



Interplay between Initiation of Penalty Provisions and Satisfaction of The Revenue

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A. INTRODUCTION

1. Chapter XXI of the Income Tax Act, 1961 (hereinafter referred to as 'the Act') enacts provisions for the levy, imposition and collection of penalty. Without such a sanction, there is a danger of evasion of tax. Thus, provisions for levy and collection of penalties for contravening their requirement, has become an integral part of such enactment and one of their purposes.

2. The provisions of section 271(1)(c) of the Act states that penalty shall be levied in case a person either "conceals the particulars of his income" or "furnishes inaccurate particulars of his income". Satisfaction of the Tax Officer as to whether the penalty is for concealment of income or for furnishing inaccurate particulars of income is an integral clog in the initiation and levy of penalty. Non satisfaction or incorrect satisfaction of the Tax Officer is challenged by the Assessee as being contrary to the law and the same has resulted into substantial litigation over the years.

3. Though, a new penalty regime has come into the force from Assessment Year 2017-18 and a new section 270A for levy of penalty in cases of underreporting of income and misreporting of income has been introduced, there are still innumerable cases of dispute under section 271(1)(c) of the Act are pending at various judicial fora.

B. WHERE DOES THE CONTROVERSY LIE?

4. The provision of section 271(1) of the Act, where the major dispute subsides, is reproduced as under:

*"271. (1) If the Assessing Officer or the Commissioner (Appeals) or the Principal Commissioner or Commissioner in the course of any proceedings under this Act, is **satisfied** that any person—*

.....

*(c) has **concealed the particulars of his income or furnished inaccurate particulars of such income,** or*

.....

he may direct that such person shall pay by way of penalty, —"

Elements essential for initiation of penalty proceedings u/s 271(1)(c) of the Act

On a bare reading of the provisions of section 271(1)(c) of the Act, it is apparent that the following conditions are precedent for initiation of penalty proceedings under the said section:

- Satisfaction of the relevant Taxing Authority, which is arrived at during the course of any proceedings under this Act, **and**

- Satisfaction to the effect whether the Assessee has either

Concealed particulars of his income

OR

Furnished inaccurate particulars of such income

5. Clause (c) of section 271(1) of the Act contains two key expressions i.e. **concealment of particulars of income and furnishing inaccurate particulars of income**. These are the two eventualities which comprise the two limbs for imposition of penalty u/s 271(1) (c) of the Act. Therefore, to levy penalty u/s 271(1)(c) of the Act, the person must have either 'concealed particulars of his income' or 'furnished inaccurate particulars of income'. These two terms have two distinctive meanings. They carry different connotations and cannot be interchanged or interpreted for one another, as has been held in the following cases:

a) **Shri T. Ashok Pai v. CIT [2007] 292 ITR 11 (SC)**

"22. 'Concealment of income' and 'furnishing of inaccurate particulars' carry different connotations. Concealment refers to deliberate act on the part of the assessee. A mere omission or negligence would not constitute a deliberate act of suppressio veri or suggestio falsi.

b) **Dilip N Shroff v. JCIT 291 ITR 519 (SC)**

43. The expression "conceal" is of great importance. According to Law Lexicon, the word "conceal" means:

"to hide or keep secret. The word "conceal" is con+celare which implies to hide. It means to hide or withdraw from observation; to cover or keep from sight; to prevent the discovery of; to withhold knowledge of. The offence of concealment is, thus, a direct attempt to hide an item of income or a portion thereof from the knowledge of the income tax authorities."

In Webster's Dictionary, "inaccurate" has been defined as: "not accurate, not exact or correct; not according to truth; erroneous; as an inaccurate statement, copy or transcript."

44. It signifies a deliberate act or omission on the part of the assessee. Such deliberate act must be either for the purpose of concealment of income or furnishing of inaccurate particulars."

Satisfaction of the relevant Taxing Authority

6. As both the limbs i.e. concealment of income and furnishing inaccurate particulars of income carry different connotations, **it is a must that the relevant Taxing Authority must be satisfied before initiation of penalty proceedings** that the case of the assessee falls either under the first limb or the second limb. The necessity of the satisfaction of the Tax Officer before initiating the penalty proceedings has been affirmed by the courts.

