REPORT OF THE

COMPTROLLER AND AUDITOR GENERAL OF INDIA

FOR THE YEAR 1982-83

UNION GOVERNMENT (CIVIL)
REVENUE RECEIPTS
VOLUME II
DIRECT TAXES

ERRATA

Page	Para	Line	*For*	*Read*
4	1.03(i) 1.03(iii) 1.04	5 from top 14 from bottom 6 from bottom	* * *	*Figures furnished by the Ministry of Finance are provisional
6	Footnote	Last line	Acconuts	Accounts
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11	1.09(i)(b)	15 from bottom	1982-33	1982-83
17	1.10(iii)	13 from top (Col. 5)	189.05	189.06
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20	1.11(v)	16 from bottom	199	1992
20	1.11(v)	7 from bottom	63	68
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75	2.20(i)(b)	8 from bottom	2,31,871	2,13,871
78	2.20(iv)	13 from bottom	until	unit
94	2.27(ii)	11 from bottom	76,57,843	76,57,483
96	2.29(i)(b)	6 from top	constructed	constituted
128	3.09(iv)	4 from bottom	(vi)	(iv)
147	3.20	5 from bottom	Incomt	Income
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REPORT OF THE

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DIRECT TAXES

TABLE OF CONTENTS

PREFATORY REMARKS

As mentioned in the prefatory remarks of Volume I of the Audit Report on Revenue Receipts of the Union Government, the results of audit of receipts under Direct Taxes are presented in this separate volume. The Report is arranged in the following order :—

(i) Chapter 1 sets out statistical and other information relating to Direct Taxes.

(ii) Chapter 2 mentions the results of audit of Corporation Tax.

(iii) Chapter 3 deals, similarly, with the points that arose in the audit of Income-tax receipts.

(iv) Chapter 4 relates to Wealth-tax, Gift-tax and Estate Duty.

The points brought out in this Report are those which have come to notice during the course of test audit. They are not intended to convey or to be understood as conveying any general reflection on the working of the Department concerned.

VOLUME II

CHAPTER 1

GENERAL

1.01 *Receipts under various Direct Taxes*

The total proceeds from Direct Taxes for the year 1982-83 amounted to Rs. 4,138.23* crores out of which a sum of Rs. 1,147.75 crores was assigned to the States. The figures for the three years 1980-81, 1981-82 and 1982-83 are given below :—

(In crores of rupees)

		1980-81@	1981-82	1982-83
020	Corporation Tax	1377.45	1969.96	2184.51
021	Taxes on Income other than Corporation Tax	1439.93	1475.50	1569.72
023	Hotel Receipts Tax	(—)0.09**	2.32	0.07
024	Interest Tax	..	..	265.47
028	Other Taxes on Income and Expenditure	89.52	231.67£	..
031	Estate Duty	16.23	20.31	20.38
032	Taxes on Wealth	67.37	78.12	90.37
033	Gift Tax	6.51	7.74	7.71
	Gross Total	2996.92	3785.62	4138.23
	Less share of net proceeds assigned to the States:			
	Income-tax	1001.97	1016.88	1131.77
	Estate Duty	12.38	16.50	15.98
	Hotel Receipts Tax	..	0.82	..
	Total	1014.35	1034.20	1147.75
	Net Receipts	1982.57	2751.42	2990.48

*Figures furnished by the Controller General of Accounts are provisional.

**Rs. 30.69 lakhs received under this Major Head "023—Hotel Receipts Tax" was to be shared with States. Provisional allocation for sharing was made for Rs. 40.01 lakhs of estimated receipts which gave rise to a negative figure of Rs. 0.09 crore.

@ Actuals for the year 1980-81 have been adopted from the "Union Government Finance Accounts 1980-81".

£Includes Rs. 231.63 crores on account of receipts under Interest Tax. This tax was discontinued with effect from 28 February 1978 but re-imposed with effect from 30 June 1980.

The gross receipts under Direct Taxes during 1982-83 went up by Rs. 352.61 crores when compared with the receipts during 1981-82 as against an increase of Rs. 788.70 crores in 1981-82 over those for 1980-81. Receipts under Corporation Tax registered an increase of Rs. 214.55 crores while receipts under "Taxes on income other than Corporation Tax" accounted for an increase of Rs. 94.22 crores.

1.02 *Variations between budget estimates and actuals*

(i) The actuals for the year 1982-83 under the Major heads 021—Taxes on Income, etc., 031—Estate Duty, 032—Taxes on Wealth and 033—Gift Tax, exceeded the budget estimates.

The figures for the years from 1978-79 to 1982-83 under the various heads are given below :—

Year	Budget estimates	Actuals	Variation	Percentage of variation
1	2	3	4	5
			(In crores of rupees)	
020—Corporation Tax				
1978-79 . . .	1441.90	1251.47	(—)190.43	(—)13.20
1979-80 . . .	1529.50	1391.90	(—)137.60	(—)8.99
1980-81 . . .	1515.00	1377.45	(—)137.55	(—)9.08
1981-82 . . .	1690.00	1969.96	279.96	16.56
1982-83 . . .	2382.00	2184.51	(—)197.49	(—)8.29
021—Taxes on Income other than Corporation Tax				
1978-79 . . .	1134.80	1177.39	42.59	3.75
1979-80 . . .	1247.10	1340.31	93.21	7.47
1980-81 . . .	1426.00	1439.93	13.93	0.98
1981-82 . . .	*1444.00	1475.50	31.50	2.18
1982-83 . . .	1562.75	1569.72	6.97	0.45
031—Estate Duty				
1978-79 . . .	11.00	13.08	2.08	18.91
1979-80 . . .	12.00	14.05	2.05	17.08
1980-81 . . .	13.00	16.23	3.23	24.85
1981-82 . . .	15.00	20.31	5.31	35.40
1982-83 . . .	17.00	20.38	3.38	19.88

*Figures have been revised and confirmed by the Ministry of Finance

1	2	3	4	5
			(In crores of rupees)	
032—Taxes on Wealth				
1978-79 . . .	55.00	55.41	0.41	0.75
1979-80 . . .	60.00	64.47	4.47	7.45
1980-81 . . .	65.00	67.37	2.37	3.65
1981-82 . . .	66.00	78.12	12.12	18.36
1982-83 . . .	80.00	90.37	10.37	12.96
033—Gift Tax				
1978-79 . . .	5.75	5.85	0.10	1.74
1979-80 . . .	5.75	6.83	1.08	18.78
1980-81 . . .	6.25	6.51	0.26	4.16
1981-82 . . .	6.25	7.74	1.49	23.84
1982-83 . . .	6.75	7.71	0.96	14.22

(ii) The details of variations under the heads subordinate to the Major Heads 020 and 021 for the year 1982-83 are given below :—

1	Budget 2	Actuals 3	Increase (+)/ shortfall (—) 4	Percentage of variation 5
			(In crores of rupees)	
020—Corporation Tax				
(i) Income-tax on companies	2315.00	2098.17	(—)216.83	(—)9.36
(ii) Surtax	59.00	69.31	10.31	17.47
(iii) Receipts awaiting transfer to other minor heads .	..	2.53	2.53	..
(iv) Other receipts . .	8.00	14.50	6.50	81.25
Total . . .	2382.00	2184.51	(—)197.49	(—)8.29
021—Taxes on income other than Corporation Tax				
(i) Income-tax . . .	1392.14	1436.65	44.51	3.20
(ii) Surcharge . . .	158.61	111.31	(—)47.30	(—)29.82
(iii) Receipts awaiting transfer to other minor heads .	..	8.50	8.50	..
(iv) Other receipts . .	12.00	13.26	1.26	10.50
(v) Deduct share of proceeds assigned to States . .	1097.88	1131.77	33.89	3.08
Total . . .	464.87	437.95	(—)26.92	(—)5.79

1.03 *Analysis of collections*

Under the provisions of the Income-tax Act, 1961, income-tax is chargeable for any assessment year in respect of the total income of the previous year at the rates prescribed in the annual

Finance Act. The Act, however, provides for pre-assessment collection by way of deduction of tax at source, advance tax and payment of tax on self-assessment. The post-assessment collection is of residuary taxes not so paid.

(i) The break-up of total collections* of Corporation Tax, Surtax and Taxes on income other than Corporation Tax by pre-assessment and post-assessment, during the year 1982-83, as furnished by the Ministry of Finance, is as under :—

	Amount (In crores of rupees)
1. Deduction at source	970.60
2. Advance tax	2547.45£
3. Self-assessment	296.01
4. Regular assessment	267.30

Besides, the Ministry of Finance have intimated Refunds of Rs. 445.42 crores.

(ii) The details of deduction at source under broad categories are as under :—

	Amount (In crores of rupees)
1. Salaries	279.09
2. Interest on securities	178.47
3. Dividends	101.30
4. Interest other than interest on securities	142.08
5. Payment to contractors and sub-contractors	139.52
6. Other items	130.14

(iii) Advance Tax*.—Tax payable and collected by way of advance tax during the year 1982-83 is as under :—

	Amount (In crores of rupees)
1. Tax payable by way of advance tax as per statements received, self-estimates or revised estimates filed and notices issued	2528.73
2. Tax collected out of (1) above	2266.77£
3. Arrears out of (1) above on 31 March 1983	261.96

1.04 *Interest**

The Act provides for payment of interest by the assessees for certain defaults such as delayed submission of returns, delayed payment of taxes, etc. In some cases such as those where advance tax has been paid in excess or where a refund due to the assessee is delayed, Government have also to pay interest.

£The discrepancy in the figures is under verification by the Ministry of Finance.

The particulars of interest levied and interest paid by Government under different provisions of the Act during the year 1982-83 are given below :—

	No. of assess-ments	Amount (In crores of rupees)
(a) The total amount of interest levied under various provisions of the Income-tax Act . . .	8,47,538	343.90
(b) Of the amount of interest levied, the amount :		
(1) Completely waived by the department .	18,151	8.70
(2) Reduced by the department . . .	1,31,458	142.85
(3) Collected by the department . . .	2,74,395	40.55
(c) The total amount of interest paid :		
(1) On advance tax paid in excess of assessed tax	1,31,275	10.79
(2) On delayed refunds	818	0.38
(3) Where no claim is needed for refund . .	8,313	2.95

1.05 *Cost of collection*

(i) The expenditure incurred during the year 1982-83 in collecting Corporation Tax and Taxes on Income other than Corporation Tax, together with the corresponding figures for the preceding three years, is as under :—

	(In crores of rupees) Gross collections	Expenditure on collections
020—Corporation Tax		
1979-80	1391.90	5.93
1980-81	1377.45	6.78
1981-82	1969.96	7.64
1982-83*	2184.51	9.02
021—Taxes on income, etc.		
1979-80	1340.31	41.48
1980-81	1439.93	47.50
1981-82	1475.50	53.48
1982-83*	1569.72	63.17

(ii) The expenditure incurred during the year 1982-83 in collecting other direct taxes, *i.e.*, Taxes on Wealth, Gift-tax and Estate Duty together with the corresponding figures for the preceding three years is as under :—

	(In crores of rupees) Gross collections	Expenditure on collections
031—Estate Duty		
1979-80	14.05	1.05
1980-81	16.23	1.21
1981-82	20.31	1.36
1982-83*	20.38	1.60

*Figures furnished by the Controller General of Accounts are provisional.

032—Taxes on Wealth		
1979-80	64.47	3.69
1980-81	67.37	4.22
1981-82	78.12	4.75
1982-83**	90.37	5.62
033—Gift Tax		
1979-80	6.83	0.53
1980-81	6.51	0.60
1981-82	7.74	0.68
1982-83**	7.71	0.80

1.06 *Number of assessees*

(i) *Income Tax*

Under the provisions of the Income-tax Act, 1961, tax is chargeable on the total income of the previous year of every person. The term 'person' includes an individual, a Hindu undivided family, a company, a firm, an association of persons or a body of individuals, a local authority and an artificial juridical person.

For the assessment year 1982-83 no income-tax was payable on a total income not exceeding Rs. 15,000 except in the case of registered firms, co-operative societies, local authorities and companies.

(a) The total number of assessees in the books of the department was 45,46,769 as on 31st March 1983 as against 46,60,865 as on 31 March 1982. The break-up of the assessees on the said two dates was as under :—

	As on 31 March 1982	As on 31 March 1983
Individuals	35,21,156	34,11,833
Hindu undivided families	2,32,521	2,23,437
Firms	7,86,321	7,71,146
Companies	46,335	48,597
Others	74,532	91,756
Total	46,60,865*	45,46,769*

(b) The number of trust assessees in the books of the department as on 31 March 1982 and 31 March 1983 included under "others" in sub-para (a) above were as follows :—

	As on 31 March 1982	As on 31 March 1983
(i) Public Charitable trusts	30,467	37,099
(ii) Discretionary trusts	13,288	9,026
Total	43,755*	46,125*

*Figures furnished by the Ministry of Finance are provisional.
**Figures furnished by the Controller General of Acconuts are provisional.

(c) The following table indicates the break-up* of the assessees according to slabs of income :—

	Individuals	Hindu undivided families	Firms	Companies	Others	Total
(*i*) Below taxable limit	8,71,313	58,298	1,18,088	24,199	53,793	11,25,691
(*ii*) Above taxable limit but upto Rs. 25,000 .	17,16,721	1,03,160	2,84,383	10,252	23,146	21,37,662
(*iii*) Rs. 25,001 to Rs. 50,000	6,61,647	47,652	2,17,746	4,595	9,414	9,41,054
(*iv*) Rs. 50,001 to Rs. 1,00,000	1,37,852	12,692	1,11,430	2, 903	3,609	2,68,486
(*v*) Rs. 1,00,001 to Rs. 5,00,000	23,701	1,578	37,959	3,720	1,580	68,538
(*vi*) Above Rs. 5,00,000	599	57	1,540	2,928	214	5,338
TOTAL . . .	34,11,833	2,23,437	7,71,146	48,597	91,756£	45,46,769

* Figures furnished by the Ministry of Finance are provisional.
£ Includes private discretionary trusts and public charitable trusts.

(ii) *Wealth Tax*

Under the provisions of the Wealth-tax Act, 1957, wealth-tax is levied for every assessment year on the net wealth of every individual and Hindu undivided family according to the rates specified in the Schedule to the Act. No wealth-tax is levied on companies with effect from 1 April 1960. However, levy of wealth-tax on companies has been revived in a limited way with effect from 1 April 1984.

For the assessment year 1982-83, no wealth-tax was payable where the net wealth is less than Rs. 1.50 lakhs.

The number of wealth-tax assessees in the books of the department as on 31 March 1982 and 31 March 1983 were as follows :—

	As on 31 March 1982	As on 31 March 1983
Individuals	3,57,652	3,68,675
Hindu undivided families	53,649	54,614
Others	86	22
Total	4,11,387	4,23,311

(iii) *Gift Tax*

Under the provisions of the Gift-tax Act, 1958, gift-tax is levied according to the rates specified in the Schedule for every assessment year in respect of gifts of movable or immovable properties made by a person to another person (including Hindu undivided family or a company or an association of persons or body of individuals whether incorporated or not) during the previous year.

During the assessment year 1982-83, no gift-tax was payable where the value of taxable gifts did not exceed Rs. 5,000.

The number of gift-tax assessment cases for the years 1981-82 and 1982-83 were as follows :—

1981-82	70,049*
1982-83	58,103*

*Figures furnished by the Ministry of Finance are provisional.

(iv) *Estate Duty*

Under the provisions of the Estate Duty Act, 1953, in the case of every person dying after 15 October 1953, estate duty at rates fixed in accordance with Section 35 of the Act is levied upon the principal value of the estate comprised of all property settled or not settled including agricultural land which passes on the death of such person.

During the assessment year 1982-83, no estate duty was chargeable where the principal value of the estate passing on death, did not exceed Rs. 1,50,000.

The number of estate duty assessment cases for the years 1981-82 and 1982-83 were as follows :—

1981-82	36,295*
1982-83	37,575*

1.07 *Public Sector Undertakings**

	Central Govt. under-takings	State Govt. under-takings
(1) No. of Public Sector undertakings (including nationalised banks) out of the company assessees, assessed to tax during the financial year 1982-83	205	466
(2) Tax paid by these undertakings during the Financial year 1982-83	(In crores of rupees)	
(i) Advance tax	787.52	28.82
(ii) Self-assessment tax	38.62	6.43
(iii) Regular tax paid in 1982-83 out of arrear and current demands	25.96	6.68
(iv) Surtax	58.00	0.74
(v) Interest tax	199.68	1.36
Total	1109.78	43.90**

*Figures furnished by the Ministry of Finance are provisional.

**The discrepancy in the figures of total is under verification by the Ministry of Finance. The figures do not include C.I.T. Lucknow charge.

1.08 *Foreign company assessees**

(i) Cases where returns had been filed for the assessment year 1982-83 and assessments completed, as on 31 March 1983 :—

	Number	Amount (In crores of rupees)
(i) No. of foreign companies	144	
(ii) Income returned		882.32
(iii) Income assessed		883.27
(iv) Gross demand		7.88
(v) Demand outstanding out of (iv) above as on 31 March 1983		0.34
(vi) Tax paid upto 31 March 1983 (iv-v) . .		7.54

(ii) Cases where returns had been filed for the assessment year 1982-83 but assessments were pending as on 31 March 1983 :—

	Number	Amount (In crores of rupees)
(i) No. of foreign companies . . .	192	
(ii) Income returned		183.95
(iii) Gross demand, being tax due on income returned		63.07
(iv) Demand outstanding out of (iii) as on 31 March 1983		1.93
(v) Tax paid upto 31 March 1983 (iii-iv) . .		61.19£

(iii) Cases where no returns had been filed for the assessment year 1982-83, as on 31 March 1983 :—

No. of foreign companies	184

1.09 *Arrears of assessments**

The limitation period for completion of assessments is 2 years in the case of Income-tax, 4 years in the case of Wealth-tax and Gift-tax and 5 years in the case of Estate Duty.

*Figure furnished by the Ministry of Finance are provisional.

£The difference of Rs. 0.05 crore in Delhi (c) charge is between the gross demand on the basis of returned income at Rs. 0.94 crore and tax collected thereon as on 31-3-1983 amounting to Rs. 0.99 crore which will be refundable on completion of regular assessments.

(i) *Income-tax including Corporation Tax*

(a) The number of assessments completed out of arrear assessments and out of current assessments during the past five years were as under :—

Financial Year	Number of assessments for disposal	Number of assessments completed				Number of assessments pending at the end of the year
		Out of current	Out of arrears	Total	Percentage	
1978-79	52,35,891	21,07,544	12,02,783	33,10,327	63.2	19,25,564
1979-80	57,89,055	18,97,276	15,92,514	34,89,790	60.0	22,99,265
1980-81	65,91,180	18,12,511	22,22,702	40,35,213	61.2	25,55,967
1981-82	72,08,405	20,05,194	25,42,522	45,47,716	63.0	26,60,689
1982-83	70,15,368	20,19,664	24,15,450	44,35,114	63.2	25,80,254

(b) Category-wise break-up of the total number of assessments completed during the years 1981-82 and 1982-33 was as under :—

	1981-82	1982-83
Scrutiny assessments	10,89,620	11,36,817
Summary assessments	34,58,096	32,98,297
Total	45,47,716	44,35,114

(c) Status-wise break-up of income-tax assessments completed during the years 1981-82 and 1982-83 was as under :—

	1981-82	1982-83
(i) Individuals	35,04,796	31,96,494
(ii) Hindu undivided families	2,11,264	1,80,561
(iii) Firms	7,29,501	6,95,369
(iv) Companies	47,238	46,751
(v) Association of persons etc.	54,917	81,341
Total	45,47,716	42,00,516£

£Figures do not include Cs.I.T. Bihar and Lucknow charges.

(d) Assessment year-wise position of pendency of income-tax assessments at the end of the last two years was as under :—

	As on 31 March 1982	As on 31 March 1983
1978-79 and earlier years	56,759	30,577
1979-80	1,68,843	16,083
1980-81	7,46,916	1,12,947
1981-82	16,88,171	6,51,248
1982-83	..	16,76,045
Total	26,60,689	24,86,900*

(e) Category-wise break-up of pending income-tax assessments as on 31 March 1982 and 31 March 1983 was as under :—

	As on 31 March 1982	As on 31 March 1983
Scrutiny assessments	9,88,100	10,86,017
Summary assessments	16,72,589	14,94,237
Total	26,60,689	25,80,254

(f) Status-wise and year-wise break-up of pendency of income-tax assessments in respect of various assessment years as on 31 March 1983 was as under :—

Status	1978-79 and earlier years	1979-80	1980-81	1981-82	1982-83	Total
(a) Company assessments	2,592	979	3,944	16,538	33,585	57,638
(b) Non-company assessments	27,985	15,104	1,09,003	6,34,710	16,42,460	24,29,262
Total	30,577	16,083	1,12,947	6,51,248	16,76,045	24,86,900*

The number of assessment cases to be finalised as on 31 March 1983 has decreased as compared to that at the close of the previous year. The number of assessments pending as on 31 March 1983 was 25,80,254 as compared to 26,60,689 as on 31 March 1982 and 25,55,967 as on 31 March 1981. Of the 25,80,254 of pending cases as many as 14,94,237 cases related to summary assessments.

*Figures do not include Cs.I.T. Lucknow, Bihar and Kanpur (C) charges.

(ii) *Wealth-tax, Gift-tax and Estate Duty*

(a) The total number of wealth-tax assessments completed during the years 1981-82 and 1982-83 were as under :—

	1981-82	1982-83
Individuals	3,37,255	3,42,231
Hindu undivided families	50,917	44,532
Others	9,039	1,066
Total	3,97,211	3,87,829

(b) The number of gift-tax assessments completed during the years 1981-82 and 1982-83 were as follows :—

	1981-82	1982-83
Individuals	67,095	71,509
Hindu undivided families	1,660	3,235
Others	209	232
Total	68,964	74,976

(c) The number of estate duty assessments completed during the years 1981-82 and 1982-83 were as under :—

1981-82	35,257
1982-83	38,483*

The break-up of the estate duty assessments completed during the year 1982-83 according to certain slabs of principal value of estate was as under :—

Principal value of property	Number of assessments completed
(1) Exceeding Rs. 20 lakhs	4
(2) Between Rs. 10 lakhs and Rs. 20 lakhs	61
(3) Between Rs. 5 lakhs and Rs. 10 lakhs	481
(4) Between Rs. 1 lakh and 5 lakhs	5,978
(5) Between Rs. 50,000 and Rs. 1 lakh	6,494
(6) Below Rs. 50,000	24,049
Total	37,067*

*The discrepancy in the figures is under verification by the Ministry of Finance.

(d) Assessment year-wise details of wealth-tax, gift-tax and estate duty assessments pending as on 31 March 1983 were as under :—

	Number of assessments pending		
	Wealth-tax	Gift-tax	Estate-duty
1978-79 and earlier years . . .	14,842	3,252	7,890
1979-80	75,368	6,066	4,137
1980-81	91,937	7,976	4,909
1981-82	1,23,533	12,357	6,807
1982-83	2,36,285	16,902	11,320
Total	5,41,965	46,553	35,063

(e) The year-wise details of assessments under Companies (Profits) Surtax Act, 1964, pending as on 31 March 1983 were as under :—

Year	Number of assessments
1978-79 and earlier years	1,261
1979-80	696
1980-81	2,400
1981-82	27,803
1982-83	52,516
Total	84,676

1.10 *Arrears of tax demands**

The Income-tax Act, 1961, provides that when any tax, interest, penalty, fine or any other sum is payable in consequence of any order passed under the Act, a notice of demand shall be served upon the assessee. The amount specified as payable in the notice of demand has to be paid within 35 days unless the time for payment is extended by the Income-tax Officer on application made by the assessee. The Act has been amended with effect from 1 October 1975 to provide that an appeal against an assessment order would be barred unless the admitted portion of the tax has been paid before filing the appeal.

*Figures furnished by the Ministry of Finance are provisional.

(i) *Corporation Tax and Income-tax*

(a) The total demand of tax raised and remaining uncollected as on 31 March 1983 was Rs. 1469.94* crores including Rs. 332.76 crores in respect of which the permissible period of 35 days had not expired as on 31 March and Rs. 6.36 crores claimed to have been paid but remaining to be verified/adjusted, Rs. 261.74 crores stayed/kept in abeyance and Rs. 24.15 crores for which instalments had been granted by the department and the Courts.

(b) Demands of Income-tax (including Corporation Tax) stayed as on 31 March 1983 on account of appeals and revision petitions were as under :—

	(In crores of rupees)
(1) By Courts	65.26
(2) Under Section 245F(2) (applications to Settlement Commission)	22.53
(3) By Tribunal	3.83
(4) By income-tax authorities due to :—	
(i) Appeals and revisions	122.94
(ii) Double income-tax claims	4.70
(iii) Restriction on remittances—Section 220(7)	1.48
(iv) Other reasons	41.00
Total	261.74

(c) The amounts of Corporation Tax, Income-tax, interest and penalty making up the gross arrears and the year-wise details thereof are given below :—

					(In crores of rupees)
	Corporation tax	Income-tax	Interest	Penalty	Total
Arrears of 1972-73 and earlier years	16.30	45.25	16.40	22.93	100.88
1973-74 to 1979-80	38.42	141.58	74.70	42.71	297.41
1980-81	30.91	58.84	34.43	13.43	137.61
1981-82	43.04	84.02	51.36	21.04	199.46
1982-83	313.40	202.31	173.46	27.19	716.36
TOTAL	442.07	532.00	350.35	127.30	1451.72*

*The discrepancy in the figures is under verification by the Ministry of Finance.

(d) The following table gives the break-up of the gross arrears of Rs. 1469.94 crores by certain slabs of income.

	Number of assessees (entries)	Total arrears of tax (In crores of rupees)
Upto Rs. 1 lakh in each case . . .	28,17,760	627.51
Over Rs. 1 lakh upto Rs. 5 lakhs in each case .	6,963	148.54
Over Rs. 5 lakhs upto Rs. 10 lakhs in each case .	1,196	83.83
Over Rs. 10 lakhs upto Rs. 25 lakhs in each case	600	89.08
Over Rs. 25 lakhs in each case	456	520.98
Total	28,26,975	1469.94

(ii) *Other Direct Taxes* (i.e., *Wealth-tax, Gift-tax and Estate Duty*)

The following table* gives the year-wise arrears of demands outstanding and the number of cases relating thereto under the three other direct taxes *i.e.*, wealth-tax, gift-tax and estate duty as on 31 March 1983 :—

(Amount in lakhs of rupees)

	Wealth-tax		Gift-tax		Estate duty	
	Number of cases	Amount	Number of cases	Amount	Number of cases	Amount
1978-79 and earlier years .	64,857	5118.29	33,026	550.03	9,851	741.70
1979-80	34,748	1942.44	7,535	107.96	2,826	308.14
1980-81	48,878	3756.85	9,268	546.76	3,565	309.00
1981-82	55,146	2995.48	12,602	260.69	5,493	621.59
1982-83	84,372	4219.92	19,430	714.20	8,520	1410.20
TOTAL .	2,88,001	18032.98	81,861	2179.64	30,255	3390.63

(iii) Where an assessee defaults in making payment of tax, penalty and interest, the Income-tax Officer may issue a certificate to the Tax Recovery Officer for recovery of the demand by attachment and sale of the defaulter's moveable or immovable property, arrest of the defaulter and his detention in prison, appointing a receiver for the management of the defaulter's moveable and immovable property, etc. The tax demands

*Figures furnished by the Ministry of Finance are provisional.

certified to the Tax Recovery Officers and the progress of recovery to end of 1982-83 are given in the following table :—

Year	Demand Certified			Demand recovered during the year	Balance at the end of the year
	At the beginning of the year	During the year	Total		
				(In crores of rupees)	
1	2	3	4	5	6
1969-70 . .	359.52	183.55	543.07	116.45	426.62
1970-71 . .	425.25	181.36	606.61	145.37	461.24
1971-72 . .	483.53	208.79	692.32	167.52	524.80
1972-73 . .	530.57	264.98	795.55	189.05	606.49
1973-74 . .	598.15	192.62	790.77	161.93	628.84
1974-75 . .	616.07	188.16	804.23	176.29	627.94
1975-76 . .	616.35	333.92	950.27	290.56	659.71
1976-77 . .	678.72	330.30	1009.02	370.67	638.35
1977-78 . .	00'8E9	258.00	896.00	244.00	652.00
1978-79 . .	655.00	309.00	964.00	267.00	697.00
1979-80 . .	703.96	323.65	1027.61	287.61	740.00
1980-81 . .	752.07	301.70	1053.77	258.58	795.19
1981-82 . .	861.58	400.24	1261.82	273.33	988.49
1982-83* . .	855.55	335.59	1167.02	324.73	867.44

Note : No. of certificates issued during the year 1982-83—4,76,269.

1.11 *Appeals, Revision petitions and writs*

Under the provisions of the Income-tax Act, 1961, if an assessee is dissatisfied with an assessment, a refund order, etc., he can file an appeal to the Appellate Assistant Commissioner. The Act also provides for appeal by the assessee direct to the Commissioner (Appeals).

A second appeal can be taken to the Income-tax Appellate Tribunal. After the Tribunal's decision, a reference on a point of law can be taken to the High Court from which an appeal lies to the Supreme Court. The assessee can also initiate writ proceedings under Article 226 of the Constitution.

A tax payer can approach the Commissioner of Income-tax to revise an order passed by an Income-tax Officer or by an Appellate Assistant Commissioner within one year from the

*Figures furnished by the Ministry of Finance are provisional. The discrepancy in the figures is under verification by the Ministry of Finance.

date of such orders. The Commissioner can also take up for revision an order which in his view is prejudicial to the interest of revenue.

(i) Particulars of Income-tax appeals* and revision petitions pending as on 31 March 1983 were as under :—

	Income-tax appeals with Appellate Assistant Commissioners/ Cs.I.T. (Appeals)	Income-tax revision petitions with Commissioners
Number of appeals/revision petitions pending—		
(a) Out of appeals/revision petitions instituted during 1982-83	1,44,818	4,906
(b) Out of appeals/revision petitions instituted in earlier years	1,04,630	7,279
Total	2,49,448	12,185

(ii) Particulars of wealth-tax, gift-tax and estate duty appeals* and revision petitions pending as on 31 March 1983 were as under :—

	Appeals with Appellate Asstt. Commissioners/ Cs.I.T. (Appeals)			Revision petitions with Commissioners		
	W.T.	G.T.	E.D.	W.T.	G.T.	E.D.
Number of appeals/ revision petitions pending :—						
(a) Out of appeals/ revision petitions instituted during 1982-83 . .	35,922	1,945	2,098	1,173	48	..
(b) Out of appeals/ revision petitions instituted in earlier years . .	39,575	2,227	3,833	2,070	91	..
Total	75,497	4,172	5,931	3,243	139	..

(iii) Year-wise break-up of income-tax appeal cases and revision petitions pending with Appellate Assistant Commissioners and Comissioners of Income-tax (Appeals), and Commissioners of Income-tax as on 31 March 1982 and 31 March 1983

*Figures furnished by the Ministry of Finance are provisional.

respectively, with reference to the year of their institution was as under :—

Years of Institution	Appeals pending with Appellate Asstt. Commissioners/Cs.I.T. (Appeals)		Revision petitions pending with Commissioners	
	31 March 1982	31 March 1983	31 March 1982	31 March 1983
1974-75 and earlier years	1,869	1,038	353	296
1975-76	1,875	1,147	157	131
1976-77	3,484	2,106	233	205
1977-78	9,069	3,167	490	441
1978-79	16,328	6,156	915	675
1979-80	32,715	14,473	1,226	917
1980-81	61,578	23,608	2,367	1,765
1981-82	1,30,910	52,935	4,903	2,849
1982-83	..	1,44,818	..	4,906
TOTAL	2,57,828	2,49,448*	10,644	12,185

(iv) Year-wise break-up of wealth-tax, gift-tax and estate duty appeal cases and revision petitions pending with Appellate Assistant Commissioners and Commissioners as on 31 March 1983, with reference to the year of their institution was as under :—

Years of Institution	*Appeals pending with Appellate Asstt. Commissioners/Cs.I.T. (Appeals)			Revision petitions pending with Commissioners		
	W.T.	G.T.	E.D.	W.T.	G.T.	E.D.
1974-75 and earlier years	61	4	26	81	..	..
1975-76	140	18	60	44	1	..
1976-77	409	37	125	100	3	..
1977-78	950	83	301	158	6	..
1978-79	2,463	126	494	140	3	..
1979-80	8,509	454	542	343	22	..
1980-81	9,450	612	794	457	17	..
1981-82	17,593	893	1,491	747	39	..
1982-83	35,922	1,945	2,098	1,173	48	..
TOTAL	75,497	4,172	5,931	3,243	139	..

*Figures furnished by the Ministry of Finance are provisional.

(v) The following table gives details of appeals/references disposed of during the years 1980-81, 1981-82 and 1982-83 :—

	1980-81	1981-82	1982-83
(a) (1) Number of appeals filed before Appellate Assistant Commissioners / Cs.I.T. (Appeals) . . .	2,19,052	2,31,574	2,34,804*
(2) Number of appeals disposed of by AACs/Cs.I.T. (Appeals) . . .	2,08,744	2,37,567	2,61,341*
(b) Number of appeals filed before Income-tax Appellate Tribunals			
(1) by the assessee . .	24,999	24,850	25,083
(2) by the department . .	18,899	21,577	24,935
(c) Number of assessee's appeals decided by the Tribunal in favour of the assessees fully out of (b) (1) above . . .	11,519	10,560	8,510
(d) Number of departmental appeals decided by the Tribunals in favour of the department fully out of (b) (2) above .	4,284	4,491	3,203
(e) Number of references filed to the High Courts			
(1) by the assessees . .	1,753	1,800	1,992
(2) by the department . .	4,593	4,145	5,240
(f) Number of references in the High Courts disposed of in favour of the			
(1) assessees . . .	357	202	113
(2) department . . .	428	490	474
(g) Number of appeals filed to the Supreme Court			
(1) by the assessees . .	11	63	9
(2) by the department . .	218	219	25
(h) Number of appeals disposed of by the Supreme Court in favour of the			
(1) Assessees . . .	31	4	1
(2) Department . . .	4	12	..

*Figures furnished by the Ministry of Finance are provisional.

(vi) Writ petitions pending :—

	In Supreme Court	In High Courts	Total
1	2	3	4
(a) Number of writ petitions pending as on 31-3-1983 . .	330	3,804	4,134
(b) Out of (a) above :			
(i) Pending for over 5 years	31	254	285
(ii) Pending for 3 to 5 years .	60	640	700
(iii) Pending for 1 to 3 years .	161	1,859	2,020
(iv) Pending upto 1 year .	78	1,051	1,129

1.12 *Completion of reopened and set aside assessments**

(i) *Income-tax*

(a) The year-wise details of assessments cancelled under Section 146 of Income-tax Act, 1961 (or under the corresponding provisions of the old Act) and pending finalisation on 31 March 1983 were as follows :—

Assessment year	Number of cases
1974-75 and earlier years	2,049
1975-76	651
1976-77	799
1977-78	1,386
1978-79	2,415
1979-80	5,121
1980-81	5,160
1981-82	2,148
1982-83	2,107
Total	21,836

(b) The year-wise details of assessments cancelled under Section 263 of Income-tax Act, 1961 (or under the corresponding

*Figures furnished by the Ministry of Finance are provisional.

provisions of the old Act) and pending finalisation on 31 March 1983 were as follows :—

Assessment year	Number of Cases
1974-75 and earlier years	173
1975-76	39
1976-77	80
1977-78	240
1978-79	569
1979-80	685
1980-81	379
1981-82	120
1982-83	169
Total	2,454

(c) The year-wise details of assessments set aside by the Appellate Assistant Commissioner/Commissioner (Appeals) under Section 251 of the Income-tax Act, 1961 (or under the corresponding provisions of the old Act), by the Appellate Tribunal under Section 254 of Income-tax Act, 1961, (or under the corresponding provisions of the old Act), where fresh assessments had not been completed as on 31 March 1983 were as under :—

Assessment year	Set aside by Appellate Assistant Commissioners/Commissioners (Appeals)	Set aside by Appellate Tribunal
	Number of cases	Number of cases
1974-75 and earlier years	1,335	240
1975-76	609	77
1976-77	829	99
1977-78	1,102	83
1978-79	1,452	82
1979-80	1,342	79
1980-81	736	44
1981-82	377	26
1982-83	404	58
Total	8,186	788

(ii) *Wealth-tax and Gift-tax*

(a) The year-wise details of assessments cancelled under Section 25 of the Wealth-tax Act, 1957 and under Section 24(2) of the Gift-tax Act, 1958 which were pending finalisation as on 31 March 1983 were as follows :—

Assessment year	Number of cases	
	W.T.	G.T.
1974-75 and earlier years	137	23
1975-76	40	6
1976-77	52	6
1977-78	35	..
1978-79	22	..
1979-80	29	2
1980-81	22	1
1981-82	5	..
1982-83	4	1
Total	346	39

(b) The year-wise details of assessments set aside by the Appellate Assistant Commissioner/Commissioner (Appeals)/ Appellate Tribunal under Section 23(5)/24(5) of the Wealth-tax Act, 1957, Section 22(5)/23(5) of the Gift-tax Act, 1958 and Section 62(5)/63(5) of the Estate Duty Act, 1953, where fresh assessments had not been completed as on 31 March 1983 were as under :—

Assessment years	Set aside by AACs/Commissioners (Appeals)			Set aside by Appellate Tribunal		
	Number of cases			Number of cases		
	W.T.	G.T.	E.D.	W.T.	G.T.	E.D
1974-75 and earlier years	2,266	93	16	149	7	1
1975-76	731	7	1	35	..	..
1976-77	759	12	7	32	1	1
1977-78	328	23	3	19	..	2
1978-79	166	7	2	21	..	3
1979-80	102	11	7	14	..	..
1980-81	76	6	10	17	2	3
1981-82	66	1	26	3	1	2
1982-83	162	5	49	18	..	7
TOTAL	4,656	165	121	308	11	19

1.13 *Reliefs and Refunds**

Refunds

Where the amount of tax paid exceeds the amount of tax payable, the assessee is entitled to a refund of the excess. If the refund is not granted by the department within three months from the end of the month in which the claim is made, simple interest at the prescribed rate becomes payable to the assessee on the amount of such refund.

(i) Refunds under Section 237:—	
(a) No. of applications pending on 1-4-1982	15,090£
(b) No. of applications received during the year 1982-83.	1,28,705
(c) No. and amount of refunds made during 1982-83 :	
(1) Out of (a) above:	
(i) No. of cases	11,816
(ii) Amount Rs. (000) . .	16,271
(2) Out of (b) above:	
(i) No. of cases . .	1,15,671
(ii) Amount Rs. (000) . . .	3,36,591
(d) No. of cases in which interest was paid under Section 243, the amount of such interest and the amount of refund on which such interest was paid during 1982-83:	
(1) Out of (a) above:	
(i) No. of cases	3,652
(ii) Amount of refund Rs. (000) .	744
(iii) Amount of interest paid Rs. (000)	9
(2) Out of (b) above:	
(i) No. of cases	1,336
(ii) Amount of refund Rs. (000) .	4,527
(iii) Amount of interest paid Rs. (000)	289
(e) No. and amount of refunds made during 1982-83 on which no interest was paid:	
(1) No. of cases . . .	98,936
(2) Amount Rs. (000)	4,59,253
(f) No. of applications pending as on 31-3-83	16,364
(g) Break-up of applications mentioned at (f) above:	
(1) For less than a year . . .	14,212
(2) Between 1 year and 2 years . .	1,955
(3) For 2 years and more . .	197

(ii) The Act also provides for refund of any amount which may become due to an assessee as a result of any order passed

*Figures furnished by the Ministry of Finance are provisional.

£The Ministry of Finance have revised the closing balance of 15,433 furnished for the year 1981-82.

in appeal or other proceedings without his having to make any claim in that behalf. Simple interest at the prescribed rate is payable to the assessee in such cases too.

The particulars of appeal/revision, etc., effects, refunds under Section 240 and payment of interest under Section 244, as furnished by the Ministry of Finance, for the year 1982-83, are given below :—

(a)	No. of assessments which were pending revision on account of appellate/revision, etc., orders as on 1-4-1982 . . .	5,412£	
(b)	No. of assessments which arose for similar revision in 1982-83	75,791	
(c)	No. of assessments which were revised during 1982-83		
	(1) Out of those pending as on 1-4-1982	3,547	
	(2) Out of those arising during 1-4-1982 to 31-3-1983	68,871	
		Number	Amount of refund Rs. (000)
(d)	No. of assessments which resulted in refunds as a result of revision and total amount of refund given:—		
	(1) Under item (c) (1) above . .	1,385	37,153
	(2) Under item (c) (2) above . .	29,239	3,38,040
(e)	No. of assessments in which interest became payable under Section 244 and amount of interest:		
	(1) Under item (d) (1) above	282	1,264
	(2) Under item (d) (2) above . .	5,503	20,553
(f)	No. of assessments pending revision as on 31-3-1983:		
	(1) Out of (a) above	2,664	
	(2) Out of (b) above	5,181	
(g)	Break-up of assessments mentioned at (f) above:		
	(1) Pending for less than 1 year . .	6,564	
	(2) Pending for more than 1 year and less than 2 years	1,241	
	(3) Pending for more than 2 years .	40	

1.14 *Cases settled by Settlement Commission*

Under the provisions of the Income-tax Act, 1961 and the Wealth-tax Act, 1957, an assessee may at any stage of a case relating to him, make an application to the Settlement Commission to have the case settled. The powers and procedures

£The Ministry of Finance have revised the closing balance of 5,747 furnished for the year 1981-82.

of the Settlement Commission are specified in the Acts. Every order of settlement passed by the Settlement Commission is conclusive as to the matter stated therein.

An analysis of the cases settled by the Settlement Commission during the years 1976-77 to 1982-83 is given below :—

(i) Income-tax

	1976-77	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83	Total
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
(a) Number of cases with the Commission on 1-4-1982 (with year-wise details)	47	108	222	228	219	247	..	1,071
(b) Number of cases filed with the Commission during 1982-83 . .	..	..	..	..	..	..	358	358
(c) Number of cases disposed of by the Commission (with year-wise details) . . .								
(1) Disposed of by issue of orders under section 245 D(4)	5	29	51	49	15	4	1	154
(2) Number of cases where applications have been rejected.	..	..	2	6	6	15	2	31
(d) Number of cases pending on 31-3-1983 (with year-wise details) .	42	79	169	173	198	228	355	1,244
(e) Total income determined in (c)(1) above								
(1) Number of cases .	154							
(2) Amount . .	Rs. 717.51 lakhs							
(f) Tax on (e) above . (including interest and penalty)	Rs. 207.02 lakhs							

(ii) Wealth-tax

(a) Number of cases with the Commission on 1-4-1982 (with year-wise details) . . .	25	61	137	67	54	77	—	421
(b) Number of cases filed with the Commission during 1982-83 . .	..	...	..	..	..	..	131	131
(c) Number of cases disposed of by the Commission (with year-wise details) :								
(1) Disposed of by issue of an order under Section 22D(4) .	..	1	16	15	4	..	..	36
(2) Number of cases where applications have been rejected	..	..	..	3	..	6	3	12
(d) Number of cases pending on 31-3-1983 (with year-wise details) . .	25	60	121	49	50	71	128	504

(e) Total wealth determined in (c) (1) above
(1) Number of cases 36
(2) Amount . . Rs. 865.79 lakhs

(f) Tax on (e) above . Rs. 10.39 lakhs
(Including interest and penalty)

1.15 *Penalties and prosecutions**

Failure to furnish return of income/wealth/gift or filing a false return invites penalties under the relevant tax law. It also constitutes an offence for which the tax payer can be prosecuted. The tax laws also provide for levy of penalty and prosecution for failure to produce accounts and documents, failure to deduct or pay tax, etc.

(i) Income-tax

A. Penalties

(a) No. of penalty orders passed under section 271(1)(c) during 1982-83	31,184
(b) Concealed income involved in (a) above	Rs. 16.09 crores
(c) Total amount of penalty levied in (a) above :	
(i) No of orders	9,355
(ii) Amount	Rs. 13.11 crores
(d) Total amount of penalty collected in (c) above :	
(i) No. of orders	1,168
(ii) Amount	Rs. 0.69 crore
(e) No. of penalty orders passed under other sections of the Act during 1982-83	4,97,411
(f) Income involved in (e) above	Rs. 42.75 crores
(g) Total amount of penalty levied in (e) above :	
(i) No. of orders	1,97,196
(ii) Amount	Rs. 16.23 crores
(h) Total amount of penalty collected in (g) above :	
(i) No. of orders	37 212
(ii) Amount	Rs. 1.88 crores

B. Prosecutions

(a) No. of prosecutions pending before the courts on 1-4-1982	2,428
(b) No. of prosecution complaints filed during 1982-83 under Sections 276C, 276CC, 276D, 277 and 278	994
(c) No. of prosecutions decided during 1982-83	69
(d) No. of convictions obtained in (c) above	28
(e) No. of cases which were compounded before launching prosecutions	41
(f) Composition money levied in such cases (e) above	Rs. 8.61 lakhs

*Figures furnished (December 1983) by the Ministry of Finance are provisional.

