REPORT OF THE COMPTROLLER AND AUDITOR GENERAL OF INDIA

FOR THE YEAR ENDED 31 MARCH 1994
NO. 5 OF 1995

UNION GOVERNMENT
(REVENUE RECEIPTS - DIRECT TAXES)

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PREFATORY REMARKS

This Report for the year ended 31 March 1994 has been prepared for submission to the President under Article 151(1)of the Constitution of India.

The Audit of Revenue Receipts— Direct Taxes of the Union Government is conducted under Section 16 of the Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971. This Report presents the results of audit of receipts under direct taxes comprising income tax, wealth tax and gift tax. The Report is arranged in the following order:-

(i) Chapter 1 includes information on the arrangements for audit of direct taxes and mentions the results thereof;

(ii) Chapter 2 incorporates important statistical information on the administration of direct taxes;

(iii) Chapter 3 includes three system appraisals on 'Survey operations under the Income Tax Act, 1961', 'Administration of tax deduction account number' and 'Double taxation avoidance agreements and relief';

(iv) Chapters 4 and 5 mention the issues resulting from the audit of corporation tax and income tax respectively;

(v) Chapter 6 highlights the results of the audit of wealth tax and gift tax.

The observations mentioned in this Report are among those which came to notice during the course of test audit during 1993-94 as well as those which came to notice in earlier years but could not be covered in the previous Reports.

OVERVIEW

1. This Report of the Comptroller and Auditor General of India presents the important results of test audit of assessments relating to direct taxes. The report features 210 paras bringing out audit observations involving a revenue effect of Rs.129.98 crores. Three systems appraisals are also featured in this Report.

2. Of the cases featured in this Report, 163 cases involving revenue of Rs.80.33 crores have been accepted by the Ministry and remedial measures have been initiated. Further, 29 cases which have been accepted by the Ministry and in which remedial action has also been completed, have not been included in this Report. The tax effect involved is Rs.304.52 lakhs. Similarly 24 other cases with potential tax effect of Rs.295.41 lakhs have also not been included in this Report as the audit observations have been accepted by the Ministry and rectificatory action has also been completed.

3. The cases featured in this Report have been selected out of 14,575 audit observations involving underassessment of tax of Rs. 595.76 crores which were intimated to the department during the course of test audit conducted in 1993-94. Some cases noticed in earlier years have also been featured. In 1943 cases out of these, the underassessment of Rs.134.62 crores has been accepted by the department.

4. An analysis of the trend of receipts reveals an increase in gross receipts from direct taxes during 1993-94 over the previous year. The actual collection for the year was Rs. 20,298.24 crores (against the budget estimates of Rs. 21,260 crores) representing 12.16 percent increase over the previous year's collection of Rs. 18,097.29 crores. There was an increase in the number of assessees as well, which rose from 93.07* lakhs to 95.76 lakhs, an increase of about 2.9 percent compared to last year.

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* Provisionally reported at 83.62 lakhs by the Ministry and printed as such in the Audit Report 1992-93.

5. The expenditure incurred on the collection of all direct taxes during the year 1993-94 was 1.65 percent of the total collection which was almost at the same level during the earlier year (1.63 percent). Gross pre-assessment collection of income tax and corporation tax during the year by way of tax deduction at source, advance tax and self-assessment tax, before adjustment of refunds was Rs.21469.62 crores (87.39 percent of the total collection). The cost of collection in respect of income tax and corporation tax alone as a percentage of post assessment collections of these taxes was 9.71 percent (against 14.02 percent in 1992-93).

6. Overall pendency of assessments increased to 15.41 lakhs cases as on 31 March 1994 (from 14.50 lakhs cases as on 31 March 1993). This happened even though the Board had issued directions for according priority to increasing the disposal of both summary and scrutiny assessments.

7. Arrears of tax have also shown an increasing trend. Cumulative arrears of corporation tax and income tax increased from Rs.9488.54 crores in 1992-93 to Rs.11365.33 crores during the period ending 31 March 1994. Of these, in 1099 cases alone, the arrears amounted to Rs.5865.06 crores with each of these cases having an arrear of more than Rs. one crore. Arrears continue to mount despite the directions of the Board for according priority to reduction of the arrear demands .

System appraisals

8. This Report also features the following system appraisals:

(a) Survey operations under the Income Tax Act, 1961,

(b) Administration of tax deduction account number,

(c) Double taxation avoidance agreements and relief.

The important audit observations on the above subjects are briefly mentioned below:

Survey operations under the Income Tax Act

(a) The Income Tax Act, 1961 empowers the departmental authorities to conduct surveys to detect new assessees as well as for detecting evasion by existing assessees. This is done by keeping a watch over the business environment, collecting material facts in respect of specific cases and monitoring ostentatious expenditure. Review in audit of the systems relating to survey operations revealed:

(i) 78 percent of the verified information collected by Central Information Branch which was entrusted with the responsibility of collecting information from external sources and disseminate the same, was not passed on to the assessing officers for suitable action.

(ii) Gains to revenue in tangible terms were nominal considering the large number of surveys undertaken (37.78 lakhs during the period 1989-90 to 1992-93).

(iii) Information collected from surveys was either not made use of, or the follow up in assessments was tardy.

(iv) Priority was not accorded to finalisation of even those cases where the survey reports indicated large tax evasion.

(v) Penal provisions were often not invoked defeating the objective of having a deterrent effect through their application. **[Para 3.1]**

Administration of Tax deduction Account Number

(b) For better monitoring of deduction of tax at source and its deposit in Government accounts, all persons responsible for deducting tax at source were required under the provisions of Income Tax Act, 1961 to obtain a tax deduction account number which shall be quoted on all challans, certificates and returns connected with tax deducted at source. A review in audit of the functioning of the scheme revealed:

(i) The department did not have complete record of persons responsible for deduction of tax at source to ensure that TAN was obtained in all cases.

(ii) Receipt of statutory returns from tax deducting agencies could not be ensured in 39 percent of the cases in 8 charges. Penal action in cases of delayed receipt of returns was also not found to have been taken in several cases.

(iii) There was lack of coordination between TAN allotting authorities and TDS authorities adversely affecting monitoring of tax deductions.

(iv) Percentage of check of TDS certificates with the records of TDS wards to verify the correctness of tax deducted at source was not found to have been prescribed except in a solitary case. **[Para 3.2]**

Double taxation avoidance agreements and relief

(c) Tax treaties are entered into by the Government of India with the government of a foreign country for granting relief in respect of income taxed under income tax laws of the two countries and for avoiding double taxation and exchange of information for prevention of tax evasion. The relief is also given under Income Tax Act, 1961 unilaterally where no such agreement exists. A test check of assessment records revealed the following:

(i) Application of incorrect rates of tax in 13 cases resulted in short levy of tax of Rs. 363.25 lakhs.

(ii) Mistakes in computation of taxable income and grant of relief in two cases led to short levy of tax of Rs. 1292.31 lakhs including potential tax of Rs. 1212.07 lakhs. **[Para 3.3]**

Corporation Tax

9(i) Avoidable mistakes like incorrect adoption of figures, double allowance of deductions, arithmetical mistakes, calculation errors and other mistakes continue to occur despite Board's instructions to ensure accuracy in the computation of income and tax. These mistakes in 18 cases led to undercharge of tax of Rs.1131.32 lakhs including potential tax effect of Rs.883.29 lakhs in 7 cases. **[Para 4.6]**

(ii) In Uttar Pradesh charge, tax on a closely held company was levied at 50 percent of the total income instead of the correct rate of 60 percent leading to short levy of tax of Rs. 18.65 lakhs. **[Para 4.7]**

(iii) In West Bengal charge, incorrect allowance of provisions for unascertained liabilities of bad debts and loss of stores and capital loss on sale of fixed assets led to underassessment of income of Rs. 2735.56 lakhs involving undercharge of tax of Rs. 1477.20 lakhs including potential tax effect of Rs. 1069.26 lakhs. **[Para 4.11(ii)]**

(iv) In Tamil Nadu charge, incorrect allowance of reserve for shipping business, there being no income after set off of carried forward losses, depreciation and investment allowance of the earlier years, resulted in excess carry forward of unabsorbed depreciation of Rs. 191.25 lakhs involving potential tax effect of Rs. 103.28 lakhs. **[Para 4.12]**

