

Forex fluctuation loss on advance received from Foreign Head Office was allowable as deduction: ITAT

Summary – The Delhi ITAT in a recent case of Cobra Instalaciones Y Servicios SA., (the Assessee) held that Assessee, Spanish company, advanced loan to its Indian PE in foreign currency for execution of project in India, which incurred foreign exchange fluctuation loss on account of differential value in INR, such fluctuation loss was allowable as deduction under section 37(1) in hands of Indian PE

Facts

- The assessee-company a foreign company was engaged in providing services of consultancy in projects, engineering and electrical contract and supplies. It was carrying out business operations from Office at Delhi (India). It had earned income from sale of goods and provision of services for various projects and had debited an amount in its profit and loss account under the head 'Exchange Fluctuation Loss. It explained that for completing the Project in India, either the advance received from the client, or the advance/loan had been received from the Head Office situated in Spain and loans were admittedly received from Head Office in EURO and had been repaid in EURO as per RBI guidelines to carry out operations in India and was outstanding in balance-sheet.
- The Assessing Officer, however, noted that the amounts received by Project Office was not a loan but a capital contribution and though it was a liability in the balance sheet of the Project Office, it could not be called a debt incurred during the course of business.
- The Assessing Officer noted that article 7 specifically prohibits any deduction of expenses relating to Head Office, except reimbursement towards actual expenditure. The Assessing Officer accordingly disallowed the claim of exchange fluctuation loss to the assessee-company and made the addition. Commissioner (Appeals) noted that as per provisions of FEMA, the Project Office located in India did not come under the list of eligible borrowers and therefore, the Project Office was not eligible for external commercial borrowings. Therefore, assessee-company could not take any liability which had to be repaid. The amount remitted to a Project Office in India by a foreign company to do business cannot be taken as 'loan'/external commercial borrowing in the hands of project office. The Commissioner (Appeals) also noted that Assessing Officer had rightly invoked article 7(3) since the same does not allow any notional expenditure/loss as deduction.
- On appeals:

Held

- The amount of the loan is utilized in day-to-day operations *i.e.*, working-capital required for project execution and to obtain material as per the terms of the contract and, thus, the utilization of the amounts received from head Office did not bring any capital asset into existence. Therefore, the amounts so received from the Head Office have been utilized to incur the operating cost. The assessee-company has filed copy of the balance-sheet to show that the amount in question have been shown as liability in assessment year under appeal. The outstanding payable to the Head Office

as on 31-03-2014 increased to Rs. 154,38,08,645/- as compared to Rs. 142,13,94,340/- as on 31-03-2013. Therefore, the contention of assessee-company is correct that for the purpose of completing the turn-key project, the funds are required, which have been provided by the Head Office. It is also explained that for receiving such funds from the Head Office, Reserve Bank of India permission have also been obtained. Though the Commissioner (Appeals) referred to FEMA Act, but, no provisions have been highlighted which assessee-company has violated. The Commissioner (Appeals) noted that Project Office located in India does not come under the list of eligible borrowers, therefore, Project Office is not eligible for external commercial borrowings. Assessee-company, however, explained that it has received loans from Head Office and assessee-company being P.E. of foreign company, is not entitled to raise loans through ECB as ECB can only be raised by Indian borrowers. Findings of Commissioner (Appeals) are, therefore, not relevant to point in issue. The assessee-company has been receiving the funds in EURO for the last so many years from the Head Office and have been admittedly repaying the amounts to the Head Office in EURO and such claim of assessee-company of foreign exchange fluctuation loss in assessment years 2012-2013 and 2013-2014 preceding to assessment year under appeal, have been accepted by the Assessing Officer under section 143(3). No material has been brought on record, if assessee-company has violated any provisions of FEMA Law or any other Act, for receiving such funds from the Head Office. Therefore, merely referring to FEMA is not enough to disallow the claim of assessee-company. It is also not in dispute that due to depreciation in the rupee prices in the International Market in the year under consideration, assessee-company has claimed foreign exchange fluctuation loss on the amount outstanding in foreign currency towards Head Office which consists of advance payment made by the Head Office towards execution of the project and the amount of Engineering charge billed in their home currency by the Head Office towards the services provided. Therefore, the character of the sundry payable to the Head Office is in the nature of payables/liability. Therefore, it is, on revenue account and the loss represents the revenue loss. The assessee-company further explained that it has not paid any interest on the funds borrowed from Head Office. Since, there is no dispute that amount received from the Head Office in Spain was in EURO to assessee in India and repaid in EURO, therefore, difference in INR and EURO was correctly claimed as foreign exchange fluctuation loss. The decision of the article 7(3) of India-Spain DTAA was not applicable in this case because nothing is paid by the assessee-company to the Head Office on account of loss and no deduction claimed. The items of expenses specified in DTAA are not applicable in case of assessee. It was a differential amount on account of foreign exchange fluctuation loss that assessee-company suffered which was claimed as deduction in the profit & loss account. The assessee-company has not violated any terms of article 7(3) because whatever bar have been provided in this article are not applicable to the case of the assessee-company. The assessee-company being P.E. of foreign company in India could not obtain any borrowings from any Bank in India, therefore, working capital was required to complete the turnkey projects. The facts and circumstances of the case as and considering the assessment orders passed by the Assessing Officer in preceding assessment years 2012-2013 and

2013-2014 clearly show that the amount received by the assessee-company from the Head Office is a 'loan'. Therefore, authorities below were not justified in holding it to be capital remittance. The assessee-company did not claim any notional expenses. Therefore, findings of the authorities below are wholly unjustified. It may also be noted here that in subsequent Assessment year 2015-2016, the assessee-company has earned foreign exchange fluctuation gain on the same set of facts in a sum of Rs. 13,37,29,120 which have been declared as income. If the Assessing Officer is of the opinion that assessee- company is not entitled for deduction on account of foreign exchange fluctuation loss, he should not have accept the similar claim of assessee-company in preceding assessment years and should have refunded the amount of tax paid on the foreign exchange capital gain shown in subsequent assessment year. It is well settled Law that rule of consistency do apply to the Income Tax proceedings. Therefore, on the same set of facts, the Assessing Officer cannot take a different view in the assessment year under appeal. The assessee-company is entitled for deduction on account of foreign exchange fluctuation loss. It is an undisputed fact that assessee Indian P.E. company received the amount from Head Office in Spain in EURO and repaid to Head Office in EURO, since the assessee-company had suffered foreign exchange fluctuation loss on account of differential value in INR, such fluctuation loss was allowable as deduction in favour of the assessee-company. Considering the totality of the facts and circumstances of the case, assessee-company is entitled for deduction on account of foreign exchange fluctuation loss.