



PENALTY FOR UNDER REPORTING AND MISREPORTING OF INCOME – SECTION 270A – NEW PENALTY PROVISIONS INTRODUCED BY FINANCE ACT, 2016

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1. Introduction

The provisions of Section 271(1) providing for penalty on concealment of Income and/or furnishing inaccurate particulars of Income has been in the statute book for more than 56 years. Major legal issues arising in penalty proceedings have to a greater extent been settled and practically it was this settled law which had to be applied to the facts of each case. Yet due to almost automatic initiation and consequent levy of penalty by Assessing Officers for additions or disallowances made under scrutiny assessment had given rise to proliferation of litigation. In *CIT v. Reliance Petro Products 322 ITR 158*, the Supreme Court stated: "If we accept the contention of the revenue then in case of every return where the claim made is not accepted by the Assessing Officer for any reason, the assessee will invite penalty under Section 271(1)(c). That is clearly not the intendment of the legislature".

Hence in view of the fact that several legal issues stood concluded and in order to cut wasteful litigation and also infuse a sense of responsibility and accountability both upon the tax-payer and the revenue the Income Tax Simplification Committee headed by Justice R. V. Easwar in the year 2015 recommended that the scope of Section 273B should be suitably enlarged to provide that penalty for concealment of income or furnishing inaccurate particulars thereof will not be imposed where any addition or disallowance is made without any evidence or in a routine manner or on estimate and in cases where the Assessing Officer takes a view which is different from the *bona fide* view adopted by the assessee on any issue involving the interpretation of any provision of the Income- tax Act or any other law in force and which is supported by any judicial ruling.

However, instead of implementing the recommendation, the Finance Act, 2016 effectively replaces Section 271 by inserting a new Section 270A under Chapter XXI which provides for penalty on under-reporting of income and misreporting of income. Hence, from AY 2017-18 there will be no penalty for concealment of income or furnishing inaccurate particulars of income u/s. 271(1)(c) but there will be penalty for under-reporting of income and misreporting of income. According to the memorandum to the Finance Bill this amendment is done in order to rationalise and bring objectivity, certainty and clarity in the penalty provisions.

Whether the new provisions achieve the desired object or it is simply a case of unsettling settled laws resulting in more litigation or it is just an old wine in new bottle will be unearthed as we look at the provisions and analyse them hereinafter.

2. Scheme of Section 270A

Under the new section, the cases for levying penalty have been bifurcated as under-reporting of income and misreporting of income. Provisions of the section are explained hereunder:

A. The AO/CIT(A)/CIT/ Pr. CIT may, during the course of any proceedings under this Act, may, during the course of any proceedings under this Act, direct that any person who has under-reported his income shall be liable to pay a penalty in addition to tax, if any on the unreported income. [Sub-section (1)]

It may be noted that the Finance Bill did not contain the phrase "during the course of any proceedings under this Act". This led to the issue whether penalty proceedings can now be initiated after the completion of the assessment proceedings or independent of assessment proceedings or as under Section 271 they will have to be initiated during the course of assessment proceedings itself. The addition of this phrase has settled this issue. Further implications of this phrase are analysed in later portion of this article.

B. As per sub-Section (2), in following cases a person shall be considered to have under-reported his income:

In case of normal assessment

- (i) The income assessed is greater than the income determined in the return processed under clause (a) of sub-Section (1) of section 143;
- (ii) Where no return of income has been furnished, the income assessed is greater than the maximum amount not chargeable to tax;

In case of reassessment

- (iii) The income reassessed is greater than the income assessed or reassessed immediately before such re-assessment;

In case where income is assessed under 115JB/ 115JC. [MAT/AMT]

- (iv) The amount of deemed total income assessed or reassessed as per MAT/AMT is greater than the deemed total income determined u/s.143(1)(a)
- (v) Where no return of income has been filed, the amount of deemed total income assessed as per MAT/AMT is greater than the maximum amount not chargeable to tax,;
- (vi) The amount of deemed total income reassessed as per the provisions of section MAT/AMT is greater than the deemed total income assessed or reassessed immediately before such reassessment. [This provision was not there in the Finance Bill.]

In case where returned loss is reduced or converted into income

- (vii) The income assessed or reassessed has the effect of reducing the loss or converting such loss into income.

Thus, essentially under-reported income will not cover the difference between returned income and income determined u/s 143(1)(a) and consequently no penalty will be levied on

the same. It would be important to note that From AY 2017-18 apart from (i) arithmetical error. and (ii) incorrect claim apparent from the return following adjustments will also form part of S.143(1)(a):

- (i) Disallowance of set off of loss where return is filed beyond due date.
- (ii) Disallowance of deduction where return is filed beyond due date.
- (iii) Form 26AS or Form 16A or Form 16 adjustments.

**C. Amount of under-reported income or computation of under-reported income.
[Sub-section(3)]**

<p>In a case where return is furnished and assessment is made for the first time. [Eg.- (Assessment order u/s 143(3))]</p>	<p>The amount of under reported income in case of all persons shall be the difference between the assessed income and the income determined under section 143(1)(a). Thus adjustments made while determining income u/s 143(1)(a) will not be considered as under-reported Income.</p>
<p>In a case where no return has been furnished and the income has been assessed for the first time.</p>	<p>The amount of under-reported income is proposed to be: For a company, firm or local authority, the assessed income; For a person other than company, firm or local authority, the difference between the assessed income and the maximum amount not chargeable to tax.</p>
<p>In case of any person, where income is not assessed for the first time. [Eg- Order u/s 147 r/w 143(3), etc.]</p>	<p>The amount of under reported income shall be the difference between the income reassessed or recomputed and the amount of income assessed, reassessed or recomputed in a preceding order. As per Explanation (a) to sub-section (3) "preceding order" means an order immediately preceding the order during the course of which the penalty under sub-section (1) has been initiated. Hence preceding order could be an order u/s 143(3), 147, 254 r.w 143(3), 263 r.w. 143(3) etc.</p>
<p>Where under reported income arises out of determination of deemed total income in accordance with the provisions of section 115JB or section 115JC,</p>	<p>The amount of total under reported income shall be determined in accordance with the following formula- $(A - B) + (C - D)$ where, A = Income assessed as per normal provision. B = Income assessed as per normal provision (-) Under reported Income C = the total income assessed as per the provisions contained in section 115JB or section 115JC;</p>