(v) In West Bengal charge, incorrect allowance of unpaid taxes and cess in the case of a public sector undertaking led to overassessment of loss by Rs.1608.99 lakhs involving potential tax effect of Rs.868.86 lakhs. **[Para 4.13(ii)]**

(vi) In West Bengal charge, incorrect deduction of bonus not actually paid to the employees resulted in underassessment of income of Rs.193 lakhs involving short levy of tax of Rs.121.59 lakhs. **[Para 4.13(v)]**

(vii) In Bihar charge, incorrect allowance of expenditure relating to earlier years led to excess computation of loss of Rs.494.37 lakhs involving potential tax effect of Rs.227.41 lakhs. **[Para 4.15(c)(i)]**

(viii) In Gujarat, Madhya Pradesh and Maharashtra charges, incorrect allowance of depreciation and investment allowance on erroneously enhanced cost of plant and machinery on account of intermediate fluctuations in the rate of exchange in 8 cases led to underassessment of income of Rs.309.38 lakhs involving short levy of tax of Rs.166.97 lakhs (including interest). **[Para 4.17]**

(ix) In Tamil Nadu charge, failure to reduce the written down value of plant and machinery consequent upon withdrawal of capitalised interest and commitment charges, led to excess determination of unabsorbed

depreciation by Rs.164.86 lakhs involving potential tax effect of Rs.89.03 lakhs. **[Para 4.18]**

(x) In Bihar and West Bengal charges, investment allowance was allowed at the rate of 25 percent of the cost of plant and machinery instead of the correct rate of 20 percent in three cases which led to under assessment of income by Rs.746.46 lakhs involving tax of Rs.415.95 lakhs (including potential tax effect of Rs.386.09 lakhs). **[Para 4.19(a)(i)]**

(xi) In West Bengal charge, incorrect increase of profits of the eligible business led to excess allowance of deduction for investment deposit account of Rs.110 lakhs involving short levy of tax and interest of Rs.102 lakhs. **[Para 4.20(a)(iii)]**

(xii) In Andhra Pradesh charge, failure to set off accumulated losses of two amalgamating companies led to erroneous deduction for investment deposit account amounting to Rs.135.85 lakhs in the case of an amalgamated company involving tax of Rs.88.03 lakhs (including potential tax effect of Rs.73.36 lakhs). **[Para 4.20 (d)]**

(xiii) In Delhi charge, non-inclusion of refund of excise duty not returned to the customers in the total income of a closely held company led to underassessment of income of Rs.92.45 lakhs involving short levy of tax of Rs.78.10 lakhs. **[Para 4.23(a)]**

(xiv) In Assam and West Bengal charges, non inclusion of accrued income from sale of power at increased rate of tariff, unexplained investments and encashment of suppliers' performance guarantee bonds in the total income in 7 cases led to under-assessment of income of Rs.1538.36 lakhs involving undercharge of tax and interest of Rs.1110.95 lakhs (including potential tax effect of Rs.806.14 lakhs). **[Para 4.23(b)]**

(xv) In Maharashtra charge, omission to include contract receipts deposited abroad led to underassessment of income of Rs.826.70 lakhs involving short levy of tax of Rs.439.83 lakhs. **[Para 4.23(c)(i)]**

(xvi) In Tamil Nadu charge, incorrect allowance of deduction from profits and gains of an industrial undertaking established after 31 March 1981 which was also engaged in trading activities resulted in under-assessment of income of Rs.61.35 lakhs

involving short levy of tax of Rs.51.74 lakhs. **[Para 4.28(a)]**

(xvii) In Tamil Nadu charge, incorrect allowance of relief in respect of export turnover resulted in underassessment of income of Rs.128.75 lakhs involving short levy of tax of Rs.92.10 lakhs. **[Para 4.29(a)(iii)]**

(xviii) In Tamil Nadu charge, the treatment of capital expenditure as revenue expenditure resulted in understatement of book profits by Rs.607.29 lakhs involving short levy of minimum tax leviable on certain companies amounting to Rs.161.37 lakhs. **[Para 4.32(b)]**

(xix) In Karnataka and Maharashtra charges, omission to add back certain provisions while computing book profits in 2 cases led to underassessment of income of Rs.358.33 lakhs involving short levy of minimum tax of Rs.276.27 lakhs. **[Para 4.32(c)]**

(xx) In Tamil Nadu charge, incorrect set off of unabsorbed depreciation and investment allowance of earlier years led to under-assessment of income of Rs.23.78 crores involving undercharge of minimum tax of Rs.17.73 crores. **[Para 4.32(e)]**

(xxi) In West Bengal charge, failure to take into account refund already granted, while making scrutiny assessment resulted in excess refund of Rs.73.74 lakhs. **[Para 4.33(i)]**

(xxii) In West Bengal charge, non-levy of interest on outstanding tax demand in a case amounted to Rs.11.83 lakhs. **[Para 4.35(ii)]**

(xxiii) In Gujarat charge, non levy of penalty for acceptance of security deposits in cash in a case amounted to Rs.70 lakhs. **[Para 4.37(ii)]**

(xxiv) In West Bengal charge, non-levy of additional tax for additions made in the returned income while processing the returns in two cases resulted in non-levy of additional tax of Rs.162.49 lakhs. **[Para 4.38(i)&(ii)]**

(xxv) In West Bengal charge, non completion of surtax assessment alongwith income tax assessment in a case involved tax effect of Rs.1116.04 lakhs. **[Para 4.39]**

Income Tax other than Corporation Tax

10. (i) Avoidable mistakes like calculation errors, adoption of incorrect figure and application of lower rate of tax in 11 cases led to undercharge of tax of Rs.90.62 lakhs (including potential tax of Rs.19.69 lakhs). **[Para 5.6 and 5.7]**

(ii) In Tamil Nadu charge, failure to invest sale consideration of an immovable property in specified assets within the prescribed time limit in one case led to incorrect exemption of capital gain of Rs.19.68 lakhs involving short levy of tax and interest amounting to Rs.20.41 lakhs. **[Para 5.11.1(i)]**

(iii) In Orissa charge, non adoption of sales figures determined by sales tax authorities in income tax assessments of two assessees resulted in underassessment of income aggregating Rs. 25.68 lakhs involving short levy of tax of Rs. 12.38 lakhs. **[Para 5.12.2]**

(iv) In Punjab charge, mistake in carry forward of loss resulted in excess carry forward of loss of Rs. 130.46 lakhs involving potential tax effect of Rs. 51.10 lakhs. **[Para 5.13(a)]**

(v) In Maharashtra charge, incorrect allowance of relief in respect of profits from export of granite stones led to underassessment of income of Rs.54.95 lakhs involving short levy of tax of Rs.35.42 lakhs. **[Para 5.14.1(a)]**

(vi) In Uttar Pradesh charge, incorrect exemption of property income of a cooperative society engaged in marketing of agricultural produce resulted in underassessment of income of Rs.23.13 lakhs with consequent undercharge of tax and interest of Rs.16.64 lakhs. **[Para 5.14.2]**

(vii) In Kerala and Tamil Nadu charges, non levy of interest on belated payment of tax demand in 5 cases resulted in short levy of tax of Rs.46.08 lakhs. **[Para 5.15.1]**

(viii) In West Bengal charge, non levy of interest for non payment of advance tax in a case amounted to Rs. 24.80 lakhs. **[Para 5.15.3(Sl.1)]**

Wealth Tax

11. (i) In Kerala charge, non-levy of wealth tax on immovable property worth Rs. 236.59 lakhs owned by a closely held company amounted to Rs.4.73 lakhs.

[Para 6.8.1(ii)]

(ii) In Tamil Nadu charge, omission to adopt market value of properties as determined by the department in 5 cases resulted in underassessment of wealth of Rs. 1157.01 lakhs involving short levy of tax of Rs. 22.69 lakhs. **[Para 6.8.2]**

Gift Tax

12. In Gujarat charge, non adoption of value of the gifted property determined by departmental valuation officer led to non assessment of deemed gift of Rs. 11 lakhs involving non levy of gift tax of Rs. 3.24 lakhs. **[Para 6.12(i)]**

Chapter 1

Introduction

General

1.1 The revenue from Direct Taxes during 1993-94 amounted to Rs. 20,298.24 crores. Time series data on the different components of the revenue from Direct Taxes and other statistical information on working of the tax administration machinery are given in Chapter 2 of this Report.

