

आयकर अपीलीय अधिकरण, 'बी' न्यायपीठ, चेन्नई
**IN THE INCOME TAX APPELLATE TRIBUNAL
'B' BENCH, CHENNAI**

श्री मनु कुमार गिरि, न्यायिक सदस्य एवं श्री एस. आर. रघुनाथा, लेखा सदस्य के समक्ष
**BEFORE SHRI MANU KUMAR GIRI, JUDICIAL MEMBER AND
SHRI S. R. RAGHUNATHA, ACCOUNTANT MEMBER**

आयकर अपील सं./ITA No.:1992/Chny/2025

निर्धारण वर्ष / **Assessment Year:2018-19**

Namakkal South India Transports, 610, Salem Road, Namakkal – 637 001.	vs.	ACIT, Circle -1, Namakkal.
[PAN:AACFN-2205-Q] (अपीलार्थी/Appellant)		(प्रत्यर्थी/Respondent)

अपीलार्थी की ओर से/Appellant by : Shri. T. Vasudevan, Advocate

प्रत्यर्थी की ओर से/Respondent by : Ms. Gouthami Manivasagam, JCIT

सुनवाई की तारीख/Date of Hearing : 27.11.2025

घोषणा की तारीख/Date of Pronouncement : 11.02.2026

आदेश /O R D E R

PER S. R. RAGHUNATHA, AM:

This appeal by the assessee is filed against the order of the Commissioner of Income Tax (Appeals), National Faceless Appeal Centre (NFAC), Delhi, for the assessment year 2018-19, dated 06.06.2025.

2. The assessee has raised the following grounds of appeal.

1. *The Order of the Commissioner of Income Tax (Appeals) NFAC dismissing the appeal is contrary to law, erroneous and unsustainable on the facts of the case.*

2. The CIT(A) NFAC erred in confirming the addition of Rs. 20,00,000/-by holding that the claim of expenditure is not allowable under sec. 37 of the Act

3. The CIT(A) NFAC failed to appreciate that the amount was paid to Chettinad Cements for loss of certain quantity of goods in the process of transportation of their goods is compensatory in nature and the payment also confirmed the party is a genuine claim and hence allowable as business expenditure.

4. The CIT(A) NFAC further failed to appreciate that the shortage of goods on delivery arises from the mishandling of goods by the assessee's vehicle drivers and hence the compensation paid by assessee was an expenditure incurred wholly and exclusively for the purpose of business and hence the claim for allowance was justified.

5. The CIT(A) NFAC was not justified in assuming that assessee had utilised the goods and claimed it as short supply in absence of any allegation by the Chettinad Cements and hence confirming the addition was wholly unjust and unsustainable on the facts of case.

6. The CIT(A) NFAC, in any event, ought to have appreciated that the payment was not penal in nature and was made to compensate the loss of quantity of goods on transit and hence the claim of assessee as business expenditure was to be allowed u/s 37 of the Act.

7. The CIT(A) NFAC ought to have directed the AO to set-off the loss determined in the earlier year, carried forward and claimed by assessee in the ROI as mandated by the provisions of the Act.

3. The brief facts of the case are that the assessee is a firm and transport operator and C & F Agent. The assessee filed its return of income admitting NIL income for the A.Y.2018-19 ON 23.10.2018. The case was selected for limited scrutiny to verify large expenditure by way of penalty or fine for violation of any law, as reported in the ITR and Form 3CD and substantial loan squared up during the year. During the assessment proceedings, the AO noticed that the assessee had claimed an expenditure of Rs.20.00 Lakhs under the head 'penalty / fine' paid to M/s.Chettinad Cements Ltd, on account of shortage of goods during the transportation. The assessee furnished the ledger account, bank statements evidencing payment and a screen shot of the email correspondence from Chettinad Cements confirming the transaction. Since, Chettinad cements did not respond to the notice u/s.133(6) issued by the revenue and no confirmation also submitted by the assessee, the AO

disallowed the expenditure u/s.37 of the Act holding that the payment was in the nature of penalty and thus not allowance as business expenditure to the tune of Rs.20.00 Lakhs and passed an order u/s.143(3) of the Act dated 31/03/2021.

