

## IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

## TAX APPEAL NO. 131 of 2013

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COMMISSIONER OF INCOME TAX III....Appellant(s)

Versus

PANCHMAHAL STEEL LTD....Opponent(s)

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Appearance:

MR KM PARIKH, ADVOCATE for the Appellant(s) No. 1

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CORAM: **HONOURABLE MR.JUSTICE AKIL KURESHI**

and

**HONOURABLE MS JUSTICE SONIA GOKANI**

Date : 28/03/2013

## ORAL ORDER

(PER : HONOURABLE MR.JUSTICE AKIL KURESHI)

1. Revenue is in appeal against the judgement of the Income Tax Appellate Tribunal dated 13.7.2012 raising following questions for our consideration :

"Whether, the Tribunal erred in deleting disallowance of Rs.34,88,834/- made on account of loss claimed due to cancellation of forward contract thereby overlooking the fact that transactions in question fell within the definition of speculative transaction as per section 43(5) of the Income Tax Act?

2. Tribunal in the impugned judgement relied on its own decision in case of **Friends and friends Shipping Pvt. Ltd.** which was carried in appeal

before this Court. This Court had also by judgement 23.8.2011 in Tax Appeal No.251/2010 upheld the decision of the Tribunal. In the said judgement, this Court had made following observations :

"Having thus heard the learned advocates for the parties and having perused the documents on record, we find that the issue is covered by the decisions of the Bombay High Court in the case of Badridas Gaurida (P) Ltd. and the Calcutta High Court in the case of Soorajmull Nagarmull (supra).

In the decision of the Bombay High Court, the assessee was in the business of export of cotton. The assessee had entered into forward contract with banks in respect of foreign exchange. Some of these contracts could not be honoured for which the assessee had to pay Rs.13.50 lacs which was debited to the profit and loss account. The assessee claimed the sum as business loss. Revenue was of the opinion that the loss was speculative in nature. Bombay High Court following the decision of the Calcutta High Court in the case of Soorajmull Nagarmull (supra) held that the expenditure would not be covered under section 43(5) of the Act as speculative transaction. It was observed as under:

"The assessee was not a dealer in foreign exchange. The assessee was a cotton exporter. The assessee was an export house. Therefore, foreign exchange contracts were booked only as incidental to the assessee's regular course of business. The Tribunal has recorded a categorical finding to this effect in its order. The Assessing Officer has not considered these facts. Under section 43(5) of the Income-tax Act, "speculative transaction" has been defined to mean a transaction in which a contract for the purchase or sale of commodity is settled otherwise than by the actual delivery or transfer

of such commodity. However, as state above, the assessee was not a dealer in foreign exchange. The assessee was an exporter of cotton. In order to hedge against losses, the assessee had booked foreign exchange in the forward market with the bank. However, the export contracts entered into by the assessee for export of cotton in some cases failed. In the circumstances, the assessee was entitled to claim deduction in respect of Rs.13.50 lakhs as a business loss. This matter is squarely covered by the judgment of the Calcutta High Court, with which we agree, in the case of CIT v. Soorajmull Nagurmull (1981) 129 ITR 169."

Before the Calcutta High Court, the assessee was a firm engaged in the business of import and export of jute. In course of business, the assessee would enter into forward contract in foreign exchange in order to cover the loss which may arise due to difference in foreign exchange valuation. In one such contract, the assessee had to pay to the Bank difference of Rs.80,491/- which was claimed by the assessee as revenue expenditure. The Assessing Officer disallowed the claim. The High Court held that the assessee was not a dealer in foreign exchange and the foreign exchanges were only incidental to the assessee's regular course of business and the loss was thus not a speculative loss but incidental to the assessee's business and allowable as such. Facts in the present case are very similar. Admittedly, the assessee is not a dealer in foreign exchange. For the purpose of hedging the loss due to fluctuation in foreign exchange while implementing the export contracts, the assessee had entered into forward contract with the banks. In some cases, the export could not be executed and the assessee had to pay certain charges to the Bank and thereby incurred certain expenses. These expenses the assessee claimed by way of expenditure towards business. We do not find that the transaction can be stated to be in speculation as to cover under sub-section (5) of section 43 of the Act.

