

SECTION 74 AND THE CULTURE OF MECHANICAL ADJUDICATION IN GST - A CALL FOR JUDICIAL INTERVENTION

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Section 74 of the GST Acts was enacted with the clear legislative intention of dealing with cases where tax has not been paid, short paid, erroneously refunded, or where input tax credit has been wrongly availed or utilized by reason of fraud, wilful misstatement, or suppression of facts to evade tax. It is a penal provision which prescribes higher penalties and an extended period of limitation of five years as against the ordinary period of three years under Section 73. In contrast, Section 73 was designed to cover ordinary cases of error, omission, or inadvertence, where tax has not been paid or short paid for reasons other than fraud or wilful suppression. The distinction between the two provisions is not merely procedural but substantive, one addresses fraudulent conduct, while the other addresses bona fide errors.

However, in practice, tax authorities across the country have been routinely invoking Section 74 even in cases where there is not the slightest element of fraud or wilful misstatement. The show cause notices issued under Section 74 are often mechanical, using template phrases such as “it appears that the taxpayer has wilfully suppressed turnover with intent to evade tax,” without any supporting particulars or evidence. There is rarely any reference to material discovered, circumstances indicating concealment, or any proof of intent to evade tax. Many such proceedings arise from routine return mismatches between GSTR-1 and GSTR-3B, delayed reversal of input tax credit, differences in books of account, or late payment of tax, which are at best procedural or clerical errors but not fraudulent acts. The invocation of Section 74 in such circumstances amounts to a misuse of a penal provision intended for exceptional cases.

The principal reason why officers prefer to proceed under Section 74 instead of Section 73 lies in the extended limitation period of five years available under the

former as opposed to three years under the latter. This longer period provides administrative comfort, particularly in audit or investigation-based cases where reconciliation takes time. Moreover, Section 74 carries higher penalties equal to the amount of tax determined and permits immediate recovery if the taxpayer admits liability and pays a reduced penalty before issuance of notice under Section 74(5). These features create a perception of higher revenue realization and “performance” for the authorities. In many cases, officers also act on audit objections or computer-generated mismatch reports and mechanically treat every difference as a suppression. The absence of any independent judicial scrutiny at the initial stage enables such mechanical application, leading to widespread misuse of the fraud provision.

Judicial authorities have consistently held that the invocation of Section 74 must be based on cogent evidence and not mere suspicion. The Supreme Court has in many cases while interpreting similar provisions under the Central Excise law, observed that penalty provisions require proof of mensrea or intent to evade. Under the GST regime, the Courts have held that the absence of allegations or evidence of fraud or suppression renders invocation of Section 74 invalid. Many High Courts have quashed proceedings initiated merely on the basis of return mismatches, reiterating that intent to evade cannot be presumed. The consistent judicial view is that fraud, wilful misstatement, or suppression are serious allegations which must be pleaded with particulars and proved by evidence. Without that, proceedings under Section 74 are wholly without jurisdiction.

In this context, a vital question arises as to how a dealer should respond when a show cause notice issued under Section 74 fails to spell out the issue of fraud or wilful misstatement or even make out a case for such conduct. When a show cause notice does not disclose any allegation or evidence of fraud, suppression, or wilful misstatement, it is fundamentally defective and suffers from a jurisdictional infirmity. Section 74 can be invoked only when the preconditions stipulated in the section exist and are alleged with precision. In the absence of those ingredients, the invocation of

Section 74 itself is without authority of law. Therefore, a dealer confronted with such a notice must begin by challenging its very maintainability. The reply should clearly state that the notice is void ab initio as it purports to invoke a penal provision without establishing any factual basis for fraud or intent to evade tax. It should be submitted that the proceedings, if at all required, should have been initiated under Section 73, which governs cases involving bona fide mistakes or interpretational differences.