	<p>D = the total income that would have been chargeable had the total income assessed as per the provisions contained in section 115JB or section 115JC been reduced by the amount of under reported income.</p> <p>However, where the amount of under reported income on any issue is considered both under the provisions contained in section 115JB or section 115JC and under general provisions, such amount shall not be reduced from total income assessed while determining the amount under item D. [A very common example will be disallowance u/s 14A]</p>
<p>Where an assessment or reassessment has the effect of reducing the loss declared in the return or converting that loss into income.</p>	<p>The amount of under reported income shall be the difference between the loss claimed and the income or loss, as the case may be, assessed or reassessed.</p> <p>Here, due to the use of the phrase “loss claimed” an issue will arise whether under-reported income will be the difference between returned loss and assessed income/loss or it will be difference between loss determined u/s 143(1)(a) and assessed income /loss. This issue is explained in the illustration given hereinafter.</p>

D. Exclusion from under-reported Income i.e. the under-reported income for the purposes of section 270A shall not include (Sub-section (6))

Explanation is offered

- a) Where the assessee offers an explanation and the income-tax authority is satisfied that the explanation is bona fide and all the material facts have been disclosed;

[This provision is substantially similar to Explanation B to s.271(1)(c).]

Estimated Income

- b) Where such under-reported income is determined on the basis of an estimate, if the accounts are correct and complete to the satisfaction of the assessing authority, but the method employed is such that the income cannot properly be deducted therefrom;

[Eg- G.P. is enhanced or ad-hoc disallowance of expenditure etc without rejecting books of accounts.]

- c) Where the assessee has, on his own, estimated a lower amount of addition or disallowance on the issue and has included such amount in the computation of his income and disclosed all the facts material to the addition or disallowance;

[Eg- disallowance u/s 14A]

Transfer Pricing

- d) Where the assessee had maintained information and documents as prescribed under section 92D, declared the international transaction under Chapter X and disclosed all the material facts relating to the transaction;

Search

- e) Where the undisclosed income is on account of a search operation and penalty is leviable under section 271AAB

E. Under-reported income is on account of misreporting [Sub-section (8) and (9)]

Where the under-reporting is because of misreporting than provision of sub-section(6) [exclusions from under-reported income] shall not apply.

The cases of **Misreporting** are as under:

- a) Misrepresentation or **suppression** of facts;
 - An issue will arise as to the meaning and scope of the terms misrepresentation and suppression.
- b) Failure to record investments in the books of account;
- c) Claim of expenditure not substantiated by any evidence;
 - An issue may arise as to the implication of the word "any".
- d) Recording of any **false** entry in the books of account;
- e) Failure to record any receipt in books of account having a bearing on total income; and
- f) Failure to report any international transaction or any transaction deemed to be an international transaction or any specified domestic transaction, to which the provisions of Chapter X apply.

F. Rate of penalty and Tax Payable. [Sub-Section (7), sub-Section (8) and sub-section (10)]

In case of under-reporting of income – 50% of tax payable on under-reported income.

In case of misreporting – 200% of tax payable on under-reported income.

As per the Finance Bill, Tax payable in respect of the under-reported income shall be the amount of tax calculated [sub-section (10)]:

- i. In case of company, firm or local authority – on such income as if such income were the total income
- ii. In other case – 30% of the amount of under-reported income.
- Thus, slab benefit was not available.

As per the Finance Act, Tax Payable is as under :

Return not filed and income assessed for	Tax calculated on (under-reporting of income + basic exemption)
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the first time	[Slab benefits available]
Total income as per immediate prior order/ where intimation is a loss.	Tax calculated on under-reported income as if it were the total income. [Slab benefits available, Loss can't be set off against under-reported income.]
Other cases	X – Y X - Tax calculated on (Under reported income + Income as per immediate prior order/intimation) Y - Tax on Income as per immediate prior order/ intimation. [Virtually tax on under-reported income but with slab benefits]

How S.270A will be implemented

Thus, first step will be to identify whether there is under-reported income in terms of sub-section (2) and sub-section (3). If there is under-reported income then the second step will be to identify which additions or disallowances constituting under-reported income are additions or disallowances which are on account of misreporting. Thereafter the third step would be to apply sub-section (6) to additions or disallowances to which misreporting does not apply and calculate total under-reported income and total misreporting income. Then calculate tax payable on under-reported income(without misreporting) and apply requisite penalty rate and calculate penalty amount. Then calculate tax payable on under-reported income(on account of misreporting) and apply requisite penalty rate and calculate penalty amount.

G. Under-reported income in a case where the source of any receipt, deposit or investment is linked to earlier year. [Sub-Section (4), and Sub-Section(5)].

Section 270A(4) is somewhat similar to erstwhile explanation 2 to section 271(1) and provides that where the source of any receipt, deposit or investment in any assessment year is claimed to be an amount added to income or deducted while computing loss, as the case may be, in any preceding assessment year and no penalty was levied in such preceding assessment year then, the under-reported income shall include such amount as is sufficient to cover such receipt, deposit or investment. Further, section 270A(5) specifies that the amount for the purpose of sub-section (4) shall firstly be from the immediately preceding assessment year and then from the year preceding that and so on.

PARTICULARS	SITUATION 1	SITUATION 2
Addition of suppressed sale in :		
AY 2014-2015	60	60
AY 2015-2016	30	30

AY 2016-2017	20	20
Investment in AY 2017-2018 claimed out of above addition.	10	90
Under-reported income of each year	AY 16-17 – 10	AY 16-17 – 20 AY 15-16 – 30 AY 14-15 – 50

H. No addition or disallowance of an amount shall form the basis for imposition of penalty, if such addition or disallowance has formed the basis of imposition of penalty in the case of the person for the same or any other assessment year. [Sub-section (11)]

