

Self-Assessment no longer 'at large' in GST Inquiry



CA. A Jatin Christopher

The author is member of the Institute. He can be reached at jatin.christopher@gmail.com and eboard@icai.in

Audit is guided by the due process laid down in section 65 and enforcement relies on section 67 of Central GST Act for its due process. Enforcement wing in different states called anti-evasion or intelligence has always had the entire 'assessment at large' to look into every aspect of compliance by taxpayer. GST has spread this responsibility to ensure taxpayer's self-assessment of tax payable in different sections from section 61 to be limited to scrutinize returns, section 65 to conduct audit and section 67 to conduct inspection-search-seizure. Read on...

Enforcement is not audit

Audit is defined in section 2(13) and the mandate is "to verify correctness" of GST compliance. This is the provision where taxpayer's self-assessment is 'at large' before the Audit Officers. But that's exactly why audit cannot be undertaken when proceedings are undertaken in section 67 of Central GST Act. Enforcement Officers recognize the absence of non-specific and routine nature of review of taxpayer's compliance in the very provision that permits inspection-search-seizure.

To select a taxpayer for audit, there are no pre-conditions to be fulfilled. Commissioner or any delegate may issue

a general or specific order stating that audit of a registered person be undertaken. It is the wisdom of the Commissioner to expeditiously deploy limited resources available to audit taxpayers. Risk-based approach would be a possible approach for the Commissioner to follow. There are certain industries that may be considered 'prone to risk of (revenue) leakage', namely, industries that:

- involve suppliers who operate in a 'impoverished' compliance ecosystem;
- supply to end-consumers who show 'indifference' to tax compliance;
- operate with unwritten and implied contractual structure.



Then there's product-risk, that is, those goods or services supplied which are prone to tax avoidance and deficient compliance. And there's entity-risk, where intelligence gathered raises questions about scruples of certain entities. While these categories of risk as well as examples are author's own imagination but is provided to extrapolate to the considerations of each Commissioner.

Commissioner's choice in audit selection – industry or product or entity – does not come in for any judicial scrutiny. Commissioner is at liberty to exercise his discretion and there are no safeguards for a taxpayer except that this discretion is left in the hands of a high-ranking Officer of the tax department. Apex Court held that:

“A discretionary power is not necessarily a discriminatory power and abuse of power is not easily to be assumed where the discretion is vested in the Government and not in a minor official.”

Matajog Dobey v. HC Bhari
AIR 1956 SC 44

Where specific intelligence is gathered that a firm in an industry is indulging in questionable transactions of a specific nature, certainly that firm can be included within the 'Commissioner's discretion' and audit conducted. In so doing, not only can those specific transactions be verified but all other associated transactions of the firm. Audit Officers are free to limit the scope of their review

and are not obliged to cover 'all' aspects of GST compliance by that firm. For the reason that even audit must ultimately culminate in the issuance of a show cause notice in the manner prescribed to demand tax or credit. And completion of audit is no bar in issuing show cause notice on any other matter, whether falling within the scope of audit or not, as long as this new demand stays within the period of limitation in law.

It is, therefore, possible to conclude that the authority to audit may overlap with enforcement but the converse does not apply, that is, enforcement proceedings cannot authorize the conduct of proceedings in the nature of audit under section 65, certainly not in the manner contemplated in section 2(13) of Central GST Act.

Jurisdiction for departmental action

Jurisdiction is not a reference limited to the geographical limits to which the authority of an Officer extends. It also refers to the authority of an Officer to act in accordance with law and the circumstances or conditions that confers this authority to so act. GST is a self-assessment-based tax and for this reason, there is no general authority to call for books and records and determine liability akin to departmental assessment (under earlier tax regime). Entire liability stands assessed 'by self' and any intervention must strictly be in accordance with 'due process' laid down in the law. Privy Council held that:



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“When a statute requires a thing to be done in a particular manner, it must be done in that manner or not at all.”

Nazir Ahmad v. King Emperor
AIR 1936 PC 253

Where there is no jurisdiction, the action is illegal, and any discovery is vitiated. Preventing leakage of revenue does not authorize glossing over 'due process' in law. Due process is the embodiment of 'justice in action' whether in judicial, quasi-judicial or administrative action touching rights of citizens in those proceedings. To this end, all departmental action remains constrained to uphold the 'Rule of Law'. And following words of Apex Court are apposite:

“Legitimacy of the result intended to be achieved does not necessarily imply that every means to achieve it is permissible; for even if the end is desirable and permissible, the

means employed must not transgress the limits laid down by the Constitution...."