Statutory Audit

1.2 The audit of Direct Taxes by the Comptroller and Auditor General of India is carried out under Section 16 of the Comptroller and Auditor General of India (Duties, Powers and Conditions of Service) Act, 1971. The important findings are reported by him to the President of India under Article 151(1) of the Constitution of India who causes this Report to be submitted to the Parliament.

1.3 The audit of Direct Taxes is conducted through test checks of assessment and other records of the department maintained in its various offices which are spread all over the country. Various prescribed checks are applied to ensure whether the tax due from assessees has been worked out in accordance with the provisions of law and levied. Reliance is placed on law as interpreted by the appellate tribunals and judicial authorities. The thrust of statutory audit is to verify whether the systems and procedures prevalent in the department are satisfactory and to that extent, the objective is to lay emphasis on 'general' than on 'particular'. With this end in view, certain topics are selected for conducting 'Systems Reviews' every year.

Present Audit Report

1.4 The arrangement of this Report has been mentioned in the prefatory remarks. In each case mentioning the results of audit, the response of Ministry, to the extent available, has been indicated. Where the reply of the Ministry has not been found acceptable, the reasons therefor have been mentioned alongwith the reply of the Ministry.

Of the total 14,575 audit observations involving underassessment of tax of Rs. 595.76 crores as noticed during test check of assessment records and referred to the department, only a small fraction has been featured in this Report. The selection of cases featured is based on either their monetary significance or which, in the perception of Audit, requires the attention of the Parliament. The present Report contains 210 audit observations pertaining to income tax, corporation tax, gift tax and wealth tax. The revenue effect of these cases amounts to Rs.129.98 crores. Besides these individual audit observations, the report also contains Systems Review on three topics.

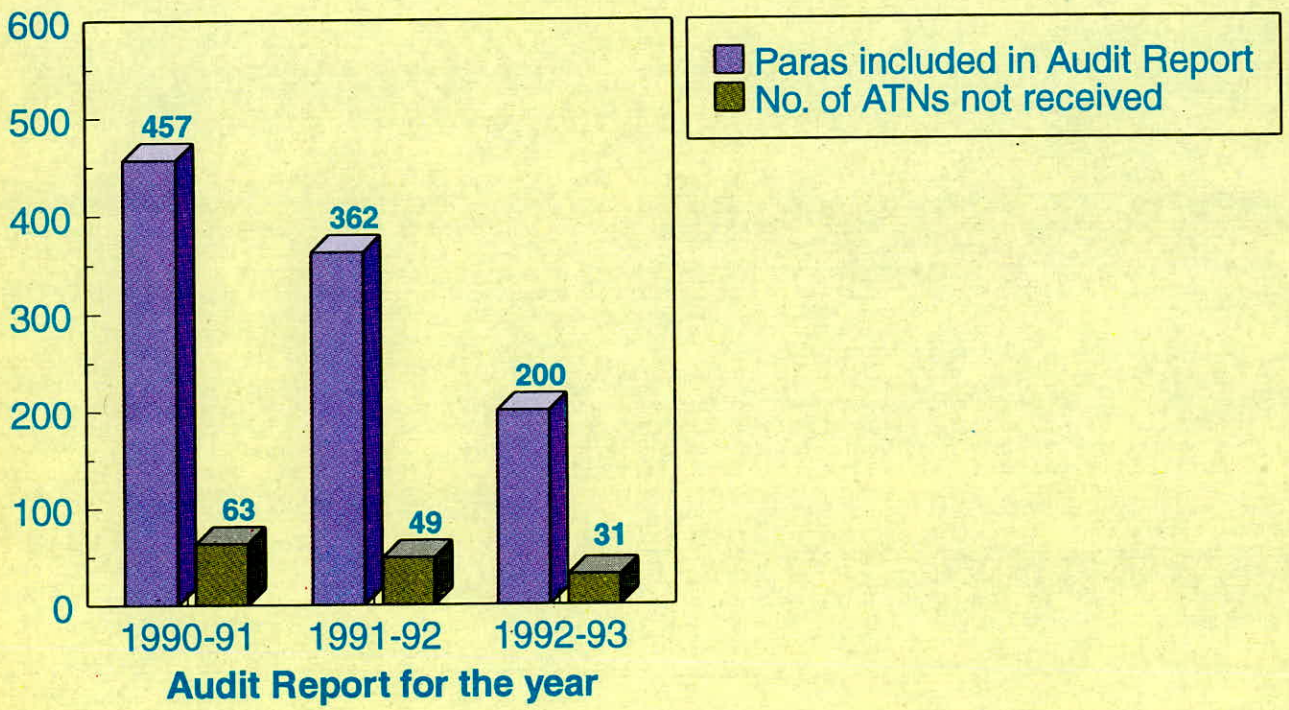
In respect of audit observations on individual cases, 163 cases with tax effect of Rs.80.33 crores have been accepted by the Ministry. The cases in which the Ministry have accepted the audit observations and have also taken rectificatory action including raising and collection of the resultant additional demand, have not been included in the Report unless the tax effect is very large or the case has some special features. 29 cases each with reasonably large tax effect aggregating Rs.304.52 lakhs have not been included in this Report on these considerations. Similarly, 24 other cases relating to excess carry forward/set off of losses having potential tax effect of Rs.295.41 lakhs have also not been included in the Report as the Ministry has accepted the audit observations and has taken the necessary remedial action.

Of the total 14,575 audit observations referred to earlier as resulting from test check, 1,943 cases with tax effect of Rs. 134.62 crores have so far been accepted by the department.

Non receipt of Board's comments on draft paragraphs

1.5 Cases with substantial tax effect are brought to the notice of the Income Tax Department and the Ministry in the form of 'draft paragraphs'. Sufficient time is allowed thereafter to them for their response so that these could be considered before finalising the Audit Report. However, despite Board's instructions that all 'draft paragraph' cases should receive the personal attention of the Commissioners of Income Tax for expeditious action, inordinate delays continue to occur in the receipt of departmental responses as indicated below in respect of the last 4 Audit Reports:

ACTION TAKEN NOTES NOT RECEIVED
(as on January 1, 1995)



Year of Report	Number of draft paragraphs Issued	Period of issue	Replies received before finalisation of Audit Report	Percentage of cases in which replies were received
1990-91	1319	Jan-Jul 1991	535	40.56
1991-92	1022	Mar-Jul 1992	136	13.30
1992-93	889	Mar-Aug 1993	629	70.75
1993-94	620	Mar-Sep 1994	536	86.45

Non-receipt of Action Taken Notes from the Government

1.6 The Lok Sabha Secretariat issued instructions (April 1982) to all the Ministries requesting them to furnish notes indicating remedial/corrective action taken by them on the various paragraphs contained in the Audit Reports as soon as they are laid on the table of the House duly vetted by Audit. Such notes are required to be submitted even for paragraphs which are not selected by the Public Accounts Committee for detailed examination.

A review of the Audit Reports for the years 1990-91 to 1992-93 revealed that the Ministry had not submitted remedial/corrective action taken notes in several cases as shown below:

Audit Report for the year	No. of paras included	No. of action taken notes not received
1990-91	457	63
1991-92	362	49
1992-93	200	31

Local Audit Report

1.7 In the field, after completion of audit of each assessment unit, audit observations are conveyed to the department through Local Audit Reports. In case of important observations, a Statement of Facts is issued to the department to verify the facts and to obtain views on the observation.

Results of Test Audit in general

1.7.1 Test audit conducted between 1 April 1993 and 31 March 1994 of the assessments completed by the Income Tax Department revealed 14,575 cases of underassessment involving a total revenue effect of Rs. 595.76 crores which were referred to the department. A resume of the deficiencies noticed is given below:

(i) Corporation Tax and Income Tax

During the period under report, 13,076 cases involving a tax effect of Rs. 578.64 crores were referred to the department. Of these cases, major audit observations were raised in 7,229 cases involving short levy of tax of Rs. 572.22 crores. The remaining 5,847 cases accounted for underassessment of tax of Rs. 6.42 crores.

