

Prosecution and Compounding under Direct Taxes

B.Ramakrishnan
Chartered Accountant

Issues Covered

Prosecution under Income Tax Act, 1961

- Offence subject to Prosecution
- Procedure for Prosecution
- Prosecution in case of Company
- Relief / abatement provided under the Act
- Compounding of offence

Prosecution under Black Money Act

Prosecution under Income Tax Act - Background

Sections 275A to 280 of Income Tax Act ('IT Act') deals with various types of offences for which the Income Tax Department can prosecute an assessee in the Court of Law.

Prosecution can be launched only at the instance of Principal Commissioner (or) Commissioner of Income Tax (or) Commissioner of Income Tax (Appeals) (or) Appropriate Authority.

Procedure for prosecution – governed by provisions of the Criminal Procedure Code, 1973 unless specifically provided by the IT Act

Prosecution under Income Tax Act - Background

Section	Offence	Punishment
275A	Contravention of any prohibitory order u/s.132(1) or 132(3) issued during the search proceedings	Any period up-to 2 years and fine
275B	Failure to afford any facility to the Authorised Officer to inspect the books and other documents u.s 132(iib) of the Act	Any period up-to 2 years and fine
276	Removal, concealment, transfer or delivery of property to thwart recovery of taxes.	

Prosecution under Income Tax Act - Background

Section	Offence	Punishment
276A	Failure to comply with provisions of sections 178(1) or section 178(3)) by liquidator of a company: <ol style="list-style-type: none"> 1. Fails to give notice u/s 178(1) 2. Fails to set aside the amount specified u/s 178(3) 3. Parts with any of the properties of the company in contravention of section 178(3) 	Any period not less than 6 months in the absence of adequate reason to the contrary recorded in the judgment; May extend up-to 2 years

Prosecution under Income Tax Act - Background

Section	Offence	Punishment
276AB	Failure to comply with provisions of section 269 UC, UE, UL relating to removal of immovable property*	
276B	Failure to pay the tax deducted at source under chapter XVII B or failure to tax payable u/s 115O(2) or second proviso to section 194B of the Act (Non-cognizable u/s 279A of the Act)	Minimum : 3 months and fine Maximum: 7 years and fine

***Section 269UC,UE,UL and other provisions of this chapter XXC are not applicable in respect of transfers on/after 01/07/2002**

Prosecution under Income Tax Act - Background

Section	Offence	Punishment
276BB	Failure to pay the tax collected at source u/s 206C	Minimum : 3 months and fine Maximum: 7 years and fine
276C	<p>(1) Wilful attempt to evade tax, penalty or interest <u>imposable</u> (or) <u>under-reported income</u> (Non-cognizable u/s 279A of the Act)</p> <p>(2) Wilful attempt to evade payment of tax, penalty or interest</p>	<p>A. <u>Tax evaded <= 25 Lakhs</u> (upto 30-06-2012 – Rs.1 Lakh) Minimum : 3 months and fine Maximum: 2 years and fine (upto 30-06-2012 – 3 years and fine)</p> <p>B. <u>Tax evaded > 25 Lakhs</u> Minimum : 6 months and fine Maximum: 7 years and fine</p>

Prosecution under Income Tax Act - Background

Section	Offence	Punishment
276CC	<p>Failure to furnish the return of income u/s 139(1)/142(1)/148/153A</p> <p><i>No prosecution if :</i></p> <ol style="list-style-type: none"> 1. <i>Return filed before expiry of Assessment Year or</i> 2. <i>Tax payable Less: TDS / advance tax <= Rs.3,000/-</i> 	<p><u>A. Tax evaded <= 25 Lakhs</u> (upto 30-06-2012 – Rs.1 Lakh) Minimum : 3 months and fine Maximum: 2 years and fine (upto 30-06-2012 – 3 years and fine)</p> <p><u>B. Tax evaded > 25 Lakhs</u></p>
276CCC	Failure to furnish the return of income in search cases.	<p>Minimum : 6 months and fine Maximum: 7 years and fine</p>

Prosecution under Income Tax Act - Background

Section	Offence	Punishment
276D	Failure to produce account books and documents u/s 142(1) or failure to get accounts audited us 142(2A)	Rigorous Imprisonment up-to 1 year and fine
277	False statement in verification, etc. (Non-cognizable as per section 276A)	<u>A. Tax evaded <= 25 Lakhs</u> (upto 30-06-2012 – Rs.1 Lakh) Minimum : 3 months and fine Maximum: 2 years and fine (upto 30-06-2012 – 3 years and fine)
278	Abatement of false returns etc.	<u>B. Tax evaded > 25 Lakhs</u> Minimum : 6 months and fine Maximum: 7 years and fine