Reliance is placed on the following judicial precedents

a) **CIT v. S.V. Angidi Chettiar (1962) 44 ITR 739 (SC)**

"The power to impose penalty under section 28 depends upon the satisfaction of the Income-tax Officer in the course of proceedings under the Act; it cannot be exercised if he is not satisfied about the existence of conditions specified in clauses (a), (b) or (c) before the proceedings are concluded."

b) **D.M. Manasvi v. CIT [1973 AIR 22] (SC)**

"What is contemplated by clause (1) of section 271 is that the Income Tax Officer or the Appellate Assistant Commissioner should have been satisfied in the course of proceedings under the Act regarding matters mentioned in the clauses of that sub-section."

c) **CIT v. Manjunatha Cotton and Ginning Factory [359 ITR 565] [Karnataka High Court]**

“Therefore, this provision makes it abundantly clear that the satisfaction of the Assessing Officer before initiation of penalty proceedings is a must. The satisfaction should be that he has concealed particulars of his income or furnished inaccurate particulars of such income”

C. RECORDING OF SATISFACTION OF THE RELEVANT TAXING AUTHORITY

7. Further, such satisfaction of the relevant Taxing Authority is conventionally indicated by striking off the inapplicable portion in the notice u/s 274 r.w.s. 271(1)(c) of the Act. It is a general practice of the department to issue notice u/s 274 r.w.s. 271(1)(c) of the Act in a standard proforma wherein all the clauses/ offences, for which penalty is leviable, are mentioned. Therefore, the relevant Taxing Authority **records their satisfaction by striking off the portion** that is inapplicable in the particular case. Alternatively, the Assessing Officers have also been recording their satisfaction by an endorsement at the foot of the assessment order such as **‘penalty proceedings u/s 271(1)(c) of the Act has been initiated for concealment of income (or furnishing inaccurate particulars of income, as the case maybe)’**.

8. While it is an undisputed fact supported by various judicial precedents that satisfaction of the relevant Taxing Authority is essential before initiation of penalty proceedings, however, it has been a **matter of conflict as to whether recording of such satisfaction of the relevant Taxing Authority is a condition essential for initiation of penalty proceedings**.

9. Revenue’s contention:

The Income Tax Department have held the view that **no separate satisfaction is required to be recorded** before initiating penalty proceedings. In this regard reliance has been placed on the following judicial precedents by the Income Tax Department:

- a) **CIT v. S.V. Angidi Chettiar (1962) 44 ITR 739 (SC)**
“Satisfaction before the conclusion of the proceeding under the Act, and not the issue of a notice or initiation of any step for imposing penalty is a condition for the exercise of the jurisdiction.”
- b) **Becker Gray And Company (1930) Ltd. v. ITO [112 ITR 503 (1977)] [Calcutta High Court]**
“It is true that the Income-tax Officer should be prima facie satisfied before the penalty notice is issued, but it does not mean that he is required to record such satisfaction in writing in every case.”
- c) **Shyam Biri Works Pvt. Ltd. v. CIT [259 ITR 625 (2002)] [Allahabad High Court]**
“We are, therefore, of the opinion that although the Assessing Officer must have satisfaction as required under section 273 of the Act, it is not necessary for him to record that satisfaction in writing before initiating penalty proceedings under section 273 of the Act.”

10. Taxpayer’s contention:

On the contrary, it is the taxpayer’s contention that in the absence of any finding or recording of satisfaction regarding the particular charge u/s 271(1)(c) of the Act i.e. concealment of income or furnishing inaccurate particulars of income, the initiation of penalty proceedings is not valid. Some of the judicial precedents on which reliance can be placed by the taxpayer:

- a) **D.M. Manasvi v. CIT [1973 AIR 22] (SC)**
“Clause (c) of sub-section (1) of section 271 shows that occasion for taking proceedings for payment of penalty arises if the Income Tax Officer or the Appellate Assistant Commissioner is satisfied that any person has concealed the particulars of his income or furnished inaccurate particulars of such income. It has also to be shown that the

Income Tax Officer or the Appellate Assistant Commissioner was so satisfied in the course of proceedings under the Act.

b) CIT v. Ram Commercial Enterprises Limited [246 ITR 568 (2000)] [Delhi High Court]

“A bare reading of the provisions of Section 271 and the law laid down by the Supreme Court makes it clear that it is the assessing authority which has to form its own opinion and record its satisfaction before initiating the penalty proceedings. Merely because the penalty proceedings have been initiated, it cannot be assumed that such a satisfaction was arrived at in the absence of the same being spelt out by the order of the assessing authority.”

c) Diwan Enterprises v. CIT [246 ITR 571 (2000)] [Delhi High Court]

“Satisfaction has to be before the issue of notice or initiation of any step for imposing penalty. In the case at hand we find the assessing officer having nowhere recorded till the conclusion of the assessment proceedings his satisfaction that the assessee had concealed the particulars of his income or furnished inaccurate particulars of such income. This is a jurisdictional defect which cannot be cured.”

