

आयकर अपीलीय अधिकरण, जयपुर न्यायपीठ, जयपुर
IN THE INCOME TAX APPELLATE TRIBUNAL,
JAIPUR BENCHES (SMC), JAIPUR

श्री भागचन्द, लेखा सदस्य के समक्ष
BEFORE: SHRI BHAGCHAND, ACCOUNTANT MEMBER

आयकर अपील सं./ITA No. 809/JP/2016
निर्धारण वर्ष/Assessment Year : 2011-12

M/s. Pawan Specialities (P) Ltd. 4-Tha-13, Jawahar Nagar ,Jaipur	बनाम Vs.	The ACIT Circle- 6, Jaipur
स्थायी लेखा सं./जीआईआर सं./PAN/GIR No.: ABPPA 5398 F		
अपीलार्थी /Appellant		प्रत्यर्थी /Respondent

निर्धारिती की ओर से / Assessee by: Shri Manish Agarwal , CA
राजस्व की ओर से / Revenue by :Smt. Poonam Rai, DCIT- DR

सुनवाई की तारीख / Date of Hearing : 14/02/2017
घोषणा की तारीख / Date of Pronouncement : 15 /02/2017

आदेश / ORDER

PER BHAGCHAND, AM

The assessee has filed an appeal against the order of the ld. CIT(A),
Jaipur dated 27-06-2016 for the assessment year 2011-12 raising therein
grounds of appeal as under:-

“1. That the ld. CIT(A) has erred in law as well as on facts in confirming the addition without considering the facts and circumstances of the case.

2 That the ld. CIT(A) has erred in making an addition of Rs. 4,77,500/- for disallowance of loss of goods by theft ignoring the facts and circumstances of the case. The same deserves to be deleted.

2.1 Apropos Ground No. 1 and 2 of the assessee, the facts as emerges from the order of the Id. CIT(A) is as under:-

“3.3 I have perused the facts of the case, the assessment order and the submissions of the appellant. The assessee had claimed loss of goods by theft for amounting to Rs. 4,7,500/-. In the assessment proceedings, the Assessing Officer had called for the details which have not been provided. It was claimed that the company has investigated and found the fraud of Tata Sky Vouchers /Coupon on the supplier company. It was further submitted that the fraud was deleted by the company’s internal control department and they have made a detailed list of frauds. The assessee records were called for and it is seen that a statement showing the calculation of Rs. 4,77,500/- was filed before the Assessing Officer, no further details or confirmations from the company supplying the coupons was filed. No FIR or any other proceedings have been launched. Even in the present proceedings, no further details relating to this fraud were filed. Assessing Officer has placed reliance on Shiv Narain Karmendra Narain vs. CIT 193 CTR 561 and 56 ITR 1 (SC). As no satisfactory details of the fraud leading to the loss claimed were filed either before the Assessing Officer or in the present proceedings, the same cannot be allowed. The Assessing Officer’s stand on the issue is confirmed. Ground of appeal is dismissed.”

2.2 During the course of hearing, the Id. AR of assessee prayed for deletion of addition of Rs. 4,77,500/- for which the Id. AR of the assessee filed the following written submission.

“Under all these grounds of appeal, the assessee has collectively challenged the action of Ld. CIT(A) in sustaining the addition of Rs. 4,77,500/- made by Ld. AO by disallowing the loss claimed by assessee on account of loss of goods by theft.

