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COMPOUNDING OF OFFENCES – A CURSE IN DISGUISE?

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“Pull the chain to stop the train” is a common sight in every cabin of a railway compartment. This emergency chain with a bright red wooden handle enables one to stop the moving train in case of any emergency. While allowing so, it also provides for a statutory warning that its misuse is an offence and shall carry a punishment / penalty of 3 months imprisonment or Rs.1000/-. Even though it was our childhood temptation to pull the chain for once, we never had that money to afford that offence. When we had the money, we were much wiser not to do it.

This could be an illustration of the “Compounding theory”. As per the Black’s Law Dictionary, “Compound” means “to settle a matter by a money payment, in lieu of other liability”. In fine, compounding of an offence is a settlement mechanism, by which, one is given an option to pay money in lieu of his prosecution, thereby avoiding a prolonged litigation.

Under the Central Excise Act, Section 9 of the Central Excise Act, 1944 which deals with Offences and penalties, provides for “imprisonment” for various offences specified therein. If prosecution is launched for all the cases enumerated under Section 9, India’s prisons would be running “house-full”, as it makes every other mistake under the sun, a prosecutable offence! Thanks to the various Circulars issued by the Government, wherein, detailed guidelines have been prescribed for institution of prosecution, such as, presence of *mens rea*, evidence of direct involvement, etc., as on date, the number of cases where prosecution is launched, is quite minimal.

Even though under Central Excise, the concept of “Compounding”, owes its origin to Rule 210 (A) of the then Central Excise Rules, 1944 (See DDT ----), categorical provisions were incorporated under Section 9A(2) of the Act, which was enacted in 2004. Similar provisions have also been made in the Customs Act. But, the much awaited Compounding of Offences Rules, giving effect to the above provisions, have been issued as a gift for the “New Year 2006!” But is it really a gift?

Central Excise (Compounding of offences) Rules, 2005 and Customs (Compounding of Offences) Rules, 2005 have been notified and instructions in the form of a Circular has also been issued. For the sake of brevity, we have reviewed the provisions of the Central Excise (Compounding of offence) Rules, 2005 only for the time being, as the basic feature of the “compounding” under Central Excise and Customs are mostly akin to each other.

At the outset, it may be observed that, even though the concept of “compounding” is only in lieu of any other liability, the present “Compounding of offences” under both the Excise and Customs Act are meant only in lieu of “prosecution”, which leads to deprivation of personal liberty viz., imprisonment. The other modes of punishment prescribed in the statute, viz., imposition of various penalties and demand of interest have got nothing to do with “compounding”. In this connection, it may be observed that during the year 1998, “Settlement Commission” has been introduced for Customs and Central Excise, which is vested with the powers of granting immunity from prosecution, waiver of interest and penalties. The only disadvantage of Settlement Commission is that it cannot grant immunity from prosecution, if such prosecution has already been launched before the filing of the application, as per proviso to Section 32 K (1) of the Act.

As per Rule 3 (1) of the Central Excise (Compounding of Offences) Rules, 2005, an applicant may file an application either before or after institution of prosecution. But, expecting a sane person to prefer the “compounding route” rather than the “Settlement Commission route”, before institution of prosecution, appears to be totally meaningless, due to the following disadvantages in the “compounding route”.

- ⌚ One has to pay the hefty compounding fees.

- ⌚ Immunity is granted only against prosecution. ⌚ He will still be liable for penalty and interest.

Accordingly, any prudent person, who foresees a prosecution under the Central Excise Act, would only opt for Settlement Commission. As such, effectively, the present “compounding” provisions would be used only by those persons, who have missed the Settlement Commission bus, where the prosecution has already been launched.

But, while opting for Settlement Commission one has to make an honest and true disclosure of his duty liability. In other words, he has to accept a duty liability of more than Rs. Two lakhs, which is a condition precedent to enter the Settlement Commission route. But, no such pre-condition has been envisaged for a person who is opting for the “compounding route”. As such, it appears that the duty liability need not be accepted while opting for the compounding route and the duty demand can still be disputed. As observed earlier, “compounding” is only in lieu of prosecution and is aimed to avoid protracted litigation. When the threat of prosecution looms over one’s head, one would prefer to pay the compounding fees and protect his personal liberty. After buying peace against such threat of prosecution by paying the compounding fee, it appears that, one is still at liberty to contest his duty demand, on merits. This unique feature of compounding route may win over the Settlement Commission route.

The amount of compounding fees prescribed in the Rules is so astronomical that we are afraid it would only discourage the assesseees from opting for the same, thus defeating the intention of the scheme. Let us delve a bit deep.

Offences under Central Excise may be broadly categorized as below:

a) First degree offences, like :

- ⌚ Where the assessee has collected duty of excise from its customers, but did not deposit it with the Government.
- ⌚ Where the assessee has raised bogus invoices and allowed its customers to avail Cenvat Credit of duties, which have not at all been paid.

b) Second degree offences, like:

- ⌚ Removal of goods without payment of duty and depriving the exchequer of its revenue. It is only a deprivation of exchequer of its due revenue. Such deprivation has not been pocketed by the assessee, justifying its treatment as a second degree offence.
- ⌚ Intentionally availing Cenvat Credit, which is not at all eligible.

c) Third degree offences, like:

- ⌚ Non-payment of duty due to interpretation, etc.
- ⌚ Violation of the procedural provisions, which may not result in short / non payment of duty.
- ⌚ Violations, which are completely revenue neutral, due to availability of Cenvat Credit, etc.
- ⌚ Non payment of duty due to pure ignorance.