(ii) Wealth-tax and Gift-tax

A. Penalties

	Wealth-tax	Gift-tax
(a) No. of penalty orders passed under section 18(1)(c)/17(1)(c) during 1982-83.	6,637	396
(b) Amount of concealed net wealth/value of gift involved in (a) above (in lakhs of rupees)	731.76	10.60
(c) Total amount of penalty levied in (a) above :		
(i) No. of orders ..	1,875	95
(ii) Amount (in lakhs of rupees)	296.50	1.16
(d) Total amount of penalty collected in (c) above :		
(i) No. of orders	853	38
(ii) Amount (in lakhs of rupees)	9.31	0.09
(e) No. of penalty orders passed under other sections during 1982-83	52,496	4,546
(f) Amount of net wealth/value of gift involved in (e) above (in lakhs of rupees)	79,983.51	159.44
(g) Total amount of penalty levied in (e) above :		
(i) No. of orders	17,934	1,117
(ii) Amount (in lakhs of rupees)	453.76	15.59
(h) Total amount of penalty collected in (g) above :		
(i) No. of orders	3,359	145
(ii) Amount (in lakhs of rupees)	21.93	0.63

B. Prosecutions

(a) No. of prosecutions pending before the courts on 1-4-1982	101
(b) No. of prosecution complaints filed during 1982-83 under Sections 35A, 35B, 35C, 35D and 35F	99
(c) No. of prosecutions decided during 1982-83.	..
(d) No. of convictions obtained in (c) above	..
(e) No. of cases which were compounded before launching prosecutions	..
(f) Composition money levied in such cases (e) above (in lakhs of rupees)	..

1.16 *Searches and Seizures**

Sections 132, 132A and 132B of the Income-tax Act, 1961, provide for search and seizure operations. A search has to be

*Figures furnished by the Ministry of Finance are provisional.

authorised by a Director of Inspection, Commissioner of Income-tax or a specified Dy-Director of Inspection or Inspecting Assistant Commissioner. Where any money, bullion, jewellery or other valuable article or thing is seized, the Income-tax Officer has, after necessary investigations, to make an order with the approval of the I.A.C. within 90 days of the seizure, estimating the undisclosed income in a summary manner on the basis of the material available with him and calculating the amount of tax on the income so estimated, specifying the amount that will be required to satisfy any existing liability and retain in his custody such assets as are, in his opinion sufficient to satisfy the aggregate of the tax demands and forthwith release the remaining portion, if any, of the assets to the person from whose custody they were seized. The books of account and other documents cannot be retained by the authorised officer for more than 180 days from the date of seizure unless the Commissioner approves of the retention for a longer period.

Searches and Seizures

(a) Number of cases in which search and seizure were conducted during the last three years :

	No. of assessees	No. of assessments
1980-81	2,105	4,102
1981-82	1,683	4,434
1982-83	3,070	5,692
(b) No. of search cases in which assessments were awaiting completion at the beginning of the year 1982-83		
(1) No. of assessees	6,172	
(2) No. of assessments	12,663	
(c) No. of search cases in which assessments were completed during the year 1982-83		
(1) No. of assessees	4,135	
(2) No. of assessments	7,860	
(d) (A) No. of search cases in which assessments are awaiting to be completed at the end of the year 1982-83		
(1) No. of assessees	5,107	
(2) No. of assessments	10,495	
(B) Number out of (A) above, which are pending for more than 2 years after the date of search :		
(1) No. of assessees	1,395	
(2) No. of assessments	3,285	

(e) Total concealed income assessed in cases referred to in item (c) above :	
(1) No. of cases	1,465
(2) Amount	Rs. 33.84 crores
(f) Penalty levied for concealment of income in search cases during the year (irrespective of whether assessments are completed in this year or earlier)	
(1) No. of cases	120
(2) Amount	Rs. 3.45 crores
(g) No. of search cases in respect of which prosecution was launched in the Court during the year 1982-83 (irrespective of whether assessments are completed in this year or earlier)	265
(h) No. of convictions obtained during the year 1982-83	17
(i) No. of cases where no concealment or tax evasion found on completion of assessments	2,670
(j) Total amount of cash, jewellery, bullion and other assets seized during the year 1982-83 (approximate value) :	
(1) Cash	Rs. 6.86 crores
(2) Bullion and jewellery	Rs. 14.39 crores + 24 Dollars
(3) Others	Rs. 6.71 crores + 55 Pounds
TOTAL	Rs. 27.96 crores + 24 Dollars + 55 Pounds
(k) No. of search cases in respect of which summary assessment orders under section 132(5) of the Income-tax Act were passed during the year 1982-83	768
(l) Amount of undisclosed income determined in the orders under section 132(5) referred to in item (k) above	Rs. 41.71 crores
(m) (1) Value of assets retained as a result of orders passed under section 132(5) referred to in item (k) above	Rs. 15.82 crores +24 Dollars
(2) Value of assets returned as a result of orders passed under section 132(5) referred to in item (k) above	Rs. 2.41 crores +55 Pounds

(n) Amount of cash, jewellery, bullion and other assets held on 31-3-1983 irrespective of the year of search :	
(1) Cash	Rs. 13.57 crores
(2) Bullion and jewellery	Rs. 17.54 crores
(3) Others	Rs. 5.80 crores +12 Silver ingots
TOTAL*	Rs. 36.91 crores +24 Dollars +55 Pounds +12 Silver ingots
(o) Arrangements made for the safe custody of the assets still held and for their physical verification	Cash is deposited in the personal Deposit Account of the Commissioners of Income-tax in the Reserve Bank of India. Other valuables are kept either in well guarded strong rooms in the office building or in the treasuries or in Bank vaults, etc.

1.17 *Functioning of Valuation Cells*

The Central Government established October 1968, a departmental Valuation Cell manned by Engineering officers taken on deputation from the Central Public Works Department to assist the assessing officers under various direct tax laws. Certain details about the functioning of the Valuation Units under the Cell are given in the following sub-paragraphs :

(i) No. of Valuation Units/Districts :

Year	No. of Units	No. of Districts
1980-81	80	10
1981-82	80	11
1982-83	80	11

	Income-tax	Wealth-tax	Gift-tax	Estate-duty
(ii) No. of cases referred				
1980-81@	16,242	15,272	133	480
1981-82	14,982	17,539	107	496
1982-83	11,619	15,815	129	599
(iii) No. of cases decided				
1980-81	13,282	10,655	100	341
1981-82	12,626	12,671	67	260
1982-83	9,864	11,444	101	424
(iv) No. of cases pending				
1980-81	2,960	4,617	33	139
1981-82	2,356	4,868	40	236
1982-83	1,755	4,369	28	175

*The discrepancy in the figurs is under verification by the Ministry of Finance.

@No. of cases brought forward from previous years have been included in respect of all the taxes.

1.18 *Revenue demands written off by the department**

(i) *Income-tax*

A demand of Rs. 485.41 lakhs in 23,251 cases was written off by the department during the year 1982-83. Of this, a sum of Rs. 224.89 lakhs relate to 84 company assessees and Rs. 260.52 lakhs to 23,167 non-company assessees.

Income-tax demands written off by the department during the year 1982-83 are given below categorywise :—

(Amount in lakhs of rupees)

	Companies		Non-companies		Total	
	No.	Amount	No.	Amount	No.	Amount
1 2	3	4	5	6	7	8
I. (a) Assessees having died leaving behind no assets or have become insolvent . .	..	..	809	21.77	809	21.77
(b) Companies which have gone into liquidation and are defunct	18	115.66	78	12.70	96	128.36
TOTAL	18	115.66	887	34.47	905	150.13
II. Assessees being untraceable	32	22.86	12,541	149.12	12,573	171.98
III. Assessees having left India	..	..	198	9.04	198	9.04

*Figure furnished by the Ministry of Finance are provisional.

1	2	3	4	5	6	7	8
IV.	Other reasons :						
	(a) Assessees having no attachable assets .	13	70.44	2,913	35.41	2,926	105.85
	(b) Amount being petty, etc.	17	1.60	5,336	20.39	5,353	21.99
	(c) Amount written off as a result of scaling down of demands	3	13.45	1,274	3.73	1,277	17.18
	TOTAL	33	85.49	9,523	59.53	9,556	145.02
V.	Amount written off on grounds of equity or as a matter of international courtesy or where time, labour and expenses involved in legal remedies for realisation are considered disproportionate to the amount of recovery .	1	0.88	18	8.36	19	9.24
	GRAND TOTAL	84	224.89	23,167	260.52	23,251	485.41

(ii) Wealth-tax, Gift-tax and Estate Duty demands written off by the department during the year 1982-83 are given below categorywise :—

(Amount in lakhs of rupees)

	Wealth-tax		Gift-tax		Estate Duty	
	No.	Amount	No.	Amount	No.	Amount
I. (a) Assessees having died leaving behind no assets or become insolvent	1	0.18	10	0.50	..	..
(b) Companies which have gone into liquidation and are defunct	2	1117.62	1	2.80	..	..
TOTAL	3	1117.80	11	3.30	..	..
II. Assessees being untraceable	644	5.53	609	6.11	..	..
III. Assessees having left India	1	0.27	11	11.47	..	..
Other reasons :						
(a) Assessees who are alive but have no attachable assets	29	5.60	12	0.01	..	..
(b) Amount being petty, etc.	..	..	..	..	..	..
(c) Amount written off as a result of scaling down of demands	..	..	300	2.72	..	..
TOTAL	29	5.60	312	2.73	..	..
V. Amount written off on grounds of equity or as a matter of international courtesy or where the time, labour and expenses involved in legal remedies for realisation are considered disproportionate to the amount of recovery	1	0.05	..	..	..	..
GRAND TOTAL	678	1129.25	943	23.61	..	..

(iii) A test check conducted in 23 Commissioners charges during the years 1979-80 to 1981-82 revealed that outstanding demands of revenue relating to income-tax/wealth-tax in 108 cases, involving a sum of Rs. 102.83 lakhs, were written off by the department on the grounds that relevant assessment records, papers relating to recovery proceedings, etc., were missing or were not traceable. Of these, in 3 cases in one Commissioner's charge, the demand written off during the year 1981-82 was Rs. 44.75 lakhs. This demand relates to different assessment years between 1956-57 and 1972-73.

1.19 *Results of test audit in general*

(i) *Corporation Tax and Income-tax*

During the period from 1 April 1982 to 31 March 1983 test audit of the documents of the income-tax offices revealed total under-assessment of tax of Rs. 3936.53 lakhs in 18,720 cases. Besides these, various defects in following the prescribed procedures also came to the notice of Audit.

Of the total 18,720 cases of under-assessment, short levy of tax of Rs. 3351.91 lakhs was noticed in 1,782 cases alone. The remaining 16,938 cases accounted for under-assessment of tax of Rs. 584.62 lakhs.

The under-assessment of tax of Rs. 3936.53 lakhs is due to mistakes categorised broadly under the following heads :–

	No. of cases	Amount (In lakhs of rupees)
1	2	3
1. Avoidable mistakes in computation of tax .	1,548	127.04
2. Failure to observe the provisions of the Finance Acts	312	51.95
3. Incorrect status adopted in assessments .	364	177.75
4. Incorrect computation of salary income .	507	13.74
5. Incorrect computation of income from house property	792	48.39
6. Incorrect computation of business income .	3,051	970.16
7. Irregularities in allowing depreciation and development rebate	1,224	483.77

1	2	3	4
8.	Irregular computation of capital gains . .	255	67.26
9.	Mistakes in assessment of firms and partners	693	107.74
10.	Omission to include income of spouse/minor child, etc.	135	29.23
11.	Income escaping assessment. . . .	1,476	193.34
12.	Irregular set off of losses	194	58.14
13.	Mistakes in assessments while giving effect to appellate orders	101	156.43
14.	Irregular exemptions and excess reliefs given .	1,727	406.64
15.	Excess or irregular refunds	627	89.58
16.	Non-levy/incorrect levy of interest for delay in submission of returns, delay in payment of tax etc.	1,906	145.36
17.	Avoidable or incorrect payment of interest by Government	767	131.21
18.	Omission/short levy of penalty . . .	810	217.03
19.	Other topics of interest/miscellaneous . .	2,098	230.39
20.	Under-assessment of Surtax/Super Profits Tax	133	231.38
	TOTAL	18,720	3,936.53

(ii) *Wealth-tax*

During test audit ot assessments made under the Wealth-tax Act, 1957, short levy of Rs. 213.56 lakhs was noticed in 3,255 cases.

The under-assessment of tax of Rs. 213.56 lakhs was due to mistakes categorised broadly under the following heads :-

	No. of cases	Amount (In lakhs of rupees)
1	2	3
1. Wealth escaping assessment . . .	568	38.57
2. Incorrect valuation of assets . . .	686	42.12
3. Mistakes in computation of net wealth . .	449	22.35
4. Incorrect status adopted in assessments .	113	11.13
5. Irregular/excessive allowances and exemptions	494	15.91
6. Mistakes in calculation of tax . . .	423	16.82
7. Non-levy or incorrect levy of additional wealth-tax	133	22.05
8. Non-levy or incorrect levy of penalty and non-levy of interest	165	11.30
9. Miscellaneous	224	33.31
TOTAL	3,255	213.56

(iii) *Gift-tax*

During the test audit of gift-tax assessments it was noticed that in 650 cases there was short levy of tax of Rs. 246.62 lakhs.

(iv) *Estate Duty*

In the test audit of estate duty assessments it was noticed that in 448 cases there was short levy of estate duty of Rs. 47.34 lakhs.

CHAPTER 2

CORPORATION TAX

2.01 The trend of receipts from corporation tax *i.e.* income-tax payable by companies was as follows during the last five years :—

Year	Amount (in crores of rupees)
1978-79	1251.47
1979-80	1391.90
1980-81	1377.45
1981-82	1969.96
1982-83	2184.51*

*2.02 According to the Department of Company Affairs, Ministry of Law, Justice and Company Affairs, there were 85,011 companies as on 31 March 1983. These included 320 foreign companies and 1,536 associations "not for profit" registered as companies limited by guarantee and 253 companies with unlimited liability. The remaining 82,902 companies comprised 943 Government companies and 81,959 non-Government companies with paid up capitals of Rs. 14,722.5 crores and Rs. 5,273.7 crores respectively. Among non-Government companies, over 86 per cent (70,588) were private limited companies.

2.03 The number of companies on the books of the income-tax department during the last five years was as follows :—

As on 31st March	Number
1979	41,532
1980	42,581
1981	44,125
1982	46,355**
1983	48,597**

*Figures furnished by the Department of Company Affairs, Ministry of Law, Justice and Company Affairs are provisional.

**Figures furnished by the Ministry of Finance are provisional.

2.04 The following table indicates the progress in the completion of assessments and collection of demand under corporation-tax during the last five years :—

Year	No. of assessments		Amount of demand	
	Completed during the year	Pending at the close of the year	Collected during the year	In arrear at the close of the year
			(In crores of rupees)	
1978-79	39,982	40,563	1251.47	168.04
1979-80	38,033	43,886	1391.90	190.34
1980-81	44,937	52,250	1377.45	290.95
1981-82	47,238	55,861	1969.96	311.74*
1982-83	46,751	57,638	2184.51	442.07*

2.05 Some instances of mistakes noticed in the assessments of companies under the Income-tax Act are given in the following paragraphs.

2.06 *Avoidable mistakes in the computation of tax*

Under-assessment of tax on account of mistakes in the computation of total income or in the determination of tax payable, attributable to carelessness or negligence and involving substantial losses of revenue have been reported every year.

In paragraph 5.21 of their 186th Report (Fifth Lok Sabha) the Public Accounts Committee commented on the commonest mistake regularly featured in the Audit Reports involving the dropping of digits, generally one lakh of rupees, either from the assessed total income or from the amount of tax payable.

In paragraphs 5.24 and 5.25 of their 51st Report (7th Lok Sabha) the Committee observed that under-assessment of taxes of substantial amounts had been noticed year after year, on account of mistakes due to carelessness or negligence, which could have been avoided had the assessing officers and their staff been a little more vigilant.

The Central Board of Direct Taxes, in their instructions issued in December 1968, May 1969, October 1970, October

*Figures furnished by the Ministry of Finance are provisional.

1972, August 1973, January 1974 and the Directorate of Inspection (Income-tax) in their circular issued in July 1981 emphasised the need for ensuring arithmetical accuracy in the computation of income and tax, carry forward of figures etc. In spite of these repeated instructions such mistakes continue to occur. A few important cases are given in the following paragraphs :—

(i) A company had debited in its profit and loss account for the previous year relevant to the assessment year 1980-81, a sum of Rs. 9,34,435 towards liability for additional wages which included Rs. 6,38,643 for the assessment years 1978-79 and 1979-80. While completing the assessment in May 1981 (revised in October 1981) the assessing officer held that the liabilities for the assessment years 1978-79 and 1979-80 were not allowable as they had already been considered in the respective assessments but added back only Rs. 4,78,981 instead of Rs. 6,38,643. This resulted in under-assessment of income by Rs. 1,59,662 with under-charge of tax of Rs. 1,02,982.

The assesment was checked in internal audit, but the mistake escaped their notice.

The paragraph was sent to the Ministry of Finance in August 1983 ; their reply is awaited (December 1983).

(ii) In the case of a company, in respect of the assessment year 1978-79, an amount of Rs. 9,23,998 being expenses on the delivery of a barge was deducted in the assessment order dated 13 May 1981. It was noticed in audit in February 1983 that the assessee company had already included this sum in the total revenue expenditure which stood reflected in the net loss returned. Allowance of the expenditure again separately as a deduction in the assessment order resulted in double deduction and overstatement of loss to the extent of Rs. 9,23,998 with a potential tax effect of Rs. 5,33,610.

The Ministry of Finance have accepted the mistake.

(iii) The total income of a private limited company for the assessment year 1979-80 was computed in February 1982 at a loss of Rs. 7,89,582. It was noticed in audit in July 1982, that the loss computed included a sum of Rs. 6,82,481 being adjusting entry carried out in the previous year relevant to the assessment

year 1979-80 in reversal of certain book-keeping errors relating to the assessment year 1977-78. Since these transactions had been already taken into account while computing the income for the assessment year 1977-78, their inclusion again in the assessment year 1979-80 was not warranted. The mistake resulted in excess computation of loss of Rs. 6,82,481 involving potential tax effect of Rs. 4,29,962.

The Ministry of Finance have accepted the mistake and have stated that the assessment in question has been revised in August 1983 reducing the loss.

(iv) In the case of an assessee company loss pertaining to the assessment year 1973-74 aggregating to Rs. 17,44,127 was allowed to be carried forward. Out of this, loss to the extent of Rs. 9,65,292 was adjusted against income in the subsequent assessment year 1975-76 leaving a balance loss of Rs. 7,78,835 for set off in subsequent assessment years. However, in the assessment for the assessment year 1977-78 completed in September 1981, a sum of Rs. 17,78,835 instead of a sum of Rs. 7,78,835 was adjusted towards loss pertaining to the assessment year 1973-74. This resulted in excess adjustment of carry forward loss by Rs. 10 lakhs involving a potential tax effect of Rs. 5,77,500.

The Ministry of Finance have accepted the mistake and have stated that the assessment in question has been rectified in June 1983 reducing the carry forward loss.

(v) A public limited industrial company debited a sum of Rs. 9,00,000 being provision for sales rebate to the profit and loss account of the previous year ended 30 June 1977 relevant to the assessment year 1978-79 (appended to the return of income filed in June 1978). The company filed a revised return of income for the same assessment year in October 1980 claiming that the correct amount of sales rebate for the year ended 30 June 1977 was Rs. 11,64,603 as against Rs. 9,00,000 shown in the accounts as well as the original return and that credit notes for the difference amounting to Rs. 2,64,603 were issued and charged off in the accounts of the subsequent year. In the assessment concluded in May 1981, the Income Tax Officer allowed the enhanced claim of Rs. 11,64,603. However, while completing the assessment for the assessment year 1979-80 in December 1981, the Income Tax Officer omitted to add back the sum of

Rs. 2,64,603 which though actually debited by the assessee in the accounts for the previous year ended 30 June 1978, related to the earlier previous year and had been allowed in the assessment for that year. The omission resulted in short computation of income for the assessment year 1979-80 by Rs. 2,64,603 with consequent undercharge of tax of Rs. 1,60,452.

While accepting the mistake the Ministry of Finance have stated that the assessment has been rectified in December 1982 and the additional tax of Rs. 1,60,452 collected.

(vi) In the assessment of another private limited company for the assessment year 1978-79 made in April 1981, due to a totalling mistake in the assessment order an amount of Rs. 18,60,962 only was added to the net profit while computing taxable income as against the correct total addition of Rs. 19,60,962.

The assessee being an industrial company with taxable income exceeding Rs. 2 lakhs, tax was required to be calculated at sixty per cent whereas the tax was calculated at 55 per cent. These two mistakes resulted in the short levy of tax of Rs. 1,15,011.

The Ministry of Finance have accepted the mistake and have stated that the assessment has been revised in October 1982 raising additional demand of Rs. 1,15,011 which has also been collected.

(vii) While computing income of an assessee, the Income Tax Officer starts from the profit or loss as shown in the profit and loss account and adds back the amount chargeable in the account and then allows deductions and reliefs as admissible under the Act.

While computing the total income of a company in February 1982 for the assessment year 1980-81, the Income Tax Officer started from the net loss of Rs. 3,19,33,054 as per the profit and loss account and disallowed therefrom a sum of Rs. 67,99,441. The resultant loss was, however, erroneously arrived at Rs. 2,52,33,613 instead of the correct loss of Rs. 2,51,33,613. The mistake resulted in excess computation and carry forward of loss of Rs. 1,00,000 for the assessment year 1980-81.

The Ministry of Finance have accepted the mistake.

(viii) While computing income, the Income Tax Officer adds back the amount of depreciation actually charged in the accounts and then allows the amount of depreciation admissible under the Act.

(a) In the assessment completed in November 1980 of a company for the assessment year 1976-77, depreciation of Rs. 4,31,679 already charged in the account was omitted to be added back although depreciation of Rs. 4,46,101 as admissible under the Act was allowed. The double deduction of depreciation once as per accounts and again under the Act resulted in excess carry forward of unabsorbed depreciation of Rs. 4,31,679 for this assessment year with consequent undercharge of tax of Rs. 2,49,294 in the assessment year 1977-78 when the unabsorbed depreciation was set off against positive income.

The Ministry of Finance have accepted the mistake and have stated that the assessments for the assessment years 1976-77 and 1977-78 have been rectified.

(b) In the case of a State Fisheries Development Corporation, for the assessment year 1979-80, (assessment made in February 1982) depreciation of Rs. 16,49,702 already charged to the account was omitted to be added back although depreciation of Rs. 8,43,642 as admissible under the Act was allowed separately. This resulted in excess allowance of depreciation of Rs. 16,49,702. Further while partially setting off of business loss of Rs. 41,10,475 against income of Rs. 14,37,142 under other sources, the resultant figure was incorrectly arrived at a loss of Rs. 39,66,733 instead of Rs. 26,73,333. These mistakes resulted in excess computation and carry forward of loss of an aggregate sum of Rs. 29,43,102 for the assessment year 1979-80 involving potential tax effect of Rs. 16,99,641.

The Ministry of Finance have accepted the mistakes.

(c) A company, in its accounts for the year relevant to the assessment year 1977-78, debited a sum of Rs. 18,76,000 towards depreciation on furniture, office equipment, motor car, etc. While completing the assessment for the assessment year 1977-78 in April 1981, the depreciation charged to the profit and loss account was added back and depreciation admissible under the Act was allowed as a deduction. While adding back the depreciation debited to the accounts, the figure of Rs. 12,99,000

debited to the accounts relating to the assessment year 1978-79 was added back by mistake in place of Rs. 18,76,000. The mistake resulted in under assessment of total income by Rs. 5,77,000 for the assessment year 1977-78 involving short levy of tax of Rs. 5,93,126 including penal interest of Rs. 99,965 for belated submission of return and interest of Rs. 1,59,944 for short payment of advance tax.

While accepting the mistake the Ministry of Finance have stated that the assessment has been revised in July 1982 and the additional demand has been collected.

(d) In computing the business income of a private company for the assessment year 1979-80 in November 1981, the Income Tax Officer omitted to add back to the net profits a sum of Rs. 1,61,608 debited to the profit and loss account on account of depreciation, although depreciation amounting to Rs. 1,56,131 admissible under the Act was allowed. The mistake resulted in excess allowance of depreciation and carry forward of loss of Rs. 1,61,608 for set off in the future years.

The Ministry of Finance have accepted the mistake.

(e) While computing the business income of a company for the assesment year 1978-79 in March 1981, the Income Tax Officer allowed depreciation of Rs. 4,81,45,401. This included a sum of Rs. 3,53,004 on account of depreciation on capital assets in hotels belonging to the company.

It was noticed in audit in September 1982, that the company had intimated the department in February 1981 that depreciation on capital assets in hotels was inadvertantly worked out as Rs. 3,53,004 against the correct amount of Rs. 9,051. Inspite of the assessee company informing the department about the excess claim of depreciation before the assessment for the assessment year 1978-79, the Income Tax Officer allowed the depreciation as originally claimed by the assessee. No rectification of the assessment to reduce the excess allowance of depreciation was also made by the Income Tax Officer till the date of audit. As a result, depreciation was allowed in excess by Rs. 3,43,953 leading to short computation of business income by an identical amount, involving short levy of tax of Rs. 1,98,630.

The Ministry of Finance have accepted the mistake.

(ix)(a) The total income of a private limited company for the assessment year 1979-80 was computed in January 1982 at Rs. 60,416 before allowing admissible depreciation amounting to Rs. 7,09,788. After set-off of the depreciation against the available income, the unabsorbed depreciation to be carried forward for adjustment in subsequent years was Rs. 6,49,372. As against that, a sum of Rs. 7,49,372 was allowed to be carried forward by the department. This resulted in carrying forward of unabsorbed depreciation in excess by Rs. 1 lakh involving a potential tax effect of Rs. 57,750.

The paragraph was sent to the Ministry of Finance in August 1983 ; their reply is awaited (December 1983).

(b) For the assessment year 1976-77, a company in which the public were substantially interested claimed a total depreciation of Rs. 58,15,702 which included a sum of Rs. 1,54,232 being depreciation on sewage works and buildings of the company. The written down value of sewage and other buildings was Rs. 3,08,465 and the amount of depreciation at the admissible rate of 5 per cent worked out to Rs. 15,425 only and not Rs. 1,54,232 as determined by the department. However, while completing the assessment in January 1980, the department allowed depreciation of Rs. 1,54,232 on sewage works as claimed by the assessee instead of allowing a sum of Rs. 15,425. The mistake resulted in under assessment of income of Rs. 1,38,807 involving short demand of tax of Rs. 80,164.

The Ministry of Finance have accepted the mistake and have reported that the assessment has been rectified raising additional demand of Rs. 80,164 which has been collected.

(c) The assessment of a company for the assessment year 1980-81 was completed in a Central Circle in November 1981 and the total income was reduced to 'nil' after setting off unabsorbed depreciation of Rs. 30,35,071 relating to the assessment year 1977-78. It was noticed in audit in October 1982 that the assessing officer determined the income under "other sources" at Rs. 1,00,061 and while computing the total income of the company, the said income instead of being added was incorrectly deducted from income under other heads of account. The mistake resulted in under

assessment of total income by Rs. 2,00,122 leading to excess carry forward of unabsorbed depreciation and loss by the same amount.

The Ministry of Finance have accepted the mistake.

(d) The total income of a company for the assessment year 1978-79 assessed in August 1981 was computed at a loss of Rs. 14,90,737 under the head "income from other sources". It was noticed in audit in July 1982 that while deducting depreciation and interest on capital amounting to Rs. 36,84,737 from the license fee of a factory given on lease for Rs. 24,00,000 the net amount was arrived at Rs. 14,90,737, instead of Rs. 12,84,737 correctly assessable. Further, although extra-shift depreciation allowance to the extent of Rs. 8,98,805 was allowed on plant and machinery in the assessment year 1977-78, the same was not taken into consideration in determining the written down value in the assessment year 1978-79 leading to excess allowance of depreciation of Rs. 2,22,846. The mistakes resulted in excess computation of loss of an aggregate sum of Rs. 4,28,846 for the assessment year 1978-79.

The Ministry of Finance have accepted the mistake and have stated that remedial action has been taken. Further report is awaited (December 1983).

(x) Under the Income-tax Act, 1961, tax deducted at source and advance tax paid are given credit for, in the regular assessment.

(a) In the assessment of a non-resident company for the assessment year 1977-78, made in March 1980 and revised in January 1981 a sum of Rs. 19,49,362 being technical service fee received by the assessee was assessed to tax and a tax credit of Rs. 4,29,835 towards tax deducted at source there on was allowed. Pursuant to an appellate order of December 1980 directing the Income Tax Officer to assess the said fee in the assessment year 1978-79, the assessment for the assessment year 1977-78 was revised allowing deletion of Rs. 19,49,362 but the tax credit of Rs. 4,29,835 allowed earlier was not withdrawn. The technical service fee was assessed to tax in the assessment year 1978-79 in March 1981 and the tax credit of Rs. 4,29,835 was also allowed in the assessment year 1978-79. Thus, the tax credit of Rs. 4,29,835 was allowed

twice, once in the assessment year 1977-78 and again in the assessment year 1978-79. The mistake resulted in tax undercharge of Rs. 4,38,404 including short-levy of penal interest of Rs. 8,596 in the assessment year 1977-78.

While accepting the mistake, the Ministry of Finance have stated that the assessment has been rectifid raising additional demand of Rs. 4,38,404 in February 1983. Further report is awaited (December 1983).

(b) In the case of a company, the assessment for the assessment year 1980-81 was completed in October 1981. It was noticed in audit (January 1983) that, while arriving at the net tax payable, the Income Tax Officer had erroneously given credit for tax of Rs. 71,052 deducted at source twice, once as such and again by adding the same amount to advance tax paid. This resulted in short levy of tax of Rs. 71,052.

While accepting the mistake the Ministry of Finance have stated that the assessment has been rectified in June 1983 and additional demand of Rs. 71,052 has been collected.

(c) In the case of a public limited company, the department, while determining the tax payable by the assessee for the assessment year 1978-79 in March 1981, allowed credit for tax deducted at source for Rs. 1,94,754 as against Rs. 1,49,754 worked out on the basis of certificates. In fact, the correct amount of tax deducted at source computed on the basis of certificates filed by the assessee, was Rs. 1,42,026 only. This resulted in short computation of tax by Rs. 70,783 including interest allowed on advance tax.

The Ministry of Finance have accepted the mistake and have stated that the assessment in question has been rectified raising additional demand of Rs. 70,783 which has been adjusted.

2.07 *Incorrect application of rate of tax*

Adoption of incorrect rates of tax is another common mistake. The following cases are illustrative of that.

(i) As per the provisions of the Finance Act, 1978, 1979 and 1980 the rate of tax applicable to income derived by way of 'royalty' or as 'fees for technical services rendered' received by a non-domestic company from an Indian concern will be

fifty per cent of such income, where the agreement made by the non-domestic company with the Indian concern is after 31st day of March, 1961 but before 1st day of April, 1976. In any other case the rate applicable is seventy per cent of such income.

A non-resident company received royalty and technical know-how fees from an Indian concern as per agreements made with the Indian concern on 1 February 1950 and 3 February 1951. Tax was to be calculated on its income received by way of technical know-how fees or royalty for the assessment years 1978-79, 1979-80 and 1980-81 at seventy per cent. However, while completing the assessments in February 1979, March 1980 and February 1982 respectively the Income Tax Officer incorrectly applied the rate of tax at fifty per cent instead of seventy per cent. The application of lower rate of tax, resulted in a total short levy of tax of Rs. 50,830 for the three assessment years.

The paragraph was sent to the Ministry of Finance in August 1983 ; their reply is awaited (December 1983).

(ii) Under the provisions of the Finance Acts applicable to the assessment years 1977-78, 1978-79 and 1979-80 a company in which public are not substantially interested and which is also not an industrial company, is charged to tax at 65 per cent of the total income. An industrial company is, however, charged to tax at the rate of fifty five per cent if the income does not exceed Rs. 2 lakhs and at 60 per cent if the total income exceeds Rs. 2 lakhs.

(a) In the case of a closely held non-industrial company, in the assessment completed in March 1982 by Inspecting Assistant Commissioner for the assessment year 1979-80 the rate of tax was adopted as 60 per cent as applicable to an industrial company against the correct rate of 65 per cent applicable to non-industrial companies. The mistake resulted in short levy of tax of Rs. 5,60.124 including short levy of interest of Rs. 1,45,217 for failure to furnish the estimate of advance tax.

The Ministry of Finance have accepted the mistake.

(b) In the case of a private non-industrial company for the assessment year 1978-79 (assessment completed in July 1981)

the department levied tax applying the rate of 60 per cent on its total income of Rs. 12,63,010 instead of the correct rate of sixty five per cent leading to under charge of tax by Rs. 66,307.

The Ministry of Finance have accepted the mistake.

(c) In the case of another private limited company which derived income from sale of old stock of goods and rental income from storage tanks, tax was calculated by the Income Tax Officer in July 1980 for the assessment year 1977-78 at the rate of fifty five per cent on its total income of Rs. 10,28,910. The company not being an industrial company but only a trading company the rate of tax applicable was sixty five per cent instead of fifty five per cent. The application of incorrect rate of tax resulted in short-levy of tax of Rs. 1,57,764 including interest for late filing of return and for failure to file mandatory estimate of advance tax.

The Ministry of Finance have accepted the mistake and have stated that the assessment has been rectified in March 1983 raising additional demand of Rs. 1,08,040. Further report regarding action taken for the recovery of balance demand is awaited (December 1983).

(d) A company did not file its return of income for the assessment year 1979-80 and the Income Tax Officer completed the assessment on best of his judgment in January 1982, computing the total income at Rs. 6,00,000, and assessed a tax of Rs. 3,46,500 calculated at the rate of 55 per cent of the income. The assessee company's application for the reopening the best judgment assessment was rejected in July 1982 by the Income Tax Officer. It was noticed in audit that in the assessments of the company for the assessment years 1972-73 to 1978-79, the company was assessed in the status of a closely held non-industrial company and taxed at the rate of 65 per cent. There was nothing on record to indicate any change in the status of the company as a widely held industrial company for the assessment year 1979-80. Failure to levy tax at 65 per cent for that year resulted in short levy of tax of Rs. 1,02,060 including penal interest for late filing of returns and for failure to file estimates of advance tax.

The Ministry of Finance have accepted the mistake and have stated that remedial action has been initiated. Further report is awaited (December 1983).

(iii) Under the provisions of the Finance Acts 1977 and 1978, an industrial company means a company which is mainly engaged in the manufacturing or processing of goods. A company shall be deemed to be mainly engaged in the manufacturing or processing of goods, if the income attributable to such activities included in its gross total income of the previous years is not less than fifty one per cent of such total income. A domestic company in which the public are not substantially interested and which is mainly engaged in industrial activity is charged to tax at 60 per cent where the income exceeds Rs. 2 lakhs. In the case of a company which is not engaged in industrial activity, the rate of tax is 65 per cent.

A private limited company engaged in export of precious and semi-precious stones was assessed in March 1981 on a total income of Rs. 35,93,740 for the assessment year 1977-78 and Rs. 10,35,886 for the assessment year 1978-79 and tax was computed at 60 per cent treating the company as an industrial company. The assessed income included Rs. 35,93,107 in the assessment year 1977-78 and Rs. 8,58,000 in the assessment year 1978-79 as income from undisclosed sources or undisclosed export business. In a separate assessment made in March 1982 for the assessment year 1978-79 to determine the additional tax liability of the assessee company on undistributed dividends in excess of statutory percentage, the assessing officer had held that in the absence of any manufacturing details of the precious stones sold outside the books, the company was not a manufacturing company. As the company was held as a non-industrial company the tax on the total income was required to be computed at 65 per cent and not at 60 per cent as was done by the department. The application of incorrect rate resulted in short levy of tax amounting to Rs. 1,88,665 in the assessment year 1977-78 and Rs. 52,334 in the assessment year 1978-79.

The Internal audit party of the department had checked the assessment but the mistakes escaped its notices.

The Ministry of Finance have accepted the mistake.

Incorrect computation of business income

Under the provisions of the Income-tax Act, 1961, any expenditure laid out or expended wholly and exclusively for the purpose of business is allowable as deduction in computing the business income of an assessee, provided the expenditure is not in the nature of capital expenditure or personal expenses of the assessee.

Some instances of mistakes noticed in the computation of business income in the case of companies and corporations are given in the following paragraphs.

2.08 *Mistakes in allowing liabilities*

A provision made in the accounts for an ascertained liability is an admissible deduction but a provision made for a contingent liability does not qualify for deduction.

(i) During the sugar seasons corresponding to the assessment years 1976-77 and 1977-78 two widely held companies sold levy sugar at prices in excess of the prices fixed by Government and filed writ petition in the High Court contending that the sale prices of levy sugar fixed by Government were not commensurate with the expenses incurred. The High Court granted interim injunctions in October/December 1974 and allowed the companies to retain the excess amounts realised by them through sales of sugar at higher prices subject to their furnishing bank guarantees. The High Court also held, *inter alia,* that in the event of any amounts becoming refundable by the companies, they would be liable to pay interest at a specified rate in respect of the amount realised in excess. It was noticed in audit in July 1982 that the companies had made provision for the aforesaid interest amounting to Rs. 9,17,361 and Rs. 13,48,995 in the accounts and this had been allowed as deduction in the assessments for the assessment years 1976-77 to 1978-79 and 1976-77 to 1979-80 respectively. As legal liability to pay could arise olny after final judgment of the High Court, the aforesaid provisions merely represented contingent liabilities and were required to be disallowed. The incorrect allowance thereof resulted in under assessment of income by Rs. 22,66,356 in the assessment years 1976-77 to 1979-80, aggregate undercharge of tax of Rs. 9,98,293 in the assessment years 1977-78 to 1979-80 and an excess carry forward of loss of Rs. 5,37,711 in the assessment year 1978-79.

The Ministry of Finance have accepted the mistake and have stated that remedial action is being initiated. Further report is awaited (December 1983).

(ii) The assessment of a public limited company for the assessment year 1975-76 was completed in April 1979 on a taxable income of Rs. 3,06,37,140. While computing the income, the assessee's claim for deduction for bad debts written off was disallowed to the extent of Rs. 12,91,303 (out of total claim

of Rs. 13,29,870). A further sum of Rs. 4,40,000 claimed as provision for doubtful debts was allowed to be deducted. It was pointed out in audit (December 1982) that the provision for doubtful debts being one for a contingent liability was not admissible and the erroneous allowance had resulted in short levy of tax of Rs. 2,54,100.

While accepting the mistake the Ministry of Finance have stated that the assessment has been rectified in March 1983 and additional demand of Rs. 2,54,100 collected.

2.09 *Incorrect allowance of contribution for scientific research*

(i) In computing the business income of an assessee, any sum paid to a scientific research association, university, college or other institution for scientific research, is an admissible deduction, provided that such association, university, college or institution is approved by the prescribed authority. With a view to encouraging development of indigenous technology and self reliance in industry, the Act was amended in 1974 to provide that, if the contribution was to be used for a specific scientific research undertaken by such institution under a programme approved by the prescribed authority having regard to the social, economic and industrial needs of India, an extra deduction of 33⅓ per cent of the contribution would be allowed.

In the income-tax assessment of a widely held company for the assessment year 1977-78, completed in September 1980, weighted deduction of Rs. 2,66,667 was allowed towards the company's contribution of Rs. 2 lakhs to an Institute of Road Transport. It was noticed in audit (September 1982) that the receipts issued by the institute in April 1976 and December 1976 specifically mentioned the year of actual receipt of amount as 1975-76. The company's accounts also confirmed that the sum of Rs. 2 lakhs was actually paid during the year ended 31st March 1976. Further, the institute was recognised (August 1976) as a scientific research institution for a three year period commencing from 9 April 1976 only. There was no evidence of approval from the prescribed authority for any research programme to be undertaken by the institute in the relevant period. The company was not, therefore, eligible for any deduction for the sums paid either for the assessment year 1977-78 or for the year 1976-77. The incorrect deduction resulted in short levy of tax of Rs. 1,54,000 for the assessment year 1977-78.

The Ministry of Finance have accepted the mistake.

(ii) Any revenue expenditure incurred on scientific research related to the business of the assessee is allowed as a deduction. From the assessment year 1968-69 any expenditure of a capital nature incurred after 31 March 1967 on scientific research related to the business carried on by the assessee is also allowable in full. However, capital expenditure is allowable only after the commencement of business and for this purpose the aggregate of capital expenditure so incurred within three years immediately preceding the commencement is deemed to have been incurred in the previous year in which the business is commenced.

In its accounts for the previous year relevant to the assessment year 1976-77 a company debited a sum of Rs. 2,83,904 which included capital expenditure of Rs. 1,80,968 incurred in connection with the purchase of land for the scientific research unit of the company which had not yet commenced its business. In computing the total income of the company in March 1982, the assessing officer allowed the entire expenditure of Rs. 2,83,904 towards scientific research. The incorrect allowance of capital expenditure of Rs. 1,80,968 resulted in short assessment of income by the same amount involving short levy of tax of Rs. 1,14,004.

The Ministry of Finance have accepted the mistake.

2.10 *Mistakes in the allowance of head office expenses*

In the case of foreign companies doing business in India, a portion of the administrative expenses of their head office becomes an allowable deduction.

Pursuant to the recommendations made by the Public Accounts Committee in paragraph 9.13 of their 176th Report (Fifth Lok Sabha) and paragraph 3.38 of their 187th Report (Fifth Lok Sabha) detailed guidelines on the subject were issued by the Central Board of Direct Taxes in June 1975 and the law was also amended with effect from 1 June 1976. The law as amended fixed a ceiling limit on the deduction on account of head office expenses as the least of the following items :—

(a) an amount equal to five per cent of the adjusted total income or

(b) an amount equal to three years average head office expenditure or

(c) an amount equal to so much of the expenditure in the nature of head office expenditure as is attributable to the business or profession of the assessee in India.

The term "head office expenditure" as defined in the Act means expenditure incurred by the assessee outside India on matters connected with executive and general administration.

The assessment for the assessment year 1978-79 of a foreign company engaged in growing and manufacture of tea in India, having its head office in London, was completed in September 1981 on an income of Rs. 11,90,810. In the profit and loss account of the previous year relevant to the assessment year 1978-79, the company had debited a sum of Rs. 8,63,785 incurred in London on account of secretarial administration, directors' remuneration, auditors' remuneration and general charges. In computing the business income of the company the assessing officer decided to limit the head office expenditure to 5 per cent of the adjusted total income as it was found to be the least of the three items prescribed in the Act. While calculating the amount of disallowance, the assessing officer took into consideration expenditure amounting to Rs. 3,07,967 on account of secretarial administration and directors' remuneration and deducted a sum of Rs. 1,40,323 therefrom being 5 per cent of adjusted total income and disallowed a sum of Rs. 1,67,644 on account of excess head office expenditure.

Omission to take into account the balance expenditure of Rs. 5,55,818 also incurred in London on account of auditors' remuneration and general charges which was connected with executive and general administration resulted in a smaller disallowance of head office expenses. After allowing 5 per cent of adjusted total income from the expenditure of Rs. 8,63,785, the amount of disallowance would correctly work out to Rs. 6,95,671 as against Rs. 1,67,644 disallowed by the assessing officer. Short disallowance on this account was Rs. 5,28,027.

The mistake resulted in under-assessment of income by **Rs. 2,11,210 involving short-levy of tax of Rs. 1,76,972** including excess interest of Rs. 21,733 paid on advance tax.

While not accepting the mistake, the Ministry of Finance have stated that the expenditure on account of audit fee and

general charges which included subscriptions to various bodies and legal charges, is not covered by head office expenditure as defined in the Act and, therefore, would not be liable to be taken into account for working out the 5 per cent limit.