I. The order imposing penalty under section 270A should be in writing [Sub-section (12)]

3. Illustrations [Kindly refer the Section]

ILLUSTRATION 1	
Returned Income	100 [14A disallowance Rs 5]
STEP 1 – 143(1)(a)- adj [` 20]	120 [100 + 20]
STEP 2 – 143(3) – 14A[ESTIMATE] ` 10 – Foreign Travel ` 10 – Miscellaneous ` 5	145 [120+ 25]
STEP 3 – SUB-SECTION (2)	145 > 120
STEP 4 – SUB-SECTION (3)(i) – Under-reported Income	25 [145-120]
STEP 5 – SUB-SECTION(6) and (9) – EXCLUSION and MISREPORTING – 14A. [EXCLUDED] – FT [NOT EXCLUDED] – Miscellaneous [MISREPORTING] – HENCE, Under-reported Income	15 [25-10]
STEP 6 – SUB-SECTION(10) – TAX PAYABLE (TP)	

<p>X - 15+120 = 135</p> <p>Y - 120</p> <p>X-Y - 15</p> <p>Tax</p>	<p>4.5 (30%)</p>
<p>STEP 7 PENALTY[SUB-SECTION(7)&(8)</p> <p>Bifurcation of tax payable on UI and M is implicit.</p> <p>Hence, On 10 TP will be 3. Penalty@50%</p> <p>On 5 TP will be 1.5. Penalty @200%</p> <p>Total Penalty</p>	<p>1.5</p> <p>3</p> <p>4.5</p>

ILLUSTRATION 2	
143(3)	145
ADD – BOGUS PURCHASES U/S 37	50
Income reassessed u/s 147	195[145 +50]
Sub-Section (2)(b)	195>145
Sub-Section (3)(ii)-Underreported Income	50[195-145]
Where Only notices not served etc	<p>Issue will be between Sub-Section (6) [Exclusion] v. Sub-section (9)[Misreporting]</p> <p>For misreporting issue will be between Sub-Section(9)(a)[Misrepresentatio] v/s (9)(b) [Any evidence]</p>
OTHER CONSEQUENCES SAME AS ILLUSTRATION 1.	

ILLUSTRATION 3 [LOSS]	
RI	(20)
143(1)(a)	(10)

143(3)	10
Sub-Section (2)(g)	Attracted.
SUB-SECTION (3) As per Sub-Section(3)(i)(a)[Scenario 1] As per Explanation(b) – [Loss Claimed interpretation][Scenario 2] [Results in UI being difference between 143(1)(a) and RI.]	20 [10 –(-10)] 30 [10 –(-20)]
SUB-SECTION(10) Sub-Section(10)(b) is attracted Sub-Section (10)(c) is attracted. Scenario 1 X - 20 + (10)= 10 Y – (10) X-Y – 20.	Either 20 or 30. Scenario 2 X – 30 + (10) = 20 Y - (10) X-Y – 30.

ILLUSTRATION 4[Book Profits]		
	RI	BP
AMOUNT	50 (tax @15)	200 (Tax@37)
143(1)(a)	100 (tax @30)	200
143(3)	150 (tax@45)	225(Tax@41.62)

Scenario 1 – Only Sub-section 2 (a) and sub-Section (3)(i)(a) is applicable and proviso is not applicable as Income is assessed under normal provisions. UI 50 Tax 15 Penalty 7.5 Hence, no penalty on adjustment	Scenario 2 – Sub-Section 2(a) and (d) are attracted Sub-Section (3)(i)(a) and proviso are attracted. UI A-B + C-D = 150-100 + 225-200 = 75. Hence, penalty on both will be levied. Tax – X – Y
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<p>under S.115JB.</p>	<p>$X = UI + 143(1)(a) = 75 + 200$ $Y = 200$ $X - Y = 75.$ Tax – 30% on 50 and 18.5% on 25. [Any other interpretation will make the provisions unworkable] Penalty – Depending on whether adjustments are classified as Misreporting or not.</p>
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4. Analysis of Section 270A

(i) Meaning/Definition – Exhaustive or inclusive

The Income tax act does-not define the terms “under-report” or “misreporting”. It merely gives instances which will constitute misreporting (Sub-section (9)) and which will not constitute under-reporting (sub-section (6)). Hence, for the purposes of interpretation and deciding various legal issues which will crop up it is necessary to find out the ordinary or dictionary meaning.

ORDINARY MEANING

UNDER-REPORT

- THE FREEDICTIONARY – To report as less or fewer than is correct.
- CAMBRIDGE DICTIONARY – To record that you have earned less than you really have on your tax return.
- MERRIAM WEBSTER – To report to be less than is actually the case.
- OXFORD DICTIONARY – Fail to report (something) fully.
- Thus, the ordinary meaning does suggest some sort of deliberate attempt to Under-report income.

MISREPORTING

ORDINARY MEANING

- OXFORD DICTIONARY – Give a false or inaccurate account of (something), A false or incorrect report.
- THE FREEDICTIONARY – To report falsely or inaccurately, an inaccurate or false report/ to report mistakenly or falsely, An inaccurate or wrong report.

The term falsity is defined as wrong and untruthful assertion of a fact known to the person. The term failure is defined as the neglect or omission of expected or required action.

- Thus, the term misreporting clearly represents existence of a guilty mind on the part of the assessee.

MEANING AS PER THE SCHEME OF SECTION 270A

UNDER-REPORT.

- Under the provisions of section 270A a difference has to be made between the terms "Under-reported his Income" and "Under-reported Income".
- As per Sub-Section (1) person is liable to penalty when that person has under-reported his income. Sub-section (2) lays down cases when a person shall be considered to have under-reported his income. It lays down six cases which essentially refer to cases where an assessment takes place and there is an addition or disallowance. The cases to a great extent manifest the ordinary meaning of the term "Under-report". Sub-section (2) is exhaustive.
- Once sub-section (2) is triggered then the amount of under-reported income is to be computed under sub-section (3) which essentially is the difference between assessed income and income as per intimation or reassessed income and assessed income. This is the under-reported income of the person. This under-reported income computed under sub-section (3) is to be further adjusted by reducing those additions / disallowances which satisfy the conditions of sub-section (6). Thus, sub-section (6) gives the "Under-reported Income" on which penalty would be finally levied.
- The sub-section (6) gives five scenarios when a particular addition /disallowance or amount of income will not form part of Under-reported Income computed under sub-section (3). Sub-section (6) uses the term "shall not include". The Apex Court in *Narpatchand A Bhandari v. Shantilal Moolshankar Jain AIR 1993 SC 1712* was considering the scope of definition of landlord in the Explanation to Section 13(1)(g) which stated that Landlord **will not include** a rent-farmer or rent collector or estate manager. The Apex court held that a mortgagee with possession would qualify as a landlord as it is not specifically excluded. Thus, scenarios which are not specifically excluded by sub-section (6) would be scenarios where penalty would be imposed. **Thus, the exclusion under sub-section(6) is exhaustive.** The exhaustive nature of sub-section(2) and sub-section(6) are in line with the object of bringing clarity in penalty provisions which was lacking in the erstwhile section 271.
- However on must note that Sub-clause(a) of Sub-section(6) is a general/universal clause which will help assessee to raise all bonafide defences against levy of penalty.