D. INSERTION OF SUB-SECTION (1B) TO SECTION 271 OF THE ACT VIDE FINANCE ACT, 2008

11. In view of the above contrary views adopted by various judicial pronouncements and in order to put an end to the incessant litigation, a new sub-section (1B) in section 271 of the Act was inserted vide Finance Act, 2008 with retrospective effect from 1st April, 1989. The provisions contained in section 271(1B) of the Act are as under:

“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).”

12. Legislative intent behind the amendment as stated in Notes on Clauses of Finance Bill, 2008 is as under:

“Clause 48 seeks to amend section 271 of the Income-tax Act, which relates to failure to furnish returns, comply with notices, concealment of income, etc.

Under the existing provisions contained in Chapter XXI the Assessing Officer is required to be satisfied during the course of penalty proceedings. Legislative intent was that such a satisfaction was required to be recorded only at the time of levy of penalty and not at the time of initiation of penalty. However, some of the judicial interpretations on this issue are favouring the view that satisfaction has to be recorded at the time of initiation of penalty proceedings also.

It is therefore proposed to insert a new sub-section (1B) in section 271 of the Income-tax Act so as to provide that 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 if such order contains a direction for initiation of penalty proceedings under 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 sub-section (1).

This amendment will take effect retrospectively from 1st April, 1989.”

13. As is clear from the Memorandum to the Finance Act 2008, the new section 271(1B) was inserted with the intention to give validity to the

satisfaction made by the Assessing Officer at any point of time during the penalty proceedings. The constitutionality of the above amendment was challenged in the **Hon'ble Delhi High Court** in the case of *Madhushree Gupta v. UOI* [WP (C) No. 5059 of 2008]. While contemplating the constitutionality of the said amendment the Hon'ble High Court interpreted the provisions of section 271(1B) read in conjunction with section 271(1) and held that -

“The contra-submission of the learned ASG that prima facie satisfaction of the Assessing Officer need not be reflected at the stage of initiation but only at the stage of imposition of penalty is in the teeth of Section 271(1)(c) of the Act. Section 271(1)(c) has to be read in consonance of Section 271(1B). The presence of prima facie satisfaction for initiation of penalty proceedings was and remains a jurisdictional fact which cannot be wished away as the provision stands even today, i.e., post amendment. If an interpretation such as the one proposed by the Revenue is accepted then, in our view, the impugned provision will fall foul of Article 14 of the Constitution as it will then be impregnated with the vice of arbitrariness. The Assessing Officer would in such a situation be in a position to pick a case for initiation of penalty merely because there is an addition or disallowance without arriving at a prima facie satisfaction with respect to infraction by the assessee of clause (c) of sub-section (1) of Section 271 of the Act. A requirement which is mandated by the provision itself.

15.7 Learned ASG also sought to place reliance on the Memorandum as well as Clause 48 of the Notes on Clauses appended to the Finance Act, 2008. Even though both the Memorandum as well as Notes On Clauses refers to the conflict in judicial opinion and gives that, as the reason for insertion of the impugned provision, in our opinion, in sub-section (1B) of Section 271 does not do away with the principle that the prima

facie satisfaction of the Assessing officer must be discernible from the order passed by the Assessing Officer during the course of assessment proceedings pending before him.”

14. Accordingly, in view of the above judgment of the Hon'ble Delhi High Court, it has been clearly set out that mere direction of the Assessing Officer in his Assessment Order stating that 'penalty provisions are initiated separately', would not be sufficient to attract the provisions of subsection (1B) of section 271 of the Act. In order to qualify for deem satisfaction, the Assessing officer has to also mention as to which limb of subsection (c) of section 271 of the Act has been charged on the Assessee in order to satisfy the provisions of section 271(1B).

