THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCH "A", HYDERABAD

BEFORE SMT P. MADHAVI DEVI, JUDICIAL MEMBER
AND SHRI S. RIFAUR RAHMAN, ACCOUNTANT MEMBER

ITA No.1387/Hyd/2017
Assessment Year: 2014-15

M/s Suri Engineers Pvt. Ltd., Hyderabad. PAN- AACCS8544A	vs.	The ITO, Ward-3(4), Hyderabad.
(Appellant)		(Respondent)

Assessee by : Shri V. Jagadisan
Revenue by : Smt. Suman Malik

Date of hearing : 18-01-2018
Date of pronouncement : 24-01-2018

ORDER

PER P. MADHAVI DEVI, J.M.:

This is assessee appeal for the A.Y 2014-15. In this appeal, the assessee is aggrieved by the order of the CIT(A)-3, Hyderabad, dated 22.05.2017. The assessee has raised the following grounds of appeal:

1. *The Learned Commissioner of Income Tax (Appeals) is not justified in dismissing the appeal without proper reasons - both legal and factual.*
2. *The Learned Commissioner of Income Tax (Appeals), having accepted that the value of machinery is directed to be allowed in the year in which the final settlement takes place between. the Assessee-Appellant and the Insurance company, is not justified in dismissing the appeal as if the claim towards loss of machinery is not an allowable deduction.*
3. *The Learned Commissioner of Income Tax (Appeals), having accepted that so far as the Insurance company is concerned the amount of loss on destruction of machinery is finally*

determined, is not legally correct in holding that the liability is not crystalized for deduction in the year under appeal in computing Total income for Assessment Year 2014-15.

4. *The Learned Commissioner of Income Tax (Appeals) cannot dismiss the legal issue set out in several case laws cited by Assessee purely on a wrong assumption that facts are not similar.*
5. *The Learned Commissioner of Income Tax (Appeals) is not legally and factually correct in holding that the loss on destruction of machinery is a capital loss (namely "Balance Sheet" item) without any finding as to whether the loss can be deducted in computing the Total Income for Assessment Year under consideration.*
6. *The Ld. CIT(A) is not legally and factually correct that the loss on destruction of machinery cannot be allowed as a deduction on a wrong understanding that the amount of loss is not ascertainable.*
7. *For the grounds and for such other grounds that may be adduced at the time of hearing of the appeal, the issue raised in this appeal may be considered.*

2. Brief facts of the case are that the assessee company, engaged in the business of manufacturing machinery used in Rice Mills, filed its return of income for the A.Y 2014-15 on 30-11-2014 admitting total income at Rs. Nil. During the assessment proceedings u/s 143(3) of the IT Act, the A.O observed that the assessee has debited a sum of Rs. 3,79,42,277/- under “extra ordinary items” and a note was furnished as under:

“*This comprises of loss on destruction of machinery. The company had imported machinery for modernization of certain operations during the year. After clearance by the customs authorities at Chennai, the truck carrying the*

machinery to the company's factory at Hyderabad capsized in Chennai, resulting in severe damage to one of the machines rendering it unfit for use. The insurance company is yet to adjudicate the claim for loss. The loss on destruction of the machine of Rs. 3,79,42,277/-, being loss incidental to business, has been charged to the statement of profit and loss. On adjudication and settlement of insurance claim, the same will be accounted for as revenue in the relevant year"

2.1 The A.O observed that the loss incurred was towards destruction of machinery which is capital in nature. Therefore, the assessee was asked to explain as to why the said loss, debited to profit and loss account, should not be disallowed, the same being capital in nature. The assessee vide letter dated 14-10-2016, submitted that the said machinery was imported from Germany during the relevant financial year and the machinery, after customs clearance at Chennai, was loaded onto a truck for transportation to the company's factory at Hyderabad, but just outside the warehouse at Chennai, the truck capsized and extensive damage was caused to the machinery in July 2013. It was submitted that the company had imported the machinery duty free on the basis of an export obligation guarantee and since the machinery was damaged and cannot be put to use, the company had to pay customs duty along with interest computed from the date of import, and hence the

loss of destruction of machine at Rs. 3,79,42,277/-, being loss incidental to business, has been charged to the statement of profit and loss account and claimed while arriving at taxable income and relied on supporting case law. The A.O, however, observed that the case law relied upon by the assessee were distinguishable on facts. Further, from the notes forming part the financial statements furnished by the assessee, he observed the CIF value of imports in relation to capital goods were shown as Rs. 3,25,12,754/- and therefore, he was of the opinion that the said machinery is a capital asset which is intended to be used in manufacturing of its products i.e Rice Mill machinery and parts thereof. He therefore, held that the loss or damage of machinery is capital in nature and hence cannot be allowed. Aggrieved, the assessee preferred an appeal before the CIT(A).