MISREPORT

As per sub-section (8) of section 270A if under-reporting is in consequence of misreporting then the exclusions provided in sub-section (6) will not apply. Further sub-section (9) gives six cases of mis-reporting. These cases are manifestation of the ordinary meaning of misreporting in the context of Income Tax act. Thus enumeration of six cases will make the meaning of misreporting exhaustive. Also as the ordinary meaning suggest culpability or existence of guilty mind , bonafide inadvertence or mistake in not recording investments or not recording any receipt in books of accounts etc can always be taken up as a defence.

(ii) BURDEN OF PROOF

POSITION	UNDER	UNDER	SECTION
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- Both the words **concealment and furnishing inaccurate particulars in the context of section 271(1)(c)** indicate prima facie the intention of an assessee to hide his income or

particulars thereof from the department. Consequently these words cast a burden on the department to prove the guilty mind as well as concealment. This legal position was confirmed by the Apex court in *CIT v. Anwar Ali (1970) 76 ITR 696 (SC)*, *Jain Brothers v. UOI (1970) 77 ITR 107 (SC)*, *Hindustan Steel Ltd v. CIT (1972) 83 ITR 26 (SC)* and *CIT v. Khoday Eswaras and sons (1972) 83 ITR 369 (SC)*.

- To get over this interpretation of law, **Explanation 1** was introduced in section 271(1)(c). This explanation shifts the burden of proof from the Assessing Officer to the assessee. Instead of the A.O. being under an obligation to establish the malafides of the assessee, the burden is on the assessee to establish his bonafides and innocence.

POSITION UNDER SECTION 270A

UNDER-REPORTED INCOME.

- A person has under-reported his income as per sub-section (2) the moment there is a difference between assessed income and income as per intimation or reassessed income and assessed income and further the said difference is also his under-reported income as per sub-section (3). Thus till this stage i.e whether a person has "under-reported his income" there is no question of burden of proof as per the mechanism provided to compute under-reported income of a person. It is simply automatic.
- The amount of under-reported income computed under sub-section(3) can be brought down or reduced or eliminated only in terms of sub-section (6). Clause (a) of sub-section (6) requires assessee to offer a *bona fide* explanation and substantiate such explanation with material facts. It is similar to Explanation 1(B) to Section 271(1)(c). Hence, the initial burden will be on the assessee to show that the benefit of exclusion under sub-section (6) is available to the assessee. Similarly in case of transfer pricing additions the initial burden will be on the assessee. In case of estimated addition referred to in clause (b) to sub-section (6) burden will be on the assessee to show that the accounts are correct and complete.

MISREPORTING

- As already discussed the term misreporting as well as six cases of misreporting will involve some sort of a deliberate attempt to misreport on the part of the assessee. Thus by applying the decisions rendered under section 271(1)(c) prior to insertion of Explanation 1 such as *Anwar Ali (supra)* etc, it can fairly be concluded that the burden is on the Assessing Officer to prove that there is misreporting.
- Further as sub-section (6) of Section 270A is not applicable or provision similar to Explanation 1 to Section 271(1)(c) is not incorporated for misreporting, the initial burden will not be on the assessee even if penalty under section 270A is held to be a civil liability. The Pune Tribunal in *Kanbay software India P Ltd v DCIT [2009] 122 TTJ 721 (Pune)* while dealing with the observation of Supreme Court in case of *Union of India v. Dharamendra Textile Processors [2008] 306 ITR 277 (SC)* to the effect that penalty under section 271(1)(c) is to provide remedy for loss of revenue and is a civil liability held that **judgment in Dharamendra Textile Processors case (supra) does not make a radical change in scheme of section 271(1)(c) but it re-emphasizes paradigm shift on burden of proof as brought about by Explanation to section**

271(1)(c). Thus, since no such explanation similar to explanation 1 is appended to misreporting the initial burden of proof will be on the revenue. Hence, it will be for the revenue to prove that there is misrepresentation, suppression, failure and falsity in terms of six cases of misreporting.

HOW TO DISCHARGE THE BURDEN.

- Before analyzing how an assessee can discharge the burden cast on him under sub-section (6), it is important to keep in mind the fundamental legal proposition that Assessment proceedings are not conclusive for levying. This was the position under section 271(1)(c) and same is the position under section 270A as sub-section(6) provides the scenario when though there is under-reported income as per sub-section (2) and (3) said under-reported income would not be exigible to penalty. Thus, Assessment proceedings and penalty proceedings are separate and distinct. Thus the law as applicable under the current regime of section 271(1)(c) will also be applicable to Section 270A.
- Findings in Assessment proceedings don't operate as res-judicata in penalty proceedings. This proposition is laid down by the decision in *CIT v. Dharamchand L. Shah (1993) 204 ITR 462 (Bom)* which decision was rendered in the context of section 271(1)(c). Further in *Vijay power generators Ltd v. ITO (2008)6 DTR 64 (Del)* it is held that "It is well settled that the findings rendered in the assessment proceedings though they constitute good evidence do not constitute conclusive evidence in penalty proceedings. During penalty proceedings, there has to be reappraisal of the very same material on the basis of which the addition was made and if further material is adduced by the assessee in the course of the penalty proceedings, it is all the more necessary that such further material should also be examined in an attempt to ascertain whether the assessee concealed his income or furnished inaccurate particulars thereof."
- Thus, under penalty proceedings Assessee can discharge his burden by relying on the same material on the basis of which assessment is made by contending that all necessary disclosures of material facts were made and that the explanation of assessee was *bona fide*. Further if there is any material or additional evidence which was not produced during assessment proceedings same can be produced in penalty proceedings as both assessment and penalty proceedings are distinct and separate.

