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Interesting Issues in Arrest and Interplay of GST laws, IPC and PMLA

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The recent decision[1] of Supreme Court which has upheld the decision of Telangana & Andhra Pradesh High Court in the matter of PV Ramana Reddy & Others v. Union of India & Others[2], wherein the High Court has held that arrest under goods & services tax laws (GST laws) is not dependent on the assessment, gives power to the authorities to tackle more efficiently with the economic frauds. In other world, the said judgment also gives power to authorities to intimidate genuine taxpayers and subject them to arrest. Hence, either appropriate changes to the legislation are to be done or instructions shall be laid by Central Board of Indirect Taxes & Customs (CBIC) when it comes for implementing the arrest provisions to see that genuine taxpayers are not harassed or subjected to intimidation and personal liberties are safeguarded.

In this article, we shall deal with certain issues pertaining to arrest and related by examining various judgments of different High Courts.

Allahabad High Court - Govind Enterprise's case[3]:

Facts & Allegations:

Petitioner has huge inward supplies but very nominal outward supplies. The bank account given at the time of registration has very few transactions. Investigation revealed that there was another bank account and there were huge cash deposits. Revenue filed First Information Report (FIR) under Section 420, 467, 468, 471, 34, 120B of Indian Penal Code (IPC).

The Revenue alleged that the Petitioner has dealt fraudulently with a dishonest intention, by submitting false documents, with an intention to evade taxes, obtained registration. Thereafter took inward supplies and passed on goods to the end users, without generating outward invoices, received money in cash and deposited in bank account which is not mentioned at time of registration.

Contentions of Petitioner:

Petitioner has contended that no case has been filed under the state goods and services tax act (ST Act) and no assessment has been done. Since assessment is not done, there cannot be any arrest under the state act. Petitioner further contented that since ST Act is a complete code, FIR filed under IPC is legally not sustainable.

Petitioner stated that procedure under ST Act is that power to arrest under Section 69 of ST Act will trigger only if Commissioner has reasons to believe that an offence is committed by taxpayer as mentioned in Section 132(1)(a),(b),(c) and (d) of ST Act. It was the contention that first a proceeding

[1] 2019 (5) TMI 1528 – Supreme Court
[2] 2019 (4) TMI 1320 – Telangana & Andhra Pradesh High Court
[3] 2019 (6) TMI 55 – Allahabad High Court

has to be taken under ST Act and then there can be an arrest after recording satisfaction and accordingly lodging of FIR straightaway is not possible.

Further, the Petitioner has contended that the assuming that offences mentioned in FIR are true in nature, in such case, there can be a maximum of penalty under Section 122 of ST Act and nothing more. Assuming further, that such offences are punishable under Section 132(1)(f)/(k) of ST Act, they become non-cognizable and bailable in terms of Section 132(4) read with 132(5) and (6). Further, by referring to Section 134, the Petitioner further contended that no court has power to take cognizance of an offence punishable under the ST Act except with previous approval of Commissioner. Accordingly lodging of FIR is illegal and proceeding could be initiated only under ST Act and not under IPC and prayed that such FIR has to be quashed and stay on arrest has to be granted.

Contentions of Revenue:

Revenue contended that Section 131 clearly suggests that the provisions of ST Act are without prejudice to the provisions of IPC and accordingly FIR is not required to be quashed. It is further pleaded that in matters of economic fraud, it would not be appropriate for court to grant stay of arrest, particularly, where FIR discloses commission of cognizable offence, as such relief may thwart investigation and discovery of further information as to who all are involved in such activity.

Revenue also pleaded that by virtue of Section 131 of ST Act, it is clear that the provisions of any other act or under any other law would be applicable despite of the fact that there is a confiscation made or penalty imposed under provisions of ST Act. Further, from the provisions of Section 135, it is clear that for offences under ST Act, there is a presumption of culpable mental state on the part of accused unless the contrary is proved by the accused to the Court.

Further, a fact is said to be proved only when the court believes it to exist beyond reasonable doubt and merely when its existence is established by a preponderance of probability. However, for offences under IPC, there is no such presumption available and accordingly the offences under IPC are qualitatively different from those punishable under ST Act. For the pleading that there is no legal restriction placed on lodging FIR and the same could be lodged even when the proceedings could be undertaken for recovery of tax, Revenue relied on apex court judgment in State of West Bengal v Narayan K Patodia 2000 4 SCC 447.

Decision of High Court:

The Court has made a reference to Section 26 of General Clauses Act, wherein it was stated that if an act or omission constitutes an offence under two or more enactments, then the offender shall be liable to be prosecuted and punished under either or any of those enactments, but shall not be liable to be punished twice for the same offence.

