

EY Tax Alert

Indian Government's Public Policy Think Tank, NITI Aayog, recommends decriminalization of various tax-related offences and procedural defaults

Executive summary

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This Tax Alert summarizes the Indian Government's Public Policy Think Tank, Niti Aayog's, paper titled "Towards India Tax Transformation: Decriminalising and Trust-Based Governance" (Paper)¹ published in October 2025. Out of the various themes that have been identified by the 'Consultative Group on Tax Policy' formed by NITI Aayog to facilitate ease of doing business, promote Foreign Direct Investment (FDI), simplify tax laws and processes and make the system future-ready, this Paper focusses on recommending measures to decriminalize the old stringent provisions resulting in prosecution even for minor or technical defaults under Income Tax Law² (ITL). This Paper aims to recommend a move from a fear-driven compliance model to a cooperative, trust-based system that reserves criminal prosecution only for deliberate, fraudulent tax evasion.

The Paper outlines the four foundational principles for criminalization: (1) it should protect fundamental societal values such as law and order, national security and property; (2) only those conducts causing clear and substantial harm should be criminalized; (3) criminal law should be used as a last resort when civil or administrative remedies are inadequate; and (4) punishment must be proportionate to culpability. The Paper also emphasizes that drafting of offences must be precise, non-duplicative and periodically reviewed to remove the outdated provisions.

The Paper, applying these principles, categorizes its recommendations on different offenses under ITL into three groups: (a) 12 offences to be fully decriminalized, (b) 17 offences to be partially decriminalized and (c) 6 offences to be retained as criminal with proportionate punishment.

¹ https://niti.gov.in/sites/default/files/2025-10/Report_Tax_Policy_Working_Paper_Series_II.pdf

² Income-tax Act, 1961 read with Income-tax Rule, 1962. Now, revamped by Income-tax Act, 2025 w.e.f. 1 April 2026



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Further, the Paper also recommends rationalizing the punishment framework which include abolishing mandatory minimum sentences that restricts judicial discretion, aligning imprisonment terms with the Bharatiya Nyaya Sanhita³, suggesting shift from rigorous imprisonment, removing the presumption of guilty intent, and simplifying legal drafting under the SARAL (Simple, Accessible, Rational, and Actionable Law) principle.

Background

- ▶ In India's tax framework, criminal penalties are traditionally used as a key tool to ensure compliance. The ITL included 54 offences across 15 provisions, many of which addressed technical or procedural lapses rather than deliberate fraud. This approach of criminalization is influenced by the Direct Taxes Enquiry Committee Report 1971, which stated that monetary penalties alone were not enough to deter non-compliance and that the "prospect of landing in jail" would encourage better adherence to tax laws.
- ▶ Over time, this approach is found to have undergone change. The said approach is seen as excessive and disproportionate to committed default and at odds with the government's focus on ease of doing business and ease of living. The shift in approach is evidenced where Central Board of Direct Taxes (CBDT)⁴ in its subsequent Circulars⁵ advised that prosecution should generally be avoided in minor or technical cases and that compounding of offences should be encouraged where appropriate. Criminal action, on the other end, should be limited to serious violations involving willful tax evasion or fraudulent behavior.
- ▶ Additionally, criminal prosecution for minor non-compliances has severe and lasting consequences such as disqualification from public employment, loss of voting rights or professional restrictions that disproportionate to the underlying infraction.
- ▶ Shift in approach is also evidenced in the revamped ITL 2025⁶, which aims to shift the focus toward simplicity, clarity and accessibility. It decriminalizes 13 offences. Despite that there are yet 35 offences across 13 provisions remain criminalized, and in some cases, the law still places the burden of proof on the accused, similar to the treatment under more stringent criminal statutes.
- ▶ In this background, in October 2025, NITI⁷ Aayog's "Consultative Group on Tax Policy" released its working Paper (Paper) under the

"Viksit Bharat 2047" vision titled "Towards India Tax Transformation: Decriminalising and Trust-Based Governance". The Paper aims to provide suggestions to move from a fear-driven compliance model to a cooperative, trust-based system, reserving criminal penalties only for serious cases involving willful tax evasion or fraud.