15. The above ratio has also been adopted by the **Hon'ble Karnataka High Court** in the case of *CIT v. Manjunatha Cotton and Ginning Factory* (359 ITR 565). The following conclusions can be inferred from the above order in relation to satisfaction of Taxing Officer for initiation of penalty proceedings:

- The relevant Taxing Authority must record a categorical finding regarding the charge alleged against the assessee i.e. concealment of income or furnishing of inaccurate particulars of income in the assessment orders passed by him. This is sufficient to initiate penalty proceedings.
- In the absence of such categorical finding, the facts contemplated in Explanation 1 to section 271(1) of the Act must be discernable from the assessment order so that deeming provision in the said Explanation is attracted and income is deemed to have been concealed and penalty proceedings can be initiated.
- If the relevant Taxing Authority is Assessing Officer and if in the order passed by him there is neither any categorical finding nor the facts contemplated in Explanation (1) are

discernable, then the order must contain direction for initiation of penalty proceedings u/s 271(1)(c) of the Act to attract the deeming provisions in section 271(1B) of the Act.

- The direction to initiate penalty u/s 271(1B) of the Act must be clear and without any ambiguity. Merely mentioning that penalty proceedings u/s 271(1)(c) of the Act are initiated separately will not satisfy the requirement of the law.
- Section 271(1B) is applicable only for assessment orders passed by Assessing Officer and not for orders passed by Commissioner (Appeals) or Commissioner.

16. Further, the **Hon'ble Karnataka High Court** in its later decision in the case of *CIT v. MWP Ltd. [ITA No. 332 of 2007]* held that phrases like 'penalty proceedings are being initiated separately' or 'penalty proceedings u/s 271(1)(c) are initiated separately' do not comply with the meaning of the word direction as contemplated in amended section 271(1B) of the Act.

17. In view of the above judicial pronouncements, both pre and post amendment, it can be concluded that for initiation of penalty proceedings, the order of the relevant Taxing Authority must categorically **record the specific charge** alleged against the assessee and in the absence of such categorical recording in the assessment order passed by the Assessing Officer, the charge alleged against the assessee must be discernable from the facts stated therein.

E. VALIDITY OF PENALTY PROCEEDINGS SANS STRIKE OFF IN PENALTY NOTICE

18. As discussed earlier, it is a regular practice of the Taxing Officer to strike off the inapplicable limb in the penalty notice u/s 274 r.w.s. 271(1)(c) of the Act in order to satisfy

himself and also in order to inform the charge to the Taxpayer. Alternatively, as discussed above, the Taxing Officer could also specifically mention the limb under which the penalty is being initiated in the Assessment Order. However, in cases where both such satisfactions are not recorded, the courts have held the penalty to be invalid. Some such cases are discussed below:

a) ***PCIT v. Goa Coastal Resorts and Recreation Pvt Ltd [Tax Appeal No 24 of 2019] [High Court of Bombay at Goa]***

"5. We have carefully examined the record as well as duly considered the rival contentions. Both the Commissioner (Appeals) as well as ITAT have categorically held that in the present case, there is no record of satisfaction by the Assessing Officer that there was any concealment of income or that any inaccurate particulars were furnished by the assessee. This being a sine qua non for initiation of penalty proceedings, in the absence of such petition, the two authorities have quite correctly ordered the dropping of penalty proceedings against the petitioner.

6. Besides, we note that the Division Bench of this Court in Samson(supra) as well as in New Era Sova Mine(supra) has held that the notice which is issued to the assessee must indicate whether the Assessing Officer is satisfied that the case of the assessee involves concealment of particulars of income or furnishing of inaccurate particulars of income or both, with clarity. If the notice is issued in the printed form, then, the necessary portions which are not applicable are required to be struck off, so as to indicate with clarity the nature of the satisfaction recorded. In both Samson Perinchery and New Era Sova Mine(supra), the notices issued had not struck off the portion which were inapplicable. From this, the Division Bench concluded that there was no proper record of satisfaction or proper application of mind in matter of initiation of penalty proceedings.

7. In the present case, as well if the notice dated 30/09/2016 (at page 33) is perused, it is apparent that the relevant portions have not been struck off. This coupled with the fact adverted to in paragraph (5) of this order, leaves no ground for interference with the impugned order. The impugned order are quite consistent by the law laid down in the case of *Samson Perinchery and New Era Sova Mine*(supra) and therefore, warrant no interference.”

b) PCIT v. Shri Hafeez S Contractor [ITA No. 796 with 872 of 2016] [Bombay High Court]

“3. It is admitted position that the facts and the law applicable in both the assessment years are identical. The impugned order of the Tribunal allowed the respondent’s appeals. This on holding that no penalty is imposable under Section 271(1)(c) of the Act for the reason that at the time of initiating penalty proceedings or even at the time of issuing show-cause notices for imposition of penalty, the Assessing Officer had not specified whether the penalty proceedings are on account of concealment of particulars or furnishing incorrect details / particulars. In the absence of the same being specified, the entire proceedings were held to be without jurisdiction.”

