the interest paid fin- the period of delay in payment of tax amounted to a business expenditure.
>
> 17. The question referred to us, therefore, is required to be and is answered in the negative in favour of the revenue and against the assessee."

19.1 Keeping in view of the above judgement, we dismiss the ground taken by the assessee as this is not a business expenditure incurred for the purpose of business.

20. Ground No.5 of the appeal of the assessee raised in ITA Nos.1980 & 1981/Bang/2018 is with regard to disallowance of depreciation on computer.

21. During the year under consideration, the assessee purchase computer software on which it claimed depreciation. The Assessing Officer disallowed the depreciation claimed on the ground that the assessee had not deducted tax at source. Since the CIT(A) granted deduction on the enhanced profits under Section 10A of the Act pursuant to the disallowance made by the Assessing Officer, the ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore CIT(A) did not adjudicate on the merits of the disallowance. In this regard, the ld. A.R. submitted that Section 40(a)(i)/(ia) applies only to expenditure which is claimed as a deduction, whereas, depreciation is not an expenditure or a pay out and is a statutory deduction under the Act. Therefore, Section 40(a) of the Act has no application to depreciation claimed by the assessee.

He relied on the following Case laws:

> PCIT v. Tally Solutions (P.) Ltd. (reported in [2021] 123 taxmann.com 21 (Karnataka)- para 10).

22. The ld. D.R. relied on the order of the ld. CIT(A).

23. We have heard the rival submissions and perused the materials available on record. This issue came for consideration before the Hon'ble Karnataka High Court in the case of Principal CIT Vs. Tally Solutions Pvt. Ltd. (2021) 123 Taxmann.com 21 (Karnataka) wherein held as under:

> 9. "We have considered the submissions made by learned counsel for the parties and have perused the record. Before proceeding further, it is apposite to take note of relevant extract of section 40 of the Act, which is reproduced below for the facility of reference:
>
> Notwithstanding anything to the contrary in sections 30 to 38, the following amounts shall not be deducted in computing the income chargeable under the head" Profits and gains of business or profession", --

(a) in the case of any assessee--

** (ia) thirty per cent of any sum payable to a resident], on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction, has not been paid on or before the due date specified in sub-section (1) of section 139 :

> Provided that where in respect of any such sum, tax has been deducted in any subsequent year, or has been deducted during the previous year but paid after ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore the due date specified in sub-section (1) of section 139, thirty per cent of such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid :
>
> Provided further that where an assessee fails to deduct the whole or any part of the tax in accordance with the provisions of Chapter XVII-B on any such sum but is not deemed to be an assessee in default under the first proviso to sub-section (1) of section 201, then, for the purpose of this sub-clause, it shall be deemed that the assessee has deducted and paid the tax on such sum on the date of furnishing of return of income by the resident payee referred to in the said proviso.
>
> Explanation.--For the purposes of this sub-clause,--
>
> (i) ** ** **
>
> (vi) "royalty" shall have the same meaning as in Explanation 2 to clause (vi) of sub-section (1) of section 9;

10. Thus, from close scrutiny of section 40(a)(i) of the Act, it is axiomatic that an amount payable towards interest, royalty, fee for technical services or other sums chargeable under this Act shall' not be deducted while computing the income under the head profit and gain of business or profession on which tax is deductible at source; but such tax has not been deducted. The expression 'amount payable' which is otherwise an allowable deduction refers to the expenditure incurred for the purpose of business of the assessee and therefore, the said expenditure is a deductible claim. Thus, section 40 refers to the outgoing amount chargeable under this at and subject to TDS under Chapter XVII-B. The deduction under section 32 is not in respect of the amount paid or payable which s subjected to TDS; but is a statutory deduction on an asset which is otherwise eligible for deduction of depreciation. Section 40(a)(i) and (ia) of the Act provides for disallowance only in respect of expenditure, which is revenue in nature, therefore, the provision does not apply to a case of the assessee whose claim is for depreciation, which is not in the nature of expenditure but an allowance. The depreciation is not an outgoing expenditure and therefore, provisions of Section 40(a)(1) and (ia) of the Act are not applicable. In the absence of any requirement of law for making deduction of tax out of expenditure, which has been capitalized and no amount was claimed as revenue expenditure, no disallowance under section 40(a)(i) and (ia) of the Act would be made. It is also pertinent to note that depreciation is a statutory deduction available to the assessee on a asset,

which is wholly or partly owned by the assessee and used for business or profession. The depreciation is an allowance and not an expenditure, loss or trading liability. The Commissioner of Income Tax (Appeals) has held that the payment has been made by the assessee for an outright purchase of Intellectual Property Rights and not towards royalty and therefore, the provision of section 40(a)(ia) of the Act is not attracted in respect of a claim for depreciation. The aforesaid finding has rightly been affirmed by the tribunal. The findings recorded by the ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore Commissioner of Income Tax (Appeals) as well as the tribunal cannot be termed as perverse.

