INCOME TAX APPELLATE TRIBUNAL
DELHI BENCH "B": NEW DELHI

BEFORE SHRI K. NARASIMHA CHARY, JUDICIAL MEMBER
AND
SHRI B.R.R. KUMAR, ACCOUNTANT MEMBER

I.T.A No. 4603/Del/2019
Assessment Year: 2012-13

Emmsons International Ltd. 101, South Delhi House, 12, Zamrudpur Community Centre, Kailash Colony, New Delhi. PAN: AAACE0442K (Appellant)	Vs.	ACIT, Circle -8(1), New Delhi. (Respondent)

Revenue by : Ms Ashima Neb, Sr. DR
Assessee by: Sh. Suresh Kumar Gupta, CA

Date of Hearing 12.09.2019
Date of pronouncement 14.10.2019

O R D E R

PER K. NARASIMHA CHARY, JM

Aggrieved by the order dated 12.04.2019 in Appeal No.15/18-19 passed by the learned Commissioner of Income-tax (A)-34, New Delhi {for short "ld.CIT (A)"), assessee preferred this appeal.

2. The appellant is company engaged in the business of international trading in commodities. For the Assessment Year 2012-13, it filed its return of income on 29/11/2012 declaring net taxable income of Rs.15,90,64,090/-. During the financial year relevant for the assessment

year 2012-13, the Export turnover of the appellant is USD 256 Million equivalent to Rs.1,282 Crore. The appellant had the practice of hedging substantial part of its foreign currency losses through forward contracts in foreign exchange. The forward cover was USD 122 million which is less than the 50% of the Export Turnover. The appellant has not indulged in any foreign currency speculation in stock exchanges or in other alternative forums. The appellant had suffered total loss of Rs.29,89,56,796/- foreign exchange fluctuation loss out of which there was loss of Rs.8,95,40,121/- on account of MTM losses in accordance with AS-11 on the foreign exchange forward contracts. It was also pointed out that in the preceding two years there had been gain from forward contracts which have been offered to tax which is evident from forward contact gains of Rs.71,58,43,411/-and Rs.3,74,90,231/- offered for tax in AY 2010-11 and AY 2011-12 respectively. There was also income of Rs.8,50,89,012/- and Rs.3,97,70,567/- for AY 2010-11 and AY 2011-12 respectively offered for tax in AY 2010-11 and AY 2011-12 respectively on account of application of AS-11 on the pending forward contracts as on close of financial years. During assessment proceeding, assessee relied on the decision of the Hon'ble Apex Court in the case of CIT vs Woodward Governor India Ltd 312 ITR 254 (SC) to support the contention as to the allowability of the foreign exchange loss. Ld. AO rejected the contention of the appellant on the ground that the issue of loss from foreign exchange forward contracts was not considered by the Court in the above judgment.

3. Ld. AO treated the above losses on forward contracts as notional and contingent in nature and thus not allowed. Ld. AO, however,

disallowed the loss of Rs.8,95,40,121/- relying on the CBDT instruction No.03/2010 dt: 23.03.2010. Ld. AO was of the view that since CBDT instruction dt: 23.03.2010 came after the judgment of Apex Court, the above CBDT instruction was takes preference to the judgment of Hon'ble Apex Court to disallow the claim of loss.

4. Further, Ld. Assessing Officer allowed the foreign travel expenses of the Directors of the assessee-company but has rejected the foreign travel expenses of their wife's and minor son observing that the foreign travel of the directors of the assessee was for business purpose, but the foreign travel of their family members accompanying the directors was not for business purposes.

5. Learned Assessing Officer, therefore, made an addition of Rs.8,95,40,121/- on account of MTM losses on account of foreign exchange fluctuation and Rs.17,09,423/- on account of disallowance of foreign travel expenses incurred in respect of the family members of the directors. Learned Assessing Officer also made an addition of Rs. 83,967/-on account of cessation of liability.

6. Challenging the assessment order making these additions, assessee preferred an appeal before the Ld. CIT(A). Ld. CIT(A) by way of impugned order, by placing reliance on CBDT instruction dated 23.03.2010, held that that where companies make adjustment through trading and P&L account by valuing financial instruments at market rate, such adjustments give rise to notional loss as no sales/conclusion/settlement of contract had taken place. According to the Ld. CIT(A) also, the decision of the Hon'ble Apex Court in Woodward

Governor (supra) was out of context of Forward Contracts/Derivatives and, therefore, CBDT instruction was relied to confirm disallowance of loss. Ld. CIT(A) did not find the mandatory compliance of AS-11, a relevant reason to allow the loss. Ld. CIT(A) also confirmed the addition made on account of foreign travel of the family members of the directors of the assessee company, observing that the assessee failed to justify the foreign travelling expenses incurred for travelling family members of the directors and other persons who are not employees of the company. Ld. CIT(A), however, deleted the addition of Rs.83, 967/-made on account of cessation of liability.

