REPORT OF THE COMPTROLLER AND AUDITOR GENERAL OF INDIA : UNION GOVT.
(REVENUE RECEIPTS-DIRECT TAXES)
CENTRAL ACTION PLAN (INCOME TAX)
1988-89, NO. 6 OF 1991
FOR THE YEAR ENDED 31 MAR. 1989

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PREFATORY REMARKS

This Audit Report on Revenue Receipts - Direct Taxes of the Union Government (Civil) contains an appraisal on the Central Action Plan (Income-tax) 1988-89.

The points brought out in this Report are those which have come to notice during the course of test audit.

OVERVIEW

1. Monitoring the implementation of the Action Plan of the Department, which has a direct bearing on collection and accountal of revenue, is primarily the responsibility of the department concerned. Action Plans are devised by the Income-tax Department, basically to ensure timely completion of assessments of income-tax returns, and to carry out certain other priority tasks such as arrears collection, settlement of audit objections, etc. The Action Plans lay down in detail, the mode of implementation of the procedure of assessment, including the basis for selection of cases for scrutiny, under the existing Summary Assessment Scheme. The Public Accounts Committee made a detailed study into the working of the various aspects of the Summary Assessment Scheme in its 173rd Report presented to Lok Sabha on 11 August 1989. The Committee had found major deficiencies in the conceptual framework of the Scheme and suggested a thorough re-examination of the Scheme as such. Action-taken Report on the recommendations of the Public Accounts Committee's Report is pending. Meanwhile, the present review, incorporated in this Report, gives a comprehensive analysis of the working of the new assessment procedure, including the revised Summary Assessment Scheme, as implemented through the Action Plan 1988-89 by the Department - especially its effectiveness, impact on revenue and vulnerability from the angle of tax evasion.

2. The striking feature of the Action Plan 1988-89 was that it pierced the ceiling of income limit to bring all returns of income, regardless of the size of the income or loss claimed in the returns, within the scope of the Summary Assessment Scheme. Scrutiny of cases was to be confined to a small percentage of all cases, under specified income groups, according to certain given criteria, the overall scrutiny being restricted to only 3 percent of all returns. Simultaneously, the Action Plan underlined the need for improving the quality of assessments by detection of concealment, and enhancing the level of deterrence by search and seizure, imposition of penalty and recourse to prosecution, etc., so as to foster voluntary compliance. The Scheme also envisaged clearance of all assessments due for disposal during 1988-89 within the same year, except for a part of search and seizure assessments to be carried over to the next year.

3. The findings of audit have been included in this Report in 5 Chapters.

4. Chapter 1 gives an analysis of the method of selection of cases for scrutiny, which by its very nature has to be representiative and revenue-oriented, since the percentage of scrutiny is limited. The Central Board of Direct Taxes had laid down 15 criteria to be followed while making selection of the cases for scrutiny by the Assessing Officers, and had done away with the random sampling method followed in the previous years. This Chapter brings out the deficiencies in such selection of cases, the subjectivity involved, the failure to identify error-prone cases and the need for

modification of the system, and the fact that according to the test-check, 56 percent of all higher income cases (above Rs.5 lakhs) went unscrutinised during the year. Further, the Chapter highlights the failure of the department in its objective of completing all assessments due in the same year (despite fixing limited target to each officer based on his working capacity) under the new Summary Assessment Scheme. There was also no judicious deployment of the expertise of the senior officers (Deputy Commissioners) who were utilised in completing a large number of summary assessment cases instead of only scrutiny of important cases.

5. The test-check by audit had also, revealed that in 11 percent of the assessments above Rs.5 lakhs completed under scrutiny, there were mistakes of one type or other. The extent of concealments detected by the assessing officers from the scrutiny of the records was only 20 percent of the total additions and 11 percent of the gross demands, after such additions, were confirmed in appeal. The above samples do not suggest that there was any significant improvement in the quality of assessments, either. Besides, the total amount of underassessment, etc., pointed by Audit during the year both in respect of summary and scrutiny cases came to over Rs.782 crores.

6. Chapter 2 of the Report highlights the omissions noticed in test-audit in carrying out the prescribed adjustments (arithmetical accuracy and adjustment of carried forward unabsorbed losses, depreciation, etc.). While during the audit of assessments in various circles, a large number of omissions of this nature were noticed, 21 important cases involving a tax effect of Rs.22.96 crores were brought to the notice of the Ministry of Finance.

A few mistakes (tax effect is given in brackets) are given below:

(i) In four cases, brought forward losses of earlier years were clubbed with the current years' losses and the current years' losses were determined in exce ss by Rs.21.55 crores resulting in excess computation of loss by equal amount (Rs.10.64 crores) **[Para 2.01.1, 2, 3, 9]**

(ii) In three other cases, the losses were incorrectly determined at Rs.195.73 lakhs instead of as Rs.70.59 lakhs, which resulted in excess computation of loss by Rs.125.14 lakhs (Rs.64.41 lakhs **[Para 2.01.4, 5 and 6]**.

(iii) Carry forward of loss beyond the prescribed period of 8 years in one case and omission to follow the prescribed order of priority for carry forward of loss, unabsorbed depreciation, etc., in another, led to incorrect carry forward of loss of Rs.6.96 crores (Rs.3.48 crores) **[Para 2.02.1(ii), (vii)]**.

(iv) Carry forward and set off of incorrect amounts of loss and depreciation led to aggregate excess carry forward of loss of Rs.10.02 crores in two cases (Rs.5.06 crores) **[Para 2.01.10, 2.02.1(i)]**.

(v) There was excess computation of loss of Rs.1.06 crores in one case due to consideration of depreciation/ unabsorbed depreciation as part of loss (Rs.61.16 lakhs) **[Para 2.02.1(iv)]**.

(vi) Irregular carry forward of loss and unabsorbed depreciation led to excess carry forward of Rs.1.67 crores in one case (Rs.87.72 lakhs) **[Para 2.02.1(iii).**

(vii) Carry forward of loss in respect of a belated return contrary to law led to excess computation and excess

carry forward of loss of Rs.2.16 crores in one case (Rs.1.13 crores) **[Para 2.02.2]**.

7. In Chapters 3 to 5 of the Report, representative cases of tax escapement under Income-tax, Corporation-tax and Other Direct Taxes respectively (out of 650 cases involving tax effect of Rs.61.80 crores) have been included, with a view to focussing attention to the magnitude and nature of such irregularities. Some of the these cases are given below. The figures in brackets represent the tax effect of each case.

(i) Allowance of unabsorbed deduction of Rs.18.26 lakhs in respect of capital expenditure on scientific research, though the entire investment was allowed to be written off in the year of incurring the expenditure, led to under-assessment of income of Rs.18.26 lakhs in one case (Rs.9.13 lakhs) **[Para 3.03]**.

(ii) There was double allowance of Rs.20.40 lakhs towards the salary of handicapped employees and the weighted deduction thereon, once as debited to accounts and again separately, which led to excess computation of loss by Rs.20.40 lakhs (Rs.10.45 lakhs) **[Para 3.04]**.

(iii) In five cases, omission to disallow expenditure on capital account, etc., aggregating to Rs.5.17 crores led to underassessment of income of Rs.5.17 crores (Rs.2.74 crores) **[Para 3.08.1(i) to (v)]**.

(iv) In one case, allowance of deferred interest of Rs.1.33 crores, which did not represent an ascertained or an accrued liability, led to excess determination of loss aggregating to Rs.1.33 crores (Rs.70.45 lakhs) **[Para 3.08.1(vi)]**.

(v) In two cases, allowance of surtax and foreign taxes aggregating Rs.2.01 crores in the computation of business income led to under-assessment of income of Rs.2.01 crores (Rs.1.13 crores) **[Para 3.12.1(i), (ii)]**.

(vi) Allowance of unpaid sales tax, central exicse duty, contribution to provident fund and other funds, etc., in the case of six assessees led to under-assessment of income of Rs.18.10 crores (Rs.9.29 crores) **[Para 3.13.1(i) to (vi)]**.

(vii) Carry forward of unabsorbed investment allowance of Rs.1.23 crores beyond the prescribed period of 8 years led to incorrect carry forward of unabsorbed investment allowance of Rs.1.23 crores. (Rs.51.54 lakhs) **[Para 4.08(ii)]**.

(viii) Concealed income of Rs.21.19 lakhs pertaining to earlier years, which was detected during the current year, was not added in the relevant years, which led to underassessment of income of Rs.21.19 lakhs (Rs.7.33 lakhs) **[Para 4.11.4(iii)]**.

(ix) In the case of four co-operative societies, carry forward of unabsorbed relief in respect of profits from newly established industrial undertakings, established prior to 31 March 1981, beyond the prescribed period of 7 years led to excess carry forward of Rs.79.12 lakhs (Rs.32.38 lakhs) **[Para 4.12.(i) and (ii)]**.

(x) Net long-term service contract receipts of Rs.73.95 lakhs were not taxed in one case leading to under-assessment of income of Rs.73.95 lakhs (Rs.42.71 lakhs) **[Para 3.15.1(i)]**.

(xi) Non-assessment of refund of central excise duty of Rs.32.74 lakhs led to underassessment of income of similar amount in another case (Rs.21.51 lakhs) **[Para 3.15.2(ii)]**.

(xii) Non-inclusion of central excise duty and sales tax, collected but not deposited to Government account, aggregating to Rs.2.40 crores, in the total income led to underassessment of Rs.2.40 crores in two cases (Rs.1.34 crores) **[Para 3.15.1(iii), (iv)]**.

(xiii) There was underassessment of wealth of Rs.67.95 lakhs in the wealth-tax asessments of an individual due to irregular exemption of compulsory deposit and value of annuity policies (Rs.3.23 lakhs) **[Para 5.02]**.

(xiv) Difference between the market value of Rs.1.50 crores and the actual sale consideration of Rs.56 lakhs on sale, of a house property was not treated as 'deemed gift' in the hands of its two co-owners (Rs.28.08 lakhs) **[Para 5.05]**.

8. The department has been declining to take cognizance of mistakes pointed out by Audit in Summary Assessment cases, which fall outside the purview of the prescribed adjustments, though serious lapses and even evasion of tax do occur in assessments covered by the Summary Assessment Scheme, and many of these are noticed by audit by verification of returns and accompanying records. The fact that these cases escape the attention of the Department largely due to the deficiencies in the procedure for selection of cases for scrutiny, itself suggests the need for taking remedial action in such cases, after they are pointed out by audit. Public Accounts Committee had also recommended in Para 6.8 of their 173rd Report that the Department should rectify all mistakes brought out by audit, which is yet to be implemented.

Chapter 1

General

1.01 The Action Plan

The Central Board of Direct Taxes has been evolving annual Action Plans as an internal mechanism to ensure and monitor achievements of set targets. Such Action Plans are closely linked with the successful implementation of the 'Summary Assessment Scheme' introduced for the first time in 1971. The Action Plans, among other things, identify the key result areas, prescribe the operational instructions which contain the details of the assessment scheme, the norms for disposal of assessments for assessing officers as also the mode of selection of cases for scrutiny assessment, and monitor their implementation through Central Action Plan statements. The system and procedure of accomplishing the tasks of the Department through annual Action Plans embodied the concept of 'Management By Objectives.'

1.02 Key Result Area

The Action Plan envisaged that:

(i) Every assessing officer will complete the prescribed minimum number of scrutiny assessments;

(ii) Assessment of cases other than those selected for scrutiny will be completed in a summary manner;

(iii) Cases will be selected for scrutiny out of all income groups but the number of cases to be selected will depend on the number of assessing officers and their working capacity;

(iv) There will be no pendency except carry over of a part of search and seizure assessments of the total work-load of pending assessments;

(v) The scheme will cause a proper level of deterrance;

(vi) Since cases with real potential for detection of concealment and launching of prosecution will be selected for scrutiny, the quality of assessments would improve appreciably.

1.03 Action Plan 1988-89

The Action Plan for the year 1988-89 relied on the co-operation of the tax payers and their integrity in completion of assessments under 'Summary Assessment Scheme', and sought deterrent punishment for any gross misdemeanour. A copy of Central Action Plan 1988-89 is given as Annexure.

A. Assessment Scheme

Under the Action Plan for 1988-89, a small percentage of the cases in specified incomes will be scrutinized as the 'working capacity' of the available manpower of the Department permitted. The rest of the cases will be disposed of irrespective of the status or income group of the assesses in summary manner. The random sample scheme was discontinued from the financial year 1988-89. There were separate norms for each level of assessing officers and the number of cases to be selected depended on the number of assessing officers available in a charge

and their 'working capacity'. For this purpose assessments were categorized under four groups(A, B, C, D,) with distribution of work as under:

		Company cases	Non-company cases
Category A	(Income-tax Officers)	Below Rs. 50,000	Below Rs.2 lakhs.
Category B	(Assistant Commissioners) of Income-tax)	Between Rs. 50,000 to Rs. 5 lakhs	Between Rs.2 to 5 lakhs
Category C	(Dy.Commissioners of Income-tax (Assessment)	Above Rs.5 lakhs	
Category D	(Assistant Commissioner of Income-tax)	Search & Seizure cases	

B. Norms for scrutiny cases

The norms for disposal of scrutiny assessments for officers of different levels were as follows:

(i)	Deputy Commissioner (Assessment)	
	Without any Income-tax Officer	35 core assessments
	With one Income-tax Officer	60 core assessments
	With two Income-tax Officers	75 core assessments
	With one or two Assistant Commissioners	100 - 120 core assessments
(ii)	Assistant Commissioner of Income-tax	150 assessments
(iii)	Income-tax Officer	100 assessments

C. Assessment procedure

According to the procedure prescribed in the Central Action Plan, out of the total workload of the pending assessments, only a part of search and seizure assessments would be carried over to the year 1989-90, while all the remaining cases would be finalised during 1988-89 itself. Assessments for scrutiny will be selected from out of the arrear assessments brought forward on 1 April 1988 and the current workload for the year 1988-89, according to the norms of disposal laid down. However, as per work norms, each assessing officer will dispose of the prescribed number of scrutiny assessments only and will

carry forward any balance to the next year. There will no random sampling scheme with effect from financial year 1988-89.

D. Selection of cases for scrutiny

According to the procedure prescribed, the asessments for scrutiny will be picked up on the basis of error (*i.e.* erroneous claims of deductions, allowances and reliefs), potential for evasion and for concealment of income. Illustrative of the criteria to be adopted while making selection of scrutiny assessments are:

(i) Low gross profit/decline in gross profit in relation to turnover.

(ii) Adverse points in the past history of the case.

(iii) Special outside information.

(iv) Existence of qualifications in Auditor's Report including Compulsory Tax Audit Report under Section 44AB.

(v) Industries/Trades which had made abnormal profits in the accounting year.

(vi) Inadequate incomes declared in the past as compared to wealth.

(vii) Claim of obvious inadmissible deductions, or exemptions or exempted income *e.g.*, agricultural income.

(viii) Large scale investments or increase in assets or increase in loan liabilities.

(ix) Expansion in cases belonging to one group.

(x) Low withdrawals for household expenses.

(xi) Personal knowledge (reduced to in writing by the assessing authority).

(xii) Inordinate delay in filing the return.

(xiii) Assessments where notices under Section 147 or 139(2)/142(1) had been issued.

(xiv) Arrear assessments where investigation so far conducted indicated possibility of establishing concealment.

(xv) Cases where the size of the turnover was suspected with reference to the available working capital.

The guidelines were fairly exhaustive and covered a number of potentially vulnerable areas to be looked into during investigation and assessment.All the same, it must be difficult for the assessing officers to take care of each and every factor and decide on the limited number of cases to be selected for scrutiny. Besides, in any such selection, the element of subjectivity could not be avoided. Even an earnest assessing officer would find it difficult to apply the larger number of the criteria laid down by the Board to the generality of the cases.It is also relevant that the criteria did not include high-income cases or industry wise evasion potential. Moreover there was no monitoring of how the assessing officers went about the selection of scrutiny cases. As compared to the 'random sampling' method which was applicable prior to

1988-89, the revised method of selection can not, thus, be said to be a more efficient technique. On the other hand, if the present system (after it is streamlined to identify error-prone cases by a more scientific selection for scrutiny), is supplemented with a selective random sampling method, the deficiencies in the system could be overcome to a great extent. Efficient use of computerised Management Information System (MIS) would also, ultimately, help the Department in proper system of selection of cases for scrutiny.

The deficiencies and shortcomings in the method of selection of cases for scrutiny, noticed during the review are given in Para 1.09 *infra*.

1.04 Action Plan for earlier years vis-a-vis that of 1988-89

Under the Income-tax Act, 1961, with effect from 1 April 1971, *i.e.*, from assessment year 1971-72, assessing officers were empowered to complete assessments in a summary manner, subject to certain prescribed adjustments to the income/loss returned. During the years from 1971-72 to 1987-88 the scope of the Summary Assessment Scheme under this provision of the Act,was enhanced periodically to cover assessees depending on the status and income group varying from Rs. 25,000 to Rs. 2 lakhs, subject to a random sample scrutiny. A detailed review of the Summary Assessment Scheme was included in Comptroller and Auditor General's Report on Direct Taxes for the year 1986-87.

With the extension of the summary assessment to all levels of income from 1988-89, with scrutiny only of a limited number of cases, the percentage of overall scrutiny came down. The liberalisation of the summary assessment scheme was intended to promote voluntary compliance on the basis of mutual trust and reciprocation. According to the Action Plan of 1988-89, the underlying objective was to improve the quality of assessments, with detection of concealment, and to achieve a level of deterrence by launching prosecution wherever necessary, as otherwise the new assessment procedure could be misused by unscrupulous tax payers.

1.05 Recommendations of Expert Committees

The Administrative Reforms Commission (1969), the Wanchoo Committee (1971) and the Chokshi Committee (1978) had all approved the summary assessment of all small income cases subject to a random sampling to cope up with the overwhelming workload. The criteria suggested specifically excluded company cases and sensitive cases. The Economic Administration Reforms Commission (1981-83) observing that the aim should be to complete the scrutiny of all selected cases within the same year, had recommended selection of cases as a percentage of the total number of cases, upto the predetermined quantum of workable disposals, on the basis of certain essential criteria,viz., scrutiny of all high income cases, search and seizure, etc., and others on the basis of a random sampling within the overall percentage. The Committee had noted that the selection of cases on the basis of error potential as in the United States is not feasible in India as that would require a high degree of computerisation.

1.06 Recommendations of the Public Accounts Committee

The Public Accounts Committee in their 217th Report (Seventh Lok

Sabha) (1983-84) on 'Cost of collection' had recommended that the Board must keep constantly reviewing the Summary Assessment Scheme and take necessary steps to simplify the procedure so that minimum possible time is spent on summary assessments and the manpower so released could be utilised for scrutiny of large revenue cases. Subsequently, the Committee reviewed the implementation of the Summary Assessment Scheme in detail during 1988-89 and made extensive recommendations in its 173rd Report (1988-89) presented to the Parliament on 11 August 1989.

1.07 Scope of Audit

Since the most important function of the Income-tax department,viz' collection of the targetted income-tax through timely and effective assessment of returns and by widening of the tax-base, is sought to be achieved through summary assessment and selective scrutiny, the Central Action Plan is a mode of implementation and monitoring of the Summary Assessment Scheme. This review analyses the performance of the Central Action Plan of the Central Board of Direct Taxes for 1988-89 and evaluates whether it has succeeded in its implementation and in achieving the desired objective. Since, effective from 1988-89, the Summary Assessment Scheme covers all income-tax assessments regardless of the amount of the returned income, the audit observations included in this review are all those noticed in respect of cases assessed in a summary manner. The audit observations which were noticed in cases covered by scrutiny assessments have been separately reported in the regular Audit Report on Direct Taxes for the year ended 31 March 1990.

1.08 Highlights

(1) The department of Income-tax introduced Summary Assessment Scheme in a limited manner from 1 April 1971 to provide for assessment of returns which are, *prima facie,* correct and complete in all material respects in a summary manner. According to a note submitted by the Ministry of Finance to the Public Accounts Committee (1983-84) (Seventh Lok Sabha) during evidence on an audit paragraph on 'Cost of collection', the underlying objectives behind the selective approach in the completion of assessments are:

(i) Reduction of mounting arrears of work;

(ii) Cutting out useless, infructuous, and unproductive work involved in the small revenue cases;

(iii) To dovetail the workload to match the available manpower resources of the department for achieving more efficiency and effective output by the department;

(iv) Deployment of the manpower so saved on higher income cases to achieve better results;

(v) To check the menace of tax evasion and tax avoidance in bigger cases.

Various Expert Committees and the Public Accounts Committee had advocated a selective approach in the completion of assessments of relatively small importance from the point of revenue subject to a random sampling, but generally were not in favour of including in its scope, high income cases,

particularly company cases, cases of search and seizure and sensitive cases warranting scrutiny on the basis of any available information or suspected tax evasion. In spite of this, the Ministry, over a period of time, extended the Summary Assessment Scheme to all assessments, regardless of income level. In order to accomplish the task of achieving the avowed objectives of the Scheme, the Department introduced Central Action Plans setting out the targets in respect of different important items of work to be performed at different levels. A review of the Central Action Plan for 1988-89, however, revealed that the main purpose of the Summary Assessment Scheme by far had turned out to be achieving nil pendency of assessments at the end of the year, rather than aiming at the broader objectives behind a selective approach, as placed before the Public Accounts Committee. This was evident from the fact that while the workload to be cleared by assessing officers had progressively been brought down by reducing the number of cases for scrutiny, very little had been gained in improving 'the efficiency and effective output by the department', in deployment of savings in manpower on higher income cases or to check the 'menace of tax evasion and its avoidance' in bigger cases.

A test-check by audit, all over the country, brought out that out of a total 25,346 cases above Rs. 5 lakhs spread over in 660 wards in 77 Commissioners charges, 14,314 cases, *i.e.*, 56 per cent of the higher income cases, were assessed in summary manner. These cases included 433 cases (39 per cent of 1106) above Rs. 50 lakhs and 1508 cases (48 per cent of 3,157) above Rs. 10 lakhs. The decision to enlarge the scope of the summary assessment scheme to cover all income groups had obviously led to a number of high value and tax yielding cases falling outside the ambit of scrutiny assessments.

