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Prosecution under Section 276C of Income-tax Act, 1961 – An Overview

By **Ravi Sawana**

Introduction

The mechanism for enforcing tax compliances under the Income-tax Act, 1961 ('the Act') is provided by way of three pillars vis-à-vis imposition of interests, imposition of penalties, and prosecutions. Chapter XXII of the Act contains provisions relating to prosecutions. Amongst other provisions, Section 276C of the Act contains provisions relating to prosecution against "wilful attempt to evade any tax, penalty or interest chargeable or imposable or under-reporting of income or, to evade payment of such tax, penalty or interest".

Analysis of legal provisions

A bare reading of Section 276C of the Act shows that it provides prosecution for wilful attempt to evade the chargeability or imposition or payment of tax, penalty or interest. The said provision is divided in two parts. Sub-section (1) deals with 'wilful attempt' to 'evade' tax, penalty or interest, which is "chargeable" or "imposable" or "under-reporting of income" whereas sub-section (2) deals with 'wilful attempt' to 'evade' 'payment' of tax, penalty or interest. Thus, both the sub-sections deal with two kinds of offences committed at two different points in time by an assessee.

Under sub-section (1), a 'wilful attempt' by an assessee to 'evade' the chargeability or imposition of tax, penalty or interest of an income either by under-reporting of income or non-reporting of income which is achieved either by falsification of books of accounts or non-recording of income, may lead to prosecution. It is germane to note that sub-section (1) lays emphasis on the evasion of tax, etc., before charging or imposition or under reporting of income. In another words, all the acts done by an assessee whereby the income is not offered to tax either due to falsification of books of accounts or non-reporting of income or under reporting of income, etc, would be a punishable offence u/s. 276C(1) of the Act.

Under sub-section (2), a 'wilful attempt' by an assessee to evade the payment of tax either by not paying the due taxes, interest or penalties or claiming excessive relief in the return of income thereby reducing the quantum of taxes payable. In another words, the provisions of sub-section (2) would operate when the payment of tax, penalty or interest is due and an attempt is made to evade such payment.

The basic difference between applicability of sub-section (1) or (2) is the stage at which an offence is committed. If an offence is committed before the stage of filing of return of income, it shall be covered by sub-section (1). Any offence committed at or after the stage of filing of return of income, would be covered by sub-section (2). However, in certain circumstances there may be overlapping between applicability of sub-section (1) and sub-section (2).

Under both the sub-sections to Section 276C of the Act, the first requirement is that the attempt to evade should be 'wilful'. This term has not been defined under the Act. Under common parlance, the word 'wilful' suggests the guilty mind of the assessee. In other words, the assessee has consciously or knowingly

attempted to thwart the chargeability or payment of tax, interest or penalty. Further, such wilful attempt should be to 'evade' chargeability or imposition or payment of tax, etc. The word 'evade' has also not been defined in the Act. As per the Cambridge Dictionary, the word "evade" means "to avoid or escape from someone or something". Further, as per the K.J. Aiyar's Judicial Dictionary, "the word evade is capable of being used in two senses, one which suggest underhand dealing, and another which means nothing more than the intentional avoidance of something disagreeable". Further, the Hon'ble Supreme Court in the case of Tamil Nadu Housing Board, has held that:

"*when the law requires an intention to evade payment of duty then it is not mere failure to pay duty. It must be something more. That is, the assessee must be aware that the duty was leviable and it must deliberately avoid paying it. The word 'evade' in the context means defeating the provisions of law of paying duty. It is made more stringent by use of the word 'intent'. In other words the assessee must deliberately avoid payment of duty which is payable in accordance with law.*"

In view of the aforesaid discussion, if an assessee intentionally commits an act to escape the chargeability or imposition or payment of any tax, penalty or interest, such an act shall be regarded as a wilful attempt to 'evade'. Thus, the law mandates the intentional escapement of chargeability or imposition of tax, etc. or non-payment of taxes due, but would not cover cases of "bonafide claim" or "delay in payment of tax, etc., on account of financial difficulties or similar situations".