c) Manu Engineering v. CIT [122 ITR 306] [Gujarat High Court]

“We find from the order of the IAC in the penalty proceedings, that is, the final conclusion as expressed in para. 4 of the order : “I am of the opinion that it well have to be said that the assessee had concealed its income and/or that it had furnished inaccurate particulars of such income”. Now, the language of “and/or” may be proper in issuing a notice as to penalty order or framing of charge in a criminal case or a quasi- criminal case, but it was incumbent upon the IAC to come to a positive finding as to whether there was concealment of income by the assessee or whether any inaccurate particulars of such

income had been furnished by the assessee. No such clear-cut finding was reached by the IAC was liable to be struck down.”

d) CIT v. Manjunatha Cotton and Ginning Factory [359 ITR 565] [Karnataka High Court]

“d) Existence of conditions stipulated in Section 271(1)(c) is a sine qua non for initiation of penalty proceedings under Section 271.

e) The existence of such conditions should be discernable from the Assessment order or order of the Appellate Authority or Revisional Authority.

....

(p) Notice under Section 274 of the Act should specifically state the grounds mentioned in section 271(1)(c), i.e., whether it is for concealment of income or for furnishing incorrect particulars of income.

(q) Sending printed form where all the ground mentioned in Section 271 are mentioned would not satisfy requirement of the law.”

e) Pr.CIT v. New Era Sova Mine [Tax Appeal No. 70 of 2018] [Bombay High Court]

f) Mrs. Indrani Sunil Pillai v. ACIT (ITA No. 1339/Mum/2016) (ITAT Mumbai)

g) Vidyavardhini v. ACIT (ITA No. 3730/Mum/2014) (ITAT Mumbai)

h) Uttam Value Steels Ltd. v. ACIT (ITA No. 3622/Mum/2016) (ITAT Mumbai)

i) Uma Shankar Agarwal v. DCIT (ITA No.s 1831 to 1835/Kol/2009) (ITAT Kolkata)

19. Further, even in cases where satisfaction was categorically recorded in the Assessment Order, but since there was no strike off of the inapplicable clause in the penalty notice, some courts held the penalty proceedings to be invalid:

a) *CTI v. SSA Emerald Meadows [ITA No. 380 of 2015] [Karnataka High Court]*

The following substantial question of law pertaining to validity of notice u/s 274 of the Act and thus, the validity of penalty proceedings was raised by the Revenue before the Hon'ble High Court:

“(2) Whether, on the facts and in the circumstances of the case, the Tribunal was justified in holding that the penalty notice under Section 274 r.w.s. 271(1)(c) in bad in law and invalid despite the amendment of section 271(1B) with retrospective effect and by virtue of the amendment, the assessing officer has initiated the penalty by properly recording the satisfaction for the same?

(3) Whether on the facts and in the circumstances of the case, the Tribunal was justified in deciding the appeal against the Revenue on the basis of notice under Section 274 without taking into consideration the assessment order when the assessing officer has specified that the assessee has concealed particulars of income?

The Hon'ble Karnataka High Court upheld the order of the Hon'ble Tribunal wherein after placing reliance on the decision of the jurisdiction High Court in the case of *CIT v. Manjunatha Cotton and Ginning Factory (359 ITR 565)* it was held that the notice issued u/s 274 r.w.s. 271(1)(c) of the Act was bad in law as it did not specify which limb of section 271(1)(c) of the Act, the penalty proceedings had been initiated for. Subsequently, the SLP filed by the revenue against the said order of the Hon'ble High Court was dismissed by the Hon'ble Supreme Court.

b) *Meherjee Cassinath Holdings P. Ltd. v. ACIT (ITA No. 2555/Mum/2012) (ITAT Mumbai)*

c) *M/s Orbit Enterprises v. ITO (ITA No. 1596/Mum/2014) (ITAT Mumbai)*

d) *Dr. Sarita Milind Davare v. ACIT (ITA No. 2187/Mum/2014) (ITAT Mumbai)*

e) *Sachin Arora v. ITO (ITA No 118/ Agra/2015) (ITAT Agra)*

F. LATEST BOMBAY HIGH COURT JUDGMENT CHANGES THE PARADIGM

20. Recently, the Hon'ble Bombay High Court in the case of *Ventura Textiles Ltd v. CIT [Income Tax Appeal No. 958 of 2017]* has changed the paradigm which was more or less settled and has given rise to new avenues in relation to penalty provisions in general and specifically in respect to satisfaction of the Taxing Officer.