(2) The Central Action Plan 1988-89 envisaged nil pendency (except for a part of the search and seizure assessments) under the revised norms. This, however, had not come true. Nearly 10 lakhs assessments, including 1.38 lakh scrutiny assessment were pending at the end of the year. The pending cases included 1.30 lakh assessments of over Rs. 1 lakh each. The pendency (13.37 per cent of the total number of cases due for disposal during the year) was despite the fact that the number of cases for disposal by scrutiny was to be determined on the basis of the working capacity of the assessing officers.

(3) The institution of the Inspecting Assistant Commissioner (Assessment) (now Deputy Commissioner) was created in October 1978 pursuant to the recommendations of the Public Accounts Committee that senior officers of the department should be directly associated with assessment work, with a view to utilising the experience gained by senior officers in making assessments in higher and complicated cases (Rs. 5 lakhs and above) and actively associating them in the day-to-day progress in completion of assessments, resulting in proper co-ordination and scrutiny.

According to the Central Action Plan 1988-89, every officer was required to complete a certain number of scrutiny assessments, and complete the rest in summary manner. With the decision to bring all assessments into the fold of summary assessment scheme, a large number of high value cases were assessed summarily and the number of scrutiny assessments in respect of cases above Rs. 5 lakhs came down. So much

so, Deputy Commissioners were also assigned the task of completing summary assessments of big cases. The deployment of these senior officers to complete summary assessments was not envisaged under the scheme of creation of these posts and can not be said to be the most useful and productive deployment of the available human resources.

(4) According to the Central Action Plan 1988-89, the accent was on a thorough and investigative scrutiny of selected cases with a view to ensuring quality. The instructions that contained in the Action Plan envisaged that the summary assessmemts should be free of arithmetical errors and mistakes in the prescribed adjustments in carry forward of losses, etc. The scrutiny assessments, especially those completed by the senior officers should be complete, legally, and arithmetically correct, devoid of any error.

The test-check by audit in 660 assessment wards revealed under-assessment of tax in 8,574 cases. Of these, the number of audit observations raised in respect of cases with income range above Rs. 5 lakhs was 2,266 (26 per cent).

Another study of 32,871 selected scrutiny assessments in different Commissioners' charges, for the five years period 1984-85 to 1988-89, revealed that a substantial part of the additions made to the returned income in those cases was by way of normal (routine) adjustments required to be made under the various provisions of the law, and the extent of concealment/evasion detected by the department during the course of investigations was only 17 per cent. The Department has not evolved any bench mark to determine the level of efficiency of scrutiny assessments. Moreover, in respect of demands raised for levy of tax as a result of both the above additions, only 11 per cent of the gross demands had been confirmed in appeals. The position regarding prosecution and penalty was also not appreciable since the department was able to obtain convictions in only 8 out of 172 cases (4.6 per cent) for which prosecutions were launched, though it was able to sustain about 50 per cent of the penalty imposed for concealment, etc.

The above statistical analysis would suggest that the emphasis on qualitative and deterrent assessments as envisaged in the Action Plan, had also not been adequately fulfilled.

(5) Justifying the achievements of the summary assessment scheme, the Ministry of Finance had deposed before the Public Accounts Committee(1989-90) (Eighth Lok Sabha), while tendering evidence on an audit paragraph on 'Assessment Procedure - Summary and Scrutiny assessments' that (i) there was increase in the pace of disposal of assessments, (ii) there was sustained and detailed investigation in selected revenue yielding cases leading to prosecutions, (iii) the tax base had been broadened, (iv) the public relations had improved, and above all (v) tax collections had gone up. The Ministry had, however, failed to identify the increase in assessment cases and tax collections attributable to the summary assessment scheme with any basic data and the Committee had noted that the increase in assessees was mainly attributable to increase in levels of income rather than the scheme, the increase in collection was due to special schemes and the revenue results of reported diversion of staff for search and seizure was marginal and had recommended that the extent of coverage under scrutiny as-

sessment scheme should be substantially increased pending a relook into the effectiveness of the scheme. The Central Action Plan for 1989-90 did, not only, continue the then existing scheme of selection of cases, but also dispensed with the prescribed percentages of 2,16,28 as mentioned in para 1.10 infra and limited the number of cases to be selected for scrutiny to certain prescribed minimum depending on the 'working capacity' of the assessing officers so as to result in nil pendency at the end of the year.

The collection of taxes in 1988-89 went up by Rs.2,071.58 crores from Rs. 6,757.18 crores in 1987-88 to Rs. 8,828.76 crores in 1988-89. While the increase, *per se,* is welcome and substantial, it is not feasible to analyse to what extent this was on account of implementation of the Central Action Plan 1988-89 and the Summary Assessment Scheme. The year 1988-89, however, had certain specific attributes as would have added to the buoyancy in collections, such as (a) as per the targets laid down in the Action Plan for 1988-89, a 10 per cent collection out of the total demand (arrear and current) pending collection was envisaged, a special 'Time Window Scheme' was in operation for 3 months from 1 July 1988 to 30 September 1988 as an incentive for realisation of tax arrears with a 50 percent reduction in interest, all companies and non-companies above income limit of Rs.50,000 were liable for a 5 per cent surcharge for the whole year, there was notable increase in tax deductions at source due to general increase in levels of income, the wholesale extensions of previous years, as a prelude to uniform accounting year, introduced with effect from 1 April 1989, had resulted in additional collection, and with * a normal inflationary rate of 8.5 per cent, and increase in GNP by 10.4 per cent, a normal growth rate of income-tax by 8-10 per cent was only to be expected. The expectations in respect of increased voluntary compliance and voluntary return showing true and correct incomes could not be said to have been achieved despite the abundant faith placed on the tax payers.

(6) For the purpose of the Action Plan, all assessments were grouped under four categories, A, B, C and D, the level of income/loss returned determining the categorisation. The income/loss limit differed for company and non-company assessments, but did not make any distinction between the different types and classes of assessees. Thus, a salary income case could get bracketed with that of a case relating to hawala-business or real estate, under the same catetgory.

On the other hand, the selection of cases based on gross income/receipts depending on the class of tax payers or some similar method would have more deterrence. Also, if under the Central Action Plan, selection was regulated with the potential for error/evasion, by classifying the assessees into various classes, the system would have been more reliable.

(7) According to the prescribed procedure for selection of cases for scrutiny, cases were to be selected on the basis of error and evasion potential. The large number of criteria laid down in the Action Plan would necessitate scrutiny of a large number of cases to enlist at least a number of them for scrutiny. Besides, in selecting the cases, the element of subjectivity was inescapable in the absence of any monitoring

* Source: Chapter 1 - Para 2 of Economic Survey 1989-90

mechanism. The absence of a random sampling method, either as such or to supplement selection based on the guidelines was another deficiency. The individual irregularities in respect of non-scrutiny cases discussed in this review would suggest that the errors could have been avoided had the selection been broadly made according to the criteria laid down in the Action Plan since bulk of the mistakes noticed were under categories falling under inadmissible deductions or exemptions or exempt income, cases to be accompanied by qualified Audit Reports, cases where the returns were filed late and cases with adverse past history, all covered under the guidelines. The 'random sample' scrutiny which was in practice earlier was perhaps a more effective tool of managerial control. The discontinuance of 'random sample' scrutiny and switch over to a selective scrutiny based on broad criteria, as the test results had indicated, did not, in any way, reduce the scope for abuse of the scheme.

(8) According to the extant instructions, every assessing offcer shall complete a minimum number of scrutiny assessments in a year, according to the category to which the officer belonged. The remaining cases with each assessing officer will be completed in summary manner. The target for disposal of summary cases for each assessing officer was between 4,500 to 6,000, depending on the requirement of the charge and the stage of computerisation. The disposals were, however, far below the targets, ranging between 270 and 3579 on an average.

(9) The test-check by audit revealed many irregularities of diverse nature, covering the entire tax laws, involving undercharge of tax of Rs.114.88 crores in 8,231 cases assessed in a summary manner. Like-wise in another study,cases completed after scrutiny were found to suffer from undercharge of Rs.667.26 crores in 14,366 cases (63.52 per cent). The nature and extent of the mistakes in mandatory adjustments gave the impression that the income returned in non-scrutiny returns were generally accepted without any preliminary check.

In sum, the Central Action Plan 1988-89 had failed in its objective of finalising all assessments (except for a part of summary and scrutiny assessments) during the year, despite dilution of the rigour of the scrutiny in terms of numbers, drastically. The discontinuance of the system of 'random sampling' and its replacement with selection based on certain given guidelines was not satisfactory in view of the inadequacy of safeguards, in identification of error-prone cases. The operational instructions did not provide for intensive scrutiny of all or at least a substantial number of high-income cases as recommended by Experts/Public Accounts Committees.

The large number of audit observations involving Rs.782.14 crores in 22,597 cases indicated that either in respect of the prescribed checks for summary assessment or the detailed checks in scrutiny cases, there were a number of shortcomings and deficiencies, as would call for streamlining the procedures, and that the quality of assessment has not improved despite introduction of summary assessment scheme and Central Action Plan. The system also leaves many avenues open for unscrupulous assessees to evade tax since the deterrance under the Scheme is not adequately pervasive.

As recommended by the Public Accounts Committee in its the Report,

the entire scheme warrants an immediate review in respect of the job classification, including that of the deployment of manpower especially at the Senior level,of the instructions regarding selection of cases for scrutiny and above all, qualitative improvement in the assessments proper.

1.09 Selection of cases for scrutiny

As stated in Para 1.03 *supra* Central Action Plan 1988-89 enumurated in detail the criteria for selection of cases for scrutiny by assessing officers. The Plan envisaged that by observing the guidelines, mostly 'error potential' cases would get selected for scrutiny. As a corollary, generally speaking, the summary cases would be those other than such 'error prone' cases. During the review, however, it came to notice that the block of summarily assessed cases, in most circles, included a large number of cases with explicit error potential, particularly cases falling under one or more of the following criteria:

(i) Understatement of profit;

(ii) Cases which were not accompanied by qualified Audit Report;

(iii) Cases where the returns were filed inordinately late;

(iv) Cases involving inadmissible deductions/exemptions etc;

(v) Cases with adverse points noticed during their past assessments;

(vi) Cases with mistakes involving substantial amounts.

A few illustrative cases are given below

(a) Low gross profit/decline in gross profit in relation to turnover

Test-check in Madhya Pradesh, Orissa, Rajasthan, Bihar, Uttar Pradesh and Himachal Pradesh audit circles disclosed 69 cases where the assessees had returned very low profit rate as compared to the earlier years.The tax effect involved in these cases came to Rs. 20.83 lakhs.

Name of the Circle	Assessee	Assessment year	Nature of objection	Revenue effect (Rs.)
(i) Madhya Pradesh	Regd.Firm 1988-89	1985-86 1988-89	Rate of gross profit of 9 percent accepted by assessee in assessment year 1984-85 not returned in later years.	1,00,605
(ii) Orissa			In 25 cases, low profit rates were adopted.	4,46,248
(iii)Rajasthan	Contractor	1986-87 to 1988-89	In 3 contractors' cases the rate of profit was adopted at 3 to 6 per cent instead of at 10 to	4,19,305

			20 percent adopted in earlier years (under assessment of income by Rs.9,19,387).	
(iv) Bihar	Regd. Firm	1988-89	Rate of profit was adopted at 1.75 per cent instead of 8.75 per cent as in 1987-88.	2,88,661
(v) Uttar Pradesh	Regd. Firm	1986-87 to 1988-89	Rate of profit of 4.5 per cent to 6.5 per cent was adopted although in past years the firm was assessed by applying a rate of 10 per cent as agreed to by the appellate authority and the assessee. under-assessment of income by Rs.3,11,436).	96,523
(vi) Himachal Pradesh	Regd.Firm	1985-86 to 1988-89	In 33 cases adoption of low rate of profit than in earlier years resulted in under-charge of income by Rs. 14,40,479.	5,96,425

(b) Inordinate delays in filing of return

Under the Income-tax Act, 1961, with effect from 1 April 1985, no loss under the head 'Profit and gains of business or profession' is allowed to be carried forward for set off unless the assessee has filed the return of loss voluntarily within the due date or within such further time as may be allowed by the Income-tax Officer. Under the Central Action Plan 1988-89, such cases were to be selected for scrutiny, but the test-check disclosed omissions to do so, as in the representative cases given below:

(i) In Bombay circle, an individual filed his returns of income for the assessment years 1986-87 and 1987-88 declaring income of Rs. 70,420 and Rs. 38,664. The assessments were completed summarily in December 1988 accepting the income as returned. It was seen from the statements of income filed along with the returns that the shares of profit from a registered firm, amounting to Rs. 37,405 for the assessment year 1986-87 and Rs. 61,428 for the assessment year 1987-88, were set off by the assessee against brought forward loss of the same firm for the assessment year 1985-86.

The above firm had filed its return of income for the assessment year 1985-86 showing a loss of Rs. 9,36,308 on 30 March 1988, though the due date was 31 July 1985, in pursuance of a notice issued by the asessing officers for escapement of income. As the return of loss of the firm for the assessment year 1985-86 was not filed voluntarily in time, the firm forfeited the benefit of carry forward of the loss. Hence, the loss of the firm for the assessment year 1985-86 was not to be brought forward and set off in the hands of the partners. The incorrect set off of brought forward loss of the firm in the assessment years 1986-87 and 1987-88 resulted in under assessment of income of Rs. 98,833 involving short levy of tax of Rs. 50,514 including interest for delayed filing of return and short payment of advance tax.

(ii) In Bombay circle, an assessee company, whose previous year ended on 30 June, filed its return of loss of Rs. 2.13 crores for assessment year 1986-87 on 23 November 1987 as against the due date of 30 June 1986. The returned loss was accepted by the Deputy Commissioner of Income-tax in the assessment for the assessment year 1986-87 completed summarily in October 1988 and the loss was allowed to be carried forward. As the return of loss was filed beyond the due date, the loss should not have been carried forward. The mistake resulted in incorrect carry forward of loss by Rs. 2.13 crores involving potential short levy of tax of Rs.1.12 crores.

(iii) An assessee company filed its return of loss of Rs. 12.64 lakhs, comprising unabsorbed depreciation of Rs. 2.31 lakhs and business loss of Rs. 10.33 lakhs for assessment year 1986-87 on 23 July 1987 after the prescribed due date of 30 June 1987 for filing the return. The assessee had not sought extension of time for filing the return. The assessing officer, however, summarily accepted the loss as returned and allowed it to be carried forward for set off in future years while completing the assessment in February 1989. As the return was filed late the carry forward of business loss of Rs.10.33 lakhs was not allowable. The irregular carry forward of business loss resulted in potentital short levy of tax of Rs. 5.96 lakhs.

(c) Qualified Audit Reports, etc.

A large number of cases, covered by qualified Audit Reports, inadmissible deductions or exemptions and adverse points noticed in the past history of the assessee, etc., came to notice during test-audit of the assessments in different circles during the year. Selected cases falling under the above categories have been detailed in Chapters 3, 4, 5 of this Report under appropriate headings.

1.10 Growth of assessees, assessments, tax collections, etc.

Prior to 1988-89, the summary assessment scheme covered non-company cases with income returned upto Rs.2 lakhs, and company cases upto Rs. 50,000. The ceiling limits were pieced with effect from 1988-89, when the summary assessment scheme was extended to all income groups, irrespective of the income/loss of the tax payers, subject to scrutiny of only a small percentage of cases as given below:

Category of assessment	Status of tax payer	Income/loss limit	Percentage
A	Companies	Upto Rs.50,000	2
	Non-companies	Upto Rs. 2 lakhs	
B	Companies	Rs. 50,000 to Rs. 4,99,999	16
	Non-companies	Rs. 2 lakhs to Rs. 4,99,999	
C	Companies	Rs.5.00,000 and above	28
	Non-companies	Rs.5,00,000 and above	
D	Search and seizure assessments		50 assessment per Dy. C.I.T. (Assessment)

However, under the Action Plan, the assessing officers were required to do only a certain minimum number of scrutiny assessments in a year as mentioned in para 03.B (Minimum of 50 assessments per annum for Assistant Commissioner in the case of search and seizure casesa subject to 100 per cent disposal of search cases upto 31 March 1987).

The following statement gives the growth of the number of assessees, assessments due for disposal and actually disposed of, tax collections, and the number of officers on assessment duty during the last six years:

Year	1983-84	1984-85	1985-86	1986-87	1987-88	1988-89 (Year of present review)
Tax Collection- (In crores of rupees)	4,498.38	4,797.33	5,621.83	6,236.46	6,757.18	8,828.76
Addition of assessees (Survey)	2,81,788	1,41,617	1,05,638	6,55,653	5,23,376	4,98,176 **
Total Number of assessees (in lakhs)	49.32	49.38	55.02	62.61	65.18	68.11 **
No. of assessments due for disposal(in lakhs)						
Summary	51.66	49.77	63.14	78.83	70.43	66.95
Scrutiny	17.26	16.66	7.54	6.32	5.30	4.31
Total	68.92	66.44	70.68	85.15	75.73	71.26
No. of assessments completed(in lakhs)						
Summary	38.40	42.75	54.55	66.70	61.24	58.80
Scrutiny	9.71	11.14	4.61	3.86	3.41	2.93
Total	48.11	53.89	59.16	70.56	64.65	61.73

Year	1983-84	1984-85	1985-86	1986-87	1987-88	1988-89 (Year of present review)
No. of assessments pending (in lakhs)						
Summary	13.26	7.02	8.58	12.12	9.19	8.15
Scrutiny	7.55	5.52	2.93	2.47	1.88	1.38
Total	20.81	12.55	11.59	14.59	11.07	9.53
No. of Officers on assessment duty	-	-	3417 +179	2447 +151	2057 +161	1947 +149*
			3596	2598	2218	2096

* Information collected from the Annual Report of the Ministry of Finance (1989-90)

** According to the figures furnished by the Ministry of Finance and included in the Audit Report for the year ended 31 March 1989.

A perusal of the above statistical information will reveal the following:

(1) While according to the Finance Ministry, the number of tax payers (assessees) added during 1988-89 by survey operations was 4,98,176 the increase in the number of assessees during 1988-89 as per information regarding the number of assessees furnished by Ministry of Finance to audit was only 2.93 lakhs.(68.11 lakhs from 65.18 lakhs in 1987-88).

(2) The number of assessments selected for scrutiny during the years 1986-87, 1987-88 and 1988-89 gradually came down to 3.39 lakhs, 2.83 lakhs and 2.43 lakhs excluding arrears brought forward, while the number of assessing officers on duty came down from 2598 to 2218 and 2096 respectively. The average number of cases scrutinised by each officer varied during the year from 133 to 153 to 139 which was due to the decision to prescribe certain minimum number ofscrutiny cases per officer, according to his 'working capacity'. The resultant saving in manpower was to be used for search and seizure, investigation etc.

(3) The number of assessments due for disposal and that actually disposed of also declined in 1988-89 as compared to 1987-88. The number of pendency in assessments did not, however, come down in 1988-89 as envisaged in the Action Plan. During the year 1988-89, there was a perceptible decline in the number of summary and scrutiny assessments completed when the assessment norms were standardised, though the number of officers on assessment duty were 2218 in 1987-88 and 2096 in 1988-89.

(4) The tax collections registered an increase of Rs.2071.58 crores in 1988-89 as compared to the collections in 1987-88, the reasons for which are given in Para .08(5) ***supra***.

1.11 Classification

Details of the assessee and assessments pending, status-wise and income range-wise, for the two years 1987-88 and 1988-89 were

		Companies		Non-Companies		Total No. of assessees/ No. of assessments pending
		No. of assessees	No. of assessment pending	No. of assessees	No. of assessment pending	
Upto Rs.1 lakh	31.3.1988	0.28	0.29	50.69	9.51	50.97/9.80
	31.3.1989	0.37	0.21	53.95	8.02	54.32/8.23
Rs.1 lakh to Rs. 5 lakhs	31.3.1988	0.11	0.14	1.52	0.97	1.63/1.11/
	31.3.1989	0.13	0.12	2.19	1.02	2.32/1.14
Above Rs.5 lakhs	31.3.1988	0.08	0.09	0.08	0.07	0.16/0.16
	31.3.1989	0.08	0.08	0.11	0.08	0.19/0.16

(Figures in lakhs)

Though the number of assessments to be selected for scrutiny was reduced from 5.30 lakhs in 1987-88 to 4.31 lakhs in 1988-89 under the Action Plan, there was only marginal decrease in the pendency in company assessments, while in the case of non-company cases, there was no reduction at all in the higher slabs. The overall position also, in respect of higher slabs was not satisfactory.

1.12 Quantum of disposal (income-wise)

The following are the particulars of the number of assessments completed, summary and scrutiny, during 1988-89 and the income range of the assessments completed in 660 charges under 77 Commissioner's charges.The percentage of summary assessments was 94 and scrutiny assessments 6.