The Ministry's reply is not in conformity with the provisions of the Act. The Act does not give an exhaustive definition of head office expenditure and expenditure on subscriptions to various bodies, legal charges and audit fees would clearly constitute general administration expenditure included in the definition.

2.11 *Incorrect computation of income of financial corporations*

Under the Income-tax Act, 1961, financial corporations engaged in providing long-term finance for industrial or agricultural development in India are entitled to a special deduction in the computation of their taxable profits, of the amount transferred by them out of such profits to a special reserve account upto an amount not exceeding 40 per cent of their total income, as computed before making any deduction under Chapter VI-A of the Act.

The Central Board of Direct Taxes issued instructions in November 1969, to the effect that the above deduction is to be calculated, by applying the specified percentage to the total income arrived at after the deduction is made. In a subsequent clarification, however, the Board stated in November 1973 that the percentage should be applied to the total income computed before making the said deduction. It was pointed out to the Board by Audit that the latter clarification was not in accordance with the provisions of the Act. The Board thereafter issued further instructions in August 1979 restoring the original position contained in the 1969 instructions. The Board also instructed the assessing authorities to take remedial action, whenever feasible, to withdraw the enhanced deduction allowed previously.

(i) In the assessments of an assessee entitled to this concession for the assessment years 1975-76 to 1977-78, deduction of Rs. 1,74,65,004 was allowed (September 1980 and September 1981) by applying a rate of 10 per cent as decided by the Appellate Tribunal for the earlier years on a total income of Rs. 17,46,50,046. For the assessment year 1978-79 (assessment completed in July 1981) a deduction of Rs. 2,20,43,360 was allowed calculated at 25 per cent on the total income of

Rs. 8,81,73,438 without limiting the deduction to the provision of Rs. 1,85,00,000 made for the year 1977 in the accounts for the period relevant to the assessment year 1978-79 for transfer to the special reserve account.

It was seen in audit (September 1982) that the income of Rs. 17,46,50,046 for the assessment years 1975-76 to 1977-78 taken for determining the amount of special deductions was income before and not after allowing the special deduction. For the assessment year 1978-79 despite the revision of the assessment in May 1982 reducing the income to Rs. 7,66,69,744 the special deduction of Rs. 2,20,43,360 as originally allowed was not correspondingly revised and the actual deduction on the income as reduced by special deduction was not recalculated.

As a result of these mistakes, special deduction of Rs. 3,95,08,364 was allowed as against a sum of Rs. 3,12,11,225 correctly admissible. The excess deduction of Rs. 82,97,139 for the four assessment years resulted in a short levy of tax of Rs. 47,91,595.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(ii) In the case of a State Financial Corporation, the total income for the assessment year 1978-79 was assessed in April 1981 by the Income-tax Officer at Rs. 49,56,183 after allowing special deduction of Rs. 14,16,052. The assessment was revised in October 1981 and the total income was reduced to Rs. 36,91,150. It was seen in audit in September 1982 that while revising the assessment, the special deduction was not recalculated with reference to the revised total income. As a result of this omission, there was underassessment of income by Rs. 3,61,438 involving short levy of tax of Rs. 2,08,731. The corporation was also liable to pay interest for late filing of returns and late payment of tax for the assessment year 1978-79 amounting to Rs. 12,626. The total short levey was Rs. 2,21,357.

The Ministry of Finance have accepted the mistake and have stated that the additional demand has been collected.

2.12 *Mistakes in the allowance of contributions to gratuity, provident funds etc.*

(i) Under the provisions of the Income-tax Act, 1961, any sum paid by an employer by way of contribution towards a gratuity fund or a provident fund or a superannuation fund created by him for the exclusive benefit of his employees shall be allowed as a deduction in computing the business income only if the fund is recognised by the Commissioner of Income-tax.

In the assessment computed in September 1979 of a company for the assessment year 1976-77, a provision of Rs. 2,99,404 made by the assessee in its accounts for the year ending 30 June 1975 in respect of gratuity payable to its employees was allowed as deduction. It was noticed in audit in February 1981 that the gratuity fund constituted by the company was accorded approval by the Commissioner of Income-tax on 2 May 1978 with effect from 29 March 1976 only. As no approved gratuity fund was in existence during the relevant previous year, the allowance of gratuity provision of Rs. 2,99,404 in the assessment year 1976-77 was incorrect. The mistake resulted in under-assessment of business income by Rs. 2,99,404 with consequent tax under charge of Rs. 2,04,343.

The Ministry of Finance have accepted the mistake.

(ii) A provision made for gratuity during the previous year relevant to any assessment year commencing on or after 1 April 1973 but before 1 April 1976 is admissible upto the prescribed limit of such a provision is made on the basis of an actuarial valuation of ascertainable liability for the payment of gratuity, an approved fund is created for the benefit of the employees and at least 50 per cent of the admissible amount is paid by the assessee as contribution to the approved gratuity fund before 1 April 1976 and the balance before 1 April 1977. The deduction would be admissible to the extent of actual provision made in each assessment year.

For the assessment years 1973-74 to 1975-76 an assessee company made a provision of Rs. 4,93,906 towards gratuity liability to its employees. During the course of audit in February 1981 it was noticed that the amount of gratuity liability was not calculated on actuarial valuation but determined by the auditors of the company and the provision of Rs. 4,93,906 made was not passed on to the trustees of the gratuity fund in any of the above assessment years.

However, while completing/revising the assessments for the assessment years 1973-74 to 1975-76 in August 1974 and January-February 1979, the department allowed deduction for the amount of Rs. 4,93,906 in computing business income of the assessee company. Failure to disallow the provision resulted in under-assessment of income by Rs. 4,93,906 with consequent short levy of tax of Rs. 3,81,450 including penal interest for short payment of advance-tax for the three assessment years.

The assessments were checked by the Internal audit party of the department, but the mistake was not detected.

The Ministry of Finance have accepted the mistake in principle.

2.13 *Mistakes in the allowance of ex-gratia payments*

As per the provisions of the Income-tax Act, 1961 any payment of bonus in excess of the limit laid down in the Payment of Bonus Act, 1965 or any *ex-gratia* payment in addition to the bonus paid under that Act is not an admissible deduction. The Central Board of Direct Taxes issued instructions in December 1980 clarifying that such additional payment canot also be treated as any other expenditure incurred wholly and exclusively for the purpose of business and resort cannot, therefore, be had to any other provisions of the Act to claim deduction in excess of what is admissible under the Bonus Act.

(i) During the previous year relevant to the assessment year 1978-79 a private limited company made an *ex-gratia* payment of Rs. 4,02,516 in order to preserve "industrial peace" and "achieve greater production" in addition to the statutory bonus amount of Rs. 2,06,677. As the *ex-gratia* payment was over and above the statutory liability for bonus, it was to be disallowed. However, while completing the assessment in September 1981, the excess amount was not disallowed. This resulted in underassessment of income by Rs. 4,02,516 with a potential tax effect of Rs. 2,53,584.

The Ministry of Finance have accepted the mistakes and have stated that remedial action has been initiated. Further report is awaited (December 1983).

(ii) In the accounts of the previous year relevant to the assessment year 1978-79, an assessee company had debited a sum of Rs. 2,12,604 being *ex-gratia* payment made to its employees as a result of settlement made with them in September 1977. The *ex-gratia* payment was over and above the bonus amount of Rs. 1,87,374 payable under the Payment of Bonus Act, 1965 and it was, therefore, not admissible as deduction. While completing the assessment in August 1981 the Income-tax Officer omitted to disallow this amount. This resulted in under assessment of income by Rs. 2,12,604 with a short levey of tax of Rs. 1,35,365.

The Ministry of Finance have acceped the mistake.

(iii) In the case of an assessee company, for the assessment years 1980-81 and 1981-82 (assessed in October 1981) *ex-gratia* payments of Rs. 96,032 and Rs. 1,91,683 were allowed in addition to the bonus paid to the employees under the Payment of Bonus Act, 1965. Since only the bonus paid under the Payment of Bonus Act is an allowable deduction the *ex-gratia* payments were not an allowable business expenditure. Failure to disallow the *ex-gratia* payments resulted in excess carry forward of loss by Rs. 96,032 and Rs. 1,91,683 in the assessment years 1980-81 and 1981-82 respectively with a potential tax effect of Rs. 2,01,040.

The Ministry of Finance have accepted the mistake and have reported that the assessments have been set aside in August 1983. Further report is awaited (December 1983).

2.14 *Income from sale of import entitlements*

Under the Income-tax Act, 1961, the value of any benefit whether convertible into money or not arising from business or exercise of a profession is chargeable to tax under the head "profits and gains of business or profession". The import entitlements granted to exporters are transferable and consequently an exporter who does not need the import of goods can sell or otherwise transfer his import entitlements. It has been held by the Madras and Calcutta High Courts in March 1980 and March 1981 respectively that profits from sale of import entitlements are assessable as business income.

A company engaged in the manufacture and sale of cables obtained premia of Rs. 7,95,849 on sale of import entitlements

during the three assessment years 1979-80, 1980-81 and 1981-82. While completing the assessments for the assessment years 1979-80 and 1980-81 in April 1981 and for the assessment year 1981-82 on 31 March 1982, the Income Tax Officer, under instructions of 26 March 1981 from Inspecting Assistant Commissioner, accepted the assessee's claim that the premia received constiuted capital receipts and further that these receipts could not be taxed as capital gains also since cost of acquisition of entiltements was nil. The department did not, however, consider whether profits would be taxable as business income in the light of the judicial decisions of March 1980 and 1981. As a result of exclusion of the premia there was under-assessment of income by Rs. 7,95,849. This mistake, along with the incorrect allowance of investment allowance of Rs. 19,866 resulted in short demand of tax of Rs. 2,30,432 for all the three years.

The Special Audit Party of the department checked the assessments but failed to detect the mistakes.

The Ministry of Finance have accepted the mistakes and have stated that additional demand for the assessment year 1981-82 has been collected. Final report regarding the collection of demand for the assessment years 1979-80 and 1980-81 is awaited (December 1983).

2.15 *Mistakes in computation*

(i) Under the Income-tax Act, 1961, where any building, machinery, plant or furniture which is owned by the assessee and used for the purpose of his business or profession, is sold, and the amount payable in respect of such building, machinery, plant or furniture, as the case may be, together with the amount of scrap value, if any, exceeds the written down value, so much of the excess as does not exceed the difference between the actual cost and the written down value shall be chargeable to income-tax as income of the business or profession.

For the assessment year 1975-76 a private limited company included in its return profit from sale of old building. While completing the assessment in June 1981 the profit on sale of the building was determined by the assessing officer by deducting a sum of Rs. 2,21,249 being the net cost of the old building instead of its written down value amounting to Rs. 60,982 from

the sale proceeds of the building. The mistake resulted in under assessment of income by Rs. 1,60,267 with short-levy of tax of Rs. 1,09,383.

The Ministry of Finance have accepted the mistake and have reported that the assessment has been set aside. Further report is awaited (December 1983).

(ii) A state industrial development corporation returned a loss of Rs. 55,97,218 for the assessment year 1977-78 on 31 March 1979. The assessment was finalised by the Income-tax Officer in March 1981 on a loss of Rs. 1,31,65,585. It was seen in audit (September 1981) that the corporation had debited in its profit and loss adjusting account relevant to the assessment year 1977-78 a sum of Rs. 62,84,111 under the head "Provision for decline in the value of stock". The provision was made on *ad hoc* basis, to be claimed in the year in which loss would actually take place. As the item of charge was inadmissible, the assessee company itself added it back in the "Statement of computation of income" filed with the return for the assessment year 1977-78. The department, however, while completing the assessment, allowed this inadmissible deduction of Rs. 62,84,111 resulting in excess carry forward of loss to that extent.

This, together with other miscellaneous mistakes amounting to Rs. 2,70,656 led to excess carry forward of loss to the extent of Rs. 65,54,767 with a potential tax effect of Rs. 37,85,378.

The Ministry of Finance have accepted the mistake and have reported that the assessment has been rectified in March 1982.

(iii) No deduction shall be allowed in computing business income in respect of any payment which is chargeable under the head 'salaries' if, it is payable outside India and tax has not been paid thereon, nor deducted at source under the provisions of the Act.

A company incurred an expenditure of Rs. 2.59 lakhs by way of remuneration and out of pocket expenses of foreign technicians during the previous year relevant to the assessment year 1979-80. This amount was payable outside India and no tax at source had been deducted by the assessee under the provisions of the Act. As such, the amount was inadmissible expen-

diture for the purpose of computation of business income. In a revised return for assessment year 1979-80 filed in November 1981 the assessee had also shown the amount as disallowable. However, in the assessment completed on 31 March 1982 the expenditure was allowed as a deduction and the total income was determined as 'nil' and the unabsorbed depreciation was allowed to be carried forward.

The omission to disallow the amount of Rs. 2.59 lakhs resulted in excess carry forward of depreciation in the hands of the assessee to that extent with a potential tax effect of Rs. 1,59,002.

The Ministry of Finance have accepted the mistake and have reported that the assessment has been rectified.

(iv) It has been judicially held in the case of Goodlass Nerolac Paints Limited *Vs.* Commissioner of Income-tax, Bombay City-II (137 ITR 58) that "secret" commission paid to employees is not allowable as expenditure as the assessees fail to furnish names and addresses of persons to whom such commission is alleged to have been paid.

A company engaged in the business of manufacturing paints debited a sum of Rs. 4,46,385 towards commission in the Profit and Loss Account for the period relevant to the assessment year 1978-79. Out of this commission a sum of Rs. 1,36,639 was paid to persons whose names and addresses were not disclosed by the assessee company. In the assessment made in May 1981, the Income Tax Officer allowed the commission in full as business expenditure. In view of the judicial decision, the commission of Rs. 1,36,639 paid to undisclosed persons is not an admissible expenditure. Failure to disallow the same resulted in under assessment of income by Rs. 1,36,639 and short-levy of tax of Rs. 86,082.

The Ministry of Finance have accepted the mistake and have stated that the assessment has been set aside in May 1983. Further report is awaited (December 1983).

2.16 *Mistakes in allowing depreciation*

In the computation of business income of an assessee a deduction on account of depreciation is admissible at the

prescribed rate on plant or machinery provided it is owned by the assessee and used for the purpose of his business during the relevant previous year.

(i) (a) In the case of a foreign company engaged in the business of carrying passengers and cargo all over the world in its airways, the value of fixed assets as in the balance sheets for the years relevant to the assessment years 1975-76 to 1979-80 included assets, shown as "Expenditure on incomplete projects including progress payments and assets not in current use" valued at £ 92.5 million, £ 49.1 million, £ 31.4 million, £ 90.1 million and £145.8 million respectively. While computing the total income in February and March 1982 the assessing officer failed to disallow depreciation on the assets which were incomplete and not used for the purpose of the assessee's business. The omission led to under-assessment of business income by an aggregate amount of Rs. 1,25,87,042 in the assessment years 1975-76 to 1979-80 with consequent under charge of tax of Rs. 1,07,01,823 including penal interest of Rs. 4,31,362 for late filing of returns and excess payment of interest of Rs. 10,18,983 on advance tax paid in excess.

The Ministry of Finance have accepted the mistake in principle.

(b) In the case of a company engaged in the business of manufacture of jute twines and sale thereof, a sum of Rs. 2,39,381 was allowed as depreciation on plant and machinery in the assessment done in July 1981 for the assessment year 1979-80. It was noticed that the jute twine mill of the company was not in operation throughout the previous year relevant to assessment year 1979-80. As the machinery was not used for the purpose of business, the company was not entitled to depreciation in the assessment year 1979-80. The incorrect allowance of depreciation on the unused plant and machinery resulted in excess allowance of depreciation of Rs. 2,39,381 leading to excess carry forward of loss by the same amount for the assessment year 1979-80.

The Ministry of Finance have accepted the mistake.

(c) In the case of a public company according to a note on the accounts recorded by the Auditors of the company, plant and machinery of the value of Rs. 23,04,848 were under installation during the previous year relevant to the assessment year 1978-79. The department, while completing the assessment in August 1981 allowed depreciation and extra shift allowance for the assessment

year 1978-79 on the plant and machinery which were not used for the purpose of the assessee's business. This resulted in excess allowance of Rs. 5,18,591 for the assessment year 1978-79, and consequent excess carry forward of loss of a like amount with a potential tax effect of Rs. 2,99,486.

The Ministry of Finance have accepted the mistake in principle.

(ii) Depreciation is allowed at the prescribed rates, on the actual cost or the written down value of assets as the case may be. The term "actual cost" has been defined in the Act to mean the actual cost of the assets to the assessee as reduced by that portion of the cost which has been met directly or indirectly by any other person or authority.

(a) The assessments of a public limited company engaged in the business of generation and distribution of electricity for the assessment years 1978-79 and 1979-80 were completed by the Inspecting Assistant Commissioner (Assessment) in March 1981 and March 1982. A subsidy of Rs. 4,17,78,735 had been received by the company from Government in the previous years upto the assessment year 1979-80 to meet a part of the cost of machinery. A part of the cost of installation of service lines upto the previous year relevant to assessment year 1979-80 (Rs. 7,94,01,370) was also contributed by the consumers. A total amount of Rs. 12,11,80,105 on account of cost of machinery and service lines not incurred by the assessee company was to be excluded for working out depreciation. The omission on the part of the department to do so resulted in excess allowance of depreciation of Rs. 1,02,67,466 with a potential tax effect of Rs. 59,29,464, for the two assessment years 1978-79 and 1979-80.

The Ministry of Finance have accepted the mistake in principle.

(b) In the case of a company in respect of the previous year relevant to assessment year 1978-79 a part of the cost of machinery was met by a subsidy of Rs. 4,00,700 received from the Central Government. While, computing depreciation and investment allowance on plant and machinery in March 1981, the Income Tax Officer did not deduct the subsidy amounting to Rs. 4,00,700 for the cost of the asset to arrive at depreciation and investment allowance. This omission resulted in excess allowance of depreciation of Rs. 60,105 and investment allowance of Rs. 1,00,175 and consequent excess carry forward of

unabsorbed depreciation and investment allowance by Rs. 1,60,280 with a potential tax effect of Rs. 1,00,976.

The Ministry of Finance have acceped the mistake.

(c) A company established its Phytochemicals project in Madurai district in Tamil Nadu and commenced manufacturing operation during the assessment year 1976-77. The company received a subsidy of Rs. 15 lakhs calculated at 15 per cent of the fixed capital expenditure incurred in the project from the Central Government in the assessment years 1977-78 and 1979-80. Accordingly, the actual cost of the assets installed in the project should have been reduced by the aforesaid 15 per cent (reimbursed to the assessee) for the purpose of allowance of depreciation. The omission to do so resulted in excess allowance of depreciation of Rs. 8,73,812 in the assessment years 1976-77 to 1979-80 leading to excess carry forward of loss by the same amount.

The Ministry of Finance have acceped the mistake.

(iii) Under the Income-tax Act, 1961, in determining the written down value of assets for purposes of allowance of depreciation, both normal depreciation and extra shift allowance are required to be taken into account and not normal depreciation alone.

In the case of a company in which public are substantially interested, although extra shift allowance was allowed on plant and machinery in the assessment years 1977-78 and 1978-79, the same was not taken into account in determining the written down value of the assets in the succeeding assessment years viz. 1978-79 and 1979-80 assessments for which were completed in June and November 1981 respectively. The mistake resulted in excess allowance of depreciation of Rs. 1,24,845 and Rs, 1,91,830 in the assessment years 1978-79 and 1979-80 respectively leading to total excess carry forward of loss of Rs. 3,16,675 in the two years.

The Ministry of Finance have accepted the mistake.

(iv) Special rates of depreciation ranging from 15 per cent to 100 per cent are prescribed for certain specified items of machinery and plant. A general rate of 10 per cent is prescribed (15 per cent from the assesment year 1984-85) in respect of machinery and plant for which no special rate has been prescribed.

For the machinery in sugar mills no special rate of depreciation is prescribed and therefore only the general rate of 10 per cent is applicable.

A company running sugar mills was assessed for the assessment year 1978-79 on a loss of Rs. 5.20 crores and the loss was allowed to be carried forward. The loss included excess allowance of depreciation allowed at the rate of 15 per cent instead of 10 per cent as also consequential excess extra shift allowance, amounting to Rs. 48,24,657 (Depreciation allowance Rs. 27,83,456+Extra Shift allowance Rs. 20,41,201). This resulted in excess carry forward of loss of Rs. 48,24,657 with a potential tax effect of Rs. 22,79,651.

The Ministry of Finance have acceped the mistake.

(v) Under the Income-tax Act, 1961, as amended by Finance (No. 2) Act, 1967, with effect from 1 April 1967 where the assessee had acquired any capital asset from a country outside India for the purpose of his business or profession on deferred payment terms or against a foreign loan before 6 June 1966, the additional rupee liability incurred by him in meeting the cost of the asset is allowed to be added to the original cost of the asset for the purpose of calculating depreciation allowance in computing the profits for the assessment year 1967-68 and subsequent years.

Consequent on the devaluation of Indian currency, on 6 June 1966 an assessee company in its accounts for the assessment years 1972-73 and 1973-74 increased the rupee value of some imported machinery by Rs. 5,55,600 and Rs. 1,48,859 respectively and claimed and was allowed depreciation on the increased cost of the assets. In its accounts for the assessment year 1977-78 the company decreased the rupee value of the outstanding sterling loan by Rs. 5,57,568 for variation in the rate of exchange, reduced the cost of the assets purchased out of the aforesaid loan by the same amount and claimed depreciation on the assets on the reduced value for the assessment years 1977-78 and thereafter. However in the assessments for the assessment years 1977-78 and 1978-79 revised in September 1981 the assessing officer did not take into account the reduced cost of the assets. This omission resulted in excess allowance of depreciation of Rs. 2,08,285 in the assessment years 1977-78 and 1978-79 leading to aggregate tax undercharge of Rs. 1,32,970 (including surtax of Rs. 12,686).

The Ministry of Finance have accepted the mistake.

2.17 *Incorrect allowance of extra shift depreciation*

In the case of plant and machinery, extra shift allowance is given where a concern claims such allowance on account of double or triple shift working. At the instance of Audit, it was clarified by the Ministry of Finance in September 1966 that extra shift allowance should be granted only in respect of machinery which has actually worked extra shift and not in respect of all machinery of the concern which has worked extra shift. Similar instructions were issued by the Central Board of Direct Taxes in December 1967 where it was found, that extra shift allowance was being granted without verifying as to how many days the plant and machinery had actually worked extra shift.

In September 1970, the Board issued instructions in modification of their instructions of December 1967 that where a concern has worked double shift or triple shift, extra shift allowance may be allowed in respect of the entire plant and machinery used by the concern without making any attempt to determine the number of days on which each machine had actually worked double or triple shift during the relevant previous year. These instructions ran counter to the instruction of September 1966 issued at the instance of Audit, as grant of extra shift allowance for the concern as a whole without reference to each machinery is not in accordance with the law. The Board was accordingly requested in July 1971 to re-examine the question. On a reference on the question for their advice, the Ministry of Law opined in February 1978, that if in any particular year any particular machine or plant was not at all used even for a day, then normal depreciation allowance was not admissible and as a corollary thereto extra-shift depreciation would not be admissible and suggested that the Board's instruction of September 1970 should be modified. It followed from the Law Ministry's advice that depreciation both normal and extra shift should be calculated not for the entire concern but with reference to the various items of machinery and plant.

In January 1979, the Board informed Audit that the extra shift allowance is allowed as a percentage of the normal depreciation and where no normal depreciation has been allowed on any particular machinery, because it has not worked even for a day,

no extra shift allowance would become allowable on it. They added that the Board's instructions of September 1970 would not require modification even in the light of Law Ministry's advice of February 1978. It was pointed out to the Board in March 1979 that the Act allows depreciation only in respect of plant and machinery and not 'for a concern' so that calculation of extra shift allowance on the basis of number of days for which the concern as a whole has worked extra shift, would be contrary to the provisions of the Income-tax Act. The Board agreed in April 1979 to examine whether the instructions would require any modification. In June 1981 also the Ministry informed Audit that the matter was under consideration in consultation with the Ministry of Law. The Board were again requested in June 1982 to review and revise their instructions of September 1970. Their reply is awaited.

The point has also come before various High Courts on a number of occasions. The Madras High Court held in September 1981 (135 ITR 206) that the Income Tax Officer has to apply his mind and examine whether the machinery owned by the assessee has been used by him in extra shift. As long as the particular machine has worked extra shift it would be eligible for extra shift allowance on the basis of the number of days it has worked. Earlier the Allahabad and Calcutta High Courts had also in October 1972, July 1974 and April 1980 held (106 ITR 704 ; 116 ITR 851 ; 126 ITR 648) that extra shift allowance has to be calculated in proportion to the number of days the plant and machinery has actually worked and not on an amount equal to the full amount of normal depreciation. In fact these two High Courts had held (73 ITR 395 and 76 ITR 541) even prior to the issue of Board's instruction of September 1970, that the extra shift allowance should be allowed proportionately for the actual number of days the machinery had worked. In all these cases, the department argued and succeeded in obtaining the court's verdict that the extra shift allowance is to be allowed only for the number of days the plant and machinery has worked double or triple shift. There is no judicial decision for the opposite view taken in the Board's instruction of September 1970. The Board have, however, not seen fit to revise their instruction so far.

Four cases where extra shift allowance allowed was not calculated on the basis of number of days the machinery had actually worked extra shift, are given below. The excess

allowance of depreciation in these cases led to short-levy of tax of Rs. 8,67,337.

(i) In the case of a private limited company extra shift allowance amounting to Rs. 2,51,184 was allowed by the Income Tax Officer for the assessment years 1974-75 to 1976-77 on machinery purchased during the previous years relevant to these assessment years. The machinery purchased during these years had not worked for the entire period and the extra shift allowance was to have been restricted to the proportionate amount on the basis of number of days the machinery had actually worked in extra shifts. There was excess allowance of depreciation amounting to Rs. 2,51,184 leading to short levy of tax of Rs. 1,13,101.

The Ministry of Finance have not accepted the mistake pleading that the Income-tax officer's action was in accordance with the existing circulars and instructions of the Board and the remedial action initiated was struck down by the Commissioner of Income-tax (Appeals).

(ii) A dairy development corporation was engaged in milk production and supply with the help of dairy plants in two Cities, besides a dairy farm in one of the Cities and a cattle feed plant and a milk powder plant in the other city. In the previous year ended 31 March 1977 relevant to the assessment year 1977-78 only two dairies worked triple shift throughout the relevant year; the powder plant worked triple shift for part of the year and the other two units did not work triple shift at all. In the course of Income-tax proceedings, in addition to the normal depreciation of Rs. 25,50,676 admissible in respect of all. In the course of Income-tax proceedings, in addition to the allowance on account of triple shift working in respect of plant and machinery in all the units, on the ground that the two dairy plants which were the main units had worked triple shift throughout the year and that some of the other units had worked for some days double/triple shifts. The claim was accepted by the department (September 1980). The department's action in accepting the claim for allowance even in respect of units which had not worked triple shift resulted in excess allowance of depreciation and consequent under-assessment of income by Rs. 7,40,850 and short levy of tax of Rs. 4,33,590.

The Ministry of Finance have accepted the mistake (December 1982) in view of the judicial decision of September

1981 and stated that the assessment is under rectification. Further report is awaited (December 1983).

(iii) A public limited company claimed Rs. 9,56,802 on account of extra shift allowance for the accounting year ending June 30, 1977, relevant to assessment year 1978-79, for having worked double and triple shifts. This was allowed by the department in the assessment completed in August 1981. It was observed from the accounts and schedules attached to the Income-tax return that the assessee had installed new machinery during the months of August 1976 to June 1977 and had claimed extra shift allowance for the full year although the machinery had not worked for the entire period. In the absence of full details even on the basis that the newly installed machinery worked for the entire period subsequent to the month of installation, the extra shift allowance granted was in excess of the permissible amount by Rs. 3,90,729, with consequent short-levy of tax of Rs. 2,25,646.

The paragraph was sent to the Ministry of Finance in Ausust 1983; their reply is awaited (December 1983).

(iv) Another company engaged in the manufacture and sale of groundnut extractions, depreciation admitted for the assessment year 1978-79 (February 1981) and allowed to be carried forward included extra shift allowance of Rs. 2,25,600 equal to normal depreciation for triple shift working. According to the particulars furnished by the assessee in December 1980 the plant had worked only for 65 days during the previous year relevant to the assessment year 1978-79. Accordingly, extra shift allowance for triple shift working should have been limited to Rs. 61,100. Omission to do so, resulted in excess depreciation of Rs. 1,64,500 being allowed to be carried forward with a potential tax effect of Rs. 95,000.

The paragraph was sent to the Ministry of Finance in Ausust 1983; their reply is awaited (December 1983).

2.18 *Other cases of extra shift allowance*

(i) Under the Income-tax Rules, 1962, kilns owned by an assessee and used for his business are entitled to depreciation at the general rate of 10 per cent. An extra shift depreciation

allowance equal to normal allowance shall be allowed where a concern claims such allowance on account of triple shift working.

A public limited company engaged in the manufacture of potteries claimed extra shift allowance for the assessment year 1975-76 on the kilns owned by them on the plea that the kilns were kept burning for technical reasons, though the factory did not work extra shift. This plea was rejected by the Commissioner (Appeals) in his order in August 1980 and the extra shift allowance allowed on the kilns for the assessment year 1975-76 was withdrawn in March 1980.

For the assessment year 1978-79 the assessee again claimed depreciation on kilns at 20 per cent, showing 10 per cent plus 10 per cent, without mentioning that the depreciation claimed included extra shift allowance. No evidence was available on record to show that the factory worked extra shift. While completing the assessment in September 1981, depreciation at the rate of 20 per cent, as claimed by the assessee on the kilns valued at Rs. 28,26,447 was allowed. Omission to disallow the excess claim of 10 per cent in the light of appellate orders for the assessment year 1975-76 resulted in incorrect allowance of depreciation amounting to Rs. 2,82,665 involving short levy of tax of Rs. 1,63,238.

In the light of appellate orders for assessment year 1975-76, the assessment for the assessment years 1976-77 and 1977-78 would also require revision.

The paragraph was sent to the Ministry of Finance in July 1983; their reply is awaited (December 1983).

(ii) No extra shift allowance for multiple shift is admissible in respect of machinery or plant against which the letters NESA appear in the depreciation schedule in the Income-tax Rules, 1962.

In computing the business income of a private limited company engaged in the production of cinematograph films, for the previous year relevant to the assessment year 1978-79, the assessee's claim for extra shift allowance of Rs. 6,27,343 in respect of certain items of plant and machinery, like sound

recording and editing equipment, was accepted by the department (March 1981). However, no extra shift allowance was admissible for such machinery used in the business of production and exhibition of cinematograph films, since these machineries have been specifically excepted by inscriptions of letters NESA in the depreciation schedule.

The irregular allowance of Rs. 6,27,343 (part of which had been carried forward and set off in the assessment of the following year) resulted in short levy of tax of Rs. 4,38,906 (including an amount of Rs. 43,680 representing interest allowed on advance tax).

The Ministry of Finance have accepted the mistake.

2.19 *Incorrect grant of development rebate*

(i) The development rebate admissible under the provisions of the Income-tax Act, 1961 was abolished with effect from 1 June 1974 by a notification issued by the Central Government in May 1971. However, the Finance Act 1974, by a special provision continued the same in respect of machineries installed after 31 May 1974 but before 1 June 1975 on the condition that the assessee furnished evidence to the satisfaction of the Income Tax Officer, that he had purchased such machinery or plant or had entered into a contract for the purchase of such machinery or plant before 1 December 1973.

On nationalisation of sick textile mills in Gujarat, the mills owned by various companies were taken over by the National Textile Corporation (Gujarat) on 23 November 1974. In the return filed for the assessment year 1975-76 relevant to the previous year ending 31 March 1975, the National Textile Corporation (Gujarat) claimed development rebate to the extent of Rs. 22.55 lakhs in respect of certain items of new plant and machinery installed during the previous year, contracts for the purchase of which, were placed by the erstwhile companies. The claim of the assessee for the above development rebate was admitted by the Income Tax Officer.

Since the assessee, National Textile Corporation, was a new assessee and also the take-over of the former mills by the assessee did not amount to 'amalgamation' as defined in the Income-tax Act, and the assessee himself had not placed the orders for the purchase of machinery or plant before 1 December

1973 (the assessee being not in existence then) the conditions required for the allowance of development rebate in respect of machineries installed after 31 May 1974 were not satisfied. The allowance of development rebate as claimed by the assessee resulted in incorrect carry forward of development rebate to the extent of Rs. 22.55 lakhs for the assessment year 1975-76.

The Ministry of Finance have accepted the mistake February 1983 and have stated that the assessment has been set aside by the Commissioner of Income-tax. Further report is awaited (December 1983).

(ii) The development rebate was admissible at 25 per cent in respect of machinery installed after 31 March 1970 and wholly used for the purpose of construction, manufacture or production of any one or more of the articles or things specified in the list in the Fifth Schedule to the Act. For machinery installed for manufacturing articles not listed in the Fifth Schedule, development rebate was admissible at the rate of fifteen per cent only.

A company manufacturing automobile tyres, commenced a new unit for manufacture of bicycle tyres during the previous year relevant to the assessment year 1974-75. In the assessment for the assessment year 1974-75 done in July 1978, the company was allowed development rebate amounting to Rs. 9,58,154 at the higher rate of twenty five per cent on machinery valued at Rs. 38,32,617 installed in the new unit. As bicycle tyre was not an item listed in the Fifth Schedule, the development rebate at the normal rate of fifteen per cent only was admissible. The incorrect allowance of higher development rebate resulted in under-assessment of income by Rs. 3,83,262 and consequent short levy of tax of Rs. 2,21,334.

Inspite of the assessment records in this case being requisitioned by Audit for examination every year from 1979-80, these were produced to Audit in 1982-83 only. By that time no remedial action was possible because of time bar and the tax short levied became loss of revenue. Had the records been produced to audit in time, in accordance with the repeated instructions issued by the Central Board of Direct Taxes in this regard, the loss of revenue could have been avoided.

The Ministry of Finance have accepted the mistake.

2.20 *Incorrect grant of investment allowance*

(i) Under the provisions of the Income-tax Act, 1961 as applicable for the assessment year 1978-79, while computing the business income of an assessee, a deduction is allowed by way of investment allowance at twenty five per cent of the actual cost of machinery or plant installed in any industrial undertaking after the 31 day of March 1976 for the purpose of business of construction, manufacture or production of any article or thing except those listed in the Eleventh Schedule to the Act. In the case of small scale industry the allowance is admissible even in respect of machinery utilised for the manufacture of any article or thing specified in the Eleventh Schedule.

(a) In the assessment made in September 1981 for the assesment year 1978-79 of a company a deduction by way of investment allowance was allowed for a total sum of Rs. 1,72,616 on Electronic Computers brought into use by the compapny for the manufacture of data processing machines. As 'data processing machine' is one of the items listed in the Eleventh Schedule to the Act and as the assessee was not a small scale manufacturer, the grant of investment allowance was irregular. This irregular allowance resulted in under-assessment of income by Rs. 1,72,616 and a consequent short levy of tax of Rs. 99,684.

The paragraph was sent to the Ministry of Finance in August 1983; their reply is awaited (December 1983).

(b) In the assessment for the assessment year 1978-79, completed in December 1980, an assessee company, whose main source of income was processing job work undertaken for others, was allowed investment allowance of Rs. 2,13,871 on its machinery. As the company was not engaged in any manufacture or production of goods it was not entitled to investment allowance. The incorrect grant of investment allowance resulted in excess carry forward of loss to the extent of Rs. 2,31,871 involving potential tax effect of Rs. 1,34,738.

The Ministry of Finance have accepted the mistake.

(c) In the case of a public limited company while completing assessment for the assessment year 1981-82 in March 1982 investment allowance of Rs. 66,19,637 was allowed in respect of plant and machinery installed during the previous year relevant to the assessment year 1981-82. It was seen in

audit in January 1983 that the actual cost of new machinery installed and put to use during the relevant previous year aggregated to Rs. 2,54,42,051 and the investment allowance admissible was only Rs. 63,69,513 as against Rs. 66,19,637 allowed. The excess allowance of investment allowance amountnig to Rs. 2,50,124 resulted in undercharge of tax of Rs. 1,47,885

The Internal audit party of the department checked the assessment but failed to detect the mistake.

The Ministry of Finance have accepted the mistake.

(ii) Investment allowance equal to twenty five per cent of the actual cost is admissible, as a deduction from business profits, in respect of new plant or machinery installed and used for purpose of business. Actual cost is defined to mean the actual cost of the assets to the assessee reduced by that portion of the cost thereof, if any, as has been met directly or indirectly by any other person or authority.

In the case of a company, investment allowance of Rs. 16,01,884 was allowed on the value of new plant and machinery (Rs. 64,07,538) installed during the previous year relevant to the assessment year 1978-79 (assessment completed on 15 October 1980). The assessee had, during the previous year relevant to assessment year 1979-80 received a capital subsidy of Rs. 8,72,270 from the Central Government in respect of these plant and machinery. In the assessment for the assessment year 1979-80 completed in July 1981 the actual cost of the plant and machinery to the assessee was reduced by the amount of subsidy to workout the depreciation admissible. The assessment for the assessment year 1978-79 was not revised to withdraw the excess investment allowance of Rs. 2,18,067 since the company was entitled to a investment allowance of Rs. 13,83,817 only as against a sum of Rs. 16,01,884 originally allowed. As a result, there was an excess carry forward of investment allowance of Rs. 2,18,067 for the assessment year 1978-79 with a potential tax effect of Rs. 1,25,934.

The Ministry of Finance have accepted the mistake.

(iii) Industrial company as defined in the Finance Act, 1966 means a company which is mainly engaged in the business of generation or distribution of electricity or any other form of power or in the construction of ships or in the manufacture of or processing of goods or in mining.

It has been judicially held (126 ITR 377) that the term industrial company covers a construction company only when it is engaged in the construction of ships. Hence companies engaged mainly or otherwise in the construction of anything other than ships cannot be considered as industrial companies and no investment allowance in respect of plant and machinery installed therein would be admissible.

(a) A company engaged in the construction of dams carrying freight and repairing barges purchased a barge costing Rs. 22,90,680 on 31 January 1977 which was used as a freight carrier in inland waters by another company who paid service charges to the assessee. The assessee claimed and was allowed investment allowance of Rs. 5,72,670 being twenty five per cent of the cost of Rs. 22,90,680 in the assessment year 1978-79 completed in December 1980. Since the assessee was not an industrial undertaking in the light of the above judicial decision the investment allowance was allowed incorrectly. This resulted in under-assessment of income by Rs. 5,72,670 and short levy of tax of Rs. 3,90,847.

While not accepting the mistake, the Ministry of Finance have stated that the assessee is carrying on the business of carrying freight, which involves operation of barge, which is a ship.

Since reunning of ship to carry on the business of freight carriage is not construction of ship within the meaning of industrial company as defined in the Act, the Ministry's reply is not in order and the assessee company, not being an industrial company, is not entitled to grant of investment allowance.

(b) Another company whose activity was that of construction of houses was allowed for the previous years relevant to assessment years 1977-78 to 1979-80 (assessment completed in June 1981 and February 1982) investment allowance of Rs. 59,900, Rs. 69,412 and Rs. 25,183 respectively. In view of the judicial decision, the company not being an industrial company, it was not eligible for investment allowance. The incorrect deductions resulted in underassessment of income by Rs. 1,54,495 and short levy of tax of Rs. 1,05,435 for the three assessment years.

The paragraph was sent to the Ministry of Finance in July 1983; their reply is awaited (December 1983).

(c) For the assessment year 1978-79 (assessment made in July 1981) a private limited company carrying on business of construction of houses was allowed investment allowance of Rs. 3,31,750 treating the company as an industrial company. The company not being an industrial company was not entitled to investment allowance and the incorrect allowance resulted in underassessment of income to the extent of Rs. 3,31,750 involving short levy of tax of Rs. 2,26,418.

The Ministry of Finance have accepted the mistake and have stated that remedial action has been initiated. Further report is awaited (December 1983).

(iv) Investment allowance in respect of new plant or machinery is admissible subject to the condition that an amount equal to seventy five per cent of the allowance is debited to the profit and loss account of the relevant previous year and credited to a reserve account. In the case of income derived from the sale of tea grown and manufactured by the seller in India, the income-tax Rules, 1962 provides that the income shall be computed as if it were income derived from business and forty per cent shall be liable to tax.

A company installed plant and machinery valued at Rs. 16,25,213 in its tea bagging unit during the assessment year 1979-80 and claimed investment allowance of Rs. 4,06,303 thereon which was allowed in full in May 1980 by the department. The assessee, however, created an investment allowance reserve of Rs. 1,22,725 only for this purpose which was a little more than seventy five per cent of forty per cent of the investment allowance. Since the income from tea bagging until was considered as wholly non-agricultural in nature and was assessed to income-tax in its entirety, the investment allowance reserve also was to be created for the full investment allowance. Granting of full investment allowance against creation of inadequate reserve resulted in incorrect allowance of investment allowance of Rs. 2,42,670 with consequent short levy of tax of Rs. 1,40,142.

The Ministry of Finance have accepted the mistake.

2.21 *Incorrect allowance of relief in respect of newly established industrial undertaking*

Under the provisions of the Income-tax Act, 1961, prior to its amendment by the Finance Act, 1980 with effect from the

assessment year 1981-82 where the gross total income of an assessee includes any profits and gains derived from a newly established industrial undertaking which went into production before 1 April 1981, the assessee is entitled to tax relief in respect of such profits and gains upto six per cent per annum (7½ per cent from 1 April 1976) of capital employed in the undertaking in the assessment year in which it began to manufacture or produce articles and also in each of the four succeeding assessment years. Where the profits and gains derived from the industrial undertaking fall short of the relevant amount of capital employed or where there are no profits and gains, the whole or balance of deficiency can be carried forward for adjustment upto the seventh assessment year reckoned from the end of the initial assessment year. The Central Board of Direct Taxes clarified in March 1976 that in determining the profits earned by a new industrial undertaking for the purpose of granting tax holiday relief, no item of expense or other allowance should be allowed as a set off against the profit of any other unit or other heads of income of the assessee and the profits and gains attributable to the new undertaking should be computed as if it is a separate business by itself.

(i) The method of computing capital employed in the industrial undertaking was laid down in the Income-tax Rules, 1962 according to which the capital employed would be the value of assets, on the first day of the computation period of the undertaking, as reduced by moneys and debts owed by the assessee on that day. Accordingly, the capital employed was calculated on the basis of owned capital and reserves only exclusive of borrowed capital.

It was judicially held by the Calcutta High Court in April 1976 (107 ITR 909) that the term capital employed as appearing in the Income-tax Act would include even borrowed capital and that the rule was ultravires of the section in the Act as it could not take away the benefit conferred under the Act. The Madras High Court also held in July 1977 (110 ITR 256) that the exclusion of borrowed capital from the capital employed for the purpose of calculating tax holiday relief through the Income-tax Rules, 1962 amounted to an excessive delegation of legislative power.

To get over the above decisions the Act was amended by the Finance Act, 1980 incorporating the provision of the rule in the Act itself retrospectively from 1 April 1972.

(a) In a case, the capital employed by a company for the assessment year 1976-77 was computed by the Income Tax Officer in September 1979 after deducting the borrowings and debts from the value of assets as laid down in the Income-tax Rules, and a relief of Rs. 10,85,664 was allowed. In appeal, following the Calcutta High Court decision, the Commissioner of Income-tax (Appeals) ordered in February 1980 that the borrowings and debts should not be deducted in the computation of capital employed in the new units. The assessment for the assessment year 1976-77 was accordingly revised in April 1980 and an aggregate relief of Rs. 12,35,984 was allowed computing the capital employed without deducting the borrowed money and debts from the value of the assets. The assessment was not revised to re-calculate the capital employed on retrospective amendment of the Act with effect from 1 April 1972. As a result, there was excess relief of Rs. 1,50,320 with consequent short levy of tax of Rs. 86,810 for the assessment year 1976-77.

The Ministry of Finance have accepted the mistake and have reported that remedial action has been initiated. Further report is awaited (December 1983).

(b) A tax holiday relief of Rs. 3,65,984 was allowed to another company for the assessment year 1975-76 in respect of a newly established undertaking of the company. In the computation of capital, liabilities and debts owed by the assessee company were not reduced. After deducting liabilities of Rs. 46,89,890 from the value of assets of Rs. 51,64,184 the capital employed in the new undertaking for the assessment year 1975-76, actually worked out to Rs. 4,74,294 on which tax holiday relief calculated at 6 per cent, worked out to Rs. 28,458 only as against relief of Rs. 3,65,984 allowed. The assessment was required to be revised to withdraw the excess relief on tax holiday consequent upon the retrospective amendment of the Act. This was, however, not done. Failure to revise the assessment resulted in excess deduction of Rs. 3,37,526 on account of tax holiday involving short levy of tax of Rs. 2,30,354.