The underassessment of tax of Rs. 578.64 crores arose due to mistakes which could broadly be categorised under the following heads:

		No. of cases	Amount (Rupees in crores)
1.	Avoidable mistakes in computation of income and tax	1140	21.01
2.	Failure to observe the provisions of the Finance Acts	546	59.58
3.	Incorrect status adopted in assessments	206	7.59
4.	Incorrect computation of income	181	1.71
5.	Incorrect computation of income from house property	133	3.55
6.	Incorrect computation of business income	2725	181.27
7.	Irregularities in allowing depreciation, investment allowance and development rebate	1452	51.34
8.	Irregular computation of capital gains	188	8.46
9.	Mistakes in assessments of firms and partners	342	4.82
10.	Income not assessed	1197	42.47
11.	Irregular set off of losses	397	47.34
12.	Irregular exemptions and excess reliefs given	854	41.09
13.	Non-levy/incorrect levy of interest for delay in submission of returns, delay in payment of tax etc.	1751	29.07
14.	Avoidable or incorrect payment of interest by Government	142	2.44
15.	Omission/short levy of penalty	594	9.70
16.	Other topics of interest (Miscellaneous)	1228	67.20
	Total	13076	578.64

(ii) Wealth Tax

During test audit of assessments made under Wealth Tax Act, 1957, short levy of Rs. 8.46 crores was referred to the department in 1318 cases.

The mistakes can be categorised under the following heads:

	No. of cases	Amount (in crores of rupees)
1.Wealth not assessed	364	4.04
2.Incorrect valuation of assets	274	1.78
3.Mistakes in computation of net wealth	155	0.53
4.Incorrect status adopted in assessments	70	0.32
5.Irregular/excessive allowances and exemption	119	0.34
6.Mistakes in calculation of tax	80	0.20
7.Non-levy or incorrect levy of additional wealth-tax	22	0.15
8.Non-levy or incorrect levy of penalty and non-levy of interest	170	0.56
9.Miscellaneous	64	0.54
Total	1318	8.46

(iii) Gift Tax

During the test check of gift tax assessments in 171 cases involving short levy of Rs. 8.38 crores were referred to the department.

(iv) Estate Duty

In the course of test audit of Estate Duty assessments it was noticed that in ten cases there was short levy of estate duty of Rs. 28.42 lakhs.

Outstanding audit observations

1.7.2 According to the departmental instructions, observations of statutory audit are to be replied to within a period of six weeks. The Public Accounts Committee (Ninth Lok Sabha) in their 20th Report recommended that the responsibility for the settlement of audit observations rests with the department and it cannot be contented merely with sending replies to audit observations. However, large number of audit observations made in 1993-94 and earlier years is still to be settled. The details are mentioned below:

(a) On 31 March 1994, 70,935 observations involving a revenue of Rs. 5646.21 crores, were pending for final action. This does not include the audit observations communicated during 1 April 1993 to 31 March 1994. The year-wise particulars of the pendency are as follows:

1.7

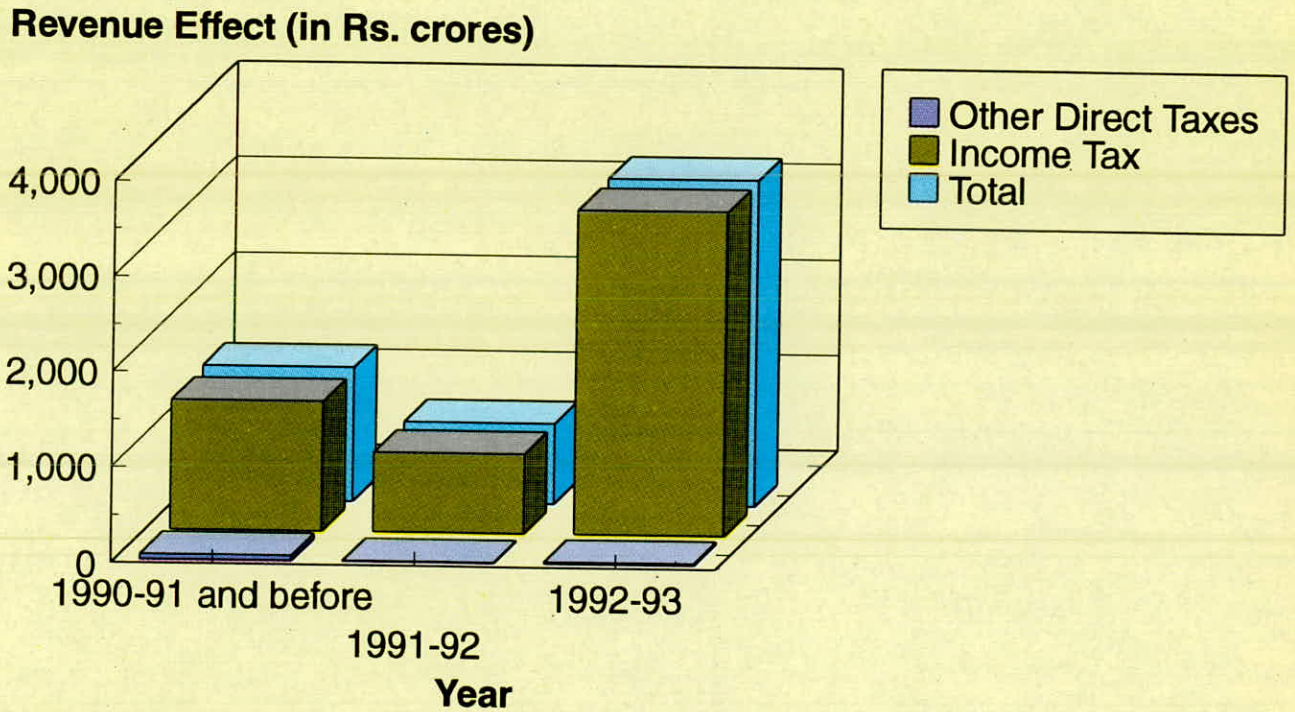
(Amount in Rs. Crores)

	Income Tax		Other Direct Taxes (Wealth Tax, Gift Tax and Estate Duty)		Total	
Year	Items	Revenue effect	Items	Revenue effect	Items	Revenue effect
1990-91 and earlier years	42990	1352.88	8206	48.88	51196	1401.76
1991-92	7929	830.10	993	7.74	8922	837.84
1992-93	9544	3387.71	1273	18.90	10817	3406.61
Total	60463	5570.69	10472	75.52	70935	5646.21

(b) There were 2141 pending audit observations (as against 1881 in earlier year) where the income tax involved in each individual case exceeded Rs. 10 lakhs. The charge-wise break-up of these cases is shown below:

Sl.No.	Name of charge	Items	Amount (In lakhs of rupees)
1.	Andhra Pradesh	25	536.89
2.	Assam	42	2239.84
3.	Bihar	38	4080.23
4.	Delhi	315	52808.25
5.	Gujarat	115	4466.75
6.	Haryana	3	45.44
7.	Himachal Pradesh	3	50.14
8.	Karnataka	41	3896.86
9.	Kerala	28	579.96
10.	Madhya Pradesh	177	15096.54
11.	Maharashtra	547	340043.42
12.	Orissa	25	991.12
13.	Punjab	22	4724.05
14.	Rajasthan	22	1211.33

REVENUE EFFECT OF OBSERVATIONS OF STATUTORY AUDIT WHICH ARE PENDING FOR FINAL ACTION



15.	Tamil Nadu	244	11774.36
16.	Uttar Pradesh	65	2622.85
17.	West Bengal	425	32055.17
18.	Chandigarh(U.T)	4	51.62
	Total	2141	477274.82

(c) The distribution of audit observations where the wealth tax involved in each case exceeded Rs.5 lakhs is as under:

Sl.No.	Name of charge	Items	Amount (In lakhs of rupees)
1.	Assam	1	9.58
2.	Delhi	7	80.68
3.	Gujarat	9	136.87
4.	Karnataka	5	92.67
5.	Kerala	3	40.94
6.	Madhya Pradesh	12	676.69
7.	Maharashtra	6	210.34
8.	Punjab	3	27.39
9.	Tamil Nadu	23	296.66
10.	Uttar Pradesh	1	8.24
11.	West Bengal	4	49.43
	Total	74	1629.49

(d) The distribution of audit observations where the total gift tax involved in each case exceeded Rs.5 lakhs is given below:

Sl.No.	Name of charge	Items	Amount (in lakhs of Rupees)
1.	Andhra Pradesh	1	66.06
2.	Delhi	3	88.60

3.	Gujarat	7	93.31
4.	Chandigarh(UT)	1	32.98
5.	Karnataka	4	86.24
6.	Madhya Pradesh	2	13.86
7.	Maharashtra	5	154.03
8.	Orissa	1	184.97
9.	Tamil Nadu	19	310.65
10.	West Bengal	7	211.66
	Total	50	1242.36

(e) The distribution of audit observations where the estate duty involved in each case exceeded Rs.5 lakhs is shown below:

Sl.No.	Name of charge	Items	Amount (in lakhs of Rupees)
1.	Andhra Pradesh	6	701.62
2.	Karnataka	2	12.81
3.	Kerala	1	10.08
4.	Tamil Nadu	2	24.18
5.	West Bengal	2	11.30
	Total	13	759.99

Of 70,935 pending cases with revenue effect of Rs.5,646.21 crores, 2,278 cases (3.2 percent) accounted for Rs.4,808.54 crores (85.16 percent). This underlines the need to assign priority to the settlement of observations with high money value.

Steps taken to settle audit observations

1.7.3 The Action Plan of the department for 1993-94 provided for 90 percent disposal of all pending major audit observations. In respect of current observations of statutory audit upto 31 December 1993 (i.e. period of report being 1993-94), replies are to be sent in 80 percent of the cases.

The targets according to Action Plan and actual achievement in settlement of the major statutory audit observations for the year 1993-94 were as under:

	Number for disposal (Amount in crores of rupees)	Number to be settled as per targets fixed	Number settled (Amount in crores of rupees)	Shortfall Cases	Shortfall Percentage
Current	9281 (9.43)	8353 (90%)	3531 (1.55)	4822	57.73
Arrear	19075 (19.47)	17168 (90%)	7422 (9.21)	9746	56.75

The achievements were, therefore, well short of targets set.

Remedial action barred by time

1.7.4 The Central Board of Direct Taxes have issued specific instructions for taking timely action on audit observations so as to avoid cases becoming time-barred leading to loss of revenue. The Public Accounts Committee (150th Report - Eighth Lok Sabha) have also recommended that the Board may review old outstanding observations in co-operation with Audit.

In a few charges reviewed during the year 1993-94, a number of cases where remedial action became barred by limitation was noticed. The number noticed as a result of review of such cases alongwith tax effect involved in selected charges are as under :

Sl.No.	Charge	Income Tax	
		Number of observations	Tax effect (in lakhs of rupees)
1.	Gujarat	258	45.54
2.	Haryana	64	17.10
3.	Kerala	85	4.96
4.	Maharashtra	233	12.39
5.	Orissa	1	0.23
6.	Punjab	53	2.72

Internal Audit

1.8 In addition to the statutory audit, the department also has an arrangement for audit of the assessments. For this purpose there is an Internal Audit Department (IAD) which conducts 100 percent audit of all immediate assessment cases(as defined under departmental instructions of September 1990). According to the departmental instructions, observations of Internal Audit Department are to be attended to by the assessing officers within three months.

During 1993-94, the total number of observations made by the Internal Audit Department was 11514 with money value of Rs. 291.94 crores.

On 31 March 1994, 34549 audit observations made by the Internal Audit involving a tax effect of Rs. 533.47 crores were pending settlement.

Outstanding observations of Internal Audit

1.8.1 According to the information furnished by the Directorate of Income Tax (Audit) of the Department , the number of major observations of the Internal Audit disposed of during the four year period 1990-94 and the number pending at the end of each of these years are given below:

Financial year	No.of cases for disposal and amount (in crores of rupees)	No.of cases disposed of and amount (in crores of rupees)	Percentage of disposal to total number of cases for disposal	No.of pending cases and amount (in crores of rupees)
1990-91	20698 (1017.37)	10044 (318.25)	48	10654 (699.12)
1991-92	18625 (936.61)	7159 (570.50)	38	11466 (366.11)

1992-93	18053 (614.59)	6750 (146.78)	37	11303 (467.82)
1993-94	18006 (788.17)	7752 (259.57)	43	10254 (526.61)

The Public Accounts Committee, in their 150th Report submitted to Eighth Lok Sabha in April 1989, had recommended that observations of Internal Audit should be analysed with reference to the year of assessment apart from the year in which these were raised, so that greater attention could be given to the settlement of observations relating to earlier years, before the cases became time-barred for re-opening. Since the normal period available for re-opening of cases is four years, all observations pertaining to 1990-91 and earlier years should have been settled by March 1994, However, this did not happen as shown in the following table which gives age-wise analysis of the pending items at the end of 1993-94 and revenue effect involved:

Year of the observation	No. of cases	Revenue effect (in crores of rupees)
1990-91 and earlier years	13878	121.83
1991-92	6155	99.85
1992-93	6537	102.45
1993-94	7979	209.34
Total	34549	533.47

Action on observations of Internal Audit

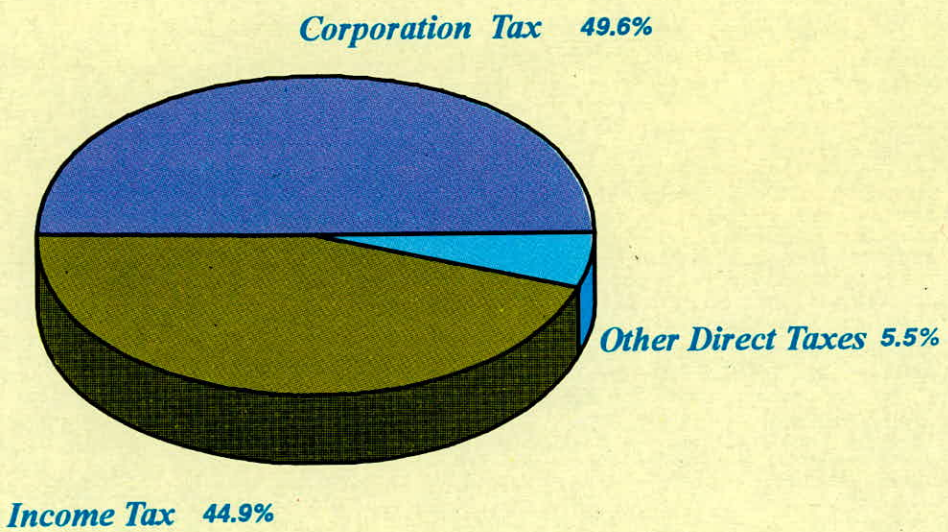
1.8.2 The Action Plan of the department for 1993-94 provided for 100 percent disposal of all pending major audit observations. In respect of current observations of Internal audit upto 31 December 1993 (i.e. period of reporting being 1993-94), replies were to be sent in 50 percent of the cases.