Sr. No.	Name of Circle	No. of CIT/ CsIT	No. of representative wards audited	No. of assessments completed 1988-89	No. of assessments completed u/s 143(1)	No. of scrutiny assessments [(5)-(6)]	Percentage of summary assessments over scrutiny assessment	Assessment cases with income above Rs.50 lakhs		Assessment cases with income above Rs.10 and Rs.50 lakhs		Assessment cases with income between Rs.5 lakhs and Rs.10 lakhs		Assessment cases with income between Rs.50,000 and Rs.5 lakhs	
								Scrutiny cases	Summary cases	Scrutiny cases	Summary cases	Scrutiny cases	Summary cases	Scrutiny cases	Summary cases
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)
1.	Maharashtra	16	-	12,65,370	12,17,625	48,105	96.2/3.8	-	-	-	-	6,388	10226	-	-
2.	West Bengal	8	24	8,054	6,480	1,574	80.5/19.5	138	103	214	227	214	258	573	596
3.	Delhi	10	107	2,07,659	1,98,592	9,067	95.6/4.4	101	70	322	388	540	813	5,648	25,714
4.	Tamil Nadu	5	20	18,245	16,424	1,821	90/10	61	27	165	114	102	108	483	1,665
5.	Karnataka	4	53	74,081	69,008	5,073	93.2/6.8	138	115	279	391	331	416	2,712	7,361
6.	Gujarat	7	43	1,22,900	1,18,637	4,263	96.5/3.5	6	-	21	4	72	43	1,998	12,507

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)
7.	Kerala	2	20	19,196	17,517	1,679	91.2/8.8	20	3	66	61	96	65	670	2,468
8.	Madhya Pradesh	2	51	1,41,176	1,13,134	10,042	92.9/7.1	13	-	71	3	167	5	3,494	14,812
9.	Bihar	2	65	1,76,259	1,69,973	6,286	96.4/3.6	11	19	53	54	106	56	2,410	5,703
10.	Punjab	3	30	51,548	47,793	3,755	92.7/7.3	1	-	11	1	19	2	1,419	4,280
11.	Andhra Pradesh	4	12	21,858	20,600	1,258	94.2/5.8	1	-	21	7	30	16	840	2,237
12.	Orissa	1	37	70,214	66,822	3,392	95.2/4.8	23	14	55	52	46	55	1,259	2,371
13.	Himachal Pradesh	1	1	2,827	2,538	289	89.8/10.2	-	-	-	-	-	-	84	154
14.	Rajasthan	2	76	2,21,585	1,76,942	44,643	80/20	42	61	82	106	195	153	5,600	4,731
15.	Assam	1	12	17,135	16,395	740	95.7/4.3	22	4	24	23	61	84	313	756
16.	Uttar Pradesh	6	86	1,56,241	1,45,323	10,918	93/7	82	14	233	31	315	38	4,912	11,011
17.	Haryana	3	23	84,662	82,328	2,334	97.2/2.8	14	3	32	46	28	45	1,276	5,453
	Total	77	660	26,59,370	25,04,131	1,55,239	94.2/5.8	673	433	1,649	1,508	8,710	12373	33,691	101819

1.13 Quality of assessments

According to the instructions issued by the Central Board of Direct Taxes in June 1985, one of the objectives of the summary assessment scheme was that there will be no error in the scrutiny assessments so that audit objections and the need for rectifications would not arise and the officers will make statutorily and arithmetically correct assessments.

The particulars of the number of assessments completed under different slabs of income during 1988-89, the number of objections raised and the error percentage are:

	Rs.50,000 to Rs.5 lakhs			Rs.5 lakhs to Rs.10 lakhs			Rs.10 lakhs to Rs.50 lakhs			Rs.50 lakhs and above			Total			Above Rs.5 lakhs		
	(i)	(ii)	(iii)	(iv)	(v)	(vi)	(vii)	(viii)	(ix)	(x)	(xi)	(xii)	(xiii)	(xiv)	(xv)	(xvi)	(xvii)	(xviii)
	No. of assessments completed	No. of audit objections	Percentage	No. of assessments completed	No. of audit objections	Percentage	No. of assessments completed	No. of audit objections	Percentage	No. of assessments completed	No. of audit objections	Percentage	No. of assessments completed	No. of audit objections	Percentage	No. of assessments completed	No. of audit objections	Per centage
Scrutiny	33,691	2,713	8.05	8,710	315	3.62	1,649	475	28.81	673	409	60.77	44,723	3,912	8.75	11,032	1,199	10.86
Summary	1,01,819	3,595	3.53	12,373	354	6	1,508	489	32.43	433	224	51.73	1,16,133	4,662	4.01	14,314	1,067	7.45

The large number of audit objections indicated that as much as 10 percent of the high income cases above Rs.5 lakhs apparently suffered from errors and omissions. The percentage of error in income ranges between Rs.10 and Rs.50 lakhs, and above Rs.50 lakhs was 28 and 60 as regards scrutiny cases and 32 and 51 as regards summary cases.

1.14 Institution of Inspecting Assistant Commissioner (now Deputy Commissioner of Income-tax)

In their 186th and 187th Reports (1975-76) (Fifth Lok Sabha), the Public Accounts Committee, with a view to improving the standard of performance and reducing the possibility of mistakes, had recommended that cases over five lakh of rupees shall be assigned to Inspecting Assistant Commissioners of Income-tax. Accepting the recommendations an institution of Inspecting Assistant Commissioners was created in the Income-tax department from the year 1977-78. In June 1985, the Board issued instructions that the total policy package to voluntary compliance reposed increasing faith in the tax payers and sought to ensure that this faith was not abused. Intensive investigation and scrutiny of the cases were, therefore, envisaged while completing the scrutiny assessments and processing of a few cases from the prosecution angle.

A review of scrutiny assessments in respect of 17 Commissioners of Incomet-ax under Rajasthan, Bombay and Gujarat circles and 218 assessing officers' charges in respect of other circles revealed the following:

		Financial years 1984-85 to 1988-89
1.	Number of scrutiny assessments completed (reviewed)	32,871
2.	Normal adjustments	
	(i) Number	27,274
	(ii) Amount	Rs. 397.28 crores
3.	Concealment additions	
	(i) Number	2,046
	(ii) Amount	Rs. 81.12 crores
4.	Additional tax (gross)	Rs. 211.50 crores
5.	Penalty for concealment	
	(i) Number	332
	(ii) Amount	Rs. 0.65 crores
6.	Number of prosecutions launched	172
7.	Number of convictions obtained	8
8.	Amount of additional tax confirmed in appeal	Rs. 23.11 crores
9.	Number of penalty confirmed and quantum	
	(i) Number	215
	(ii) Amount	Rs. 0.33 crores

NOTE: (i) Does not include information in respect of Tamil Nadu and J & K charges.
(ii) @ Information in respect of Calcutta and Rajasthan charges is for 1988-89 only.
(iii) Information for Bihar charge is for 1988-89 only.

The following position emerged from the review results:

(a) In respect of 32,871 assessments completed after detailed scrutiny and investigation during the 5 years from 1984-85 to 1988-89 in selected charges, in 27,274 cases there were normal adjustments according to the provisions of the Income-tax Act to the extent of Rs.397.28 crores, in 2,046 assessments the department detected concealments and made additions to the tune of Rs. 81.12 crores towards concealment of income (about 17 percent);

(b) Out of the gross demand of Rs. 211.50 crores,raised in assessments a sum of Rs. 23.11 crores had been confirmed in appeal, which worked out to 11 percent;

(c) In 332 cases, penalty for concealment of Rs.0.65 crore was levied, of which in 215 cases involving Rs. 0.33 crores, viz., 50 percent, the penalties were confirmed.

1.15 Results of test-audit

The test-audit of the summary assessment cases decided by the Income-tax department during the year 1988-89 revealed several irregularities of diverse nature in a total of 8,231 cases involving a revenue effect of Rs. 114.88 crores. The corresponding figures for the years 1986-87, 1987-88 and 1988-89 were 5,836, 4,090 and 6,547 cases involving revenue effect of Rs.8.38, Rs.13.82 and Rs.18.49 crores. The mistakes broadly fell under the following categories:

Income-tax

Name of irregularity	No. of cases	Tax effect (In crores of rupees)
(i) Arithmetical errors in returns, accounts and documents and *prima facie,* inadmissible expenses allowed.	587	11.76
(ii) Irregular set off and carry forward and set off of unabsorbed losses,depreciation, etc., and certain other reliefs.	325	34.27
(iii) Omission to disallow any deduction, allowance of relief, *prima facie,* inadmissible but claimed in the return.	2,239	25.65
(iv) Other irregularities viz., incorrect adoption of status, non-adoption of correct share income, income escaping assessment, irregular refund, etc.	4,897	42.98
Total	**8,048**	**114.66**
Other Direct Taxes	**183**	**0.22**
Grand Total	**8,231**	**114.88**

1.16 Statutory provisions

Summary assessment calls for two adjustments under law:

(i) correction of arithmetical errors in the return, accounts or documents accompanying the return;

(ii) Giving effect to certain expenditure, set off of carried over deficiencies in losses, depreciation, etc.

During the course of the review, a number of mistakes were noticed in the application of these provisions. The types of irregularities noticed are such as could have been avoided, had the prescribed adjustments been kept in mind and the assessments completed after verifying the returns and the accompanying accounts, documents and the assessments of earlier years, wherever called for.

1.17 Non-statutory provisions

The test-audit of the summary assessments completed during the year 1988-89 also revealed other irregularities of diverese nature in the application of the various provisions of the Income-tax law other than the prescribed adjustments.

Some of the important and interesting points noticed during the test audit of the assessments during the year 1989-90 decided in a summary manner during 1988-89 are incorporated in the following Chapters 2, 3, 4 and 5.

Chapter 2 covers omissions noticed in a large number of cases where department was expected to carry out the prescribed adjustments, while Chapters 3 to 5 bring out glaring cases of under-statement of income and tax, under different categories, where the faith reposed on the assessees under the summary assessment procedure did not get the desired response, but the department, also virtually ignored them. The cases have been highlighted in this Report, despite the refusal of the Department to take cognizance of these audit observations, with a view to inviting attention to the shortcomings and deficiencies obtaining in the present scheme.

Chapter 2

Prescribed adjustments

2.01 Arithmetical/Avoidable mistakes in computation of income and tax

Under the Income-tax, as applicable for 1988-89, the assessing officer may make assessments in a summary manner after, ***inter alia,*** rectifying any arithmetical erros in the returns, and the accounts and documents, if any, accompanying the returns. The Central Board of Direct Taxes have, from time to time (1968 to 1985), issued a number of instructions with a view to ensuring arithmetical accuracy in assessments. These were reiterated in May 1985 and again in December 1988.

Underassessments of tax on account of mistakes in the computation of total income and in determination of tax payable, involving substantial revenue were noticed during 1988-89 also, as in the past, despite the instructions mentioned above and regardless of the element of deterrance envisaged under the Action Plan. 10 very important mistakes of such nature noticed in the audit of the assessments completed under the Action Plan, 1988-89 were brought to the notice of the Ministry for comments, of which a few are given below:

1. In Bombay circle, a company returned losses of Rs. 6.92 crores and Rs. 8.52 crores respectively for the assessment years 1987-88 and 1988-89. The assessing officer, while completing the assessments, erroneously clubbed the brought forward losses of earlier years with the current year losses, and determined the loss as Rs.9.87 crores and Rs. 18.38 crores for the assessment years 1987-88 and 1988-89 respectively. The mistake resulted in excess computation of loss by Rs. 2.95 crores and Rs. 9.87 crores for the two assessment years, involving potential short levy of tax aggregating to Rs.6.66 crores for the two years.

The department has accepted the mistake.

2. In Bombay circle, while completing the assessment of a co-operative society for the assessment years 1987-88 and 1988-89 in March 1989, the department included the earlier years' brought forward losses and computed the losses at Rs.3.66 crores and Rs. 4.33 crores as against Rs. 1.43 crores and Rs. 67.11 lakhs returned by the assessee. The mistake resulted in excess computation of loss by Rs. 2.23 crores and Rs. 3.66 crores for the assessment years 1987-88 and 1988-89 respectively, with resultant aggregate potential short levy of tax of Rs.2.43 crores.

The department has accepted the audit observation.

3. In Bombay circle, a company returned losses of Rs.18.12 lakhs, Rs.15.14 lakhs and Rs. 17.80 lakhs for the assessment years 1986-87, 1987-88 and 1988-89 respectively. The assessing officer, while completing the assessment in March 1989, included the brought forward losses of earlier years in the current years' losses and determined the losses at Rs. 63.72 lakhs, Rs. 78.86 lakhs and Rs. 96.86 lakhs for the three

assessment years. The mistake resulted in excess computation of loss aggregating to Rs. 1.88 crores leading to potential short levy of tax of Rs. 1.07 crores.

The department has accepted the audit objection.

4. In Bombay circle, in the assessment of an association of persons for the assessment years 1986-87 and 1987-88, completed in March 1989, the assessing officer erroneously determined the losses at Rs. 48.82 lakhs and Rs. 56.36 lakhs respectively. The losses actually returned by the assessee were Rs. 29.0 lakhs and Rs. 7.54 lakhs. The statement of losses enclosed to the returns also confirmed this position. The mistake in determination of losses at Rs. 48.82 lakhs and Rs. 56.36 lakhs by the assessing officer, therefore, resulted in excess computation of loss to the extent of Rs. 19.82 lakhs for the assessment year 1986-87 and Rs. 48.82 lakhs for the assessment year 1987-88, involving potential tax effect of Rs. 35.01 lakhs for both the years put together.

The department has accepted the mistake.

5. In Bombay circle, in the case of an individual, the assessment for assessment year 1987-88 was completed in March 1989 determining a loss of Rs. 45.07 lakhs. The loss returned by the assessee, as indicated in the statement of computation of loss enclosed to the return, was, however, only Rs. 11.39 lakhs. The mistake committed by the assessing officer resulted in excess computation of loss to the extent of Rs. 33.68 lakhs involving potentital short levy of tax of Rs. 16.85 lakhs.

The department has accepted the audit observation.

6. In Bombay circle, a private limtied company filed its return for the assessment year 1987-88, showing a loss of Rs.1.85 crores which included current years's loss of Rs.22.66 lakhs. In the tax computation sheet furnished alongwith the return, the loss was, however, worked out at Rs.45.48 lakhs. While completing the assessment, the assessing officer adopted the amount of loss at Rs.45.48 lakhs given in the comptuation sheet, instead of the correct amount of Rs.22.66 lakhs. The mistake resulted in the excess carry forward of loss by Rs.22.82 lakhs, leading to notional short levy of tax of Rs.12.55 lakhs.

The department has accepted the audit observation.

7. In Tamil Nadu circle, the assessments of a widely held company for the assessment years 1986-87, 1987-88 and 1988-89 were completed in September 1988 on a total income of 'nil', (-) Rs. 75.95 lakhs and 'nil' respectively after allowing deduction towards expenditure on travelling, on guest house and on entertainment totalling to Rs. 5.82 lakhs, Rs. 6.49 lakhs and Rs.57,131 respectively for the assessment years 1986-87 to 1988-89. Audit scrutiny (July 1989) revealed that in the statement enclosed to the report of audit of accounts of the assessee, these items were shown as expenditure to be disallowed. However, while completing the assessments, the assessing officer failed to take note of the audit certificate, and consequently, no disallowance was made. The omission resulted in excess carry over of unabsorbed depreciation by Rs. 5.82 lakhs, Rs. 6.49 lakhs and Rs.57,131 for the assessment years 1986-87 to 1988-89 respectively involving potential under charge of tax of Rs. 7.38 lakhs.

The department has accepted the audit observation.

8. For the assessment years 1986-87 and 1987-88, a domestic company in which public are not substantially interested and which was mainly engaged in industrial activity was charged to tax at the rate of 55 per cent.

In West Bengal circle, the assessments for the assessment years 1986-87 and 1987-88 of a private limited company engaged in industrial activity were completed by the Deputy Commissioner (Assessment) in March 1989 on a total income of Rs. 18.34 lakhs and Rs. 2.69 lakhs respectively and the income was charged to tax at the rate of 50 per cent instead of at the correct rate of 55 per cent. The application of the incorrect rate of tax resulted in total under charge of tax of Rs. 5.40 lakhs (including short levy of interest of Rs. 4.30 lakhs for non-furnishing of estimate of advance tax and non-levy of interest for belated submission of returns.

9. In Bombay circle, an assessee company returned a loss of Rs. 1.10 crores for the assessment year 1988-89. While completing the assessment in February 1989 the Deputy Commissioner of Income-tax, by mistake, included the brought forward losses of earlier assessment years in the current years' losses and determined the loss for the current assessment year 1988-89 as Rs. 2.06 crores. The mistake resulted in excess computation of loss of Rs.96.30 lakhs for the assessment year 1988-89 involving notional short levy of tax of Rs. 48.15 lakhs.

10. In Madhya Pradesh circle,in the assessment of a trading company for the assessment year 1988-89 completed by the Deputy Commissioner of Income-tax in February 1989, the loss was computed at Rs. 20.79 lakhs which was carried forward alongwith the earlier years' loss of Rs. 42.28 lakhs. However, according to the computation of total income as returned by the assessee there was a profit of Rs. 20.80 lakhs and after adjustment of earlier years' losses of Rs.42.28 lakhs, the net loss to be carried forward was Rs.21.49 lakhs. Instead, excess loss of Rs.41.59 lakhs was carried forward, which resulted in potentital short levy fo tax of Rs.26.20 lakhs.

The department has accepted the mistake.

2.02 Mistakes in the adjustment of carried forward unabsorbed losses, depreciation, tax holiday, etc.

In making a summary assessment, the Act requires the assessing officer to give effect to the provisions governing the set off of carry forward deficiencies in unabsorbed losses, depreciation, development rebate, investment allowance, tax holiday, instalments in capital expenditure, etc., with reference to the records of the assessments of the earlier years. Under the Action Plan 1988-89, in respect of summarily assessed cases, care should have been taken by the assessing officer to avoid msitakes involving the above adjustments, but test audit disclosed a large number of mistakes on this area also. 11 major audit observations involving Rs.11.28 crores were sent to the Ministry of Finance, during the year to focus their attention about the need to improve the quality of assessments. Out of the above, Departmental officers have admitted four cases with tax effect of Rs.1.66 crores.

A few important cases are extracted below:

1. Where in computing the income from business (other than speculation business) of an assessee, the net result of the computation in any assessment year is a loss, and it cannot be or is not set off wholly set off against his other income for that year, so much of the loss as has not been so set off can be carried forward to the subsequent year(s) for set off against his business income for that year(s) provided the assessee continued to carry on the business for which the loss was computed, during the subsequent year(s). Such carry forward is permitted under the Act upto eight assessment years immediately succeeding the assessment year for which the loss was first computed. Similarly, depreciation allowed to the extent it cannot be absorbed in any assessment year for want of sufficient income, shall be carried forward to and added to the depreciation of the next assessment year for allowance during that year. Further, where in the case of an assessee, carried forward loss and unabsorbed depreciation are awaiting set off, business loss shall be set off first.

(i) In Karnataka circle, in the assessment of a State Government company for the years 1986-87 and 1987-88 completed in September 1988 and March 1989, the Deputy Commissioner of Income-tax accepted the assessee's claim for set off and carry forward of business loss and unabsorbed depreciation of earlier years without referring to the assessment completed after scrutiny for the earlier year, *i.e.*, 1985-86. For the assessment year 1986-87, the correct amounts that should have been allowed to be carried forward were business loss of Rs.13.02 lakhs of assessment year 1985-86 and unabsorbed depreciation of Rs. 4.24 crores of the years 1976-77 to 1985-86 (total Rs. 4.37 crores) with reference to assessment records of 1985-86, after setting off business loss of the years 1978-79 to 1983-84 and 1985-86 to the extent of available income of Rs.5 crores. However, the assessing officer allowed carry forward of business loss of Rs.2.50 crores relating to the years 1983-84 to 1985-86 and unabsorbed depreciation of Rs.4.56 crores for the years 1976-77 to 1985-86 (total Rs.7.05 crores) accepting the assessee's claims, after setting off business loss of the assessment years 1977-78 to 1983-84 against the available income of Rs.5 crores. In this process, excess business loss to the extent of Rs. 2.37 crores and excess unabsorbed depreciation of Rs.31.51 lakhs relating to the assessment years 1983-84 to 1985-86 were carried forward. Further, business loss of Rs.75.97 lakhs relating to the assessment year 1977-78 was adjusted wrongly in the assessment year 1986-87 even though it related to the ninth earlier year and was not eligible for set off.

For the assessment year 1987-88, against the correct amounts to be carried forward, viz., Rs.13.02 lakhs towards business loss of 1985-86 and Rs.4.29 crores towards unabsorbed depreciation relating to the years 1976-77 to 1987-88, the amounts actually ordered to be carried forward, accepting the claim in the return, were Rs.8.56 crores towards business loss of the assessment years 1976-77 to 1985-86, and Rs. 5.46 crores as unabsorbed depreciation of the years 1976-77 to 1987-88. This included, ***inter alia,*** business losses of the assessment years 1976-77 and 1977-78 totalling Rs. 1.82 crores which had already lapsed and the business losses of 1978-79 to 1983-84 out of which losses totalling Rs.4.24 crores had been set off in the earlier assessment year 1986-87 itself. The cumulative excess carry forward aggregated Rs.9.60 crores involving a potential tax effect of Rs. 4.80 crores.

(ii) In Karnataka circle, in the case of an assessee company, the losses, allowances and depreciation brought forward from earlier years for set off as per the statement enclosed to its return of income for the assessment year 1987-88 indicated that the company had carried forward loss amounting to Rs. 6.86 crores pertaining to the assessment year 1978-79 and earlier years. This loss was allowed to be carried forward in the assessment concluded for the assessment year 1987-88 in January 1989, though the prescribed time limit of eight years had already elapsed in respect of the losses for the assessment year 1978-79 and earlier years by 1986-87. The incorrect carry forward of such losses resulted in potential under charge of tax of Rs. 3.43 crores.

(iii) In Madhya Pradesh circle, in the assessment of a company for the year 1986-87 made in November 1988, the business loss of Rs. 12.70 lakhs and depreciation allowance of Rs. 17.88 lakhs were determined for carry forward and set off, even though the returns contained the following information.

(a) The assessee company had not commenced any manufacturing activity and had not carried out any business during the previous year relevant to the assessment year 1986-87, and hence, under the Act, the business loss or depreciation should not have been computed for carry forward and set off.

(b) The business loss could not have been allowed to be carried forward for set off because the return of loss itself was filed late, *i.e.*, on 25 September 1986 as against the due date for filing the return on 31 July 1986.

(c) The return of income was not accompanied with the profit and loss account and balance sheet, etc., and was, therefore, a defective return under the provisions of the Act.

(d) No prescribed particulars were filed in support of claim for depreciation allowance and in their absence even depreciation could not have been computed for carry forward and set off.

Further, the assessee was allowed carry forward of losses and unabsorbed depreciation allowance of Rs.2.55 lakhs of earlier assessment years from 1981-82 to 1985-86, though the assessee had ceased to manufacture its product, a pesticide used for malaria eradication, as there was no demand for the product. The assessee company had also changed its trade name and had diversified its activities to set up a biomedical project for manufacture of biomedical equipments. As such, the business loss of earlier assessment years from 1981-82 to 1985-86 was not to be allowed to be carried forward for set off. Depreciation allowance of the assessment year 1985-86 was also specifically not allowed to be carried forward in the order of assessment of that year as no business was carried out in the relevant previous year. Incorrect computation of loss and depreciation allowance pertaining to the assessment year 1986-87 amounting to Rs.30.58 lakhs, incorrect carry forward of earlier years' business losses relating to the assessment years 1981-82 to 1985-86 and incorrect granting of depreciation allowance for the assessment year 1985-86, all amounting to Rs. 1.37 crores resulted in a total incorrect carry over of losses and depreciation of Rs. 1.67 crores and potential short levy of tax of Rs. 87.72 lakhs.