In replying to such a defective notice, the dealer should first raise a jurisdictional objection and thereafter, without conceding the applicability of Section 74, respond to the factual allegations on merits. The reply should specifically point out that the notice fails to identify (a) the nature of the alleged suppression or misstatement, (b) the material or evidence relied upon, and (c) any circumstances suggesting a conscious intent to evade tax. The reply should emphasize that the burden to prove fraud or suppression lies entirely on the department, and that mere differences in returns or delayed reporting do not amount to suppression. Reference may also be made to the CBIC Instruction No. 05/2023-GST dated 13.12.2023, wherein the Board itself directed officers not to mechanically invoke Section 74 and to ensure that evidence of fraud or suppression exists before doing so. Accordingly, the dealer may request that the proceedings under Section 74 be dropped as unsustainable and, if necessary, be reinitiated under Section 73 within limitation.

When show cause notices issued under Section 74 of the Act do not specify any details of the alleged fraud, wilful misstatement, or suppression, it becomes almost impossible for the dealer to give a meaningful reply. A vague or templated notice leaves the dealer bewildered. He is unable to understand what exactly he is accused of, or what material is relied upon to allege fraud or intent to evade. Such a notice is not only unfair but also contrary to the basic principles of natural justice, because the person to whom the notice is issued is entitled to know the precise allegation against him before being called upon to defend himself. In such cases, courts must step in to protect the dealer by admitting writ petitions challenging these defective notices at

the threshold. The judiciary has to play a corrective role and make it clear that a notice under Section 74 without particulars of fraud or wilful misstatement is void and cannot form the basis of any adjudication. Recently, a Division Bench of the Allahabad High Court in Varanasi Sangam Expressway Pvt. Ltd. v. Commissioner of State Taxes quashed a vague show cause notice of this kind. The Court, in a short but significant order, noted that the show cause notice did not contain any allegations or ingredients of fraud, wilful misstatement, or suppression of facts under Section 74 of the U.P. GST Act. It accordingly set aside the notice dated 20.06.2025 while giving liberty to the Department to proceed under any other applicable provision of the Act. This decision is a welcome reminder of how constitutional courts should act when such defective notices are challenged.

Courts should also consider imposing costs or penalties on officers who issue such vague and baseless notices. Unless adjudicating authorities are firmly reprimanded, they will continue issuing these defective show cause notices, causing harassment to honest taxpayers and unnecessary litigation. Officers who misuse Section 74 dilute the seriousness of the provision and burden the judicial system with avoidable cases. The power to issue show cause notices is a quasi-judicial power, and it must be exercised with responsibility and fairness, not mechanically or for statistical performance. When officers ignore the statutory safeguards and act casually, they undermine the credibility of the tax system and create fear and uncertainty among compliant taxpayers. Therefore, holding such officers accountable would not only prevent harassment but also restore trust in the administration of tax laws. Strong judicial intervention and administrative discipline are essential to ensure that Section 74 is reserved only for genuine cases of fraud and not turned into a weapon for routine assessments.

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The misuse of Section 74 has multiple adverse consequences. It results in violation of the principles of natural justice, since the taxpayer is branded as fraudulent without any basis. It constitutes a jurisdictional error because the very condition precedent for invoking the provision existence of fraud or wilful suppression is absent. It also leads to unnecessary litigation and burden on appellate forums, as taxpayers are compelled to defend themselves against serious but unfounded allegations. Most importantly, it erodes taxpayer confidence in the fairness of the tax administration and undermines the voluntary compliance philosophy underlying the GST law.

The CBIC has categorically directed that officers should invoke the extended period only when there is clear evidence of fraud, wilful misstatement, or suppression of facts to evade tax. Despite this, such instructions have not percolated effectively to the adjudicating authorities. To restore balance and fairness, it is necessary that every notice invoking Section 74 should record reasons distinguishing it from a Section 73 case, and that supervisory officers should review the justification for invoking the penal provision before issuance. Accountability should also be fixed where orders invoking Section 74 are set aside for lack of evidence.

Section 74 is meant to be a deterrent for deliberate tax evaders, not a weapon to penalize inadvertent mistakes. When applied mechanically, it defeats the very purpose of the Act and burdens both taxpayers and the administration with unnecessary disputes. It is time for the tax authorities to realize that extended limitation and penal proceedings demand extended justification, and that Section 73, not Section 74, should be the norm in all ordinary cases of non-payment or short payment of tax arising from bona fide error, interpretational difference, or accounting omission. Only then can the spirit of fairness and trust envisioned under the GST regime truly be realized.