Further, Explanation to Section 276C also defines the phrase "wilful attempt to evade any tax, penalty or interest chargeable or imposable under this act or the payment thereof". The explanation appended to the provision provides an illustrative list of cases which can be covered under the said term. Therefore, the explanation is not exhaustive but inclusive in nature and any other circumstance which has not been defined therein but is hit by the rigours of the provisions of Section 276C of the Act, would also be punishable.

However, a question arises as to whether the explanation is applicable to the entire section 276C or is restricted either to sub-section (1) or (2) to the said section? The rules of interpretation of statutes stipulates that where an explanation is appended to a section, it is to explain the meaning of words contained in that section. The meaning to be given to an explanation must depend upon its terms. The explanation has been inserted after sub-section (1) & (2) and starts with the words "for the purpose of this section". One school of interpretation would mean that the said explanation applies to both the sub-sections to Section 276. However, a view may also be taken that the illustrative list of cases contained in the said explanation, suggests that the situations mentioned therein would occur before the stage of filing of return of income and therefore, are relevant only for the purpose of sub-section (1) to Section 276C. Nothing therein has been mentioned to suggests as to what situations can be termed as 'evasion' of payment of tax, interest or penalty. In the case of *G. Viswanathan*, it was held that the explanation is applicable only to sub-section (1) and it does not cover "wilful attempt to evade payment of any tax, penalty or interest" as covered by sub-section (2) to Section 276 of the Act.

Conclusion

Section 276C of the Act provides for prosecution where an assessee has wilfully attempted to evade the chargeability or imposition of tax, penalty or interest or has wilfully attempted to evade the payment of tax,

penalty or interest. Before a prosecution can be launched, it is necessary to show that that act of assessee was wilful as well as to evade the tax, interest or penalty. A *bona fide* claim or financial distress to pay the taxes, are some of the examples which should not be covered by the rigours of Section 276C of the Act.

[The author is a Principal Associate, Direct Tax Team, Lakshmikumaran & Sridharan, Mumbai]

Circular

Non-quoting of Aadhar Number in return filed prior to 1-4-2019: CBDT clarifies

As per Section 139AA of the Income Tax Act, 1961, quoting of Aadhar Number or enrolment application number in case Aadhar number has not be allotted, is mandatory, in application for PAN as well as in return of income. However, in wake of questions over constitutionality of Aadhar and difficulties in complying with this provisions on or after 1-7-2017, many assesses have filed returns without quoting Aadhar. By way of Circular No. 6/2019 dated 31-3-2019, CBDT has clarified that in respect of return field before 1-4-2019 without quoting Aadhar, either because the online facility permitted the same or by following judgements of certain High Courts, no adverse consequence would follow.

Ratio Decidendi

Liability for purchase transaction not covered under 'sum found credited' for purpose of Section 68 (cash credit)

The assessee had bought certain investments from a group concern and the amount was shown as payable in its books. Further the liability was settled by issue of debentures. The tax department sought to add the amount shown in credit in the books as per Section 68 on the ground that the sum presented income of the assessee and the explanation offered by the assessee was not satisfactory. The assessee argued that all particulars of the intra-group transaction of transfer of investment, including identity of parties who were also tax assesses had been shared and also in the absence of any monetary exchange in the transaction, no addition under Section 68 was warranted. Relying on *interalia* the decision of the Special Bench in the case of *Manoj Agarwal v. CIT*, 113 ITD 377 wherein a distinction was drawn between credit of receipt of money and credit of liability of the assessee to state that Section 68 will not be applicable in the latter case, the Tribunal held that the impugned transaction did not fall within the rigours of Section 68. [*Abhijeet Enterprise Ltd.* v. *ITO* - I.T.A. No. 308/Kol/2017, Order of ITAT, Kolkata dated 27-3-2019]

Definition of 'substantially financed' inserted in Section 10(23C) is not retrospective

