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Faceless Penalty Scheme, 2021

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Introduction

Under the overarching banner of 'Transparent Taxation – Honouring the Honest', the Central Government had introduced Faceless Assessment Scheme 2019, Faceless Appeal Scheme 2020 and the Taxpayer's Charter. Moving forward, the Parliament had inserted sub-section 2A to Section 274 of the Income Tax Act, 1961 ('**Act**'). This amendment empowered the Central Government for framing a scheme for e-penalty proceedings. Pursuant to this amendment, the Central Board of Direct Taxes ('**CBDT**') has announced the *Faceless Penalty Scheme 2021*[1] ('**Scheme**') effective from 12 January 2021.

Notable features of this scheme are:

i) Proceedings conducted by dynamic jurisdiction through various units.

ii) A national unit to act as a focal point for all communication.

iii) Notices to be delivered *via* electronic communication i.e., SMS, E-mail, etc.

iv) Personal hearing *via* video conferencing to be granted in certain circumstances only.

v) All communication between the units to be made electronically.

Structure for the Scheme

CBDT has proposed to set up the following '**Centres**':

i) National Faceless Penalty Centre ('**NFPC**') – Communication between the units and with the assessee, assignment of cases to penalty unit, decide on imposition or non-imposition of penalty after issuance of draft order and decide whether draft penalty order needs review.

ii) Regional Faceless Penalty Centres ('**RFPC**') will have administrative supervision over the penalty units and jurisdiction to decide on request for personal hearing.

iii) Penalty Units ('**PU**') will draft the penalty order. It will identify the points and issues, provide an opportunity of hearing to the assessee and analyse the material(s) on record.

iv) Penalty Review Units ('**PRU**') will review the draft penalty order. It will check whether the facts, relevant evidence, law, and judicial decisions have been considered in the order. It will also review the arithmetical correctness of computation of penalty.

Till the time these centres are set up by CBDT, the penalty proceedings will be undertaken by the centres and units set-up under the Faceless Assessment System[2].

Salient Features of the Scheme

- ***Authentication and Delivery of Electronic Record:*** Electronic records can be authenticated by an assessee by

[1] CBDT Notification S.O. 118(E) [No. 02/2021/F.NO.370142/51/2020-TPL], dated 12 January 2021.

[2] Sub-para(4) of Para (4) of the scheme. CBDT Order F. NO. 187/4/2021-ITA-I, Dated 20-1-2021.

electronic verification code or by digital signature.

All electronic communications will be made by the department by sending the authenticated copy to the assessee's registered email address, or Mobile App, or on the registered electronic filing account on the portal ('**Registered Account**'). The assessee will receive an alert of such communication by way of SMS, or an update on his/her email address or mobile app.

- ***No Physical interface between the assessee and revenue authorities:*** An assessee will not be required to appear before any income tax authority. He/she will file the response against any communication through the Registered Account electronically. However, an assessee may apply for personal hearing to the Chief Commissioner / Director General of the relevant RFPC. If approved, the hearing would be conducted by video conferencing.
- ***Team Based Proceedings:*** NFPC will act as a focal point of contact for all the parties of the proceedings. PRU will review the draft penalty order prepared by the PU.
- ***Appellate Proceedings:*** An appeal against the order of NFPC can be made before the Commissioner (Appeals) having jurisdiction over the jurisdictional income tax authority or before the National Faceless Appeal Centre.
- ***Dynamic Jurisdiction for Penalty Proceedings:*** The cases for penalty proceedings may be allotted to any PU under any RFPC by an automated allocation system. The case of an assessee can be undertaken from any part in India. For instance, an assessee in city A of State B may be assessed by a PU in city C of State D.

Procedure to be followed in penalty proceedings

1. The income tax authority ('**ITA**') or the NFAC shall refer cases to NFPC. In these cases, the penalty proceedings would have either been initiated or been recommended for initiation.
2. NFPC will assign the matter to a PU under any RFPC.
   - 2.1. In cases where initiation of penalty proceeding is recommended, PU will examine the materials available on record. It can either disagree with the recommendations (subject to recording reasons) or can agree with the recommendation and draft the SCN. PU will send the reasons or SCN to NFPC.
   - 2.2. In cases where penalty proceedings are already initiated, the PU shall prepare a draft show cause notice (SCN) and send it to NFPC.
   - 2.3. Depending on the PU's proposal, NFPC can either serve the SCN on the assessee or decide not to initiate the penalty proceedings.
3. The assessee must file the response to the SCN within the prescribed time limit. Extension of time can be sought by the assessee by applying to NFPC.
4. NFPC will send assessee's response to the PU and if no response is filed then it will inform PU about it.
5. PU can now request NFPC:

5.1. to obtain further information from the assessee or ITA/NFAC; or

5.2. to seek technical assistance or to conduct verification.