Prosecution under Income Tax Act - Background

Section	Offence	Punishment
277A	Falsification of books of account or documents, etc.. To evade tax /penalty/interest <u>imposable</u>	Minimum : 3 months and fine Maximum: 2 years and fine (up to 30-06-2012 – 3 years and fine)
278A	Punishment of <u>second and subsequent offence</u> u/s 276B, 276C(1), 276CC, 277 and 278	Rigorous imprisonment: Minimum : 6 months and fine Maximum: 7 years and fine
280	Disclosure of particulars by public servant in contravention of section 138(2)	(Prosecution with prior approval of CG) Up-to 6 months and Fine

278AA – Reasonable cause for failure is proved – punishment shall not be imposed for offence u/s 276A, 276AB and 276B

Procedure for Prosecution

Procedure for prosecution – governed by provisions of the Criminal Procedure Code, 1973 unless specifically provided by the IT Act

Section 280A to 280D was inserted by Finance Act, 2012 under IT Act , wherein:

1. Central Government in consultation with Chief Justice of High Court are given powers to designate Magistrate Court of the respective jurisdiction* as Special Court for offence punishable under this act which is punishable with imprisonment up to 2 years and/or with fine
2. All offence punishable under IT Act would be triable by such Special Court unless circumstances provided u/s 280B of the Act

*Jurisdiction for deciding the Magistrate Court is the place where the false return is submitted.

Procedure for Prosecution

Section 278E – Culpable Mental State

In general criminal jurisprudence, - 'Innocent until proven guilty' beyond reasonable doubt

Under IT Act - existence of culpable mental state is presumed and it shall be a defence for the accused to prove beyond reasonable doubt that he had no such mental state

Procedure for Prosecution

As per the Guidelines issued by CBDT:

A. Procedure to be followed by Department while launching Prosecution:

- The Assessing Officer on the basis of the records of the assessee sends the proposal to the respective Commissioner.
- The Commissioner issues the show cause notice to the assessee.
- If Commissioner is satisfied with the reply of the assessee he may not grant sanction to the Assessing Officer to file complaint before the Court.

Procedure for Prosecution

B. Procedure before Court:

- **On receipt of complaint, the court summons the accused by sending the copy of complaint**
- **If the accused is not present on the day of summon, a warrant against the accused can be issued, wherein he may be arrested and produced before the Court**
- **After hearing the accused, if the court feels that there is no apparent case, the complaint will be dismissed.**
- **In the presence of primary evidence, the court frames the charges – ie, court charges the accused of the offence purported to be committed and and proceedings shall continue as per the Criminal Procedure Code ('CPC').**
- **If the Trial results in conviction, the appeal to the court session will lie under CPC to be filed within 30 days of from the date of order**

Procedure for Prosecution

- Competent Authority and requisite Sanction

- Competent authority to grant sanction for prosecution is Principal Commissioner, Commissioner, Commissioner (Appeals), Chief Commissioner or the Director General.
- Prosecution, without a requisite sanction shall make the entire proceedings void ab initio
- The sanction must be in respect of each of the offences in respect of which the accused is to be prosecuted

(Champalal Girdharlal v. Emperior (1933) 1 ITR 384 (Nag) (HC)) - sanction issued for offence under S. 277, wherein the accused was found guilty of an offence under S. 276CC, it was held that an offence under S. 276CC is different from S.277, and hence the conviction was illegal

Procedure for Prosecution

- Opportunity of Being Heard before launching
 - Act does not provide that the Commissioner has to necessarily afford the assessee an opportunity to be heard before deciding to initiate proceedings.
 - However, it is being observed that the commissioners are issuing a show cause notice before sanctioning the Sanction for prosecution based on the internal manual.