3. In the meantime, the assessee's claim was accepted by the insurance company at a sum of Rs. 1,26,35,109/- as a full and final settlement of claim. The assessee did not accept the offer and filed a suit in Hon'ble Madras High Court. The Hon'ble Madras High Court passed an interim order on 16-08-2016 directing the insurance company to

pay a sum of Rs. 1,26,35,109/-, i.e the amount agreed to by the insurance company pending final result in the pending suit. The above amount was received by the assessee on 02-05-2017, and thereafter, the assessee reduced the said compensation received from the insurance company from the claim and modified the claim to Rs. 2,53,07,168/-.

4. The CIT(A), observed that the machinery imported did not reach the factory premises of the assessee and was not included in the block of assets and was not put to use and since machinery met with an accident and got damaged, the amount paid to German Company would only be a balance sheet item as an advance paid for the 'asset'. He observed that the amounts received from New India Assurance Company of Rs. 1,26,35,109/- would again be a balance sheet item under the head 'payable to insurance company' and that the said quantum of liability would be known after the insurance claim is crystalized. In these circumstances, she held that the amount of loss of Rs. 2,53,07,168/- cannot be allowed in advance, pending its crystallization, and that as and when the amount is crystalized in future, the same has to be allowed to the

assessee. Aggrieved by this direction of the CIT(A), the assessee is in appeal before us.

5. The Ld. Counsel for the assessee submitted that, the assessee had imported the machinery from Germany in order to update its machinery and in order to increase in profit earning capacity. He submitted that, since the machinery was never put to use, it cannot be referred to as a 'capital asset' as rightly held by the CIT(A). He submitted that the department has not appealed against the finding of the CIT(A) that the loss is allowable in the year of crystallization and therefore the said finding has become final. He submitted that the loss is allowable in the year of incurring the loss and as and when the assessee receives the claim from the insurance company, it would reflect the same as income during the year of receipt u/s 41(1) of the IT Act. Therefore, according to him, no prejudice was caused to the revenue and in fact it has be allowed during the relevant assessment year. In support of his contentions, he placed reliance upon the following case law:

a. *Badridas Daga Vs. CIT 34 ITR 10 (SC).*
b. *Ramchander Shivnarayan 111 ITR 263 (SC).*

c. Dr. T.A Quershi Vs CIT 287 ITR 547.
d. CIT Vs Nainital Bank Ltd., 55 ITR 707 (SC).
e. Chenab Forest Co. Vs CIT 96 ITR 568 (J &K).
f. CIT Vs Inden Biselers 181 ITR 69 (Madras).
g. Idea Cellular Ltd., Vs ACIT 65 SOT 15.

6. The Ld. DR, on the other hand, supported the orders of the authorities below and submitted that the asset being a capital asset, the capital loss cannot be allowed from the profits of the business as rightly held by the A.O.

7. Having regard to the rival contentions and the material placed on record, we find that the machinery has been imported by the assessee but before it could be transported to the assessee's premises at Hyderabad and installed and thereafter put to use, the machinery got damaged. There is no doubt that the machinery has been imported for increasing the profit earning capacity of the assessee and therefore, it is for the business of the assessee. Any expenditure incurred wholly and exclusively for the purpose of the business of the assessee has to be allowed u/s 37(1) of the Act. In the case of Badridas Daga (cited supra) relied upon by the assessee, the Hon'ble Supreme Court held that where there is no provision for a deduction, the tax of admissibility of such a deduction

depends on accepted commercial practice and principles and that the loss incurred while carrying on of business has to be allowed, unless it is expressly or impliedly prohibited. In the case of National bank Ltd., the Hon'ble Supreme Court held that the trading loss of a business is allowable in computing the profit earned by the business. In the case before us, since the machinery has not been installed and put to use by the assessee, the assessee cannot capitalize the same and the depreciation thereon cannot be allowed. An expense is capitalized when it is recorded as an asset, due to its future value on the balance sheet, rather than as an expense in the income statement. Since the machinery got damaged even before it reached the assessee's premises, and it had no future value, it was an expense. The CIT(A) has, in fact accepted that this amount is allowable to the assessee but in the year of crystalization. The reason for confirming the disallowance is that the loss has not crystalized during the year, as the appeal by the assessee against the insurance company is still pending before the Hon'ble High Court of Madras. We agree with the Ld. counsel for the assessee, that the business loss has occurred and is allowable to the assessee

in the relevant assessment year and as and when the compensation is finalized by the Hon'ble High Court of Madras, and the assessee receives it, it would have to offer the same to taxation in such assessment year of receipt. The finding of the CIT(A) has not been challenged by the revenue and therefore it has become final. Therefore, we direct the A.O to allow the business loss during the relevant assessment year before us.

8. In the result, the assessee appeal is allowed.

Pronounced in the open court on 24th January, 2018.

Sd/-	Sd/-
(S. RIFAUR RAHMAN)	**(P. MADHAVI DEVI)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Hyderabad, Dated: 24th January, 2018

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1 M/s Suri Engineers Pvt Ltd., C/o V.S. Rao & Co. CAs, 6-3-609/136, Anand nagar, Hyderabad-04.
2 ITO, Ward -3(4), Hyderabad.
3 CIT(A)-3, Hyderabad
4 Addl.CIT, Range-3, Hyderabad.
5 The DR, ITAT Hyderabad
6 Guard File