By referring to the decision of apex court in the matter of State of Rajasthan v Hat Singh[4], wherein the principle of double jeopardy was discussed with reference to Article 20(2) of Constitution read with Section 300(1) of IPC read with Section 71, the court embarked upon the principle that if the offences under two acts are same, then the such offence can be prosecuted once in light of Article 20(2). However, if the offences under both the acts are distinct and qualitatively different, then the protection under double jeopardy does not apply and accordingly the offence can be tried under both the laws separately.

[4] (2003) 2 SCC 152

The Court then took up the decision of Apex court in the matter of State (NCT of Delhi) v Sanjay[5], where in the question before the Apex court was whether the provisions contained in Section 21, 22 and other sections of Mines and Minerals (Development and Regulation) Act, 1957 (MMDR Act) operate as bar against prosecution of a person who has been charged with allegation under Section 379 of IPC?

The Apex court after reading the act in a minute manner has held that if an offence which is mentioned in MMDR Act is executed by the accused, then such offence can be tried only under such act by the procedure laid under the said act. ***However, if an act or offence which constitutes an offence under IPC, then the provisions of MMDR Act shall not stand in a way to stop the applicability of IPC and such offence can be prosecuted under IPC without waiting or following the procedure under the MMDR Act.***

Further, the High Court by making reference to the judgment relied upon by Revenue in the matter of State of West Bengal v Narayan K Patodia stated that there is nothing in sales tax act which inhibited the powers of police to try an offence under IPC and hence the order of High Court, wherein the High Court has held that a case under sales tax act can only be tried by Bureau of Investigation and no police officer can take action, was set aside.

Accordingly, the High Court has held that there is no provision in ST Act which may suggest that provision of ST Act will override IPC. The High Court also held that there is no bar in ST Act on lodging FIR under IPC even though such offences are punishable under ST Act. Further, Section 131 impliedly saves provisions of IPC would apply notwithstanding to the fact that a penalty under ST Act is imposed makes the case stronger for revenue.

The High Court also brushed away the pleading of Petitioner that by virtue of Section 132(4) read with 132(5), the offences are non-cognizable and bailable, by stating that such restriction under 132(4) is only pertaining to offences under ST Act but not offences under IPC. Finally, the Court relying on the decision of Ajit Singh v. State of UP stated that where the prayer to quash FIR cannot be accepted there should not ordinarily be stay on arrest and considering the current matter pertaining to economic fraud, stay on arrest is rejected.

Madras High Court - Mahendra Kumar Singhi's case[6]:

Facts & Allegations:

Petitioners were facing prosecution before the revenue authorities for offences punishable under Section 132. The petitioners have several entities in nature of proprietorship concerns, partnership concerns or private limited companies in which petitioners are proprietor, partner and directors and the entities are engaged in supply of iron and steel. The allegation of the revenue was that petitioners were engaged in circular trading.

The modus operandi as alleged by revenue is that the petitioners were issuing invoices without actual movement of goods by issuing bogus E-Way bills. The same goods were traded among the said entities without actual movement of goods and thereby passing on the credit to other entities so that the other entity will use the credit to pay tax without having such credit in first place.

[5] (2014) 9 SCC 772

[6] 2019 (5) TMI 310 – Madras High Court

Contentions of Petitioner:

The petitioner has taken a stand that there cannot be punishment under Section 132 of ST Act unless the revenue is satisfied that there has been tax evasion or input tax credit wrongly availed or utilised which exceeds Rs 5 Crores, which will only be known when an enquiry and opportunity has been given to petitioners in order to put forward their cases.

The petitioners further relied on the judgement of Delhi High Court in the matter of MakeMyTrip (India) (P) Limited v Union of India (2016) 73 taxmann.com 31 (Delhi) and Bir.com Pvt Limited v Union of India MANU/DE/2740/2016, wherein it was held that arrest under Finance Act, 1994 cannot be done unless an assessment is made.

Contentions of Revenue:

The Revenue argued that it is not necessary in every case to follow the procedure of assessment and make a demand and recovery under Section 73 and 74 of the Act or to follow the procedure for levying the penalty under Section 126 and only thereafter launch a prosecution under Section 132 of Act.

The Revenue relied on the judgment of Rajasthan High Court in the matter of Bharath Raj Punj v Commissioner of Central Goods & Services Tax Department, Jaipur in WP 75 of 2019 dated 12.03.19, wherein it was held that there is no force in the contention that tax has to be first determined under Section 73 or 74 before initiating the prosecution under Section 132 of Act.

