

# TAX FLASH NEWS

7 January 2020

## Prosecution proceedings can be initiated on a company for failure to deposit tax deducted at source

### Background

Recently, the Karnataka High Court in the case of Dr. Viloo Patell (Managing director of Avesthagen Limited) and Avesthagen Limited<sup>1</sup> (petitioners/taxpayers) dealt with the issue of initiation of prosecution proceedings under Section 276B of the Income-tax Act, 1961 (the Act) for failure to deposit tax deducted at source with the Government. The High Court dismissed the writ petition filed by the taxpayers against the prosecution proceedings initiated by the tax department on company for failure to deposit tax deducted at source.

### Facts of the case

During the Financial Year (FY) 2010-2011 and 2011-2012, the taxpayer, a company, failed to deposit tax deducted at source. The taxpayers were prosecuted under Section 276B of the Act for such failure.

The taxpayers filed writ petition on the following grounds:

- A show-cause notice was issued in respect of nine companies whereas the prosecution is launched only against taxpayers which was legally untenable.
- The company is a juristic person and in terms of Section 2(35) of the Act, notice is required to be issued to each of companies individually and not composite notice. Thus the prosecution launched against the petitioners suffers from basic vice.
- Further the show-cause notice was issued only to individual taxpayer being a managing director and not to the company, and hence the prosecution

launched against the taxpayers were defective and contrary to Section 276 of the Act.

- Section 276B of the Act was applied without application of mind. Tax deducted at source by the taxpayers was remitted much earlier to the issuance of sanction order, which fact is not reflected in the sanction order indicating that the sanction order has been issued without application of mind and thus the impugned proceedings are liable to be quashed.
- The section provides for mandatory term of imprisonment coupled with fine in respect of the offences committed by a company. The Supreme Court in the case of Velliappa Textiles Ltd<sup>2</sup> observed that no criminal prosecution could be sustained for the offences under Sections 276, 277 and 278 of the Act when the offences are rendered punishable with fine and imprisonment.

### High Court decision

- The notice was not issued as a show-cause notice preceding adjudication or the prosecution rather it was issued to the chairman and managing director of the group companies. Captioned subject of the said notice was to keep the managing director informed and to treat him as the principal officer of the company.
- The said notice was issued to convey the intention of the tax department to treat him as the principal officer of the above companies. It is not a show-cause notice. On the other hand, in the complaint, it is specifically stated that show-cause notice was issued to taxpayer on 14 August 2013. The taxpayer has not referred to the said document.

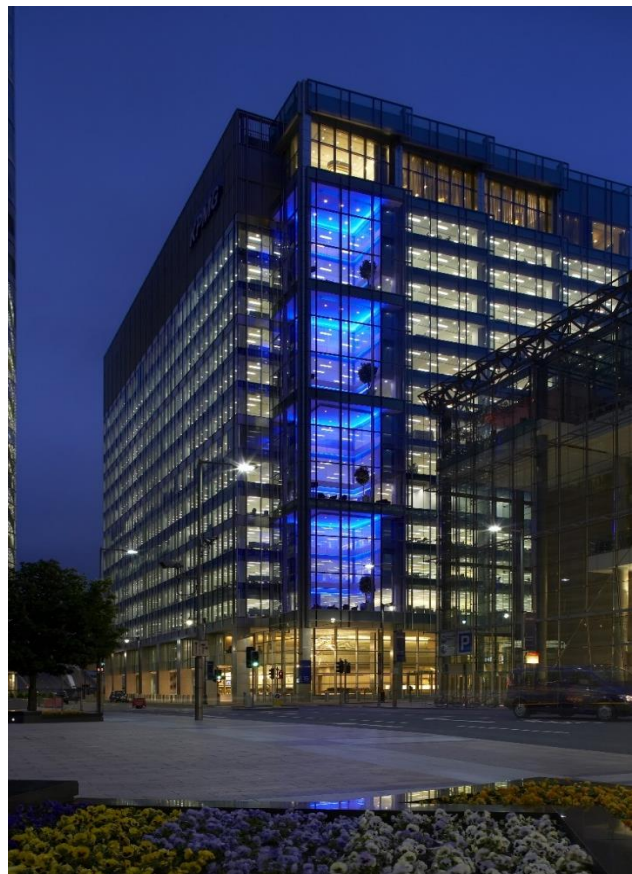
<sup>1</sup> Dr. Viloo Patell and Avesthagen Limited (Writ Petition No. 47514 of 2017, 6 September 2019) – Taxsutra.com

<sup>2</sup> ACIT v. Velliappa Textiles Ltd & Another [AIR 2004 SC 86]