(iii) REQUIREMENT OF MENS REA

- Under section 271(1)(c) the meaning of "Concealment" and "furnishing inaccurate particulars" contained an element of culpable mental state. The Apex Court in *Dilip N. Shroff v. CIT [(2007) 291 ITR 519]* held therein that in order to attract the penalty under Section 271(1)(c), mens rea was necessary, as according to the Court, the word "inaccurate" signified a deliberate act or omission on behalf of the assessee. It went on to hold that clause (iii) of Section 271(1) provided for a discretionary jurisdiction upon the assessing authority, inasmuch as the amount of penalty could not be less than the amount of tax sought to be evaded by reason of such concealment of particulars of income, but it may not exceed three times thereof. It was further held that the assessee must be found to have failed to prove that his explanation is not only not bona fide but all the facts relating to the same and material to the computation of his

income were not disclosed by him. It was then held that the explanation must be preceded by a finding as to how and in what manner, the assessee had furnished the particulars of his income. The Court ultimately went on to hold that the element of mens rea was essential.

- However, subsequently it was on the point of mens rea that the judgment in *Dilip N. Shroff v. CIT [supra]* was upset by the decision in *Union of India v. Dharamendra Textile Processors (2008) 306 ITR 277* after quoting from Section 271 extensively and also considering Section 271(1)(c), the Court came to the conclusion that since Section 271(1)(c) indicated the element of strict liability on the assessee for the concealment or for giving inaccurate particulars while filing return, there was no necessity of mens rea. The Court went on to hold that the objective behind enactment of Section 271(1)(c) read with the Explanations indicated with the said section was for providing remedy for loss of revenue and such a penalty was a civil liability and, therefore, wilful concealment is not an essential ingredient for attracting civil liability as was the case in the matter of prosecution under Section 276-C of the Act.
- From the scheme of section 270A it appears that where there is under-reporting or misreporting of income, the objective is to remedy loss to the revenue and is thus a strict and civil liability not requiring existence of mens –rea. This issue will be settled only through litigation. However the burden to prove misreporting will be on the revenue as explained earlier.

(iv) WHETHER LEVY OF PENALTY U/S. 270A IS AUTOMATIC

POSITION UNDER SECTION 271(1)(C)

- After the decision of *Apex court in UOI v. Dharmendra Textiles (Supra)* in the context of Section 271(1)(c) it was understood by the revenue authorities that penalty proceedings are automatic and that penalty is to be levied the moment addition is made or confirmed. This erroneous understanding was set at naught by the Apex Court in *Union of India vs Rajasthan Spinning & Weaving Mill (2009) 180 Taxmann 609(SC)* wherein it is held as under:

“At this stage, we need to examine the recent decision of this Court in Dharamendra Textile (supra). In almost every case relating to penalty, the decision is referred to on behalf of the Revenue as if it laid down that in every case of non-payment or short payment of duty the penalty clause would automatically get attracted and the authority had no discretion in the matter. One of us (Aftab Alam,J.) was a party to the decision in Dharmendra Textile and we see no reason to understand or read that decision in that manner.”

- In *CIT v. M/s Sidhartha Enterprises (2009) 184 Taxman 460 (P & H)(HC)* it was held that “the judgment in Dharmendra Textile cannot be read as laying down that in every case where particulars of income are inaccurate, penalty must follow. Even so, the concept of penalty has not undergone change by virtue of the said judgment. Penalty is imposed only when there is some element of deliberate default and not a mere mistake. In view of the finding that the furnishing of inaccurate particulars was simply a mistake and not a deliberate attempt to evade tax, penalty was not leviable.”
- Hence, penalty u/s. 271(1)(c) is not automatic but discretionary and that the

assessing officer must exercise the discretion judicially.

POSITION UNDER SECTION 270A

UNDER-REPORTED INCOME

Sub-section (1) of section 270A uses the term "may". Further sub-section (6) provides for situations when it cannot be said that there is under-reported income. Hence, just because a person has under-reported his income in terms of sub-section (2) and (3) would not automatically lead to the conclusion that penalty u/s 270A is leviable.

MISREPORTING

- As the burden of proving misreporting will be on the assessing officer, penalty for misreporting cannot be automatic unless AO is satisfied about misrepresentation, suppression, failure and falsity on the part of the Assessee with some degree of deliberateness on the part of the assessee.
- Thus, a bona-fide mistake or reliance on expert professional opinion would continue as a defence for assessee from levy of penalty even in cases of mis-reporting.

(v) CAN PENALTY U/S. 270A BE LEVIED ON AN INCORRECT LEGAL CLAIM/DEBATABLE ISSUE

POSITION UNDER SECTION 271(1)(C)

The Delhi High court in *New Holland Tractors India P Ltd. v. CIT [2015] 275 CTR 291 (Delhi)* has held that penalty u/s 271(1)(c) read with Explanation 1 clause (B) cannot be levied where a legal or a debatable claim is rejected. On this aspect, useful reference can be made also to the following observations of the Supreme Court in the case of *Reliance Petroproducts (P.) Ltd.,(supra):-*

"11. The learned counsel argued that "submitting an incorrect claim in law for the expenditure on interest would amount to giving inaccurate particulars of such income". We do not think that such can be the interpretation of the words concerned. The words are plain and simple. In order to expose the assessee to the penalty unless the case is strictly covered by the provision, the penalty provision cannot be invoked. By any stretch of imagination, making an incorrect claim in law cannot tantamount to furnishing inaccurate particulars."

Thus penalty u/s 271(1)(c) cannot be levied on an incorrect legal claim.

POSITION UNDER SECTION 270A

- In the case of under-reported income, clause (a) of sub-section (6) of Section 270A is similar to Explanation 1 clause (B). Hence, where a debatable issue is involved or an incorrect legal claim is involved then penalty under section 270A for under-reporting of income would not be leviable. Obviously, such under-reporting of income cannot be as a consequence of misreporting.