CIT v. Velliappa Textiles Ltd. (2003) 263 ITR 550 (SC) (567 to 569) – Absence of an opportunity to be heard will not make the order of sanction void or illegal as held in

Procedure for Prosecution

- assessee to respond for notice u/s 276CC and 277

Krishnaswami Vijayakumar V. Principal Director of Income Tax [2017] 88 taxmann.com 114 (Madras)

Principal Director (Investigation) is one of the authority enumerated u/s 279(1) of the Act and hence the Show cause issued by him cannot be questioned in a writ petition and the assessee has to respond to the show cause

The Madras HC in above case has distinguished the decision of Supreme Court in Babita Lila V. Union of India in [2016] 73 taxmann.com 32 (SC) on facts, wherein the same deals with jurisdiction after the criminal law was set in motion before the concerned criminal courts.

In the present case of K.Vijaykumar – the Show cause stage is very premature for challenging the jurisdiction

Procedure for Prosecution

- Assessee aged 70 Years and above

As per the instruction No. 5051 of 1991 dt. 7-2-1991 issued by the Board:

“Prosecution need not normally be initiated against a persons who have attained the age of 70 years at the time of commission of the offence”.

Delhi High Court in Pradip Burma v. ITO (2016) 382 ITR 418 (Delhi) (HC) - at the time of commission of offence the petitioner has not reached the age of 70 years, hence the circular was held to be not applicable.

Procedure for Prosecution

- Prosecution is independent of appeal proceedings

Prosecution can be initiated before completion of assessment or when the matter is pending in appeal since the assessment proceedings under Income Tax is independent civil proceedings from that of prosecution for offences committed are tried before a competent court

P. Jayappan v. ITO (1984) 149 ITR 696 (SC)

**Kalluri Krishan Pushkar v Dy. CIT(2016) 236 Taxman 27
(AP& T) (HC)**

Prosecution – In case of Company/Firm/AOP/BOI/HUF

Particulars	section	Individual
Company	278B	Every Person in-charge of affairs: Director, Manager, Secretary and every officer who is guilty of offence
Firm	278B	Partner
AoP or Bol	278B	Member controlling the affairs
HUF	278C	Karta or member either by acquiescence or negligence

Prosecution – In case of Company

Prosecution in case of default by Company:

- Prosecution to be initiated in the name of Director or Principal Officer responsible for TDS compliances.
- The AO has to give notice u/s 2(35) expressing his intention to treat such directors of a company as "principal officers".
- It would be sufficient compliance if in the show-cause notice issued to the company it is mentioned that the directors are to be considered as principal officers of the company.

Delhi High Court in the case of ITO V. Delhi Iron Works (P.) Ltd in [2011] 198 Taxman 174 (Delhi) : Merely because director of a company has been acquitted for non-compliance of notice under section 2(35), that would not mean that company would also be acquitted of charge under section 276B

Prosecution – In case of Company

- A director served with notice u/s 2(35) to treat him as "principal officer", can rebut that he is not the 'Principal officer' in-charge for remittance of TDS.
- However, such director being the chairman of the Board Meeting/CEO, is responsible for day-to-day operations of the Company. Hence shall be treated as 'Principal Officer' despite his denial – as held by **Karnataka High Court in Kingfisher Airlines Ltd V. ITO in [2014] 43 taxmann.com 201 (Karnataka)**

Prosecution – In case of Company

High Court Of Delhi in Income-tax Officer v. Anil Batra [2015] 53 taxmann.com 296 (Delhi) – held that:

“Once offence is shown to have been committed by company, then liability of directors in charge of its affairs is attracted and in such a case, directors cannot be acquitted merely on ground that no separate notices were issued to them especially when they have signed the balance sheet”

Prosecution – In case of Company

Delayed remittance of TDS before detection:

- **Supreme Court in the case of Madhmuilan Syntex Ltd V. Union of India in [2007] 160 Taxman 71 (SC) -**
“Prosecution can be launched in case of delayed remittance of TDS even if *TDS had been deposited to the account of the Central Government - could not be accepted.* “

Relief or Abatement provided under the Act - Section 278AA

Section 278AA: Inbuilt Defence against Prosecution u/s 276A, 276AB and 276B

if an assessee can show a reasonable cause for his failure to comply with the provision of the Act for which prosecution could be launched under section:

- a. 276A [failure to comply with sections 178(1) and 178(3)],
- b. 276AB (failure to comply with sections 269UC, UE and UL) and
- c. 276B (failure to pay tax deducted at source)

then no punishment can be imposed.

Relief or Abatement provided under the Act - Section 279(1A)

Section 279(1A): Inbuilt Defence against Prosecution u/s 276C, and 277

Prosecution u/s. 276C and 277 cannot be initiated if:

the penalty imposed or imposable for concealment of income has been reduced or waived by the Commissioner u/s. 273A.