Foundational principles for criminalization:

- ▶ The Paper, drawing on judicial precedents⁸, expert committee reports and Law Commission recommendations, highlights the basic construct for framing criminal law as a coercive instrument of the State and should be applied only to the conducts that pose a direct threat to fundamental societal values. It must be used sparingly and only when essential to protect core values of the society and the political order.
- ▶ The Paper identifies following general principles for criminalization:
 - **Criminalization must protect a fundamental societal value:**
 - The purpose of criminalization should be to safeguard values that are essential for governance and public order such as law and order, national security, life, liberty, property and social harmony. Regulatory lapses that do not threaten these values should attract only civil or administrative consequences.
 - For instance, failure to have inventory valued by a cost accountant under the ITL would not meet this principle, as it does not endanger any fundamental societal value so as to provide criminal consequences. In contrast, willful tax evasion, which undermines the nation's economic security, would satisfy this requirement.
 - **Criminalization must address a clear, direct and substantial harm:**
 - The criminalization should be only of the conduct that causes real, measurable harm to values not mere inconvenience, offence or moral disapproval. The harm must be specific, identifiable, demonstrable and directly linked to the conduct.

³ The Bharatiya Nyaya Sanhita (BNS), 2023, is India's new criminal law code that replaced the Indian Penal Code, 1860 (IPC)

⁴ The apex body administration of direct taxes in India

⁵ Manual on Prosecution and Compounding 2020 - Volume I, Income-tax Department, New Delhi

⁶ Income-tax Act, 2025 replacing Income-tax Act, 1961

⁷ National Institution for Transforming India (NITI) is the premier public policy think tank of the Government of India

⁸ Federation of Obstetrics & Gynaecological Societies of India v. Union of India (2019) 6 SCC 283, Arundhati Roy, (2002) 3 SCC 343, Harsh Mander v. Union of India ((2018) SCC OnLine Del 10427), Navtej Johar v. Union of India ((2018) 1 SCC 791), P. Rathinam v. Union of India ((1994) 3 SCC 394) and Joseph Shine v. Union of India ((2019) 3 SCC 39)

- For instance, failure to assist in inspection of records under the ITL may not cause a direct or substantial harm and, therefore, may not justify criminalization, whereas fraudulent transfer of property to defeat tax recovery has a clear and direct harmful consequence and warrants criminalization.
- **Criminalization must be the only efficient and effective solution:**
 - Criminalization must remain an instrument of last resort and shall be deployed only when other civil, regulatory or administrative mechanisms cannot effectively achieve the goal. Criminal punishment should be justified only if it serves legitimate objectives such as deterrence, incapacitation or restitution.
 - For instance, non-filing of income-tax returns as directed by the tax authority though non-compliant, can be effectively addressed through civil or administrative penalties. However, deliberate falsification of statements resulting in significant tax evasion (e.g., INR2.5mn or more) may warrant criminalization.
- **Criminalization and imposition of criminal punishment must be a proportionate response to harm:**
 - The punishment should align with seriousness of the crime. Criminalization should be only when necessary and not applied by default. The punishment must reflect culpability, distinguishing between intentional, reckless and accidental acts.
 - For instance, mere failure to produce accounts or documents may not justify criminalization, whereas the willful fabrication or falsification of entries in books of accounts with an intent to evade tax should attract criminal liability.

► The Paper further identifies following general considerations while drafting criminal provisions:

- When drafting criminal provisions under tax law to avoid duplication with general criminal statutes and ensure consistency in punishment
- Pre-legislative assessments must evaluate fiscal impact on enforcement agencies and the capacity of the justice system.
- Laws should respect constitutional rights, avoid criminalizing protected activities such as privacy or speech and prevent

disproportionate impact on marginalized groups.

- Criminal law must not be used to enforce moral beliefs unless justified by clear public harm.
- Drafting must not be omnibus, with offences explicitly defined and punishments proportionate to the severity of the act. First-time violations should be addressed through alternative sanctions like fines, community service or diversion programs rather than imprisonment.
- Periodic legislative review is necessary to identify and remove outdated or redundant offences.

