

# EY Tax Alert

## HC holds penalty imposed under Section 122 is a civil liability

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### Executive summary

This Tax Alert summarizes recent ruling of the Allahabad High Court (HC)<sup>1</sup> on whether the penalty leviable under Section 122 of the Central Goods and Services Tax Act, 2017 (CGST Act) is civil or criminal in nature. Further, whether dropping of proceedings under Section 74 of CGST Act will *ipso facto abate* the proceedings under Section 122.

The key observations of the HC are:

- ▶ Section 74 is a charging and a machinery provision for the recovery of tax assessed and imposition of penalty. Section 122 is a penal provision aimed at curbing evasion of taxes. Both the charging Sections are required to be interpreted strictly.
- ▶ *Mens rea* is essential in criminal law, but in civil matters like taxation, it is irrelevant for imposing civil liability.
- ▶ For imposition of penalty, a statute shall determine whether *mens rea* is required or not. For offences involving prosecution under a statute, *mens rea* or guilty intent is a *sine qua non*.
- ▶ Unlike Section 122, offences under Section 132 are far more serious in nature and therefore, the legislature has chosen to impose criminal punishment for the same.

Accordingly, penalty imposed under section 122 is a civil liability and the offences can be adjudicated by the proper officer or adjudicating officer.

Further, when SCN is issued both under Section 73/ 74 and also under Section 122 against the main person, dropping of proceedings under Section 73/ 74 would not automatically result in dropping of proceedings under Section 122 as the proceedings are with respect to contravention of two different offences.

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<sup>1</sup>2025-VIL-540-ALH



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# Background

- ▶ Petitioner, engaged in manufacturing of fast-moving consumer goods, is alleged of being indulged in circular trading without actual supply or receipt of goods.

A show-cause notice (SCN) was issued under Section 74 of the Central Goods and Services Tax Act, 2017 (CGST Act) proposing tax demand along with penalty under Section 122.

- ▶ Subsequently, tax demands under Section 74 were dropped in adjudication order, but penalty was confirmed under Section 122.
- ▶ Aggrieved, the petitioner filed writ petition before the Allahabad High Court (HC).
- ▶ The HC framed the following two questions for consideration:
  - ▶ Whether the “proper officer or adjudicating officer” has the power to adjudicate on the penalty provision under Section 122 of the CGST Act?
  - ▶ Whether dropping of proceedings under Section 74 will *ipso facto abate* the proceedings under Section 122 of the CGST Act?

## High Court Ruling

### Meaning of offence and penalty

- ▶ The word “offence” does not necessarily under all circumstances mean a crime that is required to be tried by the criminal court. A contravention of a rule/law wherein criminal proceedings are not initiated but only penalty is imposed for the purpose of deterrence would also amount to an offence.
- ▶ Penalty may be imposed in cases where there is a simple violation of a law or for omission to do a particular act without there being any *mens rea*. On the other hand, penalty may also be imposed for serious contravention of the law with or without *mens rea* that may amount to an offence for the purpose of deterrence and punishment.
- ▶ A statute may provide for further punishment by prosecution for the same offence/contravention, if the legislature deems it necessary.

### Interpretation of Statutes

- ▶ Section 74 at once is a charging and a machinery provision for the recovery of tax assessed and imposition of penalty.
- ▶ Section 122 is a penal provision aimed at curbing evasion of taxes.
- ▶ Both Sections 74 and 122 being charging sections are required to be interpreted strictly and plain

meaning to the word used therein should be provided by the courts.

### *Penalty in Tax Delinquency Cases*

- ▶ *Mens rea* is an essential element in criminal law for prosecuting an accused whereas in civil matters such as taxation *mens rea* is irrelevant for imposing civil liability.
- ▶ The object of the legislature in enacting a penalty provision is not to provide for punishment under criminal law but to provide a deterrent penalty.
- ▶ *Corpus Juris Secundum* states that “a penalty imposed for a tax delinquency is a civil obligation, remedial and coercive in its nature and is far different from the penalty for a crime or a fine or a forfeiture provided as punishment for violation of criminal and penal laws”.
- ▶ It is the scheme of a particular statute that shall determine whether for imposition of penalty there is a requirement for *mens rea* or not. However, when a taxing statute speaks of prosecution, for those offences *mens rea* or guilty intent is a *sine qua non*.

### *Difference between section 122 and section 132*

- ▶ Section 132 lists out only nine offences in contradiction to Section 122 of the CGST Act that enumerates twenty-one offences.
- ▶ Offences under Section 132 are far more serious in nature and therefore the legislature has chosen to impose criminal punishment for the same.
- ▶ Proviso to section 138 provides that compounding shall be allowed only after making payment of tax, interest and penalty involved in such offences. This is an indication that the legislature never intended to treat Section 122 as an offence prosecutable and punishable by way of a criminal trial.

### *Dropping of proceedings under section 74*

- ▶ From a reading of the Circular no. 171/03/2022-GST dated July 6, 2022, it is clear that the contravention under Section 73/ 74 need not necessarily be a contravention covered under Section 122 of the CGST Act.
- ▶ When SCN is issued against the main person u/s 73/74 and also against the main person u/s 122, dropping of proceedings u/s 73/74 would not automatically result in dropping of proceedings u/s 122 against the main person as the proceedings are with respect to contravention of two different offences.

### *Conclusion*

- ▶ The proceeding under Section 122 is to be adjudicated by the adjudicating officer and is not required to undergo prosecution.

- ▶ Abatement of proceedings under Section 74 of the CGST Act does not *ipso facto* abate the proceedings under Section 122 which are for completely different offences.

## Comments

- a. CBIC issued Circular 171/03/2022-GST dated 6 July 2022 clarifying tax and penal implications for transactions involving fake invoices.
- b. Section 75(13) of CGST Act provides that where any penalty is imposed under section 73 or section 74 or section 74A, no penalty for the same act or omission shall be imposed on the same person under any other provision of the Act.

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