4. Aggrieved by the order of the AO the assessee preferred an appeal before the Id.CIT(A) and the Id.CIT(A) has confirmed the same by passing an order dated 06.06.2025.

5. The assessee challenged the same before us by filing this appeal.

6. The Id.AR submitted that both the AO and Id.CIT(A) have erred in arriving at the conclusion that the payment of Rs.20.00 Lakhs which has been paid to Chettinad Cements Ltd. is towards any violation of law. The said payment made to Chettinad Cements is towards shortage of Cement in transit and not for any violation of law. Therefore, it is an expenditure in relation to the business carried on by the assessee allowable u/s.37 of the Act. Further, the Id.AR drew our attention to the Email correspondence for having claimed the cost for shortage of goods (page No.16 of the Paper book) and also to the condition No.4 in the 'Contract for transportation' (page No.9 to 11 of the Paper book) of packed and bulker cement dated 06.08.2018. Further the Id.AR also filed a ledger account (page No.15 of the Paper book) of payment of fine to Chettinad Cement, through their Bank account PNB.

7. Further, the Id.AR relied on the decision of the Hon'ble Madras High Court in the case of CIT v, VO Chidambaranar Port Trust (2019) 311 CTR 227 (Mad), Hon'ble Kerala High Court decision in the case of Annamalai Timber Trust Ltd. v. CIT (1963) 47 ITR 814 (Ker) and Hon'ble Supreme Court decision in the case of CIT v. Chandulal Keshavlal & Co.(1960) 38 ITR 601 (SC), which involves compensatory damages under contracts without any element of infraction of law.

8. In light of the above arguments the Id.AR prayed for deleting the disallowance of the expenditure by setting aside the order of the Id.CIT(A).

9. Per contra the Id.DR filed a paper book containing 1 to 19 pages including her written submissions and case laws. The Id.DR vehemently argued that the expenditure claimed is in the nature of penalty and hence not allowable u/s.37(1) of the Act. Further the Id.DR relied on the decision of the Hon'ble Supreme Court in the case Haji Aziz and Abdul Shakoor Bros. v. CIT 91961) 41 ITR 350 (SC) and prayed for confirming the order of the AO which is upheld by the Id.CIT(A).

10. We have carefully considered the rival submissions, perused the material available on record and gone through the orders of the authorities and examined the judicial precedents relied upon by both the parties. The issue that arises for our consideration is whether the payment of Rs.20,00,000/- made by the assessee to M/s.Chettinad Cements Ltd. on account of shortage of cement during transportation is allowable as business expenditure u/s.37(1) of the Act, or whether the same is hit by the Explanation to section 37(1) as being in the nature of penalty for violation of law.

11. The undisputed facts are that the assessee is a transport operator and Clearing & Forwarding Agent. During the relevant assessment year, the assessee claimed an expenditure of Rs.20,00,000/- described as "penalty/fine" paid to M/s.Chettinad Cements Ltd. The AO disallowed the said expenditure primarily on the ground that (i) it was described as penalty/fine, (ii) Chettinad Cements Ltd. did not respond to the notice issued u/s.133(6) of the Act, and (iii) the assessee failed to establish that the payment was not for violation of law. The Id. CIT(A) confirmed the said disallowance.

12. At the outset, it is well settled that the nomenclature given to an expenditure in the books of account is not determinative of its true nature. What is required to be examined is the real character of the payment and the purpose for which it was incurred. The Hon'ble Supreme Court in *CIT v. Chandulal Keshavlal & Co.* (1960) 38 ITR 601 (SC) has held that the test to be applied is whether the expenditure was incurred wholly and exclusively for the purpose of business and not whether it resulted in an immediate benefit.