In view of preceding analysis, the substantial question of law framed by a bench of this court is answered against the revenue and in favour of the assessee.

In the result, the, appeals fail and are hereby dismissed."

23.1 Keeping in view of the above judgement, this ground of assessee is allowed on similar lines.

24. Ground No.6 raised by the assessee in ITA No.1980/Bang/2018 is with regard to disallowance of service fee paid to Symphony, Japan u/s 40(a)(ia) of the Act.

25. The ld. A.R. submitted that during the assessment year 2009- 10, the assessee made payment of Rs. 1,30,42,008/- to Symphony Services Japan, as consideration for software product development and other related services rendered by the said company to the assessee's clients located in Japan. The assessee did not deduct tax at source on the payment as the same was not applicable and claimed the payment made as a deduction.

25.1 The Assessing Officer made a disallowance under Section 40(a)(i) of the Act. Since the CIT(A) granted deduction on the enhanced profits under Section 10A of the Act pursuant to the disallowance made by the Assessing Officer, the CIT(A) did not adjudicate on the merits of the disallowance.

25.2 In this regard, the ld. A.R. submitted that the payments made are towards services rendered by Symphony Japan to the customers of the assessee in Japan, i.e. outside India. The ld. A.R. further submitted that the services rendered by the Japanese entity was utilized by the assessee for the purposes of earning income from a ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore source outside India, and therefore falling within the exception contained in Section 9(1)(vii)(b) of the Act.

He relied on the following Case laws:

- Director of Income Tax v. Lufthansa Cargo India (reported in [2015] 60 taxmann.com 187 (Delhi));

- PCIT v. Motif India Infotech (P.) Ltd. (reported in [2018] 409 ITR 178 (Guj.)); and

- Infosys Ltd. v. Deputy Director of Income Tax (Order dated 25.05.2016 passed by this Hon'ble Tribunal in IT(IT)A Nos. 2&3/Bang/2014).

26. The ld. D.R. relied on the order of the ld. CIT(A).

27. We have heard the rival submissions and perused the materials available on record. Similar issue came for consideration before the Hon'ble Gujarat High Court in the case of Principal CIT Vs. Motif India Infotech (P) Ltd. (2018 409 ITR 178 (Guj) wherein held as under:

> "In the case of GE India Technology Centre P. Limited v. CIT reported in [2010] 327 ITR 456 (SC), the ratio laid down by the Supreme Court was that mere remittance of money to a non-resident would not give rise to the requirement of deducting tax at source, unless such remittance contains wholly or partly taxable income. After the judgment was rendered, the Legislature amended section 195 of the Income-tax Act, 1961 by inserting Explanation 2 by the Finance Act, 2012, but with retrospective effect from April 1, 1962. The Explanation provides that for removal of doubts, it is clarified that the obligation to comply with sub-section (1) of section 195, and to make deduction as provided therein applies and shall be deemed to have always applied to all persons, resident or non- resident, whether or not the non-resident person has a residence or place of business or business connection in India ; or any other presence in any manner whatsoever in India. Mere requirement of permanent establishment in India was thus done away with. Nevertheless, the basic principle that requirement of deduction of tax at source would arise only in a case where the payment made to a non-resident was taxable, still remains.
>
> Sub-section (1) of section 9 lists situations under which the income shall be deemed to accrue or arise in India. Clause (vii) contained therein pertains to income by way of fees for technical services payable by the Government or a person who is a resident, or a person who is a non-resident under the circumstances specified therein. As per sub-clause ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore
>
> (b) the income by way of fees for technical services payable by a person who is a resident would be deemed to accrue or arise in India. However, this clause contains two Explanations, namely, where the fees are payable in respect of services utilized in a business or profession carried on by such person outside India, or for the purpose of making or earning any income from any source outside India. In other words, therefore, if the assessment of an assessee falls in either of these two clauses, the income by way of fees for technical services paid by the assessee would still not be covered within the deeming clause of sub-section (1) of section 9.