The Ministry of Finance have reported that the deduction of 6 per cent capital base including borrowed funds was allowed as per directions of Income-tax Appellate Tribunal and the Income-tax Officer had moved an application in May 1983 requesting the

Appellate Tribunal to revise their orders in the light of retrospective amendment to the Section. Further report is awaited (December 1983).

(ii) In the assessment of a company for the assessment year 1978-79, made in September 1982, while determining the capital employed in the new industrial undertaking, the Income Tax Officer took the value of depreciable assets at the value shown in the balance-sheet as on the first day of the computation period instead of adopting their written down value as per income-tax assessment. This resulted in excess computation of capital of Rs. 20,47,586 and excess allowance of relief of Rs. 1,53,569 with consequent undercharge of tax of Rs. 88,686 in the assessment year 1978-79.

The Ministry of Finance have accepted the mistake.

(iii) An industrial company which had employed on the 1st day of the computation period, capital of Rs. 18,66,481 claimed deduction of Rs. 2,42,222 for the assessment year 1980-81 in respect of profits and gains from a newly established industrial undertaking. While completing the assessment in January 1981 the Income Tax Officer allowed the deduction as claimed, although the deduction admissible at 7½ per cent of the capital employed worked out to Rs. 1,39,985 only. As a result there was an under-assessment of income of Rs. 1,02,240 involving short levy of tax of Rs. 65,944.

The Ministry of Finance have accepted the mistake and have stated that remedial action was taken in September 1982 raising additional demand of Rs. 65,944. Further report is awaited (December 1983).

(iv) In the case of a statutory corporation deriving profits and gains from marketing and other business activities and from running of seven industrial undertakings, the total income for the assessment year 1979-80 was computed at Rs. 1,50,270 in February 1982 after allowing deduction of Rs. 2,47,008 on account of tax holiday. It was noticed in audit (September 1982) that two of the undertakings only, had returned a profit of Rs. 58,458 and remaining five units had no profits or gains during the relevant previous year. In computing the total income for the year, the amounts of deduction in respect of the two units returning profits was to be restricted to Rs. 58,458 only and the deficiency of Rs. 51,382 in their case and the

deficiency of Rs. 1,37,168 relating to the remaining five units, were to be carried forward for adjustment against the profits and gains of the respective units in the subsequent years. Incorrect adjustment of Rs. 1,88,550 resulted in short computation of income for the assessment year 1979-80 leading to under assessment of tax of Rs. 1,08,888.

The Ministry of Finance have accepted the mistake.

2.22 *Incorrect deduction in respect of inter-corporate dividends*

Under the Income-tax Act, 1961, in the case of a domestic company, where the gross total income includes any income by way of dividends from another domestic company, there shall be allowed in computing the total income, a deduction at a specified percentage of such income. The Act was, amended through the Finance Act, (No. 2) 1980 with retrospective effect from 1 April 1968 to provide that the deduction on account of inter-corporate dividends is to be allowed with reference to the net dividend income as computed in accordance with the provisions of the Act and not on the gross amount of the dividend.

(i) During the previous year relevant to the assessment year 1980-81, a private limited company received a total income of Rs. 3,61,500 by way of dividends from domestic companies in which it had invested borrowed funds. The assessee company, in its accounts for the relevant previous year, had debited administrative expenses of Rs. 997 and payment of interest Rs. 1,34,108. While completing the assessment in August 1981, after the amended provisions had come into force, the department erroneously allowed the deduction with reference to the gross amount of dividend income of Rs. 3,61,500 instead of on the net amount of Rs. 2,26,395. The mistake resulted in under-assessment of income by Rs. 81,067 and consequent short levy of tax of Rs. 56,644.

The assessment was checked by the special Audit Party of the department but the mistake was not detected by it.

The Ministry of Finance have accepted the mistake.

(ii) In the case of another private company for the assessment year 1977-78, a sum of Rs. 1.97,898 was treated by the department as expenses incurred for earning dividend income. It was, however, noticed in audit in August 1982 that in the assessment made in March 1979 the said expenditure was

not reduced from the dividend income. As a result, deduction on account of inter-corporate dividend was allowed on the gross dividend and not on net dividend. The mistake resulted in excess allowance of deduction of Rs. 1,18,740 with consequent tax undercharge of Rs. 81,040.

While accepting the mistake, the Ministry of Finance have reported in September 1983 that the assessment has been rectified in March 1983.

(iii) In the assessment of a domestic company for the assessment year 1980-81 (assessment completed in April 1980) the relief on account of inter-corporate dividend was arrived at Rs. 3,99,900 calculated at 60 per cent of the gross dividend of Rs. 6,66,500 and the deduction was limited to Rs. 3,53,235 with reference to the total income. After allowing a sum of Rs. 3,08,487 being expenditure incurred in connection with dividend income the net dividend income was Rs. 3,58,013 and the deduction admissible on the net dividend worked out to Rs. 2,14,807. The mistake resulted in an under-assessment of income of Rs. 1,38,428 with consequent excess refund of Rs. 81,845.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(iv) The income of an investment company from dividends, interest on securities and property was treated as business income of the company. Ninety per cent of the company's receipts were by way of dividends. For the assessment years 1979-80 and 1980-81 (assessments completed in January 1982) the deduction on account of inter-corporate dividends was computed by the department with reference to gross dividend income instead of the net amount after reducing the expenses from the gross figure. The deductions thus allowed for the assessment years 1979-80 and 1980-81 were Rs. 13,86,950 and Rs. 17,22,567 as against Rs. 6,80,088 and Rs. 10,57,288 respectively allowable on net dividend income. The excess deductions resulted in under-assessment of income to the tune of Rs. 7,06,862 and Rs. 6,65,279 with consequent short levy of tax of Rs. 9,47,293 for the assessment year 1979-80 and 1980-81.

The Ministry of Finance have accepted the mistake. Further report regarding rectification and raising of demand is awaited (December 1983).

2.23 *Mistakes in the grant of export markets development allowance*

The Income-tax Act, 1961 as it stood prior to its amendment by the Finance Act, 1983 provided for an export markets development allowance to resident assessees engaged in the business of export of goods outside India or in providing services or facilities outside India. A domestic company was entitled to a deduction on account of this allowance from the income assessed under the head 'Profits and gains of business or profession', at one and one third times the qualifying expenditure as prescribed in the Act. Widely held domestic companies were entitled to the deduction at one and one half times the qualifying expenditure incurred during the period from 1 March 1973 to 31 March 1978.

(i) Expenditure incurred in India in connection with distribution, supply or provision of goods and expenditure (wherever incurred) on the carriage of goods to their destination outside India were specifically excluded from the benefit of the weighted deduction.

(a) In the assessment of a company for the assessment year 1976-77 completed by an Inspecting Assistant Commissioner (Assessment) in September 1979 and revised in November 1980 an expenditure of Rs. 4,31,635 incurred by the company in India in connection with distribution, supply or provision of goods and on the carriage of goods to their destination outside India was allowed as deduction. In the assessment for the next assessment year 1977-78 completed in March 1980 by the Inspecting Assistant Commissioner (Assessment) an expenditure of Rs. 1,60,271 incurred in India on account of commission paid to Indian agents on export sales was wrongly allowed as deduction towards export market development allowance. These mistakes resulted in the total under assessment of business income by Rs. 2,95,953 with consequent under charge of tax of Rs. 1,70,913 in the two assessment years 1976-77 and 1977-78.

The assessments were checked by the Internal audit party of the department but the mistakes were not detected by it.

The paragraph was sent to the Ministry of Finance in June 1983; their reply is awaited (December 1983).

(b) A private limited company incurred an expenditure of Rs. 27,64,722 in India on commission, insurance, premium to Export Credit Guarantee Corporation, packing and forwarding charges and interest during the assessment years 1977-78 to 1979-80 and claimed weighted deduction of Rs. 9,21,574 thereon on account of export market developments allowance. In the assessments completed in May and October 1978 and August 1979, the assessing officer allowed the deduction as claimed by the assessee company. Since the expenditure was incurred in India, the assessee was not entitled to weighted deduction. The erroneous deduction resulted in under assessment of income by Rs. 9,21,574 with a short-levy of tax of Rs. 5,80,990.

The Ministry of Finance have accepted the mistake.

(ii) Expenditure incurred after 31 March 1978, was not entitled to the weighted deduction unless the domestic company was engaged in the provision of technical know-how or the rendering of services in connection with the provision of know-how to persons outside India.

(a) A private limited company engaged in broking reinsurance business between ceding companies and reinsurance companies from all over the world received commission in India and outside India for arranging such business The company claimed for the previous year relevant to the assessment year 1979-80 weighted deduction of Rs. 7,36,259 on the ground that business of broking of reinsurance amounted to provision of technical know-how to foreign companies. This as well as another amount of Rs. 2,46,531 as per an appellate order of March 1982 were allowed by the department in August 1981 and April 1982. It was noticed in audit in August 1982 that no technical know-how to persons outside India was provided by the company so as to be entitled for export markets development allowance as the company only did reinsurance business making use of the expertise in its own possession for which service it earned commission. The allowance of weighted deduction of Rs. 9,82,790 was not, therefore, in order. The incorrect allowance resulted in under assessment of income by similar amount and short levy of tax of Rs. 6,70,753. Short levy also entailed under charge of interest of Rs. 48,727 for failure to file mandatory estimate of advance tax and incorrect grant of interest of Rs. 48,577 by the department on excess payment of advance tax.

The Ministry of Finance have accepted the mistake in principle.

(b) A private limited company assessed in another charge was allowed a weighted deduction of Rs. 1,58,152 for the assessment year 1979-80 in January 1982. The company was merely rendering services like marine and cargo survey etc. to ships calling at Indian ports which could not be called business of provision of technical know-how. Although the expenditure was incurred after 31 March 1978 the services were rendered in Indian ports only, and no technical know-how was provided to persons abroad. The company was not, therefore, entitled to the weighted deduction allowed by the department. The incorrect allowance resulted in under assessment of income by Rs. 1,58,152 leading to a short levy of tax of Rs. 1,07,927.

The Ministry of Finance have accepted the mistake.

(iii) Expenditure incurred on the maintenance, outside India, of a branch, office or agency for the promotion of sale outside India of goods, services or facilities in connection with the development of export markets qualified for weighted deductions.

In the assessment of a shipping company, for the assessment year 1977-78, completed in September 1980, a weighted deduction of Rs. 5,41,18,565 was allowed on an expenditure of Rs. 3,60,79,043 on account of commission on inward and outward freight and brokerage paid to its agents in foreign ports. The payments made outside India were not towards expenditure incurred on the maintenance of an office or a branch outside the country. In fact the department had itself disallowed similar expenditure earlier in the case of a public sector shipping company on the ground that brokerage had been paid in the normal course of business and had nothing to do with sales promotion. The mistake in granting excess allowance resulted in short-levy of tax of Rs. 1,04,17,823.

The paragraph was sent to the Ministry of Finance in May 1983; their reply is awaited (December 1983).

(iv) A company was assessed for the assessment year 1978-79 in September 1981 on a total income of Rs. 4,27,33,600 and the tax liability was determined at Rs 2,46,76,654.

It was noticed in audit that the company had intimated in March 1981 that a sum of Rs. 4,00,000 was received back by it out of the export expenses of Rs. 6,39,735 incurred by it and charged to the profit and loss account during the relevant previous year. The department, however, allowed deduction of expenditure of Rs. 6,39,735 in full and also allowed export markets development allowance on it instead of on Rs. 2,39,735. This led to under-assessment of income by Rs. 4,00,000 and excess allowance of export markets development allowance by Rs. 1,00,000 and resulted in total under-assessment of income by Rs. 5,00,000 with consequent undercharge of tax of Rs. 3,73,250 (including surtax of Rs. 84,500) in the assessment year 1978-79.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(v) In the case of a closely held company, a hundred per cent subsidiary of a non-resident company, deduction towards expenditure on export markets development was allowed at one and half times instead of at one and one third times for the assessment year 1978-79. In the return of income the company itself had indicated that it was not a company in which the public were substantially interested. Nevertheless while completing the assessment for the assessment year 1978-79 in July 1981 the department allowed a deduction of Rs. 3,48,187 as against the correct amount of Rs. 2,32,125. The excess allowance of deduction resulted in under-assessment of income by Rs. 1,16,062 and short levy of tax of Rs. 67,025. In respect of earlier assessment years 1976-77 and 1977-78 also there was similar excess allowance of Rs. 37,112 involving short levy of tax of Rs. 21,430.

The total short levy for the three assessment years was Rs. 88,455.

The paragraph was sent to the Ministry of Finance in August 1983; their reply is awaited (Dectmber 1983).

2.24 *Incorrect deduction in respect of donation*

Under the Income-tax Act, 1961 in computing the total income of an assessee there shall be deducted from the gross total income an amount equal to 50 per cent of sums paid by the assessee as donations made in the previous year to the funds specified in the Act.

In the assessment of a Corporation set up by a State Government for the assessment year 1976-77, completed in December 1978, on a total income of Rs. 18,42,110, a deduction of Rs. 1,00,000 was allowed in respect of donation of Rs. 2,00,000 paid to the Chief Ministers' Relief Fund. As the assessee, had not produced any receipt in support of the payment, it was pointed out in audit in November 1980 that the receipt should be obtained and kept in the assessment records.

On investigation at the instance of Audit the Income Tax Officer found that the assessee had not actually made the payment to the Fund during the previous year relevant to the assessment year 1976-77 and accordingly submitted proposals to the Commissioner of Income-tax in April 1983, for reopening the assessment. The incorrect deduction allowed to the assessee resulted in underassessment of income by Rs. 1,00,000 with tax undercharge of Rs. 74,550 including surtax.

The Ministry of Finance have accepted the mistake and have stated that remedial action has been taken. Further report is awaited (December 1983).

2.25 *Other incorrect deductions*

(i) Under the Income-tax Act, 1961, where the gross total income of an Indian company includes income by way of royalty, fees or any similar payment received by the company from a foreign enterprise in consideration for technical services rendered outside India to the foreign enterprise, under an agreement approved by the Board, and such income is received in convertible foreign exchange in India, a deduction of the whole of such income shall be allowed in computing the income of the company. The expenditure incurred in connection with this business is consequently not deductible from the income of other business activities of the assessee company.

An Indian company, engaged in the execution of contracts in India undertook a contract in Dubai. The Central Board of Direct Taxes gave its approval in December 1976 allowing deduction of the whole of the income from the foreign contract from the gross total income of the assessee. The assessee wanted to arrive at the profits and gains of the foreign contract only on completion of the same and the position was accepted by the department. In the assessment year 1978-79, the foreign contract being incomplete, receipts and expenditure on it were

excluded from the profit and loss account and profits from Indian contracts only were subjected to taxation. However, while completing the assessment of this year in September 1981 (revised in March 1982) revenue expenditure of Rs. 43,38,608 export market development allowance amounting to Rs. 22,28,420 and depreciation allowance of Rs. 3,34,728 were allowed against the taxable Indian income although these deductions related to the foreign contracts. The incorrect allowance of deductions, reduced the taxable profits from Indian contracts and resulted in under-assessment of income by Rs. 69,01,756 and undercharge of tax of Rs. 51,52,160 (including surtax of Rs. 11,66,397) for the assessment year 1978-79.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(ii) Under the Incomt-tax Act, 1961 where in the case of an assessee the gross total income of the previous year includes any profits and gains derived from a business carried on in India of printing and publication of books or publication of books, there shall be allowed in computing the total income of the assessee, a deduction from such profits and gains of an amount equal to twenty per cent thereof.

In the case of a Government company deriving income from printing and publication of books, the Inspecting Assistant Commissioner (Assessment) while completing the assessment for the assessment year 1979-80 in September 1981 incorrectly allowed deductions calculated on the basis of figures incorporated in "estimated profit and loss account" instead of in profit and loss account. There was excess allowance of relief of Rs. 1,11,901 with undercharge of tax of Rs. 1,28,563 including interest for belated filing of return of income and short payment of advance tax and surtax during the assessment year 1979-80.

The Ministry of Finance have accepted the mistake.

2.26 *Income escaping assessment*

(i) The Income-tax Act, 1961 provides for an allowance of deduction from the income of an assessee in respect of any expenditure or trading liability incurred for the purpose of business carried on by the assessee. Where, on a subsequent date, the assessee obtains any benefit in respect of such expenditure or trading liability allowed earlier, by way of remission or cessation thereof, the benefit that accrues thereby,

shall be deemed to be profits and gains of business or profession to be charged to income-tax as income of the previous year in which such remission or cessation takes place.

(a) In the case of a company, a sum of Rs. 29,65,958 representing 'provisions for royalty on spares' was claimed as trading liability for the assessment years 1966-67 to 1971-72 and it was allowed by the Income Tax Officer in computing the business profits in the respective assessment years. Subsequently in the previous year ending 31 October 1974 relevant to the assessment year 1975-76, the assessee credited the income-account with the sum as the liability did not exist and also requested the department in October 1974 to add back the amount while computing income. However, in the assessment for the assessment year 1975-76 (assessment made in August 1979) the Income Tax Officer did not bring the sum to tax.

Non-addition of the amount of Rs. 29,65,958 in the assessment year 1975-76 resulted in income escaping assessment involving short levy of tax of Rs. 17,12,840.

The Ministry of Finance have accepted the omission.

(b) In the previous year relevant to the assessment year 1978-79, an amount of Rs. 3,73,216 representing provision for bonus made in the assessment year 1972-73 was written back by a company. While completing the assessment in August 1981, the assessing officer did not add this amount to the income of the company. Omission to add back the amount of Rs. 3,73,216 resulted in short levy of tax of Rs. 2,35,126.

The Ministry of Finance have accepted the mistake in principle. Report regarding collection of additional demand is awaited (December 1983).

(c) In the case of a public limited company, deduction in respect of provision for gratuity was allowed in the assessment years 1973-74 to 1975-76. In the accounting period relevant to the assessment year 1976-77, a sum of Rs. 2,08,615 representing excess provision for gratuity made in earlier assessment years, referred to above, was written back and transferred to general reserve. It was seen in audit in September 1981, that while completing the assessment in March 1979, the Inspecting Assistant Commissioner (Assessment) did not add

back that sum to the income for levy of tax. The omission resulted in the income of Rs. 2,08,615 escaping assessment involving short levy of tax of Rs. 1,20,470.

The paragraph was sent to the Ministry of Finance in August 1983; their reply is awaited (December 1983).

(d) Another company wrote back in its accounts for the year relevant to the assessment year 1978-79 a sum of Rs. 6,40,082 on account of excess liability provided in the earlier years. As the liability had been allowed in earlier assessments, the sum of Rs. 6,40,082 was required to be treated as income and charged to tax in the assessment year 1978-79. As this was not done, there was escapement of income of Rs. 6,40,082 leading to excess carry forward of loss by the same amount in the assessment year 1978-79.

The Ministry of Finance have accepted the mistake.

(e) In the case of a company a sum of Rs. 17,20,614 was capitalised in 1967 on account of extra liability for payment in foreign currency to a foreign supplier of plant and machinery due to devaluation of Indian currency. The said provision was considered as no longer required in the assessment year 1977-78 and was adjusted against the original cost of plant and machinery. Accordingly, the amount of total depreciation of Rs. 14,80,342 allowed in earlier assessments on the capitalised sum of Rs. 17,20,614 was required to be treated as income chargeable to tax in the assessment year 1977-78. Against this a sum of Rs. 10,51,461 only was credited by the assessee company in the profit and loss account for the period relevant to the assessment year 1977-78 and the Income Tax Officer also considered only this amount as income in the assessment made in May 1980 for the assessment year 1977-78 without making separate adjustment for treating the excess depreciation as income. As a result, income of Rs. 4,28,881 escaped assessment in the assessment year 1977-78, leading to excess carry forward of loss by the same amount.

The paragraph was sent to the Ministry of Finance in September 1983 ; their reply is awaited (December 1983).

(f) A company made a provision of Rs. 4,63,000 on account of turnover discount in the calendar year 1974 relevant to the assessment year 1975-76 and the same was allowed as expenditure in that year. The company credited to its profit

and loss appropriation account in the calendar year 1976 relevant to the assessment year 1977-78 an amount of Rs. 4,55,390 towards excess provision made in 1974 owing to the scheme having not become operative. However, while completing the assessment for the assessment year 1977-78 in September 1980 the write back of the amount of Rs. 4,55,390 was not assessed as income. The omission resulted in the income of Rs. 4,55,390 escaping assessment with a potential short levy of tax of Rs. 2,62,987.

The Ministry of Finance have accepted the mistake and have stated that the assessment has been rectified in December 1982, reducing the loss.

(g) A private limited company received sums of Rs. 33,241 and Rs. 1,09,715 being refunds of central excise duty paid and sales tax set-off during the previous years relevant to assessment years 1979-80 and 1980-81 respectively. In computing the total income of the company in July 1981 and January 1982 respectively these amounts were not considered. Their non-inclusion resulted in escapement of income of Rs. 1,42,956 for the two years with a short levy of tax of Rs. 91,707.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(ii) The assessment of a private limited company engaged in the manufacture and sale of television sets and components, for the assessment year 1980-81 (previous year ending 30 June 1979) was completed on 30 March 1982 determining a taxable income of Rs. 18,73,810. While computing the income, an amount of Rs. 1.14 lakhs was allowed as interest on the loan amounting to Rs. 7.84 lakhs taken by the assessee against fixed deposits of Rs. 12 lakhs held for sixty one months in various scheduled banks. Even though the interest on loan taken against the fixed deposits was allowed as expenditure, the interest due on the fixed deposits was not considered as income. Adopting the rate of interest at ten per cent per annum, the interest income that escaped assessment was Rs. 1.20 lakhs and the additional tax leviable was Rs. 83,400.

The Ministry of Finance have accepted the mistake.

(iii) The assessments of a company for the assessment years 1979-80 and 1980-81 were completed in a Central Circle in September 1981 and November 1981 respectively at a loss of

Rs. 2,93,079 for the assessment year 1979-80 and at nil amount for the assessment year 1980-81. During the previous years relevant to these assessment years, the assessee company had received sums of Rs. 1,65,900 and Rs. 1,95,100 respectively being power subsidy granted by the State Government of West Bengal through the West Bengal Industrial Development Corporation. It was noticed in audit in October 1982 that instead of crediting the amounts of subsidy to the profit and loss accounts and treating them as income the assessee company had credited them to the general reserve. The assessing officer did not consider the receipts as income in the respective assessments of the company. The omission resulted in the income escaping assessment and in excess carry forward of loss of Rs. 3,61,000 for the two assessment years.

The Ministry of Finance have accepted the omission.

2.27 *Mistakes in making provisional assessments*

The Income-tax Act, 1961, provides that, where an assessee files a return of income claiming that the advance tax paid and the tax deducted at source exceed the tax payable on the basis of the return of income filed by him, the Income Tax Officer should make, in a summary manner, a provisional assessment, to refund the excess tax paid by the assessee, if the regular assessment is not likely to be made within six months from the date of furnishing of the return. In making such assessment, the Income Tax Officer shall disallow any deduction, allowance or relief claimed in the return which is on the basis of information available in the return or accounts etc. is *prima facie* inadmissible. The Income Tax Officer shall also give effect, *inter alia*, to any loss carried forward from the earlier years. However, the amounts to be so adjusted should be only those computed in regular assessments of earlier years.

(i) In the case of a company, the Income-Tax Officer made a provisional assessment for the assessment year 1980-81 on 28 November 1980 based on the returned income of Rs. 11,91,38,980 and allowed a refund of Rs. 4,20,43,110 on the same date. It was seen in audit (26 February 1983) that while arriving at the returned income of Rs. 11,91,38,980 the assessee had erroneously deducted a sum of Rs. 8,76,622, re-

presenting inadmissible expenditure instead of adding it to the book profit. The error resulted in an excess refund of Rs. 10,36,605.

On this being pointed out (February 1983) the Income Tax Officer contended that the assessee had noticed the mistake and filed a revised return (10 February 1983) and that the income would not escape assessment. The fact remained that the Income Tax Officer had made an excessive refund of Rs. 10,36,605 due to his omission to rectify the arithmetical error, as required in law, and the error had also remained unrectified (for more than two years), as the regular assessment had not been completed till the date of audit. Also, the revised return, stated to have been filed by the assessee was not produced, when the file was made available to audit. The file had also not been produced to earlier audit in 1981-82.

The Ministry of Finance have accepted the mistake.

(ii) In the provisional assessment of a company for the assessment year 1980-81 made in September 1981 the assessee's claim for set off of Rs. 1,10,35,602, being deficiency for the assessment years 1978-79 and 1979-80 in respect of a newly established business, was allowed. Actually a deficiency of Rs. 76,57,483 only had been determined in the regular assessment for the assessment year 1978-79 on 24 March 1981 (regular assessment for the assessment year 1979-80 not having been made) and adjustment to that extent only was admissible in the calculation of income in provisional assessment for the assessment year 1980-81. The incorrect adjustment of Rs. 1,10,35,602 instead of Rs. 76,57,843 resulted in excess allowance of Rs. 33,78,119 involving excess refund of Rs. 19,50,862.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

2.28 *Excess refund*

In the assessment of a non-resident company for the assessment year 1977-78 the assessee's claim for a sum of Rs. 1,01,970 on account of tax deducted at source on dividends, was disallowed (August 1980) for want of the necessary tax deduction certificate. However, in a revision made in November 1980, in

compliance with an appellate order, this claim was allowed. The amount was, however, incorrectly taken as Rs. 1,10,970. In May 1981, the assessee informed the department that the original tax deduction certificate was not available and filed an indemnity bond instead. At this stage (June 1981), the department again gave credit to the assessee for a sum of Rs. 1,01,970 by reducing the arrears due for the assessment year 1965-66 resulting in double credit of the amount of Rs. 1,10,970.

While accepting the mistake the Ministry of Finance have stated that the assessment has been rectified in December 1982 and additional demand of Rs. 1,10,970 has been collected.

2.29 *Incorrect set off of loss*

(i) Under the Income-tax Act, 1961, any loss computed in respect of a speculation business can be set off only against profits and gains if any, of another speculation business. The Act further provides that where any part of the business of a company (other than an investment or a banking or a financial company) consists in the purchase and sale of shares of other companies, such company shall be deemed to be carrying on a speculation business to the extent to which the business consists of purchase and sale of such shares.

(a) During the assessment year 1980-81 an assessee company suffered a loss of Rs. 3,04,039 on purchase and sale of shares. The loss was adjusted by the department against non-speculative business income while finalising the assessment of the company in March 1981. It was noticed in audit that the assessee was not an investment, banking or financial company inasmuch as its business income included in the gross total income constituted more than 51 per cent of its total income. Consequently, the loss of Rs. 3,04,039 incurred on sale of shares was required to be treated as a speculation loss not eligible for set-off against other non-speculative income of the company. The incorrect set off of loss resulted in under assessment of total income by Rs. 3,04,039 with consequent under charge of tax of Rs. 1,79,763.

The Ministry of Finance have intimated that the Commissioner of Income-tax has set aside the assessment directing further examination as to the status of the company. Further report is awaited (December 1983).

(b) A company, *inter alia,* engaged in the business of manufacture of tea and exports, incurred a loss of Rs. 1,37,345 in share dealing transactions during the previous year relevant to the assessment year 1977-78. As the assessee was not an investment, banking or financial company, the loss of Rs. 1,37,345 arising out of share dealing business constructed a loss arising from speculation business which could only be set off against the income from another speculation business. The department, while completing the assessment in September 1980 for the assessment year 1977-78, set off the loss of Rs. 1,37,345 against non-speculative income of the assessee company. The irregular set off of the speculation loss resulted in under-assessment of income by Rs. 1,37,345 with undercharge of tax of Rs. 84,076 including short levy of interest amounting to Rs. 4,759 for late filing of return for the assessment year 1977-78.

The Ministry of Finance have accepted the mistake.

(ii) The Income-tax Act, 1961 provides that where in respect of any assessment year the net result of computation under the head "Capital gains" is a loss from long-term capital assets such loss shall be carried forward to the following assessment years and set off against capital gains relating to long term capital assets for those assessment years. Such loss cannot be adjusted against any other head of income.

In the case of a private limited company, for the assessment year 1978-79 (assessment done in March 1979) a sum of Rs. 1,12,050 was allowed as "short term capital loss" on the sale of shares of another company. The shares were actually held by the assessee company for more than 36 months prior to their sale. Hence the loss from the sale of these shares was of the nature of long-term capital loss and was not admissible to be set off against the income under any other head for the above assessment year. The incorrect set off of loss resulted in excess computation of loss to the extent of Rs. 1,12,050 with a potential tax effect of Rs. 76,474.

The Ministry of Finance have accepted and rectified the mistake in September 1981.

(iii) The assessment of a public company for the assessment year 1973-74 was revised on 13 October 1980 and the carried

forward loss was determined as Rs. 3,37,072. The assessment for the assessment year 1974-75 was consequently revised on the same date and after allowing a set off of Rs. 3,37,072 towards carried forward business loss of earlier years, the total income for the assessment year 1974-75 was determined as Rs. 54,14,401. However, it was noticed in audit (February 1983) that in the rectificatory order passed for the assessment year 1974-75 on 31 March 1977 an amount of Rs. 1,53,528 had already been set off towards carried forward loss of the assessment year 1973-74 and the balance loss amounting to Rs. 1,83,544 only was required to be set off in the revision made on 13 October 1980 for the assessment year 1974-75. The incorrect adjustment resulted in under assessment of income by Rs. 1,53,528 for the assessment year 1974-75 with consequential short-levy of tax Rs. 1,07,926 including surtax of Rs. 19,264.

The Ministry of Finance have accepted the mistake and have reported that the assessment has been rectified raising additional demand of Rs. 88,664. Further report regarding action taken for the balance demand is awaited (December 1983).

2.30 *Mistakes in assessment while giving effect to appellate orders*

(i) A private limited company engaged in the business of bottling soft drinks was claiming breakages in bottles and shells as business expenditure in the computation of its business income upto the previous year ending 30 June 1974 relevant to the assessment year 1975-76. From the assessment year 1976-77 onwards, the company claimed instead, the actual expenditure on the purchase of bottles and shells during the previous year. For the assessment year 1977-78, the assessee claimed deductions of Rs. 4,55,934 on account of purchase of bottles during the year and Rs. 1,72,554 on account of breakages of bottles purchased prior to 30 June 1974.

While completing the assessment for the assessment year 1977-78 in February 1980, the Income Tax Officer allowed only the breakages valuing Rs. 1,72,554 and disallowed the other claim. On an appeal by the assessee, the Commissioner of Income-tax (Appeals) in his order of February 1981 directed that full cost of stock of bottles and shells be allowed as business expenditure and also the breakages in respect of those on hand on 30 June 1974.

While giving effect to the appellate orders in May 1981, the full value of purchases amounting to Rs. 4,55,934 and breakages upto 30 June 1974 at Rs. 1,19,432 was allowed by the Income Tax Officer without taking into account the deduction of Rs. 1,72,554 already allowed in the original assessment made in February 1980. This resulted in excess deduction of expenditure of Rs. 1,72,554 involving excess refund of tax of Rs. 1,03,531.

The Ministry of Finance have accepted the mistake and have stated that the assessment in question has been rectified in April 1983 raising additional demand of Rs. 1,03,531. Report regarding collection of additional demand is awaited (December 1983).

(ii) A public sector corporation claimed a deduction of Rs. 3,25,876 on account of rent in its income-tax return for the assessment year 1976-77. While completing the assessment in March 1979, the Inspecting Assistant Commissioner (Assessment) allowed Rs. 1,95,317 only towards rent, and disallowed a sum of Rs. 1,30,559 on the ground that it represented advance payment of rent. This amount of Rs. 1,30,559 was allowed by the assessing officer in the assessment for the assessment year 1977-78 completed in February 1980.

The assessee corporation went in appeal against the Inspecting Assistant Commissioner's orders for the assessment year 1976-77. In his order of August 1980 the Commissioner of Income-tax (Appeals) allowed the balance of rent of Rs. 1,30,559 in the assessment year 1976-77 itself. While giving effect to the Commissioner of Income-tax's orders in September 1980, the Inspecting Assistant Commissioner (Assessment) did not withdraw the allowance of Rs. 1,30,559 made in the assessment year 1977-78. Failure to do so resulted in double deduction of Rs. 1,30,559 involving short-levy of tax of Rs. 1,01,034 including interest for failure to file estimate of advance tax.

While accepting the mistake, the Ministry of Finance have stated that the assessment has been rectified in December 1981 and the additional-tax raised has been adjusted against the refund.

(iii) The claim of a company for Rs. 4,51,021 towards additional sales-tax liability during the assessment year 1975-76 was rejected by the assessing officer while making the assessment in October 1976. On appeal, the Income-tax Appellate

Tribunal (October 1978) held that the liability might be allowed in the assessment year 1976-77 after verifying the actual amount thereof. In the meantime the sales-tax demand of Rs. 4,51,021 was reduced by the sales-tax department to Rs. 1,42,295 as per the orders of the Commercial Taxes Tribunal in July 1975.

While giving effect to the orders of the Tribunal the assessing officer allowed in August 1979 a deduction of Rs. 4,51,021 in the assessment year 1976-77 without verifying the actual liability as directed by the Tribunal. This resulted in excess allowance of sales-tax liability to the extent of Rs. 3,08,726 in the assessment year 1976-77. As the assessment for the assessment year 1976-77, was completed on a loss of R. 2,93,001 the mistake led to under assessment of income by Rs. 15,725 for the assessment year 1976-77 and Rs. 2,93,001 for the assessment year 1977-78. Consequently there was short-levy of tax of Rs. 2,01,164 for the two assessment years 1976-77 and 1977-78.

The Ministry of Finance have accepted the mistake and have reported that the assessments have been rectified in October 1982 raising additional demand of Rs. 2,01,164 which has been collected.

(iv) Under the Income-tax Act, 1961, as amended by the Finance (No. 2) Act 1967 with effect from 1 April 1967, where the assessee had acquired any capital asset from a country outside India for the purpose of his business or profession on deferred payment terms or against a foreign loan before 6 June 1966, the additional rupee liability incurred by him in meeting the cost of the asset is allowed to be added to the original cost of the asset for the purposes of calculating depreciation allowance in computing the profits for the assessment year 1967-68 and subsequent years.

Pursuant to the order of Appellate Tribunal, the assessment of a company for the assessment year 1974-75 was revised in February 1981. The company suffered a loss of Rs. 7,61,389 on actual remittance of foreign loan due to fluctuation in exchange rates in the assessment year 1974-75. The Appellate Tribunal held that the said exchange loss was allowable as revenue expenditure but in case the assessee had got any benefit in the past due to fluctuation in the rate of exchange due to devaluation of rupee in June 1966 the assessee would not be entitled to the

benefits again as that would amount to double benefit. Accordingly, the assessment for the assessment year 1974-75 was revised in February 1981 and the actual remittance loss of Rs. 7,61,389 was allowed.

It was noticed in audit (August 1982) that for the assessment years 1972-73 and 1973-74, the assessee had been allowed a notional loss of Rs. 3,48,113 which was required to be withdrawn to prevent the double allowance. While giving effect to the appellate orders a notional loss of Rs. 2,28,712 only was withdrawn, as against a sum of Rs. 3,48,113 resulting in short withdrawal of loss of Rs. 1,19,401 in the assessment year 1974-75. This led to underassesment of business income by the same amount with resultant tax undercharge of Rs. 84,089 including surtax of Rs. 15,134.

The paragraphp was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(v) In its accounts for the assessment year 1978-79 a company showed a notional profit of Rs. 9,27,239 arising out of revaluation of foreign loan balance at the close of the year due to fluctuation in the rate of exchange. In the return of income for this year the assessee did not include this sum in the total income stating that the claim of such notional loss arising in the assessment year 1972-73 had been disallowed by the Income Tax Officer in the assessment for that year and that if the disallowed notional loss is finally allowed in appeal, the said profit of Rs. 9,27,239 would be offered for taxation in the assessment year 1978-79. In the assessment for 1978-79 made in September 1982 the notional profit of Rs. 9,27,239 was not assessed to tax.

It was noticed in audit that the notional loss of assessment year 1972-73 was ultimately allowed under the appellate orders of Commissioner of Income-tax (Appeals) and the assessment was revised in November 1978. Consequently the entire notional profit on exchange amounting to Rs. 9,27,239 was required to be charged to tax in the assessment year 1978-79. This having not been done there was under assessment of business income of Rs. 9,27,239 with consequent undercharge of tax of Rs. 5,35,480 in the assessment year 1978-79.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

2.31 *Non-levy or short levy of interest*

(i) Any demand for tax should be paid by an assessee within thirty-five days of service of notice of the relevant demand and failure to do so would attract simple interest at twelve per cent per annum from the date of default. In November 1974, the Central Board of Direct Taxes issued instructions that interest for belated payment of tax should be calculated and charged within a week of the date of final payment of the tax demands.

(a) On completion of the income-tax assessment of a company for the assessment year 1977-78 in March 1980, the department raised a tax demand for Rs. 48,82,387 on 28 March 1980. The amount was paid in instalments after a delay of 9 to 13 months. The final instalment was paid in June 1981. Interest of Rs. 4,43,078 for the belated payment of tax was, however, not levied.

While accepting the mistake, the Ministry of Finance have stated that the interest amounting to Rs. 4,43,078 has been levied in October 1982 and the same has been recovered by way of adjustment of refunds due for the assessment years 1981-82 and 1982-83.

(b) After completing the assessment for the assessment year 1977-78 on 21 March 1980 a non-resident company was served with a notice of demand on 24 March 1980 to pay tax of Rs. 42,46,247 which was subsequently scaled down to Rs. 42,10,018. The tax demanded was to have been paid by the assessee company by 27 April 1980 as laid down in the Act. The foreign company, however, paid Rs. 10 lakhs only in March 1980 and the balance of Rs. 32,10,018 on 16 August 1980. Since the balance demand of Rs. 32,10,018 was not paid within the prescribed period the assessee was liable to pay interest of Rs. 96,300 for the belated payment. This was not levied by the department.

The paragraph was sent to the Ministry of Finance in August 1983 ; their reply is awaited (December 1983).

(c) The income-tax assessment of a company for the assessment year 1974-75 was revised in September 1977 and the Income Tax Officer determined the tax payable as

Rs. 18,13,530. The payment of this demand was due on or before 9 December 1977. The assessment for this assessment year was subsequently revised in June 1978 and the tax payable as per the revised order was Rs. 32,87,279. The entire demand was paid by the assessee in three instalments of Rs. 9,05,303 on 25 March 1978, Rs. 2,97,757 on 4 November 1978 and Rs. 20,86,219 on 30 March 1979. For the belated payment of tax, the department levied interest of Rs. 1,56,046 as against interest of Rs. 2,66,282 correctly leviable. This led to short levy of interest of Rs. 1,10,236.

The Ministry of Finance have accepted the mistake and have stated that the additional demand has been collected.

(d) For the assessment year 1975-76, a company in which public were not substantially interested was required to pay a demand (served on 7 February 1976) of tax of Rs. 28,56,240 which was to have been paid by the assessee by 13 March 1976. The demand was subsequently reduced to Rs. 27,20,210. The demand was collected in 9 instalments, from 13 March 1976 the last instalment being in July 1978. For the belated payment of tax, the Income Tax Officer should have charged interest of Rs. 1,16,736. No action was, however, taken by him to charge the interest.

The surtax assessment of this company for the assessment year 1975-76 was completed in January 1976 determining the surtax payable as Rs. 4,75,573. The assessment was revised in September 1978 in which the surtax payable was determined as Rs. 4,53,166. The demand was, however, paid by the assessee company in four instalments by cash credits and adjusment against refunds due between April 1976 and October 1978. It was seen in audit that for belated payment of tax, interest amounting to Rs. 89,438 was not levied.

The Ministry of Finance have accepted the mistake.

(ii) Under the provisions of the Income-tax Act, 1961, where the return for an assessment year is furnished after the specified date the assessee is liable to pay interest at 12 per cent per annum from the day immediately following the specified date to the date of furnishing of the return on the amount of tax payable on the total income as determined on regular assessment as reduced by the advance tax, if any, paid and tax deducted at source.

The income of an assessee company for the assessment year 1976-77 was originally assessed at Rs. 8,98,89,630 on 3 September 1980 which was subsequently revised on 29 October 1980, 4 August 1981 and on 29 August 1981 to Rs. 8,94,25,540, Rs. 9,16,19,490 and Rs. 9,05,53,791 respectively. The department charged interest for delayed submission of return in the assessment made on 3 September 1980 and on 29 October 1980. No interest was, however, charged on the basis of the revised tax payable in the assessment orders dated 4 and 29 August 1981 although the assessee was liable to pay interest for the default of two months in submitting the return on 28 September 1976 instead of by 30 June 1976. The omission resulted in non-levy of interest of Rs. 93,153 for the assessment year 1976-77.

The Ministry of Finance have accepted the mistake.

(iii) The Income-tax Act, 1961, further provides that where on making regular assessment the assessing officer finds that any assessee has underestimated the advance tax payable by him and has thereby reduced the amount payable in either of the first two instalments he may direct that the assessee shall pay simple interest at Rs. 12 per cent per annum for the period during which the payment was deficient.

For the assessment year 1979-80 an assessee company filed an estimate of advance tax for Rs. 5,01,30,949 in September 1978 and a revised estimate for Rs. 7,83,87,377 in March 1979. The company paid advance tax in three instalments of Rs. 1,67,10,316, 1,67,10,316 and Rs. 4,49,66,745 on 15 September 1978, 14 December 1978 and on 14 March 1979 respectively on the basis of estimates of advance tax filed by it. As the first two instalments of advance-tax were deficient the assessee company was liable to pay interest of Rs. 7,53,504 for the deficiency in payment. No interest was, however, levied by the department.

The Ministry of Finance have accepted the mistake.

2.32 *Avoidable payment of interest due to failure to make provisional assessment*

Under the Income-tax Act, 1961 where the advance tax paid by an assessee exceeds the amount of tax payable as determined on regular assessment, the Government is liable to pay interest on the amount of advance tax paid in excess for the period

from 1 April of the assessment year to the date of regular assessment. The Board issued instructions in April 1966 directing the Income Tax Officers to complete regular assessments as soon as possible after receipt of the returns.

In 1968 the Act was amended to provide for provisional assessment and grant of refund of advance tax paid in excess on the basis of provisional assessment. The Board also issued instructions that provisional assessment should be made in all cases where regular assessment is delayed beyond six months from the date of receipt of the return. These instructions were reiterated by the Board in March 1971 and again in July 1972.

In September 1974 the Board prescribed a register to be kept in the personal custody of the Income Tax Officer for noting down cases where provisional assessment would have to be made. The Income Tax Officer were also required to leave notes on the files, giving reasons as to why regular assessments could not be completed within six months. While stating that any payment of avoidable interest would be viewed seriously, the Board required the Commissioners and the Inspecting Assistant Commissioner to call for half-yearly statements of interest paid, exceeding Rs. 1,000 in each case in order to satisfy themselves that the payment of interest was unavoidable.

In their further instruction of July 1977 the Board prescribed the pro forma of a register to be maintained by the Income Tax Officers for making provisional assessments. All applications for provisional refunds and all returns with income exceeding Rs. 50,000 were required to be entered in this register as and when they are received. The Board also stated that provisional assessment for refund should be made not only in cases where the assessee had specifically claimed refunds but also where refunds were apparently due on the basis of returns filed.

Despite the controls prescribed by the Board, cases where provisional assessments were not done, continued to be noticed in audit involving avoidable payment of substantial amounts of interest by Government.

(i) For the assessment year 1978-79 a Government company paid advance tax of Rs. 17,37,641. It was noticed in audit (June 1982) that the company had filed its return of income for the assessment year 1978-79 on 28 September 1978 returning

an income of Rs. 7,41,190. As refund was *prima facie* due to the company, provisional assessment was required to be made under the Act as well as the Board's instructions. No action was, however, taken by the assessing officer to make provisional assessment to refund the tax paid in excess by the company. The regular assesment of the company was made in June 1981 determinig the income as Rs. 17,23,100 and revised in September 1981 reducing the income to Rs. 15,20,080 and a tax of Rs. 8,63,429 was refunded to the assessee alongwith interest amounting to Rs. 3,28,101. Had provisional assessment been made within six months as laid down in the Act payment of interest for 27 months amounting to Rs. 2,33,127 could have been avoided.

