



Tax Insights

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Mere holding of an office by an individual in a corporate entity is not sufficient to be treated as a principal officer; connection must be established with the corporate entity's management or administration – Delhi High Court

In brief

The Delhi High Court¹ sets aside the order under section 2(35) of the Income-tax Act, 1961 (the Act), treating the petitioner, Managing Director (MD) of the company, as the 'principal officer' for the purpose of the initiation of the proceedings under section 276B of the Act on the company in respect of default to deposit tax deducted at source (TDS).

The court observed that merely holding an office in a corporate entity was not sufficient to treat a person as a principal officer, unless it was established that the person was connected with the corporate entity's management or administration.

Accordingly, the court directed the Revenue to examine the issue afresh after considering the petitioner's response and conducting inquiry whether the petitioner could be said to be a person connected with the management or administration of the company.

In detail

Facts

- The petitioner was appointed as the Chief Executive Officer (CEO) of an Indian company on 1 January 2016. Thereafter, he was appointed as its MD on 2 May 2017. He resigned from the position of MD on 1 March 2018.
- The petitioner received a notice on 11 December 2018 treating him to be the principal officer and asking him to show cause in respect of TDS default by the company for the financial years 2016-17 and 2017-18.
- The petitioner furnished a response on 19 December 2018, submitting that although he held the offices of CEO and MD in the respective period, he was not connected with or in charge of the accounting or financing activities pertaining to the company.
- The Revenue issued orders under section 2(35) of the Act on 20 June 2019 and on 24 July 2019, concluding the petitioner to be the principal officer of the company.

¹ Writ Petition No W.P.(C) 8577/2019

- According to the Revenue the petitioner, being in the capacity of MD, was certainly associated with the company's management and administration. It further alleged the petitioner to be the person responsible for TDS compliances.

High Court's decision

- The court observed that as per section 2(35) of the Act, the principal officer with reference to a company means:
 - a. the secretary, treasurer, manager or agent of the company; or
 - b. any person connected with the management or administration of the company upon whom the Tax Officer has served a notice of their intention of treating him as the principal officer thereof.
- The court opined that merely holding an office in a corporate entity is not sufficient to place a person in part (b). The intention of the Revenue to treat an individual as the principal officer must be based on satisfying that the person was connected with the company's management or administration.
- The court noted the judicial precedents² relied upon by the petitioner, which held that the connection of any person with the company's management or administration has to be established or supported with substantial material. The details of the information have to be explicitly expressed in the notice of intention treating any person as a principal officer.
- Additionally, the court noted that the Revenue had referred to additional material in its counter affidavit, which was not mentioned in the notices issued initially or the impugned orders.
- Accordingly, the court directed the Revenue to examine the issue afresh after considering the petitioner's response and making due inquiry regarding whether the petitioner could be said to be a person connected with the company's management or administration.
- The matter stood revived from the stage of issuance of a notice under section 2(35) of the Act and to be concluded after affording due opportunity of hearing to the petitioner.

The takeaways

This is an important judgement from the Delhi High Court affirming the principles that the notice of intent to treat a person as a principal officer must be supported with evidence of their involvement in the company's management and administration. Merely holding an office in a corporate entity is not sufficient to treat a person as a principal officer under clause (b) of section 2(35) of the Act.

The decision may aid senior officials of corporates facing the risk of initiation of arbitrary prosecution *inter-alia* for TDS defaults, despite being not involved in the accounting, tax or finance related activities of the company.

² K.P.G. Nair v. Jindal Menthol India Limited [2001] 10 SCC 218 (SC); Harish Bhat v. Assist. CIT [2019] SCC OnLine Kar 3998 (Karnataka)

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