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Brief facts pertaining to these grounds of appeal are that, during the year under appeal, upon investigation, the assessee company's internal control department detected a fraud which was committed by some of its employees. Therein, it was found that a fraud of Rs. 4,77,500/- of Tata Sky Vouchers / Coupon (transferable through mobile) has been committed on the basis of records available from the supplier company. During the course of assessment proceedings, the assessee produced a detailed list of the instances where loss had occurred on account of such fraud / theft. However, the Ld. AO disallowed the loss so claimed by assessee, merely on the ground that no legal action was taken against the persons who had committed the fraud. The Ld. AO alleged that the assessee cannot be allowed to make such entry of loss in books of account in the absence of any action taken by assessee for recovery of the amount embezzled, in support of which, Ld. AO placed reliance on the judgment of Hon'ble Supreme Court in the case of Associated Banking Corporation of India Ltd. Vs. CIT (SC) reported in 56 ITR 1. In this regard it is humbly submitted that it is an admitted position that theft / fraud had indeed has taken place in the assessee company and the Ld. AO has nowhere doubted the fact of fraud. Meaning thereby, that the Ld. AO has made the impugned disallowance not because the assessee could not establish the fact of fraud, but merely because the assessee could not produce copy of First Information Report (FIR) or any other evidence of legal action taken by assessee against the employees committing fraud. It is submitted that merely because the assessee could not lodge FIR or take any other action against the concerned employees, the genuine loss claimed by assessee cannot be disallowed. Non-action against those employees cannot bring the genuineness of the loss in question, and more particularly when the fact of loss on account of fraud is an admitted position, the genuineness thereof automatically gets established. The judgment of Hon'ble Supreme Court in the case of Associated Banking Corporation of India Ltd. Vs. CIT (SC) [56 ITR 1] which has been relied upon by the Ld. AO has been rendered in different set of circumstances and is clearly distinguishable on facts of the case. In that case, embezzlement of huge amount had taken place in a banking company which had been wound up and was under liquidation. In that case it was found that there were reasonable chances of recovery by Liquidator, of the embezzled amount and therefore, it was held that so long as there was a reasonable prospect of recovering the amounts embezzled by the bank, trading loss in a commercial sense may not be deemed to have resulted. However, in the present case the Ld. AO has failed to establish that there were reasonable prospect of recovering the embezzled amount. In the instant case, the Ld. AO has not doubted the genuineness of the fraud but has merely alleged that the assessee did not make effort for recovery of the amount, however, he failed to establish that there was reasonable prospects of recovery of the amount embezzled, the burden to prove which was clearly upon him. It was submitted before the Ld. AO that legal action against the concerned employees was not taken since there was no hope of recovery of the amount. It is pertinent to

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mention here that, the aforesaid judgment of the Hon'ble
Supreme Court has been considered by CBDT who thereafter, issued a
clarification through Circular No. 35D(XLVII-20) [F.No. 10/48/65-IT
(AI)] dated 24.11.1965 (copy enclosed), which provides as under:

**CIRCULAR NO. 35D(XLVII-20) [F. NO. 10/48/65-IT(AI)]
Loss by embezzlement by employees—Deductibility thereof**

BUSINESS INCOME

SECTIONS 29,

A reference is invited to the instructions on the above subject contained in Board's Circular No. 25 of 1939 and Circular No. 13 of 1944. In these circulars it was clarified that losses arising due to embezzlement of employees or due to negligence of employees should be allowed if the loss took place in the normal course of business and the amount involved was necessarily kept for the purpose of the business in the place from which it was lost. Since the above circulars were issued, the Supreme Court has further considered the matter and laid down the law in this regard in the following two cases :—

- (1) Badri Das Daga vs. CIT (1958) 34 ITR 10 (SC) : TC 14R.202.
- (2) Associated Banking Corporation of India Ltd. vs. CIT (1965) 56 ITR 1 (SC)

In the first case, the Supreme Court has affirmed the view that the loss resulting from embezzlement by an employee or agent of a business is admissible as a deduction under s. 10(1) of the IT Act, 1922 (corresponding to s. 28 of the IT Act, 1961) if it arises out of the carrying on of the business and is incidental to it. In the second case the decision is that loss must be deemed to have arisen only when the employer comes to know about it and realises that the amounts embezzled cannot be recovered.

2. In the light of the above decisions of the Supreme Court, the legal position now is that loss by embezzlement by employees should be related as incidental to a business and this loss should be allowed as deduction in the year in which it is discovered

Thus, now it is a settled position that loss by embezzlement by employees should be related as incidental to a business and this loss should be allowed as deduction in the year in which it is discovered.

Another distinguishing feature to be noticed is that the aforesaid judgment was rendered with respect to the provisions of "Income Tax Act,

M/s. Pawan Specialities (P) Ltd. vs. ACIT, Circle- 6, Jaipur 1922”, whereas, the present case is governed by the provisions of “Income Tax Act, 1961”.

The aforesaid circular was taken into consideration by the Hon’ble Allahabad High Court in the case of **Shitla Prasad Shyam Lal Vs. CIT** reported in **188 ITR 514** wherein the Court has held as under:

“...simply because a criminal case was pending or a civil suit had not been filed, the claim of the assessee could not be left undetermined. Moreover, Circular No. 35D(XLVII-20) [F. NO. 10/48/65-IT(AI)] dated 24.11.1965 stated that “loss by embezzlement by employees should be treated as incidental to the business and the loss should be allowed in the year in which it was discovered”. Therefore, the Tribunal was not justified in holding that the assessee’s claim of loss was premature.” [page 516]

Further, in the case of **Bombay Forgings Pvt. Ltd. Vs. CIT** reported in **(1994) 206 ITR 562**, the Hon’ble Gujarat High Court held that:

“...it was an admitted position that the embezzlement had taken place during the relevant previous year and the same was duly reflected in the books of account by omission of the value of such goods from the sales as well as closing stock of the assessee in preparation of the final accounts. In a situation like this, so far as loss was concerned, detection was not relevant. The loss caused to the assessee by embezzlement during the relevant previous year was allowable as deduction in the computation of the income in that previous year itself. (P. 566, C, D)

