Principal Officer under the Income-tax Act, 1961

This article discusses different aspects relating to a principal officer under the Income-tax Act, 1961 (the Act) in the light of some important related case laws. The term "principal officer" is defined in Section 2(35) of the Act as the secretary, treasurer, manager or agent of the company and any person connected with the management or administration of the local authority, company, association or body upon whom the Assessing Officer has served a notice of his intention of treating him as the principal officer thereof. Further, this article seeks to analyse some relevant Indian case laws, highlighting key terms, and noting some practical issues.

Principal Officer

As per Wikipedia, the free encyclopedia describes the Principal Officer as the highest uniformed rank, above senior officer and below the grades of governor. A Principal Officer traditionally headed each wing of a prison.

As per sub-Section (35) of Section 2 of the Act, the principal officer means:

> *"Principal Officer" used with reference to a local authority or a company or any other public body or any association of persons or any body of individuals, means-*
>
> *(a) the secretary, treasurer, manager or agent of the authority, company, association or body, or*
>
> *(b) any person connected with the management or administration of the local authority, company, association or body upon whom the Assessing Officer[1]* has served a notice of his intention of treating him as the principal officer thereof.*
>
> ** Prior to 01-04-1988, it was Income-tax Officer who would serve a notice of his intension of treating him as the principal officer thereof.*

Whereas the Income-tax Act, 1922 (Act of 1922) provides the meaning of principal officer as follows:

> *"Section 2(12) "Principal Officer" used with reference to a local authority or a company or any other public body or association, means*
> *(a) the secretary, treasurer, manager or agent of the authority, company, body or association, or*
> *(b) any person connected with the authority, company, body or association upon whom the Income-tax Officer has served a notice of his intention of treating him as the Principal Officer thereof."*

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[1] *Substituted for "Income- tax" by the Direct Tax Laws (Amendment) Act, 1987, w. e. f. 1- 4- 1988.*

Section 2(35)(b) is wide enough to take in any person connected with the management or administration of the company.

Under the Act of 1922, connection with the company as such would have been sufficient whereas under the present Act, 1961, in order to make a person the "Principal Officer," the connection must be for the management or administration of the company.

The key differences in definition of principal officer under the Act, 1922 and 1961 are as follows:

Sl. No.	Income-tax Act, 1922	Income-tax Act, 1961
1	*any person connected with the authority,.....*	*any person connected with the management or administration of the local authority,.....*
2	*Prior to 01-04-1988*	*After 01-04-1988 & onwards*
	Income tax officer has served a notice of his intention of treating him as the principal officer thereof.	*Assessing Officer has served a notice of his intention of treating him as the principal officer thereof.*

Now, let us clarify some critical issues relating to the aforesaid section along with some case laws in this regard.

Conditions must be cumulatively satisfied

In order that a person can be said to be a 'principal officer' as defined under Section 2(35)(b), the following two ingredients must be satisfied :

(*i*) he must be a person connected with the management or administration of the company; and

(*ii*) the assessing officer must have served upon him a notice of his intention of treating him as the principal officer of the company.

The satisfaction of any one of the two conditions or ingredients will not attract this clause-*ITO vs. Official Liquidator*[2].

Sub-clause (b) of Clause (35) of Section 2 is wide enough to take in any person connected with the management or administration of the company.

The words "management" and "administration" are not defined anywhere in the Income-tax Act or the Companies Act.

The ordinary dictionary meanings of those words may be noticed.

1. "Manage" means "conduct (undertaking, *etc.*); control (household, institution, state); take charge of (cattle, *etc.*)."
2. "Administration" means "the action of administering or serving in any office; attendance; performance of duty."

The words "management" and "administration" are of broad import.

It is pertinent to notice that the expression used is "any person connected with the management or administration of the company" but not "a person in management or administration of the company."

There is a lot of difference between the two expressions. What the law makers intended is some kind of connection or nexus of the person to be called the principal officer, with the management or administration of the company.