(vi) COMMENCEMENT OF PENALTY PROCEEDINGS AND INITIATION OF PENALTY AND RECORDING OF SATISFACTION

POSITION UNDER SECTION 271(1)(C)

- Section 271(1) reads " If the assessing officer or.....in the course of any proceedings

under this Act , is satisfied that any person-.....he may direct that such person shall pay by way of penalty” [emphasis supplied]

- The Apex Court in *CIT v. S. V. Angidi Chettiar [1962] 44 ITR 739 (SC)* has held that penalty proceedings cannot be commenced by the ITO before the completion of the assessment proceedings by the ITO. However, the power to impose penalty depends upon the satisfaction of the ITO in the course of proceedings under the Act ie it could not be exercised if he is not satisfied about the existence of conditions for penalty before the proceedings are concluded. Satisfaction before conclusion of the proceeding under the Act, is a condition for the exercise of the jurisdiction. Considering the said decision, the Bombay High Court in *CIT v. Dajibhai Kanjibhai [1991] 189 ITR 41 (Bom)* has held that AO must “record” his satisfaction during the course of assessment proceedings. The Full bench of the Delhi High Court in *CIT v. Rampur Engg Co Ltd [2009] 309 ITR 143 (Delhi)* has held that the “power to impose penalty under section 271(1) depends upon satisfaction of Assessing Officer in course of assessment proceedings and it cannot be exercised if he is not satisfied and has not recorded his satisfaction about existence of conditions specified in clauses (a), (b) and (c) of sub-section (1) of section 271 before proceedings are concluded.”

- Hence, there has to be satisfaction, such satisfaction has to be recorded, recording must be before completion of assessment proceedings and penalty proceedings though initiated before completion of assessment proceedings they will have to commence after passing of assessment order.

- After taking note of the judicial pronouncements in this regard, the Legislature thought it fit to insert Section 271(1)(B), which reads as under:

“271(1)(B) Where any amount is added or disallowed in computing the total income or loss of an assessee in any order of assessment or reassessment and the said order contains a direction for initiation of penalty proceedings under clause (c) of sub-section (1), such an order of assessment or reassessment shall be deemed to constitute satisfaction of the Assessing Officer for initiation of the penalty proceedings under the said clause (c).”

The above provision came up for interpretation before the Delhi High Court in the case of *Ms. Madhushree Gupta v. Union of India [2009] 309 ITR 143(Del)* wherein the Delhi High Court held that both in post amendment and pre amendment there is not much difference and the satisfaction is required to be arrived in the course of assessment proceedings and should be discernable in the assessment order.

- The Karnataka High Court in *CIT v. Manjunath Cotton and Ginning Factory [2013] 359 ITR 565 (Karnataka)* interpreted the term “Direction” IN Section 271(1B) and held at para 50 that

“.....The meaning of the word direction is of importance. Merely saying that penalty proceedings are being initiated will not satisfy the requirement. The direction to initiate proceedings should be clear and not be ambiguous.....As the words used in the legal fiction or the deeming provisions of Section 271(1B) is Direction, it is imperative that the assessment order contains a direction. Use of the phrases like (a) penalty proceedings are being initiated separately and (b) penalty proceedings under

Section 271(l)(c) are initiated separately, do not comply with the meaning of the word direction as contemplated even in the amended provisions of law.A direction by a statutory authority is in the nature of an order requiring positive compliance. When it is left to the option and discretion of the ITO whether or not take action, it cannot be described as a direction."

Following the above ratio, in *CIT v. MWP Ltd [2014] 264 CTR 502 (Karn)* wherein in the assessment order it was recorded "Penalty u/s 271(1)(c) initiated separately." penalty was deleted.

- Thus there has to be a satisfaction and direction to initiate penalty should be clear, unambiguous and akin to an order requiring positive compliance.

POSITION UNDER SECTION 270A.

- Section 270A (1) reads as under :
- "The AO/CIT(A)/CIT/ Pr. CIT may, during the course of any proceedings under this Act, direct that any person who has under-reported his income shall be liable to pay a penalty in addition to tax, if any on the unreported income."
- As pointed out earlier, the Finance Bill did not contain the phrase "during the course of any proceedings under this act". However with the introduction of the said phrase which also existed under section 271(1) and the interpretation of section 271(1) given by the courts as pointed out above it can be concluded that penalty proceedings can commence only after completion of assessment proceedings but there has to be a direction to initiate penalty proceedings before the completion of assessment proceedings. Obviously such direction has to form part of the assessment order.
 - At the first glance of section 270A(1) there seems to be no requirement for AO to have satisfaction and record such satisfaction as was required under the erstwhile section 271(1) as the term satisfaction is not used in S.270A(1).
 - However my view is that there is an implied requirement. This is because the term "may" which qualifies the term "direct" indicates that penalty is not automatic and thus if penalty is to be initiated, AO must be satisfied of the quantum of under-reported income or misreporting and only upon such satisfaction or application of mind he can direct during the course of any proceedings under this act that any person who has under-reported his income shall be liable to pay a penalty. Also, the term "direct" or "direction" as pointed out above in *CIT v. Manjunath Cotton and Ginning Factory(supra)* itself requires AO to pass an order requiring positive compliance.
 - The conclusion is further strengthened by the language used in Section 270AA(3) being "....., where the proceedings for penalty under section 270A has not been initiated under the circumstances referred to in sub-section (9) of the said section 270A".
 - Hence, if in an assessment an expenditure is disallowed or there is estimation, there will be an unreported income under Sub-section(2) and (3) of S.270A. When the said expenditure is being disallowed / income is estimated, AO has a choice to decide whether to direct levy of penalty or not, which will depend on satisfaction of AO as

to applicability of Sub-Section (6) in the facts of the case. Thus if AO is satisfied [ie after application of mind] that sub-section (6) will not apply or that expenditure disallowed is on account of misreporting, he will have to direct the levy of penalty under section 270A and such direction will have to be recorded in the assessment order.

(vii) WHETHER PENALTY UNDER SECTION 270A IS LEVIABLE ON ADJUSTMENTS TO BOOK PROFIT WHEN INCOME IS ASSESSED UNDER NORMAL PROVISIONS

Only where the income computed u/s. 115JB/ 115JC is deemed to be the total income of the assessee, is the formula '(A-B) + (C-D)' applicable. Where the income is finally assessable under normal provisions only, then any adjustment in Book profit u/s. 115JB and 115JC may not attract penalty.