13. In the present case, the assessee has placed on record:

- The contract for transportation entered into with M/s. Chettinad Cements Ltd., wherein clause 4 clearly stipulates that the transporter shall be responsible for shortage or loss of goods during transit.
- Email correspondence from M/s. Chettinad Cements Ltd. evidencing the claim raised for shortage of cement during transportation.
- Ledger account and bank statements evidencing actual payment of Rs.20,00,000/- through banking channels.

14. These documents cumulatively establish that the payment was made pursuant to contractual obligations arising out of shortage of goods during transit.

15. The finding of the Assessing Officer that the expenditure is penal in nature is not supported by any material on record. There is no finding that the assessee violated any statutory provision or any law in force. There is also no allegation by M/s.Chettinad Cements Ltd. that the assessee misappropriated or utilised the goods. The shortage has been attributed to mishandling during transportation, which is an incident intrinsic to the business of a transporter.

16. The Explanation to section 37(1) disallows expenditure incurred for any purpose which is an offence or which is prohibited by law. In the present case, the payment is compensatory in nature, made to indemnify the principal for loss

of goods entrusted to the assessee for carriage. Such compensation cannot be equated with a penalty imposed for infraction of law.

17. The Hon'ble Madras High Court in *CIT v. V.O. Chidambaranar Port Trust* (2019) 311 CTR 227 (Mad) has clearly held that payments which are compensatory and arise out of contractual obligations do not partake the character of penalty, and hence are allowable as business expenditure. Similarly, the Hon'ble Kerala High Court in *Annamalai Timber Trust Ltd. v. CIT* (1963) 47 ITR 814 (Ker) held that damages paid for breach of contract in the course of business are allowable deductions. These decisions squarely apply to the facts of the present case.

18. The reliance placed by the Id. DR on the decision of the Hon'ble Supreme Court in *Haji Aziz and Abdul Shakoor Bros. v. CIT* (1961) 41 ITR 350 (SC) is misplaced, as that case dealt with penalty paid for contravention of statutory provisions, which is clearly distinguishable from the facts of the present case where no statutory violation has been established.

19. The non-response of M/s.Chettinad Cements Ltd. to the notice issued u/s.133(6) of the Act, by itself, cannot be a ground to disallow the claim when the assessee has furnished contemporaneous documentary evidence substantiating the transaction and the payment has been made through banking channels. The genuineness of the payment has not been doubted by the authorities below.

20. In view of the above discussion, we hold that the payment of Rs.20,00,000/- made by the assessee to M/s.Chettinad Cements Ltd. is compensatory in nature, incurred wholly and exclusively for the purpose of business, and does not fall within the mischief of the Explanation to section 37(1) of the Act. Accordingly, the disallowance made by the Assessing Officer and confirmed by the Id. CIT(A) is unsustainable.

21. As regards Ground No.7 relating to set-off of carried forward loss, since the primary disallowance itself is deleted, the Assessing Officer is directed to recompute the total income and allow consequential relief in accordance with law.

22. In the result, the appeal filed by the assessee is allowed.

Order pronounced in the open court on 11th February, 2026 at Chennai.

Sd/-

(मनु कुमार गिरि)
(MANU KUMAR GIRI)

न्यायिक सदस्य/**Judicial Member**

Sd/-

(एस. आर. रघुनाथा)
(S.R.RAGHUNATHA)

लेखा सदस्य/**Accountant Member**

चेन्नई/Chennai,

दिनांक/Dated, the 11th February, 2026

SP

आदेश की प्रतिलिपि अग्रेषित/Copy to:

1. अपीलार्थी/Appellant
2. प्रत्यर्थी/Respondent
3. आयकर आयुक्त/CIT– Chennai/Coimbatore/Madurai/Salem
4. विभागीय प्रतिनिधि/DR
5. गार्ड फाईल/GF