Relief or Abatement provided under the Act - Section 279(1A)

As per section 279(1A), where penalty has been waived/cancelled u/s 273A, prosecution cannot be launched for the offence u/s 276C or 277.

However, the above restriction is not applicable in cases where penalty was not imposed (eg: penalty not levied in absence of ingredient u/s 271 of the Act)

Where levy of penalty is in appeal, prosecution proceedings should be kept in abeyance (***Prabhava Organics (P) Ltd V. DCIT & Anr. [2008] 297 ITR 0392 (AP); ITO Giggles P Ltd & Ors. [2008] 301 ITR 0032 (Del); Balaji Oil Traders V. ITO [1984] 150 ITR 128 (Kar).***

Relief or Abatement provided under the Act - Compounding

Section 279(2): Power to Compound

Powers given to Chief Commissioner of Income Tax to compound offences under Chapter XXII of the Act

As per section 2(15A) and 2(21) Chief Commissioner includes Principal Chief Commissioner of Income Tax

Compounding can be done either before or after the institution of prosecution proceedings.

Relief or Abatement provided under the Act - Compounding

Section 279(2): Guideline issued by CBDT in respect of Power to Compound dated 23-12-2014

CBDT Issued Instruction No. 1317, dated 11-3-1980, providing guidelines for exercise of the power U/s 279(2)

The same was amended from time to time and the recent guideline issued on 23-12-2014 vide F No.285/35/2013IT(INV), which is applicable w.e.f 01-01-2015

According to Explanation to section 279, the powers of Commissioner in compounding offences should be in conformity with instruction issued by CBDT.

Relief or Abatement provided under the Act - Compounding

Section 279(2): Salient features of Guideline issued by CBDT in respect of Power to Compound:

- Offences u/s. 276, 276B, 276BB, 276D, 276E, and offence u/s 277 and 278 relating to Category A offence are classified as Category 'A' offence
- Offence u/s 275A, 275B, 276, 276A, 276AA, 276AB, 276C, 276CC, 276CCC, 276D, 277A and offence u/s 277, 278 relating to Category B offence are classified as Category 'B' Offence.

Relief or Abatement provided under the Act - Compounding

Section 279(2): Salient features of Guideline issued by CBDT in respect of Power to Compound:

Conditions to be satisfied for compounding an offence.

- a) There should be an application from the assessee in the format specified
- b) The amount of undisputed tax, interest and penalties relating to the default should have been paid.
- c) The assessee undertakes to pay both the prescribed compounding fees as well as establishment expenses.
- d) The Assessee undertakes to withdraw any appeal pending (or modification of respective ground of appeal as the case may be) which is having a bearing on the offence sought to be compounded

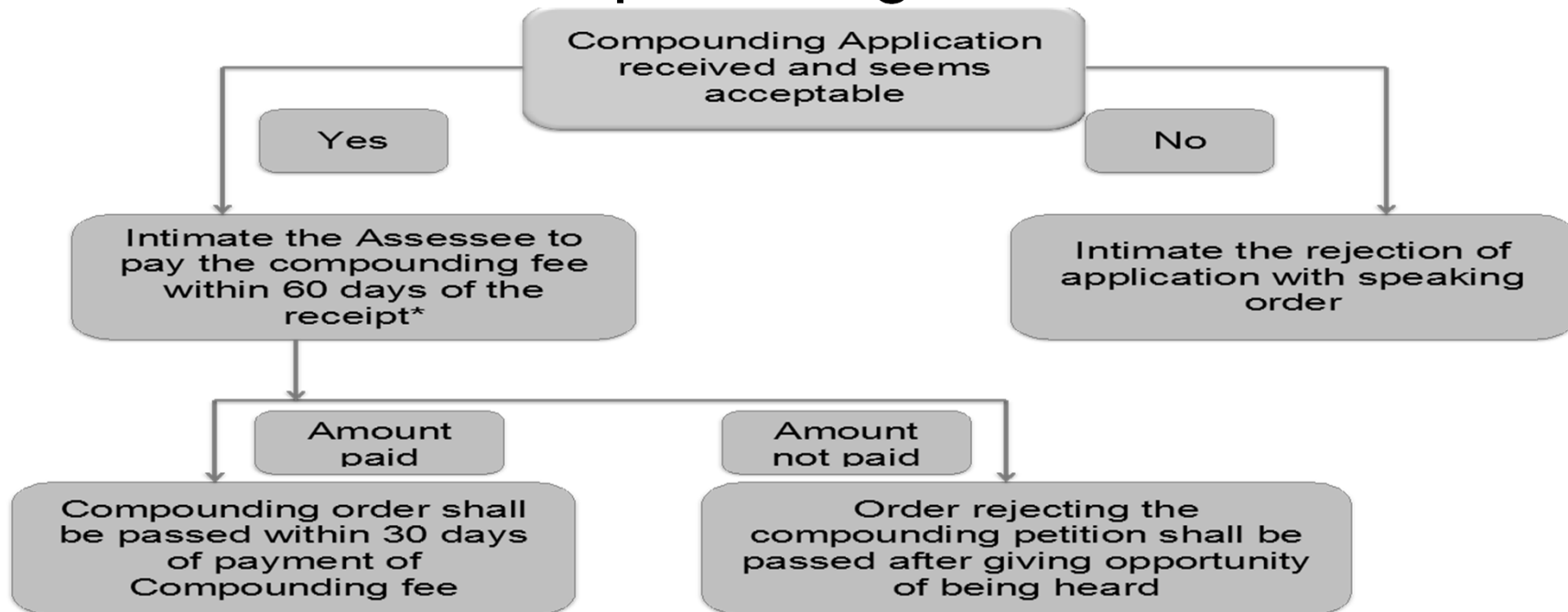
Relief or Abatement provided under the Act - Compounding