Fixing the compounding fees at 20 % of the market value of goods in many cases, viewed from the backdrop of the fact that the rate of duty on many goods is itself only 16 % makes the compounding fees harsher than the draconian Section 11 AC. Similar is the case of fixing the compounding fees at

100 % of the credit, for offences relating to Cenvat Credit. In cases of Cenvat Credit, there is always a time lag between the availment of Cenvat Credit and its utilization. The offence in such cases can be said to have been committed, only when such irregularly availed credit is utilized, thereby depriving the exchequer of its dues. But, these niceties are not taken into account while fixing the compounding fees for the offences relating to Cenvat Credit.

For the reasons best known to the lawmakers, the Circular has categorized the offences under Section 9 of the Act, as "substantive offences" and "technical offences". In the Rules, out of the seven offences, which is the subject matter, only one has been classified as a "technical offence", i.e. offences under Section 9 (1) (d) (Attempt and abetment). It has also been clarified in the Circular that the compounding of "substantive offences" shall be allowed **only once**. Having classified almost all offences as "substantive offences", it shall only make the compounding route as a once-in-a-life-time affair. There is also another grave contradiction. In the table prescribing the compounding fees, against SI. Nos. (1) and (6), the fees is prescribed as Rs. 50000/- for the first time, which gets doubled for every subsequent offence of the same kind. SI No (1) deals with the offences under Section 9(1)(a) and SI No 6 with the offences under Section 9(1)(c) of the Act. On one hand, having categorized the offences under Section 9(1)(a) and (c) as "substantive offences" which are entitled for only one time compounding and on the other hand prescribing a fees for its subsequent offences, is nothing but a pathetic testimony of non application of mind while drafting the hottest Rules of the Nation. Further it may be observed that there is no such restriction contained either in the Act or in the Rules. It remains to be seen as to whether this instruction of the Board, which has not at all been supported by any legal provisions, is legally valid or not. Similarly, various other prohibitions contained in the CBEC Circular, do not have the support of statutory provisions and are prone to litigation. Further, the circular also prohibits compounding by such persons, who have already availed such compounding, in respect of goods having a value of more than Rs. One Crore (involving a duty of Rs. 16 lakhs!). The legality of such condition is also highly doubtful, for want of statutory support.

Further, as per Rule 4 (6) of the Rules, the compounding fees once paid shall not be refunded, unless the Court rejects the immunity granted to the applicant. It is not clear, as to who will take the matter of grant of immunity to the Court. If "compounding" is ordered by the Chief Commissioner, the applicant has to pay the fixed fees. As such, the applicant cannot complain about the quantum of fine, as it is at the discretion of the Chief Commissioner. If the applicant has not complied with any conditions imposed by the Chief Commissioner or has concealed certain vital information, the immunity from prosecution granted by the Chief Commissioner would be withdrawn, as per Rule 7 *ibid*. Once such immunity is withdrawn, we feel that there is no reason to retain the compounding fees already collected. That too, as already stated, when such compounding fees has been fixed at an astronomical rates (upto 20% of the value), denying the immunity on one hand and also retaining the compounding fees on the other hand, is nothing but a shameful proposition.

Last but not the least, though this compounding scheme is intended to benefit the trade community and minimize litigations, in fact, it only brings glamour to the office of the Chief Commissioners. Hitherto, the offices of the Chief Commissioners were only transit points between the Commissioners and the Board. The long grievance of the Chief Commissioners that they do not have either executive or quasi-judicial powers (which even an Assistant Commissioner is vested with) has now been duly compensated by giving enormous powers and discretion to them, beyond any comprehension, in the name of "compounding!" The enormous discretion vested with the Chief Commissioners to determine the "compounding fees" between Rs 10 lakhs and 20% of the market value of the goods, makes the post most powerful than United States Secretary of State! That too, with no appellate remedy prescribed, its going to be the Chief Commissioners who shall have the last (s)word!

Before parting...

In general, compounding of offences is available only in respect of those offences committed against individuals and not against those offences against the public policy / society. The offences listed under



Section 320 of the Criminal Procedure Code would fortify the above. Though the offences under the Central Excise Act, 1944 / Customs Act, 1962 are against the exchequer, the liberal attitude of the Government to provide for "compounding" of such offences against public is definitely a welcome measure. But, the manner in which the Rules have been framed and clarified raises our eyebrows!

The prescription of exorbitant fees and the refusal to refund the compounding fees paid, make us to believe that the Government is considering the "compounding scheme", only as a source of income! Further, the Circular also says that the performance of each zone in terms of realization of compounding amount would be periodically reported to the Government. All this, only compounds our fear that the "compounding" is viewed by the Government, not as a measure of avoiding litigation but as an additional source of revenue. We are afraid that the provisions of these Rules could be mis-used as a threat of prosecution, so as to realize "huge compounding fees". Prosecution, which is currently being initiated only in rarest of the truly deserving cases, may be a thing of the past and shall give rise to proliferation of prosecution, just to generate more money, thus making the "compounding of offences" **a curse in disguise!**