Similarly, the Hon’ble Gujarat High Court in the case of **Kamla Cotton Co. Vs. CIT** reported in **(1997) 226 ITR 605** has held that:

“...The requirement that a debt has become bad or irrecoverable does not mean that the Department can insist upon demonstrative and infallible proof that the debt had become bad. It is not compulsory for the assessee to take legal proceedings against the debtor for recovery of the claim before writing it off as a bad debt. When a creditor bona fide writes off a debt because there appears no chance of its recovery in the foreseeable future or where the recovery proceedings would be so cumbersome and expensive as to outweigh any advantage of instituting any recovery proceedings, the assessee discharges the onus and would be entitled to claim deduction of the bad debt under clause (vii) of section 36(1) of the Income Tax Act, 1961.”

Thus, in light of the above it becomes clear merely on account of non-action against employees for embezzlement, the undoubted genuineness of the loss claimed by assessee on account of such embezzlement cannot be

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disallowed. Therefore, it is humbly prayed that the addition of Rs. 4,77,500/-
may please be deleted. “

2.3 On the other hand, the Id. DR relied on the orders of the authorities below.

2.4 I have heard the rival contentions and perused the materials available on record. It is noted from the records that the assessee had claimed loss of goods (i.e. Tata Sky Vouchers / Coupon of the supplier company) by theft. However, in the assessment proceedings, the AO required the justification in this regard or also to produce the copy of the FIR for the legal action taken by the assessee which the assessee could not produced before the AO. The AO for want of the evidence or justification as to the theft of the goods disallowed the claim of Rs. 4,77,500/- made by the assessee which has been confirmed by the Id. CIT(A) in first appeal. In the appellate proceedings, the Id. AR of the prayed that it is an admitted position that theft/ fraud had indeed taken place in the assessee company and the AO had nowhere doubted the fact of fraud but he disallowed the claim of the assessee for the reason that the assessee could not establish the fact of fraud like non- production of copy of FIR and not taking any legal action against the employee who was involved in this activity of fraud. The Id. AR further submitted that non-action against those employees cannot bring the genuineness of the loss in

question and more particularly when the fact of loss on account of fraud is an admitted position and thus the genuineness thereof automatically gets established. The ld. AR of the assessee relied on decision of Hon'ble Supreme Court in the case of Associated Banking of India Ltd. vs. CIT (supra). Further the ld. AR of the assessee took resort of CBDT Circular No.25 of 1939 and Circular No. 13 of 1994 wherein it was clarified that losses arising due to embezzlement of employees or due to negligence of employees should be allowed if the loss took place in the normal course of business and the amount involved was necessarily kept for the purpose of the business in the place from which it was lost. The Hon'ble Supreme Court has further considered the matter and laid down the law in this regard in the following two cases.

(1) Badri Das Daga vs. CIT (1958) 34 ITR 10 (SC) : TC 14R.202.

(2) Associated Banking Corporation of India Ltd. vs. CIT (1965) 56 ITR 1 (SC)

On the enquiry by the Bench, it was confirmed by the ld. AR of the assessee that the turnover of the assessee company is more than Rs. 1.00 crore. It is further noted that such issue has been decided by the Hon'ble Courts in favour of the assessee.

(1) Shitla Prasad Shyam Lal vs. CIT , 188 ITR 514 (All.)

(2) Bombay Forgings (P) Ltd. vs. CIT 206 ITR
562 (Bom.)

(3) Kamla Cotton Co. vs. CIT 226 ITR 605 (Guj.)

In view of the above deliberations, case laws and the CBDT circular relied on (supra), I do not concur with the views of the lower authorities on this issue. Thus the appeal of the assessee is allowed.

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

Order pronounced in the open Court on 15 -02-2017.

Sd/-

(भागचन्द)

(Bhagchand)

लेखा सदस्य / Accountant Member

जयपुर / Jaipur

दिनांक / Dated:-

15 /02/ 2017

*Mishra

आदेश की प्रतिलिपि अग्रेषित / Copy of the order forwarded to:

1. अपीलार्थी / The Appellant- M/s. Pawan Specialities (P) Ltd., Jaipur
2. प्रत्यर्थी / The Respondent- The ACIT, Circle- 6, Jaipur
3. आयकर आयुक्त(अपील) / CIT(A).
4. आयकर आयुक्त / CIT,
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, जयपुर / DR, ITAT, Jaipur
6. गार्ड फाईल / Guard File (ITA No. 809/JP/2016)

आदेशानुसार / By order,

सहायक पंजीकार / Assistant. Registrar