The department has accepted the mistake.

(iv) In Madhya Pradesh circle, in the assessment of a company for the assessment year 1988-89 completed by the Deputy Commissioner of Income-tax (Assessment) in December 1989, the business loss was computed at Rs. 1.11 crores by adding back a sum of Rs. 34.38 lakhs on account of current depreciation to the loss of Rs. 1.45 crores as per profit and loss account. Unabsorbed depreciation of the current year, carried forward for set off, was shown separately at Rs.34.38 lakhs. However, depreciation debited to the profit and loss account was actually Rs.1.40 crores, which included depreciation of Rs. 1.06 crores for the earlier years. The business loss for the assessment year 1988-89 was, therefore, only Rs. 5.12 lakhs, to be worked out by adding back the sum of Rs.1.40 crores (depreciation debited to Profit & Loss Account) to the loss, as per profit and loss account, of Rs.1.45 crores. The mistake resulted in the business loss being computed in excess by Rs.1.06 crores resulting in potential short levy of tax of Rs.61.16 lakhs.

The department has accepted the mistake.

(v) In the case of another company, the assessment for the assessment year 1986-87 was made in March 1989 and against the assessed income of Rs.59.67 lakhs, carried forward loss of the assessment year 1983-84 comprising business loss, unabsorbed depreciation and investment allowance aggregating to Rs. 3.14 crores was set off to the extent of income, and the balance of Rs. 2.54 crores was, further, carried forward for set off. However, as per the revision made in August 1988 for the assessment year 1983-84 loss to be carried forward for set off was only Rs. 2.94 crores. The determination of the excess carry forward of loss of Rs. 0.20 crores (Rs.3.14 crores as against Rs. 2.94 crores) resulted in potential short levy of tax of Rs. 11.02 lakhs.

The department has accepted the mistake.

(vi) In West Bengal circle, an assessee company filed the return of income for the assessment year 1986-87 in December 1986 showing a loss of Rs. 34.32 lakhs which included business income of Rs. 7.24 lakhs, long term capital loss of Rs. 7,464 and unabsorbed loss of earlier year of Rs. 41.49 lakhs. The assessing officer completed the assessment in March 1989 on a total loss of Rs. 34.32 lakhs as per return, but the loss was not allowed to be carried forward. As all the past losses were fully set off in the assessment for the assessment year 1985-86 completed in January 1988,completion of assessment for assessment year 1986-87 in March 1989 on a total loss of Rs. 34.32 lakhs as per return, ignoring the fact that all the past losses had already been set off, was irregular. The mistake resulted in under-assessment of income of Rs.7.24 lakhs with consequent under charge of tax of Rs.6.27 lakhs (including non-levy of interes of Rs.26,144 for late filing of return and non-levy of interest of Rs. 1.83 lakhs for non-payment of advance tax).

The department has accepted the mistake.

(vii) In Bombay circle, in the assessment for the assessment year 1987-88 completed in March 1989, the income of an assessee company was computed as 'nil', after setting off an amount of Rs. 10.59 lakhs as loss carried forward from assessment year 1979-80. However, according to the assessment order for assessment year 1979-80, no loss was to be carried forward as directed by the

Commissioner of Income-tax. Hence the setting off of the amount in question was irregular and resulted in short levy of tax of Rs. 5.29 lakhs.

(viii) In Bombay circle, the assessment of a company for the assessment year 1987-88 was completed by the Deputy Commissioner of Income-tax in March 1989 on an income of Rs.24.77 lakhs as returned by the assessee. While computing the taxable income, the company had set off unabsorbed depreciation of Rs. 22.23 lakhs in respect of assessment year 1986-87. It was, however, seen from the assessment order of January 1989, for the assessment year 1986-87 that the depreciation of Rs.1.02 crores allowed in that year was fully set off and there was no unabsorbed depreciation to be carried forward to the following assessment years. The mistake resulted in under assessment of income of Rs. 22.23 lakhs leading to short levy of tax of Rs. 11.12 lakhs.

(ix) In Bihar circle, in the assessment of a private limtied company for the assessment year 1987-88 completed by the Deputy Commissioner of Income-tax in December 1988, unabsorbed depreciation and losses of earlier years amounting to Rs.12.32 lakhs and Rs.10.80 lakhs as against the correct amounts of Rs.10.50 lakhs and Rs.6.88 lakhs respectively were allowed as claimed by the assessee. The mistake resulted in excess computation of loss by Rs.5.74 lakhs involving potential tax effect of Rs.3.45 lakhs.

2. With effect from 1 April 1985 no business loss can be carried forward for set off in subsequent years unless the assessee has filed the return of loss within the due date or within such further time as permitted by the assessing officer. The assessment of a domestic company for the assessment year 1988-89 was completed in February 1989 at a loss of Rs.8.83 crores which included a carried forward loss of Rs.2.16 crores for the assessment year 1985-86. It was noticed in audit in October 1989 that the assessee company filed a return of income for the assessment year 1985-86 showing a loss of Rs. 2.16 crores the assessment of which was made in March 1988 at a loss of Rs.69.58 lakhs with the stipulation that the loss would not be carried forward due to late filing of the return. Since no loss was allowed to be carried forward for the assessment year 1985-86, inclusion and carry forward of the said loss of Rs. 2.16 crores in the assessment for the assessment year 1988-89, ignoring the provisions of the Act, resulted in excess computation and excess carry forward of loss of Rs. 2.16 crores for the assessment year 1988-89 involving a potential tax effect of Rs. 1.13 crores.

3. Where the assessee is a partner of an unregistered firm which has not been treated as a registered firm under the Act and his share in the income of the firm is a loss, then, whether the firm had already been assessed or not, such loss shall not be set off or carried forward and set off against his own income. Any loss of the firm shall be set off or carried forward and set off only against the income of the firm.

For the assessment year 1986-87, in Bombay circle, an assessee firm filed the return of income in the status of a registered firm showing loss of Rs. 21.90 lakhs. While completing the assessment for the assessment year 1987-88 in March 1989, the assessing officer accepted the loss as returned and allocated the loss amongst the partners of the firm, treating the firm as a registered firm. The loss of Rs.21.90 lakhs allocated amongst the

partners of the registerd firm included carried forward loss of Rs.2.82 lakhs pertaining to the assessment years 1985-86 and 1986-87. Audit scrutiny revealed that the assessee firm was treated as an unregistered firm for the assessment years 1985-86 and 1987-88 and the loss of Rs. 12.82 lakhs had been carried forward in the hands of the firm. Any loss of an unregistered firm shall be set-off or carried forward and set-off only against the income of the unregistered firm. The incorrect carry forward of the losses of the unregistered firm amounting to Rs. 12.82 lakhs of the earlier years as loss of the registered firm in the assessment year 1987-88 and allocating the loss to the partners of the registered firm resulted in potential undercharge of tax of Rs.6.41 lakhs.

Chapter - 3

Corporation tax

352 major observations noticed in the audit of company assessments made in summary manner, involving tax effect of Rs.54.71 crores were sent to Ministry of Finance for comments during January 1990 to July 1990.Since the mistakes were not those covered under the Scheme, the assessing officers were not bound to rectify them. Some important cases are given below:

3.01. Incorrect computation of income from house property

Under the provisions of Income-tax Act,1961, the income chargeable under the head Income from house property is computed after making certain deductions from the annual value in respect of repairs, a fixed allowance of a sum equal to one sixth of annual value, insurance premium, annual charges, ground rent, interest on borrowed capital, if any, etc.

1. In Assam circle, while completing the assessment for the assessment year 1986-87 in March 1989 of a private limited tea company, the Deputy Commissioner (Assessment) accepted the house property income at Rs.23,953 as returned by the assessee. Audit scrutiny in September 1989 revealed that out of warehouse rent receipts of Rs.6.98 lakhs, a sum of Rs.1.16 lakhs was an admissible deduction, against which the assessee deducted Rs.6.74 lakhs for the assessment year 1986-87, though such incorrect deduction claimed for the assessment year 1985-86 was disallowed in regular assessment. Further, claim of development allowance of Rs.1.04 lakhs had been irregularly allowed,though it was without any supporting documents. These irregular deductions resulted in under assessment of income of Rs.6.62 lakhs leading to undercharge of tax of Rs.4.06 lakhs(including interest of Rs.23,896 for belated submission of return).

2. It has been held by the Supreme Court in 1972* that income derived from letting out of buildings owned by the assessee to tenants is to be computed under the head 'Income from house property' and not under the head'Income from profits and gains of business or profession'.

In the assessments of a private company, for the assesment years 1984-85 and 1985-86 in Karnataka Circle, the income of the assessee from lease rent and service charges of the buildings owned by the company was wrongly treated as income from business. On the irregularity being pointed out by Audit, these orders were set aside by the Commissioner of Income-tax in February 1989 with the direction that rental income should be treated as income from house property. The orders of the Commissioner of Income-tax were given effect to in March 1989 treating the rental income as income from house property.For the subsequent assessment years 1986-87,1987-88 and 1988-89 also,the assessee continued to show this income under business and returned a

* 83 ITR 700 - S.G. Mercantile Corporation V. C.I.T., Calcutta.

loss of Rs.6,930, Rs.43,641 and Rs.66,557 respectively.This was accepted while concluding the assessments for these assessment years summarily in January 1989 overlooking the earlier orders of the Commissioner of Income-tax (February 1988) treating the rental income as income from house property.The total income assessable to tax if the rental income was computed under house property would amount to Rs.1.12 lakhs, Rs.1.83 lakhs and Rs.2.58 lakhs for the assessment years 1986-87,1987-88 and 1988-89 respectively as against the losses returned.The omission to assess the income under the prescribed head resulted in non-levy of tax of Rs.3.43 lakhs.

Incorrect computation of business income

3.02. Irregularities in allowing investment deposit allowance

Under the Income-tax Act,1961, with effect from 1 April 1987, in the case of an assessee, whose total income includes any income under the head 'Profits and gains of business or profession' and who has out of such income, deposited any amount in the deposit account with the Development Bank, before the expiry of six months from the end of the previous year or before furnishing the return of his income whichever is earlier, or has utilised any amount during the previous year, for the purchase of any new machinery or plant, without depositing any amount in a deposit account, shall be allowed a deduction equal to the amount or the aggregate of the amounts so deposited or any amount so utilised, or an amount equal to 20 per cent of the eligible profits of business or profession, whichever is less.

In Tamil Nadu Circle, the assessment of a closely held company for the assessment year 1987-88 was completed by the Deputy commissioner of Income-tax in January 1989 allowing a deduction of Rs.92.10 lakhs in respect of investment deposit account.Audit scrutiny (March 1990), however, revealed that while computing the profits for the purpose of allowing the above deduction the entire provision for taxation of Rs.2.71 crores was added and this sum included Rs.55.20 lakhs being provision made for surtax for the assessment years 1986-87 and 1987-88 pending completion of the surtax assessments for these assessment years. For the purpose of allowing deduction in respect of investment deposit account, only the surtax paid or payable under Companies (Profits) Surtax Act,1964 is contemplated for addition whereas even a provision in respect of income-tax could be added. Therefore, the amount of surtax determined with reference to completed assessment and not the provision made thereof could only be added.The mistake in adding the provision for surtax resulted in excess deduction by Rs.11.04 lakhs leading to short levy of tax of Rs.7.67 lakhs including interest for short payment of advance tax.

3.03. Incorrect allowance of capital expenditure on scientific research

Under the provisions of the Income-tax Act,1961, expenditure of a capital nature incurred by an assessee on scientific research during the relevant previous year is deductible in computing the taxable income for that assessment year.When the deduction cannot be allowed in full in any assessment year for want of sufficieint income in that year, the balance of deduction remaining unabsorbed can be carried forward and added to the allowance of deduction in the following assessment year.

In Bombay Circle, the assessment of a company for the assessment year 1987-88 was completed by the Deputy Commissioner of Income-tax (Special Range) in March 1989, accepting the income as returned.The assessee had claimed unabsorbed deduction of Rs.18.26 lakhs in respect of capital expenditure on scientific research in respect of the assessment year 1986-87.Audit scrutiny revealed that the deduction allowable for the assessment year 1986-87 was allowed in full in that year in the assessment completed in January 1989.Accordingly, the unabsorbed deduction of Rs.18.26 lakhs claimed in the assessment year 1987-88 should have been disallowed.Omission to do so resulted in under assessment of income of Rs.18.26 lakhs involving short levy of tax of Rs.9.13 lakhs.

3.04 Irregular deduction for salary of handicapped employee

In computing the business income of an assessee the Income-tax Act,1961, as applicable to assessment years 1981-82 to 1983-84 provides for deduction of a sum equal to one and a one third times the amount of expenditure incurred on payment of any salary to any employee who as at the end of previous year was totally blind or suffered from a permanent physical disability. By an amendment to the Act, brought in by Finance Act,1984, this weighted deduction was discontinued with effect from the assessment year 1984-85.

In Karnataka Charge, the assessments of an assessee company for the assessment years 1986-87 and 1987-88 were completed by the Deputy commissioner of Income-tax(Special Range) in January 1989 accepting the loss as returned by the assessee.Scrutiny in audit in August 1989 revealed that the assessee in his returns of loss for the above assessment years added to the loss as per profit and loss account, amounts of Rs.9.97 lakhs and Rs.10.43 lakhs towards the salary of handicapped employees and the weighted deduction at one-third of such salary.As the salary of physically handicapped employees stood already debited to the profit and loss account while arriving at the loss, the addition of salary once again to the loss amounted to claiming such expenditure twice.Further, the weighted deduction at one third the salary was also not admissible for the assessment years 1986-87 and 1987-88. Omission to reduce the loss by the above amounts resulted in excess computation of loss by Rs.20.40 lakhs involving a potential tax effect of Rs.10.45 lakhs for two years.

3.05 Excess allowance of expenditure on technical know -how

Under the Income-tax Act,1961, with effect from 1 April 1986, where the assessee has paid in a previous year any lumpsum consideration for acquiring technical know how for use for the purpose of his business, one sixth of the amount so paid shall be deducted from the profits and gains of the business for that year and the balance amount shall be deducted in equal instalments for each of the five immediately succeeding previous years.

In Bombay circle, in the assessment of a company for the assessment years 1986-87 and 1987-88 completed in January 1989, the full amount of technical know-how fees of Rs.1.67 lakhs and Rs.16.25 lakhs paid during the relevant previous years were allowed as deduction as claimed by the assessee. As the deduction was allowable only to the extent of one sixth of the amounts paid viz. Rs.27,778 in the assessment year 1986-

87 and Rs.2.99 lakhs in the assessment year 1987-88, the balance of Rs.1.39 lakhs and Rs.13.26 lakhs should have been disallowed in the respective assessment years.The omission to do so resulted in short levy of tax aggregating to Rs.3.73 lakhs (including interest for short payment of advance tax for both the assessment years).

3.06. Incorrect deduction of rural development programme

Under the Income-tax Act,1961, where an assessee incurs any expenditure by way of payment of any sum to an association or institution, which has as its object, the undertaking of any programme of rural development or payment of any sum to rural development fund set up and notified by the Central Government on this behalf, the assessee shall be allowed a deduction of the amount of such expenditure incurred during the previous year. Deduction under the Act shall not be allowed unless the assessee furnishes a certificate from the competent authority.

In the assessment of a tea company in N.E.Region Shillong Circle, for the assessment year 1986-87 deduction of Rs.19 lakhs was allowed by the Deputy Commissioner (Assessment) towards payments made by the company in the previous year to the 'Society for Integral Development' for carrying out programme of rural development. Audit scrutiny in November 1989 revealed that assessment for the assessment year 1985-86 was rectified to withdraw the benefit allowed to the donor company consequent upon fradulent involvment of the society and withdrawal of approval by the State level Committee with effect from December 1982. But while making assessment for assessment year 1986-87 in March 1989, irregular donation of Rs.19 lakhs was not disallowed though the fact was known to the assessing officer. Further, relief on export turnover of Rs.7.26 lakhs was incorrectly deducted from 40 per cent of income liable to income-tax only instead of deducting the same from composite income.Omission to disallow irregular donation together with erroneous calculation of export turnover resulted in under assessment of income of Rs.11.96 lakhs (being 40 per cent of Rs.19 lakhs plus 60 per cent of Rs.7.26 lakhs) involving under charge of tax of Rs.10.44 lakhs(including interest of Rs.3.53 lakhs for short payment of advance tax).

3.07 Incorrect allowance for bad debts

The Act further provides that the amount of any debt or part thereof or any recoverable dues which is established to have become bad in the previous year and written off in the accounts shall be allowed as deduction in computing the business income of the assessee.

In Tamil Nadu Circle, the assessment of a closely held company for the assessment year 1986-87 was completed by the Deputy Commissioner of Income-tax in December 1988 allowing a deduction of Rs.81.57 lakhs towards bad debts.Audit scrutiny in February 1990 revealed that the amount represented unrealisable dues from a joint venture unit.As the joint venture unit continued to incur loss and all efforts to sustain its activity and improve its performance had not met with success the assessee company decided to create adequate reserve in its accounts by transfer from general reserve towards the outstanding dues from the unit and kept the Reserve Bank of India and Government of India informed of the present status of the unit for taking appproprirate action in

consultation with them. It was also seen from the Directors Report (September 1988), on the accounts for the year ended 31 March 1988, that the assessee was still in touch with the Reserve Bank of India and Government of India to decide about the further steps to be taken regarding the dues.Thus, the debt was not established to have become irrecoverable in the previous year relevant to assessment year 1986-87 and there was no write off entry in the profit and loss account in respect of this debt.Since the essential conditions prescribed in the Act to allow the bad debts as deduction were not fulfilled, the deduction allowed was not in order. The mistake led to short levy of tax of Rs.49.46 lakhs.

3.08 Irregular deductions allowed

(i) In Calcutta circle, the assessment of a State Electricity Board for the assessment year 1986-87 was completed in March 1989 at a loss of Rs.65.82 crores as per return filed by the assessee. Audit scrutiny in November 1989 revealed that the assessee had debited in its profit and loss account for the previous year relevant to the assessment year 1986-87, a sum of Rs.3.65 crores towards prior period adjustment account. Though full details of income and expenditure booked under 'prior period adjustment' were not available in the assessment records of the assessee, the accounts of the assessee revealed that the sum of Rs.3.65 crores comprised of net minus credit (income) of Rs.2.04 crores and net debit (expenditure) of Rs.1.61 crores relating to past previous years.As neither the reduction of income nor the expenditure booked in the accounts, pertained to the previous year relevant to the assessment year 1986-87, the net debit of Rs.3.65 crores was required to be disallowed and added back in the assessment. The Deputy Commissioner of Income-tax (Special Range) while making the assessment, however, omitted to disallow and add back the same. The mistake resulted in excess computation of loss of Rs.3.65 crores for the assessment year 1986-87 involving potential tax effect of Rs.1.92 crores.

(ii) In the case of a company following mercantile system of accounting in Bombay circle, amounts of Rs.18.72 lakhs and Rs.17.33 lakhs relating to earlier years expenses were debited in the profit and loss accounts of the previous years relevant to assessment year 1986-87 and 1987-88 respectively and they were allowed as deduction by the Deputy commissioner of Income-tax (Special Range) in the assessments for assessment year 1986-87 and 1987-88 completed in November 1988.As the amounts in question did not relate to the previous years relevant to assessment years 1986-87 and 1987-88 the same should have been disallowed while computing the income for those years. Omission to do so resulted in excess determination of loss aggregating to Rs.36.04 lakhs involving potential short levy of tax of Rs.18.49 lakhs in both the years.

(iii) In its return for the assessment year 1987-88 a company in Bombay circle claimed deduction for an amount of Rs.48.88 lakhs being expenditure carried forward under the heading 'expenditure pending allocation'.The expenditure was incurred in connection with the manufacture of a new range of products the production of which had not yet commenced.The amount in question appeared in the relevant balance sheet under fixed assets. In the assessment for the assessment year 1987-88 completed in March 1989, the Deputy commissioner of Income-tax (Special Range) allowed the aforesaid deduction as claimed by the company.As the expen-

diture did not relate to revenue expenditure incurred during the relevant previous year, it was not allowable as a deduction. The mistake resulted in excess determination of loss by Rs.48.88 lakhs involving potential short levy of tax of Rs.26.89 lakhs.

(iv) In Bombay circle, the assessments of a company for the assessment year 1986-87 and 1987-88 were completed by Deputy commissioner of Income-tax (Special Range) in January 1989, accepting the income as returned.The company had debited to its profit and loss account of the relevant previous years an amount of Rs.36.50 lakhs and Rs.4.83 lakhs towards expenses pertaining to earlier years. As the company was following mercantile system of accounting, expenses pertaining to earlier years was not an allowable deduction for computing income. Omission to disallow the expenses in question resulted in under assessment of income of Rs.36.50 lakhs and Rs.4.83 lakhs respectively for the assessment years 1986-87 and 1987-88 involving notional short levy of tax aggregating to Rs.22.49 lakhs for both the years.

(v) In Bombay circle, the case of a company, in the profit and loss account for the previous year relevant to the assessment year 1987-88 an amount of interest of Rs.25.78 lakhs relating to an earlier year was debited in its profits and loss account and the same was allowed as deduction in the assessment year 1987-88 completed by the Deputy commissioner of Income-tax (Special Range) in January 1989.As the expenditure in question did not relate to the previous year relevant to assessment year 1987-88 it should have been disallowed while computing the income for the year. Omission to do so resulted in excess determination of loss by Rs.25.78 lakhs involving a potential short levy of tax of Rs.14.18 lakhs.

(vi) Under the Income-tax Act,1961, while computing the business income of an assessee for an assessment year only an ascertained liability which was incurred during the relevant previous year is allowable as a deduction.