The Ministry of Finance have accepted the mistake in principle.

(ii) A state financial corporation filed its return of income for the assessment year 1976-77, on 31 July 1976 declaring an income of Rs. 10,72,570. As the amount of tax deducted at source together with advance-tax paid, exceeded the tax payable on the basis of income returned, the Income Tax Officer made (16 November 1976) a provisional assessment and the tax refundable was arrived at Rs. 4,34,605. As the amount of refund was more than Rs. 1,00,000, the assessing officer sought permission (25 November 1976) of the Inspecting Assistant Commissioner of Income-tax, who directed (29 November 1976) that totalling mistake and other defects should be rectified. The case was not resubmitted to the Inspecting Assistant Commissioner, but the regular assessment was completed on 31 March 1979 making a refund of excess advance tax amounting to Rs. 4,71,076. Failure to make the provisional assessment in this case led to payment of interest (May 1979) amounting to Rs. 1,64,844 on excess advance-tax paid. Had the refund been made in November 1976 itself, payment of interest to the extent of Rs. 1,27,160 could have been avoided.

While accepting the failure to make the refund in time so as to avoid payment of interest, in principle, the Ministry of Finance have stated that the "interest payable was as per the provisions of the Act and there was as such no mistake in the amount of interest paid".

(iii) A company in which public were substantially interested filed a return of income for the assessment year 1978-79 in

June 1978 admitting a total income of Rs. 71,69,330. As the advance tax paid and the tax deducted at source amounting to Rs. 69,20,636 exceeded the income-tax of Rs. 41,40,288 due on the returned income, a provisional assessment was required to be done as provided in the Act to refund the advance-tax paid in excess. The assessee also made a claim in July 1978 for a provisional assessment and refund of Rs. 27,80,348.

No provisional assessment was, however, made by the Income Tax Officer. The regular assessment was done in July 1981, after a lapse of three years and a refund of Rs. 16,09,454 together with interest of Rs. 6,26,966 was made. Failure to make the provisional assessment resulted in avoidable payment of interest of Rs. 4,82,836.

The Ministry of Finance have accepted the mistake.

(iv) A non-resident company which paid advance tax of Rs. 1,01,25,360 filed its return of income for the assessment year 1979-80 on 26 March 1980 declaring a total income of Rs. 96,76,710. Refund became apparently due on the basis of the return, and, therefore, a provisional assessment was required to be made to allow the refund. However, the department did not make the provisional assessment. The regular assessment was made in February 1982 and interest of Rs. 21,99,120 on account of excess payment of advance tax was paid.

Had a provisional assessment been made in this case within the prescribed time limit of six months, payment of interest to the extent of Rs. 4,85,447 could have been avoided.

The Ministry of Finance have accepted the mistake in principle.

(v) In the case of three other companies in two Commissioners' charges, the advance tax paid and tax deducted at source for the assessment years 1978-79 and 1979-80 amounted to Rs. 3,30,73,801. The companies filed their returns on 3 July 1978, 29 July 1978 and 31 July 1979. As refunds were, *prima facie* due to these companies, provisional assessments were required to be made under the Act as well as under the Board's instructions. No action was, however, taken by the assessing officers to make provisional assessments within the

statutory period of six months, with a view to refunding the taxes paid in excess by the assessees. The regular assessments were completed on 22 July 1981, 22 September 1981 and 27 March 1982 and taxes amounting to Rs. 58,03,489 paid in excess were refunded to the companies alongwith interest of Rs. 14,83,822. Had provisional assessments been made within the prescribed time limit of six months payment of interest (for a period of over two years) amounting to Rs. 11,23,601 could have been avoided.

The Ministry of Finance have accepted the mistake in principle.

2.33 *Avoidable payment of interest due to delay in implementing appellate orders*

Under the provisions of the Income-tax Act, 1961, refund should be given to the assessee within three months from the end of the month in which relevant order is passed in appeal or other proceedings under the Act, resulting in such refund. Delay (beyond 3 months) in granting refund will render the Government liable to pay interest to the assessee. Instructions were issued by the Central Board of Direct Taxes in July 1962 to the effect that such refund cases should be finalised within a fortnight of the receipt of appellate orders.

An assessee company became entitled to a total refund of Rs. 1,11,806 in respect of the assessment years 1957-58. 1958-59, 1960-61 to 1963-64, 1965-66 and 1966-67 as a result of certain appellate orders and rectificatory orders of the assessing officer passed between March 1962 and February 1977. As a result of delay in granting refunds varying from 4 years to 18 years the department had to pay interest of Rs. 97,106 on a total refund of Rs. 1,11,806 made in May 1981 which could have been avoided, had timely action been taken by the assessing officer.

The Ministry of Finance have accepted the mistake.

OTHER TOPICS OF INTEREST

2.34 *Incorrect application of rate of exchange*

Under the Income-tax Rules, 1962 the rate of exchange for calculation of value in rupees of any income payable to the assessee outside India or any income accruing or arising to the assessee in foreign currency shall be at the telegraphic transfer

buying rate of the State Bank of India on the specific dates when the income in question accrues or arises. With a view to avoiding any possible difficulties in obtaining these rates by the assessing officers, the Central Board of Direct Taxes communicated in September 1978, the telegraphic transfer buying rates of foreign currency of the State Bank of India as on the last day of each month for the period October 1977 to June 1978. According to this communication, the telegraphic transfer buying rate of US dollar as on 31 March 1978 for the equivalent of Rs. 100 was $ 11.01.

A Government company engaged a foreign company incorporated in the U.S.A. as its technical consultants. According to the agreement entered into with the foreign company, royalty and fee for technical services were payable in U.S. dollars. For the assessment year 1978-79, the foreign company was paid royalty and fees amounting to $ 11,66,667. While completing the assessment in March 1981 the Income Tax Officer calculated the income from royalty and technical fees payable in U.S. dollars by adopting the conversion rate of 11.72 U.S. dollars for Rs. 100 based on a certificate furnished by the assessee obtained from the State Bank of Travancore, as against the rate of 11.01 U.S. dollars for every Rs. 100 communicated by the Board. The adoption of incorrect rate of conversion resulted in underassessment of income by Rs. 6,41,667 involving short levy of tax of Rs. 1,51,434.

The Ministry of Finance have accepted the mistake and have reported that the assessment has been revised and additional demand of Rs. 1,51,434 collected in March 1983.

2.35 *Failure to revise the assessment of a company consequent upon the firm's assessment in which it is a partner*

Under the Income-tax Act, 1961, where at the time of assessment of partners of a firm, assessment of the firm has not been completed and the final share income of the partners is not known, the assessments of partners are to be completed by taking their share incomes from the firm on provisional basis. In such cases, the assessment of the partners are to be revised subsequently to include the final share incomes when the assessment of the firm is completed. For this purpose, the Income Tax Officers are required, under instructions of the

Central Board of Direct Taxes issued in March 1973, to maintain a register of cases of provisional share incomes so that timely action is taken to revise the partners' assessments and to ensure that cases are not omitted to be rectified whenever necessary.

The Public Accounts Committee has, from time to time, expressed concern at the delay in the revision of provisional assessments of partners' share income after completion of firms' assessments and has taken serious notice of the failure to keep a proper watch over such cases. In paragraphs 5.7 to 5.10 of their 85th Report (Seventh Lok Sabha) the Committee reiterated their views suggesting *inter alia* that the administrative instructions and the time limits laid down by the Board in 1973 are statutory and their observance should be insisted upon.

A private limited company engaged in the business of purchase and sale of yarn was also a partner in a registered firm. In its return for the assessment year 1976-77, the company had shown, its income from the registered firm, as a loss of Rs. 1,07,29,591. The regular assessment of the company was completed by the Income Tax Officer in July 1979 taking the share income from the firm as declared, subject to rectification and the total income for assessment year 1976-77 was determined at a loss of Rs. 1,06,32,880. The regular assessment of the firm was finalised in August 1979 and the share income allocated to the company was loss of Rs. 74,84,840. Due to an appellate order in the case of firm in August 1981, the share of loss finally allocated to the company was Rs. 75,06,160. Though the assessment of the company for the assessment year 1976-77 was revised on 15 March 1982 to give effect to certain appellate orders, no action was taken by the Income Tax Officer, till the date of audit, to adopt the correct share income of the company from the firm at a loss of Rs. 75,06,160 as against loss of Rs. 1,07,29,591 originally adopted. This resulted in excess computation of loss of the company by Rs. 32,23,431 for the assessment year 1976-77 with a potential tax effect of Rs. 22 lakhs.

The Ministry of Finance have accepted the mistake and have stated that remedial action has been completed in December 1982.

2.36 *Excess allowance of double income-tax relief*

Under the Income-tax Act, 1961, a resident person is entitled to a relief in respect of his foreign income, taxed both in India

and in a foreign country. The quantum of relief is governed by agreements entered into by the two countries.

Under the agreement for avoidance of double taxation between India and the Federal German Republic where an enterprise in one of the territories derives profits through shipping operation, the tax leviable on such profits shall be reduced by an amount equal to fifty per cent thereof. Income-tax on any non-shipping income will be retained in full by the country where the source of the income is located.

A non-resident shipping company was allowed double taxation avoidance relief as per the agreement in respect of its income earned in India at 50 per cent of tax determined on the income derived through shipping operations for the assessment years 1977-78 and 1978-79 (assessments made in June 1981 and September 1982 respectively).

It was noticed in audit that interest incomes of Rs. 97,620 and Rs. 2,25,316 earned by the assessee company in India on bank deposits during the assessment years 1977-78 and 1978-79 respectively were also allowed double taxation avoidance relief. Bank interest being a non-shipping income and having been earned from a source situated in India, should not have been allowed such relief as per the agreement. The mistake resulted in excess allowance of relief leading to undercharge of tax of Rs. 1,50,911 including short levy of interest of Rs. 7,233 for late filing of returns for both the assessment years.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

SURTAX

As a disincentive to excessive profits, a special tax called super profits tax was imposed on companies making excessive profits during the assessment year 1963-64 under the Super Profits Tax Act, 1963. This tax was replaced from the assessment year 1964-65 by surtax levied under the Companies (Profits) Surtax Act, 1964.

Surtax is levied on the "chargeable profits" of a company in so far as they exceed the statutory deduction, which is an amount equal to 10 per cent (15 per cent from 1 April 1977) of the capital of the company or Rs. 2 lakhs, whichever is greater.

During the period under review, underassessment of super profits tax/ surtax of Rs. 231.38 lakhs was noticed in 133 cases. A few illustrative cases are given in the following paragraphs.

2.37 *Incorrect computation of capital*

(i) Paid-up share capital or reserve brought into existence by revaluation or otherwise of any book asset is not capital for computing the capital base for surtax purposes.

In the surtax assessments of a company for the assessment years 1971-72 to 1975-76, completed between July 1977 and March 1980, share capital of Rs. 95,54,409 brought into existence by revaluation of book assets was incorrectly included in the computation of capital base as on the first day of the relevant previous years in contravention of the provisions of the Act. The mistake resulted in excess computation of capital by Rs. 47,77,205 with consequent undercharge of surtax (excess refund) of Rs. 15,52,590.

The Ministry of Finance have accepted the mistake.

(ii) Any premium received in cash alone by the company on the issue of its shares standing to the credit of the share premium account will form part of its paid-up share capital.

In the surtax assessments of a company for the assessment years 1971-72 to 1975-76 made between July 1977 and March 1980 a sum of Rs. 1,11,38,943 representing share premium not received in cash was also included in the capital base as on the first day of the relevant previous years. The mistake resulted in excess computation of capital by an amount of Rs. 55,69,470 with consequent undercharge of surtax (excess refund) of Rs. 18,10,077 for the assessment years from 1971-72 to 1975-76.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

2.38 *Mistake in the computation of chargeable profits*

In computing the chargeable profits of a company for the purpose of levy of surtax, a deduction is allowed on account of income-tax payable by it as reduced by any relief, rebate or deduction allowable under the Income-tax Act or the Finance Act concerned.

In the surtax assessment of a company for the assessment year 1977-78, the department, in arriving at the chargeable profits, deducted a sum of Rs. 1,41,20,695 towards income-tax payable. The said sum comprised income-tax of Rs. 1,34,48,281 and surcharge thereon of Rs. 6,72,414. It was noticed in audit that in the income-tax assessment for this assessment year, no surcharge on income-tax was levied in view of deposit of Rs. 6,98,000 made by the assessee under the Companies Deposits (Surcharge on Income-tax) Scheme, 1976. As surcharge on income-tax was not payable by the company, the deduction to be allowed on account of income-tax payable should have been Rs. 1,34,48,281 only and not Rs. 1,41,20,695. The mistake resulted in underassessment of net chargeable profits by Rs. 6,72,414 with consequent short levy of surtax of Rs. 2,68,470 in the assessment year 1977-78.

Further in the assessment year 1976-77 as against surtax Rs. 1,69,591 correctly leviable tax of Rs. 1,44,591 only was levied leading to short levy of surtax of Rs. 25,000. Total short levy in the two assessment years thus amounted to Rs. 2,93,470.

The Ministry of Finance have accepted the mistake and have stated that the assessments have been rectified in May and August 1983 raising additional demand of Rs. 2,93,470. Report regarding collection is awaited (November 1983).

2.39 *Omission to make surtax assessment*

Under the Companies (Profits) Surtax Act 1964, no statutory limit has been prescribed for completion of surtax assessments. In pursuance of the recommendations of the Public Accounts Committee, the Central Board of Direct Taxes issued instructions in October 1974 that surtax assessment proceedings should be initiated alongwith the income-tax assessments and that these should not be kept pending on the ground that additions made in the income-tax assessments were disputed in appeal; the time lag between the date of completion of income-tax assessments and surtax assessments should not ordinarily exceed one month unless there are special reasons justifying the delay.

While taking note of the persistent failures in taking up surtax assessments in spite of their earlier recommendations and the Board's instructions in pursuance thereof, the Public Accounts Committee reiterated in paragraphs 3.3 to 3.10 of

their 85th Report (Seventh Lok Sabha) that a statutory time limit for completion of assessment under the Surtax Act should be fixed. That has not been done so far.

In the absence of statutory time limit for completion of surtax assessments, instances of delay in the completion of such assessments with consequent postponement of realisation of revenue continue to be noticed in Audit. The following cases are illustrative of that :—

(i) The income-tax assessment of a company for the assessment year 1976-77 was completed in September 1979 on the basis of which the company was liable to pay surtax of Rs. 1,16,46,747. Although a provisional surtax assessment levying a surtax of Rs. 1,12,35,900 for the assessment year 1976-77 was made in November 1977, no action to make the regular surtax assessment in revision of the provisional assessment was taken by the department. The omission led to non-levy of surtax of Rs. 4,10,847 for the assessment year 1976-77.

In the case of the same company the taxable income for the assessment year 1977-78 was determined at Rs. 14,28,96,346 in April 1981. The company was assessable to surtax of Rs. 75,39,084. However, the assessee company did not file the return of chargeable profits and the assessing officer also did not initiate necessary proceedings for levy of surtax. The omission resulted in non-levy of surtax of Rs. 75,39,084 for the assessment year 1977-78.

The Ministry of Finance have accepted the omission in principle.

(ii) The provisional surtax assessment for the assessment year 1978-79 of a company was made in January 1979 raising a surtax demand of Rs. 40,10,514. The regular income-tax assessment of the company for the assessment year 1978-79 was made in May 1981 and was subsequently revised in September 1981. On the basis of the revised income-tax assessment, surtax leviable was Rs. 45,46,979. No action was, however, taken by the department to make regular surtax assessment till the date of audit (May 1982). The omission led to short levy of surtax of Rs. 5,36,465 for the assessment year 1978-79.

The Ministry of Finance have accepted the omission in principle.

(iii) For the assessment years 1974-75 to 1978-79, a company in which the public were substantially interested filed returns of income declaring losses. The company did not file returns under the Surtax Act. The department did not accept the losses returned by the company but completed the income-tax assessments on large incomes. As a consequential measure, the department should have examined the surtax liability of the company and completed surtax assessments provisionally following the instructions of the Board in this regard. In spite of this omission being pointed out by the Special Audit Party of the department in November 1981, this was not done. Only for the assessment year 1978-79, a notice was issued in August 1982 but no provisional assessment was made even for that year. The omission to make a provisional assessment for the four assessment years 1974-75 and 1976-77 to 1978-79 resulted in non-levy of surtax of Rs. 21,66,084.

While not accepting the mistake on the ground that the lapse had earlier been pointed out by the Special Audit Party, the Ministry of Finance have stated that remedial action, has been initiated by issue of notices.

The fact remains that no action was taken by the department, inspite of the Special Audit Party pointing out the lapse and that remedial action was initiated only after the Revenue Audit pointed out the omission.

(iv) The taxable incomes of a company for the assessment years 1976-77 to 1979-80 were determined at Rs. 6,48,860, Rs. 11,01,416, Rs. 7,18,684 and Rs. 8,98,060 in May 1978, April 1979, March 1981 and March 1982 respectively. The company was assessable to surtax of Rs. 10,019, Rs. 74,601, Rs. 16,217 and Rs. 42,303 in the respective assessment years. However, neither the assessee filed returns of chargeable profits nor did the assessing officer initiated necessary proceedings for levy of surtax. The omission led to non-levy of surtax of Rs. 1,43,140 for the four assessment years. In addition, the assessee rendered itself liable to a penalty of Rs. 1,43,140 for failure to furnish the relevant returns of chargeable profits.

The Ministry of Finance have accepted the omission in principle and have stated that notice has been issued to the assessee. Further report is awaited (December 1983).

(v) For the assessment year 1981-82, a company filed its income-tax return on 18 July 1981 and filed only a statement of surtax payable on 22 July 1981. The regular income-tax assessment was finalised on 2 January 1982. As per the Board's instructions of October 1974, the regular surtax assessment was required to be made before 2 February 1982.

It was noticed in audit (October 1982) that the Income-tax Officer had made neither provisional assessment nor regular assessment. The omission to make the surtax assessments for the assessment year 1981-82 resulted in the non-levy of surtax of Rs. 3,74,060.

The Ministry of Finance have accepted the mistake.

(vi) For the assessement year 1976-77, a company filed its surtax return on 30 September, 1976 and paid surtax of Rs. 1,26,700. It filed a 'nil' surtax return for the assessment year 1977-78 on 27th September, 1977. The regular income-tax assessments for these assessment years determining income at Rs. 23,99,560 and Rs. 18,52,494 were completed on 10 July 1979 and 16 September 1980 respectively. Since the chargeable profits of the company attracted levy of surtax assessments for these assessment years ought to have been completed before 10 August 1979 and 16 October 1980 respectively, as laid down in Board's instructions of October 1974.

It was seen in audit (November 1982) that the department had not initiated any proceedings for making regular surtax assessments in respect of these two years. The delay in making surtax assessments even after two to three years of completion of the relevant income-tax assessments resulted in non-levy of surtax of Rs. 1,16,762 for the two years.

The Ministry of Finance have accepted the mistake in principle.

(vii) For the assessment year 1977-78 the provisional surtax assessment of a company was made in February 1978 raising a surtax demand of Rs. 75,11,956. The regular income-tax assessment of the company for the assessment year 1977-78 was completed in July 1980, computing the taxable income at Rs. 4,60,17,870 and the tax payable thereon was determined as Rs. 2,53,76,320. On the basis of the income as determined in the income-tax assessment, the surtax leviable worked out to

Rs. 80,13,620 as against Rs. 75,11,956 levied on provisional assessment. Omission to revise the surtax assessment resulted in non-levy of additional demand of Rs. 5,01,664.

The Ministry of Finance have accepted the mistake in principle.

2.40 *Excess refund of surtax*

The original surtax assessment of a company for the assessment year 1972-73 made in July 1977 was revised in July 1981 with a refund of Rs. 1,70,371. After adjusting refund to the extent of Rs. 1,55,049 against the surtax demand for the assessment year 1974-75, the balance amount of Rs. 15,322 was refunded in cash. The assessment for the assessment year 1972-73 was revised again in February 1982 and a further refund of Rs. 2,10,372 was made.

It was noticed in audit (August 1982) that while working out the refundable amount the amount of Rs. 1,70,371 already refunded was omitted to be taken into account. The omission resulted in excess refund of surtax of Rs. 1,70,371.

While accepting the omission the Ministry of Finance have stated that remedial action has been taken and additional demand of Rs. 1,70,371 has been collected.

CHAPTER 3

Income-tax

3.01 Income-tax collected from persons other than companies is booked under the Major Head "021-Taxes on Income other than Corporation-tax". Eighty five per cent of the net proceeds of this tax, except in so far as these are attributable to Union emoluments, Union Territories and Union surcharges, is assigned to the states in accordance with the recommendations of the Seventh Finance Commission.

3.02 Some instances of mistakes noticed in the assessments of persons other than companies are given in the following paragraphs.

3.03 *Avoidable mistakes in the computation of tax*

Under-assessment of taxes of substantial amount have been noticed year after year on account of avoidable mistakes resulting from carelessness or negligence. Such mistakes continue to occur in spite of repeated instructions by the department.

A few cases are given in the following paragraphs :

(i) An assessee firm engaged in the distribution of feature films was allowed deduction of Rs. 6,06,960 in the assessment for the assessment year 1979-80 as cost of acquisition of distribution rights of feature films. The firm had acquired distribution rights of two films by lending certain amounts to the producers. The firm had not incurred any expenditure towards cost of acquiring distribution rights. As such no deduction towards cost of acquisition of the films was admissible. The irregular allowance of deduction resulted in under-assessment of income of Rs. 6,06,960. This together with other minor mistakes led to short assessment of income of Rs. 6,44,003 resulting in short-levy of tax of Rs. 3,37,556 in the hands of the firm and its partners.

The Ministry of Finance have accepted the mistake.

(ii) In the assessment of a registered firm for the assessment year 1977-78 (completed in August 1980 and revised in March 1981) depreciation of Rs. 92,623 already charged in accounts of the relevant previous year was omitted to be added back to the total income although depreciation of a sum of Rs. 98,700 as admissible under the Act was allowed separately. The mistake resulted in excess allowance of depreciation of Rs. 92,623 with an aggregate tax under charge of Rs. 1,17,197 in the hands of the firm and its partners together with penal interest for delayed submission of return of income.

The Ministry of Finance have accepted the mistake.

(iii) In the case of a firm, the assessing officer disallowed the claim for export markets development allowance amounting to Rs. 1,14,547 for the assessment year 1979-80 (assessment made in December 1979) stating that the firm was not entitled to the benefit as it was recognised as a small-scale industry only from the date of registration *viz.*, July 1979, relevant to the assessment year 1980-81.

However, while computing the taxable income, the Income-tax Officer overlooked to add back the sum of Rs. 1,14,547 to income. The mistake together with other minor arithmetical mistakes led to short computation of income by Rs. 1,17,608 resulting in under-charge of tax of Rs. 52,933.

The Ministry of Finance have accepted the mistake.

(iv) In the course of assessment of an individual for the assessment year 1979-80 (completed in December 1981) the assessing officer noticed concealed income amounting to Rs. 60,306 from undisclosed sources but failed to include the amount as taxable income in the actual assessment. The omission resulted in short-levy of tax of Rs. 53,660 including interest for failure to file estimate of advance tax.

The Ministry of Finance have accepted the mistake.

3.04 *Incorrect status adopted in assessments*

With a view to curbing the creation of multiple Hindu undivided families (HUFs), the Finance Act (No. 2), 1980 amended

the Income-tax Act, 1961 derecognising partial partitions effected after 31 December 1978, for tax purposes. A Hindu undivided family taxed in the status of a HUF, will continue to be taxed as such, unless there has been a total partition of the family properties by metes and bounds and a finding to that effect is recorded by the Income-tax Officer.

In the case of a Hindu undivided family, a partial partition effected in March 1979 was recognised by the department in November 1979. However, while computing the income for the assessment years 1980-81 and 1981-82 in October 1981, *i.e.,* after the law is amended, derecognising partial partition, the assessing officer did not include the income arising from the partitioned property. The omission resulted in short demand of tax of Rs. 45,295 for both the assessment years.

The Ministry of Finance have accepted the mistake.

3.05 *Incorrect computation of salary income*

Under the provisions of the Income-tax Act, 1961, income received by an employee from an employer is chargeable to tax under the head 'salary'. Salary includes profits in lieu of salary received from the employer.

(i) It has been judicially held that the mere fact that a professional, by reason of his being a professional, engages in service, will not convert his 'salary' into professional earnings [Re Bhagwati Shankar (1944)(12 ITR 193)].

(a) Four medical practitioners were appointed as employees by a hospital trust. According to the terms of employment, their remuneration was in two parts, first part comprising fixed monthly salary and the other being share in annual income arising out of treatment of patients in the particular department of the hospital. The appointment order (December 1972) in one case specifically stipulated full-time employment and prohibited private practice outside the hospital. In other cases the appointment order (August 1973) mentioned the fact of employment and the details of remuneration. In all these cases the amounts received by the assessees as share in the annual income of the particular department of the hospital were assessed by the department as income from profession after allowing deductions for the expenses claimed by them, whereas the fixed monthly salary income was

charged to tax under the head 'salary'. As there was an apparent employer-employee relationship, the whole income arising from the agreement of employment was assessable under the head 'salary'. The incorrect classification of part of income as income from profession, instead of salary, resulted in under-assessment of income by Rs. 4,30,705 involving short-levy of tax of Rs. 2,91,293 for the three assessment years 1977-78 to 1979-80.

On this being pointed out in June 1981, the department contended (March 1983) that :—

(i) salary and profits were paid under two different agreements.

(ii) receipt of remuneration for holding office did not necessarily give rise to relationship of master and servant; and

(iii) the assessees were allowed to have private practice in the hospital premises without any control, supervision or interference of the hospital over their work.

The reply of the department was, however, not correct as the appointment order of December 1972, as already stated, indicated full-time appointment prohibiting private practice outside the hospital and both the appointment orders gave details of both components of remuneration. It could not be that there was employer-employee relationship for one part of the appointment and none such for another part as assumed in the assessments made by the department. The test of control and supervision can be applied only with due regard to the nature of work and not in absolute terms [Dharanghadara Chemical Works (AIR 1957 SC 264)]. It has been specifically held also that if under the terms of contract of employment, remuneration or recompense for the services rendered by the employee is determined at a fixed percentage of turn over achieved by him then such remuneration or recompense will partake of the character of salary [Gestetner Duplicator (P) Ltd. (117 ITR 1)].

The paragraph was forwarded to the Ministry of Finance in August 1983 ; their reply is awaited (December 1983).

(b) An assessee, a medical practitioner was employed by a hospital trust. The remuneration received by him was in two parts, first part comprising fixed monthly salary and other being

share in annual income arising from treatment of patients in particular department of the hospital. During the previous year relevant to the assessment year 1980-81, the assessee received salary income of Rs. 12,000 and share of hospital income amounting to Rs. 1,50,588. It was noticed (October 1982) that the amount received by the assessee as share of hospital income was assessed as income from 'profession' after allowing deduction of Rs. 76,426 for the expenses claimed whereas the fixed monthly salary income was charged to tax under the head 'salary'. As there was an apparent employer-employee relationship, the whole income arising from the hospital was assessable under the head 'salary'. The incorrect classification of part of the income as income from 'profession', instead of 'salary' resulted in under-assessment of income of Rs. 76,426 involving short-levy of tax of Rs. 55,029.

The paragraph was forwarded to the Ministry of Finance in August 1983; their reply is awaited (December 1983).

(ii) Under the provisions of the Income-tax Act, 1961, any special allowance or benefit specifically granted to meet expenses wholly, necessarily and exclusively incurred in the performance of the duties of an office or employment of profit, to the extent to which such expenses are actually incurred for that purpose, shall not be included in the total income of an assessee. It is further clarified that any allowance granted to the assessee to meet his personal expenses at the place where the duties of his office or employment of profit are ordinarily performed by him or at the place where he ordinarily resides shall not be regarded as a special allowance granted to meet expenses wholly, necessarily and exclusively incurred in the performance of such duties.

During the previous years relevant to assessment years 1979-80 and 1980-81, an assessee received Rs. 1,02,050 and Rs. 78,300 respectively towards local living expenses which were meant for meeting his personal expenses for lodging and boarding. In the income-tax assessments of the assessee completed for the assessment years 1979-80 and 1980-81, 50 per cent of such expenses were allowed as special allowance in the performance of employment. As no portion of the living expenses received by the assessee could be considered as a special allowance granted to meet expenses wholly, necessarily and exclusively in the performance of the duties of employment, the deduction allowed was not in order. The mistake resulted in under-assessment of

income of Rs. 51,025 and Rs. 39,150 for assessment years 1979-80 and 1980-81 leading to short-levy of tax of Rs. 57,379 in the aggregate.

The Ministry of Finance have accepted the mistake.

3.06 *Incorrect computation in the case of foreign technician*

The Income-tax Act, 1961, allows under certain conditions, exemption from tax on remuneration of foreign technicians in the employment of the Government or of a local authority or of a statutory corporation or in any business carried on in India. If the foreign technician is an employee of an Indian concern, the tax paid by the employer is to be treated as perquisite and taxed on 'tax on tax' basis. If he is an employee of a foreign enterprise, but the tax is paid by the Indian concern, the same is to be treated as "income from other sources" in the hands of the technician and taxed accordingly.

In the case of a foreign technician, who was employed by an Indian company, tax of Rs. 39,641 paid by the Indian employer was added to the total taxable income of Rs. 91,410, paid to the assessee tax free in the assessment year 1978-79 (assessment completed in March 1981). The perquisite calculated on 'tax on tax' basis, however, actually worked out to Rs. 1,26,300 which should have been added to the taxable income of the foreign technician. Incorrect calculation of the value of perquisite resulted in under-assessment of income of Rs. 86,660 and short-levy of tax of Rs. 59,802.

The paragraph was forwarded to the Ministry of Finance in August 1983; their reply is awaited (December 1983).

3.07 *Incorrect computation of business income*

(i) Under the provisions of the Income-tax Act, 1961, any expenditure not being in the nature of capital expenditure or personal expenses of an assessee which is wholly and exclusively incurred for the purpose of business is allowable in computing the business income of the assessee.

(a) In the case of a registered firm the assessing officer held in the draft assessment order for the assessment year 1978-79, that the entire sales commission paid to selling agent was excessive because there was no service rendered to the firm.

The Inspecting Assistant Commissioner also confirmed the disallowance proposed by the assessing officer on this account. But, while computing the total income of the assessee at Rs. 3,40,056 in August 1981, the assessing officer did not add back the commission on sales amounting to Rs. 1,27,171 resulting in under-assessment of income to that extent. For the same reasons, the sales commission of Rs. 1,44,181 and Rs. 1,56,267 for the assessment years 1979-80 and 1980-81 for which assessments were completed in December 1981 and March 1982, was also not admissible as deduction. The omission to add back commission on sales resulted in under-assessment of income totalling Rs. 4,27,619 leading to aggregate undercharge of tax of Rs. 3,17,635.

The paragraph was sent to the Ministry of Finance in July 1983; their reply is awaited (December 1983).

(b) An assessee's accounting year ended on 31 December 1979. The return for the assessment year 1980-81 showing a loss of Rs. 3,99,230 was filed on 16 March 1981. Profit and loss account of the assessee for the year ending 31 December 1979 showed that an amount of Rs. 6,72,217 was debited for current repairs of building and plant and machinery which were heavily damaged by accidental fire. The assessee received Rs. 5,71,316 and Rs. 5,71,316 on account of insurance claim of building and plant and machinery respectively in the previous year relevant to the assessment year 1980-81. As the repairs were not of minor and revenue nature but of major and of capital nature, the amount spent on repairs was required to be capitalised. The incorrect treatment of capital expenditure as revenue expenditure resulted in under-assessment of income of Rs. 6,72,217 and a short levy of tax of Rs. 1,84,850 in the hands of the firm and its partners including interest.

The Ministry of Finance have accepted the mistake.

(c) An assessee, a registered firm, advanced loans to a private limited company from 1972-73 onwards. Two partners of the assessee firm were Chairman and Managing Director of the company. The company did not repay the loans and interest thereon. The loan amount outstanding as on 31 December 1978 (assessment year 1979-80) was shown in accounts as Rs. 4,84,625. The assessee sold his rights to recover the amount to another party for Rs. 1,92,000 and debited Rs. 2,92,625 in his accounts as expenses.

Transferring of right in an asset was "transfer" within the meaning of the Act and hence the loss arising therefrom was expenditure of a capital nature and as such was required to be excluded from business expenditure. The incorrect deduction thereof resulted in underassessment of income of Rs. 2,92,625 and short levy of tax of Rs. 80,765 in the hands of the firm. Tax effect in the hands of the partners is yet to be ascertained.

The Ministry of Finance have accepted the mistake.

(ii) The amount of any debt or part thereof, which is established to have become bad in the previous year, is allowed as deduction in computing the business income.

While making the assessment of a registered firm for the assessment year 1979-80 in March 1982, the Income-tax Officer allowed deduction of Rs. 6,47,543 as claimed by the assessee for the reason that the amount was considered as irrecoverable from the Tamil Nadu Civil Supplies Corporation to whom rice was supplied, as the disputed claim was pending in a court of law. The amount in question could not be said to have become irrecoverable till the decision of the court. Its incorrect deduction led to short computation of income of Rs. 6,47,543, involving under charge of tax of Rs. 5,99,579 in the case of the firm and partners, including Rs. 97,386 as interest for late filing of return.

The paragraph was sent to the Ministry of Finance in August 1983; their reply is awaited (December 1983).

(iii) Under the provisions of the Income-tax Act, as operative during the period April 1979 to March 1981, where the aggregate expenditure on advertisement, publicity and sales promotion in India exceeds half a per cent of the turn over, 15 per cent of the adjusted expenditure thereof has to be disallowed. This provision which applied to all categories of tax-payers carrying on business or profession was not applicable to cases where the aggregate amount of such expenditure does not exceed Rs. 40,000. The expression "adjusted expenditure" meant the aggregate expenditure incurred on advertisement, publicity and sales promotion in India as reduced by expenditure not allowable as business expenditure under the general head and further reduced by expenditure specifically stated in the Act as admissible, such as, that incurred on advertisement in any small newspaper or advertisement for recruitment of personnel etc.

The gross turn over of a firm engaged in manufacture of drugs amounted to Rs. 1011.07 lakhs in the previous year relevant to the assessment year 1980-81. The expenditure on account of advertisement amounted to Rs. 31.16 lakhs out of which a sum of Rs. 21.80 lakhs was incurred on specified categories thereof admissible under the provisions of the Act. The entire expenditure of Rs. 31.16 lakhs was allowed as business expenditure in the assessment completed in October 1980. The omission to disallow 15 per cent of the expenditure of Rs. 9.36 lakhs (after deducting Rs. 21.80 lakhs admissible under the Act) resulted in under-assessment of income by Rs. 1,40,280 involving short levy of tax of Rs. 1,12,315 in the hands of the firm and its three partners.

The Ministry of Finance have accepted the mistake.

(iv) Under the provisions of the Income-tax Act, 1961 any sum paid by an assessee as an employer by way of contribution towards an approved gratuity fund created by him for the exclusive benefit of his employees under an irrevocable trust is an admissible deduction in computing income from business.

In computing the business income of a Hindu undivided family for the assessment year 1977-78 in December 1980, contribution to an unapproved gratuity fund was incorrectly allowed as deduction. This resulted in under-assessment of income by Rs. 84,559 and short levy of tax of Rs. 69,349.

The Ministry of Finance have accepted the mistake.

(v) Where an assessee has been allowed, in the assessment of his income, a deduction on account of any trading liability and subsequently he obtains some benefit in respect of such trading liability, the value of benefit accruing to him is chargeable to tax in the year in which the liability is liquidated.

While computing the business income of two registered firms for the assessment years 1979-80 and 1981-82 (in March 1982) the department allowed exemption to sales tax subsidy of Rs. 1,79,634 and Rs. 1,84,694 respectively received by the assessee treating it as capital receipt. As sales-tax subsidy was allowed by the State Government as a percentage of sales tax paid, for which the assessee firms had already been allowed deduction in their assessments, the amounts received should have been brought to tax. Their incorrect exemption resulted in undercharge of tax aggregating to Rs. 1,73,477.

The Paragraph was sent to the Ministry of Finance in August 1983; their reply is awaited (December 1983).

3.08 *Mistakes in the grant of export markets development allowance*

Under the Income-tax Act, 1961, domestic companies and resident non-corporate assessees engaged in the business of export of goods outside India or of providing services or facilities outside India were entitled (upto March 1983) to an export markets development allowance equal to the actual amount of expenditure plus an extra amount of one-third thereof. Expenditure on distribution and supply of goods in India and expenditure wherever incurred on the carriage of such goods to their destination outside India or on the insurance of such goods while in transit did not qualify for this allowance.

Expenditure on export of goods, services etc., outside India qualified for the allowance only if these were incurred outside India and before 1 April 1978.

(i) While completing the assessment for the assessment year 1978-79 in respect of a Hindu undivided family in September 1981, the department considered a total expenditure of Rs. 8,52,623 as having been incurred towards development of export markets and allowed weighted deduction for a sum of Rs. 11,36,831 equal to one-third of such expenditure. It was noticed that out of the aforesaid expenditure of Rs. 8,52,623, expenditure to the extent of Rs. 75,965 only could qualify for the weighted deduction. The balance expenditure of Rs. 7,76,658 was incurred on insurance of goods in transit, handling charges by Port Commissioners and on other items in India. The allowance of weighted deduction on expenditure of Rs. 7,76,658 was, therefore, not correct. The mistake resulted in underassessment of total income by Rs. 2,58,886 (1/3rd of Rs. 7,76,658) with consequent tax undercharge of Rs. 1,78,632.

The Ministry of Finance have accepted the mistake.

(ii) In the case of an assessee firm, weighted deduction was allowed in the assessment years 1978-79, 1979-80 and 1980-81 on expenditure incurred on salary and other allowance of the staff employed in India and on interest on bank loan and bank charges etc. paid in India. Since the expenditure was incurred

in India, the weighted deduction was not admissible. The incorrect allowance resulted in short levy of tax aggregating to Rs. 87,874.

The Ministry of Finance have accepted the mistake.

3.09 *Incorrect allowances of depreciation, development rebate and investment allowance*

(i) In computing income from business, the Income-tax Act, 1961, provides for the grant of depreciation on buildings, plant and machinery and furniture owned by an assessee and used for the purpose of his business. Under the Income-tax Rules, 1962 special rates of depreciation ranging from 15 per cent to 100 per cent are prescribed for certain specified items of machinery and plant. A general rate of 10 per cent is prescribed in respect of machinery and plant for which no special rate of depreciation is prescribed.

During the previous year, relevant to the assessment year 1979-80, two assessees, registered firms, acquired "Terex Loaders" at a cost of Rs. 33,13,997 for the contract business of transporting coal from coal fields and loading in railway wagons. The assessees claimed depreciation at the special rate of 30 per cent which was allowed by the department treating the loaders as earth moving machinery used in open-cast mining. As loaders were not earthmoving machinery but were used only for lifting coal lying in railway sidings and pouring it into railway wagons, these were entitled to depreciation at the rate of 10 per cent only and not at 30 per cent. The department's omission to disallow the claim at the higher rate for the assessment year 1979-80, resulted in under-assessment of income by Rs. 6,63,799 and short-levy of tax of Rs. 1,82,943.

The Paragraph was sent to the Ministry of Finance in July 1983; their reply is awaited (December 1983).

(ii) Under the Income-tax Act, 1961, development rebate was allowed in respect of new plant and machinery installed by an assessee and used for the purpose of his business or profession. The relief was abolished from 1 June 1974 except for a limited period in certain cases. The Finance Act, 1976 introduced a new scheme of investment allowance with effect from 1 April 1976. The Act provides for withdrawal of the rebate already allowed if the assets are sold or otherwise transferred to any person at any time before the expiry of eight years from the end of the previous year in which the assets were acquired or installed.

A registered firm was dissolved on the last day (30 June 1978) of the previous year relevant to the assessment year 1979-80. Its assets were taken over by a new firm formed on 1 July 1978. While completing the assessment of the dissolved firm for the assessment year 1979-80, the assessing authority disallowed (February 1982) its claim for investment allowance (Rs. 34,894) in respect of assets acquired during the relevant accounting year on the ground that the assets were transferred to the new firm before the expiry of the stipulated period. Pursuant to its finding that the dissolved firm had transferred its assets to another firm, the department did not examine whether any development rebate/investment allowance had also been allowed in the preceding seven years which had to be withdrawn. Audit scrutiny indicated (October 1982) that the dissolved firm had been allowed a total amount of Rs. 2,19,436 towards development rebate and investment allowance in respect of the assessment years 1973-74, 1974-75 and 1978-79 and the department's omission to withdraw these allowances had resulted in short-levy of tax of Rs. 1,03,833 in the hands of the firm and its partners.

The paragraph was sent to the Ministry of Finance in July 1983; their reply is awaited (December 1983).

(iii) The right to investment allowance is lost even if the transfer within eight years of an asset results from a business reorganisation or expansion *e.g.*, when a sole proprietory firm is formed into a partnership.

In the assessments of an individual for the assessment years 1979-80 and 1980-81, completed in October 1981, it was noticed (December 1982) that upto the assessment year 1980-81 the assessee was a sole proprietor. The business was taken over by a partnership concern with effect from 1 April 1980 vide partnership deed dated 23 April 1980. Since the machinery owned by the assessee was transferred to a partnership concern, the investment allowance of Rs. 95,689 allowed in the assessment years 1979-80 and 1980-81 was to be withdrawn. Omission to withdraw this allowance resulted in short demand of tax of Rs. 73,822 including interest for late filing of return.

The Ministry of Finance have accepted the mistake.

(vi) Investment allowance is not admissible on plant or machinery the whole cost of which has been allowed as a deduction (whether by way of depreciation or otherwise) while computing business income.

In the assessment of a registered firm for the assessment year 1978-79 (made in July 1981) the department incorrectly allowed investment allowance of Rs. 70,642 on the actual cost of machinery viz., Rs. 2,83,107 on which 100 per cent depreciation had been allowed. The incorrect grant of investment allowance led to undercharge of tax of Rs. 54,790 in the hands of the assessee firm and its partners.

The Ministry of Finance have accepted the mistake.

(v) The investment allowance is admissible only if the plant and machinery is used for the purpose of business of generation or distribution of power or construction, manufacture or production of certain articles.

In the case of a registered firm engaged in the business of sinking bore wells for water, investment allowance of Rs. 1,28,638 was allowed for the assessment year 1980-81, even though the business of the firm was neither construction nor manufacture or production of articles. Also, for the assessment years 1979-80 to 1981-82, depreciation on rigs and compressors was allowed at the rate of 30 per cent, applicable to mineral oil concerns, instead of at the general rate of 10 per cent. The two mistakes resulted in a short levy of tax of Rs. 52,177 in the hands of firm and its partners for the assessment years 1979-80 to 1981-82.

The Ministry of Finance have accepted the mistake.

3.10 *Omission to levy capital gains tax*

Under the provisions of the Income-tax Act, 1961, any profits or gain arising from the transfer of a capital asset are chargeable to income tax under the head 'capital gains'. For the purpose of computation of capital gains, the term 'transfer' has been defined in the Act to include 'sale, exchange or relinquishment of an asset or extinguishment of any rights therein'. It has been judicially held that, when a person brings his assets into a firm in which he is a partner as his capital contribution, it amounts to a transfer of capital assets, as the person loses his exclusive right over the said assets which become the property of the firm, his right in the assets being limited to his share in money representing the value of the property of the firm as a whole.

(i) In a case, two partners transferred a piece of land in which they had life interest and remaindermans interest respectively towards capital contribution to the firm. It was agreed that they would be paid along with another partner fixed shares of profits of Rs. 75,000 per annum for a period of about 47 years. This interest on capitalisation amounted to Rs. 10,50,000. Capital gains amounting to Rs. 9.50 lakhs (Rs. 10.50 lakhs minus assumed value as on 1 January 1954 at Rs. 1.00 lakh) arising to them as association of persons were not taxed. The tax not levied amounted to Rs. 4,98,856.

The Ministry of Finance have accepted the mistake in principle.

(ii) In the assessment of two individuals (sisters) for the assessment year 1981-82, completed in February/March 1982, incomes were returned and assessed at Rs. 42,401 and Rs. 42,431 respectively under the summary assessment scheme. It was noticed in audit (December 1892) that the assessees had transferred their immovable property (a plot of 2400 sq. yds.) to a firm in which they became partners, with one third share each. The capital accounts of the assessees were credited with Rs. 2,50,000 each on 1 May 1980 towards the cost of the land but the capital gains arising to them thereby were not brought to tax. This resulted in non-levy of tax of Rs. 2,29,536.

