

Towards India's Tax Transformation:

Decriminalisation and Trust-Based Governance

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Historical Context

How Criminalization Crept into the Income-tax Act



Expansion Phase (1961–1980): Most criminal provisions were introduced during this period, when India operated a high-control, regulation-heavy economic model.



Repeated Calls for Reform: Expert bodies—including the Kelkar Committee, Shome Committee, and Tax Administration Reform Commission (TARC)—have consistently recommended decriminalisation and simplification of tax administration.



Outdated Drafting: Several offences still retain language and procedural assumptions from a pre-automation era, predating PAN-based systems, digital records, and faceless assessments.

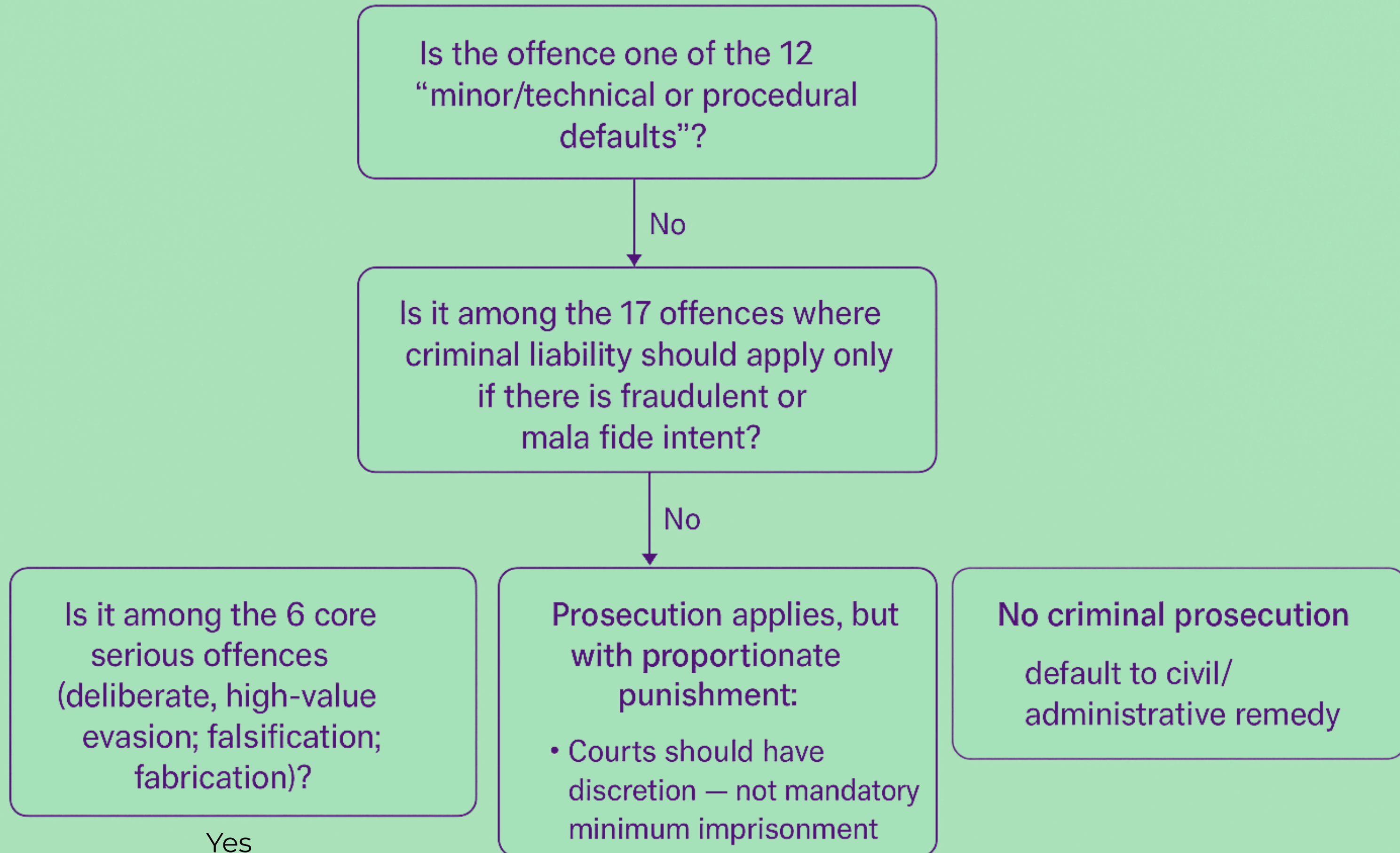


BACKGROUND

- Recently, NITI Aayog released a working paper on “Decriminalisation and Trust-Based Governance” under the Income-tax Act, 2025.
- The Act currently contains several criminal provisions, many relating to technical or procedural lapses.
- The paper argues for shifting from fear-based compliance to a trust-driven, taxpayer-friendly regime.
- Global practices favour civil penalties for minor defaults and criminal action only for deliberate tax evasion.



When Should Criminal Prosecution Apply?



Key Recommendations of NITI Aayog

Decriminalise 12 offences fully and resolve them through civil/monetary penalties.

Keep criminal prosecution for a limited set of serious, high-value evasion cases.

Remove mandatory minimum imprisonment and restore judicial discretion.

Retain criminal liability for other offences only where fraudulent or wilful intent is proven.

Shift burden of proving intent back to tax authorities.

Reclassifies offences based on severity: minor, intent-based, and serious.

Global Alignment on Decriminalisation of Tax Offences

USA (IRS): Criminal cases require proven fraudulent intent, with most non-fraud underreporting dealt with civilly.

Australia (ATO): Negligent misreporting attracts only civil penalties; criminal action is limited to intentional tax evasion.

UK (HMRC): Criminal prosecution is used only for deliberate tax evasion, while mistakes and negligence are handled through civil penalties.

Tier 1 — Fully Decriminalised

Nature of offence	NITI Aayog's recommendation	Our Views
Failure to pay tax collected at source	Section 477 (in the new Act) is criminalised but NITI proposes to omit or decriminalise it because such failures may be due to procedural / technical lapses, not malafide intent.	Agree: Criminalising TCS failures (especially for small or honest mistakes) creates excessive risk for compliance teams.