6. Upon PU's request in point (5), NFPC can make appropriate requisition to the assessee or ITA/NFAC. For technical assistance or verification, NFPC shall request NFAC to furnish a report within a prescribed time-period. Information or report received by NFPC will be forwarded to PU.

7. After considering all the materials on record including the responses and the report, PU may:

7.1. propose for imposition of penalty and prepare a draft order; or

7.2. propose for non-imposition of penalty and record the reasons.

8. PU will send its proposal along with the draft order or the recorded reasons to the NFPC.

9. NFPC has to examine the proposal in accordance with the risk management strategy by way of an automated examination tool. After examining it NFPC may decide:

9.1. to pass the penalty order as per the draft, and serve the order to the assessee; or

9.2. not to impose the penalty as per the proposal, and inform the assessee about it; or

9.3. assign the case to a PRU under any of the RFPC for review.

10. The PRU may either concur with the proposal or suggest modification to it and record reasons for such modification.

11. If PRU has concurred with the proposal, then NFPC will pass an order as per PU's proposal.

12. If PRU has suggested certain modifications, then NFPC will assign the case to a specific PU other than the PU which initially proposed the imposition or non-imposition of penalty.

13. The new PU will examine all the materials on record including the suggestions and reasons of the PRU. If modifications suggested by PRU are prejudicial to the interest of the assessee, the PU will follow the procedure from point (2.2) to (7) to prepare the revised draft penalty order. If modifications suggested are not prejudicial to the interest of the assessee, then the PU will prepare a revised draft penalty order. PU may also propose non-imposition of penalty and record the reasons for it.

14. NFPC shall pass the penalty order as per the draft prepared by the new PU and serve a copy of the order to the assessee and the ITA/NFAC. If the NFPC has received reasons for non-imposition of penalty, then NFPC shall not impose penalty and inform the assessee and ITA/NFAC about it.

Regardless of the above-mentioned procedure, the Principal Chief Commissioner, or the Principal Director General (who is in charge of the National Faceless Penalty Centre) can transfer penalty proceedings to the income-tax authority / NFAC. The proceedings may be transferred at any stage with the prior approval of the CBDT.

Procedure to be followed in proceedings for rectification

An application for rectification of mistake can be filed with the NFPC by an assessee, PU, PRU or Income tax authority / NFAC. This application will be allotted to a PU for examination by NFPC. PU shall serve a notice to the assessee, if the application is filed by revenue and *vice versa,* to show cause why rectification should not be carried out. After the response to such notice is filed with NFPC and forwarded to PU, the PU will draft an order either to accept or reject the application. NFPC will receive the draft order along with reasons from PU. NFPC will pass the order and communicate it to the assessee.

Important points for the Assessee

1. Assessee should ensure to put correct email ID and contact number in the e-filling portal.
2. Assessee should regularly check the portal and keep a track of the timelines.
3. As personal hearing may not be allowed in every case, prompt and detailed responses must be submitted against any notice. Facts must be explained in detail and all relevant evidence must be uploaded. Reliance on relevant judicial precedents must be explained properly in the response.
4. As all the relevant documents have to be submitted electronically, they must be scanned and uploaded online carefully.

Authors' view

The Scheme is expected to reduce the chances of error in penalty order and discretion of tax officer in the penalty proceedings.

Risk management Strategy and automated examination tool have not been defined in the Scheme. We would have to wait for CBDT's clarification to get a better understanding.

The circumstances in which the assessee may be granted a right to personal hearing *via* video conferencing has neither been provided in the Scheme nor has been notified by the CBDT separately. Therefore, a suitable clarification is awaited. The lack of reasonable opportunity of being heard may be considered as violation of principles of natural justice and may become an issue of litigation.

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Notification

Extension of the deadline of Vivad se Vishwas Scheme

CBDT *vide* Notification No. 04/2021, dated 31 January 2021 has extended the last date for filing declaration under Section 3 of the Direct Tax Vivad se Vishwas Act, 2020. Now the last date is 28 February 2021.