Sakal Papers (P) Ltd. & Ors v. UoI AIR 1962 SC 305

Passion to prevent leakage of revenue is not the domain of tax administration, Legislature too desires exactly this. And for this purpose, Legislature laid down 'due process' so that not only is leakage of revenue arrested but is done while upholding Rule of Law. And to borrow the words from another decision of Apex Court:

"From a positivistic point of view, equality is antithetic to arbitrariness. In fact equality and arbitrariness are sworn enemies; one belongs to the rule of law in a republic while the other, to the whim and caprice of an absolute monarch. Where an act is arbitrary it is implicit in it that it is unequal both according to political logic and constitutional law and is therefore violative of Art. 14, and if it affects any matter relating to public employment, it is also violative of Art. 16. Arts. 14 and 16 strike at arbitrariness in State action and ensure fairness and equality of treatment. They require that State action must be based on valent relevant principles applicable alike to all similarly situate and it must not be guided by any extraneous or irrelevant considerations because that would be denial of equality. Where the operative reason for State action,

as distinguished from motive inducing from the antechamber of the mind, is not legitimate and relevant but is extraneous and outside the area of permissible considerations, it would : amount to mala fide exercise of power and that is hit by Arts. 14 and 16. Mala fide exercise of Power and arbitrariness are different lethal radiations emanating from the same vice : in fact the later comprehends the former."

EP Royappa v. State of TN
AIR 1974 SC 555

Principles of natural justice are not limited to judicial actions but is now well accepted to be required in quasi-judicial and administrative actions. Apex Court has held that:

"15. Effect of civil consequences arising out of determination of lis under a statue is stated in State of Orissa v. Dr (Miss) Binapani Dey and Ors. (1967) 2 SCR 625. It is an authority for the proposition when by reason of action of the part of a statutory authority, civil or evil consequence ensue, principles of natural justice are required to be followed. In such an event, although no express provisions is laid down in this behalf compliance of principles of natural justice would be implicit. In case of denial of principles of natural justice in a statute, the same may also be held to be ultra vires Article 14 of

the Constitution."

Rajesh Kumar & Ors. v. Dy.CIT & Ors. (2007) 2 SCC 181

Jurisdiction for commencement of enforcement proceedings

Section 67 of Central GST Act furnishes the jurisdiction for enforcement *qua* 'taxable person' differently from 'any person'. In so far as taxable person is concerned, it is evident that such person ought to attract section 9 and not necessarily be a registered person under section 22 of Central GST Act. Taxable person is defined in like manner in section 2(107) of Central GST Act.

At the outset, authority is vested with Proper Officer 'not below' the rank of Joint Commissioner who must hold 'reasons to believe' about certain specific matters laid down in section 67(1)(a) *qua* taxable person and section 67(1)(b) *qua* any person to invoke the authority in section 67 of Central GST Act.

Reasons to believe *qua* taxable person must pertain to any one or all of the matters listed in section 67(1)(a) of Central GST Act and no others. One might argue that in the definition of audit in section 2(13) of Central GST Act that takes within its sweep correctness of turnover declared, taxes paid, refund claimed and input tax credit availed, and to assess compliance with provisions of Act or rules, could well cover the specific matters listed in section 67(1)(a) of Central GST Act too. But here, question is

not whether audit under section 65 can inquire into matters covered under section 67 of Central GST Act but whether proceedings under section 67 can inquire into matters covered under section 65 of Central GST Act without the pre-requisites of 'reasons to believe'.

Therefore, it is not only that those very specific matters are to be inquired in proceedings under section 67 of Central GST Act but also that 'reasons to believe' must pre-exist commencement of any proceedings about 'evasion of tax'. Here lies taxpayers safeguards that improper exercise of authority in section 67 of Central GST Act does not authorize going into matters that lie beyond those reasons to believe.

On a perusal of the specific matters listed in section 67(1)(a) of Central GST Act, 'evasion of tax' runs like a common thread



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in all those matters. First, where taxable person '**has suppressed**' either supply or stock of goods, evasion of tax is inbuilt when there's suppression. Second, where taxable person '**has claimed**' input tax credit in excess of his entitlement is not the result of an exercise to determine 'entitlement' but one where the claim is ex facie in excess. Lastly, where taxable '**has indulged**' in contravention to evade payment of tax needs no elaboration.