(viii) WHETHER PENALTY U/S. 270A CAN BE LEVIED ON AGREED ADDITION

POSITION UNDER SECTION 271(1)(C)

- There may be cases where assessee agrees to an addition during assessment proceedings, or during survey or does not prefer an appeal. An issue arose whether in such situation penalty u/s 271(1)(c) would be automatic particularly in view of deeming fiction u/s Explanation 1 to Section 271(1)(c). In *Sir Shadilal Sugar and General Mills Ltd. v. CIT (1987) 168 ITR 705(SC)* it was held as under:

"We find that the assessee admitted that these were the incomes of the assessee but that was not an admission that there was deliberate concealment. From agreeing to additions, it does not follow that the amount agreed to be added was concealed income. There may be a hundred and one reasons for such admission"

- The apex court in the case of *K. P. Madhusudan v. CIT (2001) 251 ITR 99* has held that decision in Shadilal's case (Supra) is no more good law after insertion of Expl-1. After the decision in the case of K. P. Madhusudan, it was noticed that just because the assessee has agreed for the addition, the penalties were levied u/s 271(1)(c). It is to be stated that the above decision in the case of K. P. Madhusudan is not to be interpreted as meaning that in an agreed addition, penalty would automatically follow. It simply holds that under the Explanation 1, the assessee should show that his failure to return correct income was not due to fraud or neglect. No separate enquiry is necessary for imposing penalty but the assessee is at liberty to show his bonafides in the penalty proceedings and if he does, no penalty can be imposed. This decision of Supreme Court had been so considered and analysed in the following decisions.

i. *ITO v. Smt. DevibaiParmani [84 ITD 342]*

ii. *Dy. Director of Income Tax v. Chirag Metal Rolling Mills Ltd. [305 ITR 29 (MP)]*

iii. *CIT v. P. Govindswamy [263 ITR 509]*

- Infact, In *CIT v. Suresh Chandra Mittal (2000) 241 ITR 124 (M.P.)* after considering Explanation 1 Upheld decision of the Tribunal in which the Tribunal held as under:

"The assessee had no chance of carrying through his explanation and the Assessing

Officer too did not record any finding as to the acceptability or otherwise of the explanation of the assessee. Under these circumstances the proviso to Explanation 1 to section 271 is not attracted. The Revenue did not at all discharge the burden to prove that there was concealment of income by the assessee. It simply rested its conclusion on the act of voluntary surrender by the assessee, which obviously was done in good faith and to buy peace."

The above decision is upheld by the Supreme Court in *CIT v. Suresh Chandra Mittal (2001) 251 ITR 9 (SC)*. Thus it can be fairly concluded that once assessee gives a bonafide explanation for agreeing to addition then the burden shifts on the revenue to prove concealment. This position is further fortified by the apex Court in *MAK Data P Ltd. v. CIT (2013) 358 ITR 593(SC)* wherein it is held as under :

"The AO, in our view, shall not be carried away by the plea of the assessee like "voluntary disclosure", "buy peace", "avoid litigation", "amicable settlement", etc. to explain away its conduct. The question is whether the assessee has offered any explanation for concealment of particulars of income or furnishing inaccurate particulars of income. Explanation to Section 271(1) raises a presumption of concealment, when a difference is noticed by the AO, between reported and assessed income. The burden is then on the assessee to show otherwise, by cogent and reliable evidence. When the initial onus placed by the explanation, has been discharged by him, the onus shifts on the Revenue to show that the amount in question constituted the income and not otherwise."

- It may also be noted where declaration is made during survey and the due date of return has not expired and declared amount is offered for tax then there can be no penalty u/s. 271(1)(c) read with Explanation 1 as held in following decisions:
 - i) *Shri Dilip M. Shah Mumbai v. ACIT ITA 4413/Bom/98 A.Y. 1994- 95 dt. 25/1/1999.*
 - ii) *CIT v. SAS Pharmaceuticals (2011) 335 ITR 259 (Del.)(HC).*
 - iii) *ACIT v. Crescent Property Developers ITA No. 2770/M/2012, Dt. 19/6/2014.*

POSITION UNDER SECTION 270A

- This issue has to be seen in the light of section 270AA which provides for immunity from penalty under section 270A if tax and interest is paid. Thus, if assessee chooses not to challenge the assessment order, then he can apply for immunity under section 270AA and subject to the provisions of section 270AA assessee will be granted from immunity from penalty.
- However, when assessee becomes ineligible to apply for immunity u/s 270AA say for instance assessee agrees to some addition and files appeal for some other addition or assessee agrees for addition but the charge is of misreporting etc then the issue arises whether penalty on agreed additions will be leviable or not.
- As far as Under-reported Income is concerned, the ratio deciphered above in the context of Section 271(1)(c) would also apply to Section 270A in view of clause (a) to sub-section (6) to Section 270A which permits assessee to give a bona-fide explanation. However if it is proved that the agreed addition is on account of misreporting then

penalty under section 270A would certainly be leviable.

(ix) WHETHER ISSUE OF SHOW CAUSE NOTICE IS MANDATORY FOR LEVYING PENALTY U/S. 270A.

- Section 274 of the Income Tax Act which provides for opportunity of hearing before imposing penalty would apply to Section 270A also.
- If the provisions of section 270A are interpreted in the manner that the assessment order must record a proper direction as to whether penalty is initiated for under-reporting or misreporting then even the show cause notice must be in consonance with such direction and the final penalty order must be in consonance with the show cause notice.
- Thus, it cannot be that SCN is for under-reporting and penalty is levied for misreporting. Even in the context of Section 271(1)(c) it has been held that show cause notices for penalty must strike either concealment if penalty is levied on furnishing inaccurate particulars and vice versa and further penalty order cannot levy penalty on concealment if show cause notice is for furnishing inaccurate particulars and vice versa. For this proposition reliance can be placed on various decisions such as *Commissioner of Income-tax v. SSA'S Emerald Meadows [2016] 73 taxmann.com 248 (SC)*, *CIT v. Manjunath Cotton and Ginning Factory (2013) 359 ITR 565(Karn)(Para 59-61 and 63)*, *Suvaprasanna Bhattacharya v ACIT ITA No 1303/Kol/2010 AY 06-07, Dt 6-11-2015 (Kol).(Rel para 8)*, *New Sorathia Engg. Co (2006) 282 ITR 642 (Guj)*, *CIT v. Lakhdhir Lalji [1972] 85 ITR 77 (GUJ.)* and *CIT v. Manu Engg. Works [1980] 122 ITR 306 (GUJ)*. The ratio of these decisions would also apply to SCN issued u/s 274 r.w.S 270A.