The assessee was a company engaged in software development. It provided software related services to its overseas clients. During the course of scrutiny assessment for the assessment year 2009-10, the Assessing Officer raised question of non-deduction of tax at source, while making payment of a

sum of Rs. 5.51 crores by the assessee towards fees for technical services to a foreign based company. The assessee argued that the payment received by the nonresident was not taxable and that therefore, there was no requirement for deducting tax at source while making such payment. The Assessing Officer, however disallowed the expenditure. The Commissioner (Appeals) held in favour of the assessee observing that there was no dispute that the services were in the nature of technical services, but would be covered under the Explanation clause contained in section 9(1)(vii)(b). This was upheld by the Tribunal. On appeal :

> Held, dismissing the appeal, that the Commissioner (Appeals) and the Tribunal had accepted the assessee's factual assertion that the payments were for technical services provided by a non-resident, for providing services to be utilized for serving the assessee's foreign clients. Clearly, the source of income namely the assessee's customers were the foreign based companies. Tax was not deductible on such payment."
>
> 27.1 In view of the above precedent, we are inclined to allow the ground taken by the assessee on similar lines.
>
> 28. Ground No.7 is common in all the three appeals and this ground of appeal of the assessee is with regard to reduction of expenses incurred in foreign currency from export turnover while computing deduction u/s 10A of the Act.
>
> 29. The ld. A.R. submitted that the assessee incurred expenses in foreign currency in the nature of travel, consultancy, franchise commission which are not in the nature of expenses which are to be ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore reduced in terms of Section 10A of the Act. Accordingly, the assessee did not reduce the expenses while computing the eligible deduction.
>
> 29.1 The Assessing Officer being of the view that the expenses were incurred to render technical services outside India, reduced the expenses from the export turnover. The CIT(A) directed reduction of the expenses both from the export turnover as well as the total turnover.
>
> 29.2 In this regard, the ld. A.R. submitted that no part of the expenditure in foreign currency was incurred towards performing technical services outside India, or for delivery of software outside India. The employees are required to travel overseas predominantly for business development, coordination, meetings and discussions with clients and not for rendering technical services outside India.

Therefore, the expenses are not liable to be excluded from export turnover.

He relied on the following Case laws:

- CIT v. Tata Elxsi Ltd. (reported in [2017] 80 taxmann.com 118 (Karnataka); and

- CIT v. Kshema Technologies Ltd. (reported in [2016] 66 taxmann.com 165 (Karnataka)

30. The ld. D.R. relied on the order of the ld. CIT(A).

31. We have heard the rival submissions and perused the materials available on record. In this regard, the contention of the assessee was rejected by the AO for the following reasons:

"The viewpoint of the assessee is not tenable in as much as, the definition of export turnover as provided in explanation 2 is in connection with "export turnover" appearing in sub section (4) of section 10A. Further, sub section (4) is a machinery provision in connection with implementation of substantive provision, i.e., sub section (1) of section ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore 10A by virtue of which the assessee is entitled to claim deduction in connection with the profits derived from the export of computer software. As such, the definition of "export turnover" provided in explanation 2 is wholly and exclusively for the purpose of computing deduction as 10A in terms of sub sections (1) and (4). In view of this, the phraseology, i.e., "incurred in foreign exchange in providing the technical services outside India", appearing in explanation 2 shall not be read, in isolation, but has to be linked to the substantive provisions, i.e. sub section (1). After considering the same, the meaning of "incurred in foreign exchange in providing the technical services outside India" would be translated to "incurred in foreign exchange in connection with the development and supply of computer software outside India". Accordingly, the assessee is required to exclude the expenditure incurred in foreign currency from the export turnover."