7. Aggrieved by the impugned order sustaining the additions on the aspect of MTM losses on forward contract and foreign travel expenses, assessee preferred this appeal. Insofar as the first ground is concerned, it is the contention of the Ld. AR that the authorities ignored the fact that the loss claimed on forward contracts is allowable and the same has been upheld by various judicial authorities and, therefore, the Revenue is not justified in treating the loss claimed on forward contracts as notional loss and not allowable under the provisions of income tax. He placed reliance on the decision reported in CIT *vs Woodward Governor P Ltd (supra), ONGC vs CIT* 322 ITR 180 (SC), Silicon Graphics Systems (India) Pvt Ltd vs DCITin ITA No.2976/Del/2013 dt: 24.08.2016, CIT vs D Chetan & Co.ITA No. 278 of 2014 dt: 01.10.2016, PCIT vs International Gold Company Ltd.,ITA No. 1827 of 2016 dt: 27.02.2019, DCIT vs HCL Comnet Ltd.,ITA No.4809/Del/2016 dt: 06.06.2019 etc.

8. Per contra, Ld. DR argued that in view of CBDT instructions, the findings of the authorities below are justified and MTM losses on

account of forward contract/derivatives are not allowable and in the marked to market methodology financial instruments are valued at market rate so as to report their actual value on the reporting date; and that where companies make such adjustment through the trading or profit and loss account, they book loss in their accounts and such loss is notional loss as no sale had actually taken place and the assets continue to be owned and possessed by the company. While referring to the findings of the Ld. CIT(A) in the impugned order, she submitted that in cases where no sale of settlement had actually taken place and the loss on marked to market basis has resulted in reduction of book profit, such notional loss would be contingent in nature and cannot be allowed to be set off against the taxable income. She also heavily relied upon the observations of the Ld. CIT(A) that the assessee had also claimed forward contract forex loss on the basis of Marked to market methodology adopted for various contracts for forward loss of foreign currency which it was expecting from exports proceeds made by it and it affects change in foreign exchange rates on all assets receivable/payable in foreign currency and, therefore, was claimed by the assessee is notional loss and cannot be allowed as expense. She also submitted that the CBDT had issued the instructions after the decision of the Hon'ble Apex Court in the case of Woodward Governor of India Ltd (supra).

9. We have gone through the record. In this case, the pending forward contracts were restated on the basis of the foreign exchange rate, and since there is no dispute as to the details of forward contract booked up to 31.03.2012 and gain/loss thereon, furnished by the assessee, all the losses are the losses booked by the assessee in

compliance of mandatory accounting standard AS -11. It is also not in dispute that in the preceding two years there had been gain from forward contracts which have been offered to tax which is evident from forward contact gains of Rs.71,58,43,411/- and Rs.3,74,90,231/- offered for tax in AY 2010-11 and AY 2011-12 respectively; and that there were also income of Rs.8,50,89,012/- and Rs.3,97,70,567/- for AY 11 and AY 2011-12 respectively offered for tax in AY 2010-11 and AY 11-12 respectively on account of application of AS-11 on the pending forward contracts as on close of financial years.

10. In CIT vs Woodward Governor P Ltd (supra) it is held that the exchange differences on foreign currency transactions in compliance of AS-11 need be considered in the accounts and the losses and profit arising therefrom need to be recognized as such for Income Tax purposes. It is further held that when the Revenue taxed the gains which accrued to the assessee on the basis of accrual and it is only in the year in question when the dollar rate stood increased, resulting in loss that the Revenue has disallowed the deduction/debt, which amounts to double standards adopted by the department. In the absence of any finding of Ld. AO as to the completeness and correctness of the accounts and also on want of compliance of accounting standards, it was held that the loss suffered by the assessee on account of exchange difference as on date of balance sheet is item of expenditure u/s 37(1) of IT Act.

11. In ONGC vs CIT 322 ITR 180 (SC) also, Hon'ble Apex Court took a similar view and held that loss on account of foreign exchange fluctuation on balance sheet date is item of expenditure u/s 37(1) of IT Act notwithstanding that liability had not been discharged in which

fluctuation in the rate of foreign exchange occurred. This view is followed by the Bombay High Court in the case of CIT vs D Chetan & Co.,ITA No. 278 of 2014 dt: 01.10.2016 and PCIT vs International Gold Company Ltd.,ITA No. 1827 of 2016 dt: 27.02.2019 wherein it was held that loss on forward contracts is not a notional loss and therefore need be allowed. In this case, it is the contention of the department that such loss is a notional loss was decided against the department on the ground that in case of export and import business hedging of risk in foreign exchange is a normal course of business activity and such loss need to be allowed.