Ratio Decidendi

Rectification – Limitation commences from original order if issue in consideration is not appealed

Relying on the judgement of Supreme Court[3] and Karnataka High Court[4], ITAT Bengaluru has held that the period of limitation for rectification under Section 154 of the Income Tax Act would commence from the date of original order if the subject matter of the appeal is not related to the subject matter of the rectification order.

The taxpayer/assessee, for Assessment Year 2002-03, declared his income 'NIL' by deducting unabsorbed depreciation from the net profit of the assessee. The assessment order under Section 143(3) was passed by AO on 10 February 2005 computing book profit under Section 115JB. CIT exercising its revisionary power under Section 263 disallowed two expenditures as capital expenditure. Against which the assessee filed an appeal before ITAT. ITAT remanded back the matter for fresh adjudication. Pursuant to which, AO on 20 October 2011 passed the assessment order disallowing the expenditures as capital expenditure. The appeal against the same is pending before CIT(A).

Meanwhile, AO passed a rectification order under Section 154 wherein deduction under Section 80IA was disallowed. Assessee objected against the rectification order and pressed it on the ground of limitation. AO held that the limitation will be calculated from 20 October 2011 and relied on the doctrine of merger. Therefore, he concluded that the rectification order was not barred by limitation. On appeal, CIT(A) upheld the rectification order passed by AO. The ITAT however held that the period of limitation would be calculated from 10 February 2005 and not from 20 October 2011. The appeal of the assessee was allowed and order of CIT(A) was set aside**.** [*Karnataka Power Corporation Ltd.* v. *ACIT* - Order dated 11 January 2021 in ITA No. 282/Bang/2017, ITAT Bengaluru]

TDS exemption on LTC when employee takes a circuitous route involving a foreign leg

Pursuant to the survey proceedings, the AO found that assessee had failed to deduct TDS under Section 192 of the Income Tax Act, 1961 on the salary of the employee. The AO observed that the exemption of LTC under Section 10(5) was available to the employee only when he travels in India and through shortest route, however, in the present facts, employee had devised circuitous route involving a foreign leg. Therefore, it was held that the grant of LTC would not fall under exemption available under Section 10(5) and the assessee wrongly determined the income of the employee. The CIT(A) upheld the order of the AO on the same ground.

On appeal, ITAT Mumbai Bench relied on the decision of Madhya Pradesh High Court[5] and held that the duty is cast upon the employer-assessee to assess the income of the employee in a *bona fide* manner. It noted that the tax withholding obligation is clearly in respect of 'estimated income of the assessee' and not in respect of 'taxable income of the assessee' and hence as long as the conduct of the employer in this exercise is *bona fide*, he cannot be said to be wanting in his conduct under Section 192. It noted that Section 10(5) does not require the

[3] *CIT* v. *Alagendran Finance Ltd*. - (2007) 293 ITR 1 (SC).
[4] *Kothari Industrial Corporation Limited* v. *Agri. ITO* - 230 ITR 306.
[5] *CIT* v. *Gwalior Rayon & Silk Mills Ltd*. - 140 ITR 832.

employee to take the shortest route to 'any place in India' and that it only restricts the amount of exemption to fare of the national carrier by the shortest route by way of Rule 2B. Therefore, per Section 10(5) read with Rule 2B of the Income Tax Rules, the employer is supposed to grant exemption of LTC for the shortest route of travel to the employees. Although, the employee travel through different route, LTC exemption should be granted on the shortest route available for the travel. It was held that in the present case, assessee-employer acted in a *bona fide* way while calculating LTC exemption. Therefore, the appeal was allowed and proceeding under Section 201 was quashed. [*SBI* v. *ACIT* – Order dated 27 January 2021 in ITA No. 1717/Mum/2019, ITAT Mumbai]

No liability of withholding tax if provision not present on date of payment – Subsequent retrospective change in law is not material

During Financial Year 2011-12, assessee paid lease line charges for internet services rendered to it by a supplier without deducting tax at source. AO disallowed the expenditure under Section 40(a)(ia) of the Income Tax Act, 1961 on the ground that TDS was not deducted by the assessee under Section 194J and the payment for lease line charges was royalty in nature as per amendment brought in Section 9(1)(vi) *vide* Finance Act, 2012 with retrospective effect from 1 June 1976. On appeal, CIT(A) upheld the order of the AO on the same ground.