It is true that the CIT(Appeals) has made some observations which would prima facie suggest that there was no direct co-relation between the exchange document and the precise export contract. However, such observations cannot be seen in isolation. CIT(Appeals) himself has noted that the assessee had entered into seven separate contracts with the bankers. In the case of **M.G.Brothers** (supra), the Andhra Pradesh High Court was concerned with a case where the assessee was carrying on business of groundnut oil and the assessee entered into forward transactions in neem oil and cotton seed oil. In that view of the matter, the Court held that it was not a hedging transaction since there was no evidence that the assessee had adequate stock of raw materials to the extent of hedging transactions.

In the case of Joseph John (supra), the Apex Court observed that the burden of proof is upon the assessee to show that the transaction is not speculative transaction but a hedging transaction and further that the finding of the Tribunal that the transaction carried out by the assessee is speculative in nature and not hedging transactions is essentially a finding on a question of fact.

The above noted decisions do not directly touch the controversy arising in the present appeal. We find that the decisions of the Bombay High Court and the Calcutta High Court noted above would cover the situation.

Tax appeal is therefore dismissed."

3. Learned counsel for the Revenue stated that said decision of this Court was not carried in appeal on the ground that it involved tax effect lower than what is prescribed by the CBDT in circular dated 9.2.2011 permitting the Revenue to carry such appeal before the Supreme Court. Counsel for

the Revenue was unable to point out any factual distinction between the two cases.

4. Be that as it may, insofar as this Court is concerned, above decision is binding. In the result, this tax appeal is also dismissed

(AKIL KURESHI, J.)

(MS SONIA GOKANI, J.)

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## IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

TAX APPEAL No. 251 of 2010

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COMMISSIONER OF INCOME TAX-I - Appellant(s)

Versus

FRIENDS AND FRIENDS SHIPPING PVT LTD - Opponent(s)

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## Appearance :

MRS MAUNA M BHATT for Appellant(s) : 1,  
MR KIRTIKANT THAKER for Opponent(s) : 1,  
MR PRAVIN P PANCHAL for Opponent(s) : 1,

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CORAM : HONOURABLE MR.JUSTICE AKIL KURESHI

and

HONOURABLE MS JUSTICE SONIA GOKANI

Date : 23/08/2011

## ORAL ORDER

(Per : HONOURABLE MR.JUSTICE AKIL KURESHI)

Revenue is in appeal against the judgment of the Tribunal dated 29.5.2009 raising following questions for our consideration :

*"Whether the Appellate Tribunal is right in law and on facts in reversing the order passed by CIT(A) and thereby deleting the disallowance of Rs.15,04,910/- made on account of Foreign Exchange Difference ?"*

From the record, it emerges that the assessee who is an exporter had entered into forward contracts with the Bankers to hedge against any loss arising out of fluctuation in foreign currency. From the order passed by the CIT(A), we gather that the contract



between the assessee and the bank provided that the assessee would buy some quantity of dollars at a particular rate to cover export bill payment. The contract gave delivery option dates. The assessee had to take the delivery within the period indicated in the contract and if for some reason it was not possible to do so, the assessee had to give instructions to the Bank for cancellation of the contract. Since on some occasions, the assessee was required to give instructions for cancellation of forward contract, the assessee had to pay agreed charges to the Bank. In the process the assessee suffered loss of Rs.15 lacs. The Assessing Officer disallowed the loss holding it as speculative in nature and therefore covered under sub-section (5) of section 43 of the Act. In further appeal, CIT(A) confirmed the order of the Assessing Officer relying on the decision of the Andhra Pradesh High Court in the case of **M.G.Brothers v. CIT**, (1985) 154 ITR 695 and also in the case of **Commissioner of Income Tax v. Joseph John**, 67 ITR 74. On further appeal, the Tribunal deleted the disallowance relying on the decision of the Bombay High Court in the case of **CIT v. Badridas Gauridu (P) Ltd.**, 261 ITR 256. We may notice that the Bombay High Court in the said decision had relied on a decision of the Calcutta High Court in the case of **CIT v. Soorajmull Nagarmull**, 129 ITR 169 (Cal.)

Counsel for the Revenue vehemently contended that the Assessing Officer as well as the CIT (Appeals) had examined the issue threadbare. It was found that

there was no direct connection between the export contract and the booking of dollars by the assessee. The entire transaction was thus in the nature of speculation.