The assessee trust was formed solely for educational purposes. It had received substantial grants from the government. It had also received certain sums from other sources. The grants received from the government was in excess of 50% of total receipts/ total expenditure, during the year. The Trust treated itself to be 'substantially financed by the government' and accordingly claimed its income to be exempt under Section 10(23C)(iiiab) of the IT Act. The revenue authority however held that, in the absence of a definition of the phrase 'substantially funded by the Government', the phrase has to be understood as per the meaning given in the Comptroller Auditor General's (Duties, Powers and Conditions of Service) Act, 1971 ('CAG Act'). The CAG Act deems any institution which funds more than 75% of its expenditure through government grants as 'substantially financed' by such grants. The revenue authority held that the tax payer was not funded to the extent of 75% of its total expenditure from the Government and consequentially held the tax payer to be in-eligible for exemption under Section 10(23C)(iiiab). On appeal, the High Court held that the scope and purposes of the IT Act is entirely different from the CAG Act and hence, a phrase not defined in the IT Act cannot take its meaning from the CAG Act. Given that the Parliament has subsequently clarified its intention of holding 50% funding as the criteria for determining substantial funding, without holding the subsequent clarification to be retrospective, the High Court interpreted the phrase 'substantially funded' to mean either (a) funding of more than 50% of expenditure, or (b) granting more than 50% of total receipts, by the government as the qualifying criteria, for the purpose of claiming exemption under Section 10(23C)(iiiab) of the IT Act. [*DIT (Exemptions)* v. *Tata Institute of Social Sciences* - 1179 of 2013, decision dated 26th March 2019, High Court of Bombay]

Deduction under Section 80P allowable to a credit cooperative society even if loans are given to associate members

The assessee, a primary agricultural credit cooperative society registered under the Tamil Nadu Cooperative Societies Act, 1983 (the TNCS Act) claimed portion of its income as deduction under Section 80P(2)(a)(i) and 80P(2)(d) of the IT Act. The revenue authority observed that the 'associate members' of the Society did not have right to vote or dividend in the Society and hence, the income earned from them was ineligible for deduction under Section 80P of the IT Act. On appeal, the High Court held TNCS Act permits a borrower to be an 'associate member' in a lender society and when the governing statute recognises such borrowers as members, the Revenue Authorities cannot disregard the privilege granted under the TNSC Act. The High Court also observed that the judgment of the Supreme Court in the case of *Citizen Cooperative Society Limited* [2017] 397 ITR 1 (SC)] was rendered in the context of lending of money in a manner contrary to the States Cooperative Societies Act and hence would not apply to the facts of the Tax Payer. [*PCIT* v. *Ammapet Primary Agricultural Cooperative Bank Ltd*. - 882 & 891 of 2018, decision dated 6th December 2018, High Court of Madras]

TPO can determine ALP of 'specified domestic transactions' only if the transaction is referred to him by AO

The Tax Payer had demerged one of its business undertakings into its holding company. It also reported certain specified domestic transactions ('SDT') in Form 3CEB. The Assessing Officer

('AO') made a reference to the Transfer Pricing Officer ('TPO') in respect of the SDTs reported in Form 3CEB. The TPO, in the course of proceedings before him noted that there were certain other SDTs not reported by the Tax Payer and sought to determine the Arm's Length Price of such SDTs not referred to him. On a writ petition, the High Court observed that Section 92CA(2A) and (3A) of the IT Act which permits the TPO to determine ALP of transactions not referred to him, will apply only to international transactions and not to SDT. The High Court held that sub-section 92(3A) and the provisions relating to determination of SDT were inserted by Finance Act, 2012, and had the Legislature thought it necessary, they could have included a reference to SDT's in the sub-section. The High Court accordingly held that it would not be open to the TPO to exercise his powers to determine ALP without a reference made to him by the AO. [*Times Global Broadcasting Co. Ltd.* v. *Union of India* - [2019] 103 taxmann.com 388 (Bombay)]