Failure to furnish return / information / documents	Section 479/480/481 : Some such non-submission offences could be decriminalised entirely, treated as administrative defaults	Use of civil penalties tied to delay / severity for small non-filers to encourage voluntary compliance rather than penal threat.
False statement in verification (minor)	If the false statement results in a tax mis-report that is not very large or is unintentional, criminal liability might be excessive; decriminalisation is recommended for lower-impact cases.	There should be a line between intentional lying vs minor incorrect statements. Retain criminal prosecution only for statements where there is clear evidence of intent to defraud or repeated false verifications.

Tier 2 — Partially Decriminalised

Nature of offence	NITI Aayog's recommendation	Our Views
Under-reporting income (Section 478(1))	Decriminalise the conduct that arises from bonafide error, technical misreporting, or interpretative dispute, without fraudulent intent. The monetary threshold of Rs. 25 lakh should be revised to Rs. 1 crore.	Agree, this aligns with fairness however, if there is suspected intent, proactively correct or disclose and voluntarily pay interest and penalty, ideally before escalation to criminal.
False entries in books of account (Section 478(4)(b))	Criminal liability should remain, but only if there is falsification with intent. For cases involving amounts less than Rs. 1 crore, add a proviso requiring civil penalty award to have been confirmed by the ITAT prior to launching criminal prosecution.	Agree, this avoids penalising genuine bookkeeping error. Self-reporting of suspected material misstatements before they turn into intentional fraud should be encouraged.
Wilfully attempting to evade the payment of any tax, penalty, or interest chargeable or imposable (Section 478)	The framing of the offence lacks precision and specificity. Such vague and broad sections risk blurring lines between minor infractions and fraudulent conduct, and lead to criminalisation of minor or technical non compliances.	While deliberate tax evasion must continue to attract strict criminal consequences, the punishment should always be proportionate to the nature and gravity of the offence. Where non-compliance arises from an honest mistake or lack of intent, such cases should be addressed through civil or administrative remedies instead.