On appeal, ITAT Pune Bench held that the payment was made between two residents and as per amended Section 9(1)(vi) lease line charges qualify as royalty. However, Tribunal noted that liability to withhold tax cannot be fastened on the assessee when at the time of making payment the provision was not enacted. In present facts, payment was made in Financial Year 2011-12 and the provision was amended through Finance Act, 2012. Noting that the provision was retrospective but when the payment was made the provision was not effective, the Tribunal allowed the appeal of the assessee. [*DCIT* v. *Barclays Technology Centre India Pvt. Ltd.* – Order dated 12 January 2021 in ITA No.601/PUN/2017, ITAT Pune]

No TDS on sale of assets by liquidator – IBC Section 53 to have overriding effect on Section 194-IA of Income Tax Act

In a dispute involving interface of income tax and the insolvency provisions, the NCLAT has held that Section 53(1)(e) of the Insolvency and Bankruptcy Code, 2016 shall have overriding effect on the provisions of the Section 194-IA of the Income Tax Act, 1961. The Appellate Tribunal noted that with regard to the recovery of Government dues (including income tax) from the company in liquidation under IBC, there is inconsistency between Section 194-IA of the Income Tax Act and Section 53(1)(e) of the IBC, because as per Section 194-IA, 1% TDS is to be recovered on priority to other creditors of the transferor, whereas, Section 53(1)(e) provides that the Government dues come fifth in the order of priority. Setting aside the NCLT Order, the NCLAT observed that adjudicating Authority had erroneously held that the deduction of tax at source does not mean raising demand for collection of tax by the Department. [*Om Prakash Agrawal* v. *Chief Commissioner* – Judgement dated 8 February 2021 in Company Appeal (AT) (Insolvency) No. 624 of 2020, NCLAT]

Adjustment of refund against outstanding demand without issuance of intimation under Section 245 is illegal – Adjustment of refund against stayed demand is also illegal

The Petitioner appealed against additions to its return of income for AY 2017-18 and sought a

stay of demand before the CIT(A). Stay of demand was granted subject to the payment of 20% of demand. The Petitioner deposited 10% and requested for the remaining 10% to be adjusted against refund due to the assessee. Without any prior notice under Section 245 of the Income Tax Act, 1961, the AO adjusted the entire refund due to the petitioner for an amount exceeding the remaining 10%.

Before the High Court, the assessee contended that:

- In terms of CBDT Instruction No.1914 read with Office Memorandum and assessing officer's order, the petitioner was mandated to only deposit a sum of 20% of the outstanding demand and therefore, the department could not have recovered a higher sum from the refund due of the AY 2018-19.

- Recovery of demands which have been stayed by the Revenue Authorities has no legal sanction.

- Since CBDT Instruction has binding authority on the Assessing Officer, adjustment of refund under Section 245 for more than 20% was illegal.

- Adjustment was made without issuing any notice under Section 245 prior to such adjustment, and a notice under Section 245 issued after such adjustment of refund, was also illegal.

Placing reliance on the decision of Division Bench of the Andhra Pradesh High Court in case of *Japson Estates (P) Ltd.* and decision of Delhi High Court in case of *Glaxo Smith Kline Asia (P) Ltd.*, the Telangana High Court held that adjustment was per se illegal, as it was done without issuing a prior intimation under Section 245 of the Act. Further, noting that there existed no outstanding demand because of the stay, it held that adjustment of refund beyond what was required to grant stay was not allowable. [*TSI Business Parks Hyderabad Pvt. Ltd.* – TS-39-HC-2021(TEL)]

Absence of specific mention on retrospectivity of the provision makes it prospective

The Madras High Court has held that insertion of provision of Section 234D of the Income Tax Act, 1961 is substantive provision and therefore, in the absence of any express words used in the provision making levy of interest retrospective, it can only be prospective, i.e., from the date on which it came into force. The Court was also of the view that merely because the order of assessment was passed subsequent to the insertion of the said provision in the law, it would not make the said provision retrospective. It held that in the absence of any specific mention, the amended provision shall come into force only after the commencement of the assessment and cannot be applied retrospectively. [*Commissioner v. S.R.A Systems Ltd.* – [2021] 123 taxmann.com 469 (Madras)]

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