31.1 It is clear from the aforesaid observations of the AO in the order of assessment that he has not disputed the factual position that expenditure incurred in foreign currency was not for the purpose of verifying technical services outside India or for delivery of software outside India. The employees' travelled overseas predominantly for business development coordination, meetings and discussions with clients and not for rendering technical services outside India. The contention of the assessee in this regard is contained at pages 743 & 744 of the assessee's paper book, wherein the breakup of expenditure incurred in foreign currency have been given. The same are as follows:

The unit wise details of expenses incurred in foreign currency are as below:

(Amount in INR) Nature of Bangalore Mumbai Pune Total expenditure incurred in foreign currency Travel 49,600,269 3,301,404 34,408,518 87,310,191 Consultancy 685,000 -- -- 685,000 fees Franchise -- 9,714,805 -- 9,714,805 commission Others 6,131,588 -- 151,230 6,282,818 ITA Nos.1980 to 1982/Bang/2018 M/s. Harman

Connected Services Corporation India Pvt. Ltd., Bangalore 31.2 The definition of export turnover for the purpose of section 10A of the Act is given in explanation (2)(i)(b) to section 10A of the Act and the same reads as follows:

"the consideration in respect of export by the undertaking of articles or things or computer software received in or brought into India by the assessee in convertible foreign exchange in accordance with sub section 3 but does not include freight, telecommunication charges or insurance attributable to the delivery of the articles or things or computer software outside India or expenses if any incurred in foreign exchange in providing the technical services outside India"

31.3 The reading of the aforesaid definition makes it very clear that it is only expenses incurred in foreign exchange in providing technical services outside India that have to be excluded from export turnover. In this regard, the Ld. Counsel has placed reliance on the decision of the Hon'ble Karnataka High Court in the case of Kshema Technologies Ltd. (supra). The Hon'ble Karnataka High Court in the aforesaid decision held as follows:

'Export turnover' is defined under Explanation (2)(iv) to section 10A. The said export turnover as per Explanation (2)(iv) to section 10A means the consideration in respect of export by the undertaking of articles or things or computer software received in. or brought into, India by the assessee in convertible foreign exchange in accordance with sub-section (3), but does not include freight, telecommunication charges or insurance attributable to the delivery of the articles or things or computer software outside', India or expenses, if any, incurred in foreign exchange in providing the technical services outside India.

What is relevant to be noticed as per this provision is that the consideration in respect of export of computer software received in or brought into India by the assessee in convertible foreign exchange is an export turnover and what is excluded from this clause is (a) freight, (b) telecommunication charges or insurance attributable to the delivery of the articles or things or computer software outside India (c) expenses, if any, incurred in foreign exchange in providing the technical services outside India. Explanation (3) inserted by Finance Act, 2001 with effect from 1-4-2001 explains that the profits and gains derived from on site development of computer software including services for development of software, outside ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore India shall be deemed to be the profits and gains derived from the export of computer software outside India. Thus, it is clarified by the legislature by inserting Explanation (3) to section 10A that the profits and gains derived from on site development of computer software including services for the development of such software outside India is deemed to be the profits and gains derived from the export of computer software outside India. In other words, the services rendered by the assessee relating to the development of computer software is deemed to be part of export turnover of computer software outside India. [Para 13] An identical issue

relating to section 80HHE was considered by this court in the case of CIT v. Motor Industries Co. Ltd. [20151 55 taxmann.com 377 (Kar.) and this court has held that though the services rendered in deputing the software engineers abroad who among other things have to do testing, installation and monitoring of software supplied to the client, appears to be technical in nature, it does not fall within the clause of providing technical service outside India in connection with the development or production of computer software and, accordingly, such expenditure cannot be excluded in computing export turnover.

To decide the question on hand, the Tribunal has placed reliance on the judgment passed by the Tribunal in the case of CIT v. Mphasis Ltd. [IT.Appeal No. 1075 of 2008, dated 1-8-2014]. The very same judgment was subjected to judicial scrutiny before this court in ITA No. 1075/2008 connected with ITA No. 196/2009, wherein this court, following the judgment of Motor Industries Co. Ltd. (supra), answered the substantial question of law in favour of the assessee and against the revenue. This court has held that the expenditure incurred in the development or production of computer software though is in the nature of technical services, is not so, for the purposes of the Act and the said expenditure cannot be excluded in computing export turnover. Thus, the said judgment is squarely applicable to the facts of the present case. [Para 14] The Tribunal was correct in holding that expenses incurred in foreign currency for providing software development services outside should not be excluded from the export turnover for the purpose of computation of deduction under section 10A."

31.4 In the light of the aforesaid decision of the Hon'ble Karnataka High Court, we are of the view that the disputed sum cannot be reduced from the export turnover. We hold and direct accordingly and allow the relevant ground of appeal of the assessee.

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32. Ground No.8 raised only in ITA No.1980/Bang/2018 is with regard to denial of deduction u/s 10A of the Act of foreign exchange gain on restatement of balance in CPC account.