Tier 3 — Core Offences

According to NITI, six core offences should continue to attract criminal sanction, these are:

-  Sec. 475 : Fraudulent removal, transfer, or concealment of property to avoid tax recovery
-  Obstruction of tax enforcement / public servant
-  Sec. 483 : Falsification of books of account or document, etc.
-  Other high-value or deliberate evasion, presumably where tax loss is large & intentional.
-  Sec. 484 : Abetment of false tax returns
-  Possibly fabrication of evidence to mislead tax authorities or courts.

From a compliance perspective, the tiered model is very helpful. It shifts the burden away from “all or nothing” criminal risk, and helps focus on real wrongdoing rather than penalising honest procedural mistakes.

● Criminal punishments such as rigorous imprisonment are disproportionately harsh for most income-tax offences, many of which arise from technical lapses, interpretational differences, or genuine compliance challenges rather than deliberate wrongdoing.

● It is essential that the legislation clearly and precisely defines the specific elements of each offence. Terms such as ‘concealment,’ ‘fraudulent removal,’ or other misconduct indicators should be articulated with objective criteria, monetary thresholds, and clear evidentiary requirements.

● Engaging with the government and tax authorities through consultations to refine these definitions will help ensure that only genuinely culpable conduct is targeted.

● This will significantly reduce the risk of unintended or overbroad criminal exposure for taxpayers and provide much needed certainty for compliance teams in interpreting and applying the law.



IS
CRIMINALISATION
THE WAY ?

- **Reduced Prosecution Volumes:** A significant drop in issuance of prosecution notices is expected as fewer offences will qualify for criminal action.
- **Revised Enforcement Framework:** CBDT is likely to update its Standard Operating Procedures (SOPs) for initiating prosecution in line with the decriminalised regime.
- **Higher Monetary Thresholds:** Cases involving tax amounts below ₹1 crore are expected to fall outside the scope of criminal prosecution.
- **Fewer Accidental Prosecutions:** Lower risk of prosecution arising from data mismatches, minor non-compliances, or technical errors, due to shift towards civil/monetary penalties.



IMPACT ON LITIGATION

Industry Impact of Decriminalisation — Who Gains Most?

NBFCs

- Frequent TDS/TCS, reporting & documentation lapses
- High procedural risk → major relief

Startups

- Return filing delays, TDS gaps, rapid scaling issues
- Reduces founder-level prosecution anxiety

MSMEs

- Cash transaction mismatches
- Procedural errors no longer criminal

E-commerce & Logistics

- E-commerce & Logistics
- TCS mismatches, seller-level reporting issues

Professional Services

- Good compliance capacity; limited direct effect

What Taxpayers Should Start Doing Today.



1. Strengthen Documentation Trails

- Maintain clear back-ups for transactions, invoices, TDS/TCS workings, TP files.
- Ensure version-controlled, searchable records.



2. Self-Audit for “False Entry” Exposure

- Review books for potential mismatches or unsupported entries.
- Reconcile high-risk areas: purchases, loans, cash, journal entries.



3. Maintain Evidence of Good-Faith Conduct

- Archive emails, approvals, instructions, and compliance notes.
- Track timelines showing proactive intent and diligence.



4. Improve Internal Controls

- Put maker-checker processes in place.
- Set triggers for late filings, TDS deposits, and reconciliation gaps.



5. Train Teams on “Intent Classification”

- Ensure staff can distinguish procedural lapse vs. intentional non-compliance.
- Train accounts, compliance, and operations teams.

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THANK YOU