आयकर अपीलीय अधिकरण "एल" न्यायपीठ मुंबई में।

IN THE INCOME TAX APPELLATE TRIBUNAL " L " BENCH, MUMBAI

श्री दिनेश कुमार अग्रवाल, न्यायिक सदस्य **एवं** श्री, पी.एम. जगताप लेखा सदस्य के समक्ष ।

BEFORE SHRI DINESH KUMAR AGARWAL, JM AND
SHRI P.M. JAGTAP, AM

आयकर अपील सं./I.T.A. No. 8716/Mum/2010
(**निर्धारण वर्ष /** Assessment Years : 2007-08)

Credit Suisse (Singapore) Limited, C/o BMR & Associates, 3F, Contractor Building, 41, R Kamani Marg, Ballard Estate, Mumbai – 400 001.	**बनाम** Vs.	The Assistant Director of Income Tax (International Taxation) – Range 1(2), Scindia House, Ballard Estate, Mumbai – 400 001.
स्थायी लेखा सं./PAN: AACCC7328N		
(अपीलार्थी /**Appellant**)	..	(प्रत्यर्थी / **Respondent**)

अपीलार्थी की ओर से/**Appellant by**	Shri Arvind Sonde
प्रत्यर्थी की ओर से/**Respondent by :**	Shri Narendra Kumar

सुनवाई की तारीख /**Date of Hearing : 19-7-2012**
घोषणा की तारीख /**Date of Pronouncement : 27-7-2012**

आदेश / O R D E R

PER DINESH KUMAR AGARWAL, J.M.:

This appeal preferred by the assessee is directed against the order dtd. 12-10-2010 passed in pursuance to the directions of the Dispute Resolution

Panel (DRP) by the A.O. u/s 143(3) r.w.s. 144C(13) of the Income Tax Act, 1961 (The Act).

2. Briefly stated facts of the case are that Credit Suisse (Singapore) Limited (in short CSSL) is a company incorporated in Singapore and a tax resident of Singapore. CSSL, inter alia, conducts portfolio investments in Indian securities and is registered with the Securities and Exchange Board of India (SEBI) as a sub-account of Credit Suisse : a SEBI registered Foreign Institutional Investor (FII). The A.O. observed that for the year under consideration, the assessee company has shown the following income in the revised return of income (para 3 of the assessment order) :

> - "Net short term capital loss from sale of shares of Rs. 348,207,4000/-.
> - Net short term capital loss from sale of shares underlying FCCBs: Rs. 111,660,628/-.
> - Gains from exchange traded derivative contracts Rs. 472,664,0493/-;
>
> The above net resultant gains of Rs. 1,132,905,865/- are claimed as exempt under Article 13(4) of the India-Singapore tax treaty by the assessee. Further the dividend income of Rs. 104,531,125/- is also claimed to be exempt u/s 10(34) of the Act."

The A.O. further observed that in the notes to the computation of income, the assessee has claimed that gains of Rs.304,847,277/- on cancellation of foreign exchange forward contracts is on capital account and not chargeable to tax in India. Without prejudice to this claim, the assessee has claimed that if the income is treated as capital gains, it is not taxable as per Article 13(4) of the India-Singapore tax treaty. If such income is treated as business income, it is not taxable as per Article 7 of the India-Singapore tax treaty as the assessee does not have a permanent establishment in India as defined in Article 5 of the India-Singapore tax treaty. The assessee was asked to show cause as to why the gains of Rs. 304,847,277/- on cancellation of foreign exchange forward contracts be not taxed as income from other sources and the benefit of exemption of India-Singapore tax treaty be denied on this gain. In response, the assessee's representative filed his explanation vide 18-12-2009 inter alia submitted that in the assessment for A.Y. 2006-07 these gains were regarded as capital gains exempt under India-Singapore tax treaty. The assessee's representative vide letter dtd. 21-12-2009 submitted as under (page 5 of A.O.'s order –Point No. 3):-

"In conclusion, we respectfully submit that :

- CSSL is a company incorporated in Singapore and a tax resident of Singapore. CSSL is eligible to claim benefits of the India-Singapore tax treaty and it does not have a PE in India as defined in Article 5 of the India-Singapore tax treaty.

- Foreign exchange forward contracts are entered by CSSL to hedge its exposures in respect of its Indian Investments being shares/exchange traded derivative contracts. Accordingly, the gains realized by CSSL on cancellation of foreign exchange forward contract are capital in nature and are not liable to tax in India.