12. In PCIT vs International Gold Company ltd. (supra),the question that had fallen for consideration was whether the loss from foreign exchange contract is a notional or contingent in nature. Hon'ble Bombay High Court referred to instruction No.03/2010 dt: 23.03.2010 to confirm that such loss is business loss allowable under the Act and held that CBDT circular/instruction has no applicability.

13. On a careful consideration of the facts involved in this case, we are of the considered opinion that the decision in the case of *Woodward Governor P Ltd* (supra) and ONGC vs CIT (supra) are applicable, and the line of judicial view is that the Revenue cannot be permitted to contend that there is a CBDT instruction No. 03/2010 dated 23/3/2010 to the contrary. No CBDT circular or instruction can be contrary to the decision of the Hon'ble Apex Court, even subsequent to the decision of the Hon'ble Apex Court. We, therefore, accept the contention of the assessee and hold that the addition is unsustainable. We, accordingly, direct the Assessing Officer to delete the same.

14. Now coming to the addition of Rs. 17,09,423/- on account of disallowance of foreign travelling expense, during the assessment proceedings, learned Assessing Officer noticed that the assessee had claimed foreign travel (others) to the extent of Rs.91,76,602/-, apart from the expenses on account of foreign travel (directors) expenses of Rs.41,52,414/-. Learned Assessing Officer further noticed that most of these expenses were incurred either in respect of family members/relatives of the directors such as Mr/MsManya Monga, Samay Monga, Rashi Monga, Punam Monga, Renu Monga, master Shiraj Monga, master Tej Monga etc or in respect of persons, who are neither family members of directors nor employees of the assessee company. On a verification of the details furnished by the assessee, learned Assessing Officer did not find any justification in respect of the expenses incurred in respect of certain family members of the directors and disallowed a sum of Rs.17,09,423/- on the ground that no satisfactory explanations have been given by the assessee with regard to the expenses of 16 persons named in paragraph No. 3.3 of the order.

15. It is contended on behalf of the assessee that the foreign travel expenses in respect of the wife and minor children of the directors was wholly and exclusively incurred for the business of the assessee and if at all the Revenue feels, it has to be brought to tax in the hands of the beneficiary director as perquisite. Assessee vide letter dated 21.12.2015 submitted that the directors of the assessee company during their foreign business trips were accompanied by their family members and no isolated trips were made by the family members of the directors of the assessee company. According to the assessee, the trips of the family

members are made to accompany directors of the assessee company during their business trips. Therefore, such expenses are ought to be allowed under 37(1) of the Act.

16. Ld. AR further submitted that the statement showing detail of foreign travel related to family members of directors and others are placed in paper book**.** In case cited by Ld. AO in para 3.3. of the impugned order, most of the family members are either wives of the directors/employees or their minor son. According to him, in order that expenditure should qualify for deduction as contemplated by section 37(1) of the Act, one of the requirements of the provision is that the expenditure must have been laid out wholly and exclusively for the purpose of business. Hence, it is for the assessee who claims deduction of the expenditure under sub-section to satisfy the department of the purpose for which the amount was spent. In view of the provisions of section 40A(2) of the Act, so far as a company is concerned, it is open to the taxing authorities to go into the reasonableness of the expenses also.

17. He submitted that the Assessing Officer is also entitled to be satisfied as to the commercial necessity of spending that amount. In other words, there must be nexus between the expenditure and the business purpose; that the capacity in which the assessee spends will also be relevant; that the purpose must be for the purpose of business, i.e., the expenditure must be incurred for carrying on of the business and the assessee should have incurred it in his capacity as a person carrying on the business; that the term 'wholly' refers to the quantum of the expenditure and 'exclusively' refers to the motive, objective and purpose of the expenditure; and that the true test of an expenditure laid out

wholly and exclusively for the purposes of trade or business is that it is incurred by the assessee as incidental to his trade for the purpose of keeping the trade going and making it pay and not in any other capacity than that of a trader. He placed reliance on decision reported in CIT v. Alfa Laval (I) Ltd 282 ITR 445 (Bom).

18. It is further submitted by the Ld. AR that when the Board of Directors of the assessee had thought it fit to spend on the foreign tour of the accompanying wife of the Managing Director for commercial expediency, it was not within the province of the Income-tax Authority to disallow such expenditure by sitting over the decision of the Board, in the absence of any specific bar created by the Statute for such expenditure. In support of this contention he placed reliance on addition of the Hon'ble Calcutta High Court in the case of J.K. Industries Ltd. Vs CIT,ITA No.624 of 2004.