Tax to be deducted on salary paid to missionaries and nuns surrendered to religious institutions: Income not diverted at source

In a writ filed by the Union of India, the High Court has held that Section 192 of the Income-tax Act has nothing to do with religious character of teachers who are paid such salary by the State in form of Grant-in-Aid. The State Government provided Grant-in-Aid to schools wherein certain nuns, sisters and priests were teachers. The teachers claimed that they are bound by their canon law to vows of poverty to the Christ, and thus, having renounced the world, they have suffered a civil death and thus cannot be subject to tax deduction at source. The issue arose since the mode of payment by the State changed from a lump sum payment to the educational institution to direct transfer to the beneficiaries account, from which the Department instructed the authorities of the State Government to deduct tax. The Court held that the salaries received by the missionaries, although belonging to the Church, were only an application of income and not in the nature of diversion of income by overriding title. The 'vows of poverty' taken by the missionaries would not alter the taxability of the receipts as salary. The Court observed that operation of TDS provisions of the Act is uniform and not affected by the religious character of the recipient of the income. The Court, thus upheld the instructions of the Union Government to the State Government to deduct tax at source from the payments made by way of salary or pensions to members of religious congregations. [*Union of India* v. *Society of Mary Immaculate (Tamil Nadu), Madras* - [2019] 103 taxmann.com 333 (Madras)]

NEW DELHI
5 Link Road, Jangpura Extension,
Opp. Jangpura Metro Station,
New Delhi 110014
Phone : +91-11-4129 9811

B-6/10, Safdarjung Enclave
New Delhi -110 029
Phone : +91-11-4129 9900
E-mail : lsdel@lakshmisri.com

MUMBAI
2nd floor, B&C Wing,
Cnergy IT Park, Appa Saheb Marathe Marg,
(Near Century Bazar)Prabhadevi,
Mumbai - 400025
Phone : +91-22-24392500
E-mail : lsbom@lakshmisri.com

CHENNAI
2, Wallace Garden, 2nd Street
Chennai - 600 006
Phone : +91-44-2833 4700
E-mail : lsmds@lakshmisri.com

BENGALURU
4th floor, World Trade Center
Brigade Gateway Campus
26/1, Dr. Rajkumar Road,
Malleswaram West, Bangalore-560 055.
Ph: +91(80) 49331800
Fax:+91(80) 49331899
E-mail : lsblr@lakshmisri.com

HYDERABAD
'Hastigiri', 5-9-163, Chapel Road
Opp. Methodist Church,
Nampally
Hyderabad - 500 001
Phone : +91-40-2323 4924
E-mail :lshyd@lakshmisri.com

AHMEDABAD
B-334, SAKAR-VII,
Nehru Bridge Corner, Ashram Road,
Ahmedabad - 380 009
Phone : +91-79-4001 4500
E-mail : lsahd@lakshmisri.com

PUNE
607-609, Nucleus, 1 Church Road,
Camp, Pune-411 001.
Phone : +91-20-6680 1900
E-mail :lspune@lakshmisri.com

KOLKATA
2nd Floor, Kanak Building
41, Chowringhee Road,
Kolkatta-700071
Phone : +91-33-4005 5570
E-mail : lskolkata@lakshmisri.com

CHANDIGARH
1st Floor, SCO No. 59,
Sector 26,
Chandigarh -160026
Phone : +91-172-4921700
E-mail :lschd@lakshmisri.com

GURGAON
OS2 & OS3, 5th floor,
Corporate Office Tower,
Ambience Island,
Sector 25-A,
Gurgaon-122001
phone: +91-0124 - 477 1300
Email: lsgurgaon@lakshmisri.com

ALLAHABAD
3/1A/3, (opposite Auto Sales),
Colvin Road, (Lohia Marg),
Allahabad -211001 (U.R)
phone . +91-0532 - 2421037, 2420359
Email:lsallahabad@lakshmisri.com