21. Brief Facts of the case

- The assessment proceedings for AY 2003-04 concluded vide Assessment Order passed u/s 143(3) on 28.02.2006 wherein an addition of Rs. 62,47,460/- was made, which was claimed as bad debt u/s 36(1)(vii) by the assessee in the return of income, by holding that the amount was not a debt and it was further held that the amount was not admissible u/s 37(1) as well. The above addition was also confirmed by CIT(A).
- In the said assessment order, the Assessing Officer initiated penalty proceedings u/s 271(1)(c) by categorically stating that the assessee had furnished inaccurate particulars of income. Further, the Assessing Officer issued a show cause notice u/s 274 r.w.s. 271(1)(c) on the same date i.e. 28.02.2006, however, the Assessing Officer did not strike off the inapplicable portion in the said notice.
- By penalty order dated 14.02.2014, Assessing Officer held that by making an improper and unsubstantiated claim of bad debt of Rs. 62,47,460.00/-, the assessee had wilfully reduced its incidence of taxation, thereby concealing its income as well as furnishing inaccurate particulars of income. Therefore, invoking Section 271(1)(c) of the Act, the Assessing Officer imposed the minimum penalty,

being 100% of the amount of tax. Such imposition of penalty was upheld by the CIT(Appeal) as well as the Hon'ble ITAT. Hence, the assessee preferred an appeal before the Hon'ble High Court.

22. Arguments of the Assessee on the validity of satisfaction of the Assessing Officer:

One of the contentions raised by the appellant before the Hon'ble High Court was that the non-striking of the inapplicable portion in the notice u/s 274 r.w.s. 271(1)(c) of the Act vitiated the penalty proceedings. The learned counsel for the appellant submitted that at the outset, the notice issued to the petitioner under Section 274 read with Section 271 of the Act proposing to impose penalty was in printed format but the inapplicable portion therein was not struck off. Consequently, whether penalty was sought to be imposed for concealment of particulars of income or for furnishing inaccurate particulars of such income was not indicated in the notice. Since, penalty proceeding is initiated by the show cause notice, non-striking off the inapplicable portion in the notice reflects non-application of mind and vitiates penalty proceedings.

23. Interesting observations made by the Hon'ble High Court:

- If the Assessing Officer proposes to invoke the first limb, then the notice has to be appropriately marked. Similarly, if the Assessing Officer wants to invoke the second limb then the notice has also to be appropriately marked. If there is no striking off of the inapplicable portion in the notice which is in printed format, it would lead to an inference as to non-application of mind. In such a case, penalty would not be sustainable. [Para 17]
- It is noticed that the Assessing Officer had ordered that since the assessee had furnished inaccurate particulars

of income, penalty proceedings under Section 271(1)(c) were also initiated separately. Therefore, it was apparent that penalty proceedings were initiated for furnishing inaccurate particulars of income. Further in the statutory show-cause notice under Section 274 read with Section 271 of the Act proposing to impose penalty was issued, though at the bottom of the notice it was mentioned 'delete inappropriate words and paragraphs', unfortunately, the Assessing Officer omitted to strike off the inapplicable portion in the notice i.e., whether the penalty was sought to be imposed for concealment of particulars of income or for furnishing inaccurate particulars of such income. Such omission certainly reflects a mechanical approach and non-application of mind on the part of the Assessing Officer. [Para 22 and 23]

- On the basis of the facts of the case, it was observed that the penalty proceedings were initiated for furnishing of inaccurate particulars of income and on analysis it was held that the assessee had declared full facts and there was no furnishing of inaccurate particulars of income. Accordingly, the penalty was deleted on this ground. [Para 35 and 36]

24. Observation on the issue of validity of show cause notice

Addressing the above contention, the Hon'ble High Court held that **if the assessment order and the show cause notice for penalty, both issued on the same date i.e., on 28.02.2006, are read in conjunction, a view can reasonably be taken that notwithstanding the defective notice, assessee was fully aware of the reason as to why the Assessing Officer sought to impose penalty.** The purpose of a notice is to make the noticee aware of the ground(s) of notice and that it would be too technical and pedantic to take the view that because in the printed notice the inapplicable portion was not

struck off, the order of penalty should be set aside even though in the assessment order it was clearly mentioned that penalty proceedings under Section 271(1)(c) of the Act had been initiated separately for furnishing inaccurate particulars of income.