The Ministry of Finance have accepted the mistake and added that the assessments made under the summary scheme are being rectified.

(iii) Members of a family formed a registered firm with effect from 1 January 1981 with a view to conducting business, among other things, in real estate and shares, debentures etc. It was, noticed (February 1983) that capital assets held by the members in the form of shares were transferred to the firm at market rate during the period January 1981 to March 1981. The resultant capital gains of Rs. 9,60,899 arising to the members of the family were not, brought to tax in the assessment year 1981-82. This led to short levy of tax of Rs. 2,13,139.

The Ministry of Finance have accepted the mistake.

(iv) An assessee introduced a building costing Rs. 3,00,000 in the firm towards his capital contribution of Rs. 5 lakhs. The

capital gain arising out of the transfer was not taxed. The consequent short levy of tax inclusive of interest amounted to Rs. 1,36,495.

The Ministry of Finance have accepted the mistake.

(v) The wealth-tax assessment records of an assessee for the assessment year 1976-77, the assessment of which was completed on 31 March 1981, revealed that the assessee had transferred 25,700 square yards of lands valued at Rs. 2,00,000 to a firm towards her share capital. The transfer of lands involved a capital gain of Rs. 1,24,875 which was not subjected to tax. The omission resulted in under-assessment of income by Rs. 1,24,875 with a consequential short levy of tax of Rs. 86,917.

While accepting the mistake, the Ministry of Finance have stated that remedial action was barred by limitation. The mistake having been pointed out in July 1982, time was available for rectification upto 30 March 1983. Omission to take timely action resulted in loss of revenue of Rs. 86,917.

(vi) The wealth-tax return of an assessee for the assessment year 1975-76 showed that certain immovable properties were sold by the Tax Recovery Officer (Income-tax Department) and Commercial Taxes Officer of the State Government for a total amount of Rs. 5,30,000 in the previous years relevant to assessment years 1974-75 and 1975-76 and for Rs. 61,620 in the assessment year 1971-72 by the assessee himself. Assuming the fair market price of properties at Rs. 3,14,000 on 1 January 1954 by taking into account the valuation of these properties adopted in the wealth-tax assessments for the assessment year 1958-59, the capital gains worked out to Rs. 2,77,620. The income by way of capital gains was not brought to assessment during the assessment years 1971-72, 1974-75 and 1975-76 leading to short levy of tax of Rs. 1,14,529.

While admitting the objection, the Ministry of Finance have stated that remedial action for the assessment year 1971-72 had been time barred and for the assessment years 1974-75 and 1975-76, the remedial action is being taken.

3.11 *Mistakes in computing capital gains*

(i) Under the provisions of the Income-tax Act, 1961, as applicable upto the assessment year 1982-83 where a capital

gain arises from the transfer of a capital asset, being house property, which in the two years immediately preceding the date on which the transfer took place, was being used by the assessee or a parent of his, mainly for the purpose of his own or his parent's own residence, and the assessee has, within a period of one year before or two years after that date, purchased a house property for the purposes of his own residence and the amount of capital gain is equal to or less than the cost of the new asset, then, the entire capital gain is not to be charged to tax.

An individual purchased two house properties for Rs. 6,000 and Rs. 30,000 in September 1960, and February 1966 respectively. Though income was being returned by the assessee in respect of the second house as self-occupied property, no property income was returned in respect of the first house on the ground that it was used for business. The assessee sold these properties for a total consideration of Rs. 2,16,000 in June 1979 and purchased another house property in September 1979 for Rs. 2,16,960.

In the assessment for the assessment year 1980-81 completed in November 1980, the capital gain arising from the transfer was exempted as the entire proceeds of sale of the old house properties were reinvested in a new house property within one year.

Audit scrutiny, however, revealed (August 1982) that according to the income-tax returns for the assessment years 1980-81 and 1981-82, the assessee had used only a portion of the new house as his residence and had let out the other portion to his son, the rental income being returned separately.

Further, one of the houses sold was used only for his business and not used either by the assessee or his parent as residence in the two years preceding the date of transfer. As two of the essential conditions stipulated for the grant of exemption were not fulfilled, the exemption allowed was not in order. The irregular exemption resulted in short levy of tax of Rs. 77,571.

The Ministry of Finance have accepted the mistake.

(ii) Certain deductions are admissible, in the computation of income under the head 'capital gains', under Chapter VIA of the Act. In the case of long-term capital gains included in the 'gross total income' of an assessee, where such capital gains do

not exceed Rs. 5,000, the whole of such long term capital gains is allowed as deduction. In other cases deduction admissible is Rs. 5,000 as increased by 25 per cent of the amount by which the long-term capital gains relating to capital assets being lands and buildings exceed Rs. 5,000.

An assessee returned a capital gain of Rs. 54,366 in respect of the sale of a house property in the assessment year 1981-82. This was accepted by the department. The details of computation of the amount of Rs. 54,366 returned by the assessee showed that from the capital gain of Rs. 5,61,199 derived on the sale of the old house, deduction admissible under Chapter VIA of the Act was first allowed and cost of the new asset amounting to Rs. 3,62,783 was deducted thereafter. This was not correct. The cost of the new asset amounting to Rs. 3,62,783 should have been deducted first from the capital gain of Rs. 5,61,199 and the deduction of Rs. 53,354 admissible under Chapter VIA should have been allowed from the resultant amount of Rs. 1,98,416 to arrive at a taxable capital gain of Rs. 1,45,062. The incorrect procedure adopted in the computation of capital gain liable to tax resulted in under-assessment of income by Rs. 90,696 with consequent short levy of tax of Rs. 59,858.

The Ministry of Finance have accepted the mistake.

3.12 *Mistakes in assessment of partners of firm*

Under the Income-tax Act, 1961, firms are classified into registered firms and unregistered firms. A registered firm pays only a small amount of tax on its income, the rest of its income is apportioned among the partners and included in their individual assessments. An unregistered firm pays full tax on its total income. When at the time of completion of the assessments of the partners, the assessment of the firm has not been completed, the share income from the firm is included in the assessments of the partners on a provisional basis and revised later to include the final share income, when the assessment of the firm is completed. For this purpose, the Income-tax Officers are required, under the instructions of the Central Board of Direct Taxes issued in March 1973, to maintain a register of cases of provisional share income so that these cases are not omitted to be rectified.

Instances of default in the revision of the partners' assessments in such cases have been commented upon in a number of Audit

Reports, the latest being in paragraph 3.20 (Audit Report 1981-82). The Public Accounts Committee have also, from time to time, expressed concern at the delay in the revision of provisional assessments of partners' share income after completion of firms' assessments. The Committee took serious note of the failure to keep proper watch over such cases in their recommendations/ observations made in paragraph 65 of their 21st Report (Third Lok Sabha), paragraph 45 of their 28th report (Third Lok Sabha) and paragraph 2.224 of their 186th Report (Fifth Lok Sabha). In paragraph 5.7 of their 85th Report (Seventh Lok Sabha), the Committee observed that they were distressed to note that despite their earlier recommendations and the action taken in pursuance thereof the situation had not improved.

In spite of the remedial action taken by the department in the light of the recommendations of the Committee, instance have come to the notice of audit where the default continued to occur, as illustrated in the following paragraphs.

(i) The income of a firm for the assessment year 1972-73 was reassessed on 24 September 1981 and the share of each of its two partners was determined at Rs. 8,87,790 as against the original share income of Rs. 24,665 assessed in their hands. However, the consequent rectification in the hands of the two partners was not carried out. This resulted in under-assessment of income of Rs. 8,63,125 in each of the partners' cases with consequent short-levy of tax of Rs. 8,19,629 in each case resulting in aggregate short-levy of tax of Rs. 16,39,258 for the assessment year 1972-73.

The Ministry of Finance have accepted the mistake.

(ii) The taxable income of a registered firm for the assessment year 1978-79 was determined in a survey circle as Rs. 13,49,650 on 31 March, 1981 and the share of income of four partners (assessed in three different wards), as Rs. 2,41,212 each. It was observed (December 1981) from the assessment records that three of the four partners had not filed the returns of income for the assessment year 1978-79. In the assessment of the fourth partner, the assessments made on 1 March 1981 adopting share income of Rs. 2,08,555 provisionally was not revised adopting the final share income of Rs. 2,41,212.

On the omissions being pointed out in audit the department stated (March 1983) that the assessments of all the partners had been revised on the basis of the share incomes assessed in three different wards. On further verification (June 1983), the reply of the department was found to be factually incorrect. Action remained to be taken in all the four cases. The three partners had not even filed returns of incomes for the assessment year 1978-79. In one case, a notice for assessment of escaped income was issued on 24 December 1980, but there was no follow-up action. In the fourth case no rectification was carried out.

Thus, taxable income of Rs. 7,23,636 escaped assessment in the hands of the three partners. If the partners had no other source of income, the tax chargeable worked out to Rs. 4,27,542. The tax effect in the hands of the fourth partner in whose case income had not been revised so far would, come to Rs. 22,530.

The total short levy of tax was Rs. 4,50,172.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(iii) During the course of audit (July 1982) it was noticed that the share income of two assessees from a firm was incorrectly worked out as under for the three successive assessment years 1975-76 to 1977-78 leading to an undercharge of tax of Rs. 2,65,255. Besides, the prescribed register of cases of provisional share income was not maintained in the ward.

The share incomes of two partners for the assessment year 1975-76 were taken as Rs. 13,691 each in the assessment completed in March 1978 without any indication in the assessment orders that incomes were provisionally taken. As per the assessment of the firm completed in September 1978 the share income allocated to each of these partners was Rs. 51,580. The assessment of the partners were not revised. The incorrect share income adopted for assessment resulted in aggregate short levy of tax amounting to Rs. 33,617.

The share incomes of these partners for the assessment year 1976-77 were taken as Rs. 5,180 each quoting the order passed in the case of the firm in September 1978. However, the order passed in September 1978 related, in fact to the assessment year 1975-76 allocating an amount of Rs. 51,580 to each of the

partners and not Rs. 5,180. The actual amount allocated to each of the partners for the assessment year 1976-77 in September 1979 amounted to Rs. 73,213. The incorrect adoption of share income resulted in aggregate short levy of tax of Rs. 1,02,473.

For the assessment year 1977-78, the share income of these assessees was taken as loss of Rs. 61,667 in the assessment order passed on 21 January 1980. In the firm's assessment completed on 18 September 1980 the share income allotted to each of the partners was profit of Rs. 37,871. The partners' cases were not revised to adopt the correct share income. This resulted in aggregate short levy of tax of Rs. 1,29,165.

The Ministry of Finance have accepted the mistake.

(iv) A registered firm and its two partners were assessed in the same ward. A reassessment of the firm for the assesment year 1975-76 was made in September 1981, resulting in an addition of Rs. 1,10,727 to the taxable income of the firm. As a consequence, the assessing authority was required to revise the assessment of partners to bring to tax their revised share income from the firm. This was not done resulting in underassessment of tax of Rs. 67,052.

The Ministry of Finance have accepted the mistake.

3.13 *Mistakes in assessment of firms and partners*

According to the provisions of the Income-tax Act, 1961, registration granted to a firm for purposes of income-tax remains effective for every subsequent year provided that there is no change in the constitution of the firm or in the shares of the partners as evidenced by the instrument of partnership on the basis of which registration was granted.

In the case of a firm, registration for the assessment year 1977-78 sought for by the firm was refused on the ground that the partnership deed drawn in November 1976 was invalid as one of the full-fledged partners was a minor on the date of execution of the instrument of partnership. The firm was, therefore, assessed to tax in the status of an unregistered firm. However, the firm was wrongly granted registration for the assessment year 1978-79 on the basis of the same deed which was treated as invalid for the previous assessment year. This irregular grant of registration resulted in under assessment of tax of Rs. 1,80,832.

The Ministry of Finance have accepted the mistake and further stated that the additional demand has been fully recovered.

3.14 *Omission to include income of minor*

Under the provisions of Income-tax Act, 1961, in computing the total income of an individual, there shall be included all such income as arises directly or indirectly to the minor child of the individual from the admission of the minor to the benefits of partnership in a firm. For this purpose, the income of the minor shall be included in the income of that parent whose total income is greater.

(i) In the case of two assessees, incomes of three minor children arising from their admission to the benefits of a partnership firm were not included in their total incomes for the assessment years 1976-77 to 1981-82 in accordance with the clubbing provisions of the Act. This resulted in under-assessment of tax of Rs. 3,36,021.

The Ministry of Finance have accepted the mistake.

(ii) The Act also provides that if any person has concealed the particulars of his income or furnished inaccurate particulars of such income, he shall, in addition to tax payable, be liable to pay a minimum penalty equal to the amount of tax sought to be evaded.

Fourteen minor children of four individuals were admitted to the benefits of partnership in two firms for the assessment year 1976-77. The individuals did not include the share incomes of the minors in their own returns of income filed for the assessment year 1976-77. The assessments were completed in March 1977 on the basis of returns filed.

The Income-tax Officer who completed the firms' assessments intimated the share income of the minors to the Income-tax Officer who had made the assessments of the individuals in September 1977. Subsequently, the files of the individuals were transferred to the ward where the firms had been assessed. No action was taken in either ward to revise the assessments of the individuals to include the share incomes of the minors. The total short-levy of tax including penalty for concealment of particulars of income of the minors by the individuals amounted to Rs. 1,02,254.

The Ministry of Finance have accepted the mistake.

(iii) A transaction of loan implies an agreement to repay the money borrowed. The essence of a loan is a contract. It has been judicially held in October 1981 that there can be no loan from a father to a minor son, such a transaction is clearly unenforceable. Where money is transferred in the name of minor by way of interest free loan and the amounts are invested and interest is earned, the interest income is includible in the total income of the transferor under the clubbing provisions of the Income-tax Act.

An individual, who was a director in two private limited companies, transferred a sum of Rs. 1,00,000 during the previous year relevant to the assessment year 1973-74 and again a sum of Rs. 77,000 during the previous year relevant to the assessment year 1978-79 to his minor son as an interest-free loan, by debit to his deposit account with one of the companies. The minor son invested these amounts in two companies and earned interest and dividend. The interest and dividend earned had to be included in the total income of the assessee as income derived by the minor from assets transferred by the assessee to him. However, for the assessment years 1974-75 to 1978-79, the department assessed the income in the hands of the minor son instead of clubbing it with that of the assessee. The mistake resulted in short-levy of tax of Rs. 55,736 for the assessment years 1974-75 to 1978-79.

The Ministry of Finance have accepted the mistake.

3.15 *Income escaping assessment*

(i) Receipts of a capital nature are not assessable as income. Compensation receipts may be of revenue or capital nature depending upon their intrinsic character. That these are measured in terms of loss of profits is not important, what is important is whether the entire structure of the business is affected to such an extent that no business is left or done. If business is continued, any compensation paid for making up a certain loss of profits will be of the nature of income *vide* Commissioner of Income-tax Vs. M/s. Shamsher Printing Works (39 ITR 30) decided by the Supereme Court in March 1960.

The profit sharing ratio of an assessee (Hindu undivided family), a partner in a firm dealing in tractors manufactured by

another manufacturer, was reduced from 37 per cent to 22 per cent due to a change in the constitution of the firm during the accounting year relevant to assessment year 1978-79. The assessee received an amount of Rs. 2,59,000 from the incoming partners in lieu thereof. The payment of Rs. 2,59,000 by the incoming partners was on *ad hoc* basis and there was no evidence of a documentary and circumstantial nature to indicate that there had been any consideration other than the reduction of profit sharing ratio by the assessee. Applying the above ratio, as the assessee family continued in the same business, without any capital loss, but with reduced share percentage, the amount was in the nature of compensation for agreeing to reduction in share of profits and hence of revenue nature. The amount had not, however, been assessed to tax while assessing the income of the assessee for the assessment year 1978-79 in November 1980.

The omission to assess the said income of Rs. 2,59,000 to tax resulted in short-levy of tax of Rs. 1,54,790.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(ii) Under the Income-tax Act, 1961, all income accruing or arising to an assessee in India in a previous year relevant to the assessment year is includible in the total income of that assessee.

(a) An individual assessee was carrying on the business of manufacture of oxygen and other industrial-gases in his factory. The factory was leased out to a company for a period of three years from 1 April 1973, by an agreement dated 7 April 1973 on a rent of Rs. 11,000 per month. It was, however, observed that in the assessments for the assessment years 1976-77 to 1978-79, lease rent was returned and assessed at Rs. 72,000, Rs. 48,000 and Rs. 48,000 respectively thereby resulting in short computation of taxable income by Rs. 60,000, Rs. 84,000 and Rs. 84,000. The omission resulted in total under-charge of tax of Rs. 1,48,257, besides penalty for concealment of income.

While accepting the mistake for the assessment years 1976-77 and 1977-78, the Ministry of Finance have stated that the facts are being verified for the assessment year 1978-79.

(b) An individual, derived income from transport under a contract with the Food Corporation of India. The work on

behalf of the Corporation was carried on by the assessee at two different ports. For the assessment year 1977-78, the assessee filed a return of income pursuant to a notice issued by the department showing a net profit of Rs. 11,500. Since the assessee had not maintained any books of account and did not also produce any proof for the expenditure incurred, in the assessment completed in March 1980, the Income-tax Officer estimated the income as a percentage of receipts. The percentage adopted was eighteen and the same was applied on the amount of Rs. 2,30,009 received by the assessee for the contract work done in one port. The percentage of eighteen was subsequently reduced to fifteen in appeal in March 1981. It was noticed that the assessee had also received an amount of Rs. 7,16,453 for the contract work done in another port during the previous year relevant to assessment year 1977-78 and this fact was also communicated to the Income-tax Officer by the branch manager of the Corporation concerned. Yet these receipts were not brought to tax.

Applying the same percentage of fifteen as finally determined in appeal, on the contract receipts of Rs. 7,16,453 an income of Rs. 1,07,467 escaped tax with consequent under-assessment of tax of Rs. 99,772 including interest for belated submission of return.

The Ministry of Finance have accepted the mistake

(iii) An assessee, maintaining accounts on mercantile system, disclosed a turn over of Rs. 60.62 lakhs for the accounting year relevant to the assessment year 1979-80. However, it was noticed in audit (November 1981) that for the period from 1 October 1977 to 31 March 1978 forming part of the previous year relevant to the assessment year 1979-80, the assessee had been assessed to sales-tax by the commercial tax authorities of the State on a turn-over of Rs. 78.20 lakhs. The under statement of the turn-over to the extent of Rs. 17.58 lakhs resulted in short computation of income to the same extent for the assessment year 1979-80 involving a short levy of tax of Rs. 11,28,285 in the hands of the firm and its partners.

The Ministry of Finance have agreed to take remedial action.

3.16 *Irregular set-off of losses*

(i) Under the Income-tax Act, 1961, losses arising under the heads 'profit and gains of business' and 'capital gains', which

cannot be adjusted against other incomes in the assessment of same assessment year, are permitted to be carried forward to the following assessment years, for set-off against the respective income of those years, subject to certain conditions. Further, where full effect cannot be given to depreciation allowance in any assessment year for want of sufficient profits assessable for that year, the balance of unabsorbed depreciation can be carried forward and added to the amount of depreciation for the following years.

In the case of an individual, running a proprietory business, unabsorbed depreciation and business loss for the assessment year 1974-75 were determined in September 1979, as Rs. 11,14,318 and 'nil' respectively. A capital loss of Rs. 7,70,406 had been determined in March 1979, for being carried forward in respect of the assessment year 1972-73.

The assessment for the assessment year 1977-78 in which the carried forward amounts were finally set-off, was completed in September 1980 and revised in December 1980. The records of that assessment were produced for audit only in December 1982. Audit scrutiny then revealed the following :

(a) A total amount of Rs. 12,68,132 had been set-off in the assessments for the assessment years 1976-77 and 1977-78 on account of unabsorbed depreciation as against Rs. 11,14,318 actually determined for carry forward in the assessment for the assessment year 1974-75.

(b) An amount of Rs. 82,331 had been set-off in the assessment for the assessment year 1977-78 on account of business loss relating to the assessment year 1974-75 even though there was no such loss determined for carry forward in the assessment for the assessment year 1974-75.

(c) An amount of Rs. 8,45,306 had been set-off in the assessments for the assessment years 1973-74 to 1976-77 as carried forward capital loss as against the correct amount of Rs. 7,70,406, determined for carry forward on that account in respect of the assessment year 1972-73. The excess set-off of Rs. 74,900 reduced the taxable income by an equivalent amount for the assessment year 1977-78 in which the carried forward losses etc., of earlier assessment years were finally set-off.

These mistakes had resulted in total under-charge of income by Rs. 3,11,045 for the assessment year 1977-78 with a consequential tax effect of Rs. 2,05,290.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(ii) The benefit of carrying forward unabsorbed business loss to a subsequent year is subject to the condition that the business or profession for which the loss was originally computed is continued to be carried on by the assessee in the previous year in which the loss carried forward is adjusted.

A registered firm of two partners, engaged in the business of manufacturing rexine commodities, was incurring losses and was dissolved on 31 March 1977 (assessment year 1977-78). One of the partners took over its entire assets and liabilities. The other partner received a sum of Rs. 39,036 in full settlement and started a proprietory concern of buying and selling rexine goods. During the accounting year relevant to the assessment year 1978-79, he derived a total income of Rs. 2,03,870 from several sources. The department assessed (March 1981) him on a net loss of Rs. 1,48,603 after adjusting a loss of Rs. 3,52,473 being his share in the unabsorbed loss of the dissolved firm, for the earlier assessment year.

The set-off of the brought forward loss was incorrect, as the statutory pre-condition that the assessee should continue to carry on the business for which the loss was originally computed was not fulfilled. On the dissolution of the firm, the assessee's connection with the firm's business came to an end and he could not be said to carry on that business in the subsequent year. The dissolved firm was a manufacturing concern, whereas the assessee's new business was in a different line, namely, trading. That he used the knowledge, experience and capital of the dissolved firm would not make the new business the same as that of the firm for which the loss was originally computed. The irregular set-off, resulted in an under assessment of income of Rs. 2,03,870 and a short demand of tax of Rs. 1,16,750 for the assessment year 1978-79.

The Ministry of Finance have accepted the mistake.

(iii) Under the Income-tax Act, a non-resident assessee suffers tax only on income received, arising or accruing to him in India.

Since a non-resident is not taxable on any income arising outside India, he is not also eligible for set-off of losses arising outside India.

A Hindu undivided family was assessed as a non-resident for the assessment year 1977-78. In the assessment completed in October 1979 an amount of Rs. 28,699 representing the carried forward foreign loss was adjusted against the Indian income. The foreign income for the assessment year was not, however, considered as the assessee was assessed in the status of non-resident. Similarly, an amount of Rs. 19,967 being foreign loss, was set-off against Indian income in the assessment completed in December 1980, for the assessment year 1978-79. The mistakes resulted in excess set-off of loss of Rs. 48,666 with tax effect of Rs. 44,015.

The Ministry of Finance have accepted the mistake.

3.17 *Mistakes in giving effect to appellate orders*

(i) The Income-tax Act, 1961, provides for a deduction of 20 per cent of profits and gains derived by an assessee from new industrial undertaking established in backward areas.

In the case of a registered firm the assessment for the assessment year 1978-79 was completed in March 1981 allowing a deduction of Rs. 2,33,902 in respect of profits and gains derived by the firm from a new industrial undertaking established in a backward area. However, on appeal by the assessee, the appellate authority determined the admissible deduction as Rs. 4,63,538.

While giving effect (August 1981) to the appellate orders, the assessing officer deducted the entire amount (Rs. 4,63,538) determined by the appellate authority from the taxable income overlooking the fact that a deduction of Rs. 2,33,902 had already been allowed in the original assessment. This resulted in under-assessment of income by Rs. 2,33,902 and a short-levy of tax of Rs. 91,978 (including tax on partners).

The Ministry of Finance have replied that the mistake was in the appellate order and not in the assessment order and that the Income-tax Officer failed to seek rectification of the appellate

order. The Ministry have also reported that the firm's assessment has been rectified raising additional demand of tax of Rs. 54,432 and the partners' assessments were yet to be rectified.

(ii) In the assessments of two individuals for the assessment year 1978-79, completed in September 1981, addition of Rs. 1,27,040 in each case was made on account of unexplained investment in the construction of hotel-building. On an appeal preferred by the assessees, the Commissioner of Income-tax (Appeals) in his orders of April 1982, held that the unexplained investment be assessed in each case at Rs. 9,517, Rs. 45,207 and Rs. 46,546 in the assessment years 1976-77, 1977-78 and 1978-79 respectively. The Income-tax Officer while redetermining (30 April 1982) the income, pursuant to the appellate orders, allowed relief to the assessees for the assessment year 1978-79 but did not reopen the assessments in respect of the assessment years 1976-77 and 1977-78 to bring to tax the unexplained investments for these years. As a result, income of Rs. 54,724 escaped assessment in each case, leading to short levy of tax aggregating to Rs. 65,272.

The paragraph was sent to the Ministry of Finance in August 1983; their reply is awaited (December 1983).

3.18 *Irregular exemptions and reliefs*

(i) Chapter VI A of the Income-tax Act, 1961, provides for certain deduction to be made from the gross total income. The overriding condition is that the total deduction should not exceed the gross total income of the assessee. 'Gross total income' has been defined as the total income computed in accordance with the provisions of the Act before making deductions under Chapter VI A. Set-off of unabsorbed losses of earlier years being an anterior stage, it follows that where such set-off results in reducing the total income to 'nil' no deductions under Chapter VI A are admissible.

The total income of a co-operative society for the assessment year 1980-81 was determined (assessment completed on 1 May 1981) at Rs. 1,00,103 after allowing a deduction of Rs. 3,55,557 (Rs. 3,48,857 being relief admissible to cooperative societies and Rs. 6,700 towards relief on donation under Chapter VI A *ibid*). The assessment was subsequently rectified in July 1981, on the ground that the assessee had carried forward losses and

unabsorbed depreciation amounting to Rs. 11,60,421 from the assessment year 1979-80, reducing the total income to nil, with an absorbed depreciation and carried forward loss of Rs. 10,60,318.

Since the deduction under Chapter VI A would be admissible only where there is a positive gross total income deduction of Rs. 3,55,557 which was allowed even in the rectificatory order, resulted in excess carried forward of loss to that extent.

The Ministry of Finance have accepted the mistake.

(ii) In computing the total income of an assessee, a deduction is allowed on account of any interest paid on moneys borrowed for payment of any tax due under the Income-tax Act, 1961.

In the assessments of an individual for the assessment years 1976-77 to 1980-81, the department allowed deduction for a total sum of Rs. 2,76,627 towards interest paid on moneys claimed to have been borrowed for payment of taxes due.

The above assessments resulted in granting of refunds to the assessee as taxes already deducted at source exceeded the tax leviable on assessment. No advance tax was paid except in one year. Further, the assessee did not have any outstanding tax liability for any earlier assessment year also. It was also noticed from the wealth tax records that interest of Rs. 88,339 was paid by the assessee on borrowed money during the assessment year 1980-81 but the borrowed money was actually utilised by him for purchase of agricultural lands. The deductions allowed for interest paid on moneys claimed to have been borrowed for payment of income-tax will not, therefore, be admissible. The incorrect allowance resulted in under-charge of tax of Rs. 1,34,318 during the five assessment years 1976-77 to 1980-81.

The Ministry of Finance have accepted the mistake.

(iii) Under the Income-tax Act 1961, co-operative societies enjoy certain tax concessions in respect of their income. The Finance Act (No. 2) 1971, introduced a new provision exempting from tax the business income of labour co-operative societies which arises from the collective disposal of the labour of its members. The concession would be admissible only to those

co-operative societies which restrict voting rights to members constituting the labour force, the State Government and co-operaive societies providing financial assistance.

An assessee, a labour co-operative society claimed exemption under the above provision to the extent of Rs. 29.48 lakhs for the assessment year 1976-77. The Income-tax Officer, in the draft assessment order sent for approval of the Inspecting Assistant Commissioner, worked out the business income entitled to exemption as Rs. 43,807 being 1.6 per cent of the gross total income. The Inspecting Assistant Commissioner held that 63.88 per cent of the profit was earned because of participation of the members and accordingly arrived at a figure of Rs. 17,49,003 applying the above percentage to the gross total income as entitled to exemption. However, the gross total income of the assessee underwent a change on account of adjustment of carry forward depreciation etc., in the final assessment order. Also, the said income included dividends, interest and income from property which are incomes assessed under heads other than business income and for which exemptions were claimed under the other provisions of the Act governing such incomes. The failure of the department to apply the percentage of profit approved by the Inspecting Assistant Commissioner to the gross total income as arrived at in the final assessment order after excluding the income relatable to dividends, interest and property resulted in excess relief of Rs. 1,74,094 with consequent under assessment of tax of Rs. 76,601 for the assessment year 1976-77. Similarly, for the assessment year 1977-78, the failure to apply the percentage of profit *viz.*, 69.05 per cent which was held as attributable to members, to the business income only included in the gross total income after exclusion of the income assessable under other heads, resulted in excess relief of Rs. 91,484 with consequent under assessment of tax of Rs. 40,252. The aggregate short levy of tax for both the assessment years 1976-77 and 1977-78 amounted to Rs. 1,16,853.

The Ministry of Finance have accepted the mistake.

(iv) Under the provisions of the Income-tax Act, 1961, income derived by statutory marketing authorities from letting out of godowns or warehouses for storage, processing or facilitating the marketing of commodities is not to be included in the total income computed in respect of such authorities.

In computing the total income of a registered firm for the assessment years 1978-79, 1979-80, 1980-81 and 1981-82 incomes amounting to Rs. 91,341, Rs. 40,678, Rs. 61,526 and Rs. 42,966 respectively from letting out of godowns were treated as exempt as claimed by the assessee. Since the assessee was not an authority constituted under any law for the purpose specified in the Act, the exemption allowed was not correct. The mistake resulted in short-charge of tax amounting to Rs. 86,720 in the case of the assessee firm, for the four years and its three partners for three years (assessments of partners for the year 1981-82 were not finalised).

The Ministry of Finance have accepted the mistake.

3.19 *Incorrect allowance of relief in respect of newly established undertaking*

Where the gross income of an assessee includes any profits and gains from small scale industrial undertaking established in rural areas, a deduction of 20 per cent of profits derived from such undertaking is allowed in computing taxable income. An industrial undertaking is deemed to be a small scale industrial undertaking, if the aggregate value of the machinery and plant installed on the last day of the previous year ending before August 1980 does not exceed rupees ten lakhs.

In the assessment of an industrial undertaking (a registered firm) for the assessment year 1980-81 (previous year ending 30 September 1979), a deduction of Rs. 90,385 was allowed even though the value of the machinery and plant installed as on the last day of previous year exceeded rupees ten lakhs. The undertaking was, not small scale industrial undertaking and was not eligible for the incentive. The mistake resulted in short-levy of tax of about Rs. 64,640 in the hands of the firm and its partners.

The Ministry of Finance have accepted the mistake.

3.20 *Short-levy or non-levy of interest/penalty*

Under the provisions of the Incomt-tax Act, 1961, where the return for an assessment year is furnished after the specified date, the assessee is liable to pay interest at the prescribed rates from the day immediately following the specified date to the date of furnishing the return on the amount of tax payable on

the total income as determined on regular assessment, as reduced by the advance tax, if any, paid, and any tax deducted at source. The Act further provides that for calculation of interest in the case of a registered firm, the tax payable on the total income shall be the amount of tax which would have been payable if the firm had been assessed as an unregistered firm.

At the time of finalising the assessment of firm for the assessment year 1974-75 in March 1978, the Income-tax Officer noticed that the assessee had taxable income for the assessment year 1973-74 also and had failed to furnish the return for that year. Accordingly, the Income-tax Officer issued a specific notice (in April 1978) to the assessee to furnish the return for the assessment year 1973-74 which the assessee filed in December 1979. The assessment for the assessment year 1973-74 was originally completed on 30 August 1980 and subsequently rectified on 17 March 1982. While calculating the interest leviable for belated submission of the return, the Income-tax Officer levied interest calculating the period from the last date stipulated as per his notice to the assessee to furnish the return *viz.*, 20 April 1978 to 4 December 1979 instead of from 1 April 1973 to 4 December 1979 and also calculated the interest on the amount of tax payable by the assessee as a registered firm instead of the tax payable as an unregistered firm. This resulted in short-levy of interest amounting to Rs. 79,838.

The Ministry of Finance have, while accepting the mistake, reported that additional demand of tax of Rs. 79,838 has been raised in June 1983.

3.21 *Avoidable payment of interest due to failure to make provisional assessment*

Under the Income-tax Act, 1961, where an assessee claims that the aggregate tax paid at source or in advance exceeds the tax payable on the basis of the return filed by him and the Income-tax Officer is of the opinion that regular assessment is not likely to be made within a period of six months from the date of furnishing the return, the assessing authority shall proceed to make in a summary manner, within the said period of six months, a provisional assessment of the sum refundable to the assessee after making the necessary adjustments. The Act further provides that where advance tax paid by an assessee exceeds the tax determined by the department on regular

assessment, interest on such excess is payable by Government from the 1 April of the assessment year to the date of regular assessment. In case, however, any part of such excess had been refunded on the basis of a provisional assessment no interest is payable on such part after the date of such provisional assessment.

An assessee firm and its seven partners filed returns of income for the assessment year 1979-80 in May 1979. The assessees requested in October 1979 for a provisional assessment being made for refund to them of taxes overpaid. The assessing officer, however, did not make the provisional assessments till January 1981. This inordinate delay in violation of the provisions of the Act, entailed avoidable payment of interest of Rs. 1,77,971 for the period December 1979 to December 1980.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

OTHER TOPICS OF INTEREST

3.22 *Loss of revenue due to non-completion of assessments in time*

Under the provisions of the Income-tax Act, 1961, an assessment has to be completed within two years from the end of the relevant assessment year or within one year of submission of a revised return of income whichever is later. The time taken in obtaining directions of the Inspecting Assistant Commissioner (not exceeding one hundred and eighty days commencing from the date of forwarding the draft assessment order to the assessee by the Income-tax Officer) is to be excluded for computing this period.

A registered firm filed revised return of income for the assessment year 1972-73 on 12 March 1975 and return for the assessment year 1974-75 on 29 July 1974. The Income-tax Officer forwarded draft assessment orders for the two years to the assessee for acceptance on 11 March 1976 and 26 March 1977. The orders of the Inspecting Assistant Commissioner were received by the Income-tax Officer on 14 July 1977 for the assessment year 1972-73 and on 27 September 1977 for the assessment year 1974-75. Taking into account, the period

which was to be excluded for computing the period of limitation, assessments for the two years were required to be completed by 15 July 1976 and 27 September 1977. But the Income-tax Officer completed the assessment for the assessment year 1972-73 on 22 July 1976 and that for the assessment year 1974-75 on 28 September 1977 on total incomes of Rs. 6,52,590 and Rs. 4,49,764 respectively. On appeal by the assessee against the assessment orders, the Commissioner (Appeals) nullified the assessments (5 December 1978 and 27 September 1978) as having been made beyond the prescribed periods of limitation. The Income-tax Appellate Tribunal also confirmed (March 1980) the decision of the Commissioner (Appeals). Thus, non-completion of assessments in time resulted in loss of revenue of Rs. 3,73,896 including that in the case of partners.

The assessment records were not produced for audit till the audit for 1981-82 was taken up in February 1983 when only the above position was brought to notice.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

3.23 *Omission to club income arising from the converted Hindu undivided family property*

Under the provisions of the Income-tax Act, 1961, as amended from 1 April 1976, where an individual converts his personal property into property belonging to Hindu undivided family at any time after 31 December 1969, the entire income arising from such converted property is to be clubbed with the other income of that individual assessee.

An assessee individual transferred his capital balances in certain firms on 31 August 1971, to the Hindu undivided family comprising self, wife and two major sons. The entire income derived from the converted property was to be clubbed with the other income of the assessee. The department, however, continued to assess only 50 per cent of the income derived from the converted property in the hands of the individual during the assessment years 1976-77 to 1979-80 instead of the whole of such income. The omission resulted in under-assessment of income by Rs. 3,65,820 for the assessment years 1976-77 to 1979-80.

The Ministry of Finance have accepted the mistake and stated that additional demand of Rs. 76,641 has been raised.

3.24 *Irregular collection of amounts to make good the shortfall of budget estimates*

Under the provisions of the Income-tax Act, the department is authorised to collect from an assessee only such sums as are due to Government on the basis of a statutory notice quantifying the demand. The department is not auhorised to make any collections when no demand is raised or outstanding. In para 55(d) of Audit Report on Revenue Receipts, 1967 cases of irregular collection of amounts from assessees to make good the shortfall of budget estimates were reported. In para 2.145 of the 29th Report (Fourth Lok Sabha) the Public Accounts Committee took a serious view of the device adopted by the Income-tax Officers to fulfil the budget targets. In para 2.18 of their 76th Report (Fourth Lok Sabha) the Public Accounts Committee advised the Central Board of Direct Taxes to keep a special watch in this connection. Similar cases were also reported in para 35(ii) of the Audit Report on Revenue Receipts 1971-72. The Central Board of Direct Taxes in their instructions dated August 1973 viewed recurrence of this practice of irregular collections with extreme displeasure.

During the local audit of an Income-tax Office in July 1982 it was seen that a sum of Rs. 5,50,000 was collected from eight assessees on the last date of the financial year 1980-81 though as per the assessments completed earlier the demand of tax totalled Rs. 8,441 in three cases and in the remaining cases a refund of Rs. 19,044 was involved. The Income-tax Officer refunded a sum of Rs. 5,60,603 on 2 April 1981 after adjusting the demand of Rs. 8,441. Thus, the amounts were got deposited only for the purpose of making good the shortfall in budget estimates with reference to the actual tax collections for the year 1980-81 in the ward.

The Ministry of Finance have accepted the mistake and stated that the amount paid in by the assessees having been refunded, no remedial action was called for.

3.25 *Non-observance of the provisions of the law relating to contractors*

3.25.01 Under the Income-tax Act, 1961, read with the rules framed thereunder, where any contractor enters into a contract with any other person for construction of buildings or supply of goods or services in connection therewith, the value of

which exceeds Rs. 50,000, he shall within one month of entering into contract furnish to the assessing authority, particulars of the contract in the prescribed form. The provision originally made in 1964 in respect of building contracts was, in 1966, extended to all contracts for carrying out any works, and for supply of goods and services in connection therewith. In the event of failure to furnish such particulars, the Commissioner of Income-tax may impose a fine not exceeding Rs. 50 for each day of default subject to a maximum of 25 per cent of the value of the contract.

Every person responsible for paying any sum to a resident for carrying out any work (including supply of labour for carrying out such work) in pursuance of a contract of the value of more than Rs. 5,000 (Rs. 10,000 with effect from 1 June 1982) between the contractor and Government or a corporation established by law or a company or a co-operative society is required to deduct an amount equal to two per cent of such sum as income-tax at the time of making payment in cash, by cheque or draft or by any other mode. Similarly, when payments are made to a sub-contractor by a contractor, tax is deductible at source at the rate of one per cent of such payments. The tax so deducted has to be credited to Government within one week from the last day of the month in which the deduction is made. Omission to deduct, or after deduction to remit the tax to Government account, entails levy of penal interest and penalty. The person deducting the tax is required to send to the Income-tax Officer having jurisdiction to assess him a quarterly return on 15 July, 15 October, 15 January and 15 April, in respect of deductions made by him during the immediate preceding quarter.

3.25.02 The provision relating to the filing of statutory statement referred to above has been enacted as an anti-tax evasion measure. So also is the provision regarding deduction of tax at source. The Direct Taxes Enquiry Committee (December 1971) had found that the department faced considerable difficulties in tracing contractors after they obtained payments for work done and to levy and realise tax from them. The Committee had accordingly, recommended :

> "With the accent of development in our planning, large scale governmental and public sector projects are executed through contractors all over the country and there is considerable scope for leakage of revenue. We are also aware of the wide-spread practice of obtaining

contracts in benami names. In these circumstances, the solution to the problem is deduction of tax at source from payments to contractors."

3.25.03 The details of tax collected through deduction at source and the part thereof deducted from payments to contractors and sub-contractors during the five years 1978-79 to 1982-83 are as under :—

Year	Total collection of tax through deduction at source.	Deduction from payments to contractors and sub-contractors.	Percentage of column 3 to column 2
	(In crores of rupees)		
(1)	(2)	(3)	(4)
1978-79	528.48	59.43	11.24
1979-80	643.06	77.94	12.12
1980-81	745.23	104.48	14.02
1981-82	845.18	124.70	14.75
1982-83	970.60*	139.52	14.37

3.25.04 The omissions or delays in rendering statutory statements of particulars by contractors and inaction on the part of the department to initiate penalty proceedings for such defaults were commented upon in para 49 of the Audit Report 1976-77. Omissions to deduct tax at source from payments made to contractors/sub-contractors and failure to institute penal/prosecution proceedings against the defaulters were also commented upon in that para. Considering the fact that payments to contractors all over the country were quite substantial and the tax deduction at source was not being given the attention that it deserved, the Public Accounts Committee recommended that the Board should take up the matter with the Government departments, particularly the Central and State Public Works Departments and devise procedures to obviate the possibility of leakage of revenue on this account. Reporting the action taken by the Government on the recommendation, the Ministry of Finance apprised the Committee in November 1978 that a working group had been constituted in September 1977 with a view to making efficient administrative arrangements for management of various functions relating to tax deduction at source and the report of the group was under consideration

*Figures furnished by the Ministry of Finance are provisional.

of the Central Board of Direct Taxes. The Committee desired to be informed of the conclusive action taken by October 1979 (paras 7 and 8 of Public Accounts Committee's 142nd Report—1978-79—Sixth Lok Sabha). The Ministry of Finance have not sent any further intimation (December 1983).

3.25.05 A test check was conducted in a few selected income-tax wards in some of the Commissioner's charges to find out the extent of compliance with the provisions of the law in this regard. The results of this test check are given in the following paragraph·

(A) Statutory statements of particulars.

(i) Omission to file statutory statements of particulars by contractors

In 98 income-tax wards, in 33 Commissioners' charges, it was noticed that in 571 cases relating to the years 1974-75 to 1982-83 the statutory statements were not filed by the contractors for periods ranging from 28 to 2,922 days (upto the date of audit) but no action had been initiated by the department either to call for the statutory statements or to invoke the penal provisions of the law. The amount of maximum fine leviable for the default in these cases amounted to Rs. 5.18 crores.

In a ward in another Commissioner's charge, though the value of bills received for works done by ten contractors aggregated Rs. 24,805 lakhs, neither the prescribed statements were filed nor were the provisions invoked.

In a ward in Bihar, the number of contractors, as per the departmental books, was 1729 for the financial years 1979-80 to 1981-82. The statutory statements were filed by 32 contractors only. When the omission to take action for such widespread non-compliance with the provision was pointed out, the Commissioner of Income-tax stated (February 1983) that after the introduction of the system of tax deduction at source from 1972 the requirement of filing statutory statement of particulars had been reduced to a mere technical formality.

(ii) Omission to levy fine for delay in submission of statutory statements of particulars.

In twenty seven income-tax wards spread over 10 Commissioners' charges, in 141 cases, statutory statements were received

after delays ranging from 8 to 3,994 days during the years 1978-79 to 1982-83. The department did not initiate penal action for levy of fine for belated submission of the statements as required under the law. The maximum fine leviable in these cases as per scales laid down in the Act would be Rs. 46 lakhs.

(iii) Miscellaneous :

In six income-tax wards lying in 4 Commissioners' charges, it was noticed that statutory statements of particulars were received from 61 contractors. The total value of their contracts entered into between March 1979 and March 1983 was Rs. 7.09 crores. The names of these contractors were not borne on the departmental records. The contractors did not file their returns of income. The department also did not initiate action to call for the returns to assess the incomes arising from these contracts.

(B) Deduction of tax at source.

(i) Omission to file quarterly returns of tax deducted at source or belated filing of returns.

From the credits given for tax deducted at source in the assessments of contractors, it was noticed in 30 income-tax wards in 7 Commissioners' charges that in 227 cases relating to the years 1977-78 to 1982-83, the disbursing authorities had not filed quarterly returns of tax deducted at source. No penal action was taken by the department on the disbursing authorities for such omissions.

(ii) Omission to deduct tax at source/delay in remittance of tax deducted.

(a) In two cases in a ward in Maharashtra where assessments were made between February 1978 and December 1981, tax of Rs. 1,02,547 was not deducted at source. Penal interest of Rs. 29,245 upto the date of assessment was not charged on the disburser for the omission.