1.8

The targets according to Action Plan and actual achievement in settlement of the major internal audit observations for the year 1993-94 were as under:

	Number for disposal (Amount in crores of rupees)	Number to be settled as per targets fixed	Number settled (Amount in crores of rupees)	Shortfall	
				Cases	Percentage
Current	6190 (2880.04)	5571	2426 (80.29)	3145	56.45
Arrear	11816 (498.13)	10634	5326 (179.28)	5308	49.92

REVENUE FROM DIRECT TAXES (1993-94)



Corporation Tax	Rs.10,060.06 crores
Income Tax	Rs. 9,122.62 crores
Other Direct Taxes	Rs. 1,115.56 crores

CHAPTER 2

Statistical Information on Administration of Direct Taxes

Receipts under various Direct Taxes

2.1 The total proceeds from Direct Taxes for the year 1993-94 amounted to Rs.20,298.24 crores out of which a sum of Rs.7,767.50 crores was assigned to the States. The figures for the three years 1991-92, 1992-93 and 1993-94 are given below:

(In crores of Rupees)

		1991-92	1992-93	1993-94	Increase in 1993-94 over the previous year
0020	Corporation Tax	7867.67	8889.24	10060.06	1170.82
0021	Taxes on income other than Corporation-tax	6705.80	7863.49	9122.62	1259.13
0023	Hotel Receipts Tax	1.24	0.37	0.05	(-)0.32
0024	Interest Tax	305.04	714.70	727.58	12.88
0028	Other Taxes on Income and Expenditure	144.38	152.00	228.75	76.75
0031	Estate Duty	2.86	0.95	0.21	(-)0.74
0032	Taxes on wealth	306.93	467.27	153.98	(-)313.29
0033	Gift tax	8.44	9.27	4.99	(-)4.28
	Gross Receipts	15342.36	18097.29	20298.24	2200.95
	Less share of net proceeds assigned to the States:				
	Income Tax	5,104.32	6059.45	7767.50	
	Net Receipts	10,238.04	12037.84	12530.74	

Trend of collection

2.2(i) The trend in collection of Direct Taxes since 1989-90 is as follows:

2.2-2.3

Year	Collection (in crores of rupees)				Index taking 1989-90 as base			
	Corporation Tax	Income Tax other than Corporation Tax	Other Direct Taxes	Total	Corporation tax	Income Tax other than Corporation tax	Other Direct Taxes	Total
1989-90	4728.92	5006.98	269.88	10007.78	100.00	100.00	100.00	100.00
1990-91	5335.27	5375.34	318.33	11028.94	112.8	107.3	118.00	110.2
1991-92	7867.67	6705.80	768.89	15342.36	166.4	133.9	284.9	153.3
1992-93	8889.24	7863.49	1344.56	18097.29	188.0	157.0	498.2	180.8
1993-94	10060.06	9122.62	1115.56	20298.24	212.7	182.1	413.3	202.8

(ii) Corporation tax and income tax collections since 1989-90 shown as percentage of the Gross Domestic Product are as follows:

Year	Corporation Tax	Income Tax other than corporation tax	GDP at factor cost (current prices)*.	As a percentage of G.D.P. Corporation tax	Income tax.
	(rupees in crores)				
1989-90	4728.92	5008.98	3,95,143	1.2	1.3
1990-91	5335.27	5375.34	4,72,660	1.1	1.2
1991-92	7867.67	6705.80	5,41,888	1.5	1.2
1992-93	8889.24	7863.49	6,27,913	1.4	1.2
1993-94	10060.06	9122.62	7,07,145	1.4	1.3

Variation between Budget estimates and Actuals

2.3(i) The comparative position of actual receipts vis-a-vis the budget estimates under the different heads for the years 1989-90 to 1993-94 are as follows :

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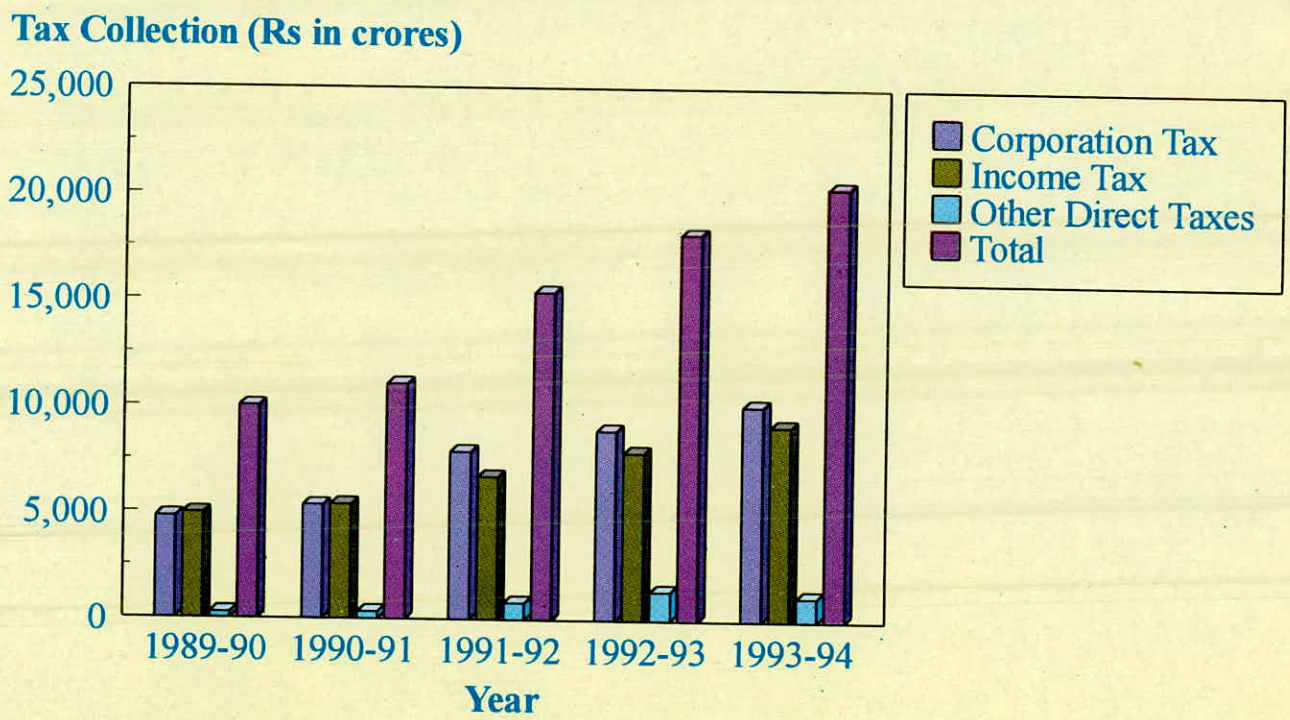
* GDP figures collected from National Accounts Statistics Organisation, Ministry of Planning. GDP figures for 1993-94 are as per estimates of NASO.

TREND IN COLLECTION OF DIRECT TAXES (1989-90 TO 1993-94)



Year	Budget Estimates	Actuals	Variation	Percentage of variation
		(In crores of Rupees)		
0020-Corporation Tax				
1989-90	4,500.00	4,728.92	228.92	5.08
1990-91	5,289.00	5,335.27	46.27	0.87
1991-92	6,704.00	7,867.67	1163.67	17.35
1992-93	8,125.00	8,889.24	764.24	9.41
1993-94	10,500.00	10,060.06	(-)439.94	(-)4.19
0021-Taxes on Income other than Corporation Tax				
1989-90	4,000.00	5,008.98	1008.98	25.22
1990-91	5,676.00	5,375.34	(-)300.66	(-)5.30
1991-92	6,152.00	6,705.80	553.80	9.00
1992-93	7,870.00	7,863.49	(-)6.51	(-)0.08
1993-94	9,500.00	9,122.62	(-)377.38	(-)3.97
Other Direct Taxes##				
1989-90	132.60	194.79	62.19	46.90
1990-91	187.50	236.76	49.26	26.27
1991-92	801.30	623.27	(-)178.03	(-)22.21
1992-93	1158.00	1344.56	186.56	16.11
1993-94	1260.00	1115.56	(-)144.44	(-)11.46

(ii) The details of variation under the heads subordinate to the Major Heads 0020 and 0021 for the year 1993-94 are as follows:

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includes Interest Tax, Estate Duty, Wealth Tax, Gift Tax. Details are given in Appendix I.

	Budget Estimates	Actuals	Variation	Percentage of variation
		(In crores of Rupees)		
0020-Corporation Tax				
(i) Income Tax on companies	9096.00	9664.14	568.14	6.25
(ii) Surtax	13.00	0.40	(-)12.60	(-)96.92
(iii) Surcharge	1365.00	315.07	(-)1049.93	(-)76.92
(iv) Other receipts	26.00	80.45	54.45	209.42
Total	10500.00	10060.06	(-)439.94	(-)4.19
0021-Taxes on Income other than Corporation Tax				
(i) Income-tax	8912.00	8935.50	23.50	0.26
(ii) Surcharge	534.00	113.38	(-)420.62	(-)78.77
(iii) Other receipts	54.00	73.74	19.74	36.55
(iv) Deduct share of proceeds assigned to States	7136.02	7767.50	631.48	8.85
Total	2363.98	1355.12	(-)1008.86	(-)42.68

Analysis of collection

2.4 Under the provisions of the Income Tax Act, 1961, income tax is chargeable for any assessment year in respect of the total income of the previous year at the rates prescribed in the annual Finance Act. The Act provides for pre-assessment collection by way of deduction of tax at source, advance tax and payment of tax on self-assessment. The post-assessment collection is of residuary taxes not so paid.