In Bombay circle, a company claimed deduction for deferred interest of Rs.38.33 lakhs,Rs.51.61 lakhs and Rs.42.80 lakhs in its returns for the assessment years 1986-87 to 1988-89 respectively.The deduction claimed was allowed by the Deputy Commissioner of Income-tax in the assessments for assessment years 1986-87 to 1988-89 completed in September 1988. As deferred interest does not represent an ascertained or an accrued liability the deduction allowed on this account was not in order.The mistake resulted in excess determination of loss aggregating to Rs.1.33 crores involving total potential short levy of tax of Rs.70.45 lakhs in the three years.

3.09 Incorrect allowance of provisions

1. A provision made in the accounts for an accrued or known liability is an admissible deduction while other provisions made do not qualify for deduction.

Under the Income-tax Act,1961, any debt or part thereof or any recoverable dues which is established to have become bad in the previous year and written off in the accounts shall be allowed as deduction in computing the business income of the assessee for that year.

(i) In Tamil Nadu Circle, the assessment of a widely held company for the assessment year 1986-87 was completed in March 1989 after allowing deductions

of Rs.21.11 lakhs towards provisions for bad debts and Rs.17.92 lakhs being provision towards supplies on D.G.S.D. rate contract intended to cover the difference in sale value.The deduction towards bad debts could be allowed only if it was established to have become bad and written off in the accounts. The difference on D.G.S.D.sales was allowable only on the basis of actual sale value realised, and a provision thereof on estimate basis is not an ascertained liability and is not allowable.The incorrect alowance of deductions aggregating to Rs.39.03 lakhs led to excess carry over of loss by a like amount involving potential tax effect of Rs.20.49 lakhs.

(ii) In Bombay circle, the assessments of a company for the assessment years 1986-87 to 1988-89 were completed in March 1989.It was seen in audit that while computing the taxable income the company had claimed deduction of Rs.20.09 lakhs, Rs.6.73 lakhs and Rs.6.65 lakhs respectively towards liability for enhanced rent.The deduction claimed being merely a provision and not an ascertained liability, the claim was required to be disallowed by the assessing officer.Similar claim made in the assessment year 1985-86 had been disallowed.The incorrect allowance of the contingent liability resulted in short levy of tax of Rs.17.40 lakhs for the three assessment years.

(iii) In the case of a company in Calcutta circle for the assessment year 1986-87, the assessment of which was completed in March 1989, the company had debited in its profit and loss account for the year ended 31 March 1986 relevant to assessment year 1986-87, an amount of Rs.62.61 lakhs being the provision for doubtful debts.While completing the assessment, the assessing officer omitted to add back this provision and this was allowed in the assessment.As the amount was merely a provision and not an ascertained liability, it was not an allowable deduction. The mistake resulted in over assessment of loss of Rs.62.61 lakhs involving consequent excess carry forward of loss by an identical amount involving potential tax effect of Rs.32.87 lakhs.

(iv) In Bombay Circle, a Government owned company following mercantile system of accounting debited in its previous year relevant to the assessment year 1987-88 an amount of Rs.1.12 crores towards provisions for doubtful debts and advances. As it was only a provision and not an ascertained liability, it was not allowable as a deduction. However, the Deputy commissioner of Income-tax (Assessment) allowed the provision as a deduction in the assessment for the assessment year 1987-88 completed in November 1988.The incorrect allowance of deduction resulted in under assessment of income of Rs.1.12 crores involving potential short levy of tax of Rs.55.96 lakhs.

3.10 Omission to disallow inadmissible expenditure on advertisement

Under the Income-tax Rules, 1962, the expenditure incurred by the assessee on advertisement by way of presentation of an article of gift shall be allowed as deduction in computing the business income of an assessee provided the expenditure on each such article of gift for presentation does not exceed fifty rupees.

In Karnataka circle, the assessments of a public limited company for the assessment years 1986-87 to 1988-89 were completed between February 1989 and March 1989 accepting the loss as

returned.It was, however, seen from the audit report furnished by the Chartered Accountants for the relevant previous years that the Chartered Accountants had shown the total of excess expenditure over the limits prescribed in respect of advertisement, travel, entertainment and salary and perquisites and the inadmissible expenditure in respect of guest house, clubs and unrecognised funds as Rs.4.79 lakhs,Rs.6.51 lakhs and Rs.10.69 lakhs for the assessment years 1986-87, 1987-88 and 1988-89 respectively.Neither the assessee reduced the loss by the above amounts while computing the loss for these years nor the assessing officer did so in the assessments. Omission to reduce the loss resulted in excess computation of loss by Rs.21.99 lakhs for the three years involving a potential tax effect of Rs.11.38 lakhs.

3.11 Incorrect allowance of expenditure on guest house

Under the Income-tax Act,1961, no deduction is allowed in respect of any expenditure incurred by an assessee after 28 February 1970 on the maintenance of any residential accommodation in the nature of guest house.The Act also provides that with effect from assessment year 1971-72 and onwards, no allowance shall be made in respect of depreciation on any building used as a guest house and on any assets in a guest house.

In Madhya Pradesh Circle, in the assessment of a company for the assessment year 1988-89 made in March 1989, expenditure of Rs.6.64 lakhs incurred by the assessee on the maintenance of the guest house was allowed in computing the total income of the assessee, inspite of the fact, that its inadmissibility was pointed out by the Chartered Accountants in the report of their audit, filed by the assessee alongwith the return of income. Incorrect allowance of expenditure which is not admissible under the specific provisions of the Act, resulted in short levy of tax of Rs.3.48 lakhs.

3.12 Incorrect allowance of deduction for payment of tax on income

Under the Income-tax Act,1961, in the computation of income chargeable under the head profits and gains of business or profession any sum paid on account of any rate of tax levied on the profits or gains or any business or profession is not allowable as deduction.

(i) In the case of a company in Bombay circle, in the assessments completed by the Deputy Commissioner of Income-tax in March 1989, for the assessment years 1987-88 and 1988-89, deductions for the payments of Rs.4.10 lakhs and Rs.1.88 crores being the payments of foreign taxes respectively were allowed. It was seen in audit that these were the taxes on the income earned by the assessee in the foreign countries. As the taxes were paid out of profits and not for earning income the deduction claimed, therefore, by the assessee was not allowable. The irregular allowance of deduction resulted in an aggregate under assessment of income of Rs.1.92 crores for both the assessment years involving short levy of tax of Rs.1.07 crores (including interest of Rs.6.66 lakhs paid by the Government for excess payment of advance tax).

(ii) In Bombay circle the assessment of a company for the assessment year 1986-87 was completed by the Deputy Commissioner of Income-tax (Special Range) in January 1989 accepting the total income of Rs.1.38 crores as returned.It was seen in audit that while arriving at the taxable income, the

company had deducted an amount of Rs.8.97 lakhs towards surtax liabiliy. The payment of surtax not being an allowable expenditure in computing the business income the assessing officer should have disallowed the claim. Omission to do so resulted in under assessment of income of Rs.8.97 lakhs with consequent short levy of tax of Rs.5.65 lakhs.

3.13 Incorrect allowance of provisions for contribution to unrecognised funds

1. Under the provisions of the Income-tax Act,1961, no deduction shall be allowed in respect of any provision for gratuity to employees on retirement or on termination of employment for any reason unless it is by way of contribution towards an approved gratuity fund or for the payment of gratuity that has become payable during the previous year. The Act also provides that a deduction otherwise allowable in respect of any sum payable by an assessee as an employer by way of contribution to any provident fund, superannuation or gratuity or any other fund for the welfare of employees is to be allowed only in computing the income of the previous year in which such sum is actually paid.

(i) In Bombay circle, the assessment of a widely held company for the assessment year 1988-89 was completed in August 1988. It was seen from the notes forming part of accounts that out of an amount of Rs.1.20 crores collected as Central Sales Tax an amount of Rs.16.90 lakhs was not paid to the Government. The unpaid amount of sales tax being statutory liability was required to be disallowed which was not done. The mistake resulted in under assessment of income of Rs.16.90 lakhs with consequent short levy of tax of Rs.9.65 lakhs (including interest of Rs.77,636 for short payment of advance tax).

(ii) In Karnataka circle, the assessment of a public limited company for the assessment year 1987-88 was completed in March 1989 accepting the loss as returned by the assessee company. It was, however, seen from the return of income that the assessee had not added back to the taxable income unpaid amounts of Central sales tax, State sales tax and Central excise duty aggregating Rs.51.69 lakhs outstanding at the end of the previous year on the ground that these amounts were not debited to the profit and loss account. Similarly, a sum of Rs.83,665 being the contribution to employees state insurance although debited to the profit and loss account was not paid during the relevant previous year but was not added back to the taxable income. As Sales tax and Central excise duty collections were part of trading receipts and as they were not paid to Government at the end of previous year, the amount of Rs.51.69 lakhs should have been brought to tax. Similarly the amount of Rs.83,665 being the unpaid employees State insurance contribution should have been disallowed in the assessment. The omission resulted in excess computation of loss by Rs.52.53 lakhs involving a potential tax effect of Rs.26.26 lakhs.

(iii) In West Bengal circle, the assessment of a company for the assessment year 1986-87 was completed by the Deputy Commissioner of Income-tax (Special Range) in March 1989 at a loss of Rs.6.64 crores. The Tax Audit Report of the company for the previous year relevant to the assessment year 1986-87 revealed that contribution to provident fund, superannuation fund, employees state insurance fund, deposit linked insurance fund, raw jute tax and turnover tax aggregating to Rs.1.12 crores was debited in the profit and loss account by the assessee during the rele-

vant previous year but was not paid during the year. Further, a sum of Rs.88,355 was paid to the employees of the company as salary in excess of the limits prescribed in the Act. As such, the aggregate of these two sums amounting to Rs.1.12 crores should have been disallowed and added back in the assessment. It was, however, noticed in audit (January 1990)that the same was not so added back.The mistake resulted in excess computation and excess carry forward of loss of Rs.1.12 crores for the assessment year 1986-87 involving potential tax effect of Rs.59.06 lakhs.

(iv) The assessments of a widely held industrial company in Calcutta circle, for the assessment years 1986-87 and 1987-88 were completed by the Deputy Commissioner of Income-tax (Special Range) in February 1989 at a loss of Rs.62.10 crores and Rs.80.38 crores respectively.The Tax Audit Reports for the previous years relevant to assessment years 1986-87 and 1987-88, revealed that taxes and duties amounting to Rs.7.26 crores and Rs.8.14 crores respectively debited in the relevant profit and loss account were not paid during the previous years. According to the provisions of the Act, the said sums of Rs.7.26 corres and Rs.8.14 crores were required to be disallowed and added back in the assessments. It was, however, noticed in audit in October 1989, that no such disallowance were made. Omission to make the above disallowance, therefore, resulted in excess computation of loss of Rs.7.26 crores and Rs.8.14 crores for the assessment years 1986-87 and 1987-88 respectively involving potential tax effect of Rs.7.88 crores.

(v) An assessee company in West Bengal circle debited in its account for the previous year relevant to the assessment year 1986-87, a sum of Rs.63.35 lakhs which included Rs.32.66 lakhs as sales tax liability, Rs.21.00 lakhs as provident fund,Rs.9.26 lakhs as employees state insurance and Rs.0.43 lakh on account of other funds for the welfare of the employees.The aforesaid amount of Rs.63.35 lakhs had not been paid to Government/appropriate authority in the previous year relevant to assessment year 1986-87. Since these statutory liabilities had not been actually paid in the relevant previous year, the assessee company was not entitled to deduction and the amount was required to be disallowed. While completing the assessment for the assessment year 1986-87 in March 1989, the assessing officer, however, failed to disallow the said sum of Rs.63.35 lakhs. The mistake resulted in over assessment of loss of Rs.63.35 lakhs with consequent excess carry forward of loss by an identical amount for the assessment year 1986-87 involving potential tax effect of Rs.33.26 lakhs.

(vi) In Karnataka circle, the assessments of a public limited company for the assessment years 1986-87 and 1987-88 were concluded in January 1989 accepting the loss returned by the assessee company. It was, however, seen from the audit report enclosed to the return of income for the above two assessment years as required under the Act, that out of the expenditure debited to the profit and loss account towards provident fund and central excise duty, amounts of Rs.12.26 lakhs and Rs.9.04 lakhs remained unpaid at the end of the relevant previous years. These sums were required to be disallowed.Further the assessee had collected state and central sales tax from its customers during the previous years relevant to assessment year 1986-87 and 1987-88 and the balance amounts of such collections not made over to Government at the end of each year amounted to Rs.2.78 lakhs

and Rs.1.14 lakhs respectively.These sums were to be treated as trading receipts and taxed. Omission to disallow unpaid provident fund and central excise duty and to add back unpaid sales tax collection resulted in excess computation of loss of Rs.15.04 lakhs and Rs.10.19 lakhs for the assessment year 1986-87 and 1987-88 respectively involving a total potential tax effect of Rs.12.99 lakhs.

3.14 Irregularities in allowing depreciation and investment allowance

1(i) In Karnataka circle, in the assessment of a company for the assessment years 1986-87 and 1987-88 completed by the Deputy Commissioner of Income tax in January 1989, the assessing officer allowed additional depreciation of Rs.15.67 lakhs and Rs.23.80 lakhs respectively as claimed by the assessee. Audit scrutiny, however, revealed that the machineries on which additional depreciation was claimed and allowed were installed after 31 March 1985 and as such no additional depreciation was admissible on them. The incorrect allowance of additional depreciation resulted in excess computation of loss by Rs.39.46 lakhs involving a potential tax effect of Rs.20.12 lakhs in aggregate for the two assessment years.

(ii) In Tamil Nadu circle, the assesments of a closely held company for the assessment years 1986-87 and 1987-88 were completed by the Deputy Commissioner of Income-tax in January 1989. Audit scrutiny (in March 1990) however, revealed that the company had purchased certain machinery on deferred payment basis, capitalised the interest due on future payments under deferred payment scheme and added the capitalised interest of Rs.63.84 lakhs and Rs.7.51 lakhs to the cost of machineries purchased during the previous years 1986-87 and 1987-88 respectively.The department allowed depreciation of Rs.14.36 lakhs and investment allowance of Rs.15.96 lakhs for assessment year 1986-87 and depreciation of Rs.1.69 lakhs for assessment year 1987-88 on the amount so added to the capital cost.The allowance of depreciation and investment allowance on the amount of interest wrongly added to the capital cost of the machinery resulted in an aggregate short levy of tax of Rs.17.35 lakhs for the two assessment years.

(iii) In Madhya Pradesh circle, in the assessment of a Banking company for the assessment year 1988-89, made by the Deputy Commissioer of Income-tax in March 1989, a deduction of Rs.28.12 lakhs was erroneously allowed in respect of purchases of 'data entry machine' (Rs.1.11 lakhs) and 'advance Ledger posting machine' (Rs.27.01 lakhs) during the year though the machineries were of the nature of calculating devices. Incorrect allowance of deduction of Rs.28.12 lakhs resulted in short levy of tax of Rs.14.76 lakhs.

(iv) In Bombay circle, in the assessment of a company for assessment year 1988-89 completed by the Deputy Commissioner of Income-tax in March 1989, the assessing officer allowed an amount of Rs.48.38 lakhs to be carried forward as unabsorbed investment allowance relating to assessment year 1986-87. Audit scrutiny revealed that the amount of unabsorbed investment allowance relating to assessment year 1986-87 which still remained to be set off, after taking into account the adjustments made in assessment year 1987-88, was to the extent of Rs.30.17 lakhs only as against Rs.48.38 lakhs carried forward by the assessing officer.The mistake resulted in excess carry forward of unabsorbed investment

allowance by Rs.18.20 lakhs involving potential short levy of tax of Rs.9.56 lakhs.

3.15 Income escaping assessment

1. (i) In Tamil Nadu circle, the assessment of a closely held company for the assessment year 1986-87 was completed in March 1989 on a taxable income of Rs.24.93 lakhs. Audit scrutiny in July 1989 revealed that during the relevant previous year, the assessee company received Rs.87.32 lakhs as long term service contract receipts and had incurred an expenditure of Rs.13.36 lakhs therefrom but the net receipts amounting to Rs.73.95 lakhs was not offered to tax nor did the department include it in the taxable income. Similar receipts were taxed in the assessment for the assessment year 1984-85 and the same was upheld in the appeals preferred by the assessee company. Omission to bring to tax the above contract recipts resulted in underassessment of income by Rs.73.95 lakhs for assessment year 1986-87 involving short levy of tax of Rs.42.71 lakhs.

(ii) In Gujarat circle during the previous year relevant to the assessment year 1983-84 an assessee private Ltd company received an amount of Rs.21.06 lakhs on account of remission of liabilities taken over from its holding company and realisation of claims relating to preacquisition transactions. However, this was treated as capital receipts and transferred directly to capital reserve account in the balance sheet without being routed through the profit and loss account. Audit scrutiny revealed that the assessee company was a 100 per cent subsidiary of the vendor company and the former had purchased one of the divisions of the business of the vendor company as a going concern with all movable and immovable assets together with assets and liabilities through an agreement dated 23 March 1981 and the sum of Rs.21.06 lakhs received was mainly from remission of liabilities and claims of pre-acquisition transactions of the business of the vendor company which was taken over by the assessee company. Therefore, the sum of Rs.21.06 lakhs received as stated above was required to be treated as income of the assessee company for the assessment year 1983-84. However, in the assessment for the assessment year 1983-84 completed in March 1986, the assessing officer did not bring to tax the aforesaid income even though he had brought similar income of later years to tax in the subsequent assessment years' assessments. Failure to do so resulted in under assessment of income of Rs.21.06 lakhs with short levy of tax of Rs.15.68 lakhs (including short levy of interest for default in filing return and for furnishing the estimate of income).

(iii) In Bombay circle, a private limited company collected central excise duty of Rs.88.21 lakhs and Rs.1.22 crores during the previous years relevant to assessment years 1987-88 and 1988-89 respectively, and these amounts were outstanding as liabilities, at the end of the previous year in the balance sheets for the respective years. The amounts were obviously neither credited to Government nor refunded to the concerned parties before the close of the relevant previous years. As such, these amounts should have been included as trading receipts while computing the business income of the assessee company as held by the Supreme Court. However, in the assessments for assessment year 1987-88 and 1988-89 completed in March 1989 the assessing officer did not include the aforesaid amounts while computing the business income.

Omission to do so resulted in escapment of income aggregating to Rs.2.10 crores leading to total short levy of tax of Rs.1.19 crores.

(iv) In West Bengal circle, the assessment records of an assessee company for the previous year relevant to the assessment year 1987-88 indicated that the sale-tax collected by the company during the year and not deposited to Government amounted to Rs.30.48 lakhs. The company did not include the amounts collected by it towards Sales tax in its profit and loss accounts.Sales-tax collected being a trading receipt, the unpaid amount of Rs.30.48 lakhs should have been brought to tax However,in the assessment of the said company for the assessment year 1987-88 completed in October 1988, the unpaid amount of sales tax was not brought to tax. The omission resulted in under assessment of income of Rs.30.48 lakhs with consequential under charge of tax of Rs.15.24 lakhs.

2. It has been judicially held* that the 'cash compensatory assistance' received by an assessee from Government towards his export performance constituted his revenue receipts, and chargeable to tax.

(i) A private limited company received 'Cash compensatory assistance' for exports amounting to Rs.6.10 lakhs, Rs.7.20 lakhs and Rs.21.50 lakhs in the previous years relevant to the assessment years 1986-87 to 1988-89 respectively.The assessee claimed the exemption from tax for these receipts on the plea that the receipts were of capital nature and not taxable as income. In the assessments for these years completed in March 1989 the assessing officer accepted the assessee's claim and omitted to assess the amounts received. As the cash compensatory assistance received by the assessee was a revenue receipts it was liable to be taxed accordingly. The omission to do so resulted in the aggregate under assessment of income of Rs.34.79 lakhs for the assessment years 1986-87 to 1988-89 involving short levy of tax of Rs.21.70 lakhs.

(ii) During the previous year relevant to assessment year 1988-89, a private limited company in Bombay Circle received refund of central excise duty of Rs.32.74 lakhs.As the refund in question relates to central excise duty allowed as deduction in earlier years, the refund received should have been included as income while computing the business income for assessment year 1988-89. However, in the assessment for assessment year 1988-89 completed in March 1989 the assesing officer did not include the aforesaid amount while computing the business income. Omission to do so resulted in escapment of income by Rs.32.74 lakhs leading to short levy of tax of Rs.21.51 lakhs including interest for failure to file higher estimate of income for advance tax.

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* 142 ITR 448 - Jeevanlal (1929) Ltd. V, C.I.T. (Central Circle II) Calcutta.

Chapter 4

Income-tax

Some of the important observations noticed during the course of audit of non-company assessments,completed by assessing officers in summary manner are given below. In all 276 audit observations involving tax effect of Rs. 6.64 crores were forwarded to the Ministry of Finance for comments during January 1990 to July 1990. The following cases will give an idea of the type of irrregularities which escaped the notice of the department because of the wholesale coverage of Summary Assessment Scheme.

4.01 Incorrect application of rates of tax

Under the provisions of Income-tax Act, 1961, income derived from property held under trust wholly for religious and charitable purposes, subject to certain conditions, is exempt from income-tax, but if the income of such a trust is used or applied directly or indirectly for the benefit of the author of the trust or a person who has made a substantial contribution to the funds of the trust or for the benefit of any concern in which any such person has a substantial interest or if any funds of the trust are invested or deposited in a form or mode other than the prescribed ones, tax shall be charged at the maximum marginal rate.

In the case of a trust in Utter Pradesh circle, funds amounting to Rs. 3.84 lakhs, Rs. 4.30 lakhs and Rs.4.30 lakhs remained deposited with a company whose managing director was the trustee of the trust during the previous years relevant to the assessment years 1985-86, 1986-87 and 1987-88 respectively. The interest income accrued on these deposits was accounted for only in the assessment year 1985-86 and the interest of Rs. 51,581 (@ 12 per cent on Rs. 4.30 lakhs) accrued in each of the assessment years 1986-87 and 1987-88 was not accounted for and consequently had escaped assessment. Since the assessee had deposited its funds in a company whose managing director was the trustee and the deposit was not in a form or mode prescribed in Section 11(5) of the Income-tax Act, the maximum marginal rate of tax was applicable but the department charged tax at the ordinary rates. The escapement of interest income and omission to apply the maximum marginal rate resulted in short charge of tax amounting to Rs. 91,711.

