IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 14.03.2019

CORAM

THE HON'BLE DR.JUSTICE VINEET KOTHARI
AND
THE HON'BLE MR.JUSTICE C.V.KARTHIKEYAN

Tax Case Appeal No. 195 of 2017

Principal Commissioner of Income Tax
Central 2
No.108, Mahatma Gandhi Road
Chennai - 600 034. Appellant / Respondent

Vs.

M/s. Saravana Selvarathnam Trading &
Manufacturing Pvt. Ltd.,
No.14, Ranganathan Street,
T.Nagar, Chennai - 600 017.
PAN: AAG CS 3757 J Respondent / Appellant

Tax Case Appeal filed under Section 260A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, Madras 'B' Bench, Chennai, dated 11.08.2016 made in ITA No.2202/Mds/2015, against the proceedings of the Commissioner of Income Tax (Appeals) dated:23.09.2015 made in ITA No.296/13-14, and against the Assessment order of the Assistant Commissioner of Income Tax dated 24.03.2014 for the Assessment year 2012-13.

For Appellant : M/s. K.G.Usha Rani
Senior Standing Counsel

For Respondent : M/s. Sumithra
for M/s. R.Sivaraman

J U D G M E N T

(Delivered by DR.VINEET KOTHARI, J)

The Revenue has filed this Appeal under Section 260-A of the Act raising the following purported substantial questions of law arising from the order of the learned Tribunal dated 11.08.2016:-

> "1. On the facts and in the circumstances of the case and in law, whether the ITAT is correct in allowing the amount claimed by the assessee towards bad debts, as loss arising out of embezzlement of cash?;
>
> 2. On the facts and in the circumstances of the case and in law, whether the ITAT is correct in allowing the loss towards embezzlement of the cash in the assessment year 2012-13 whereas the claim relates to the Assessment year 2007-08?;
>
> 3. Whether the ITAT is correct in directing the Department to allow loss towards embezzlement in the assessment year 2012-13 not withstanding the fact that the civil/criminal proceedings initiated by the assessee for recovery of the amount from the concerned employee Director have not reached finality?"

2. The learned Tribunal had allowed business loss to the extent of Rs.1,86,24,839/- which represented the amount allegedly embezzled by a Director representing the workmen on the Board of the Company, who was dealing with the day today affairs of the Company business. Upon such embezzlement being found out by the internal audit procedure, he was not only removed from the Board of Directors, but was also prosecuted by filing a criminal complaint in the Court of XVII Metropolitan Magistrate, Chennai, which is said to be still pending.

3. The relevant findings of the learned Tribunal are quoted below for ready reference:-

> "5. We have considered the rival submissions on either side and also perused the material available on record. During the course of internal audit check, the Assessee found that one of the employee Director embezzled an amount of Rs.240 lakhs. Immediately the said employee was removed from directorship and steps were taken to recover the amount by way of civil and criminal proceedings. The Assessee has filed a criminal complaint before the XVII Metropolitan Magistrate, Chennai. The prosecution is still pending before the

> Metropolitan Magistrate. The question arises for consideration is when there was an embezzlement of cash by the employee of the assessee in the course of the business activity whether it could be allowed as a bad debt or not? For the purpose of claiming a debt as bad, the conditions prescribed under Section 36(2) of the Act have to be complied with. In the case before us, the conditions prescribed under Section 36(2) of the Act were not complied with, therefore, the claim of the Assessee cannot be allowed as bad debt. However, it is a loss suffered in the course of business activity and it is inevitable loss in the hands of the Assessee. When the Assessee trusted Shri Arumugamswamy and allowed him to manage the day-to-day affairs, embezzled the cash to the extent of Rs.240 lakhs. The net embezzled amount comes to Rs.1,86,24,839/-. This Tribunal is of the considered opinion that the embezzled cash by Shri Arumugamswamy in the course of business activity has to be allowed as business loss. In view of the above, this Tribunal is unable to uphold the orders of the lower authorities. Accordingly, the orders of the lower authorities are set aside and the Assessing Officer is directed to allow the embezzled cash of Rs.1,86,24,839/- by Shir Arumugamswamy as business loss."

4. The learned counsel for the Appellant/Revenue submitted that that since the conditions prescribed under Section 36(2) of the Act to claim the said deduction by way of bad debt were not complied with by the Assessee and also since there was a legal opinion obtained by the Assessee that the amount embezzled is recoverable, the same had therefore not turned as bad debt. It was urged that the learned Tribunal had erred in allowing the same as business loss in the hands of the Assessee.

5. The learned counsel for the Assessee supported the impugned order and opposed the submissions of the learned counsel for the Revenue.

6. Having heard the learned counsel for the parties, we are satisfied that no substantial question of law arises in the present case and the findings of the fact arrived at by the learned Tribunal cannot be said to be perverse in any manner.

7. The embezzlement by one of the Directors or an employee of the business of the Assessee Company during the ordinary course of business can be a business loss of the Assessee irrespective of criminal prosecution of the accused director/employee of the Company. The final fate of the criminal proceedings or recovery of the amount in question would not determine the claim of the Assessee in the present year writing off the same as a business loss.

8. In our opinion the learned Tribunal had rightly held it to be a business loss as it was treated to be only a pilferage of the company funds by an employee or a Director on the Board of Company. Therefore, such findings of facts by the Tribunal do not give rise to any substantial question requiring our further consideration under Section 260-A of the Act. Thus we do not find any merits in the Appeal filed by the Revenue and the same is liable to be dismissed.

9. Accordingly, the Appeal filed by the Revenue is dismissed. No costs.

Sd/-
Assistant Registrar (CS-VIII)

//True Copy//

Sub Assistant Registrar

vsg

To

1) The Registrar,
Income Tax Appellate Tribunal,
Madras 'B' Bench, Chennai,

2) The Commissioner of Income Tax (Appeals)-18,
Chennai - 34.

3) The Assistant Commissioner of Income Tax
Central Circle - IV(2),
Chennai - 34.

+1 cc to Mr.R.Sivaraman, Advocate, S.R.No.24309

Tax Case Appeal No. 195 of 2017

PPA(CO)
SSM(12/04/2019).
SSM(07/05/2019).