33. The ld. A.R. submitted that the assessee recognized net foreign exchange gain of Rs. 9,79,49,077/- on account of fluctuation of foreign currency in respect of the export proceeds. Of the above sum, an amount of Rs. 9,98,10,412/- pertains to realised foreign exchange gains, i.e. the gain arising on account of differences in the foreign exchange rates as on the date of realization of money into the EEFC account and the rate as on the date of withdrawal of the balances from such account or transfer of the same into current account. The remaining net gain is the unrealized foreign exchange gain on account of restatement of the balances lying in the EEFC account. The Assessing Officer denied the deduction claimed. The CIT(A) affirmed the denial of the deduction.

33.1 In this regard, the ld. A.R. submitted that the EEFC account maintained by the assessee is only for the purpose of receiving export proceeds. Hence, any gain/loss arising on account of the fluctuation of foreign currency, either on account of restatement or at the time of realization has a direct nexus with the export activities of the assessee and is derived from the export activities. Therefore, such gain is eligible for deduction under Section 10A of the Act.

He relied on the following Case laws:

> - CIT v. Hewlett Packard Global Soft Ltd. (reported in [2017] 87 taxmann.com 182 (Karnataka) (FB)- para 34-38; and
>
> - CIT v. Motorola India Electronics (P.) Ltd. (reported in [2014] 46 taxmann.com 167 (Karnataka)- para 8.
>
> ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore

34. The ld. D.R. relied on the order of the ld. CIT(A).

35. We have heard the rival submissions and perused the materials available on record. This issue came for consideration before the Hon'ble Karnataka High Court in the case of CIT Vs. Motorola India Electronics (P) Ltd. (2014) 46 taxmann.com 167. In the case of CIT Vs. Hewlett Packard Global Soft Ltd. (2017) 87 taxmann.com 182 (Karn.) the Hon'ble Karnataka High Court held as under:

> "Exemption under sections 10-A and 10-B encompasses the entire income derived from the business of export of such eligible undertakings including interest income derived from the temporary parking of funds by such undertakings in Banks or even Staff loans. The dedicated nature of business or their special geographical locations in STPI or SEZs. etc. makes them a special category of assessees entitled to the incentive in the form of 100 per cent deduction under sections 10-A or 10-B. The computation of income entitled to exemption under section 10-A or 10-B is done at the prior stage of computation of Income from profits and gains of business sections 28 to 44 under Part-D of Chapter IV before 'Gross Total Income' as under section 80-B(5) is computed and after which the consideration of deductions under Chapter VI-A in section 80HH etc. comes into picture. all profits and gains of the 100 percent EOU including the incidental income by of interest on bank deposits or staff loans would be entitled to 100 per exemption or deduction under section 10-A and 10-B. Such interest income arises ss the ordinary course of export business of the Undertaking even though not as a direct result of export but from the bank deposits etc., and is therefore eligible for 100 per cent deduction. [Para 35] The respondent assessee was entitled to 100 per cent exemption or deduction under section 10-A in respect of the interest income earned by it on the deposits made by it with the Banks in the ordinary course of its business and also interest earned by it from the staff loans and

> such interest income would 'not be taxable as 'Income from other Sources' under section
>
> 56. The incidental activity of parking of surplus Funds with the Banks or advancing of staff loans by such special category of assessees covered under section 10 A or 10 B was integral part of their export business-activity and a business decision taken in view of the commercial expediency and the interest income earned incidentally could not be de-linked from its profits and gains derived y the undertaking engaged in the export of articles as envisaged under section 10-B and could not be taxed separately under section 56. [Para 37]."

ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore 35.1 In view of the above judgement of jurisdictional High Court, we allow the ground taken by the assessee holding that it should be considered as part of export income. This ground of appeal of the assessee is allowed.

36. Ground No.9 raised by the assessee in ITA Nos.1980 & 1981/Bang/2018 is with regard to disallowance u/s 14A of the Act.

37. The ld. A.R. submitted that the Assessing Officer made a disallowance under Section 14A of the Act while computing the taxable income, without first issuing a show cause notice to the assessee or recording any reasons. The CIT(A) affirmed the disallowance.

37.1 In this regard, the ld. A.R. submitted that it is a settled position that to invoke the provisions of Section 14A of the Act, at the threshold, the Assessing Officer ought to record his dissatisfaction as to the correctness of the claim of the assessee, having regard to the books of accounts. In the present case, no such satisfaction is recorded by the Assessing Officer, and therefore the disallowance is liable to be set aside.