Section 279(2): Salient features of Guideline issued by CBDT in respect of Power to Compound: Cont...

Powers to Compound:

Offence specified in Category 'B' involving compounding charges in excess of 10 Lakhs	CCIT on recommendation of a committee of three members : PCIT; DGIT(Inv.); CCIT
Other cases	CCIT

Relief or Abatement provided under the Act - Procedure for Compounding:



*On written request from assessee on exceptional circumstances, period may be extended to 120 days by the CCIT (wherein the assessee is liable to pay additional 2% compounding charge per month /part of a month)

Compounding Fee

Section	Compounding Fee (<u>payable along with legal and administrative expenses</u>)
Sec 276B	3% per month of the amount of tax in default.
Sec 276BB	3% per month of the amount of tax in default.
Sec 276C(1)	100% of the tax amount sought to be evaded
Sec 276C(2)	3% per month of the amount of tax the payment of which is sought to be evaded.
Sec 276CC	2% per month of the assessed tax.
Sec 276CCC	2% per month of the assessed tax.
Sec 276DD	20% of the Loan or deposit accepted in contravention of 269SS
Sec 276E	20% of the Loan or deposit repaid in contravention of 269T

Compounding Fee

Section	Compounding Fee (<u>payable along with legal and administrative expenses</u>)
Sec 277 and Sec 278	<ul style="list-style-type: none"> • 277 and 278 attracted – Shall be treated as single offence for compounding purpose • 276C(1) and 277 attracted – Shall be treated as single offence for compounding purpose • Both 278B / 278C – 10% of the compounding fee of the main offence for each director / partner or more as may be decided by appropriate authority • No other offence under IT Act except in 277 and 278 - Authority may decide
<p><u>Compounding fee shall be payable along with legal and administrative expenses</u></p> <p>No composition fees is prescribed for other offences. However, it has been provided that the Board can consider the same on a case to case basis. The compounding charges shall also include prosecution establishment expenses which will be charged @ 10% of the composition fee subject to a maximum of Rs. 50,000/-.</p>	

Compounding Application

Essential contents of Compounding Application:

- Nature of offence for which prosecution is launched or proposed to be launched;
- Reasons and circumstances under which the offence was committed;
- Applicant's willingness to pay the compounding fees including the part of litigation expenses incurred by the Department till the date of compounding of the offence;
- Whether the applicant satisfies the requisite conditions or not.
- Prayer to compound the offence by accepting the compounding fees as applicable

Compounding Application - Specified format

CBDT has issued a specific format for compounding application as Annexure 1 to the Guidelines issued on 23-12-2013.

Procedure for Compounding

- Compounding powers to be read with orders of CBDT

HIGH COURT OF DELHI in [1998] 231 ITR 755 (DELHI) Dr. K. Jagadeesan v. Central Board of Direct Taxes

CBDT

- The petitioner was convicted and appeal was pending before Sessions Judge.
- The petitioner's effort at directly approaching the CBDT for issuance of order, instruction or direction so as to compound his prosecution was entirely misconceived. No fault could be found with the Board having turned down the petitioner's such attempt.