International tax practice:

The Paper also considers international best practices in countries like the U.S., U.K. and Germany which reserve criminal action for the most egregious cases of deliberate and fraudulent tax evasion, while using civil penalties for other non-compliances.

Decriminalization or retention of criminal provisions of ITL 2025:

► In light of the above principles of criminalization, the Paper has reviewed the prosecution provisions of ITL 2025. Based on fulfilment of the principles, the Paper has recommended following three categories of reforms in prosecution provisions:

► **Category 1: The provisions which are suggested to be decriminalized:**

- The Paper has suggested decriminalization of 12 offenses which, *inter alia*, involve failure to pay withholding tax and tax collected at source, failure to furnish returns in search cases, willful failure to produce documents or comply with a direction for audit/valuation.
- For example, Section (S.) 479 of ITL 2025 (corresponding to S. 276CC of ITL 1961) criminalizes willful failure to file a return of income within the prescribed time, provided the default is without reasonable cause and the tax liability exceeds a specified threshold of INR2.5mn.
- The Paper notes that this provision does not fully satisfy the four foundational principles of criminalization. It notes that failure to furnish return of income is a procedural lapse and does not itself indicate an intent to evade tax. There are various reasons ranging from personal hardship to technical glitches in filing tax returns.

- According to Paper, therefore, failure to furnish return of income within specified time does not in itself cause direct and substantial harm to public for criminalizing the default. The ITL imposes harsh and disproportionate punishment even where such act attracts civil penalties and requires reconsideration.

Harm to protected value	Requirement of intent	Proportionality of punishment
Not met	Not met (willful attempt is considered and not fraudulent intent)	Not met

► **Category 2: The provisions which are suggested to be partially decriminalized:**

- The Paper has suggested partial decriminalization of 17 offenses like knowingly making a false statement in verification, contravention of order of deemed seizure, willful attempt to evade taxes, failure to provide assistance in investigation of books of accounts, etc.
- For example, S.478 of ITL 2025 (corresponding to S.276C of ITL 1961) deals with willful attempt to evade tax by underreporting income in excess of INR2.50mn. It prescribes rigorous imprisonment ranging from six months to seven years, along with a fine, depending on the quantum of tax sought to be evaded.
- The Paper notes that evasion of tax liability by underreporting of income poses direct threat to fiscal integrity of the country. However, prosecution should be limited to action conducted due to fraudulent intent only. Any underreporting of income due to bona fide error, technical oversight, should be decriminalized. The punishment in applying provisions to all defaults regardless of their cause is disproportionate to the action of underreporting of income.
- The Paper has, therefore, recommended partial decriminalization of this action of underreporting of income by restricting punishment to cases of underreporting of income by fraudulent intent. Additionally, it also recommends increasing the threshold limit of INR2.50mn to INR10mn where punishment provided for is rigorous imprisonment.

Harm to protected value	Requirement of intent	Proportionality of punishment
Met	Not met	Not met

► **Category 3: The provisions which are suggested to be not decriminalized**

- The Paper has suggested retaining prosecution for 6 offenses like fraudulent removal, concealment or transfer of property to prevent tax recovery, abetment of a false return or statement etc.
- For example, S.484 of ITL 2025 (corresponding to S.277A of ITL 1961) deals with willfully making false entry or statement in books of accounts or documents to enable other person to evade tax. Notably, the provision does not require proof that the second person actually succeeded in evading tax—the offence is complete upon the act of falsification with intent. This act is punishable with imprisonment of 3 months to 2 years with fine.
- The Paper notes that this provision fulfils all the principles of criminalization as *mens rea* is required for invoking provision. This sets higher threshold for criminal liability and distinguishes from conduct of technical or bona fide errors.
- The Paper states that criminalization is preferred for such offence but in minor or first-time contravention only civil penalties should be sufficient.