(b) Six persons in Orissa charges who had deducted a sum of Rs. 1.19 lakhs in 63 cases during the previous years relevant to the assessment years 1979-80 and 1980-81 remitted the amount to government account after delays ranging upto 369 days. No action was taken by the department to levy penal interest and penalty for the default.

(c) In a ward in Madhya Pradesh, the quarterly returns received in 32 cases revealed that the figures shown therein as taxes deducted at source did not tally with the taxes deducted at source as per the certificates attached to the income-tax returns filed by the contractors for the assessment years 1980-81 to 1982-83. The credits afforded in the assessments as per the certificates produced by the assessees were for Rs. 2.77 lakhs whereas the quarterly returns filed by the disbursers available in the assessment records showed credit of Rs. 0.58 lakhs only. The department merely stated that the figures shown in the returns were for each quarter whereas the figures shown in the tax deduction certificate were for one year and the two would never tally. If the correlation is not feasible, the receipt of quarterly returns from the disbursers would appear purposeless.

(C) Systems defects.

(i) The statutory statements as and when received from contractors in various wards were kept in separate bundles alongwith other different types of records and not with the assessment records of the individual contractors (except in some stray and isolated cases). The statements were neither filed nor arranged, nor indexed in any register to facilitate easy link up with the tax returns.

In fact no system had been evolved by the department either to watch the receipt of statutory statements of particulars from contractors or to initiate action in cases of non-compliance or belated compliance with the legal requirements. No guidelines had also been framed for making use of the particulars in the statement filed by the contractors.

(ii) No system had also been evolved by the department to watch the receipt of quarterly returns of tax deducted at source, to initiate follow up action in cases of non-receipt or to make use of the particulars contained in the returns as and when received.

(iii) The quarterly return showing the tax deducted at source from payments made to contractors/sub-contractors in the prescribed form has to be filed by the disburser with the Income-tax Officer having jurisdiction to assess him. In respect of work done for Central/State Government departments, even though tax is deducted at source while making payments, as disbursers, the Central/State Government departments are not required to file the prescribed quarterly returns being entities not assessable

under the Income-tax Act. This renders correlation of tax deducted at source with the assessment of income, impossible. In such circumstances, escapement of income from tax cannot be ruled out.

(iv) Where a contractor and the person making payments to him and deducting tax therefrom come under separate jurisdictions, there was no system evolved by the department to correlate the particulars in the statutory statement filed by the contractor with the quarterly returns filed by the person making payments to him and *vice versa* to ensure that no income escapes assessment. The lack of such system also implies failure to verify the correctness of the credits given for taxes deducted at source as per the certificates produced by the contractor with the taxes deducted at source as shown in the quarterly returns filed by the persons making payments.

3.25.06 Conclusions.

The statutory statements of particulars from contractors are intended to furnish data or material to enable the Income-tax Officer to cause an inquiry to be made in good time with a view to finding out whether a particular building which is intended to be put up is to be constructed with monies, the source of which is detectable. The provision is enacted for tracking down persons who are believed to have evaded payment of tax on their income. Arrangements to receive the statements, to properly record and systematically shift and analyse them and initiate further action on the basis of the results thrown out, appear to be completely absent. Timely non-detection of omission to render the statements by contractors and non-initiation of penal proceedings, point to the need for stricter enforcement of the provisions of the law. Similarly, receipt of quarterly returns from disbursing authorities about payments made to contractors, taxes deducted and credited to government account, is not closely watched and penal provisions resorted to wherever necessary. Returns received are also not made use of for detecting income that escaped assessment, if any, or even to reconcile the taxes deducted at source with those given credit in the assessments.

3.25.07 The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

3.26 *Working of a Film Circle*

3.26.01 In their 91st Report (1981-82), the Public Accounts Committee (Seventh Lok Sabha), recommended *inter alia* a review of the method of allowing the cost of production/ distribution rights of feature films. The Committee desired that a Study Group consisting, among others, of experts in taxation, accountancy and audit and eminent non-officials having intimate knowledge of the operations of the film industry should be set up to make an indepth study to devise ways and means to curb the growing tendency to funnel large amounts of un-accounted money into star studded-films and to ensure that the interests of revenue are adequately protected.

3.26.02 The Committee also recommended initiation of legistlative measures for regulating the deferred annuity scheme not only in regard to film artistes but also in respect of other professionals so that revenue is not in jeopardy. The Committee further urged a thorough and critical evaluation of the usefulness and effectiveness of film circles with a view to streamlining their functioning.

3.26.03 Some aspects of working of the Film Circle, Bombay were reviewed in audit in March—May 1983. The results of this review are given below :—

With a view to ensuring proper co-ordination and enforcement, cases of all producers, distributors, film artistes, film editors, exhibitors, camera-men, movie-art and dance directors, film financiers and others connected with the film industry in Bombay were centralised in the Film Circle which came into existence in 1964.

The circle is headed by a range Inspecting Assistant Commissioner, supervising the work of 10 Income-tax Officers and other complementary staff like Inspectors. From 1979, one Inspecting Assistant Commissioner (Assessment) is also associated with the assessment work. The Commissioner of Income-tax III exercises jurisdiction over the Circle and the two Inspecting Assistant Commissioner's ranges.

Cases of some assessees which require investigation have been assigned to Income-tax Officers in central circles, under the jurisdiction of the Commissioner of Income-tax (Central).

3.26.04 No. of films produced.

The numbers of films certified for exhibition by the Bombay Regional Office of the Central Board of Film Censors during the last five years were as follows :—

Year	No. of pictures
1978.	172
1979.	178
1980.	201
1981.	206
1982.	210

3.26.05 No. of assessees.

The numbers of assessees borne on the records of the department category-wise, as on March ending, from 1980 to 1983 were as follows :—

Category	As on 31 March 1980	As on 31 March 1981	As on 31 March 1982	As on 31 March 1983
Film Financiers	41	65	105	14
Producers	310	371	393	327
Distributors	244	299	394	174
Artistes	454	511	546	379
Others	5,624	5,946	5,769	5,076

3.26.06 No. of assessments completed/pending.

The numbers of assessments completed during the year 1982-83 and those pending on 1 April 1982 and 31 March 1983 were as follows :—

Tax	Pending as on April 1 1982	Completed during 1982-83	Pending as on 31 March 1983
Income-tax	7,563	5,282	7,464
Wealth-tax	2,465	830	2,441
Gift-tax	122	44	93

3.26.07 Demand, collection and arrears of tax.

The table below shows the arrears of demand of tax at the commencement of the year, the demand made during the year 1982-83, the tax collected and the balance outstanding as on 31 March 1983 (as furnished by the department) :—

Nature of tax	Demand outstanding as on 1 April 1982	Demand made during 1982-83	Total	Demand collected during 1982-83	Demand outstanding on 31 March 1983	Demand outstanding on 31 March 1983 as reported by the department.
			(In lakhs of rupees)			
1	2	3	4	5	6	7
Income-tax . .	887	1,209	2,096	471	1,625	1,189
Wealth-tax . .	146	63	209	28	181	140
Gift-tax . .	7	3	10	—	10	5
Total . .	1,040	1,275	2,315	499	1,816*	1,334*

3.26.08 The Income-tax Act provides that a film producer should file with the Income-tax Officer concerned a statement in Form 52 A for each financial year or part of it till completion of production, showing particulars of all payments of over Rs. 5,000 in the aggregate made by him or due from him. This statement is to be filed within 30 days from the end of the financial year during which the production of film is carried on or within 30 days from the date of completion of the film whichever is earlier. It is intended as a check on the tendency on the part of film producers to inflate the cost of production of pictures likely to be a grand success fetching huge profits.

In 15 out of 16 cases test checked in audit the said annual statements were not filed by the producers, though they had indicated the total cost of production in the returns of income. In one case where the statutory statement was filed by a producer, it was noticed that the total cost of the film as returned

*The difference of Rs.482 lakhs (Rs. 1,816—1,334) remains to be reconciled.

was Rs. 1.22 crores and the total payments of over Rs. 5,000 in the aggregate made during the financial years 1979-80 to 1981-82 were only Rs. 18.29 lakhs, *i.e.*, the percentage of the payments exceeding Rs. 5,000 in the aggregate to total cost worked out to fifteen.

The penalty prescribed in the Act for omission to file the statutory statement by the due date may extend to Rs. 10 for every day during which the failure continues. The quantum of penalty even over a long period of delay would be very nominal, compared to the huge cost of production of a film. The following table brings out the number of producers who had not filed the statutory statement and number of cases where penal action was initiated and the amount of penalty levied.

Year	No. of producers who had filed the statement belatedly	No. of producers who had not filed the statement	No. of producers in whose cases penal action was taken	Amount of penalty levied and the No. of cases
1976-77 . . .	11	10	3	Rs. 2,500 (2 cases)
1977-78 . . .	51	4	11	Rs. 5,620 (5 cases)
1978-79 . . .	19	10	5	(Rs. 1,650 (4 cases)
1979-80 . . .	24	20	6	(Nil (one case)
1980-81 . . .	28	5	7	Rs. 9,840 (3 cases)

3.26.09 In a note furnished to the Public Accounts Committee about the system followed to check the correctness of returns filed by film artistes in October 1981, the Ministry of Finance had stated that since all the top producers were assessed in Films circles, in important cases, receipts shown by the artistes were cross-verified with the producers' cases and with the statements filed by the producers under section 285B.

An attempt was made in audit to reconcile the payments made by the producers to various artistes, etc., in respect of a few films with the receipts shown in the returns of the artistes.

The reconciliation was found to be impracticable due to the following reasons :—

(a) While the producers maintained their accounts on mercantile basis, the artistes maintained their accounts on cash basis. The different systems of accounting would require correlation of receipts and payments over a number of years. No such correlation was made in the wards.

(b) The accounting years of producers and artistes were different.

(c) In most cases, the producers did not furnish artiste-wise and picture-wise details indicating the total amount of remuneration/fees payable as per agreement, the amount actually paid by cheques or through annuity, dates of payments and balance of amount payable. Similarly, the artistes also did not file vital details like date of contract, contract money and date of release of picture, name of the film producer, particulars of annuities received, etc. The assessing officers also did not obtain necessary details from producers and artistes and keep them on record.

Despite the aforesaid limitations, the following discrepancies were noticed in a test check of the records of 16 pictures :—

(a) The particulars of amounts due to a director from the producers in a case as per the producer's records and the amounts received by the director as per his records, available in the assessment records showed the following :—

As per producers account			As per director's account	
Assessment year (previous year ended)	Amount due	Balance shown as outstanding under sundry creditors	Assessment year (previous year ended)	Receipts included in the return
1978-79 (30 June 1977)	—	LIC annuity 3,36,848	1979-80 (31 March 1979)	1,25,000
1979-80 (30 June 1978)	—	Remuneration 16,55,193	1980-81 (31 March 1980)	1,25,000
1980-81 (30 June 1979)	Over flow share 35 per cent 5,27,901	2,40,808	1981-82 (31 March 1981)	32,000
1981-82 (30 June 1980)	-do- 3,95,819	6,24,715	1982-83 (31 March 1982)	1,50,000

As the system of accounting and the period of accounting of the producer and the director differed, a reconciliation could not be effected.

(b) A partnership firm consisting of family members produced a film at a total cost of Rs. 3.03 crores and the film was released in August 1975. A private limited company also consisting of the family members of the producer as shareholders, was appointed in August 1975 as distributor of the film for the Bombay circuit for a period of 11 years. As per the terms and conditions, the distributors were to spend, on behalf of the firm, upto Rs. 3 lakhs towards pre-release and release publicity of the film and in consideration of the service, the distributors were entitled to a commission of 10 per cent on the net realisation of the said film.

The total realisations from the picture as shown by the distributors in their books for the period ending 30 September 1977 and by the producers in their books as at the end of 31 December 1977 were as below :—

Distributors Accounts		Producers Accounts	
Period	Amount (Rupees)	Period	Amount (Rupees)
As on 30 September 1976	53,64,341	As on 31 December 1976	55,11,496
1 October 1976 to 30 September 1977	24,72,868	1 January 1977 to 31 December 1977	16,05,587
As on 30 September 1977	78,37,209	As on 31 December 1977	71,17,083

The producers' account in the books of the distributor for the year ending 30 September 1976 showed a credit balance of Rs. 0.61 lakh *i.e.* amount payable to the producer. However, the opening balance on 1 October 1976 was shown as debit of Rs. 14.95 lakhs, *i.e.*, amount receivable from the producer. In the books of the producer, the total amount of collections in respect of the picture from various distributors for the previous year relevant to the assessment year 1978-79 was indicated as Rs. 14.43 lakhs against the distributing company for the Bombay circuit. However, in the ledger account of the distributing company responsible for collections in the territory for the same period, amount collected was indicated as Rs. 16.06 lakhs.

The discrepancies in the figures of realisations in respect of the same film as recorded in the producers' books and distributors' books and the amounts due to the producer and *vice versa* were not reconciled.

3.26.10 In para 1.68 of their 91st Report (Seventh Lok Sabha), the Public Accounts Committee called for a review of the scheme of amortisation laid down in Rules 9A and 9B of the Income-tax Rules. Rule 9A prescribes procedure for amortisation of expenditure on production of feature films. When a film producer sells the rights of exhibition of a feature film for all territories specified in sub rule 11 of Rule 9A along with table in it, he is allowed to deduct the entire cost of production while computing the profits and gains of the business of production of the feature film. The sale of exhibition rights does not always conform to the classification of territories and the Income-tax Officers have been given discretion in the matter of allowing reduced deduction in such cases. The Income-tax Officers, however, had allowed full deduction even when sale of exhibition rights to only part of the territories was made by the producers to the distributors. A few instances are given below :

(i) As per Income-tax Rules, amortisation of cost of production is allowed at 17 per cent if the exhibition rights are sold for the territory comprising the whole of the States of Assam, Bihar, Manipur, Meghalaya, Nagaland, Orissa, Tripura, Sikkim, West Bengal, the whole of the Union Territories of Andeman and Nicobar Islands, Arunachal Pradesh and Mizoram. Similarly, amortisation is allowed at the rate of 8 per cent if the exhibition rights are sold for the territory comprising the whole of the States of Haryana, Himachal Pradesh, Jammu & Kashmir, Punjab and the Union Territory of Chandigarh. Amortisation is allowed at 17 per cent if the exhibition rights are sold for the territory comprising districts of Ahmednagar, Greater Bombay, Cellaba, Kolhapur, Nasik, Pune, etc., the whole of the State of Gujarat, some districts in Karnataka and the Union Territories of Dadra, Nagar Haveli, etc.

(a) In the case of a film, the cost of production of which was Rs. 1.28 crores and the date of release was 24 August 1979, amortisation was allowed at 17 per cent and 8 per cent even though, the exhibition rights were sold only for a part of the territory, namely, Bengal and East Punjab respectively.

(b) In the case of another film, the cost of production of which was Rs. 60.21 lakhs, the exhibition rights were sold only for a part of the territory, namely, Bombay. However, full amortisation at 17 per cent was allowed. The same mistake as in (a) was committed in this case also.

The grant of amortisation in full, though the distribution rights were sold only for a part of the territory resulted in excess amortisation allowance leading to short-levy of tax.

(ii) On of the methods of transferring the distribution rights of the films is to sell them for a fixed period of years. The producer has nothing to do with the profits or losses on the film except that the distribution rights will revert to the producer after the expiry of the stipulated period. Distribution rights of many of the highly successful films have good resale value. To quote a film weekly old pictures like "Phool Aur Pathar", "Ek Phool Do Mali", "Roti Kapada Aur Makaan", "Talash" and "Gumnam" released—recently in Bombay were doing bumper business. The department has no system to watch whether income from sale of distribution rights of such old films was returned and charged to tax. The value of rights of such old pictures is also neither returned by the producers nor assessed by the department for the purposes of levy of wealth tax.

3.26.11 The Direct Taxes Enquiry Committee (December 1971) observed that one of the devices which tax dodgers often adopt to escape proper liability to tax and penal consequences is to take shelter behind the plea that no accounts have been maintained and recommended insertion of a statutory provision in the Income-tax Act requiring maintenance of accounts by all persons in professions and by businessmen having income above a certain monetary level. An enabling provision was incorporated in the Act through the Taxation Laws Amendment Act, 1975 effective from 1 April 1976 providing therein that the books of accounts and other documents required to be maintained would be prescribed by rules. In para 1.78 of their 91st Report (Seventh Lok Sabha), the Public Accounts Committee noted that the books of the accounts required to be maintained from 1 September 1982 were specified as late as in December 1981, *i.e.*, only after the matter was raised by the Committee, though the enabling provision had been inserted in the Act from

1 April 1976. The Income-tax Rules have thereafter been amended in 1983 requiring the assessees to maintain the prescribed books of accounts with effect from 1 March 1983.

3.26.12 In his Report "Indian Tax Reform Report of a Survey" Professor Nicholas Kaldor (1956) expressed the view that malpractices like the presentation of false and miscellaneous accounts could be checked to a great extent if it were made compulsory for tax payers to present audited arcounts in all cases in which income or property exceeded certain limits. The Direct Taxes Enquiry Committee (December 1971) also considered that it would facilitate the administration of tax laws to a considerable extent if simultaneously with a compulsory maintenance of accounts, there is a statutory provision for their mandatory audit, at least in bigger cases.

Necessary enabling provision was brought into the statute through the Finance Act 1975 effective from 1 April 1976 providing that the Income-tax Officer can, with the prior approval of the Commissioner of Income-tax, direct the assessee to get the accounts audited by an accountant to be nominated by the Commissioner. The compulsory audit of accounts has not, however, been made mandatory. In para 1.65 of their 91st Report (Seventh Lok Sabha), the Public Accounts Committee desired to know how frequently the power to get the accounts audited has been exercised in each of the Commissioner's charges during the last three years in the cases of assessments of films artistes, producers etc., and with what results. The Ministry stated in reply in March 1983 that no case was referred to a nominated Chartered Accountant under this enabling provision.

3.26.13 The income and wealth returned and assessed in respect of some of the leading film artistes are as below :—

Name Assessment	Income		Wealth	
	Returned	Assessed	Returned	Assessed
	(In lakhs of rupees)			
H 1974-75	3.30	3.71	(—)5.72	10.49
1975-76	10.76	12.78	(—)5.78	46.53
1976-77	9.81	18.85	26.52	37.88
1977-78	13.28	18.46	29.53	48.54
1978-79	7.66	10.98	29.97	45.98
1979-80	5.30	8.43	7.97	—
1980-81	5.99	9.23	(—)0.43	—
1981-82	6.44	—	(—)10.07	—

R	1974-75	6.40	6.97	1.80	6.62
	1975-76	7.57	10.67	(—)3.10	12.56
	1976-77	7.43	7.31	0.99	22.52
	1977-78	(—)1.21	*	(—)2.59	39.74
	1978-79	(—)0.04	*	(—)1.19	35.76
	1979-80	(—)2.59	*	(—)5.49	—
	1980-81	(—)1.15	—	2.65	—
	1981-82	6.26	—	(—)12.46	—
S	1974-75	0.72	0.86	1.20	1.71
	1975-76	1.94	2.14	4.83	1.45
	1976-77	3.87	4.05	8.81	6.22
	1977-78	8.51	9.04	11.19	7.51
	1978-79	5.97	7.33	9.80	22.65
	1979-80	11.25	33.41	10.39	—
	1980-81	(—)4.68	(—)0.79	12.20	—
	1981-82	6.02	—	10.34	—
K	1974-75	2.19	2.24	1.12	6.86
	1975-76	2.38	2.54	0.71	6.40
	1976-77	1.61	1.71	2.59	7.89
	1977-78	3.66	3.74	4.47	10.11
	1978-79	3.92	6.83	7.63	13.24
	1979-80	3.35	7.88	8.27	—
	1980-81	7.37	7.22	8.84	—
	1981-82	11.86	—	12.07	—

3.26.14 Some of the cases of artistes in which the arrear demand exceeded Rs. 25 lakhs are listed below together with the assessment years to which they relate :

Name of the film artiste	Demand outstanding (In lakhs of rupees)	Assessment years to which arrears related
H	26.04	1973-74 to 1980-81
J	34.89	1979-80 and 1980-81
R	31.80	1975-76 and 1978-79

—denotes assessments pending.
*denotes assessments cancelled.

(i) The assessee J filed return of income for the assessment year 1979-80 on 28 July 1979 for Rs. 14,710. He filed a revised return on 15 September 1980 showing income of Rs. 10,180. On 24 November 1982, he filed another revised return showing income of Rs. 5,00,678. He had neither paid advance tax nor self-assessment tax. The assessment was completed on 25 March 1982 determining the income at Rs. 37,80,020. The assessee preferred an appeal and the Commissioner of Income-tax (Appeals) partly allowed it in April 1983. The assessment awaits rectification. Meanwhile, the assessee made a settlement petition for addition of Rs. 24,85,000 to the returned income. The department had issued a show cause notice for levy of penalty for concealment of income.

The same assessee filed return of income for the assessment year 1980-81 on 14 July 1982 showing income of Rs. 4,23,094. On 24 December 1982, he filed a revised return with income of Rs. 9,66,094. For this year also, he neither paid advance tax nor self-assessment tax. The Income-tax Officer fixed the income as Rs. 20,17,760 on 21 March 1983 and raised a tax demand of Rs. 22,27,396 including interest for belated filing of return and non payment of advance tax. The demand is pending recovery.

(ii) The assessee 'R' filed return of income for the assessment year 1975-76 on 3 March 1976 showing the income as nil. He had not paid any advance tax or self-assessment tax. In the assessment made on 18 March 1981, after obtaining the approval of the Inspecting Assistant Commissioner, the Income-tax Officer determined the income at Rs. 20,98,075 with 30,000 as agricultural income. In April 1981, the assessee preferred an appeal to the Commissioner of Income-tax (Appeals). The appeal is still pending. The department has issued a notice for levy of penalty for belated filing of the return.

(iii) In the case of assessee 'K' referred to in sub-para 13 above, a search was conducted in 1980-81 and cash of Rs. 12,12,274 and jewellery of Rs. 72,275 were seized. The assessment for the assessment year 1980-81 was made adding an income of Rs. 4,98,000 and raising a demand for payment of tax of Rs. 3,52,800. The assessments for the assessment years 1979-80 and 1981-82 remained to be completed. However, a settlement was arrived at in the case for an addition of Rs. 16,22,270 towards concealed income.

3.26.15 *To sum up—*

(i) Despite the formation of separate film circles there is no proper co-ordination in the assessments of producers, distributors, film artistes, etc. Apart from inherent difficulties due to different accounting years, different systems of accounting etc., vital data, necessary for proper co-ordination, are not collected by the department and kept on record.

(ii) Amortisation of cost of production of films is not regulated as laid down in the rules. The Public Accounts Committee had suggested a review of the system by a Study Group consisting among others, of experts in taxation, accountancy and audit and eminent non-officials having intimate knowledge of the operations of the film industry. The Ministry of Finance have stated (July 1983) that a departmental Study Group had been formed for the purpose in July 1983 and their report is awaited within three months from the date of formation.

(iii) Deferred annuity schemes through which current income gets distributed to a number of years in the future and become chargeable to tax only in the spread-over years, is very popular in the film world. No date of policies purchased and the beneficiaries thereof the collected and correlated with assessments. The Public Accounts Committee in para 1.72 of their 91st Report (Seventh Lok Sabha), recommended legislative measures for regulating such schemes so that the revenue is not affected adversely. Action is yet to be taken in this regard.

(iv) Provisions made in the law to secure better check on the assessments in the film wards are not enforced:

(a) No watch is kept on the receipt of statements prescribed to serve as a check on the tendency to inflate the cost of production of successful films. In most of the cases, no penal action is initiated for failure to render the statements or for rendering them belatedly.

(b) Provisions for compulsory maintenance of accounts was made in the Act in 1976. Rules to give effect to this provision have been framed only in 1983.

(c) Provisions for having the accounts audited was also made in 1976. The power has not been used in any case.

(v) The assessees falling in high income groups return disproportionately low incomes, avoid payment of advance and self-assessment taxes and when after strenuous deliberations, real incomes are determined and heavy demands of tax are raised, they come up with settlement petitions. In the process, recovery of final tax demand gets postponed. The arrear demand which was Rs. 1040 lakhs on 31 of March 1982 rose up to Rs. 1816 lakhs on 31 of March 1983.

3.26.16 The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

3.27 *Tax deduction at source from Indians employed in foreign missions*

Indian employees of foreign missions in India are subject to Indian income-tax. The Public Accounts Committee noted in 1967-68 that out of 74 foreign missions in India, 70 missions had either not sent the annual returns in respect of their Indian employees or had not deducted tax at source from the salaries paid to them [36th Report of the Public Accounts Committee (Fourth Lok Sabha)]. The Committee also noted that the department did not look into the matter for nearly 12 years after 1947 and when they did move in the matter in 1959, they were not able to arrive at a conclusion even after considering it for more than seven years. The Committee desired the Ministry of External Affairs to pursue the issue of tax deduction at source at diplomatic level, request foreign missions to co-operate with the Indian authorities in the matter and after ascertaining the names of Indian employees in foreign missions to issue notices to them to file returns of income.

The Ministry assured the Committee in 1968-69 that names of Indian employees working in foreign missions had been and were being collected and suitable action for assessment would be taken. The Ministry further informed the Committee that 38 foreign missions had supplied particulars of employees working in their offices and that two of them had started deducting tax at source and the number of Indian employees in the remaining 36 missions was 266, of whom for 125 notices had to be issued calling for returns.

The work relating to deduction of tax at source from Indian employees by foreign missions during the period 1977-78 to

1981-82 and its remittance to Government account was reviewed in audit in March 1983 with the following results.

(i) Board's instructions and action taken thereon.

The Central Board of Direct Taxes advised the Commissioner of Income-tax in November 1967 to write to all the missions who had neither furnished lists of employees nor deducted tax at source, to send a list of their Indian employees with their salary, perquisites, etc., and to refer to the Board in case there was non-compliance from the missions. In the case of other missions, the Board desired that necessary notices should be issued and assessments made in the normal course. On inquiry what action was taken on these instructions of the Board, the Commissioner of Income-tax stated in April 1983 that the department unfortunately did not have the relevant papers with them, that no foreign mission appeared to have so far filed any statement of salaries paid to the Indian employees and tax deducted therefrom and that action would be initiated to obtain the particulars from the various missions. The Commissioner also stated that the department did have a list of foreign missions operating in India.

(ii) Number of foreign missions and number of Indian employees in them.

Complete information as to the number of missions in India during the financial years 1977-78 t(1981-82 was not available from any of the records maintained by the department.

The particulars gathered from the Ministry of External Affairs in March 1983 indicated the following position :—

Year	Number of missions	No. of Indian employees as on 1 January of the year
1977	87	3322
1978	87	3320
1979	87	3592
1980	86	1734(x)
1981	88	2454 (x)
1982	90	3744

(x) Nos. of employees in 60 and 50 missions for the years 1980 and 1981 respectively called for from the Ministry in March 1983 were still awaited.

(iii) No. of missions that deducted tax at source.

According to the particulars available in the department, only one embassy during the year 1979-80 and two embassies during the year 1980-81 had deducted tax at source from the salaries paid to Indian employees.

The department had no information about the tax, if any, deducted at source by the remaining missions for the years 1977-78 to 1981-82 and for the aforesaid two missions in respect of the other years.

(iv) No. of missions that had/had not filed annual establishment return.

Only three embassies furnished the list of employees. No action was taken by the department to call for the statements to ensure that either tax had been deducted at source or for issuing notices directing the individuals to file returns of income for assessment. Confirming that the foreign missions had not filed the annual returns, the department stated in February 1983, that the foreign missions are not under any legal obligation to file the returns as the provisions of the Income-tax Act, 1961, are not applicable to them.

(v) No. of cases where individual returns were filed.

The number of Indian employees who had filed returns of income assessment yearwise and the number of related missions for the assessment years 1977-78 to 1981-82, culled out from the records in the department are as below :—

Assessment year	No. of Indian employees who filed the return of income	No. of related missions.
1977-78	781	45
1978-79	573	33
1979-80	483	31
1980-81	349	24
1981-82	91	13

The particulars in respect of the remaining missions were not available in the departmental records.

The Ministry of Finance have stated that details of Indian Employees who have filed the returns of income are being collected and that it would be ensured that all such employees with assessable income are brought into tax net.

CHAPTER 4

OTHER DIRECT TAXES

A. WEALTH-TAX

4.01 In the financial years 1978-79 to 1982-83, wealth-tax receipts *vis-a-vis* the budget estimates were as given below :—

Year	Budget Estimates (In crores of rupees)	Actuals
1978-79	55.00	55.41
1979-80	60.00	64.47
1980-81	65.00	67.37
1981-82	66.00	78.12
1982-83	80.00	*90.37

4.02 The arrears of demand pending collection and number of cases pending assessment as at the end of the years 1978-79 to 1982-83 are given below :—

Year	Number of cases pending assessment at the end of	Arrears of demand pending collection at the end of (In crores of rupees)
1978-79	3,31,561	184.08
1979-80	4,32,988	180.54
1980-81	4,99,903	217.11
1981-82	5,67,381	208.92
1982-83*	5,41,965	180.33

*Provisional

4.03 During the test audit of assessments made under the Wealth-tax Act, 1957, conducted during the period 1 April 1982 to 31 March 1983, the following types of mistakes were noticed :—

(i) Wealth escaping assessment.

(ii) Incorrect valuation of immovable properties.

(iii) Incorrect valuation of partner's interest in partnership firms.

(iv) Incorrect valuation of unquoted equity shares.

(v) Incorrect valuation of gold and jewellery.

(vi) Incorrect computation of net wealth.

(vii) Incorrect exemptions and deductions.

(viii) Mistakes in application of rates of tax and calculation of tax.

(ix) Non-levy/short levy of additional wealth-tax.

(x) Non-levy/short levy of penalty.

(xi) Excess refund.

(xii) Non-completion of assessment within the time limit.

A few important cases illustrating these mistakes are given in the following paragraphs.

4.04 *Wealth escaping assessment*

(i) Under the Wealth-tax Act, 1957, the net wealth of an assessee means the aggregate value of all assets, wherever located, belonging to the assessee, as reduced by the aggregate value of all admissible debts owed by him on the valuation date.

(a) Funds of an individual assessee, which were lying with the assessee's solicitor-firm, were impounded by Government but were released in two instalments of Rs. 18,57,013 and Rs. 15,25,561 in July 1972 and February 1973, respectively. The assessee filed his wealth-tax returns disclosing Rs. 18,57,013, for the assessment year 1973-74 and Rs. 33,82,574 (Rs. 18,57,013+Rs. 15,25,561) or the assessment year 1974-75 (previous year ending on 31st December each year). The

Wealth-tax Officer completed the assessments for both the years in March 1979 on the wealth returned by the assessee. Since the entire amount lying with the solicitor-firm belonged to the assessee, the sum of Rs. 33,82,574 should have been assessed as his wealth for the assessment year 1973-74 also. The omission resulted in under-assessment of wealth by Rs. 15,25,561, with consequential undercharge of tax of Rs. 1,13,057.

The Ministry of Finance have accepted the mistake (December 1983).

(b) In computing the net wealth of an assessee, for the assessment year 1975-76 in March 1980, an amount of Rs. 4,37,191 returned by the assessee as cash in hand or deposits in banks was omitted to be included in the total wealth of the assessee by the Wealth-tax Officer.

Further the value of certain lands owned by the assessee and valued at Rs. 25,000, for the assessment year 1976-77, was also omitted to be included in the assessment for the year 1975-76.

The two omissions resulted in under-assessment of wealth-tax of Rs. 44,539.

The Ministry of Finance have accepted the mistakes and have stated (August 1983) that additional demand of Rs. 44,539 has been raised.

(c) The Central Board of Direct Taxes issued instructions (November 1973) emphasising the need for proper coordination among assessment records pertaining to different direct taxes with a view to finding out cases of evasion of wealth-tax.

An assessee, in her wealth-tax return, for the assessment year 1975-76, excluded the value of properties inherited from her deceased husband by giving a foot-note that the properties left by the deceased were in the possession and control of the deceased's brother and if any part of the same was includible in law in the hands of the assessee details could be had from the said person. The Wealth-tax Officer, without making further enquiries about the extent and ownership of the properties left by the deceased husband excluded value of these properties from the net wealth of the assessee (March 1980).

It was noticed that the estate duty assessment of the deceased husband of the assessee was finalised on 29 October 1977 and properties valued at Rs. 5,75,083 passed on to her on the death of her husband on 6 September 1970. Since the ownership of the properties left by the husband on his death devolved on the assessee, these formed part of her wealth for the assessment years 1971-72 to 1975-76 and were liable to wealth-tax. The omission to include these resulted in non-levy of tax of Rs. 54,686.

The Ministry of Finance have accepted the mistake in principle (November 1983).

(ii) An assessee formed a partnership firm with his mother and son as partners under a partnership deed dated 19 September 1963. The assessee retired voluntarily from the firm on 24 October 1963. In terms of memorandum of agreement drawn up and executed by the other two partners and the assessee on 24 October 1963, the assessee continued to have half share in the goodwill of the firm even after his retirement and was also entitled to rejoin the firm as a partner with the same share.

The assessee was not a partner in the firm during the assessment years 1964-65 to 1974-75 and 1977-78 to 1979-80. Based on the agreement dated 24 October 1963 half share of the goodwill estimated at Rs. 36,00,000, *viz.*, Rs. 18,00,000 for each assessment year was included by the Wealth-tax Officer in his net wealth, for the assessment years 1964-65 to 1974-75. The Income-tax Appellate Tribunal also upheld (June 1982) such inclusion and observed that yield aspect of the assets should be considered while valuing the assessee's interest in the goodwill.

It was noticed in audit (January 1983) that the half share of goodwill was not included in the net wealth for the assessment years 1977-78 to 1979-80 (assessments completed between October and November 1981). In the absence of recomputation of the value of goodwill by the department in the light of the decision (June 1982) of the Income-tax Appellate Tribunal, the value of goodwill to the extent of Rs. 18,00,000, in each assessment year, had escaped assessment. This resulted in short levy of tax of Rs. 1,82,400.

The Ministry of Finance have accepted the mistake (December 1983).

(iii) In computing the net wealth of an assessee, for the assessment years 1975-76 to 1977-78, in August 1979, her half

share of Rs. 4,42,238, receivable by way of compensation in respect of agricultural land acquired by a State Government in April 1974 (amount of compensation declared in July 1977) was omitted to be included in each of the three assessment years. It was seen that the amount of the compensation was not returned by the assessee also. The assessee simply showed value of the agricultural land, which was not owned by her on the relevant valuation dates, at Rs. 1,19,986, claiming it to be exempt under the Wealth-tax Act, 1957, which was accepted in the assessment. The omission resulted in short levy of wealth-tax of Rs. 30,358.

The paragraph was sent to the Ministry of Finance in June 1983; their reply is awaited (December 1983).

(iv) For the purpose of Wealth-tax Act, 1957, the term "asset" includes property of every description, but does not include an interest in property where the interest is available to an assessee for a period not exceeding six years from the date the interest vests in the assessee.

(a) A right to exploit a cinema film in a particular territory for a period of time has been held to be a capital asset for income-tax purposes and correspondingly such items will constitute chargeable assets under the Wealth-tax Act. A Hindu undivided family (specified) engaged in the business of distribution, exhibition and exploitation of feature films, entered into two lease agreements with producers of films in September 1975 and April 1977, respectively acquiring the rights of sub-lease, exclusive distribution, exhibition and exploitation of two films for a period of seven years from the date of first release of the pictures. The value of interest accruing to the assessee as lessee for exploitation of the films in the accounting years relevant to the assessment year 1977-78 and onwards was not determined and included in its net wealth. Applying the annuity method to the realisations during the accounting years 1977-78 and 1978-79, the value of this interest would work out to Rs. 11,35,935 for the assessment year 1977-78 and Rs. 8,71,328 for the assessment year 1978-79. The non-inclusion of these amounts resulted in undercharge of wealth-tax of Rs. 54,630.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(b) An assessee obtained lease of a cinema house, as per lease deed executed and registered in July 1977, for a period of 30 years terminating on 6 August 1994, at a monthly lease rent of Rs. 2,000 from 1 April 1970 to 6 August 1974, Rs. 3,500 from 7 August 1974 to 6 August 1984 and Rs. 4,000 from 7 August 1984 to 6 August 1994, with power to sub-lease the property. The fair market rent of the said building was estimated in May 1974 at Rs. 5,760 per month by the Executive Engineer, Alwar and expenses on proper maintenance of the property and on other outgoings were estimated by him at Rs. 8,700 per annum in May 1974. The value of the interest acquired by the assessee on account of maintainable rent (fair market rent less outgoings) being higher than the lease rent, was, therefore, includible in the net wealth of the assessee. The value of such interest worked out to Rs. 4,42,900 for the assessment year 1971-72 and Rs. 1,67,300 for the assessment year 1980-81. Omission to evaluate the lease interest of the assessee resulted in escapement of wealth, with consequent non-levy of wealth-tax of Rs. 26,345, for the assessment years 1971-72 to 1980-81.

The Ministry of Finance have accepted the mistake and stated (November 1983) that rectification for the assessment year 1971-72 has become time-barred and for the assessment years 1972-73 to 1976-77 additional demand of Rs. 30,880 has been raised. Further, report regarding completion of assessments for the assessment years 1977-78 to 1980-81 is awaited (December 1983).

4.05 *Incorrect valuation of immovable properties*

(i) Under the Wealth-tax Act, 1957, the value of any property shall be estimated to be the price which it would fetch if sold in the open market on the valuation date.

The Central Board of Direct Taxes have not issued any instructions or guidelines on the valuation of agricultural lands for wealth-tax purposes. In April 1959, however, they had issued instructions on the valuation of agricultural lands for estate duty purposes. According to these instructions, land values should be fixed on the basis of actual recorded sales and independent checks should be made on the market sales by comparing the sale price with the net income derived from land, the value being determined at 12 to 20 times the net yield of the land arrived at after allowing a deduction of 50 per cent from the gross yield towards expenses.

(a) An assessee (Individual) in his returns of wealth, for the assessment years 1978-79, 1979-80 and 1980-81, indicated the value of his agricultural lands as Rs. 87,875, Rs. 81,888 and Rs. 1,02,460, respectively and claimed exemption therefor from wealth-tax. The net agricultural incomes returned for aggregation and rate purposes in connection with income-tax assessments, for the above assessment years were Rs. 45,000, Rs. 72,500 and Rs. 3,15,000, respectively. Compared to these incomes the declared values of the lands were disproportionately low. In the absence of any valuation, the value could have been worked out on the basis of income capitalisation method. Under this method, capitalising the average net income of Rs. 1,45,000 even at a yield rate of 10 per cent the value of the lands would not be less than Rs. 14.5 lakhs. If this value was adopted, there would be an increase in the net wealth of Rs. 39 lakhs in the aggregate, for the assessment years 1978-79 to 1980-81. The under-valuation of the agricultural lands resulted in short levy of wealth-tax of Rs. 97,952.

The Ministry of Finance have stated (December 1983) that the market value of the agricultural land as well as the probable yield therefrom will be referred to the valuation officer.

(b) Wealth-tax returns of a Hindu undivided family, for the assessment years 1975-76 to 1977-78, included a piece of land situated in a city, measuring 8,081 sq. metres and a house constructed thereon on an area of 232 sq. metres. The land was claimed by the assessee to be agricultural land.

An Inspector of the department, who was deputed to survey the property reported in October 1977 that the land was uncultivated and only flowers of various varieties were grown. It was also reported by him that the area was extensively developed with all modern amenities available there and cost of the land in the vicinity was Rs. 8 or Rs. 9 per sq. foot. The Inspector estimated the value of the house at Rs. 55,000 and that of the land not covered by the house at Rs. 5,07,000, applying the rate of Rs. 6 per sq. foot, based on the rate at which the development authority of the city had sold plots in an adjacent locality. Records of Sub-Registrar's office also indicated that land in the locality was sold at Rs. 7.5 or Rs. 8 per sq. foot.

The assessments, for the assessment years 1975-76 to 1977-78, were completed in March 1978 after the receipt of the Inspector's report in October 1977, but the report was ignored by the assessing officer. The values of land and building were adopted in the assessments for each of the years at Rs. 60,000

and Rs. 40,000, respectively, as against Rs. 5,07,000 and Rs. 55,000, estimated by the Inspector. The land was also incorrectly treated as exempt under the Act. This resulted in short computation of wealth of the assessee for each of the assessment years of Rs. 5,22,000, with consequent under charge of tax amounting to Rs. 58,503 (including additional wealth-tax of Rs. 24,370 leviable but not levied on urban immovable properties for the assessment years 1975-76 and 1976-77).

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(ii) In the wealth-tax assessment of an assessee, for the assessment year 1975-76, completed in December 1979, on a net wealth of Rs. 6,59,400, the value of a house property on a site measuring 41.3 grounds in a metropolitan city was adopted as Rs. 3,82,000. This was less than the value of Rs. 6,37,595 adopted for the assessment year 1974-75. According to an earlier decision of the department on the other hand an addition of Rs. 41,300 should have been made to the value adopted for 1974-75 to cover appreciation of land value. The correct value of the property for the assessment year 1975-76 should have been taken as Rs. 6,78,895. The mistake resulted in under-assessment of the value of the property by Rs. 2,96,895, involving short-levy of tax of Rs. 23,059 (including additional wealth-tax on the urban asset).

The Ministry of Finance have accepted the mistake and have stated (October 1983) that remedial action has become time-barred.

(iii) Under the Wealth-tax Rules, 1957, as amended with effect from 1 April 1979, the value of a house which is wholly or mainly used for residential purposes, shall be 12.5 times of the net maintainable rent.

The net wealth of two individuals included 50 per cent share of a house property, the value of which was computed by the Wealth-tax Officer at Rs. 1,50,000 in each case, for the assessment year 1980-81. The property was let out. It was seen from the income-tax assessment records of the assessees for the assessment year 1980-81, that the income from this property had been assessed at Rs. 43,600 in each case. The value of the property on the basis of net maintainable rent method would, therefore, be Rs. 5,45,500 in each case. There

was thus under-assessment of wealth of Rs. 7,90,000, with consequent short levy of tax of Rs. 29,867.

The Ministry of Finance have accepted the mistake in principle (December 1983).

4.06 *Incorrect valuation of partner's interest in partnership firms*

(i) Under the provisions of the Wealth-tax Act, 1957, where an assessee is a partner in a firm, the value of his interest in the net assets of the firm is to be included in his net wealth. As a partnership firm as such is not a chargeable person under the Act it is not entitled to any exemptions under the Act. Also what is included in the partner's assessment is the value of his interest in the firm, and not values of any particular assets so that exemptions related to specified assets such as house property are not available to the partner also even if the firm's property includes such assets. It was held by the Madras High Court (August 1975) that neither the firm nor the partners are entitled to any exemptions in such cases.

The Central Board of Direct Taxes in their circular dated 29 July 1974 expressed the view that exemption under the Act could not be granted to a partner if the house belongs to a firm. The Board also stated that the larger issue whether any or some or all of the exemptions listed in the Act are available while computing the net wealth of the firm under the Wealth-tax Rules, 1957, was under consideration. Even after a lapse of over 9 years, the Board have not issued any instructions for the guidance of the assessing officers, with the result that the assessing officers have not maintained uniformity in assessment. The instruction dated 29 July 1974, issued by the Board, has also been generally overlooked.

In the wealth-tax assessments of fourteen assessees, for the assessment years 1973-74 to 1980-81, values of interest of the assessees in the firms, in which they were partners, were determined after deducting from the net wealth of the firms the value of certain assets such as shares, gold bonds, etc., held by the firms, which were treated as exempt. This resulted in aggregate short levy of wealth-tax of Rs. 2,89,266.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(ii) The Wealth-tax Rules, 1957, provide that where the market value of any asset exceeds its book value by more than 20 per cent, the market value is to be substituted for the book value in such valuation.

In the case of a partner of a firm his share of interest in the firm is to be valued with reference to the net wealth of the firm. In the case of an individual, who was a partner in six firms, the Wealth-tax Officer completed the assessment for the assessment year 1977-78 (valuation date 31 March 1977) on 31 March 1982. While working out the assessee's share interest in the assets of these firms, the Wealth-tax Officer enhanced the value of lands and buildings owned by the firms, but in respect of other assets of the firm such as machinery, etc., the Wealth-tax Officer adopted only their book values.