Decision of High Court:

The High Court stated that the Delhi High Court in the matter of MakeMyTrip (supra) was dealing with an arrest under Finance Act, 1994, where in the prosecution under said act was guided by Circular and which was not followed by the Revenue and accordingly the Delhi High Court directed such prosecution was bad in law.

Further, under the Finance Act, the Delhi High Court has held that penalty and prosecution provisions will have to preceded by adjudication for the purposes of determining the evasion of tax. Hence, there is a pre-requisite under Finance Act to determine the liability and then proceed for prosecution since the prosecution is dependent on such liability.

However, the High Court in the instant matter stated that there in nothing in Section 132 of ST Act which puts such condition as existed under service tax law. ***Section 132 of ST Act as per Court will apply with all force the moment an invoice or a bill issued without, movement of goods or credit has been availed wrongly without waiting for assessment.*** Accordingly, the High Court held that prosecution can be launched prior to assessment and rejected the application for anticipatory bail of petitioners.

Madras High Court -Jayachandran Alloy (P) Limited's case[7]:

Just five days later, another bench of same High Court ***has held that Section 132 applies only after completion of assessment and not prior to that. The bench stated this is clear from the usage of the word 'commit' under Section 132 which mandates the revenue to fix the act of committal of the offence first before punishment is imposed. The bench has further relied on the judgment of Delhi High Court in the matter of MakeMyTrip to come to this conclusion.***

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[7] 2019 (5) TMI 895 – Madras High Court

Rajasthan High Court – Bharath Raj Punj's case[8]

Facts & Allegations:

Petitioner 1 (Managing Director) of Petitioner 2, which is a company have filed writ petition seeking quashing and setting aside of summons issued by Commissioner of CT. The Revenue alleges that the petitioner has fraudulently availed credit of Rs 40 Crores by issuance of fictitious sale invoices and sister concerns of company and petitioner company had fraudulently availed credit of Rs 328 Crores. On conclusion of raid, the Revenue has arrested the Director and CFO.

Contentions of Petitioners:

Petitioner 1 states that he was issued summons and apprehends that he will be arrested in similar way as the director and CFO was arrested. Petitioner further relied on the judgment of Delhi High Court in the matter of MakeMyTrip (supra) and pleaded that Revenue cannot bypass a procedure before going ahead with arrest of person.

Petitioner further relied on Meghraj Moolchand Burad v Directorate General of GST in SLP (Criminal) 244/2019 dated 13.12.18, wherein the Apex Court has granted protection from arrest and permitted the accused to appear before GST (Intelligence). Accordingly, Petitioner pleaded that till date no determination of tax has been done either under Section 73 or 74, Revenue does not have right to arrest.

Contentions of Revenue:

Revenue contended that the judgment of Delhi High Court in the matter of MakeMyTrip (supra) does not apply since in that case revenue failed to establish that tax passed onto hotels was actually remitted by hotels or not. Further, they have pleaded that determination of tax under Section 73 or 74 is not necessary for invoking the power of arrest under Section 69 read with Section 132.

Decision of High Court:

The Court has held that the judgment of Delhi High Court in the matter of MakeMyTrip (supra) does not apply to the current facts, since in that case, the arrest was made without examining that the hotels were paying service tax or not. Since the responsibility to pay service tax was on hotels, the Delhi High Court said arrest of officials of MakeMyTrip is not in accordance with the law. Further, the Court also stated that the decision of Meghraj Moolchand Burad does not apply to the current facts, since said case deal with anticipatory bail. However, in the current case , it is issue of availment of credit based on fake input invoices. Accordingly, the Court has not allowed the writ petition and upheld the issuance of summons.

Bombay High Court – Prasad Purshottam Mantri's case[9]:

Facts & Allegations:

Writ Petition is filed seeking direction to the Revenue to follow the mandatory provisions of the Criminal Procedure Code before taking any further action.

[8] 2019 (3) TMI 1187 – Rajasthan High Court
[9] 2019 (6) TMI 107 – Bombay High Court

Decision of High Court:

The Court making reference to the provisions of Section 132 of CT Act and Section 91 of Finance Act and placing reliance on the judgement of Delhi High Court in the matter of MakeMyTrip (supra) has reached a prima facie conclusion that arrest cannot be made unless assessment under Section 73 or 74 is done.

The court stated alternatively, in view of provisions of Section 167(2) of Code of Criminal Procedure, the petitioner will be entitled for bail if charge sheet is not filed within 60 days from the date of arrest. Since 57 days have already exhausted and Revenue is not confident of filing charge sheet within three days, the petitioner is granted bail.