They did not intend the person to be in actual management or administration of the company. The person who is in actual management or administration of the company may have a direct and proximate hand in the affairs of the company during the period of management. Such a person would fall within the provisions of sub-clause (a) itself which takes in a manager or agent of the company. For the purpose of bringing a person within the meaning of Section 2(35), he need not actually manage or administer the affairs of the company but suffice it if he has some connection with the management or administration of the company.

Prior notice of hearing is not necessary

Before treating a person concerned as a principal officer under Section 2(35)(b) by the ITO, it is not necessary to determine that question upon hearing the submission or representation of the person concerned.-*Hungerford Investment Trust Ltd. vs. ITO*[3].

In the case of *M. M. Ipoh vs. CJT*[4], it was observed that (p. 120);

> *"There is, in our judgment, nothing in the Act which supports the contention of counsel for the assessee that before proceedings in assessment can commence against an association of persons a notice must be issued and an order passed after*

[2] *[1977]106 ITR 119 (AP)*
[3] *[1983]142 ITR 601 (Cal)*
[4] *[1968]67 ITR 106 (SC)*

giving opportunity to the person proposed to be treated as the principal officer, to show cause why he should not be so treated. It is open to the Income-tax Officer to serve a notice on a person who is intended to be treated as the principal officer. The person so served may object that he is not the principal officer or that the association is not properly formed. The Income-tax Officer will then consider whether the person served is the principal officer and whether he has some connection or concern with the income sought to be assessed."

So, it is not necessary to give a hearing before treating a person as the principal officer of a company. The question whether a person is a principal officer of the company should be determined in the assessment proceeding.

Liquidator is a 'manager'

The word 'manager' in Section 2(12) of the 1922 Act includes liquidator of a company-*CIT vs. Official Liquidator of the Agra Spg. &Wvg. Mills Co. Ltd*[5].

Official Liquidator is the principal officer

In *Hari Prasad Jayantilal and Co. vs. V. S. Gupta, Income-tax Officer, Ahmedabad*[6], the Supreme Court, in dealing with the case of a company in voluntary liquidation, explained the position of the liquidator thus:

"A company which has resolved to be voluntarily wound-up may be dissolved in the manner provided by Section 497(5); till then the company has corporate existence and corporate powers. The property of the company does not vest in the liquidator; it continues to remain vested in the company. On the appointment of a liquidator, all the powers of the board of directors and of the managing or whole-time directors, managing agents, secretaries and treasurers cease, and the liquidator may exercise the powers mentioned in Section 512, including the power to do such things

For the purpose of bringing a person within the meaning of Section 2(35), he need not actually manage or administer the affairs of the company but suffice it if he has some connection with the management or administration of the company.

It is not necessary to give a hearing before treating a person as the Principal Officer of a company. The question whether a person is a principal officer of the company should be determined in the assessment proceeding.

as may be necessary for winding-up the affairs of the company and distributing its assets. The liquidator appointed in a members' winding up is merely an agent of the company to administer the property of the company for purpose prescribed by the statute. In distributing the assets including accumulated profits, the liquidator acts merely as an agent or administrator for and on behalf of the company."

The fact that there are no assets of the company in his hands and that ex-directors were liable for the income-tax arrears of the company, will not alter this legal position-*ITO vs. Official Liquidator*[7].

Even after a winding up order was passed, a company continued to be a "person" within the meaning of Section 4 of the Income-tax Act, 1961, and the liquidator would be the principal officer of such company within the meaning of Section 2(35) (a) of the Income-tax Act.-*Mysore Spun Silk Mills Ltd. vs. CIT*[8].

In *Knowles vs. Scott Romer J. [1891]* has stated that, in his view, a voluntary liquidator is more rightly described as the agent of the company.

In Palmer's Company Law, twenty-first edition, at page 754, the position of a liquidator in winding up by court has been stated as that of an agent employed for the purpose of winding-up the company. The said statement relies on *Knowles vs. Scott.*

So, official liquidator can be rightly termed as the agent of the company. Therefore, the liquidator, on an order for winding-up being made, becomes the "Principle Officer" of the company within the meaning of Section 2(35)(a) of the Income-tax Act, 1961.