And reasons to believe qua any person identifies (i) such person as one who is engaged in transportation of goods or operates a warehouse (ii-a) where such transportation or warehouse is involved in keeping goods which have escaped tax or (ii-b) where accounts or goods are kept such that evasion is likely to be imminent result. If goods are no longer available (in transit or storage), there is no inference that can be drawn about the conveyance or warehouse. Similarly, past investigation into evasion or other antecedents of taxpayer do not furnish reasons by themselves, unless there is material available in each new and current instance to invoke provisions of section 67(1)(b) of Central GST Act. Therefore, the question of 'reasons to believe' assumes plenary position as it touches jurisdiction.

Reasons to believe

Suspicion is not sufficient to furnish 'reasons to believe'. Suspicion is the product of an analytical mind examining available information and

locating some incongruity in the data. Suspicion is a comparison of what is with what ought to be. Suspicion can arise even when everything is matching because it is an ideal that may not be possible in every area of compliance.

Reasons to believe requires that the belief must be held in good faith and it cannot be a mere pretence. Reasons must pre-exist to support the grant of authorization to inspect the premises of taxable person (or any person). Reasons cannot be discovered after conducting inspection. Apex Court held:

"The belief must be held in good faith: it cannot be merely a pretence. To put it differently it is open to the Court to examine the question whether the reasons for the belief have a rational connection or a relevant bearing to the formation of the belief and, are not extraneous or irrelevant to the purpose of the section."

S Narayanappa & Ors. v. CIT
AIR 1967 SC 523

Whether a *bona fide* mistake or even misinformation could furnish reasons to believe, requires reference to the guidance of Apex Court which held:

"The words 'consider is necessary' postulate that the authority concerned has thought over the matter deliberately and with care and it has been found necessary as a result of such thinking to pass the order.....If the



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impugned order were to show that there has been no careful thinking or proper application of mind as to the necessity of obtaining and examining the documents specified in the order, the essential requisite to the makings of the order would be held to be non-existent.....

If, however, there has been consideration of the matter regarding the necessity to obtain and examine all the documents and an order is passed thereafter, the Court would stay its hand in the matter and would not substitute its own opinion for that of the authority concerned regarding the necessity to obtain the documents in question."

Barium Chemicals Ltd. &
Anr. v. AJ Rana & Ors. AIR
1972 SC 591

Since Legislature desired to allow Proper Officer to inspect premises, section 67 of Central GST Act contains all these safeguards, that is, to (i) require that there be reasons to believe (in evasion of tax), (ii) this authority be left in the hands of

no less than Joint Commissioner to be satisfied (with evasion) and (iii) specify the circumstances in clause (a) and (b) to inspect the location(s). Compare this law-making effort with the language in section 67(1) with that in section 65(1) of Central GST Act.

Inspection of a premises is an extremely invasive power that may be exercised without prior notice to taxable person (or any person) provided the Proper Officer has 'reasons to believe'. These 'reasons to believe' must be founded on some material or grounds and either stated in the search warrant (INS1) itself or in a record (such as, file noting) anterior in time to the actual issuance of such warrant. And if these were to be called into question, contemporaneous records would be available for the Court to examine and satisfy itself – that there were reasons to believe in the form and manner specified in section 67(1) of Central GST Act – for authorizing such extreme action and that the action was not taken for extraneous and irrelevant reasons.

Waiver by taxpayer

Failure to explicitly question validity of inspection proceedings or implicitly acquiescing to proceedings by reply on merits may result in waiver of taxpayer-rights, as provided in section 160(2) of Central GST Act. Taxpayers' own acquiescence can result in forfeiture of remedies against invalid proceedings. It is, therefore, imperative that every inspection be questioned as to

its validity. Taxable person (or any person) may not be required to prevent inspection on own suspicion about its validity but retain this ground and call it into question in any process such as inquiry or notice issued pursuant to these proceedings. This taxpayer safeguard is evident in the instruction issued by CBIC 1/2020-21 dated 2 Feb 2021.

Whether section 160(2) of Central GST Act will be successfully side-stepping taxpayer's remedies and cause irreparable prejudice even if there were any discovery in illegal inspection without any pre-existing 'reasons to believe', is still to be raised for judicial consideration. But it cannot be ignored that when a notice is issued raising legitimate questions about the correctness of compliance, taxpayer runs risk of responding on merits in view of the prohibition from raising grounds that were not raised in earlier proceedings in rule 112 of Central GST Rules.

Grant of authorization

Authorization must be granted



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in Form GST INS1 'before' conducting inspection. And if reasons to believe furnish jurisdiction to inspect, those reasons (with all its ingredients and their due consideration) must also exist prior to grant of such authorization. While it is not necessary to disclose the reasons to believe in the authorization, but it is not permissible for it to be undisclosed on the files.