Telangana & Andhra Pradesh High Court – PV Ramana Reddy's case[10]:

Facts & Allegations:

A challenge was made against summons issued by Superintendent (Anti -Evasion) of Hyderabad GST and invocation of penal provisions of Section 69 of CT Act. The Revenue alleged that the petitioners are group of entities have been floated or incorporated for claiming of credit without invoices. The bogus or fake invoices were used to avail and utilise the fraudulent credit by the recipient of such invoices.

The documents clearly showed circular trading without there being any actual trading. Apart from circular trading the petitioners have also created fake invoices to enable their friendly business entities to take credit. Revenue alleged that by increasing the turnover, they have defrauded the banks by taking several facilities from such banks.

Accordingly, the revenue contended that petitioners have carried on offences under Section 132 and such offences when read with Section 132(5) are cognizable and non-bailable.

Contentions of Petitioner:

There are various petitions with different set of facts. The common prayer is that the summons issued under Section 70 of CT Act has to be quashed. The Petitioners main grievance is about the possibility of their arrest and detention to custody.

Contentions of Revenue:

The Revenue's objection is that the writ proceedings are not to be converted into proceedings for anticipatory bail.

Decision of High Court:

The Court stated that the prayer from Writ Petition is akin to a prayer for Anticipatory bail. Since no FIR gets registered before the power of arrest under Section 69(1), the petitioners cannot invoke Section 438 for anticipatory bail. Hence, the only way to seek protection against pre-prosecution arrest is to seek a writ remedy.

[10] 2019 (4) TMI 1320 – TG & AP High Court

The Court stated that the contention of the revenue that the writ proceedings cannot be converted into proceedings for anticipatory bail, is unacceptable because, if proceedings initiated by Commissioner under CT Act are criminal proceedings, then petitioner can very well invoke provisions of Section 438 to seek anticipatory bail. However, if the proceedings are not in criminal proceedings, then petitioner can invoke writ jurisdiction to pray for anticipatory bail. The Court stated that even if the inquiry under Section 70(1) is not by its nature a criminal proceeding, it is nevertheless a judicial proceeding by virtue of Section 70(2).

The Court further stated that a person who faces the threat of arrest in a criminal proceeding, may be entitled to involve Section 438 subject to two conditions: (1) That Section 438 applies to the state in which the prosecution takes place and (2) that the application of Section 438 is not ousted by any special enactment under which the person is prosecuted.

Where the applicability of Section 438 is specifically excluded, the High Court shall be extremely cautious while exercising the same power indirectly resorting to Article 226, the writ jurisdiction. Though the Constitution Bench of apex court stated that there is no bar for the High Court to grant bail under Article 226 despite of the fact that Section 438 is not applicable to such state, the High Court has to sparingly use such power, since it creates a second window for the relief which is consciously denied by making Section 438 not applicable in the State. The Court referred to the judgments of Km Hema Mishra v State of Uttar Pradesh 2014 (4) SCC 453 and Kartar Singh v State of Punjab 1994 (3) SCC 569.

Hence, the Court stated that the argument of Revenue that writ petition cannot be converted into application for anticipatory bail is not in accordance with the law, however due care has to be used for granting such relief under Article 226. The Court concluded that since the petitioners in the instant case does not deserve the sparing treatment, the bail is not granted under Article 226.

One more plea taken by the Petitioner is that as per Section 41 and 41A of CrPC prohibits arrest of person who complies and continues with a notice for appearance issued under Section 41A(1) of the CrPC. Since the petitioner are ready to comply with the notices, the arrest is not required. The Revenue contended that the provisions of Section 41 or 41A will attract only after arrest of persons as per Section 69(3).

The Court stated that on reading of Section 69(1) along with Section 132(5), it is evident that Commissioner can arrest a person if he has reasons to believe that such person has committed an offence under Section 132(1)(a) to (d). By virtue of Section 132(4) except offences mentioned from (a) to (d) of Section 132(1), all other offences are non-cognizable and bailable. That is to say all other offences under (f) to (l) under Section 132(1), the Commissioner can arrest only with the permission of Magistrate.

However, the provisions of Section 69(3), which are subject to the CrPC states that a person who has been arrested under Section 132(4), he shall be admitted to bail or in default of bail, forwarded to the custody of Magistrate. The Court stated that on close reading of Section 69 and Section 132, there exists incongruence, since Section 132(4) states that certain offences are non-cognizable and on other hand vide Section 69(3)(a) states that a person arrested for an offence under Section 132(4) has to be forwarded to the Magistrate. When the offence itself is non-cognizable, where would the Commissioner yield power to arrest so that using the provisions of Section 69(3) makes reference to the Magistrate.