- He relied on the following Case laws:

> - Godrej & Boyce Manufacturing Company Ltd. v. DCIT (reported in [2017] 81 taxmann.com 111 (SC)- para 37;
>
> - Hindustan Aeronautics Ltd. v. ACIT (reported in [2021] 125 taxmann.com 80 (Karnataka)- para 12; and
>
> - Eicher Motors Ltd. v. CIT (reported in [2017] 86 taxmann.com 49 (Delhi)- para 13.

38. The ld. D.R. relied on the order of the ld. CIT(A).

39. We have heard the rival submissions and perused the materials available on record. The main objection of the ld. A.R. is ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore that the AO has not recorded the satisfaction before invoking

the provisions u/s 14A of the Act. In our opinion, the question of recording satisfaction u/s 14A of the Act r.w. Rule 8D of the IT Rules does not arise as the assessee has not disallowed any amount u/s 14A of the Act r.w. Rule 8D of the IT Rules. In our opinion, when assessee itself disallowed the deduction u/s 14A of the Act r.w. Rule 8D, the A.O. suo-motu cannot disallow the same and tinker the disallowance made by assessee without recording the satisfaction for such action for invoking the provisions of section 14A of the Act r.w. Rule 8D of the Rules. With regard to disallowance u/s 14A of the Act r.w. Rule 8D of the Rules, the contention of the ld. A.R. is that the AO has not given proper opportunity of hearing to the assessee before making such disallowances. Hence, in our opinion, this issue requires re-examination by the AO for examining the applicability of section 14A of the Act r.w. Rule 8D(i), (ii) & (iii) of the Rules and accordingly this issue is remitted back to the file of AO for fresh consideration after hearing opportunity of hearing to the assessee.

40. Ground No.10 raised by the assessee only in ITA No.1980/Bang/2018 is with regard to levy of interest u/s 234B of the Act.

41. The ld. A.R. submitted that the Assessing Officer erred in levying interest u/s 234B of the Act.

42. The ld. D.R. relied on the order of the ld. CIT(A).

43. We have heard the rival submissions and perused the materials available on record. After hearing both the parties, we remit this issue to the file of AO to recompute the interest u/s 234B of the Act in accordance with law. This ground is allowed for statistical purposes.

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44. Ground No.11 raised by the assessee only in ITA No.1980/Bang/2018 is with regard to levy of interest u/s 234C of the Act.

45. The ld. A.R. submitted that the Assessing Officer erred in computing interest under Section 234C of the Act on assessed income instead of returned income. While this error was rectified in the subsequent assessment year by the CIT(A), in the assessment year 2009-10 the CIT(A) rejected the assessee's claim. He submitted that in terms of Section 234C of the Act, the interest, if at all, can be levied only on the returned income and not assessed income.

46. The ld. D.R. relied on the order of the ld. CIT(A).

47. We have heard the rival submissions and perused the materials available on record. We direct the AO to recompute the interest u/s 234C of the Act on assessed income only. This ground is partly allowed. Directed accordingly.

48. Ground No.12 raised by the assessee only in ITA No.1981/Bang/2018 is with regard to disallowance of legal and professional charges u/s 40A of the Act.

49. The ld. A.R. submitted that during the year under consideration, the assessee incurred an amount of Rs. 4,45,29,047/- towards legal and professional expenses. During the course of the assessment proceedings, the assessee inadvertently failed to furnish the relevant details, and therefore the Officer made a disallowance of Rs. 70,73,657/-.

49.1 The ld. A.R. further submitted that while the assessee furnished the relevant details before the CIT(A), the CIT(A) failed to ITA Nos.1980 to 1982/Bang/2018 M/s. Harman Connected Services Corporation India Pvt. Ltd., Bangalore adjudicate on this issue on merits. In view of the above, the ld. A.R. submitted that the disallowance made may be deleted.

50. The ld. D.R. relied on the order of the ld. CIT(A).

51. We have heard the rival submissions and perused the materials available on record. We remit this issue to the file of AO to produce the necessary evidences in support of claim of expenditure. The AO shall re-examine the same in accordance with law. This ground is partly allowed for statistical purposes.

52. Ground No.13 raised by the assessee only in ITA No.1980/Bang/2018 is with regard to restriction of depreciation on networking equipment.