4.02 Mistakes in the computation of trust income

Under the provisions of the Income-tax Act 1961, as applicable from the assessment year 1985-86, where the income of a trust consists of or includes income from business, the trust is liable to be taxed at the maximum marginal rate.

In Gujarat circle, an assesses trust, which had been carrying on some trading activities up to the assessment year 1984-85, discontinued such activities and returned the income for assessment years 1985-86 to 1988-89 under the head 'other sources'. The income returned by the assessee comprised the excess of interest receipts over interest payment. It

was noticed that the assesses trust had a capital of more Rs.1.38 lakhs on an average during these four years while it had resorted to borrowings to the extent of Rs. 98 lakhs (average) and had lent money to the extent of Rs. 99.92 lakhs (average) to more than a hundred parties. Obviously the assessee was engaged in the business of borrowings for the purpose of lending and the assessee's case cannot be considered as receiving interest on investment of surplus funds. Since there was obviously, business activity, the income was liable to be taxed under the head business income and the assesses was liable to be taxed at the maximum marginal rate. The mistake in accepting the returns and completing the assessment in August 1989 resulted in short levy of tax of Rs. 3.46 lakhs including penalty of Rs. 1.53 lakhs and interest of Rs. 39,282 for non payment of advance tax.

4.03 Incorrect computation of income from house property

Under the provisions of the Income-tax Act, 1961, the annual value of property consisting of building and lands appurtenant thereto, of which the assessee is the owner, is assessable as 'income from house property'. It has, been judicially held ǂ that the income derived from letting out of building owned by the assessee to tenants is to be computed under the head 'Income from house property' and not under the head 'Income and gains of business or profession' regardless of the object of the assessee.

In West Bengal circle, in the assessment of an individual for the assessment years 1983-84 to 1987-88 completed between March 1986 and January 1988 rental income from letting out of garage to various tenants was assessed under the 'Profits and gains of business or profession' computing a total income of Rs. 2.79 lakhs for the five assessment years. As the rental income from letting out of a building was assessable under the head 'Income from house property' after allowing deductions on account of actual municipal taxes and repair and collection charges at the prescribed rates, the income from the property for the five assessment years was assessable at Rs. 5.55 lakhs. The mistake in classifying the income under a wrong head resulted in under assessment of income of Rs. 2.76 lakhs involving short levy of tax of Rs. 1.87 lakhs including interest for belated submission of returns and short payment of advance tax in assessment years 1983-84 to 1987-88.

4.04 Incorrect allowance of expenditure on guest house

In the assessment of co-operative society in Madhya Pradesh circle for the assessment years 1986-87 to 1988-89 made in January 1989, deductions for expenditure on advertisement in souvenirs of political parties, travelling in excess of prescribed limits, maintenanace of guest house,provision for bad and doubtful debts and liabilities of taxes and provident fund were allowed amounting to Rs.1.74 lakhs, Rs. 1.09 lakhs and Rs. 4.16 lakhs in respect of assessment years 1986-87, 1987-88 and 1988-89 respectively, in contravention of the provisions of the Act. The incorrect allowance of expenditure resulted in excessive carry forward of losses to the extent of inadmissible expenses and potential short levy of tax aggregating to Rs. 2.69 lakhs

ǂ 83 ITR 700 - SG Mercantile Corporation (P) Ltd. V. C.I.T. Calcutta

4.05 Incorrect allowance of liabilities

1. Under the provisions of the Income-tax Act 1961, as applicable from the assessment year 1984-85, in computing the business income of an assessee, liability for any sum payable by way of tax or duty under any law for the time being in force will be allowed out of the income of the previous year in which such sum is actually paid irrespective of the method of accounting employed by the assessee. In other words, these deductions are admissible only on actual payment and not on accrual basis.

(i) In Karnataka circle, three assessee co-operative sugar factories A, B and C debited to their profit and loss accounts for the years relevant to assessment years 1986-87 to 1988-89, certain sums towards purchase tax liability. The amount of purchase tax debited were Rs. 12.41 lakhs for the previous year relevant to the assessment year 1987-88, Rs.1.18 crores for three previous years relevant to assessment years 1986-87 to 1988-89 and Rs. 11.88 lakhs for the previous year relevant to assessment year 1986-87 in the cases of A, B and C respectively. The above liabilities had not been discharged till the end of the relevant previous years. Accordingly these liabilities should have been disallowed in the assessments. However, these liabilities were not disallowed in the summary assessments concluded in November 1988, October 1988 and December 1988 in respect of the assessees A, B and C respectively. The omission led to total excess computation of loss of Rs. 1.43 crores involving potentital tax effect of Rs. 57.76 lakhs.

(ii) In the assessments of 3 registered firms assessed in West Bengal circle for different assessment years between 1985-86 and 1988-89 during June 1987 and June 1989 sales tax amounting to Rs. 11.16 lakhs was allowed as deduction although the sums collected in the relevant previous years were not actually paid and featured as current liability in the balance sheets. The omission resulted in under assessment of income of Rs.28.41 lakhs involving short levy of tax of Rs.7.70 lakhs.

4.06 Mistake in valuation of closing stock

In order to determine the profits from business an assessee who maintains accounts on mercantile basis, may choose to value the closing stock of his business every year, at cost or market price, whichever is lower. It has been judicially [2] held in September 1980 that the privilege of valuing closing stock in a consistent manner would be available only to a continuing business and that it cannot be adopted where a business comes to an end when stock in hand would be valued at the market (value) price in order to determine the true profits of business on the date of closure of business. The Ministry of Law also had confirmed this position in August 1982 and March 1984.

In Gujarat circle, an assessee firm engaged in the business of manufacturing and selling of salt followed mercantile system of accounts and opted to choose valuing the closing stock 'at cost'. During the previous year relevant to assessment year 1988-89 (assessment made in August 1988) the total salt manufactured as per the cost account filed with the return of income worked out to 18,676 tonnes and average cost per tonne was arrived at Rs. 42.59. It

[2] 102 ITR 622 - A.L.A. Firm V. C.I.T., Madras

was, however, noticed in audit that closing stock of salt was shown as 19,140 tonnes the value of which was shown at Rs. 2.87 lakhs at the rate of Rs. 15 per tonne as against the actual cost of Rs. 42.59 per tonne. The market price of salt based on the sale price realised during the year was Rs. 69 per tonne. The closing stock of the business, to be valued at cost or market price whichever is less, was thus required to be valued at the rate of Rs. 42.59 per tonne whereas it was valued at Rs.15 per tonne. This resulted in under valuation of the closing stock to the extent of Rs. 5.28 lakhs with consequent short levy of tax of Rs. 3.31 lakhs.

Irregularities in allowing depreciation, investment allowance and investment deposit account

4.07 Mistakes in the allowance of depreciation

Under the Income-tax Act, 1961, in computing the business income of an assessee, a deduction on account of depreciation on plant, machinery or other assets is admissible at the prescribed rates provided these are owned by the assessee and used for the purpose of business during the relevant previous year. Depreciation on buildings, plant and machinery is calculated on their cost or written down value, as the case may be, according to the rates prescribed in the Income-tax Rule 1962. A general rate of 10 per cent (15 per cent from the assessment year 1984-85) has been prescribed in respect of plant and machinery for which no special rate has been prescribed.

(i) Upto the assessment year 1987-88, depreciation on motor cars was admissible at 40 percent of the written down value if the cars were used in the business of running them on hire, otherwise, the admissible rate was 20 percent only.

While completing the assessment of a registered firm in Maharashtra circle for the assessment years 1984-85 and 1985-86 in June 1985 and December 1985 respectively, depreciation of Rs. 2.41 lakhs and Rs. 3.51 lakhs was allowed on motor cars at the rate of 40 percent. As the cars were not used in the business of running them on hire the depreciation was allowable at 20 percent only. The mistake resulted in underassessment of income of Rs. 1.20 lakhs and Rs. 1.75 lakhs for assessment years 1984-85 and 1985-86 respectively involving a total short levy of tax of Rs. 1.98 lakhs.

(ii) In Maharashtra circle, in the assessment of a registered firm, engaged in the business of construction work, for assessment years 1984-85 to 1987-88 (assessed between March 1987 and March 1988), depreciation on plant and machinery was allowed at the rate of 20 percent instead of at the correct rate of depreciation of 15 percent. The incorrect allowance of depreciation resulted in excess allowance of depreciation of Rs. 1.72 lakhs involving short levy of tax of Rs.1.36 lakhs.

(iii) In Karnataka circle, the assessments of an assessee co-operative sugar factory for the assessment years 1985-86, 1986-87 and 1987-88 were completed in October 1988 and that for the assessment year 1988-89 in March 1989 accepting the income/loss as returned by the assessee. A scrutiny in audit revealed that the assessee had filed a revised return, for the assessment year 1984-85 in October 1986 with a revised chart of depreciation. This return was accepted in the scrutiny assess-

ment concluded in October 1987. The revised written down value to be adopted for calculating depreciation for the next assessment year 1985-86, accordingly was Rs. 2.65 crore as against the written down value of Rs. 3.34 crores shown in the return of income for the assessment year 1985-86. The adoption of incorrect written down value of Rs. 3.34 crores for calculation of depreciation for the assessment year 1985-86 resulted in excess allowance of depreciation aggregating to Rs. 47.97 lakhs for the assessment years from 1985-86 to 1988-89 involving a potential tax effect of Rs. 20.23 lakhs.

4.08 Incorrect grant of investment allowance

1. Under the Income-tax Act, 1961, in computing the business income of an assessee, a deduction is allowed by way of investment allowance at twenty five percent of the actual cost of machinery or plant installed after 31 March 1976 but before 1 April 1987 for the purpose of business of manufacture or production of any article or thing except those specified in the Eleventh Schedule to the Act and in the case of a small scale industrial undertaking, any article or thing.

(i) In Madhya Pradesh circle, an assessee firm engaged in the busiess of transportation was not engaged in any activity of manufacture or production of any article or thing and was, therefore, not entitled to the deduction by way of investment allowance. However, in the assessment for the assessment year 1985-86 made in March 1988, investment allowance of Rs. 6.52 lakhs in respect of poclain machinery costing Rs. 26.07 lakhs was allowed out of which a sum of Rs. 4.44 lakhs was adjusted against the profit of the year and the balance of Rs. 7.08 lakhs was carried forward and allowed to be set off against the profit for the assessment year 1986-87 in the assessment made in October 1988. The assessment for the assessment year 1986-87 was revised subsequently, in March 1989 to withdraw the incorrect investment allowance of Rs. 2.08 lakhs holding that the assessee was not entitled to the deduction of investment allowance, being not engaged in the business of manufacture and production of any article or thing. However, no action was initiated to revise assessment for the assessment year 1985-86 to withdraw the deduction of investment allowance of Rs. 4.44 lakhs granted incorrectly for the reasons discussed in the revisionary orders for the assessment year 1986-87. This resulted in incorrect grant of investment allowance of Rs. 4.44 lakhs in the assessment year 1985-86 and short levy of tax of Rs. 2.10 lakhs in the case of the firm and its partners and including undercharge of interest of Rs. 28,831 for default in payment of advance tax.

(ii) In Karnataka circle, the assessment of a co-operative sugar factory for the assessment year 1988-89 was completed in December 1988 allowing carry forward of unabsorbed investment allowance amounting to Rs. 1.23 crores in respect of the assessment years 1979-80 and 1980-81. As the unabsorbed investment allowance of assessment years 1979-80 and 1980-81 could not be carried forward beyond the assessment year 1987-88 and 1988-89 respectively, the benefit of carry forward allowed in the assessment for the year 1988-89 was not in order. The incorrect carry forward of unabsorbed investment allowance involved potential tax effect of Rs. 51.54 lakhs.

4.09 Irregular computation of capital gains

1. Under the Income-tax Act, 1961, any profits or gains arising from the transfer of a capital asset effected in the previous year shall be chargeable to income-tax under the head "Capital gains" and shall be deemed to be the income of the previous year in which the transfer took place. Capital assets are classified under the Act as short term assets or long-term assets according to the period for which they are held by an assessee. Those capital assets held for not more than thirty six months immediately preceding the date of transfer will be termed as short term capital assets, and other as long term capital assets. While the capital gains derived from the sale of long term capital assets are chargeable to income-tax after allowing certain deduction, the capital gains relating to short term capital assets are chargeable to tax without allowing such deduction.

The capital gain is computed with reference to the cost of acquisition of the asset, or where the capital asset became the property of the assessee before 1 April 1974, at the option of the assessee, on the basis of fair market value of the asset as on that date

In the case of an assessee (AOP) in Bihar circle for the assessment year 1987-88, assessment completed in January 1988, the capital gain of Rs. 1.14 lakhs on the transfer of its properties was computed by taking the fair market value as on 1 April 1974 at Rs.18.72 lakhs as shown in the valuation report submitted with the return for the assessment year 1987-88. The assessee's wealth-tax return showed the value as on 1 April 1974 at Rs. 3.20 lakhs in respect of the said properties. The incorrect substitution of the fair market value led to under valuation of capital gain by Rs. 2.16 lakhs involving short levy of tax of Rs. 1.39 lakhs, including interest for belated submission of the return

2 Capital gains on the transfer of a capital asset is computed with reference to the cost of acquisition of the asset or where the capital asset became the property of the assessee before 1 January 1964, at the option of the assessee, the fair market of the asset as on that date.

In Andhra Pradesh circle an assessee sold his land admeasuring 4.60 acres for a consideration of Rs. 2.66 lakhs and another piece of land admeasuring 2.46 acres for a consideration of Rs. 1.72 lakhs in the previous years relevant to the assessment years 1983-84 and 1984-85 respectively. The fair market value of the lands as on 1 January 1964 were adopted by the assessee at Rs. 2.01 lakhs and Rs. 1.23 lakhs respectively for the two pieces of lands and the same were accepted by the assessing officer in the assessments completed in November 1986. Correlation of the wealth-tax records of the assessee revealed that the assessee had declared the value of the two properties at Rs.60,400 and Rs. 49,600 respectively for the assessment year 1976-77 based on the registered valuer's report of February 1971. Even adopting these values as the fair market values of the properties as on 1 January 1964, there was short computation of capital gains by Rs. 87,960 and Rs. 44,040 respectively for the years 1983-84 and 1984-85 resulting in short levy of tax of Rs. 1.03 lakhs including interest for late filing of returns.

3. From the assessment year 1978-79, the capital gains arising from

the transfer of a long term asset are exempted from tax, if the net value of the consideration received or accruing as a result of the transfer is invested or deposited by the assessee in specified asset within a period of six months after the date of transfer. During the period from 28 February 1979 to 1 March 1983, relevant to the assessment years 1979-80 to 1983-84, the benefit of exemption would be available, only if the net consideration was invested in 7 year National Rural Development Bonds. Further, under the Act, where the gross total income of an assessee, not being a company, includes any income chargeable under the head 'Long term capital gains' and such income exceeds five thousand rupees, there shall be allowed in computing the total income a deduction from such income of an amount equal to five thousand rupees as increased by a sum calculated at prescribed rates with reference to the amount by which the long term capital gains exceeds five thousand rupees.

During the previous year ending 31 December 1982, relevant to the assessment year 1983-84, an individual in West Bengal circle sold a house property for Rs. 20.40lakhs. In the computation of total icnome, filed along with the return of income for the assessment year 1983-84, the assessee took the capital gains from the sale of house property at Rs. 17.86 lakhs (after deducting cost of acquisition of Rs. 2.50 lakhs and legal expenses of Rs. 4,000) and claimed an exemption of Rs. 12 lakhs on account of investment in specified assets. The assessee also, after adjustment of other incomes had a business loss of Rs. 3.33 lakhs. The assessee claimed a deduction from the amount of capital gain of Rs. 5.86 lakhs, a sum of Rs. 2.37 lakhs as admissible under the Act and offered the balance of Rs. 3.49 lakhs as income from long term capital gains on the sale of house property ignoring the loss of Rs. 3.33 lakhs omitting to restrict the deduction admissible from capital gain to the amount admissible with reference to the net total income assessed after adjustment of loss. The assessing officer, accepted the computation made by the assessee and completed the assessment in December 1985. Audit scrutiny made in June 1988 revealed that out of the investment of Rs. 12 lakhs on which exemption was claimed and allowed, Rs. 5 lakhs were invested in fixed deposits in a nationalised bank and Rs. 9.25 lakhs were appropriated towards purchase of machinery for a press owned by the assessee. As both the above investments did not fall within the meaning of specified asset as defined in the Act, the assessee was not entitled to any exemption from capital gains. Therefore, on the gross total income of Rs. 14.53 lakhs arrived at after the adjustment of business loss of Rs. 3.33 lakhs against the capital gain of Rs. 17.86 lakhs from the sale of house property, a deduction of Rs. 5.84 lakhs was admissible and the balance of Rs. 12.02 lakhs (Rs. 17.86 lakhs less Rs. 5.84 lakhs) was to be treated as capital gains on sale of the said property. But due to incorrect computation of capital gain and irregular allowance of exemption, the capital gain was erroneously computed at Rs. 3.49 lakhs. The mistake resulted in under assessment of capital gain of Rs. 8.53 lakhs (Rs.12.02 lakhs minus Rs. 3.49 lakhs) with consequent undercharge of tax of Rs. 5.51 lakhs for theassessment year 1983-84.

4. Capital asset does not include personal effects. It has been judicially held that mere possibility of such articles capable of being put to personal use would not be sufficient to treat them as intended for personal or

household use; it has to be proved that such articles are put to personal or household use at least occasionally, if not regularly.

An assessee individual in West Bengal circle acquired silver utensils weighing 235 kilograms at an average cost of Rs. 472.34 per kilogram in the previous years relevant to the assessment years 1972-73 and 1973-74. Out of the said stock of silver utensils, 90 kilograms and 123 kilograms were sold at Rs. 2,430 and Rs. 3,100 per kilogram in the previous years relevant to the assessment years 1983-84 and 1985-86 respectively. The capital gains made thereon to the extent of Rs.1.31 lakhs and Rs. 2.73 lakhs (after allowing maximum deduction of Rs.50,000 in each year)were neither returned by the assessee nor assessed to tax accordingly in the assessment completed in September 1986 and May 1987. Omission to do so resulted in aggregate short levy of income-tax of Rs. 3.98 lakhs including non-levy of interest of Rs.71,042 for belated submission of return and Rs. 89,381 for short payment of advance tax in assessment years 1983-84 and 1985-86.

4.10 Mistakes in the assessment of firms and partners

Under the provisions of the Income-tax Act, 1961, if the assessment of the firm had not been completed, the share income from the firm is included in the assessments of the partners on provisional basis and revised later to include the final share income on completion of the assessment of the firm. For this purpose, the Income-tax Officer, is required under the instructions issued by the Central Board of Direct Taxes in March 1973 to maintain a register of cases of provisional share income so that these cases are not omitted to be rectified. No revision of assessment of partner can, however, be made under the Act, after the expiry of four years from the end of the financial year in which the final order was passed in the case of the firm.

(i) While concluding the assessments of a partner of a firm in Karnataka circle for the assessment years 1985-86 and 1986-87 in March 1988 and November 1988, the share of profit from the firm was provisionally adopted as Rs. 50,782 and Rs. 30,000 for the respective assessment years, subject to revision on completion of assessments of the firm, which was also under the jurisdiction of the same assessment range. Audit scrutiny revealed that the assessments of the firm for the assessment years 1985-86 and 1986-87 were completed in February 1988 and January 1989 determining the share of profits of the partner as Rs. 1.85 lakhs and Rs. 3.85 lakhs respectively. Even though the assessment of the firm for the assessment year 1985-86 had already been completed in February 1988 in the same range determining the correct share of profits of partners, the assessment of the partner concluded later in March 1988, nevertheless, adopted the provisional share income returned by the assessee. The assessment of the partner continued to remain unrectified till the mistake was pointed out by audit in December 1989. Likewise, the assessment of the partner for the assessment year 1986-87 was also not revised adopting the correct share of profits, on the basis of the firm's assessment finalised in January 1989. The mistakes resulted in under assessment of income of Rs. 4.89 lakhs with a consequent short levy of tax of Rs.2.61 lakhs.

(ii) In Maharashtra circle, a registered firm was paying royalty to one of its partners regularly every year. Audit scrutiny of the assessment records for the assessment year 1988-89 revealed that (a) the partner had been assessed to tax upto the assessment year 1979-80 by another assessing officer and the file had been discontinued in 1983-84 (b) she had been in receipt of the royalty even after the assessment year 1979-80 and had received a sum of Rs. 21.50 lakhs in aggregate by way of royalty during the assessment years 1980-81 to 1988-89 and (c) she had filed estimates of income of Rs. 18,000 for each of the assessment years 1986-87 to 1988-89. As no assessment was done after the assessment year 1979-80, there was an aggregate under assessment of income of Rs. 24.49 lakhs for the assessment years 1980-81 to 1988-89. The undercharge of tax for the last three years 1986-87 to 1988-89 alone amounted to Rs.3.94 lakhs.

4.11 Income escaping assessment

1. Under the provisions of Income-tax Act, 1961, the total income of a person for any previous year includes all income from whatever source derived, which is received or deemed to be received or which accrues or arises or deemed to accrue or arise during such previous year unless specifically exempted from tax.

In Karnataka circle, in the balance sheets of a co-operative society as at the end of previous years relevant to the assessment years 1985-86 to 1988-89, a sum of Rs. 151.52 lakhs was being shown as a liability under 'sugar sales suspense account' representing the claim pertaining to levy sugar which was pending before the Supreme Court. This amount was kept as fixed deposit in a co-operative bank and a total amount of Rs. 18.61 lakhs was earned as interest on this deposit during the previous years relevant to the assessment years 1985-86 to 1988-89. This interest amount was not considered as income of the society in the assessments concluded for the assessment years 1985-86 to 1987-88 in October 1988 and for the assessment year 1988-89 in March 1989, though similar amount of interest was brought to tax in the earlier assessment year 1984-85 in the assessment concluded in October 1987. The omission to include the interest income resulted in short computation of income by Rs. 18.61 lakhs. Further, an amount of Rs. 5 lakhs debited to the profit and loss account of the previous year relevant to the assessment year 1986-87 towards provision of interest on sugar sale suspense account was also not disallowed as being only a provision and not an ascertained liability. Thus there was total short computation of income by Rs. 23.61 lakhs resulting in potential tax effect of Rs. 9.52 lakhs for assessment years 1985-86 to 1988-89.