(x) CERTAIN INCONSISTENCIES.WHICH NEEDS TO BE ADDRESSED

- As per Section 270A, where no return has been filed, the clause specifies that under-reported income shall be difference between the assessed income and maximum amount not chargeable to tax in case of persons other than company, firm and local authority. No exception is carved out in case where tax has been paid but only return is not filed.
- No clarity on rate of tax to be taken in case of firm, company or local authority say where a company which opts for section 115BA (25 %) etc. Further, as per the formula, under-reported income includes addition under normal provision as also under MAT/AMT provision which totals up to form the under-reported income. Then what shall be the rate applicable to compute the tax payable in such case is not clear.
- Section 246A which provides for appealable order before Commissioner (Appeals) specifically provides that order imposing penalty u/s 271(1) is appealable. However, the Finance Act,2016 does not amend section 246A to specifically provide that order imposing penalty under section 270A will be appealable. Section 246A(1)(q) provides that an order imposing penalty under Chapter XXI is appealable and as Section 270A is in chapter XXI, order imposing penalty under section 270A will be appealable. However a specific amendment will avoid controversy.

5. Amendments consequential to insertion of section 270A

SECTION AMENDE D	EXISTING PROVISION	AMENDMENT
271A	Section 271A provides for penalty where there is failure of keep, maintain or retain books etc.	Section 271A is without prejudice to the provisions of section 271 and therefore consequential amendment is made to make it without prejudice to provisions of section 270A also.
271AA	Section 271AA provides for penalty in respect of Transfer Pricing documents	Section 271AA is without prejudice to the provisions of section 271 and therefore consequential amendment is made to make it without prejudice to provisions of section 270A also.
271AAB	Section 271AAB provides for penalty for specified assessment years in case where search is initiated.	Section 271AAB provides for penalty in case of specified assessment years where search has taken place. Those assessment years are outside the ambit of section 271(1)(c) as per section 271AAB(2). Now, amendment is made to keep those assessment years outside the ambit of section 270A also.
273A	Section 273A provides for the power of Pr. CIT/ CIT to reduce or waive penalty levied u/s 271(1)(iii) if the conditions given are fulfilled.	Section 273A is proposed to apply to section 270A and the Pr. CIT/CIT shall have the power to waive or reduce penalty levied under the said section 270A. Section 273A however does not substitute the words concealment of income and furnishing inaccurate particulars of Income by Under-reported Income giving rise to an anomaly.
279	Section 279 provides that prosecution it to be at the instance of the Pr. CCIT, CCIT, Pr. CIT, CIT. Sub-section (1A) provides that where the penalty u/s 271(1)(iii) has been waived off or reduced u/s 273A, then no such person shall be proceeded against.	Section 279(1A) is amended to provide that where the penalty u/s 270A has been waived or reduced u/s 273A then no prosecution can be initiated.

6. Insertion of new section – 270AA – immunity from imposition of penalty, etc.

The new section 270AA provides for immunity from penalty u/s 270A and prosecution u/s

276C in certain cases.

Pre-condition for Immunity

An assessee may make an application to the Assessing Officer for grant of immunity from imposition of penalty under section 270A and initiation of proceedings under section 276C or section 276CC, provided he pays the tax and interest payable as per the order of assessment or reassessment within the period specified in such notice of demand and does not prefer an appeal against such assessment order.

Time Limit for making application

The assessee can make such application within one month from the end of the month in which the order of assessment or reassessment is received in the form and manner, as may be prescribed.

Conditions for grant of Immunity

Immunity from initiation of penalty and proceeding under section 276C will be granted if the penalty proceedings under section 270A has not been initiated on account of the of misreporting u/s 270A.

Time limit for passing order.

The Assessing Officer shall pass an order accepting or rejecting such application within a period of one month from the end of the month in which such application is received. However, in the interest of natural justice, no order rejecting the application shall be passed by the Assessing Officer unless the assessee has been given an opportunity of being heard.

Binding Effect

The order of Assessing Officer under the said section shall be final.

Effect of order under Section 270AA accepting the application.

No appeal under section 246A or an application for revision under section 264 shall be admissible against the order of assessment or reassessment referred to in clause (a) of sub-section (1), in a case where an order under section 270AA has been made accepting the application.

Remedy against order rejecting application.

By virtue of amendment in section 249 and section 253, an appeal against order of rejection passed under section 270AA is to be made before the Commissioner (Appeals) within thirty days of the receipt of the notice of demand relating to an assessment order. The period beginning from the date on which such application is made to the date on which the order rejecting the application is served on the assessee shall be excluded for calculation of the thirty days period.

ANALYSIS

- In case of penalty on under-reported income which is not as a consequence of misreporting AO is bound to grant immunity subject to fulfillment of other conditions.
- In case of misreporting AO has a discretion.

- It appears that where penalty is levied on certain additions on ground of mis-reporting and certain additions on ground of only under-reporting than assessee will have to make a choice whether to file appeal or make application for immunity as he cannot file appeal on penalty levied on mis-reported income and immunity application for under-reported income.
- There is no bar to filing appeal against quantum order with application for condonation of delay after rejection of application for immunity.
- There is no specific bar prohibiting revision u/s 263 of order accepting immunity application.

7. Conclusion

The analysis of new section 270A indicates that there will be number of issues on which both the assessee and revenue will be at loggerheads. In-fact majority of those issues would be the ones which are settled u/s 271(1). Hence, to a substantial extent section 270A will either result in either unsettling settled principles of law or will confirm them but only after litigation. It will be like old wine in new bottle. Hence, this article is made comprehensive so as to give complete up-to-date picture of position u/s 271(1) as well. The object of introducing Section 270A will be defeated. According to me , the Government must invite views on this Section and decide whether the same needs to be scrapped or retained. The implementation of Easwer committee recommendations as referred in the introduction of this article appears to have been a better way forward.



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