Authorization in Form GST INS1 contains three Parts. Part A relates to inspection of premises of taxable person. This 'taxable person' is defined in section 2(107) to be a person who is registered or liable to register. Part B relates to inspection of premises of any person who is not the taxable person. Such person is one who (i) is engaged in business of transporting or warehousing goods and (ii) such goods transported or stored, have escaped payment of tax or (iii) such person has kept accounts or goods which could result in evasion. Part C relates to articles liable to seizure.

Jurisdiction for commencement of search proceedings

Search proceedings under section 67(2) can be initiated "*pursuant to an inspection carried out*", that is, there may be a 'discovery' during inspection that justifies that search to be conducted.

Authorization granted in INS1 with reasons to justify 'inspection only' indicates that there were no reasons to justify 'inspection and search'. Even

if there may have been some suspicion earlier but since authorization granted was limited to conduct inspection only, search cannot be conducted beyond the scope of authorization granted.

Section 67(2) also authorizes search to be conducted "*otherwise*" than pursuant to inspection, indicates that reasons may exist *a priori* that are already sufficient to justify both 'inspect and search' to be conducted. In such cases, authorization must be accordingly granted. Form GST INS1 contains Part C, where provision is made for recording reasons that form the ingredients to conduct search.

Once authorized, search can be conducted in respect of (i) goods liable to confiscation are secreted or (ii) documents, books or things (which would be useful for any proceedings) are secreted, under section 67(2) of Central GST Act. It is very important to note that search cannot be authorized by 'guesswork' that the said articles may be 'secreted'. Some material must be available on record and after due consideration of such material along with attendant circumstances, a reasonable conclusion may be drawn that at the said place of inspection, the said articles are 'secreted'. It is not necessary to have proof of said articles being secreted but certainly some reliable material which is more than mere suspicion, howsoever logical and plausible it may be, must exist which furnishes the 'reasons to believe' (discussed earlier).

Out-of-bounds in enforcement

Enforcement extends to all actions authorized by section 67 and 68 and not under section 61 to 65. With respect to inspection under section 67, persons who do not satisfy the criteria listed in section 67(1)(a) or (b), cannot be brought within the operation of enforcement proceedings. Reasons to believe may exist but such reasons must identify the (i) persons to be inspected and (ii) locations to be inspected. Deficiencies in identifying the specific persons and specific locations, would render the inspection unauthorized either against incorrect persons or at incorrect locations.

Further, enforcement action by tax administration cannot take-up matters such as (i) classification (ii) valuation (iii) input tax credit (iv) monthly returns and annual returns (v) other compliance matters, even if there may be errors in taxpayer's self-assessment carried out. Any enforcement action on these matters must involve reasons to believe that taxable person (a) has suppressed supply or stock or (b) has availed input tax credit beyond entitlement or (c) has indulged in any contravention to evade tax. If all these comprehensive ingredients are not found to exist as documented at the time of grant of authorization, enforcement action will be illegal and contrary to law.

Failure to question the legality of such improper authorization

results in forfeiture of remedy available in law due to section 160(2). But the time to question the validity of authorization granted will not be lost and are due only after conclusion of inspection and / or search proceedings (discussed later).

Comparison with language in different legislations

A quick comparison with provisions under other legislations can explain the boundaries to the power conferred under section 67 when legislature could have given 'expansive powers' under those legislations which are not found in section 67 only indicates that powers under section 67 is 'limited' and not as much as is permitted in those legislations.

"147. If the Assessing Officer has reason to believe that any income chargeable to tax has escaped assessment for any assessment year, he may, subject to the provisions of sections 148 to 153, assess or reassess such income and also any other income chargeable to tax which has escaped assessment and which comes to his notice subsequently in the course of the proceedings under this section, or recompute the loss or the depreciation allowance or any other allowance, as the case may be, for the assessment year concerned"

Section 147 of Income-tax Act

Expansive powers in section 147 of Income-tax Act makes for very interesting comparison in the nature of powers granted by Legislature where not only income escaping assessment (suspected before initiating proceedings) can be brought under assessment but also income "which comes to his notice subsequently in the course of the proceedings". Such expansive powers are conspicuously absent in section 67 of Central GST Act. The guidance, therefore, is that there cannot be 'discovery of reasons' after conducting inspection-search but all reasons which operate as pre-conditions (to furnish jurisdiction to conduct inspection-search) must pre-exist and pre-date visit to premises and clearly stated in INS1 in Parts A, B or C.