- Thus, the contentions of the taxpayers were totally misconceived and cannot be a ground to quash the proceedings
- The taxpayer contended that a joint notice was issued to all the companies; but it is not so. Order passed under section 201(1) and 201(1A) of the Act makes it evident that the order was passed only against taxpayer company and not against all the companies
- With respect to sanction order, it was observed that an opportunity was given to the taxpayer in default to make the payment. Under the said circumstances, if any amount was paid pursuant to the said show cause notice, the proof thereof could have been produced by taxpayers so as to avoid criminal prosecution. There was nothing on record to show that the remittances made by taxpayers have been brought to the notice of the central government. Thus, the sanction order did not reflect any errors warranting interference by the Court.
- Taxpayer contended that since the section provides for mandatory imprisonment coupled with fine, no criminal prosecution could be sustained as the company cannot be sentenced to imprisonment. The High Court observed that the contention is no more res integra in view of the decision of the Constitution Bench of the Supreme Court in the case of Standard Chartered Bank<sup>3</sup>. The Supreme Court while overruling the decision in Velliappa Textiles Ltd, held that there was no immunity to the companies from prosecution merely because the prosecution was in respect of offences for which the punishment prescribed was mandatory imprisonment.

dismissed the writ petition filed by the taxpayers against prosecution proceedings initiated by the tax department on the company for failure to deposit tax deducted at source.

Therefore, companies should examine whether they have complied with the TDS provisions and deposited tax appropriately to the government's account to avoid any prosecution proceedings.



## Our comments

The issue with respect to the initiation of prosecution proceedings under Section 276B on a company for failure to deposit tax deducted at source has been a subject matter of debate before the Courts.

The Supreme Court in the case of Velliappa Textiles Ltd observed that no criminal prosecution could be sustained for the offences under Sections 276, 277 and 278 of the Act when the offences are rendered punishable with fine and imprisonment.

However, the Constitution Bench of the Supreme Court in the case of Standard Chartered Bank overruled the decision in Velliappa Textiles Ltd and held that there was no immunity to the companies from prosecution merely because the prosecution was in respect of offences for which the punishment prescribed was mandatory imprisonment.

The High Court in the present case relied on the Supreme Court decision in the case of Standard Chartered Bank and on the basis of facts of the case

<sup>3</sup> Standard Chartered Bank v. Directorate of Enforcement [2005] 145 Taxman 154 (SC)

#### **Ahmedabad**

Commerce House V, 9th Floor,  
902, Near Vodafone House,  
Corporate Road,  
Pralhad Nagar,  
Ahmedabad – 380 051.  
Tel: +91 79 4040 2200

#### **Bengaluru**

Embassy Golf Links Business Park,  
Pebble Beach, 'B' Block,  
1st & 2nd Floor,  
Off Intermediate Ring Road,  
Bengaluru – 560071  
Tel: +91 80 6833 5000

#### **Chandigarh**

SCO 22-23 (1st Floor),  
Sector 8C, Madhya Marg,  
Chandigarh – 160 009.  
Tel: +91 172 664 4000

#### **Chennai**

KRM Towers, Ground Floor,  
1, 2 & 3 Floor, Harrington Road,  
Chetpet, Chennai – 600 031.  
Tel: +91 44 3914 5000

#### **Gurugram**

Building No.10, 8th Floor,  
DLF Cyber City, Phase II,  
Gurugram, Haryana – 122 002.  
Tel: +91 124 307 4000

#### **Hyderabad**

Salarpuria Knowledge City,  
6th Floor, Unit 3, Phase III,  
Sy No. 83/1, Plot No 2,  
Serilingampally Mandal,  
Ranga Reddy District,  
Hyderabad – 500 081.  
Tel: +91 40 6111 6000

#### **Jaipur**

Regus Radiant Centre Pvt Ltd.,  
Level 6, Jaipur Centre Mall,  
B2 By pass Tonk Road,  
Jaipur – 302 018.  
Tel: +91 141 - 7103224

#### **Kochi**

Syama Business Centre,  
3rd Floor, NH By Pass Road,  
Vytilla, Kochi – 682 019.  
Tel: +91 484 302 5600

#### **Kolkata**

Unit No. 604,  
6th Floor, Tower – 1,  
Godrej Waterside,  
Sector – V, Salt Lake,  
Kolkata – 700 091.  
Tel: +91 33 4403 4000

#### **Mumbai**

1st Floor, Lodha Excelus,  
Apollo Mills,  
N. M. Joshi Marg,  
Mahalaxmi,  
Mumbai – 400 011.  
Tel: +91 22 3989 6000

#### **Noida**

Unit No. 501, 5th Floor,  
Advant Navis Business Park,  
Tower-A, Plot# 7, Sector 142,  
Expressway Noida,  
Gautam Budh Nagar,  
Noida – 201 305.  
Tel: +91 0120 386 8000

#### **Pune**

9th floor, Business Plaza,  
Westin Hotel Campus, 36/3-B,  
Koregaon Park Annex,  
Mundhwa Road, Ghorpadi,  
Pune – 411 001.  
Tel: +91 20 6747 7000

#### **Vadodara**

Ocean Building, 303, 3rd Floor,  
Beside Center Square Mall,  
Opp. Vadodara Central Mall,  
Dr. Vikram Sarabhai Marg,  
Vadodara – 390 023.  
Tel: +91 265 619 4200

#### **Vijayawada**

Door No. 54-15-18E,  
Sai Odyssey,  
Gurunanak Nagar Road, NH 5,  
Opp. Executive Club, Vijayawada,  
Krishna District,  
Andhra Pradesh – 520 008.  
Tel: +91 0866 669 1000