53. The ld. A.R. submitted that the assessee capitalized computer servers and accessories of Rs. 13,02,505/- under the 60% depreciation block "computer and software", and claimed depreciation at the rate of 30%. The Assessing Officer treated the servers and accessories as 'plant and machinery' and granted deprecation at the rate of 15%. The ld. CIT(A) failed to adjudicate the ground on merits.

53.1 The ld. A.R. submitted that this issue is covered in favour of the assessee by the order of the CIT(A) passed for the assessment year 2012-13 and the order of the Tribunal for assessment year 2014-15 (IT(TP)A No. 3401/Bang/2018) and assessment year 2015- 16 (IT(TP)A No. 2243/Bang/2019). Moreover, this issue is also covered in favour of the assessee by the decision of the Hon'ble High Court of Karnataka in Mphasis (supra). Therefore, the ld. A.R. submitted that this ground ought to be allowed.

54. The ld. D.R. relied on the order of the ld. CIT(A).

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55. We have heard the rival submissions and perused the materials available on record. After hearing both the parties, we are of the opinion that this issue came for consideration in the case of Principal CIT Vs. Mphasis Ltd. [2021] 128 taxmann.com 138 wherein the Hon'ble Karnataka High Court has held as under:

"11. Heard the learned counsel for the parties at length and perused the record. In respect of the first substantial question of law, the judgment delivered by the Delhi High Court in the case of BSES Yamuna Powers Ltd. (supra) has concluded the controversy. The Delhi High Court in paragraphs 5 and 6 of the aforesaid judgment has held as under:--

'5. However, upon a perusal of the file, we find that the higher rate of depreciation was allowed both by the Commissioner of Income-tax (Appeals) ("CIT(A)") and the Tribunal. In fact, the Tribunal in its impugned order has observed as under :--

"The issue involved in this appeal is covered by the decision of Coordinate Bench of the Tribunal as discussed below:-

In the case of ITO v. Samiran Majumdar f20061 98 ITD 119 (Kol.), Income- tax Appellate Tribunal, Kolkata Bench "B", has taken a view that the printer and scanner are integral part of the computer system and are to be treated as computer for the purpose of allowing higher rate of depreciation, i.e., 60%. 3.2 The Income-tax Appellate Tribunal, Delhi "F" Bench in the case of Expeditors International (India) (P. Ltd. v. CIT reported in [2008] 118 TTJ 652 (Delhi) has held that peripherals such as printer, scanners, NT Server, etc. form integral part of the computer and the same, therefore, are eligible for depreciation at the rate of 60% as applicable to a computer.

4. Respectfully following the aforesaid decisions of the Coordinate Bench, we uphold the order of the learned Commissioner of Income-tax (Appeals) in allowing the depreciation at 60% on computer peripherals and accessories, and, thus, the ground raised by the revenue is rejected.

5. In the result, the appeal filed by the revenue is dismissed."

6. We are in agreement with the view of the Tribunal that computer accessories and peripherals such as, printers, scanners and server etc. form an integral part of the computer system. In fact, the computer accessories and peripherals cannot be used without the computer. Consequently, as they are the part of the computer system, they are entitled to depreciation at the higher rate of 60%.

12. The Delhi High Court has held that the computer accessories and peripherals such as printers, scanners and server etc., form an integral part of the computer system.

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13. In light of aforesaid judgment, it can be safely held that the switches and routers as they cannot be used without computer, they form part of peripherals of the computer and entitled to 'depreciation at 60%. The revenue has not been able to controvert the said finding of the Tribunal

and therefore, in light of the judgment delivered by the Delhi High Court, the first substantial question of law is answered in favour of the assessee and against the revenue." 55.1 In view of the above judgement, this ground of assessee is allowed on similar lines.

56. In the result, all the appeals filed by the assessee are partly allowed for statistical purposes.

Order pronounced in the open court on 12th Jan, 2023.

| | |
|---|---|
| Sd/- | Sd/- |
| (N.V. Vasudevan) | (Chandra Poojari) |
| Vice President | Accountant Member |

Bangalore,
Dated 12th Jan, 2023.
VG/SPS
Copy to:

1. The Applicant
2. The Respondent
3. The CIT
4. The CIT(A)
5. The DR, ITAT, Bangalore.
6. Guard file

By order

Asst. Registrar, ITAT, Bangalore.