- Without prejudice to the above, since CSSL is an FII sub-account and given the provisions of Section 115AD of the Act, wherein the transactions in underlying assets against which the foreign exchange forward cover contracts are entered into, are taxed as 'capital gains', the foreign exchange forward cover contracts should also take the colour of their underlying assets (being capital assets); consequently, the gains realized from cancellation of such forward cover contracts should be regarded as capital gains. Such capital gains are not liable to tax in India as per Article 13(4) of the India –Singapore tax treaty.

- Without prejudice to the above, the gains realized from cancellation of foreign exchange forward contracts may be taxed as business profits in the hands of CSSL. Such business profits are not liable to tax in India under Article 7 of the India-Singapore tax treaty since CSSL does not have a PE in India.

- Gains realized from cancellation of foreign exchange forward contracts should first qualify as 'capital gains' under Article – 13 of the India-Singapore tax treaty or, at best, qualify as 'business profits' under Article 7 of the India-Singapore tax treaty. Since such gains would fall within one of the Articles expressly covering a specific type of income (i.e. either capital gains or business profits), the gains cannot be classified as 'income from other sources' taxable under Article 23 of the India-Singapore tax treaty."

The A.O., however, did not accept the assessee's explanation. According to the A.O. the transaction in forward purchase of foreign exchange and settlement thereby cannot be said to be resulting in capital gains as the same was never held by the assessee as capital asset but meant to be settled by price difference. He further observed that since the assessee is not eligible to carry on business in India as per SEBI regulations the income arising from settlement of forward contracts cannot be treated as business income. He further observed that the income of the assessee from cancellation of foreign exchange forward contracts is neither capital gains income nor business income but 'income from other sources' under Article – 23 of the India-Singapore tax treaty. The A.O. after relying on the appellate order dtd. 28-11-2008 in the case of Citicorp Investment Bank Singapore Ltd. for A.Y. 2005-06 and the assessment order in the case of D.B. International Asia for assessment years 2005-06 & 2006-07 held that the above transaction does not come under the purview of permanent establishment relating to business profits and also u/s 45(1), the gains of Rs.

304,847,277/- which has arisen to the assessee is not on account of any adventure in trade or business nor relates to the head “income from capital gains” but as “income from other sources” in view of Article – 23 of Indo-Singapore treaty, wherein it has been provided that the incomes which are not expressly mentioned in the other Articles of the said agreement, the same may be taxed in accordance with the tax laws of the respective contracting states and accordingly he treated the income of Rs. 304,847,277/- as ‘income from other sources’ which for the same reasons has also been confirmed by the DRP vide directions dtd. 16-9-2010 passed u/s 144C(5) of the Act.

3. Being aggrieved by the order of the DRP -1, the assessee is in appeal before us taking the following grounds of appeal:-

> “The Appellant respectfully submits that the learned Assessing Officer (‘Assessing Officer’) based on the directions issued by the Dispute Resolution Panel under section 144C(5) of the Income Tax Act, 1961 (‘the Act’) has, in his order under section 143(3) read with section 144C(13) of the Act, erred in law and in facts and circumstances of the case:
>
> 1. In not considering the gains realized by the Appellant on cancellation of foreign exchange forward contracts (‘forward covers’) are realized on capital account.
>
> 2. Notwithstanding ground 1 above, in not considering the gains arising on cancellation of forward covers as capital gains and hence not liable to tax under Article 13(4) of the Double Taxation Avoidance Agreement between India and Singapore (‘the treaty’).
>
> 3. Notwithstanding ground 1 above, in not considering the gains arising on cancellation of forward covers as business profits and that such business profits are not liable to tax in India under Article 7 of the treaty, given that the Appellant does not have a permanent establishment in India as defined in Article 5 of the treaty.

4. In holding that the gains arising on cancellation of forward covers is taxable as 'Income from other Sources' under Article 23 of the treaty.

5. In disregarding the provisions of section 209 of the Act and levying interest under section 234B of the Act.

6. Notwithstanding ground 5 above, in not following the decision of the Bombay High Court (ie jurisdictional High Court) issued in the case of NGC Networks Asia LLC vs. DIT (313 ITR 187) and levying interest under section 234B of the Act."