2. It has judicially been held [3] that foregoing of interest, being not on the grounds of commercial expediency, is to be included in the total income of the assessee.

An assessee individual in Madhya Pradesh circle advanced loan to a housing society. The balances at the end of the previous years relevant to the assessment years 1986-87, 1987-88 and 1988-89 were Rs.34.49 lakhs, Rs. 34.35 lakhs and Rs. 34.41 lakhs respectively. The assessee did not include any interest accrued on these loans in respect of each of the assessment years stating that

[3] 137 ITR 272 - Smt. Sushila Devi Pampuria V. C.I.T., W.B.II

interest was not charged in view of the financial difficulties and losses sustained by the society. Although, the assessing officer had included in the total income, the interest from such loan at 15 percent of the balance at the end of the previous year relevant to the assessment year 1985-86, in the assessment made in January 1988, no such interest was included in the assessment for the assessment years 1986-87 to 1988-89 made in January 1989. This resulted in escapement of income of Rs. 5.17 lakhs, Rs. 5.15 lakhs and Rs. 5.16 lakhs being accrued income from interest on loan of 15 percent of the balances at the end of the previous years relevant to the assessment years 1986-87, 1987-88 and 1988-89 resulting in potentital short levy of tax of Rs. 7.87 lakhs in aggregate.

3. It has judicially been held[4] that if the Government, as an incentive to boosting trade or for any other desirable reason to the benefit of the economy of the country, grants subsidies connected with the business of certain class of persons, such subsidies, generally speaking are receipts of revenue nature. Also, if a subsidy is given to recoup revenue expenditure it partakes the colour of a revenue receipt in the hands of the assessee [5].

In Madhya Pradesh circle, an assessee co-operative society received yarn subsidy of Rs. 14 lakhs during the previous year relevant to the assessment year 1986-87. This was not, however, offered for tax in the return of loss filed by the assessee. The assessing officer, in the assessment made accepted the loss of Rs.30.79 lakhs as returned by the assessee. Thus, the yarn subsidy received by the assessee escaped assesement resulting in potential short levy of tax of Rs. 5.60 lakhs.

4. It has been judicially held [6] that cash compensatory support given to exporters is taxable as trading receipts.

(i) While completing the assessment of a registered firm in Maharashtra circle for the assessment year 1988-89 in January 1989, assessee's claim that cash compensatory support of Rs. 17.32 lakhs received during the relevant previous year was exempt being capital receipt was accepted by the assessing officer though the cash compensatory support received was taxable as trading receipt. Omission to do so resulted in under assessment of income of Rs. 17.32 lakhs involving short levy of tax of Rs. 4.36 lakhs in the hands of the firm alone.

(ii). In Tamil Nadu circle, in the assessment of a registered firm dealing in the business of garment exports for the assessment years 1987-88 and 1988-89 completed in March 1989 receipts towards cash incentives amounting to Rs. 13.64 lakhs and Rs. 17.70 lakhs were deducted while computing the taxable income. Since cash incentive/cash compensation constitute revenue receipts, they would require to be included in the business income. Omission to do so resulted in under assessment of income by Rs. 13.64 lakhs and Rs.17.70 lakhs for assessment years 1987-88 and 1988-89 respectively involving an aggregate short levy of tax of Rs. 11.11 lakhs including interest of Rs. 48,359 for non-filing of estimate in the hands of firm and partners.

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4 106 ITR 473 - Dharangadhara Chemical Works Ltd. V. C.I.T., Bombay

5 122 ITR 942 - Ludhiana Central Co-op Consumers Stores Ltd. V. C.I.T.

6 142 ITR 448 - Jeevanlal (1929) Ltd. V. C.I.T. (Central Circle II) Calcutta.

(iii) In Delhi circle, while making the assessment of a registered firm engaged in construction activity for the assessment year 1986-87 (assessment completed in March 1989), the assessing officer assessed suppressed income of Rs. 29.91 lakhs of the assessee firm in the assessment years 1984-85 to 1986-87 on the basis of receipts filed by the assessee (value of work done) *i.e.* Rs. 13.26 lakhs in assessment year 1984-85, Rs. 7.93 lakhs in assessment year 1985-86 and Rs. 8.72 lakhs in assessment year 1986-87. The assessing officer, accordingly added Rs.8.72 lakhs as concealed income to the assessment year 1986-87 but omitted to add Rs. 13.26 lakhs and Rs. 7.93 lakhs in the assessment years 1984-85 and 1985-86 respectively. This resulted in under assessment of income by Rs. 21.19 lakhs for these assessment years involving undercharge of tax of Rs.7.33 lakhs including interest for late filing of returns and short payment of advance tax.

5. It has been judicially held [7] that before the property income of a person is assessed to tax, it is not necessary that he must be the owner of the property by virtue of a sale in his favour .

In West Bengal circle, in the assessments for the assessment years 1983-84 to 1987-88 made between February 1986 and November 1987, the assessing officer completed the assessments without considering the rental income from an ownership flat of the assessee. The income of the said property was not disclosed in the returns filed by the assessee since the ownership flat was not registered with the Registration authority. In fact, the assessee received the rent in respect of this flat by letting it out and also paid municipal taxes for the flat. Audit scrutiny (June 1988) revealed that the rental income of the flat was actually assessed for the assessment years 1980-81 to 1982-83 under the head 'income from house property' and also the assessments for the assessment years 1980-81 and 1981-82 were confirmed by the appellate authority. The rental income of the flat should, therefore, have been included in the total income of the assessee for the subsequent assessment years. The omission to do so led to net under assessment of income of Rs. 3.73 lakhs and under charge of tax aggregating to Rs. 1.36 lakhs including interest for belated submission of returns and non-payment of advance tax for the five assessment years.

6. Under the provisions of the Income-tax Act, 1961, as amended with effect from 1 April 1987, an assessee being an Indian company or other assessee resident in India engaged in the business of export of goods or merchandise other than mineral oils, minerals and ores was entitled to a deduction in the computation of taxable income of an amount equal to 4 percent of the net foreign exchange realisation plus a further amount of 50 percent of so much of the profits derived from the export of such goods of merchandise as exceeds the amount of 4 percent of net foreign exchange realisation.

(i) In Karnataka circle, in the case of an assessee firm which quarried granite stones polishes and exported them, deduction of Rs.10.89 lakhs, Rs. 5.34 lakhs and Rs. 6.10 lakhs was allowed on its export turnover for the assessment years 1986-87, 1987-88 and 1988-89 while concluding the assessments in March 1988, March 1989 and November 1989 though the commodity granite

[7] 130 ITR 321 - Smt. Kalarani V. C.I.T. Patiala-I

stones fell under the category of 'minerals and ores' not qualifying for the deduction. The incorrect allowance resulted in an aggregate short levy of tax of Rs.5.41 lakhs in the hands of the firm and Rs. 8.44 lakhs of its partners for the three years.

(ii) In Maharashtra circle, in the assessment for the assessment year 1987-88 completed in December 1988 an assessee, a registered firm, was allowed deduction of Rs. 2.63 lakhs in respect of profits retained for export business as claimed by the assessee. The profit and loss account for the period relevant to the assessment year 1987-88 did not show any income from export business received in convertible foreign exchange. The Chartered Accountant in his report had also stated that the assessee had not effected any exports during the year. The assessee firm was, therefore, not eligible for deduction in respect of profits retained for export business. The incorrect allowance of deduction of Rs. 2.63 lakhs resulted in under assessment of like amount involving short levy of tax of Rs. 1.54 lakhs in the hands of the firm and its partners.

7. The deduction shall not be admissible unless the assessee furnishes in the prescribed form alongwith the return of income the report of an accountant certifying that the deduction has been correctly claimed.

A registered firm in Maharashtra circle claimed deduction amounting to Rs.23.45 lakhs and Rs. 38.10 lakhs towards relief in respect of profits derived from export business for assessment years 1987-88 and 1988-89 respectively, and the same was allowed by the department. However, as per the certified audit report, furnished by the assessee, the deduction allowable worked out to Rs.19.53 lakhs and Rs. 23.32 lakhs only for assessment years 1987-88 and 1988-89 respectively. The excess allowance of deduction resulted in under assessment of income of Rs. 3.92 lakhs for assessment year 1987-88 and Rs. 4.78 lakhs for assessment year 1988-89 with aggregate short levy of tax of Rs. 2.14 lakhs in the hands of firm alone.

4.12 Incorrect carry forward of relief in respect of profits from newly established industrial undertaking established prior to 1 April 1981

Under the provisions of the income-tax Act, 1961, prior to its amendment by Finance Act, 1980, with effect from the assessment year 1981-82, where the gross total income of an assessee included any profits and gains derived from a newly established undertaking which went into production before 1 April 1981, the assessee became entitled to tax relief in respect of such profis and gains upto six percent per annum of the 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, however, such profits and gains fell short of the relevant amount of the capital employed during the previous year, the amount of such shortfall or deficiency was to be carried forward and set off against future profits upto the seventh assessment year reckoned from the end of the initial assessment year and not beyond.

(i) In Karnataka circle, the assessment of a co-operative sugar factory for the assessment year 1988-89 was completed in December 1988 allowing carry forward of unabsorbed relief amounting to Rs. 42.32 lakhs in respect

of profits from newly established industrial undertaking relating to assessment years 1979-80 to 1981-82. As the initial assessment year in which such relief was allowable was 1979-80 the unabsorbed relief pertaining to asessment years 1979-80 to 1981-82 could not be carried forward beyond the assessment year 1986-87. The incorrect carry forward of relief to the extent of Rs. 42.32 lakhs involved a potential tax effect of Rs. 17.73 lakhs.

(ii) In Karnataka circle, the assessments of three co-operative sugar factories,viz., 'A' for the assessment year 1986-87, 'B' for the assessment year 1987-88 and 'C' for the assessment year 1988-89 were completed in December 1988, November 1988 and October 1988 respectively allowing carry forward of unabsorbed relief in respect of profits from newly established industrial undertakings as detailed below:

Factory	Assessment year to which the unabsorbed relief relates	Amount of unabsorbed relief
A	1979-80, 1980-81 and 1982-83	Rs. 25.92 lakhs
B	1980-81	Rs. 8.44 lakhs
C	1983-84	Rs. 2.45 lakhs

Scrutiny in audit, however, revealed that the initial assessment in which the reliefs were first allowed were assessment year 1976-77 in the case of Factory A, and 1979-80 in respect of factories B and C. Accordingly, the benefit of carry forward of the deficiency allowed in the assessment for the assessment years 1986-87, 1987-88 and 1988-89 was not correct as it was beyond seventh assessment year as reckoned from the end of the initial assessment year. The incorrect carry forward of unabsorbed relief in respect of the above three assessees resulted in a total excess carry forward of Rs. 36.80 lakhs involving a potential tax effect of Rs. 14.65 lakhs.

4.13 Incorrect computation of business income of a co-operative society

In the assessment of a co-operative society in Haryana circle for the assessment years 1987-88 and 1988-89, assessments completed in March 1989 and December 1988, inadmissible items of expenditure aggregating to Rs. 1.51 lakhs and Rs. 13.36 lakhs representing expenditure of capital nature, personal expenses, expenditure on the maintenance of guest house and expenditure of earlier years, debited by the assessee to the profit and loss account of the previous year relevant to the assessment year 1987-88 and 1988-89 was not disallowed. Failure to add back such inadmissible expenditure resulted in over assessment and carry forward of loss to the extent of Rs.1.51 lakhs for the assesment year 1987-88 and under assessment to the extent of Rs. 13.36 lakhs for the assessment year 1988-89 leading to short demand of tax of Rs. 6.24 lakhs in the assessment year 1988-89 after adjusting previous losses against previous losses against the positive income.

4.14 Mistake in the computation of business income

With the omission of the provisions of Section 80V of Income-tax Act,

1961 with effect from 1 April 1986 by the Finance Act, 1986 regarding deduction of interest on moneys borrowed for the payment of income-tax, no deduction is admissible for and from the assessment year 1986-87 in respect of payment of such interest.

In Madhya Pradesh circle two Hindu undivided family assessees, claimed deductions towards interest on money borrowed for payments of income-tax of Rs. 2.27 lakhs in respect of the assessment year 1988-89 in one case and Rs. 32,456 in respect of the assessment year 1987-88 in the other case, which were allowed in the assessment made by the assessing officer in March 1989. The deduction,was, however, not admissible from the assessment year 1986-87 and onwards. The incorrect allowance of deduction resulted in short levy of tax of Rs. 1.65 lakhs in two cases (including interest of Rs. 18,003 for default in payment of advance tax in the first case).

Chapter 5

Other Direct Taxes

22 major obserations noticed in the audit of other direct taxes involving tax effect of Rs.45.32 lakhs were sent to Ministry of Finance for comments during January 1990 to July 1990. Some important cases are given below:

5.01 During the test-audit of the assessments made in a summary manner under the Wealth-tax Act, 1957, Gift-tax Act, 1958 and the Estate Duty Act, 1953, conducted during the period 1 April 1989 to 31 March 1990, the following types of mistakes were noticed:

Nature of irregularity	No. of Cases	Tax effect (Rs.in lakhs)
Wealth-tax		
(a) Wealth escaping assessment	65	6.51
(b) Incorrect valuation and computation of wealth	37	5.93
(c) Irregular or excess exemptions and deductions	32	1.26
(d) Other irregularities	37	2.74
Total	**171**	**16.44**
Gift-tax		
(a) Gift escaping assessment	3	5.11
(b) Incorrect valuation and computation of wealth	2	0.13
(c) Other irregularities	2	0.12
Total	**7**	**5.36**
Estate Duty		
(a) Incorrect valuation and computation of wealth	1	0.61
(b) Other irregularities	4	0.49
Total	**5**	**1.10**

(Excludes the figures of Delhi charges)

A. Wealth-tax

5.02 Wealth escaping assessment

The value of tax payer's right to receive an annuity purchased by him or purchased by another person in pursuance of a contract with the tax payer, will be reckoned as his asset irrespective of whether the annuity is commutable or not.

In the wealth-tax assessments of an individual in Maharashtra circle for the assessment years 1984-85 and 1985-86 completed in January 1989, compulsory deposits amounting to Rs. 1.73 lakhs and annuity policies valued at Rs. 28.12 lakhs for assessment year 1984-85 were not included in net wealth treating them as exempt. Similarly compulsory deposit amounting to Rs. 1.93 lakhs and annuity policies valued at Rs. 36.17 lakhs for the assessment year 1985-86 were also not included in net wealth for the same reason. These mistakes resulted in under assessment of wealth of Rs. 29.85 lakhs and Rs. 38.10 lakhs for the assessment years 1984-85 and 1985-86 respectively and an aggregate short levy of tax of Rs.3.24 lakhs.

5.03 Incorrect valuation and computation of wealth

1. Under the Wealth-tax Act 1957, the value of any property 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 relevant valuation date.

In Tamil Nadu circle, in the wealth-tax assessments of a Hindu undivided family of a specified category for the assessment years 1982-83, 1983-84 and 1984-85 completed in March 1986, the value of assessee's 1/3rd share of a building property was assessed at Rs. 35,000 for each year as returned by the assessee. For the assessment years 1985-86 and 1986-87, the assessee's share in the property was assessed in the assessments completed in March 1989 at Rs. 9 lakhs and Rs.12 lakhs respectively as against the value returned, viz., Rs.4.54 lakhs and Rs. 4.21 lakhs on the basis of the sale consideration of the property effected in January 1989. However, for assessment year 1987-88 the value of Rs. 4.21 lakhs returned by the assessee was accepted as such in the assessment completed in March 1989. Audit scrutiny (December 1989) revealed that the property was sold for a sum of Rs.63 lakhs in January 1989, the assessee's 1/3rd share being Rs.21 lakhs. Considering this actual sale value of the property, the value adopted on the valuation dates relevant to assessment years 1982-83 to 1987-88 was very much lower indicating gross under valuation. Assuming a ten percent deduction in the value of the property on the successive valuation dates relevant to the assessment years 1987-88 to 1982-83 there was an under assessment in the assessee's 1/3rd share of the property by Rs. 12.79 lakhs, Rs. 3.30 lakhs,Rs.4.78 lakhs, Rs. 12.05 lakhs, Rs. 10.81 lakhs and Rs.9.69 lakhs for the assessment years 1987-88 to 1982-83 respectively involving an aggregate short levy of tax of Rs.1.69 lakhs.

2. (i) Under the Wealth-tax Act, 1957, the value of a house property belonging to an assessee and exclusively used by him for his residential purposes throughout the period of twelve months immediately preceding the valuation date may at the option of the assessee be taken to be the price which it would fetch if sold in the open market on the valuation date relevant to the assessment year commencing on the 1 April 1971, whichever valuation date is later.

In Tamil Nadu circle, an individual owning a house property measuring 8 grounds and 1,051 sq. ft. in the heart of a metropolitan city returned the value of the property at Rs. 2.22 lakhs for assessment years 1980-81 to 1982-83 and at Rs. 1.90 lakhs for assessment years 1983-84 to 1985-86, which was accepted by the department. As the built-up area of the house was only 25 per cent of the total extent of land, the Commissioner of Income-tax in his orders of March 1987 for the assessment years 1980-81 and 1981-82 held that the freezing of value under the provisions of Wealth-tax Act, 1957, could be availed of only in respect of the residential house and not in respect of vacant land adjoining the house which is prejudicial to the interests of revenue and set aside the assessments for these two years directing the assessing officer to redo the assessments. In the revised assessments for assessment years 1980-81 and 1981-82 completed in March 1989, the assessing officer adopted the value of the property on the basis of its sale value of Rs. 20 lakhs in 1984. However, the department failed to reopen the assessments for assessment years 1982-83 to 1985-86 completed between December 1986 and October 1987 to consider this enhanced value. Assuming a normal rate of appreciation of 10 percent in the value of the property each year the value to be adopted for the assessment years 1982-83 to 1985-86 worked out to Rs. 14.58 lakhs, Rs.16.20 lakhs, Rs. 18 lakhs and Rs. 20 lakhs as against the value of Rs. 2.22 lakhs adopted for assessment year 1982-83 and Rs. 1.90 lakhs for assessment years 1983-84 to 1985-86 as returned by the assessee. Omission to adopt the enhanced value resulted in an aggregate under assessment of wealth of Rs.60.86 lakhs for assessment years 1982-83 to 1985-86 involving a short levy of wealth-tax of Rs. 1.61 lakhs.

(ii) In Karnataka circle two private discretionary trusts and an individual were among others, partners in a partnership firm, each holding one eighth share of interest in the firm. While completing the assessments of the individual, for the assessment years 1980-81 to 1984-85 between March 1985 and February 1989 under the scrutiny assessment procedure, the assessing officer rejected the value of the share of interest in the firm returned by the assessee and revised it upwards for all the years, taking into account the market value of certain assets and adopting the method of valuation of interest as prescribed in the Wealth-tax Rules. However, the assessments of the two trusts for the assessment years 1980-81 to 1984-85 were completed in the same wards/circle between September 1987 and March 1989 under summary assessment scheme accepting the returned wealth, including the values of one-eighth share of interest in the firm (which were the same as those returned by the individual also) for these years. The non-adoption of the market value of the assets for computing the share interest as adopted by the department in the case of the individual resulted in under-valuation of wealth aggregating to Rs. 42.07 lakhs involving an aggregate short levy of tax of Rs. 1.22 lakhs.

3. The Wealth-tax Rules, 1957, provide that where the market value of any asset exceeds its book value by more than twenty percent, the market value is to be substituted for the book value in such valuation. It has been judicially held * that income capitalization method

* 101 ITR 621 - R.V. Govindarajulu & Others V. C.I.T. Mysore

is ideally suited for estimating the market value of commercial properties.

In West Bengal cirlce, an individual was a partner of a firm having one-seventh share during the assessment years 1980-81 and 1981-82 and 11 percent share during the assessment years 1982-83 to 1984-85. The income-tax assessment records of the firm for the assessment years 1980-81 to 1984-85 showed that the firm had four godowns which yielded net maintainable rent of Rs. 8.28 lakhs, Rs. 9.21 lakhs, Rs. 9.91 lakhs, Rs. 9.23 lakhs and Rs. 8.32 lakhs respectively. Fair market value of the godowns would work out to Rs. 82.79 lakhs, Rs. 92.09 lakhs, Rs. 99.07 lakhs, Rs.92.27 lakhs and Rs. 83.19 lakhs following income capitalization method by adopting the multiplier of 10 of the net maintainable rent. The book value of the godowns was Rs.5.76 lakhs, Rs. 6.12 lakhs, Rs. 6.37 lakhs, Rs. 6.37 lakhs and Rs. 6.37 lakhs in the assessment years 1980-81 to 1984-85 respectively which were adopted for wealth-tax assessment. As the market value exceeded the book value by more than twenty percent, the Wealth-tax Officer ought to have adopted the market value of the godowns of the firm instead of their book value in calculating share interest in the firm of the assessee partner for the purpose of wealth-tax assessment. The omission to do so resulted in aggregate under assessment of wealth of Rs. 52.88 lakhs (including excess allowance of exemption of Rs. 1.50 lakhs in the assessment year 1982-83) and short levy of wealth-tax of Rs. 1.24 lakhs for five assessments of the assessee.

5.04 Other irregularities

In Karnataka circle, the assessment of a Hindu undivided family for the assessment years 1987-88 and 1988-89 were concluded by the assessing officer determining the net wealth at Rs. 13.62 lakhs and Rs. 18.16 lakhs respectively, on which tax was levied, at the lower rate applicable to ordinary Hindu undivided families,instead of at the higher rate application to Hindu undivided families which had a member having taxable wealth as on the valuation dates relevant to both the assessment years. The incorrect application of rate of tax resulted in short levy of tax of Rs. 43,956.