25. Further, the judgement held that,

“26. Reverting back to the facts of the present case, if the assessment order and the show cause notice, both issued on the same date i.e., on 28.02.2006, are read in conjunction, a view can reasonably be taken that notwithstanding the defective notice, assessee was fully aware of the reason as to why the Assessing Officer sought to impose penalty. It was quite clear that for breach of the second limb of Section 271 (1)(c) of the Act i.e., for furnishing inaccurate particulars of income that the penalty proceedings were initiated.”

G. WHAT CONSTITUTES ASSESSEE BEING AWARE?

26. The Hon’ble Bombay High Court in the case of *Ventura Textiles Ltd v. CIT (supra)* deliberated over the question of whether the assessee had notice as to why the penalty was sought to be imposed on it. For answering the above question, the Hon’ble Bench interpreted the meaning of the term ‘notice’ by adverting to different definitions and Supreme Court judgments and concluded that *“The purpose of a notice is to make the noticee aware of the grounds of notice.”*

27. Accordingly, the **Hon’ble Bombay High Court** held the non-striking off of the inapplicable portion in the penalty show cause notice to not be invalid by stating that the assessee was aware of the allegation of penalty against him as he had notice of why the charge was being levied. This observation by the Hon’ble Bombay High Court, even though is very case specific, raises a moot question,

‘What constitutes that the assessee is aware of the charge?’

28. Interestingly, this very question was examined and answered extensively by the Hon’ble Andhra Pradesh High Court in the case of *CIT v. Chandulal [(1985) 152 ITR 238]*, wherein numerous instances were enumerated which would lead to an assumption that the assessee was aware of the allegations against him. The relevant extract is as under:

“So long as the object of putting the assessee in the awareness and knowledge of the initiation of the penalty proceedings is accomplished by the issuance of a notice, the question of invalidity does not arise on account of either inappropriate language in the notice or on account of any inappropriate portions of the notice not being struck off. There was no offence to any of the rules prescribed in as much as the notice is given to secure the assessee’s explanation to fulfil the requirement of natural justice. It is not in dispute that the assessee did not entertain any doubt in his mind when he received the notice issued by the ITO under s. 274. If the assessee was under a mistaken view about the real intent and effect of the notice issued, he could have asked the ITO to clarify whether the penalty proceedings were initiated for concealment of income or for furnishing inaccurate particulars of such income. In the present case, it is not denied that in the explanation given to the ITO in response to the notice issued under s. 274, the assessee did not raise any objection on the ground that the notice did not convey the nature of offence committed by him. No objection was also taken regarding the validity of the notice on that ground. It is, therefore, clear that the assessee was not under any misapprehension about the offence alleged against him. There was proper understanding and indeed, in the explanation filed, the assessee dealt with the reasons for contending that no penalty could be levied under s. 271(1)(c). It was not shown to us that any prejudice was caused to the assessee on account of the assessee not

being put in the knowledge of the nature of offence committed by him. The contention regarding the validity of the notice was urged only during the course of the appeal before the Tribunal and it seems to us that the explanation was only an after-thought. The assessee certainly understood the offence

alleged against him and showed cause to the ITO by pointing of s. 274 would apply not only to concealment of income but also for furnishing inaccurate particulars of such income and where the offence is two-fold, there is no need on the part of the ITO to strike off any inappropriate portions.”

H. ANALYSIS OF VALIDITY/ LEGALITY OF PENALTY PROCEEDINGS UNDER DIFFERENT CIRCUMSTANCES:

Sr. No.	Scenario	Analysis
1.	Specific charge u/s 271(1)(c) of the Act is mentioned in the assessment order and inapplicable portion is struck off in notice u/s 274 r.w.s. 271(1)(c) of the Act	Penalty proceedings shall be valid .
2.	Specific charge u/s 271(1)(c) of the Act is not mentioned in the assessment order and inapplicable portion is not struck off in notice u/s 274 r.w.s. 271(1)(c) of the Act:	Generally, the conclusion in such a scenario is that the assessee is not aware about the charge alleged against him which would impair his rights of reasonable opportunity of being heard as the assessee is rendered incapable of defending himself without knowing the clear allegations against him. Further, as discussed above it is well settled by various judicial precedents that no penalty can be levied when there is neither any specific charge u/s 271(1)(c) of the Act mentioned in the assessment order nor the inapplicable portion has been struck off in notice u/s 274 r.w.s. 271(1)(c) of the Act. Therefore, the penalty proceedings shall be invalid . [Refer cases in Paragraph 18 above]
3.	Specific charge u/s 271(1)(c) of the Act is not mentioned in the assessment order and inapplicable portion is struck off in notice u/s 274 r.w.s. 271(1)(c) of the Act:	Even though the specific charge is not mentioned in the Assessment order, the striking off the inapplicable portion in the penalty show cause notice would infer that the Taxing Officer is satisfied and the assessee has been made aware of the charge levied on him. Therefore, the penalty proceedings shall be valid .