4. At the time of hearing the ld. counsel for the assessee, at the outset, submits that in this case the A.O. while treating the gains as income from other sources has followed the order of the ld. CIT(A) dtd. 28-11-2008 in the case of Citicorp Investment Bank (Singapore) Ltd. for the A.Y. 2005-06 which has been reversed by the Tribunal in the case of Citicorp Investment Bank (Singapore) Ltd. vs. Dy. Director of Income Tax (Intl. Taxation) in ITA No. 2877/Mum/2003 & 910/Mum/2009 for assessment years 1998-99 & 2005-06 order dtd. 8-6-2011 wherein the Tribunal after following the order of the Tribunal in the case of Citicorp Banking Corporation, Behrain vs. Addl. Director of Income Tax (International Taxation) in ITA No. 6525/M/09 for A.Y. 2005-06 has held that gains arising from early settlement of forward foreign exchange contract has to be treated as capital gain. He also placed on record the copy of the said orders of the Tribunal. He, therefore, submits that the addition made by the A.O. and sustained by the DRP be deleted.

5. On the other hand the ld. D.R. while relying on the order of the A.O submits that since the transaction in forward purchase of foreign exchange and

settlement thereof cannot be said to be resulting in capital gain as the same was never held by the assessee as capital asset but meant to be settled by price difference, therefore, the A.O. was justified in treating the same as 'income form other sources' under Article 23 of India-Singapore Treaty r.w.s. Income tax Act 1961. He further submits that the Tribunal in the cases of Citicorp Investment Bank (Singapore) Ltd. (supra) and Citicorp Banking Corporation, Behrain (supra) cited by the ld. counsel for the assessee has considered the decision of the Special Bench of the Tribunal in the case of Apollo Tyres Ltd. vs. ACIT (2004) 84 TTJ (Del)[SB] 741 wherein it has been held that the gain arising from cancellation of forward contracts which are connected with the foreign loans raised for purchase of machinery are capital in nature and are liable to be reduced from cost of the machinery by virtue of section 43A(1) r/w Expln. 3 thereto. In the light of this he submits that the gain arising from cancellation of forward contracts should be adjusted to the cost of the forward contracts and the balance is liable to be taxed as income from other sources. For the proposition that such transactions are not capital assets, the reliance was also placed in CIT vs. All India Tea & Trading Co. Ltd. (1979) 117 ITR 525 (Cal) wherein it has been held that for the purpose of capital gains assets "held by the assessee" includes physical, actual, constructive and also symbolic possession of a property of any kind. Since in the present case the assessee does not hold any such property, the A.O. has rightly treated the gain arising from the forward contracts as 'income from other sources' and, therefore, the order passed by the A.O. be upheld.

6. In the rejoinder, the ld. counsel for the assessee submits that in the case of Apollo Tyres Ltd. (supra) the issue before the Special Bench of the Tribunal was "Whether on facts and in law, the gains earned on cancellation of the foreign exchange forward contract are capital receipt or revenue receipt? If it is capital receipt, whether the same should be reduced from the cost of plant and machinery in connection with which the forward contract was entered into?". He further submits that at page 747 of the report the Special Bench has considered the above question as under:-

> "(i) Whether the gains earned on cancellation of the foreign exchange forward contracts are capital receipt or revenue receipt; and
>
> (ii) If gains are capital receipt, whether the same should reduce the actual cost of plant and machinery by virtue of Expln. 3 to s. 43A."

The question No. 1 has been answered by the Special Bench vide para 17 appearing at page 755 of the report as under:-

> "17. Viewed in the backdrop of the aforesaid facts and circumstances, we are inclined to accept the contention of learned counsel for the assessee that the entire activity of entering into and cancellation of forward contracts, which are directly connected with the repayment of foreign currency loans fall in the capital field and gains arising therefrom would, therefore, be capital receipts."

He further submits that the second limb of the question is not relevant for the assessee's case, as there is no machinery or plant, therefore, the provisions of section 43A(1) r/w Expln. 3 thereto are not applicable in the assessee's case.

7. We have carefully considered the submissions of the rival parties and perused the material available on record. We find that the facts are not in dispute. The only issue before us is that the gains of Rs. 304,847,277/- on cancellation of foreign exchange forwarding contracts is a capital receipt liable to capital gain or to be assessed under the head 'income from other sources'.