On the other hand, learned counsel Shri Thaker appearing on behalf of the assessee contended that the issue is squarely covered by the decision of the Bombay High Court in the case of Badridas Gauridu (P) Ltd. (supra). The assessee is admittedly not a dealer in foreign exchange. The charges that the assessee had to pay to the Bank were in the nature of revenue expenditure in the course of business. Counsel further submitted that the Reserve Bank of India's guidelines would not permit the Bank to enter into a forward contract with respect to foreign currency unless the assessee had export contract on hand.

Having thus heard the learned advocates for the parties and having perused the documents on record, we find that the issue is covered by the decisions of the Bombay High Court in the case of Badridas Gaurida (P) Ltd. and the Calcutta High Court in the case of Soorajmull Nagarmull (supra).

In the decision of the Bombay High Court, the assessee was in the business of export of cotton. The assessee had entered into forward contract with banks in respect of foreign exchange. Some of these contracts could not be honoured for which the assessee had to pay Rs.13.50 lacs which was debited



to the profit and loss account. The assessee claimed the sum as business loss. Revenue was of the opinion that the loss was speculative in nature. Bombay High Court following the decision of the Calcutta High Court in the case of Soorajmull Nagarmull (supra) held that the expenditure would not be covered under section 43(5) of the Act as speculative transaction. It was observed as under:

"The assessee was not a dealer in foreign exchange. The assessee was a cotton exporter. The assessee was an export house. Therefore, foreign exchange contracts were booked only as incidental to the assessee's regular course of business. The Tribunal has recorded a categorical finding to this effect in its order. The Assessing Officer has not considered these facts. Under section 43(5) of the Income-tax Act, "speculative transaction" has been defined to mean a transaction in which a contract for the purchase or sale of commodity is settled otherwise than by the actual delivery or transfer of such commodity. However, as state above, the assessee was not a dealer in foreign exchange. The assessee was an exporter of cotton. In order to hedge against losses, the assessee had booked foreign exchange in the forward market with the bank. However, the export contracts entered into by the assessee for export of cotton in some caes failed. In the circumstances, the assessee was entitled to claim deduction in respect of Rs.13.50 lakhs as a business loss. This matter is squarely covered by the jdugment of the Calcutta High Court, with which we agree, in thecase of CIT v.Soorajmull Nagurmull(1981) 129 ITR 169."

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order to cover the loss which may arise due to difference in foreign exchange valuation. In one such contract, the assessee had to pay to the Bank difference of Rs.80,491/- which was claimed by the assessee as revenue expenditure. The Assessing Officer disallowed the claim. The High Court held that the assessee was not a dealer in foreign exchange and the foreign exchanges were only incidental to the assessee's regular course of business and the loss was thus not a speculative loss but incidental to the assessee's business and allowable as such. Facts in the present case are very similar. Admittedly, the assessee is not a dealer in foreign exchange. For the purpose of hedging the loss due to fluctuation in foreign exchange while implementing the export contracts, the assessee had entered into forward contract with the banks. In some cases, the export could not be executed and the assessee had to pay certain charges to the Bank and thereby incurred certain expenses. These expenses the assessee claimed by way of expenditure towards business. We do not find that the transaction can be stated to be in speculation as to cover under sub-section (5) of section 43 of the Act.

It is true that the CIT(Appeals) has made some observations which would prima facie suggest that there was no direct co-relation between the exchange document and the precise export contract. However, such observations cannot be seen in isolation. CIT(Appeals) himself has noted that the assessee had

entered into seven separate contracts with the bankers. In the case of **M.G.Brothers** (supra), the Andhra Pradesh High Court was concerned with a case where the assessee was carrying on business of groundnut oil and the assessee entered into forward transactions in neem oil and cotton seed oil. In that view of the matter, the Court held that it was not a hedging transaction since there was no evidence that the assessee had adequate stock of raw materials to the extent of hedging transactions.

In the case of Joseph John (supra), the Apex Court observed that the burden of proof is upon the assessee to show that the transaction is not speculative transaction but a hedging transaction and further that the finding of the Tribunal that the transaction carried out by the assessee is speculative in nature and not hedging transactions is essentially a finding on a question of fact.

The above noted decisions do not directly touch the controversy arising in the present appeal. We find that the decisions of the Bombay High Court and the Calcutta High Court noted above would cover the situation.

Tax appeal is therefore dismissed.

(Akil Kureshi J.)

(Ms.Sonia Gokani, J.)

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