In the case of one of these firms it was noticed in audit (July 1982) that the firm had sold certain machinery during the previous year relevant to the assessment year 1979-80 for a total sum of Rs. 45,14,362 whereas the written down value of the machinery was Rs. 4,41,250 only as on January 1976 and Rs. 3,64,670 as on January 1978. As the market value exceeded the book value by more than 20 per cent, the Wealth-tax Officer ought to have adopted the market value of these machineries, instead of their book value in the wealth-tax assessment. The omission to do so resulted in under-assessment of wealth of Rs. 9,68,600, with consequent short levy of wealth-tax of Rs. 32,755 (market value of the machinery reckoned at ten times the book value as on 1 January 1976, *i.e.*, Rs. 44,12,500).

The Ministry of Finance have accepted the mistake (December 1983).

4.07 *Incorrect valuation of unquoted equity shares*

(i) Under Rule 1-D of the Wealth-tax Rules, 1957, amounts set apart for payment of dividends but not declared before the valuation dates at an annual general body meeting, should not be considered as liabilities of the company for the concerned assessment year for the purpose of valuation of its shares.

The net wealth of three individual assessees, for the assessment years 1976-77 and 1977-78, included value of 1,060, 1,058 and 1,722 unquoted equity shares of a private limited company during both the assessment years. In valuing the shares of the

company sums of Rs. 13,80,000 and Rs. 6,00,000, representing provisions for proposed dividends for the financial years relevant to the assessment years 1976-77 and 1977-78, respectively, were allowed as liabilities, although the dividends were declared in February 1977 and March 1978, long after the relevant valuation dates, viz., 31 March 1976 and 31 March 1977.

This irregular allowance of liabilities resulted in under-valuation of shares by Rs. 207 and Rs. 102 per share for the assessment years 1976-77 and 1977-78, respectively, with consequent under-assessment of wealth of Rs. 11,86,560 and undercharge of tax of Rs. 72,919.

The Ministry of Finance have accepted the mistakes in all the three cases and have stated (December 1983) that action is being taken for rectification.

(ii) Under Rule 1-D of the Wealth-tax Rules, 1957, the break-up value of unquoted equity shares is to be worked out without taking into account, reserves by whatever name called and contingent liabilities, depicted on the liability side of the balance sheet of a company.

Net wealth of 12 assessees *inter alia* included value of unquoted equity shares of a company the break-up value of which was adopted at Rs. 2.11 and Rs. 9.96, for the assessment years 1976-77 and 1977-78, respectively. In arriving at the break-up value a sum of Rs. 67.48 lakhs for the assessment year 1976-77 and Rs. 50.97 lakhs for the assessment year 1977-78, on account of provision for gratuity was deducted from the value of assets, alongwith other admissible items shown on the liability side of the balance sheet of the company for the relevant previous years. Since provision for gratuity was in the nature of reserve it was not to be taken into account in determining the break-up value of equity shares of the company. Excluding the item shown as provision for gratuity, the market value of each equity share worked out to Rs. 11.67 and Rs. 17.18 in place of Rs. 2.11 and Rs. 9.96 adopted by the department, for the assessment years 1976-77 and 1977-78, respectively. The net wealth of the 12 assessees who held varying number of shares ranging from 9,000 to 28,500 was consequently short computed leading to under-assessment of tax of Rs. 60,623.

The Ministry of Finance have accepted the audit objection (September 1983).

4.08 *Incorrect valuation of gold and jewellery*

Under the Wealth-tax Act, 1957, the value of any property, including gold, jewellery, etc., shall be estimated to be the price which, in the opinion of the Wealth-tax Officer, it would fetch if sold in the open market on the valuation date.

In the wealth-tax assessments of two Hindu undivided families (specified), represented by their respective *kartas*, who were partners in a firm dealing in gold and jewellery, the value of 3,941 grams of gold jewellery received by each of them on dissolution of the firm on the relevant valuation date (Dussehra 1978) was assessed on the basis of book value at Rs. 1,07,354, for the assessment year 1979-80. The market rate of gold on the valuation date was Rs. 870 per 10 grams. The market value of the gold jewellery, after giving allowance at 15 per cent for impurities, worked out to Rs. 2,91,437, in respect of each of the assessees.

Further, for the assessment years 1980-81 and 1981-82 the value of shares of the above two Hindu undivided families in the closing stock of gold jewellery of another newly constituted firm, in which they were partners with equal shares, was adopted on the basis of book value at Rs. 8,49,271. The market rate of gold on the relevant valuation dates, viz., Dussehra 1979 and Dussehra 1980, was Rs. 1,220 per ten grams and Rs. 1,600 per ten grams, respectively. At these rates the market value of gold jewellery, after giving allowance at 15 per cent for impurities, worked out to Rs. 24,60,677. As market value of the gold jewellery in these cases exceeded the book value by over 20 per cent the market value should have been taken into account in computing the wealth of the assessee. The omission to do so resulted in short computation of wealth by Rs. 19,79,572 and consequent short levy of tax of Rs. 42,377.

The Ministry of Finance have accepted the mistake and have stated (November 1983) that additional demand of Rs. 51,531 has been raised.

4.09 *Incorrect computation of net wealth*

Under the Wealth-tax Act, 1957, where assets are held by a trustee on behalf of some other persons wealth-tax shall be

levied upon and recoverable from the trustee in the like manner and to the same extent as it would be leviable upon and recoverable from the person for whose benefit the assets are held. The Act also provides for the inclusion of the value of the beneficiary's interest in the trust in the wealth of the beneficiary for assessment directly in his hands. Instructions were issued by the Board in April 1979, emphasising the need for a proper co-ordination between officers assessing the trustees and those assessing the beneficiaries to avoid escapement of assessment of trusts properties.

An assessee who was the sole beneficiary of a trust was having other wealth also. He sent two returns to two different wards, one for his interest in the trust and the other for his individual wealth. The net wealth of the trust, for the assessment years 1969-70 and 1970-71, was assessed to the wealth-tax in September 1973 in the first ward. For the assessment years 1971-72 to 1977-78, the assessments of the trust were made (between September 1973 and March 1982) with 'nil' demand on the understanding that the trust's wealth would be assessed directly in the beneficiary's hands in his individual assessments in the second ward. No communication in this regard was, however, sent by the Income-tax Officer of the first ward to the Income-tax Officer in the second ward assessing the beneficiary's individual wealth.

Meanwhile, assessments on the individual wealth of the assessee were completed in the second ward, for the assessment years 1969-70 to 1980-81, without including the interest in the trust.

The omission caused by the lack of co-ordination between the two assessing officers resulted in short-levy of wealth-tax of Rs. 1,18,486 (tax due Rs. 7,94,570 minus tax levied Rs. 6,76,084 including Rs. 281 levied on trust's wealth for the assessment years 1969-70 and 1970-71).

The Ministry of Finance have accepted the mistake in principle and have stated (September 1983) that rectification for the assessment years 1969-70 to 1973-74 has become time-barred. Assessments for the assessment years 1974-75 and 1975-76 have been reopened and assessments for the assessment years 1976-77 to 1980-81 have been set aside.

4.10 *Incorrect exemptions and deductions*

(i) Under the Wealth-tax Act, 1957, debts which are secured on, or which have been incurred in relation to any property in respect of which wealth-tax is not chargeable, are not to be deducted in computing the net wealth.

In the case of three assessees, while computing the net wealth, for the assessment years 1976-77 and 1980-81, debts incurred for acquiring National Defence Gold Bonds and Units of the Unit Trust of India were allowed as deduction, even though the value of these assets was excluded from the computation of net wealth, being exempted assets under the Act. This incorrect deduction resulted in under-assessment of wealth of Rs. 13,17,843 and consequent short levy of wealth-tax of Rs. 61,014.

The Ministry of Finance have accepted the mistakes (July and November 1983).

(ii) Under the Wealth-tax Act, 1957, in computing net wealth of an assessee the value of any equity shares held by him in any specified type of companies which are established with the main object of carrying on the business of manufacture or production of any one or more of the articles or things mentioned in the Ninth Schedule to the Income-tax Act, 1961, is not to be included in his wealth.

In computing (September 1981) the net wealth of an individual, for the assessment years 1980-81 and 1981-82, equity shares valued at Rs. 4,67,000 and Rs. 6,45,750, held by him on the relevant valuation dates in a newly established company, were not included. It was seen from the income-tax records that the company was engaged in the manufacture of Tungston Filaments and Molybdemum Wires used in electric lamps which were not specified in the Ninth Schedule to the Income-tax Act. The incorrect exclusion of the value of these equity shares from his wealth resulted in short levy of tax amounting to Rs. 29,223.

The Ministry of Finance have accepted the mistake and have stated (October 1983) that additional demand of Rs. 29,223 has been raised.

4.11 *Mistakes in application of rates of tax and calculation of tax*

(i) From the assessment year 1974-75, the Schedule to the Wealth-tax Act, 1957, was amended to provide for a higher

rate of tax for every Hindu undivided family (HUF) having at least one member with assessable net wealth exceeding Rs. one lakh upto the assessment year 1979-80 and Rs. one lakh and fifty thousands from the assessment year 1980-81 and subsequent years.

In the assessments of twenty one of such Hindu undivided families, in seventeen Commissioners' charges, it was noticed that the prescribed higher rates were not applied in the wealth-tax assessments for the assessment years 1974-75 to 1981-82. This resulted in an aggregate short levy of tax of Rs. 3,12,623 in these cases.

The Ministry of Finance have accepted the short levy in ninteen cases; their reply is awaited in the remaining two cases (December 1983).

(ii) The wealth-tax assessment of an assessee belonging to a Hindu undivided family, for the assessment year 1976-77, was completed in March 1982 on a net wealth of Rs. 19,94,200. The tax due at the rate applicable to the assessment year 1976-77 was Rs. 1,06,048. However, the tax was calculated at the lower rates prescribed in the Finance Act, 1976, for the assessment year 1977-78 and was determined as Rs. 41,322. This resulted in short levy of tax of Rs. 64,726.

The Ministry of Finance have accepted the mistake in principle (August 1983).

(iii) The net wealth of an assessee comprising urban immovable properties was assessed, for the assessment years 1974-75 to 1976-77, in March 1982, at Rs. 15,00,000 in each of the assessment years. The department, however, incorrectly calculated wealth-tax and additional wealth-tax on net wealth of Rs. 10,00,000 instead of Rs. 15,00,000 in each assessment year. This resulted in an aggregate short levy of wealth-tax (including additional wealth-tax) of Rs. 1,65,680.

The Ministry of Finance have accepted the mistake and have stated (September 1983) that additional demand of Rs. 1,65,680 has been raised.

(iv) In the wealth-tax assessment of an individual assessee, for the assessment year 1976-77, completed in November 1980,

the net wealth was determined at Rs. 9,89,717 including urban immovable properties valued at Rs. 7,77,110. The assessing officer incorrectly applied the rates of tax applicable for the assessment year 1977-78 instead of those for the assessment year 1976-77 and also did not levied additional wealth-tax on the urban immovable properties.

Further, the value of immovable properties was taken at Rs. 10,78,100 instead of Rs. 11,87,800 fixed by the Departmental Valuation Officer. These properties were categorised by the Valuation Officer as non-agricultural but in the assessment one of the properties was incorrectly taken as agricultural and exemption of Rs. 1.50 lakhs was allowed. The combined effect of these mistakes was short levy of tax of Rs. 51,034.

The Ministry of Finance have accepted the mistakes and have stated (August 1983) that additional demand of Rs. 51,034 has been raised.

4.12 *Non-levy/short-levy of additional wealth-tax*

Under the Wealth-tax Act, 1957, before its amendment by the Finance Act, 1976, where the net wealth of an individual or a Hindu undivided family included buildings or lands (other than business premises) or any rights therein, situated in an urban area additional wealth-tax was leviable on the value of such urban assets exceeding rupees five lakhs.

(i) The net wealth of four individuals and three Hindu undivided families assessed for the assessment years 1968-69 to 1976-77, included urban immovable properties valued at Rs. 256.50 lakhs on which additional wealth-tax was leviable. The department, however, did not levy such tax. This resulted in undercharge of tax of Rs. 7,50,208 in these cases.

The Ministry of Finance have accepted the undercharge of tax in all the seven cases.

(ii) The net wealth of five individuals and two Hindu undivided families, for the assessment years 1971-72 to 1973-74, 1975-76 and 1976-77, included urban immovable properties valued at Rs. 93.56 lakhs, on which additional wealth-tax was not levied/short levied by the department. This resulted in undercharge of tax of Rs. 1,78,884 in these cases.

The Ministry of Finance have accepted the undercharge of tax in all the seven cases.

(iii) The net wealth of an individual, for the assessment years 1971-72 to 1976-77, assessed on 23 March 1982, included, *inter alia,* six urban house properties valued at Rs. 8,40,240 on which additional wealth-tax amounting to Rs. 72,072 was leviable in these six years. However, the department levied additional wealth-tax of Rs. 7,800 on one house property included in these urban assets. The omission resulted in short levy of tax of Rs. 64,272.

The Ministry of Finance have accepted the mistake and have stated (November 1983) that action is being taken for rectification.

(iv) The net wealth of a Hindu undivided family (specified), for the assessment year 1976-77, computed in March 1981 at Rs. 30,00,000, included urban immovable properties of the value of Rs. 18,07,300 but no additional wealth-tax was levied by the department. There was also calculation mistake in computing wealth-tax during the assessment years 1976-77 and 1977-78. These mistakes resulted in undercharge of tax of Rs. 94,484.

The Ministry of Finance have accepted the mistakes and have stated (November 1983) that additional demand has been raised.

4.13 *Non-levy/short levy of penalty*

Under the Wealth-tax Act, 1957, penalty is leviable where the assessing officer is satisfied that an assessee has, without reasonable cause, failed to furnish wealth-tax return within the prescribed time. Upto 31 March 1976, the penalty leviable was a sum, for every month, during which the default continued, equal to half per cent of the net wealth assessed, as reduced by the amount of initial exemption but subject to a maximum of equal to 100 per cent of the net wealth assessed. The Act was amended with effect from 1 April 1976, to provide that the penalty should be equal to two per cent of the assessed tax for every month during which the default continued. As regards cases where the default took place prior to the amendment and continued after the amendment, the Central Board of Direct Taxes issued instructions (February 1977) that such default

being a continuous one, the penalty should be imposed for every month during which the default continued, by applying the unamended provisions for the period prior to 1 April 1976 and the amended provisions thereafter. However, in April 1981, the Supreme Court held that :

(a) the default was not continuous but was a single default, committed on the last date on which the return had to be filed, and

(b) the penalty should be imposed in accordance with the law in force on that day.

In view of the judgment, the aforesaid instructions of February 1977 were withdrawn by the Board in October 1981.

(i) An individual, filed his return of net wealth for the assessment year 1974-75 (valuation date 31 March 1974) in January 1980, much later than the due date (30 June 1974). While computing the assessment, a penalty of Rs. 54,967 was levied in March 1982 (by which time the Board's instructions of February 1977 had been withdrawn) by the department for the delay of 66 months, in filing the return. The penalty was, incorrectly computed by reference to the assessed net wealth for the period from the due date of filing of return to 31 March 1976 under the law then in force and by reference to the assessed tax from 1 April 1976 to the date of filing the return.

But as per the law enunciated by the Supreme Court in April 1981, the penalty leviable would work out to Rs. 1,46,097. The omission to rectify the levy of penalty resulted in short levy of penalty of Rs. 91,130.

The Ministry of Finance have accepted the mistake and have stated (August 1983) that additional demand of Rs. 91,130 has been raised.

(ii) An assessee, a Hindu undivided family, filed the returns of net wealth, for the assessment years 1971-72 to 1975-76, on 15 January 1977 *i.e.*, long after the due date, *viz.*, 30 June of the relevant assessment year. The period of delay ranged between 18 months and 66 months. While completing the assessments, penalties levied were incorrectly computed at 2 per cent of the assessed tax for every month of default instead of the rate of one-half per cent of the net wealth assessed for

every month of default as per the law as on the last date on which return for a particular year was to be filed. This resulted in short levy of minimum penalty of Rs. 3,49,587.

The Ministry of Finance have accepted the mistake in principle (December 1983).

(iii) An individual filed returns of net wealth, for the assessment years 1972-73 to 1974-75, in August 1978, much later than the due dates. The periods of delay ranged between 48 months and 72 months. While completing the assessment on 30 December 1981, the Wealth-tax Officer levied penalty of Rs. 2,506, for delay in filing of returns. The penalty levied was incorrectly computed at the rate of 2 per cent of the assessed tax for each month of default instead of at the rate of one-half per cent of the net wealth assessed for each month of default as per provisions of law on the date on which returns had to be filed. The omission resulted in short levy of penalty of Rs. 54,314.

The Ministry of Finance have accepted the mistake (October 1983).

(iv) An individual, filed his return of net wealth for the assessment year 1975-76 (valuation date 31 March 1975) in January 1978, much later than the due date (30 June 1975). While computing the assessment, a penalty of Rs. 25,840 was levied in February 1982 (by which time the Board's instructions of February 1977 had been withdrawn) by the department for the delay of 31 months in filing the return. The penalty was incorrectly computed by reference to the assessed net wealth for the period from the due date of filing of return to 31 March 1976 under the law then in force and by reference to the assessed tax from 1 April 1976 to the date of filing the return.

But as per the law enunciated by the Supreme Court in April 1981, the penalty leviable would work out to Rs. 77,329. The omission to rectify the levy of penalty resulted in short levy of penalty of Rs. 51,489.

The Ministry of Finance have accepted the mistake and have stated (September 1983) that action is being taken for rectification.

4.14 *Excess refund*

In the case of an individual, the Wealth-tax Officer levied (June 1976) penalty of Rs. 25,875 for the assessment year 1969-70 towards delay of nine months in filing the wealth-tax return. The penalty order was subsequently rectified (February 1977) taking the delay as twelve months and the quantum of penalty was raised to Rs. 34,500. The assessee paid in January 1980 a sum of Rs. 49,962 including interest on the belated payment. The rectification order of February 1977 was, however, quashed by the Appellate Tribunal (January 1980) with the observation that the rectification order was not valid.

The order of the Appellate Tribunal was given effect to in December 1981 and sums of Rs. 49,962 towards penalty and Rs. 10,479 towards interest for delay in giving effect to the appellate order were refunded to the assessee. As, however, the Appellate Tribunal quashed only the rectification order of February 1977, the assessee was entitled to a refund of Rs. 12,219 towards penalty and Rs. 2,562 as interest for the delay in giving effect to appellate order. Refund of Rs. 45,660 was made in excess.

The Ministry of Finance have accepted the mistake (December 1983).

4.15 *Non-completion of assessment within the time limit*

Under the Wealth-tax Act, 1957, as amended by the Taxation Laws (Amendment) Act, 1975, assessments relating to the assessment year 1975-76 and subsequent assessment years are to be completed within four years from the end of the relevant assessment year or one year from the date of the filing of a return or a revised return, whichever is later.

An assessee submitted her wealth-tax returns, for the assessment years 1975-76, 1976-77 and 1977-78, in November 1975, December 1976 and December 1977, respectively. The assessments relating to the assessment years 1975-76 and 1977-78 were completed by the department in December 1979 and March 1982, respectively. For the assessment year 1976-77, the department issued notice to the assessee in December 1976, posting the case for hearing in January 1977. No follow-up action was taken and the assessment was not completed by 31 March 1981, the time stipulated in the Act for completion of the assessment.

Further, net wealth returned by the assessee for the assessment year 1976-77 was Rs. 5,16,200 and tax of Rs. 5,486 was paid by the assessee on that basis in December 1976. Audit scrutiny revealed that the value of immovable properties of the assessee worked out to Rs. 12,83,828 on the basis of values adopted in earlier assessments against the value of Rs. 8,59,630 included by the assessee in her return for the assessment year 1976-77. Adding the difference of Rs. 4,24,198 to the net wealth returned by the assessee for the year, the amount of taxable net wealth worked out to Rs. 9,06,200 (after allowing for further deduction towards additional tax liability).

Had the assessment been completed in due time taking into account the correct values of the properties there would have been additional demand of Rs. 32,010 on account of wealth-tax and additional wealth-tax, after adjusting Rs. 5,486 already paid by the assessee.

The Ministry of Finance have accepted the mistake and have stated (October 1983) that remedial action had become time-barred.

B—GIFT TAX

4.16 Gift-tax is levied on the aggregate value of all gifts made by a person during the relevant previous year. All transfers of property which are made without adequate consideration in money or money's worth are liable to tax unless specially exempted by the Gift-tax Act. The term 'property' for the purpose of the Gift-tax Act connotes not only tangible movable and immovable property including agricultural land but also other valuable rights and interests.

4.17 Receipts under gift-tax in the financial years 1978-79 to 1982-83 compared as under with the budget estimates of these years :—

Year	Budget Estimates	Actuals
	(In crores of rupees)	
1978-79	5.75	5.85
1979-80	5.75	6.83
1980-81	6.25	6.51
1981-82	6.25	7.74
1982-83	6.75	7.71*

*Provisional

4.18 Particulars of cases pending assessment and arrears of demand are given below :—

Year	No. of pending assessments	Arrears of demand at the end of (In crores of rupees)
1978-79	21,807	17.72
1979-80	27,403	15.77
1980-81	38,226	29.52
1981-82	53,100	31.16
1982-83	46,553*	21.80*

4.19 During the test audit of assessments made under the Gift-tax Act, 1958, conducted during the period from 1 April 1982 to 31 March 1983, following types of mistakes were noticed :

(i) Gifts escaping assessment.

(ii) Non-levy of tax on deemed gifts.

(iii) Incorrect valuation of gifts.

(iv) Incorrect valuation of unquoted equity shares, and

(v) Mistakes in calculation of tax.

A few important cases of these mistakes are given in the following paragraphs.

4.20 *Gifts escaping assessment*

(i) Records of a private limited company for the assessment year 1977-78 in a company circle indicated the transfer, by two shareholders, of their shares to their relatives without any consideration. No gift-tax proceedings were initiated in these two cases, as the Income-tax Officer of the company circle did not take extracts and send them to the Income-tax Officer connected with these gift-tax assessments. These unquoted equity shares transferred valued Rs. 6,35,580 and Rs. 1,58,895 respectively on the basis of the balance-sheet of the company. For gift-tax levy, however, these shares were to be valued under rule 10(2) of the Gift-tax Rules, 1958 read with the instructions

*(Provisional)

of the Board of Direct Taxes No. 772 of October 1974 and 835 of May 1975 on the basis of the total asset of the company, taking them at their market value including the value of goodwill, whether reflected in the balance-sheet or not. Computed at book value of assets, the total non-levy of gift-tax in this case, after allowing exemption, was not less than Rs. 1,52,953 for the assessment year 1977-78.

The Ministry of Finance have accepted the audit objection in principle.

(ii) Gifts made to institutions established for a charitable purpose are exempt from tax, if such institutions do not enure for the benefit of a particular religious community or caste.

Four co-owners of a building, valuing Rs. 5,18,000, in a city created a trust in January 1979 by settling the building on trust for the benefit of a particular religious sect. As the trust was created for the benefit of a particular religious sect, the exemption from gift-tax was not available. The department did not, however, levy gift-tax. The non-levy of tax in the four cases amounted to Rs. 65,600 in total for the assessment year 1979-80.

The Ministry of Finance have accepted the audit objection and stated (August 1983) that tax raised and collected in one case on assessment is Rs. 30,500 and the remaining three assessments are yet to be finalised.

(iii) Wealth-tax assessments of several private trusts belonging to a family group showed that they transferred in the previous year relevant to the assessment year 1974-75, property held in the form of shares of companies belonging to the same family group to firms, in which they became partners, as their capital contribution, at a value far below their fair market value. Though these transfers attracted gift-tax on the excess of the fair market value of the shares over their declared consideration, action was not taken in any case to levy gift-tax. In fourteen cases noticed during audit of a company ward, aggregate gifts of Rs. 25.12 lakhs escaped assessment in the assessment year 1974-75 with non-levy of tax of Rs. 3,83,886.

The paragraph was forwarded to the Ministry of Finance in August 1983; their reply is awaited (December 1983).

(iv) A private family trust of the same family group introduced as capital, on its entry as a partner in a registered firm in the previous year relevant to the assessment year 1974-75, unquoted equity shares of two different companies controlled by the family group. The values of these shares credited to the capital account of the assessee-trust in the firm's accounts were Rs. 1,404 and Rs. 1,800 as against their market values of Rs. 3,650 and Rs. 7,400 determined by the departmental Valuer as on 31 December 1973. The excess of market value of the shares over the amount credited to the assessee's capital account amounting to Rs. 6,16,030 attracted levy of gift-tax, as deemed gift. The omission to levy gift-tax on this gift resulted in deemed gift of Rs. 6,16,030 escaping assessment and consequent non-levy of gift-tax of Rs. 1,41,309 for the assessment year 1974-75.

The paragraph was forwarded to the Ministry of Finance in July 1983; their reply is awaited (December 1983).

(v) Income-tax records of an assessee, a registered firm, revealed that it had made loans to a privated limited company from 1972-73 onwards. Two senior partners having 40 per cent share in the firm were Chairman and Managing Director of the company. The loans were not connected with its business and were being made when there was no repayment even of interest over the period. The amount of loan outstanding as on 31-12-1978, as shown in accounts of the firm, was Rs. 4,84,625 including Rs. 2 lakhs made in 1978 the period relevant to the assessment year 1979-80. The assessee sold its rights to recover this amount to trustees of a private family trust for Rs. 1,92,000 and debited the balance of Rs. 2,92,625 in its accounts as "expenses" in the previous year relevant to the assessment year 1979-80. The transfer of the right of recovery of loan by the firm was, thus, for inadequate consideration which amounted to gift chargeable to gift-tax. No gift-tax proceedings were, however, initiated. There was consequent escapement of gift of Rs. 2,92,625 and non-levy of tax of Rs. 53,406 for the assessment year 1979-80.

The Ministry of Finance have accepted the audit objection.

(vi) An assessee, who was assessed as an "individual" upto the date of his death on 13 March 1974, died intestate. His heirs a son and daughter, continued his business. The heirs were entitled to equal share in the property of the deceased valued

at Rs. 4,20,000. They, however, distributed various sums totalling Rs. 2,40,000, out of the property of the deceased during the previous year relevant to the assessment year 1975-76, to their relatives such as grandson, granddaughter and daughter-in law of the deceased person. This distribution made in the previous year relevant to the assessment year 1975-76 without consideration to members of the family, other than legal heirs of the deceased, amounted to gift. These gifts by son of Rs. 1,30,000 and by daughter of Rs. 1,10,000 would attract gift-tax in their hands. The gift-tax of Rs. 29,000 was, however, not levied.

The Ministry of Finance have accepted the omission.

4.21 *Non-levy of tax on deemed gifts*

Under the provisions of the Gift-tax Act, 1958, where property is transferred otherwise than for adequate consideration, the amount by which the market value of the property on the date of transfer exceeds the declared consideration is deemed to be a gift made by the transferor and is chargeable to gift-tax.

(i) The income-tax records of an individual assessee showed that, during the previous year relevant to the assessment year 1976-77 (assessment completed in February 1979), a property was sold by him to his sons for a declared consideration of Rs. 1,00,000. The fair market value of the property was determined at Rs. 8,94,300. Since the property was transferred at a declared consideration less than the fair market value, the difference of Rs. 7,94,300 was a deemed gift under the Gift-tax Act. No gift-tax proceedings were, however, initiated. The omission resulted in escapement of taxable gift of Rs. 7,94,300 and non-levy of gift-tax of Rs. 1,93,290.

The Ministry of Finance, while accepting the audit objection in principle, have stated (November 1983) that notice for bringing the escaped gift to tax has been issued and served on 21-10-1982 and the case for valuation of the property has been referred to the Valuation Cell on 14 June 1983.

(ii) Where a partnership firm is reconstituted either with the same old partners or on retirement of some of the partners or on admission of new partners and the profit-sharing ratios of the partners are revised, any interest surrendered or relinquished

by one or more of such partners (without adequate consideration in money or money's worth) in favour of others would attract levy of gift-tax.

During the previous year relevant to the assessment year 1978-79, an individual assessee, holding one-third share in a registered firm, retired from it in May 1976 and withdrew his capital amount of Rs. 1,00,000 in full. The balance of Rs. 1,52,256 in his current account was not withdrawn by him but was distributed equally between the remaining two partners by credit to their accounts in the firm. Similarly, the assessee's balance of Rs. 73,296, held in another firm, was allowed to be appropriated by these other two individuals. The amount of Rs. 2,25,552 (1,52,256+73,296), thus surrendered, attracted levy of gift-tax. Neither the assessee filed any return of gift nor did the department call for the same. The omission led to non-levy of gift-tax of Rs. 36,638 in the aggregate for the assessment year 1978-79.

The Ministry of Finance have accepted the omission in September 1983. Further report regarding assessment and recovery of additional demand is awaited (December 1983).

(iii) In the previous year relevant to the assessment year 1976-77, an individual assessee sold jewellery, containing gold and precious stones, at a total consideration of Rs. 1,04,000. The market value of this jewellery was determined at Rs. 2,50,000 by the assessing officer for levy of capital gains tax. The sale thus involved a deemed gift of Rs. 1,46,000. It was, however, noticed (September 1982) in audit that the department did not call for any gift-tax return. As a result, a gift of Rs. 1,46,000 escaped assessment with consequent undercharge of tax of Rs. 32,500 for the assessment year 1976-77.

The Ministry of Finance have accepted the mistake.

4.22 *Incorrect valuation of gifts*

Under the provisions of the Gift-tax Act, 1958, the value of any property gifted should be estimated to be the price which it would fetch if sold in the open market on the date of gift.

(i) In the gift-tax assessment of an individual assessee, who gifted half and one-fourth shares of a house property in a metropolitan city in the periods relevant to the assessment years 1974-75 and 1975-76, the assessing officer determined (25-5-1981) the values of the gifted property at Rs. 59,500 and Rs. 29,750 as against the returned values of Rs. 32,500 and Rs. 13,750. A scrutiny by Audit (October 1982) revealed that immediately after these gifts, the entire property was leased out at an annual rent of Rs. 60,000. The occupiers were to bear the share of municipal taxes and repair charges. The value of the property under the "rent capitalization" method worked out to Rs. 7,18,392 (12 times of Rs. 60,000 minus Rs. 134 being owner's share of municipal taxes). The value of the gifted parts of the property would work out to Rs. 3,59,196 and Rs. 1,79,598 for the assessment years 1974-75 and 1975-76 respectively. The undervaluation of the property in the assessments made resulted in under-assessment of taxable gifts to the tune of Rs. 4,49,544, with consequent undercharge of tax of Rs. 1,04,172, in the aggregate, for the two assessment years.

While accepting the audit objection, the Ministry of Finance have stated (November 1983) that the Commissioner of Income-tax has set aside the assessment for fresh assessment.

(ii) During the previous year relevant to the assessment year 1981-82, an assessee gifted 60 per cent of a house property owned by her in a metropolitan city, and, valuing the property at Rs. 2,00,000, offered Rs. 1,20,000 for gift-tax. The gift returned was accepted and taxed accordingly on 19-12-1981. The property had been last valued at Rs. 1.45 lakhs on 8-10-1976 and this value had been adopted for wealth-tax purposes for the assessment years 1977-78 to 1980-81. According to the Board's executive instructions issued in December, 1957, value was to be reviewed and revised at normal intervals of three years. This had not been done in the wealth-tax assessment for the assessment year 1980-81. Moreover, the property had been let out at Rs. 2,700 p.m. in the period relevant to the assessment year 1980-81 and at Rs. 6,300 p.m. in the period relevant for the assessment year 1981-82. On the basis of rent of Rs.6,300 per month derived from this property, less municipal taxes and repair charges, the value of the property under rule 1BB of the wealth-tax rules, capitalizing the net maintainable rent at 8 per cent, would work out to Rs. 5,90,625 and the value of 60 per cent thereof which was gifted, would

be Rs. 3,54,375 as against Rs. 1,20,000 brought to tax. The undervaluation of gift by Rs. 2,34,375 led to short levy of gift-tax of Rs. 54,250.

While accepting the undervaluation, the Ministry of Finance have stated (December 1983) that remedial action is being initiated.

4.23 *Incorrect valuation of unquoted equity shares.*

(i) The income-tax return of an assessee for the assessment year 1981-82 showed a long-term capital loss of Rs. 1,44,500 to be carried forward on sale of 3,700 unquoted equity shares of a company (a public limited company not listed on stock exchanges). The shares were shown to have been purchased by the assessee at a cost of Rs. 2 lakhs between 1953 and 1969. The shares of this company had been yielding heavy dividends all along, including issue of bonus shares. The sale of these 3,700 shares was, however, for Rs. 55,500 *i.e.* at Rs. 15 per share, as against their "fully paid" face value of Rs. 3,70,000 *i.e.* at Rs. 100 each. The company, being a public limited company not listed on stock exchanges, had no quotation for its shares. If the principles laid down by the Supreme Court in Jalan's case are followed and the shares are valued under the "yield method", the value of each share would be Rs. 362.26 as against the declared consideration of Rs. 15 each. The omission to bring deemed gift of Rs. 12,84,862 (difference between fair market value of Rs. 13,40,362 and declared consideration of Rs. 55,500) resulted in non-levy of tax of Rs. 3,70,445 for the assessment year 1981-82.

The Ministry of Finance have accepted the mistake.

(ii) In the income-tax assessment of an individual for the assessment year 1980-81, completed in March 1982, capital loss of Rs. 30,300 returned by the assessee was accepted by the department. The loss was computed on the sale of 1010 shares held by the assessee in a private limited company to another company at Rs. 70 per share, its cost being Rs. 100 per share.

Audit scrutiny revealed (September, 1982) that the market value of each share, ascertained by reference to the value of the total assets of the company under the rule 10(2) of the Gift-tax Rules, 1958, worked out to Rs. 266 as on 31 March 1979, as against the sale at Rs. 70 per share. The difference

of Rs. 1,97,960 between the market value and the declared sale consideration attracted levy of gift-tax of Rs. 42,740 (including the effect of non-aggregation of a gift for the assessment year 1977-78 for rate purposes). This levy of gift-tax was not, however, considered by the department for the assessment year 1980-81.

The Ministry of Finance have accepted the omission.

4.24 *Mistakes in calculation of tax*

Under the Gift-tax Act, 1958, as amended by the Taxation Laws (Amendment) Act, 1975 with effect from 1 April 1976, gifts spread over five years are aggregated. Gift-tax is first computed on the gifts of relevant previous year aggregated with gifts of the 'preceding four previous years' (excluding gifts made before 1 June 1973, at the rates of tax for the assessment year in hand. From the gift-tax so computed, gift-tax on the gifts of the preceding four years at the same rate is deducted. The balance is the gift-tax payable.

Such aggregation of gifts was not made in the cases of three individual assessees, while completing assessments in March 1981 on assessed gifts of Rs. 46.38 lakhs, Rs. 62.83 lakhs and Rs. 35.61 lakhs for the assessment year 1976-77. The resultant short levy of tax was of Rs. 6.76 lakhs, Rs. 5.39 lakhs and Rs. 6.93 lakhs respectively. Thus, the aggregate short levy amounted to Rs. 19.08 lakhs for the assessment year 1976-77 in these three cases.

Though the cases were checked by the Internal Audit, the mistake was not pointed out by them in one case. In the other two cases, they pointed out the non-aggregation of gift of Rs. 52,500 and Rs. 59,900 made in the assessment year 1975-76 but not of the other gifts of Rs. 15,46,210 and Rs. 10,70,150 made after 1 June 1973, included in the total assessed gifts of Rs. 20,45,890 and Rs. 11,57,210 for the assessment year 1974-75, in these two cases respectively.

The Ministry of Finance in their reply of September 1983 have accepted the omission. Further report regarding additional demand raised and recovered is awaited (December 1983).

C—ESTATE DUTY

4.25 Receipts under estate duty in the financial years 1978-79 to 1982-83 compared as under with the budget estimates of these years :—

Year	Budget Estimates	Actuals
	(In crores of rupees)	
1978-79	11.00	13.08
1979-80	12.00	14.05
1980-81	13.00	16.23
1981-82	15.00	20.31
1982-83	17.00	20.38*

4.26 The arrears of demand and the number of assessments pending as at the end of various assessment years were as follows :—

Year	No. of assessments pending	Arrears of demand (In crores of rupees)
1978-79	28,278	17.11
1979-80	34,891	17.23
1980-81	35,862	27.65
1981-82	36,581	30.73
1982-83	35,063*	33.91*

4.27 During test audit of assessments made under the Estate Duty Act, 1953, conducted during the period from 1 April 1982 to 31 March 1983, the following types of mistakes resulting in under-assessment of duty were noticed :—

(i) Estates escaping assessment.

(ii) Incorrect computation of the principal value of estates.

(iii) Delay in taking remedial action on internal audit objection.

* (Provisional)

A few instances of these mistakes are given in the following paragraphs.

4.28 *Estates escaping assessment*

(i) The estate of a person, who died in August 1971, comprised individual movable property of Rs. 6,907, one-fifth share of estate left by his pre-deceased grandmother. His share of estate left by his pre-deceased grandmother. His grandmother also had been one-fifth co-sharer of the estate left by his late father.

A sum of Rs. 25 lakhs, representing an *ad hoc* compensation, attributable to the estate of the pre-deceased father of the deceased was received in 1975 from the Custodian of Enemy property, Government of India. The deceased's share in the above compensation amounted to Rs. 6,25,000 (1/5th of Rs. 25 lakhs plus 1/4th of Rs. 5 lakhs attributable to the estate of his pre-deceased grandmother and was includible in his estate. Though the particulars of receipt of compensation were on record, having been disclosed by the accountable person in 1977 before completion of the estate duty assessment on 29 January 1982, these assets escaped assessment. The escapement led to under-assessment of estate by Rs. 6,25,000 with consequent short levy of duty of Rs. 1,74,203.

The paragraph was forwarded to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

(ii) In the case of a person, who died in June, 1971, income-tax of Rs. 5,34,058 pertaining to the assessment years 1945-46 to 1947-48 and 1949-50 was deducted as an outstanding liability from the principal value of the estate in the estate duty assessment made on 26 October 1981. It was, however, noticed that the income-tax demand had already been reduced to Rs. 1,30,952 and the reduced demand collected by adjustment against refunds due in respect of earlier excess profits tax and income-tax assessments. The fact of collection of demand by adjustment had been confirmed by the Income-tax Officer concerned of another charge in a letter of January, 1974. Though the information was with the assessing officer at the time of assessment, it was not acted upon, resulting in excess allowance of liability of Rs. 5,34,058 in computing the principal value of the estate with consequent under-assessment of estate duty of Rs. 1,48,486.

The Ministry of Finance have accepted the omission.

(iii) The properties gifted within two years of the death of the deceased are deemed to pass on death and are includible in the dutiable estate of the deceased.

From the income-tax assessment records of a deceased person (died on 15 November 1976) it was seen in audit that the deceased had been a partner in two partnership firms and had made cash gifts of Rs. 30,000 within two years before the date of his death. The value of his share interests in the firms and the amount of gifts exceeded the no-duty limit for estate duty. His estate was, however, not charged to estate duty. On this omission being pointed out in audit (June 1979), the department brought the principal value of the estate to estate duty in July 1982.

The Ministry of Finance have stated in July 1983 that the assessment has been made in July 1982 and, out of the demand of duty of Rs. 53,354, a sum of Rs. 28,000 has been collected.

4.29 *Incorrect computation of the principal value of estates*

(i) In the estate duty assessment, completed in July 1978 and revised in February 1981, in respect of a deceased person (died in January 1976) an amount of Rs. 2,00,000 was shown, as payable to her as a result of partial partition, in the boos of a Hindu undivided family of which she was a member. This partial partition had also been accepted (March 1973) by the Income-tax Officer for purposes of income-tax and wealth-tax. The amount was not, however, included by the accountable person in the estate. The assessing officer, while determining the principal value of her estate at Rs. 6,00,442 (revised to Rs. 6,22,892 in February 1981), excluded it on the ground that the husband of the deceased had executed a will (1965), leaving all shares in Hindu undivided family property to his grandsons and daughter-in-law. As under the Hindu law, a *karta* of a Hindu undivided family could dispose of, by will, only his share in the common property of the family and not the common property itself, the amount of Rs. 2,00,000 so receivable by the deceased could not have been covered by his will and was includible in the estate passing on her death. The incorrect exclusion of this amount led to under-assessment of the estate by Rs. 2,00,000 and consequent undercharge of duty of Rs. 59,960.

Accepting the mistake, the Ministry of Finance have stated (August 1983) that rectificatory action had been initiated in September 1982.

(ii) Provision for gratuity constitutes only a contingent liability. However, while computing the principal value of the estate of a deceased person (died in June 1977), provision for gratuity amounting to Rs. 95,603 made in the accounts of her proprietory business was incorrectly treated as debt owed by the business and allowed as deduction in its valuation. This mistake led to short levy of duty of Rs. 38,240 in the assessment made in March 1979.

The Ministry of Finance have accepted the mistake and stated (November 1983) that additional duty raised on re-assessment on 30 March 1982 is Rs. 38,240.

(iii) The estate duty assessment made in January 1982 in respect of a person, who died in January 1981, disclosed the following mistakes.

(a) Under the provisions of the Estate Duty Act, 1953, where a deceased person had taken a policy of insurance on his own life for the benefit of his wife and/or his children under the Married Women's Property Act from the very inception of the policy and maintained the same during his life-time, the sum payable on the policy on his death shall be deemed to pass for levy of estate duty. But as the deceased person had never had interest in the policy, the sum payable under it is chargeable to duty as his separate estate. Where, however, a policy of insurance taken had subsequently been transferred or nominated by the deceased person in favour of his wife and/or children, sum payable on the policy on his death shall be aggregated with his other estate for levy of estate duty.

Sums payable under six insurance policies taken by the deceased person on his life and maintained by him during his life-time were incorrectly treated as his 'separate estate' in assessment. These policies had not been originally taken for the benefit of his family under the Married Women's Property Act. The omission to aggregate these policies resulted in short levy of estate duty of Rs. 51,427.

(b) The same deceased person had been carrying on the profession of a legal practitioner in a partnership firm with his son and had retired from the firm on 31 May 1980. After his

retirement, the tenancy right was vested in his son under the retirement deed. The tenancy right was computed at three times the amount of Rs. 16,668, which was the excess of the market rent of Rs. 31,320 over the rent of Rs. 14,652 payable in respect of the premises and 51 per cent share of the deceased therein amounting to Rs. 25,500 was included in his estate as the property passing on death. However, a scrutiny of assessment records revealed that the lease of the above property was for a period of forty years and, the period of lease having commenced from 29 June 1975, its unexpired period exceeded thirty-four years on the date of death. Since the unexpired period of lease exceeded twenty-five years, reversionary interest of the lessor was nil. Consequently, the value of the lessee's right was to be computed under the income-capitalisation method without adjustment in the number of years' purchase. Even adopting a net return of nine per cent, the value of the tenancy right would be Rs. 1.85 lakhs and the deceased's share would be Rs. 94,442, as against Rs. 25,500 adopted. The under-assessment on account of incorrect valuation of deceased's tenancy right as lessee amounted to Rs. 68,942 with short levy of duty of Rs. 27,576.

The combined effect of these mistakes was short levy of duty of Rs. 79,003.

The paragraph was sent to the Ministry of Finance in September 1983; their reply is awaited (December 1983).

4.30 *Delay in taking remedial action on internal audit objection*

For the purpose of checking the correctness of assessments, the Central Board of Direct Taxes have constituted internal audit parties in every Commissioner's charge. According to the executive instructions issued by the Board in 1977, action to rectify the mistakes pointed out in internal audit should be taken by the assessing authorities within a month of the receipt of the objections from them and completed, as far as possible, within three months thereof.

In the case of a person, who died in December 1973, the Assistant Controller of Estate Duty completed the estate duty assessment in June, 1976 on a principal value of Rs. 14,15,433. The assessment was later revised in February 1977 and July 1978 to give effect to certain appellate orders and in June 1981

to rectify some mistakes. In January, 1979, the internal audit party of the department, which had scrutinised the assessment, had pointed out a number of omissions leading to non-inclusion, in the principal value of the estate, the value of certain properties valuing Rs. 2,12,139. Pursuant to the internal audit objection, the Assistant Controller of Estate Duty issued notice in February, 1979 for re-opening the assessment. Audit scrutiny revealed (January 1983) that though nearly four years had elapsed and though the assessment had undergone another revision in June 1981, no action had been taken to rectify the mistakes. The omission involved short levy of duty of Rs. 1,06,069.

The Ministry of Finance have accepted the audit objection.

N. Subramanian

(N. SIVA SUBRAMANIAN)
Director of Receipt Audit-I

New Delhi.
The 18 Feb. 1984 1984.

Countersigned

Prakash

(GIAN PRAKASH)
Comptroller and Auditor General of India

New Delhi.
The 1984.

20-2-1984