19. Lastly, it is contended by the Ld. AR that if at all the Revenue feels that the amount is excessive or the family members ought should not have been permitted to travel with the director/employee, such an amount has to be treated as a perquisite in the hands of the employee, but no disallowance of expense could be made in the hands of the assessee.

20. Per contra it is the submission of the Ld. DR that in this type of cases what has to be located by the assessing officer is the status of the parties as spelt out and the nature or character of the trade or venture, the purpose for which the expenses were incurred and the object which was sought to be achieved in incurring those expenses. In the absence of

any plausible and acceptable explanation by the assessee as to how the travel by an infant or minor or non-employee would serve business purpose, the assessing officer is bound to make such addition. Even before the Tribunal also except arguing that the expenditure was genuinely incurred and the travel was for business purpose, no proper explanation as to what business purpose was served by the travel of a minor or some other person than the employee was served. She submitted that the decision in Alpha Laval (supra) does not help the case of the assessee.

21. We have gone through the record in the light of the submissions made on either side. It is an undisputed fact that not only the wives of the directors, but the minor children and some other persons whose relationship between the directors of the employees is explained for example Matilde Francis, Sumitra Balani, Mohammad Mustafa etc. had also travelled and such expenditure is also included in the claim made by the assessee. Besides these people, some overseas employees also travelled with their wives. Even before us also the assessee failed to explain what the commercial expediency was involved in this travel by such people and what business purpose that was served by the travel of minor children of the directors or management trainees or the overseas employees and their wives.

22. In CIT v. Alfa Laval (I) Ltd 282 ITR 445 (Bom) it was held as under:

> *"4. ……..It is not in dispute that the expenses as a fact were incurred. The amount of expenses incurred is not in doubt. The expenses must stand to the test of commercial expediency. The test of commercial expediency cannot be reduced in the shape of a ritualistic formula, nor can it be put in a watertight compartment*

> *so as to be confined in a straitjacket formula. All that law requires is that the expenditure should not be in the nature of capital expenditure or personal expenditure of the assessee and it should be wholly and exclusively laid out for the purposes of the business. It is well-settled that items of expenditure are to be considered from the point of view of a normal, prudent businessman. The test merely means that the Court will place itself in the position of a businessman and find out whether the expenses incurred could be said to have been laid out for the purpose of the business. It seems that in the ultimate analysis the matter would depend on the status of the parties as spelt out and the nature or character of the trade or venture, the purpose for which the expenses were incurred and the object which was sought to be achieved in incurring those expenses.*
>
> 5. Applying normal, prudent businessman's approach, we do not think that the expenses incurred by the assessee on a foreign trip of the wife of the company's president could be said to be not for the purposes of the business of the assessee-company. Considering the concurrent finding of fact recorded by both the authorities below, in our view, the expenditure would be allowable as deduction while computing the profits and gains of the business."

23. All the decisions cited by the assessee clearly show that the expenses not only proved to have been incurred, but they must also stand to the test of commercial expediency. Unless and until, it is shown that it is customary for the directors or the employees to attend such business meetings or so with wives and minor children, merely because the assessee says so, it cannot be assumed that the accompaniment of wife and minor children of the directors, management trainees and overseas employees was due to commercial expediency. It is not the case of the assessee that the directors or other employees of the company have declared in their returns of income the foreign travel is a perquisite. In the circumstances, we are of the considered opinion that the foreign travel expenses in respect of the wives, minor children and

others fail the test of commercial expediency and there are no valid reasons to interfere with the findings of the authorities below on the disallowance of the foreign travel expense relatable to the wives and minor children of the directors, management trainees and overseas employees of the assessee company. We therefore dismiss ground No. 2 of assessee's appeal.

24. In the result, appeal of the assessee is allowed in part.

Order is pronounced in the open court on 14th October, 2019.

Sd/-	**sd/-**
(B.R.R. KUMAR)	**(K. NARASIMHA CHARY)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Dated: 14th October, 2019/VJ

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1. Appellant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR
ITAT, New Delhi

Date of dictation	10.10.2019
Date on which the typed draft is placed before the dictating member	10.10.2019
Date on which the typed draft is placed before the other member	14.10.2019
Date on which the approved draft comes to the Sr. PS/ PS	14.10.2019
Date on which the fair order is placed before the dictating member for pronouncement	14.10.2019
Date on which the fair order comes back to the Sr. PS/ PS	14.10.2019
Date on which the final order is uploaded on the website of ITAT	14.10.2019
date on which the file goes to the Bench Clerk	14.10.2019
Date on which the file goes to the Head Clerk	
The date on which the file goes to the Assistant Registrar for	

signature on the order	
Date of dispatch of the order	