Role of Commissioner as Magistrate under section 165(5) of Cr.PC

Code of Criminal Procedure is made applicable to search and seizure under section 67 of Central GST Act. Apex Court has held that:

"We are therefore of opinion that safeguards provided in S.165 also apply to searches made under sub-s. (2). These safeguards are – (i) the empowered officer must have reasonable grounds for believing that anything necessary for the purpose of recovery of tax may be found in any place within the jurisdiction, (ii) he must be of the opinion that such thing cannot be otherwise got without undue delay, (iii) he (sic) must record in writing



Enforcement extends to all actions authorized by section 67 and 68 and not under section 61 to 65.

the grounds of his belief, and (iv) he must specify in such writing so far as possible the thing for which search is to be made. After he has done these things, he can make the search. These safeguards, which in our opinion apply (to, sic) searches under sub-s.(2) also clearly show that the power to search under sub-s.(2) is not arbitrary."

CCT v. RS Jhaver & Ors. AIR 1968 SC 59

In an earlier and authoritative pronouncement it was held that:

"The power of search given under this chapter is incidental to the conduct of investigation the police officer is authorized by law to make. Under s.165 four conditions are imposed : (i) the police officer must have reasonable ground for believing that anything necessary for the purposes of an investigation of an offence cannot, in his opinion, be obtained otherwise than by making a search, without undue delay; (ii) he should record in writing is to be made; (iii) he must conduct the search, if practicable, in person; and (iv) if it is not practicable to make the search himself, he must record in writing

the reasons for not himself making the search and shall authorize a subordinate officer to make the search after specifying in writing the place to be searched, and, so far as possible, the thing for which search is to be made, as search is a process exceedingly arbitrary in character, stringent statutory conditions are imposed on the exercise of the power.”

State of Rajasthan v. Rehman
AIR 1960 SC 210

In view of these safeguards imported into section 67, it is important that person who is issued a notice under section 73, 74, 76 or any other provision must, before responding to the allegations in the notice, make an application to the jurisdictional Commissioner under section 67(10) to be the Magistrate in s.165(5) of Cr.PC which reads as:

“s.165.....

(5) Copies of any record made under sub-section (1) or sub-section (3) shall forthwith be sent to the nearest Magistrate empowered to take cognizance of the offence, and the owner or occupier of the place searched shall, on application, be furnished, free of cost, with a copy of the same by the Magistrate.”

It is therefore imperative that taxpayers make this ‘application’ to Commissioner asking for all the information and then to ‘question’ matters such as jurisdiction, reasons to believe and the ingredients necessary to invoke the provisions of section 67 of Central GST Act.

Access to business premises in section 71 does not authorize inspection

No authority flows on standalone basis from section 71, much less any authority to conduct inspection or search when there is express provision in section 67 of Central GST Act. Similarly, when there is express authority in section 65 and 66 to conduct ‘audit’ and in section 22 to grant ‘registration’ or section 69 to ‘arrest’ offender, there is no authority to conduct any specific proceeding on standalone basis under section 71 of Central GST Act.

Authority conferred under section 71 is “for the purposes of” conducting (i) audit (ii) scrutiny (iii) verification and (iv) checks. Section 71 cannot compete or operate at cross-purposes with authorized proceedings of audit under section 65 or 66 or inspection-search under section 67 of Central GST Act.

Considering that elaborate procedures along with adequate taxpayer-safeguards have been laid down in case of audit and inspection-search under the CGST Act, use of these expressions – audit, scrutiny, verification and checks – cannot authorize yet another provision to conduct a ‘new or special’ kind of inquiry without specifying the (i) nature of inquiry to be conducted and (ii) limits to authority for such inquiry, but only machinery provisions authorizing ‘access to business premises’ for purposes of exercising the authority vested elsewhere in the Central GST Act to audit or inspect premises.

This limitation of authority in section 71 of Central GST Act



No authority flows on standalone basis from section 71, much less any authority to conduct inspection or search when there is express provision in section 67 of Central GST Act.

is forthcoming the fact that “authorized by the proper officer not below Joint Commissioner” is found in the opening words in this section and there is neither a rule corresponding to this section nor a form wherein the Joint Commissioner is to grant authorization. As such, section 71 of Central GST Act precludes taxpayer from refusing access to business premises or to the books and records, to person accessing who is either an Officer acting under section 65 or other specified section provisions of law or to the Special Auditor authorized under section 66 of the Central GST Act.

Conclusion

When power is given to do a particular thing, then that thing must be done only in that manner. This holds good for Central GST Act also where the law does not provide unrestricted authority for intrusive actions. And therefore, the taxpayers should take note of the contours of this authority to avoid any action which lacks due authority. GST comes through in ensuring that diligent taxpayers will truly experience ‘minimum Government, maximum governance.’