Harm to protected value	Requirement of intent	Proportionality of punishment
Met	Met	Not met (for minor cases)

Recommendations for the rationalization of the punishment framework:

- The Paper proposes amendments to the existing criminal offenses in ITL which are not aligned with a trust-based governance system. Imprisonment terms and forms, which are typically reserved for grave and serious offenses, are used excessively, creating a need for reform to ensure punishments are just, fair, and reasonable.
- **Remove mandatory minimum sentences:** The Paper identifies that ITL imposes mandatory minimum imprisonment in 25 of 35 offences (approx. 71%), severely restricting judicial discretion of the court. Comparable Union laws prescribe such minima in only ~13% of cases. Minimum terms even for minor defaults like failure to deposit tax deducted at source equate these offenses with heinous crimes (e.g., child prostitution or grievous hurt under the BNS). Hence, it recommends abolishing mandatory minima and restoring judicial discretion to ensure proportionate sentencing.

- ▶ **Rationalize imprisonment terms and reinstate discretion:** The Paper identifies that nearly 38% of offences under ITL carry imprisonment up to seven years which is excessive for tax defaults. For example, failing to provide data assistance draws two years' imprisonment, while a comparable BNS offence carries one month. Hence, it recommends aligning punishments with the BNS and permits courts to impose imprisonment, fine or both, as monetary harm can often be redressed through recovery and penalties, imprisonment should not be the default.
- ▶ **Amend rigorous-imprisonment mandate:** The Paper identifies about 97% of imprisonable offences prescribe rigorous imprisonment under ITL, while only 7-11% of offences under general laws or the BNS call for such imprisonment. Even serious crimes like attempts to murder permit judicial choice. It recommends amending provisions to allow "either form of imprisonment" based on the nature of offence.
- ▶ **Omit presumption of culpable mental state:** The Provisions of ITL presume guilty intent ("willfully" or "fraudulently") and shifts the burden of proof on the accused which is appropriate only for grave statutes like Narcotic Drugs and Psychotropic Substances Act or The Protection of Children from Sexual Offences Act. Hence, it recommends deleting the presumption of culpable mental state.
- ▶ **Simplify and clarify drafting:** Paper identifies that current provisions are complex, cross-referenced and inaccessible to average citizen. Hence, it recommends redrafting offences following the SARAL principle (Simple, Accessible, Rational, and Actionable Law) and each section should clearly specify the prohibited act, intent and punishment in direct, plain language.

Comments

NITI Aayog serves as the Government's policy advisory body, a think tank that formulates long-term strategies and promotes innovation in governance. Over time, it has proposed a range of reforms across sectors. Recently, in the tax domain, it has recommended measures to refine tax rules relating to the determination of permanent establishment and attribution of profits⁹.

In the similar breadth, as a welcome move by NITI Aayog it recommends aligning the criminal provisions under the ITL with the Union Government's broader vision of fostering a trust-based governance system and a compliance-first culture. These recommendations are consistent with the Government's ongoing efforts under the Jan Vishwas¹⁰ initiatives (1.0 and 2.0), as outlined in the Union Budget 2025, which aim to promote decriminalization and enhance the ease of doing business.

The recommendations include (a) removal of the presumption of culpable mental state (b) abolition of mandatory minimum sentences and restoration of judicial discretion to adopt principles of proportionality of punishment. These are critical proposal to align the tax provisions with the principles of general criminal jurisprudence as reflected in the BNS.

While these are progressive recommendations, their success may largely depend on the strengthening of civil and administrative enforcement mechanisms. Effective enforcement may be needed to ensure that habitual or willful defaulters do not exploit decriminalization to avoid liability under the guise of "technical or procedural lapses". Ensuring this balance between leniency for genuine taxpayers and deterrence for deliberate evasion may stand as critical test for the success of these reforms.

⁹ Refer EY Tax Alert, dated 7 October 2025, titled "Indian Government's Public Policy Think Tank, NITI Aayog, recommends a presumptive tax regime for foreign enterprises"

¹⁰ The Jan Vishwas legislation is an initiative by the Indian government to decriminalize minor offenses to promote ease of living and doing business under allied laws.

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