Prosecution in the absence of Principal Officer

A company is not a natural person but legal or juristic person. But that would not mean that it is not liable to prosecution under the Act.

[5] *[1934] 2 ITR 79 (All)*
[6] *[1966] 59 ITR 794 (SC)*
[7] *[1977] 106 ITR 119 (AP)*
[8] *[1971] 79 ITR 399 (KN)*

Even after a winding up order was passed, a company continued to be a "person" within the meaning of Section 4 of the Income-tax Act, 1961, and the liquidator would be the Principal Officer of such company within the meaning of Section 2(35)(a)

In *Greatway (P) Ltd. & Ors. vs. Assistant CIT*[9], the Punjab & Haryana High Court has held that in the absence of appointment of a Principal Officer by issuing a notice by the department, the prosecution, if any, could only be launched against the company.

In *Standard Chartered Bank vs. Directorate of Enforcement*[10], Crl. A. No. 109/2011, the Supreme Court held that juristic person is also subject to criminal liability under the relevant law. Only thing is that in case of substantive sentence, the order is not enforceable and juristic person cannot be ordered to suffer imprisonment.

As the company cannot be sentenced to imprisonment, the court cannot impose that punishment, but when imprisonment and fine is the prescribed punishment, the court can impose the punishment of fine which could be enforced against the company.

Managing director cannot be equated with 'manager'

In *ITO vs. Joseph*[11] (p. 7 & 8) it was held that:

> *"7. The managing director is not one of the persons falling under the category enumerated under Section 2(35)(a) or 2(35)(b). The persons taken in under clause (a) are "the secretary, treasurer, manager or agent." Under the Indian Companies Act, manager and managing director are two different entities. So the managing director cannot be equated with the manager. The learned appellate judge, it appears, has brought the respondent under clause (b) as "a person connected with the management or administration of the company. "The "managing director," under the Indian Companies Act, means; "A director who by virtue of an agreement with the company..... is entrusted with powers of management..."*
>
> *8. Even if the respondent is construed as one entrusted with or entitled to the management of the company, he should have been served with a notice by the Income-tax Officer of his intention to treat him as the Principal Officer in order that he may be brought under clause (b) of Section 2(35) of the Act. Such a notice was evidently not given in the instant case. It would, therefore, be wrong to say that the respondent, C. L. Joseph, was the principal officer of the company at the relevant time."*

The Hon'ble Supreme Court in *Municipal Corporation of Delhi vs. Ram Kishan Rohtagi*[12], held that (at page 70):

> *"So far as the manager is concerned, we are satisfied that from the very nature of his duties it can be safely inferred that he would undoubtedly be vicariously liable for the offence; vicarious liability being an incident of an offence under the Act. So far as the directors are concerned, there is not even a whisper nor a shred of evidence nor anything to show, apart from the presumption drawn by the complainant, that there is any act committed by the directors from which a reasonable inference can be drawn that they could also be vicariously liable. In these circumstances, therefore, we find ourselves in complete agreement with the argument of the High Court that no case against the directors (accused Nos. 4 to 7) has been made out ex facie on the allegations made in the complaint and the proceedings against them were rightly quashed."*

Hence, a managing director is not one of the persons falling under the category of principal officer enumerated under sub-clause (a) or (b) of Section 2(35). The managing director cannot be equated with the manager. Even if he is construed as one entrusted with or entitled to the management of the company, he should have been served with a notice by the ITO of his intention to treat him as the principal officer in order that he may be brought under sub-clause (b) of Section 2(35).

A company is not a natural person but legal or juristic person. But that would not mean that it is not liable to prosecution under the Act.

[9] *[1993] 199 ITR 391 (P&H)*
[10] *[2005] 8 SCC 530 (SC)*
[11] *[1972] 83 ITR 362 (Ker)*
[12] *1983 AIR 67 (SC)*

Partners of firm

In *Shital N. Shah And Others vs. Income-Tax Officer*[13], the petitioners, stated to be partners, do not fall within the category of the secretary, treasurer, manager, or agent of the authority, company, or body, and further, they had also not been served with any notice by the Income-tax Officer divulging his intention of treating any one of them as the Principal Officer connected with the management or administration of the firm.