HIGH COURT OF DELHI in 2008] 173 Taxman 21 (Delhi) Sangeeta Exports (P.) Ltd. V. Union of India

- Commissioner has to exercise discretion under section 279(2) for compounding offences in conformity with instructions issued by Central Board of Direct Taxes (CBDT) under section 119(1) from time to time.
- CBDT rejected the compounding petition and the compounding was rejected when the assessee approached the CCIT.

Compounding after conviction

Madras High Court in [2001] 118 TAXMAN 499 (MAD.) **Income-tax Officer v. Dr. K. Jagadeesan**

- Section 279(2) confers the discretion on the Commissioner to compound any offence.
- The accused had also filed an application for compounding the case wherein the order of the Chief Commissioner in agreeing to compound the case, subject to leave of the Court, was in accordance with law.
- As the offence was compounded, the conviction and the sentence imposed on the accused were liable to be set aside.

Compounding after conviction

Madras High Court in **V.G. Paneerdas & Co. (P.) Ltd. V. Secretary, Central Board of Direct Taxes [2013] 36 taxmann.com 559 (Madras)**

- There is no bar for considering the request of the petitioner for compounding the offence, even if the petitioner had been convicted.
- The petitioner is permitted to submit an appropriate application, before the CCIT, in the format prescribed in the guidelines issued by the CBDT, for the compounding of the offence.

Prosecution under Black Money (undisclosed Foreign Income and Assets) and imposition of Tax Act, 2015

Section 48 :

- Prosecution under Black Money Act is in addition to prosecution under any other law
- It shall be no defence that the order has not been made on account of time limitation or for any other reason.

Prosecution under Black Money (undisclosed Foreign Income and Assets) and imposition of Tax Act, 2015

Section	Offence	Punishment
49	Punishment for failure to furnish return	Rigorous imprisonment - not less than 6 months up-to 7 years
50	Failure to furnish in return, information about assets (including financial interest)	(Bank account balance up-to 5 lakhs is exempted from penalty and imprisonments)
51(1)	<u>Willful attempt to evade</u> any tax, penalty or interest <u>by Resident</u> other than not ordinarily resident in India	<u>Rigorous imprisonment</u> - not less than 3 years up-to 10 years <u>and with fine.</u>
51(2)	<u>Willful attempt to evade</u> any tax, penalty or interest <u>by a person</u>	<u>Rigorous imprisonment</u> - not less than 3 months up-to 3 years <u>And/or with fine at the discretion of the Court.</u>

Prosecution under Black Money (undisclosed Foreign Income and Assets) and imposition of Tax Act, 2015

Section	Offence	Punishment
52	A person makes statement on verification is false and he knows it to be false or not true	<u>Rigorous imprisonment</u> - not less than 6 months up-to 7 years <u>and</u> <u>with fine.</u>
53	Abets or induces another person to make a false statement knowing it to be false or does not believe to be true or commit an offence u/s 51(1) *	<u>Rigorous imprisonment</u> - not less than 6 months up-to 7 years <u>and</u> <u>with fine.</u>

Prosecution under Black Money (undisclosed Foreign Income and Assets) and imposition of Tax Act, 2015

Section	Offence	Punishment
56	<p><u>Offence by a company</u></p> <p>Persons guilty:</p> <ol style="list-style-type: none">1. Company2. every person in charge of, and responsible to the conduct of business*3. Offence committed with the consent of director, manager, secretary or other officer	<p>Company shall be punished with fine</p> <p>Other Persons – shall be punished in accordance with this act</p>

*any such person liable to any punishment proves that the offence was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such offence

Prosecution under Black Money (undisclosed Foreign Income and Assets) and imposition of Tax Act, 2015

Section 58: Second and subsequent offence

If a person is again convicted of an offence for more than once under any of the aforesaid provisions, he shall be punishable for the second and every subsequent offence with rigorous imprisonment for a term which shall not be less than three years, but which may extend to ten years and with fine which shall not be less than five lakh rupees, but which may extend to one crore rupees

Compounding under Black-money Act

"CBDT has made it clear to all the assessment and investigation ranges of the I-T department that the provision of compounding of an overseas tax evasion case under the new anti-black money Act is not to be allowed as the scheme of the Act does not have such a feature,"

Thank You