8. In Citicorp Investment Bank (Singapore) Ltd. (supra) the Tribunal after considering the decision of the Special Bench of the Tribunal in the case of Apollo Tyres Ltd. (supra) relied on by the ld. D.R. and the decision of Citicorp Banking Corporation, Behrain (supra) has held vide para 4.4 of the order as under:-

> "...........The dispute raised before us is only with regard to the nature of income from early settlement of forward foreign exchange contract taken to safeguard the foreign exchange loan which had been availed by the assessee for purchase of debentures. The income from sale of debenture has been assessed as capital gain. Therefore, respectfully following the decision of the Tribunal in the case of sister concern Citicorp Bank Corporation, Bahrain (supra) we hold that gains arising from early settlement of forward foreign exchange contract has to be treated as capital gain. We accordingly set aside the orders of the CIT(A) and allow the appeals filed by the assessee."

9. In Citicorp Banking Corporation, Behrain (supra), the Tribunal after following the decision of the Special Bench of the Tribunal in Apollo Tyres Ltd. (supra) and Sutlej Cotton Mills Ltd. vs. CIT (1979) 116 ITR 1 (SC) has held vide penultimate para of the order as under:-

> "So far as the facts before us are concerned, nowhere it is controverted by both the authorities below that the dominant purpose for entering into foreign exchange forward contract by the assessee was for clearly to hedge against the

> depreciation of the foreign currency and it has direct nexus with the investments made by the assessee. It is also admitted fact that the assessee is not doing any business here and the assessee is FII and only engaged in the investment and this fact is nowhere denied by both the authorities below. In our opinion, the loss accrued / arose on account of cancellation of foreign exchange forward contract is capital loss having direct nexus with the investment of the assessee and hence the assessee is entitled to set off the same. So far as the reference u/s.115AD is concerned, in our opinion, the said section decide the quantum of the tax payable by the FIIS on the income from securities or capital gains and it has nothing to do with the determination of the nature of gain or loss, whether same is on account of capital or revenue account. Accordingly, grounds taken by the assessee are allowed."

10. In All India Tea & Trading Co. Ltd. (supra) relied on by the ld. D.R., it has been held (Headnote):

> "┘ Held,┘ that the assessee used the lands for agricultural purposes and derived agricultural income from the lands at the time of their requisition in 1949. The lands were being used by the landless people, after requisition, for agricultural purposes and were also deriving agricultural income from the lands at the time of their acquisition in 1959. Therefore, at all material times, the lands were agricultural lands and they were held by the assessee as owner although the assessee lost their physical possession in 1949 by requisition. Though the assessee was prevented from earning any agricultural income from the lands due to the requisition, the landless people by using the lands for agricultural purposes actually derived agricultural income from the lands in 1949, and at no point of time the agricultural lands became "capital assets" in the hands of the assessee. Therefore, the sum of Rs. 1,34,459 was exempt from capital gains tax."

In the case before us the issue is entirely different, therefore, the decision relied on by the ld. D.R. is distinguishable and not applicable to the facts of the present case.

11. In the absence of any other distinguishing feature brought on record by the ld. D.R., we respectfully following the consistent view of the Tribunal (supra) hold that the gains arising on cancellation of foreign exchange forward contract has to be treated as capital gain and accordingly the A.O. and the DRP were not

justified in treating the said gain as 'income from other sources'. The grounds taken by the assessee are, therefore, allowed.

12. The next dispute is regarding is levy of interest u/s 234B of the Act.

13. At the time of hearing both the parties have not argued the above ground. This being so, we are of the view that the levy of interest u/s 234B of the Act is only consequential. The A.O. is directed to recompute the interest at the time of giving effect to this order. The grounds taken by the assessee are, therefore, partly allowed.

14. In the result, assessee's appeal stands partly allowed.

परिणामतः निर्धारिती की अपील आंशिक स्वीकृत की जाती है ।

Order pronounced in the open court on 27-7-2012.. .

आदेश की घोषणा खुले न्यायालय में दिनांकः 27-7-2012 को की गई ।

Sd/-	sd/-
(**P.M. JAGTAP**)	(**DINESH KUMAR AGARWAL**)
लेखा सदस्य / ACCOUNTANT MEMBER	न्यायिक सदस्य / JUDICIAL MEMBER

मुंबई Mumbai; दिनांक Dated 27-7-2012.

व.नि.स./ . *R.K.* , Sr. PS

<u>आदेश की प्रतिलिपि अग्रेषित/Copy of the Order forwarded to</u> :

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

आदेशानुसार/ BY ORDER,

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