Section 2(35) would then step in to find out as to who the principal officer would be. This section has been extracted earlier and it appears to be clear that the partners of the firm do not fall within that fold unless the Income-tax officer had served a notice on any of them of his intention of treating them as the principal officer of the firm, connected with the management or administration thereof.

In *M. A. Unneerikutty and Ors. vs. Deputy Commissioner of Income Tax*[14], it was held that by virtue of Section 2(35) of the Act, partners do not come within the definition of "Principal Officer" unless the Income-tax Officer had served notice of his intention to treat them or any one of them as the principal officer of the firm connected with the management or administration.

No bar for treating more than one person as the Principal Officer

The Supreme Court in the case of *Madumilan Syntex Ltd. & Ors vs. Union of India [2007]*[15], held that as under:

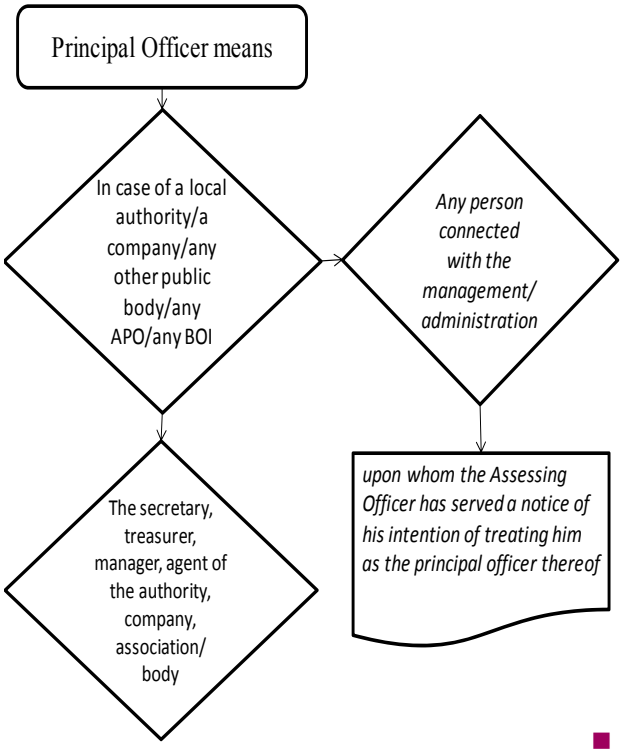
> *"27. So far as the directors are concerned, it is alleged in the show-cause notice as well as in the compliant that they were "Principal Officers" of the company. In the show-cause notice, it was assessed that the appellants were considered as principal officers under Section 2(35) of the Act. In the complaint also, it was stated that the other accused were associated with the business of the company and were treated as principal officers under Section 2(35) of the Act and hence they could be prosecuted. Dealing with an application for discharge, the trail court observed that accused no. 1 was the company whereas the other accused were the directors. Whether they could be said to be Principal Officers or not would require evidence and it could be considered at the stage of trail and the application was rejected. In revision, the first additional session's judge took a similar view."*

The Hon'ble High Court of Karnataka in the case of *M/s Kingfisher Airlines Ltd. vs. The Income tax Department*[16], held that the subsequent event treating one Shri. T. R. Venkatadri as the Principal Officer of the petitioner company will not result in quashing of the proceedings against the main accused-Shri Vijay Mallya–Chairman and Managing Director of M/s Kingfisher Airlines Ltd. It is open for the respondent authorities to proceed against the company, its directors or any other principal officer/s responsible for the default.

A reading of Section 2(35) of the Act specifies that there is no bar for treating more than one person as the Principal Officer for initiation of criminal proceedings.

Conclusion

It is a part of the machinery provision and must be construed and viewed in that light. The flow chart below summarises the position of principal officer as per the Income tax law.



[13] [1991] 188 ITR 376
[14] [1996] 218 ITR 606
[15] Appeal (crl.) 1377 of 1999
[16] TS - 677-ITAT-2013