Sr. No.	Scenario	Analysis
4.	Specific charge u/s 271(1)(c) of the Act is mentioned in the assessment order and inapplicable portion is not struck off in notice u/s 274 r.w.s. 271(1)(c) of the Act:	If specific charge u/s 271(1)(c) of the Act is mentioned in the assessment order and inapplicable portion is not struck off in notice u/s 274 r.w.s. 271(1)(c) of the Act, then while deciding the validity of the penalty proceedings, the following cases may emerge:
Case A	Whether penalty notice u/s 274 r.w.s. 271(1)(c) of the Act was issued after the date of issue of assessment order?	While contemplating the validity of penalty proceedings vis-à-vis the requirements of law regarding notice u/s 274 of the Act, the Hon'ble Karnataka High Court in the case of <i>CIT v. Manjunatha Cotton and Ginning Factory (359 ITR 565)</i> noted that if the order passed by the relevant Authority categorically records a finding regarding the specific charge against the assessee u/s 271(1)(c) of the Act and then the penalty proceedings are initiated, then the notice to be issued u/s 274 of the Act could conveniently refer to the above order which contains the satisfaction of the relevant Authority passing such order. Accordingly, in such cases, penalty proceedings shall be valid .
Case B	Whether penalty notice u/s 274 r.w.s. 271(1)(c) of the Act was issued before the completion of the assessment proceedings?	The Hon'ble Bombay High Court in the case of <i>CIT v. Smt Kaushalya Devi [(1995) 216 ITR 660] (Bom HC)</i> , held that the vagueness and the ambiguity in the notice prejudiced the right of reasonable opportunity of being heard of the assessee and quashed the penalty proceedings. Accordingly, in such cases, penalty proceedings shall be invalid .
Case C	Whether assessment order and penalty notice u/s 274 r.w.s. 271(1)(c) of the Act were issued on the same date?	If the answer to the above question is in the affirmative, then following the decision of the Hon'ble Bombay High Court in the case of <i>Ventura Textiles Ltd v. CIT [Supra]</i> , it can be concluded that the penalty proceedings shall not be vitiated by reason of non-striking off of inapplicable portion in notice u/s 274 r.w.s. 271(1)(c) of the Act, if specific charge is mentioned in the assessment order.

Sr. No.	Scenario	Analysis
		<p>Contrary Judgements with identical facts in the case of <i>Meherjee Cassinath Holdings P. Ltd v. ACIT (ITA No. 2555/Mum/2012)</i> and <i>M/s Orbit Enterprises v. ITO (ITA No. 1596/Mum/2014)</i> held the penalty proceedings to be invalid. However, the same have been now superseded by the Hon'ble Bombay High Court case of <i>Ventura Textiles Ltd. (supra)</i>. Accordingly, in such cases, penalty proceedings shall be valid.</p>

APPLICABILITY OF PRINCIPLES IN NEW PROVISION

29. As stated earlier, the provisions of section 271 of the Act have been replaced by section 270A of the Act from AY 2017-18. The offences for which penalty is leviable u/s 270A of the Act are **under reporting of income** and **under reporting of income in consequence of misreporting thereof**. Similar to quondam provision of section 271 of the Act, the new section 270A of the Act also confers discretionary power on the relevant Taxing Authority to levy penalty i.e. levy of penalty is not automatic u/s 270A of the Act which is evident from the wordings of the section “*The Assessing Officer or the Commissioner (Appeals) or the Principal Commissioner or Commissioner may, during the course of any proceedings under this Act, direct that any person...*” The implication of such a discretionary power is that the relevant Taxing Authority will be required to prima facie satisfy himself that an offence, as provided in section 270A of the Act i.e. either under-reporting of income or under-reporting of income in consequence of misreporting thereof has been committed, to initiate penalty proceedings under the said section. Accordingly, the principles laid down by various judicial precedents relevant to section 271 of the Act as discussed above in so far as giving ‘direction’ for penalty and recording of satisfaction of the

relevant Taxing Authority is concerned, shall equally apply to the new section 270A of the Act.



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