B Gift-tax

5.05 Gift escaping assessment

In Tamil Nadu circle, the income-tax assessment records of an individual for the assessment year 1987-88, disclosed that during the previous year relevant to the assessment year 1987-88, the assessee and his daughter had sold a house property in which they were having 50 percent share each for a consideration of Rs. 56 lakhs. The property consisted of land measuring 28 grounds and a building with a built up area of 900 sq. metres. A scrutiny of income-tax records of another individual (assessed in the same ward) revealed that a house property adjoining the above property and having a land of about 9 grounds and a building with a built up area of 4,165 sq. ft. was acquired by the 'appropriate authority' of the department in February 1987 for a consideration of Rs. 50 lakhs. On the basis of this sale which represented the market value of properties in the adjoining area in the previous year relevant to the assessment year 1987-88 the market value of the property sold by the assessee worked out to Rs. 1.50 crores. As the sale consideration received was far below the market price, the difference between the market price and the sale consideration amounting to Rs. 94 lakhs should have

been brought to tax as deemed gift in the hands of the two assessees at Rs. 47 lakhs each. The omission resulted in non-levy of gift-tax aggregating to Rs. 28.08 lakhs.

C Estate Duty

5.06 Estate escaping assessment

The Estate Duty Act, 1953 provides for levy of estate duty on the principal value of the estate that passes or is deemed to pass on the date of death of a person.

In Maharashtra circle, in the case of a person who died in May 1982, the assessment was completed in December 1987 determining the principal value of the estate as Rs.6.26 lakhs. It was seen that out of the sundry loans of Rs. 7.58 lakhs owing to the deceased on the date of death an amount of Rs. 3.79 lakhs only was assessed to estate duty. The omission resulted in the estate of Rs. 3.79 lakhs escaping assessment leading to short levy of estate duty of Rs. 1.14 lakhs.

5.07 Incorrect grant of relief/deduction

Under the provisions of the Estate Duty Act, 1953, the allowance of debt and liabilities against the principal value of estate is limited to those for which the deceased was liable at the time of death and any liability accruing after the death of the deceased on account of any default by accountable person is not an admissible deduction.

In Karnataka circle in the estate duty assessment of an Ex-ruler who died in August 1980 completed in March 1988, the claim for exemption of entire cost of the official residence of the deceased was allowed. In addition to this, a deduction of Rs. one lakh claimed by the accountable person was also allowed on the same property. As the exemption for the value of building was allowed in full, further deduction of Rs. one lakh allowed resulted in under assessment of estate by Rs. one lakh with consequent short levy of duty of Rs. 30,000.

T.S Madhavan

(T.SETHUMADHAVAN)
Principal Director of Receipt Audit
(Direct Taxes)

New Delhi
The 6 MAY 1991

Countersigned

(C.G.SOMIAH)
Comptroller & Auditor General of India

New Delhi
The 6 MAY 1991

G.N. GUPTA
CHAIRMAN

D.O.F.No.17/1/88-OD-I
Central Board of Direct Taxes,
New Delhi.
Dated the 28th Sept., 88

My dear Chief Commissioner

Action Plan for 1988-89

This is in continuation of my D.O. letter F.No. DIR(Hqrs)/CH(DT)/88-89 dated 1.6.1988 on the subject.

2. I am enclosing the detailed Action Plan for the year 1988-89. As you are aware material changes have been made in the methodology of work which was being followed for the last 15 years or so. Of the total workload of pending assessments, only a part of search and seizure assessments would be carried over to the year 1989-90. All the remaining assessments would be finalised during the year 1988-89.

3. The salient features of the Action Plan relating management of I.T. assessments are as follows:

i. Practical shape has been given to the concept of MBO in as much as the filed formations have been given in the liberty to increase or decerease their workload of scrutiny assessments in accordance with the manpower resources available with them. They are required to scrutinise only as many case as the working capatiy of the available manpower permits. The result of the cases can be disposed of summarily u/s 143(1).

ii. The Summary Assessment Scheme has been extrended to all income groups irrespective of the size of income or loss reported by the tax payer.

iii. In every income group, a small percentage of cases would be subjected to scrutiny as follows:

Category of Asstts.	All India Target of scrutiny
Category 'A' Assessments	2%
Category 'B' Assessments	16%
Category 'C' Assessments	28%
Category 'D' Assessments	50%
Overall	3%

These percentages are, however, based on the consolidated figures of workload and available manpower on all India basis.

iv. The scheme of job classification has been built into the Action Plan in as much as non-company cases below Rs.2 lakhs and company cases below Rs.50,000 shall be assessed by ITOs. The remaining cases shall be assessed by ACs and DCs (Asstt.).

4. As a result of the extension of summary assessment to all levels of income in the Action Plan for 1988-89 the percentage of overall scrutiny is likely to fall this year as compared to earlier years. This fact underlines the need for improving the quality of assessment work. I mayemphasise that in order to promote voluntary compliance with tax laws, we have to make quality assessments detect concealments, impose penalties and launch prosecutions successfully. Unless this happens, there is every likelihood of the liberalised assessment scheme being misused by the unscrupulous taxpyers. Administrative Commissioners in your region should be advised to ensure that cases selected for scrutiny have a real potential for detection of concealment and launching of prosecution.

5. You are already aware of the targets in regard to the quantum of entries of carried forward I.T. demand. It may be mentioned that the target of 10% reduction in the total quantum of arrears to be carried forward as on 1.4.1989 defies monthly or quarterly monitoring. Under the circumstances you may advise the Commissioners in your region to set monthly or quarterly targets of reduction in arrear and current demands, and monitor them regularly so that the end result of 10% reduction in quantum and 30% reduction in number of entries of the total carried forward I.T. demand is achieved.

6. An abstract of the consolidated Action Plan in respect of your region, as approved, may be seen at Annexure-II. The Central Action Plan is limited to only a few key result areas. You have to manage other important areas of work at your own level.

7. I would also like to draw your attention to the "Operational Instructions (Annexure-III). This contains the details of the new Assessment Scheme, as also the norms of disposal for Assessing Officers. The procedure to be followed for selecting scrutiny assessments has also been set out.

8. As a result of modifications in the Action Plan, consequential changes have been made in the CAP-ONE, CAP-TWO and Quarterly Statements. Columns relating to expected workload in various categories have been deleted from the monthly telegraphic report (CAP-TWO). However, this information would continue to be called for in the quarterly statement (Annexure-IV). Kindly ensure that all statements in the revised formats reach us well before the due dates.

9. Before I close, I may re-emphasise that the success or otherwise of this year's Action Plan depends entire on your initiative and management capacity. Amongst other things the objective of achieving a proper level of deterrence has a prior claim on your attention. Unless we succeed on this front, the liberal policy of the Government as regards the new assessment procedures is liable to be misused by unscrupulous tax payers. It is, therefore, important that the crusade against tax evasion is carried out with some "effect".

Yours sincerely,

Sd/-
(G.N. GUPTA)

All Chief Commissioners

D.O.F.No.DIR(HQRS)/CH(DT)/88-89/334-61

G.N. GUPTA
Member (IT)

GOVERNMENT OF INDIA
MINISTRY OF FINANCE
DEPARTMENT OF REVENUE
CENTRAL BOARD OF DIRECT TAXES,

New Delhi, the 1.06.88

My dear

Sub: Action Plan for 1988-89.

Please refer to the minutes of the Regional Conference at Bombay circulated by letter No. CC(A)/Conf/87-88 dated 12.4.1988 from IAC(Hqqrs.), Bombay and my D.O. letter No. 1866/M(IT)/Action Plan dated 21.4.1988 containing the principles for the formulation of Action Plan for 1988-89 already decided by the Board. The above letters should be read with Chairman's D.O. letter No. Dir(Hqrs.)/CH(DT)/88-89 dated 15.4.1988 on re-organisation of the Income-tax Department defining the jurisdiction of the different categories of the assessing officers.

II. Inspite of the above clear guidelines, various doubts have been raised by CCs/CsIT about the formulaation of the Action Plan. In some cases, the CCs and CITs have even sent new suggestions regarding formulation of the Action Plan and the jurisdiction of the different categories of assessing officers.

III. In order to set at rest all such queries, I am elaborating the principles of the Action Plan for 1988-89 as under:

(i) The juriscition of the different categories of assessing officers have been defined in Chairman's D.O. letter No. Dir(Hqrs)/CH(DT)/88-89 dated 15.4.1988 to all CCs/DsG. Those guidelines are to be followed strictly. The re-organisation of the Department should be completed accordingly if not already done. The early completion of this exercise shall enable you to achieve your Action Plan targets of assessments.

(ii) Assessments (a) Scrutiny assessments

Every assessing officers shall complete the following minimum number of scrutiny assessments in a year:

(i)	Dy. Commissioner (Asstt.)		
	Without any ITO	-	35 core assessments
	With one ITO	-	60 core assessments
	With two ITOs	-	75 core assessments

[In Bombay we are even contemplating to have one Assistant Commissioner and two ITOs under a Deputy Commissioner (Asstt). to increase the number of scrutiny cases].

When one or two Asstt. Commissioners are provided in place of ITOs, the quota may be raised to 100 to 120.

(ii)	Assistant Commissioner	-	150 assessments
(iii)	ITO	-	100 assessments.

Thus cases shall be selected for scrutiny out of all income groups. Out of all cases with him each assessing officer shall select as many cases for scrutiny as per his capacity according to the above norms and complete the rest in a summary manner. Therefore, the total number of cases selected for scrutiny shall depend on the number of assessing officers in a charge.

Accordingly the commissioner shall fix his target of scrutiny assessments to be completed during the year.

(b) Summary Assessments

Assessment of cases with each assessing officer other than those selected for scrutiny shall be completed in a summary manner by him.

Action Plan for summary assessment is 100% of all cases. The target for each ITO should be between 4500 to 6000 summary assessments depending on the requirement of the charge, and stage of computerisation.

(Note: Wherever computers have been installed, steps shoudl be taken to use them for completing summary assessments).

The workload should be evenly distributed so that the action plan targets are met both in summary and scrutiny assessments.

Your individual draft Action Plans in the area of assessments shall be moderated by the Board and the DOMS, and intimated to you. But you should start working in the above lines without waiting for the approved Action Plan.

(c) Selection of cases

Selection of cases for scrutiny should be made according to the following criteria. The list, however, is illustrative and not exhaustive.

(1) The concept of F, for example low decline in gross profit to turnover ratio.

(2) Adverse points in the past history of the case.

(3) Specific outside information; *e.g.*

i. complaints.
ii. local enquiries.
iii. Survey u/s 133A or cases having potential for such surveys.

Dy. Directors (Inv) will also assist the commissioners in selection of such cases so as to take the cases of some of the new assessees added in 1987-88.

(4) The existence of qualifications in the Auditor's Report including compulsory Tax Audit Report u/s 44AB.

(5) Industries/Trades making abnormal profits in the accounting year.

(6) Inadequate incomes declared in the past as compared to wealth.

(7) Claims of obvious inadmissible deductions or exemptions or exempted income *e.g.* agricultural income.

(8) Large scale investments or increase in assets or increases in loan liabilities.

(9) Expansion in cases belonging to one group.

(10) Low withdrawal for house-hold expenses.

(11) Personal knowledge.

(12) Inordinate delay in filing of return, *e.g.*, where the return is furnished after the expiry of the relevant assessment year.

(13) Arrear assessments where investigation so far conducted indicate possibility of establishing concealment.

(Note:The reasons for identifying a case for scrutiny should be recorded in writing).

Cases selected for scrutiny by the ITO and Assistant Commissioner shall be approved by the Deputy Commissioner and those selected for scrutiny by the Deputy Commissioner (Asstt) shall be approved by the C.I.T. C.I.T. and Deputy Commissioner may for this purpose consult the Investigation Wing wherever necessary.

(d) Search and Seizure Assessments

Each Assistant Commissioner in charge of Search & Seizure Cases (INvestigation Circle) must complete at least 50 assessments during the year subject to the overall condition that assessments of all cases where search were conducted before 31.3.1987 must be completed by 31.3.1989.

The object should be that by 31.3.1989, the Department should have a clean slate so far as assessments except search and seizure assessments are concerned (Does not apply to central circles).

(iii) Collection of Demand

(1) Demand carried forward as on 1.4.1989 should be 10% less than the demand carried forward as on 1.4.1988.

(2) Number of entries carried forward as on 1.4.89 should be not more than 70% of entries carried forward as on 1.4.88.

IV. I shall like to clarify that the Board has already taken the above decisions about re-organisation of the Department, job classification and formulation of the Action Plan for 1988-89. Therefore, the CCs, CsIT need not send their own suggestions about modifications of the above ppolicy decisions. They are requested to implement those decisions forthwith. However, genuine difficulties if any faced in implementing these decisions which cannot be clarified by the guidelines may be sent for guidance by the Board.

V. With a view to scrutinise the maximum number of cases having income/loss of Rs.5 lakh and above, the DC(Asst) should be provided with 2 ITOs. Wherever Asst. Commissioners are available after filling up all the circles in the charge one or both the ITOs may be replaced by Asst. Commissioners.

I must emphasise three specific features of the Action Plan of 1988-89(i) the number of cases to be scrutinised is dependent on the manpower and the norms of disposal indicated above (ii) the selection of cases for scrutiny is left to the field officers (iii) the areas of Action Plan have been drastically curtailed. Therefore, no excuse whatsoever shall be accepted for failure to meet the targets and the concerned assessing officers and the supervisory officers should, therefore, ensure that the targets are reached. Similarly since the selection of cases for scrutiny is left to the field officers the Board, no doubt, expect that the assessing officers would be able to make effective and deterrent assessments establishing concealments leading to prosecution in those cases selected for their concealment potential.

Yours sincerely,

Sd/-
(G.N. GUPTA)

To all Chief Commissioners/
Directors General

Copy to:

1. All Members of the Board
2. DOMS

Sd/- (G.N. GUPTA)

CENTRAL ACTION PLANT FOR 1988-89

S.No.	Key Result Area	Target
I.	DISPOSAL OF I.T. ASSESSMENTS	
a.	Category 'A' Assessments	
	Company assessments with income/loss below Rs.50,000 and	i. Dispose of @ 100 assessments per Income-tax Officer u/s 143(3)
	Non-company assessments with income/loss below Rs.2 lakhs	ii. Dispose of the remaining workload u/s 143(1).
b.	Category 'B' Assessments-	
	Company assessment with income/loss of Rs.50,000 and above but below Rs.5 lakhs; and	i. Dispose of @150 assessments per annum per Assistant Commissioner of Income-tax u/s 143(3)
	Non-company assessments with income/loss of Rs.2 lakhs and above but below Rs.5 lakhs.	ii. Dispose of the remaining workload u/s 143(1).
c.	Category 'C' Assessments-	
	All assessments with income/ loss of Rs.5 lakhs and above	i. Dispose of u/s 143(3) selected assessments per Deputy Commis sioner (Asstt.) according to following norms: 35 core asstt. -without any ITO 60 core asstts. -with one ITO 75 core asstts. -with two ITOs ii. Dispose of the remaining workload u/s 143(1).
d.	Category 'D' Assessments	
	Search & Seizuure Assessments	Dispose 100% of the assessments related to searches conductedup to 31.3.1987. Minimum norm is

50 asstts. per annum per Assistant Commissioner.

II. DEMAND AND COLLECTION

i.	I.T. Demand (Arrear and Current)	Total arrear demand to be carried forward as on 1.4.89 out of both Arrear and Current demand should not exceed 90% of the total arrear demand brought forward on 1.4.1988.
ii.	Number of entries of I.T. Demand (Arrear & current)	Number of entries of total arrear demand carried forward on 1.4.89 should be less than 70% of such entries as on 1.4.88.

QUARTERLY TARGETS
(in terms of %age of Annual Workload)

	Upto end of IInd qtr.	Upto end of IIrd qtr.	Upto end IVth qtr.
I. I.T. ASSESSMENTS			
Categories A,B,C & D Assessments	30%	75%	100%

ANNEXURE-II

DISPOSAL OF I.T. ASSESSMENTS — **ACTION PLAN FOR 1988-89 - C.C. (TECH.), BOMBAY**

Category of assessments	Anticipated workload for 1988-89	No. of cases proposed to be disposed of U/s 143(3)	U/s 143(1)	Total	Proposed deployment of Assessing officers ITOs	ACs	DC(Astt)	Norms proposed by DOMS/CBDT U/s 143(3)	U/s 143(1)	Planned disposal as per Action Plan submitted by CC U/s 143(3)	U/s 143(1)
A.i. Non-company Asstts. below Rs.2 lakhs	5,64,082	8,900 (1.58%)	5,55,182 (99.42%)	5,64,082 (100%)	89	-	-	100	4600-6000	100	6238
ii. Company assts. below Rs.50,000											
B. Asstts. with income below Rs.5 lakhs											
i. Non-company asstts. with income/loss from Rs.2 to 5 lakhs	12,639	3,310 (26.19%)	9,339 (73.81%)	12,639 (100%)	-	22	-	150	-	450	-
ii. Company asstts. with income/loss from Rs.50,000 to 5 lakhs.											
C. Asstts. with income of Rs.5 lakhs and above	3,780	900 (23.81%)	2,848 (76.19%)	3,768 (100%)	24	-	12	35 without ITO 60 with 1 ITO 75 with 2 ITOs	-	75	-
D. Search and Seizure Assts.	1,217	608 (49.96)	-	608 (49.96%)	-	11	-	50	-	55	-
Total	5,81,718	13,708 (2.36	5,67,401 (97.53%)	5,81,109 (99.89%)	113	33	12				

DEMAND & COLLECTION:REDUCTION IN I.T. DEMAND AND NUMBER OF ENTRIES OF I.T. DEMAND AS PER ANNEXURE - I

ANNEXURE - III

OPERATIONAL INSTRUCTIONS

A Deployment of Officers

1. ITOs shall be deployed on the following type of assessment work (Category A asstts):

   i. Non-company assessments with returnd income/loss below Rs.2 lakhs; and

   ii. company assessments with returned income/loss below Rs.50,000.

2. Assistant Commissioners shall be deployed on the following type of assessment work (Category B asstts.)

   i. Non-company assessments with returned income/loss of Rs.2,00,000 - 4.99.999 and

   ii. Company assessments with returned income/loss of Rs.50,000 - 4,99,999.

3. Deputy Commissioners (Asstt.) shall be deployed on cases with returned income/loss of Rs.5 lakhs and above (Category C asstts.).

4. Assistant Commissioners shall be deployed on search & seizures assessment (Category 'D' assessments).

B. Jurisdiction

1. The different classes of assessing officers mentioned in Para A above shall exercise jurisdiction over cases with income limits specified above (Para A).

2. The returned income/loss referred to above is:

   i. When the assessmenof one or more years is pending on 1st April, the highest of the returned incomes of these years

   ii. When no assessment is pending on 1st April the retunred income of the latest assessment year for which assessment has been made.

3. Where no return has been filed by an assessee for any assessment year, the jurisdiction shall ordinarily vest in the Asstt. Commssioner unless the same has been vested in the ITO by the Chief Commissioner/Commissioner.

C. Assessment Scheme

1. The Central Circles shall continue to function without any change.

2. Assessing Officers deployed on Search & Seizure assessments shall continue disposing 50 cases per annum per Assessing Officer.

However, all cases relating to searches conducted upto 31.3.1987 have to be disposed of by 31.3.89.

3. The norms for scrutiny cases for different levels of officers are as follows:

a)	DCs (Assessment)	35 core assessments without any ITO 60 core asstts. with one ITO 75 core asstts. with two ITOs
b)	Assistant Commissioners	150 assessments
c)	I.T.Os	100 assessments

4. When one/two Assistant Commissioners are provided in place of ITOs to asst DCs(Asstt.) the quota of disposal may abe raised to 100/120 core assessments.

5. Cases shall be selected for scrutiny out of all income groups. The number of cases to be selected shall depend on the number of assessing officers available in a charge and their working capacity according to the above norms

6. The number of scrutiny assessments to be completed by the Assessing Officers shall be limited to the norms specified in Para-3 above.

The rest of the cases in the jurisdiction of each of the Assessing Officers shall be disposed of u/s 143(1) irrespective of the status or income group of the assessees.

This applies to all the Assessing Officers except those posted in Central circles and Search & Seizure Circles.

7. The randome sample scheme shall be discontinued w.e.f. the financial year 1988-89.

D. Selection of Scrutiny Cases

1. The assessments shall be picked up for scrutiny on the basis of error/evasion/concealment potential.

2. The criteria for selection of scrutiny assessments would include the following:

i. Low gross profit/decline in gross profit in relation to turn-over.

ii. Adverse points in the past history of the case.

iii. Specific outside information *e.g.*

a. Complaints
b. Local enquiries
c. Surveys u/s 133A or cases having potential for such surveys

iv. Existence of qualifications in the Auditors' Report including Compulsory Tax Audit Report u/s 44AB.

v. Industries/Trades making abnormal profits in the accounting year.

vi. Inadequate incomes declared in the past as compared to wealth.

vii. Claims of obvious inadmissible deductions or exemptions or exempted income *e.g.* agricultural income.

viii. Large scale investments or increase in assets or increase in loan liabilities.

ix. Expansion in cases belonging to one group.

x. Low wirhdrawals for household expenses.

xi. Personal knowledge (reduced to writing by the assessing authority).

xii. Inordinate delay in filing the return.

xiii. Assessments where notices u/s 147 or 139(2) have been issued.

xiv. Arrear assessments where investigation so far conducted indicates possibility of establishing concealment.

xv. Cases where the size of the turnover is suspsect with reference to the available working capital.

This creteria (for selection listed above) is only illustrative and not exhaustive.

3. The scrutiny assessments may be selected either out of the current assessments for the year 1988-89 or arrear assessments brought forward on 1.4.1988.

4. The assessments picked up for scrutiny by the ACs and ITOs shall be approved in advance by the Range DC.

5. The assessments picked up for scrutiny by the DC(Asstt.) shall be approved by the CIT.

6. The selection of assessments for scrutiny shall be done in consultation with the Intelligence Wing.

7. The reasons for identifying a case for scrutiny should be recorded in writing.

8. It may be emphasised one again that an assessing officer should not normally be asked to complete assessments in excess of the norms. In case, the pendency increases through re-opened tax evasion cases or b/f cases already under investigation, the number of other scrutiny cases should be reduced accordingly. Failure to implement this policy would undoubtedly be at the cost of quality of assessment.