Therefore, the Court stated that though in light of the fact that Section 69(1) authorises arrest only of persons who are believed to have committed cognizable offences and non-bailable offences but Section 69(3) deals with grant of bail and procedure for grant of bail even to persons who are arrested in connection with non-cognizable and bailable offences, the contention of the Revenue that provisions of Section 41 or 41A will apply only after arrest as per Section 69(3) does not appear to be correct.

Conclusion:

From reading of the above judgements and consequent confirmation of decision of Telangana & Andhra Pradesh in the matter of PV Ramana Reddy & Others (supra) by the Supreme Court, the issue appears to be settled for now, that prosecution is not dependent upon the assessment unlike in the era of service tax laws. Once the Commissioner has reasons to believe that accused has committed an offence under Section 132(1) (a) to (d), he may authorise arrest without waiting for completion of assessment.

Effects of Circular Trading vis-à-vis Prevention of Money Laundering Act, 2002:

The judgment of Allahabad High Court in Govind Enterprises (supra) also clearly states that there is no bar under the GST laws which would prevent to initiate prosecution under IPC. Hence, the view that by virtue of Section 132(4), since all the offences except as provided under Section 132(5), are non-cognizable and bailable and hence no FIR can be lodged under IPC shall not be appropriate, because, Section 132(4) makes offences non-cognizable for the purposes of GST laws but not for IPC. Hence, a separate prosecution can be initiated by competent officer under IPC as far as other offences under GST laws are concerned.

The above conclusion assumes importance because of its impact under the Prevention of Money - Laundering Act, 2002 (PMLA). Section 3 of PMLA provides that *whosever directly or indirectly attempts to indulge or knowing assists or knowingly is a party or is actually involved in any process or activity connected with the **proceeds of crime** including its concealment, possession, acquisition or use and projecting or claiming it as untainted property shall be guilty of money-laundering.*

The expression 'proceeds of crime' has been defined under Section 2(u) of PMLA to *mean any property derived or obtained, directly or indirectly, by any person as a result of criminal activity relating to a **scheduled offence** or the value of any property or where such property is taken or held outside the country, then the property equivalent in value held within the country or abroad.*

The expression 'scheduled offence' has been defined under Section 2(y) of PMLA to *mean offences specified under Part A of the Schedule or the offences specified under Part B of the Schedule if total value involved in such offences is one crore or more or the offences specified under Part C of Schedule.*

On a combined reading of Section 3, Section 2(u) and Section 2(y), what transpires is that there cannot be any action under PMLA unless the proceeds of crime pertain to scheduled offence. In other words, if the offence is not a scheduled offence, then such offence shall be outside the ambit of PMLA. Hence, if the activity of circular trading is a scheduled offence, then such activity would attract action under PMLA. Let us examine, if such circular trading is covered under the schedules.

Paragraph 12 of Part A of Schedule deals evasion of duty or prohibitions under the Customs Act, 1962 and Part B notifies false declaration, false documents etc in terms of Section 132 of Customs Act, 1962 as scheduled offence. Whereas, the evasion of duty or issuance of false documents under GST laws is

not covered as scheduled offences under the current PMLA. Hence, there appears that circular trading which involves issuing of fake/bogus invoices does not come under the ambit of PMLA.

However, offences under Section 120B, Section 467 and Section 471 are scheduled offences vide Paragraph 1 of Part A to PMLA. Hence, if the competent authority under IPC books the taxpayer under the said sections namely Section 120B (criminal conspiracy), Section 467 (forgery of valuable security, will, etc.,) and Section 471 (using as genuine a forged document or electronic record), then the said offence would fall under the ambit of PMLA.

In the case of circular trading, there involves a criminal conspiracy among group of players to defraud revenue by issuing fake/bogus invoices, thereby attracting Section 120B, and by issuing bogus e-way bills, the accused would also attract provisions of Section 467 and 471, resulting in various scheduled offences, giving the competent authority power to invoke provisions of PMLA.

Hence, in light of the Allhabad High Court judgment in the matter of Govind Enterprises (supra), wherein it was held that there is no bar under GST laws to invoke prosecution under IPC, an officer can invoke prosecution under IPC and simultaneously the provisions of PMLA may also get triggered. It is important to note that Section 131 of CT Act states that penalty imposed under the provisions of CT Act shall not prevent the infliction of any other punishment to which person affected thereby is liable under provisions of this act or ***under any other law*** for time being in force. Hence, in the instances of circular trading, there is every possibility that the provisions of PMLA could be invoked because the GST laws do not state otherwise.