(i) The break-up of total collections of corporation tax and surtax from companies and taxes on income other than corporation tax from non-companies, at pre-assessment and post-assessment stages, during the year 1993-94 as furnished by the Ministry of Finance is as follows :

(In crores of rupees)

	Company			Non-company	Grand Total
	Corporation Tax	Surtax	Total	Income Tax	
Tax deducted at source	2,772.27		2,772.27	4,510.31	7,282.58
Advance Tax	7,303.43	-	7,303.43	3,794.34	11,097.77
Self-assessment	1,250.58	-	1,250.58	1,156.06	2,406.64
Regular assessment	2,382.51	-	2,382.51	714.19	3,096.70
Other receipts including surcharge	397.06	0.40	397.46	285.17	682.63
Total collections	14,105.85	0.40	14,106.25	10,460.07	24,566.32
Refunds	4,045.96	-	4,045.96	1,340.96	5,386.92
Net collections	10059.89	0.40	10060.29	9119.11	19179.40*

(ii) The sub-head-wise break-up of total income tax collections for companies, non companies and total thereof for the years 1989-90 to 1993-94, as furnished by the Ministry of Finance, are given below:

(In crores of rupees)

Year	Tax collection						Refunds	Net Collection
	Tax Deducted at source	Advance Tax	Self Assess-ment	Regular Assess-ment	Other Receipts	Total Collec-tions		
Company								
1989-90	1,684.89	3,017.30	364.31	1,029.75	80.19	6,176.44	1,462.25	4,714.19
1990-91	1,499.58	4,085.01	355.98	1,127.67	207.17	7,275.41	1,944.79	5,330.62
1991-92	2,348.13	5,962.38	455.31	1,157.09	543.56	10,466.47	2,613.67	7,852.80
1992-93	2,321.19	6,886.67	1032.48	1,437.88	424.86	12,103.08	2,489.04	9,614.04
1993-94	2,772.27	7,303.43	1,250.58	2,382.51	397.46	14,106.25	4,045.96	10,060.29

* Figures of net collections do not tally with those given at para 2.1 and will be reconciled by the Ministry of Finance.

2.4

Non-company								
1989-90	2,665.67	1,967.21	535.94	326.90	81.83	5,577.55	569.26	5,008.29
1990-91	2,583.36	2,227.64	639.30	562.18	175.89	6,188.37	827.74	5,360.63
1991-92	3,627.80	2,504.81	721.32	414.33	255.71	7,523.97	794.79	6,729.18
1992-93	3,888.34	3,030.98	1005.38	676.60	459.49	9,060.79	1165.44	7,895.35
1993-94	4,510.31	3,794.34	1156.06	714.19	285.17	10460.07	1340.96	9119.11
Total								
1989-90	4,305.56	4,984.51	900.25	1,356.65	162.02	11,753.99	2,031.51	9,722.48
1990-91	4,082.94	6,312.65	995.28	1,689.85	383.06	13,463.78	2,772.53	10,691.25
1991-92	5,975.93	8,467.19	1,176.63	1,568.08	802.61	17,990.44	3,408.46	14,581.98
1992-93	6,209.53	9,917.65	2,037.86	2,114.48	884.35	21,163.87	3,654.48	17,509.39
1993-94	7,282.58	11,907.77	2,406.64	3,096.70	682.63	24,566.32	5,386.92	19,179.40

(iii) The details of tax deduction at source during the year 1993-94 under broad categories are as under:

	Amount (in crores of rupees)
Salaries	**1926.11**
Interest on securities	**1809.99**
Dividends	**408.89**
Interest	**1,007.73**
Winnings from lottery or cross word puzzles	**34.74**
Winnings from horse races	**9.42**
Payments to contractors and sub-contractors	**1065.71**
Insurance commission	**47.29**
Payment to non-residents and others	**972.70**
Total	**7282.58**

(iv) The details of statements of tax deducted at source for the year 1993-94 under broad categories are as under:

1.	No. of Tax deductors as on 1 April 1993	4,55,878
2.	Adjustment/progressive additions upto 31 March 1994	35,445
3.	Effective Tax Deductors(1+2)	4,91,323
4.	No. of returns required to be filed by tax deductors at 3	4,87,770
5.	Returns received upto 31 March 1994	3,54,268
6.	Balance 4-5	1,33,502

Cost of collection

2.5.1 The total expenditure incurred during the year 1993-94 and earlier three years in collecting the direct taxes are as under:

Year	Collection	Expenditure	Percentage
	(In crores of Rupees)		
1990-91	11,028.94	230.18	2.09
1991-92	15,342.36	256.46	1.67
1992-93	18,097.29	296.48	1.63
1993-94	20,298.24	335.43	1.65

2.5.2 The expenditure incurred during the year 1993-94 in collecting corporation tax, taxes on income other than corporation tax and other direct taxes together with the corresponding figures for the preceding three years, is as follows:

	Collection	Expenditure on collection	Percentage
	(In crores of Rupees)		
0020-Corporation Tax			
1990-91	5,335.27	27.62	0.52
1991-92	7,867.67	30.77	0.39
1992-93	8,889.24	35.44	0.39
1993-94	10,060.06	40.04	0.39
0021-Taxes on income etc.			
1990-91	5,375.34	179.53	3.33
1991-92	6,705.80	200.02	2.98
1992-93	7,863.49	230.43	2.93
1993-94	9,122.62	260.63	2.85
Other Direct Taxes#			
1990-91	317.03	23.03	7.26
1991-92	767.65	25.67	3.34
1992-93	1,344.56	30.61	2.27
1993-94	1,115.56	34.76	3.12

Number of assessees

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

Income tax

2.6.1 For the assessment year 1993-94, no income tax was payable on a total income not exceeding Rs. 28,000 except in the case of specified Hindu undivided family, registered firms, co-operative society, local authority and company where a lower limit is applicable.

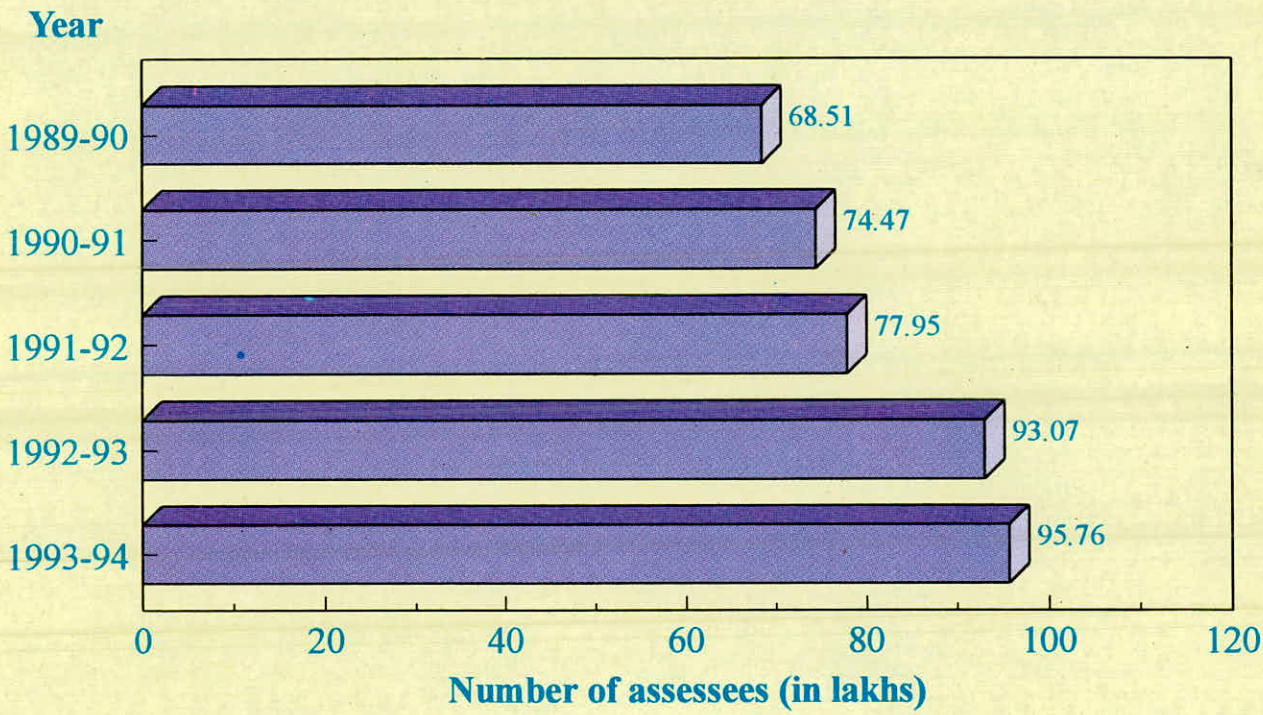
(i) The total number of assessees in the books of the department was 95,76,177 as on 31 March 1994 as against 93,06,706 as on 31 March 1993. The break-up of the assessees on the said two dates was as under:

	As on 31 March 1993	As on 31 March 1994
Individuals	74,26,561	77,43,572
Hindu undivided families	4,25,933	4,03,474
Firms	12,27,859	12,00,041
Companies	1,55,418	1,61,075
Trusts	38,651	38,205
Others	32,284	29,810
Total	93,06,706*	95,76,177

Includes interest tax, expenditure tax estate duty, wealth tax and gift tax. For details, see Appendix II

* Provisionally reported as 83.62 lakhs by the Ministry and printed as such in the Audit Report 1992-93

GROWTH IN NUMBER OF ASSESSEES (1989-90 TO 1993-94)



(ii)[$] The following table indicates the category wise break up of assessees:

Category	Individuals	Hindu undivided families	Firms	Companies	Others (including Trusts)	Total
(i) Category 'A'	75,00,275	3,86,725	11,32,256	87,067	62,082	91,68,405
(ii) Category 'B' (Lower)	1,82,954	11,590	46,691	38,473	3,903	2,83,611
(iii) Category 'B' (Higher)	36,061	2,226	11,786	14,101	573	64,747
(iv) Category 'C'	9,177	1,095	5,288	20,214	1,337	37,111
(v) Category 'D'	15,105	1,838	4,020	1,220	120	22,303
Total	77,43,572	4,03,474	12,00,041	1,61,075	68,015	95,76,177

Surtax

(iii) Under the Companies (Profits) Surtax Act, 1964, surtax is levied on the chargeable profits of a company in so far as they exceed the statutory deductions, which is equal to 15 percent (from 1 April 1977) of the capital of the company or Rs. two lakhs, which ever is greater.

$ Shillong charge not included.

1. Category A : company assessments with income/loss below Rs.50,000 and non company assessments with income/loss below Rs.2 lakhs.
2. Category B (lower) : company assessments with income/loss of Rs.50,000 and above but below Rs.5 lakhs and non-company assessments with income/loss of Rs.2 lakhs and above and below Rs. 5 lakhs.
3. Category B (higher) : company assessments and non-company assessments with income/loss of Rs.5 lakhs and above but below Rs.10 lakhs.
4. Category C : company and non-company assessments with income/loss of Rs. 10 lakhs and above
5. Category D : search and seizure assessments.

2.6

The number of surtax assessees in the books of the department as furnished by the Ministry of Finance for the last three years were as under:

Year ending	No.of assessees
31 March 1992	1,411
31 March 1993	1,037
31 March 1994	1,190

Interest Tax

(iv) The number of assessees for interest tax in the books of the department as furnished by the Ministry of Finance for the last three years were as under:

Year ending	No. of assessees
31 March 1992	142
31 March 1993	850
31 March 1994	1,385

Wealth Tax

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

For the assessment year 1993-94 no wealth tax was payable where the net wealth was less than Rs. 15 lakhs.

The number of wealth tax assessees in the books of the department as on 31 March 1993 and 31 March 1994 were as follows:

	As on 31 March 1993	31 March 1994
Individuals	6,38,243	5,52,914
Hindu undivided family	87,692	70,153
Companies	16,816	16,406
Total	7,42,751	6,39,473

Gift Tax

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

During the assessment year 1993-94 no gift tax was payable where the value of taxable gifts did not exceed Rs.30,000.

The number of gift tax assessment cases for disposal for the years 1992-93 and 1993-94 were as follows:

1992-93	40,138
1993-94	51,064

Arrears of assessment

2.7.1 The limitation period for completion of assessment is 2 years in the case of income tax, wealth tax and gift tax.

Sanctioned and working strength of officers on assessment duty as on 31 March 1994 was as under:

Nature of Posts	Sanctioned strength	Working strength
(a) Income Tax Officers on assessment duty	1356	1376
(b) Assistant Commissioners	739	722
(c) Additional Commissioners/ Deputy Commissioners	199	198
Total	2294	2296

2.7.2 Income Tax including Corporation Tax

(i) The number of assessments completed during the five years was as under:

Financial year	Number of assessments for disposal			Number of assessments completed			
	Scrutiny	Summary	Total	Scrutiny	Summary	Total	Percentage of disposal
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1989-90	4,44,724	64,42,103	68,86,827	2,97,543	54,01,950	56,99,493	82.76
1990-91	4,41,797	72,28,910	76,70,707	2,60,722	61,27,783	63,88,505	83.28
1991-92	5,34,174	75,00,631	80,34,805	3,06,495	64,06,919	67,13,414	83.55
1992-93	5,09,406	74,43,737	79,53,143	2,85,867	62,17,076	65,02,943	81.76
1993-94	4,98,327	84,65,578	89,63,905	3,36,894	70,86,282	74,23,176	82.81

The break-up of number of assessments pending at the end of the year is given below:

	Scrutiny	Summary	Total
1989-90	1,47,181	10,40,153	11,87,334
	(12.40)	(87.60)	
1990-91	1,77,766	11,04,436	12,82,202
	(13.86)	(86.14)	
1991-92	2,27,679	10,93,712	13,21,391
	(17.23)	(82.77)	
1992-93	2,23,539	12,26,661	14,50,200
	(43.88)	(16.47)	
1993-94	1,61,403	13,79,296	15,40,699
	(32.39)	(16.29)	

(Figures in parentheses denote percentage of pendency)

It would be seen from the above table that percentage of pending scrutiny cases has continued to remain very high, ranging from 12.40 per cent in 1989-90 to 32.39 per cent in 1993-94. The number of summary assessments has also increased as compared to last year. This has happened, even though the Board had issued instructions for according priority to increasing disposal of both summary and scrutiny assessments.

(ii) Status-wise break - up of income tax assessments completed during the year 1992-93 and 1993-94 was as under:

	1992-93	1993-94
(i) Individuals	49,90,063	59,68,510
(ii) Hindu undivided families	3,14,207	2,87,786
(iii) Firms	10,07,298	9,27,505
(iv) Companies	1,51,913	1,81,130
(v) Others	39,462	58,245
Total	65,02,943	74,23,176

(iii) Status-wise and income range-wise break-up of pendency of assessments as on 31 March 1994 was as under:

Sr. No.	Status	No. of pending assessments with category					
		Category 'A'	Category 'B' (lower)	Category 'B' (higher)	Category 'C'	Category 'D'	Total
1.	Company	29,697	15,884	7,485	19,701	1,447	74,214
2.	Non Company	13,63,653	33,115	13,818	10,641	10,455	14,31,682
3.	Total	13,93,350	48,999	21,303	30,342	11,902	15,05,896

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

	As on 31 March 1993	As on 31 March 1994
1989-90 and earlier years	12,676	39,368
1990-91	29,553	23,099
1991-92	2,25,173	45,254
1992-93	11,82,798	2,18,435
1993-94	--	10,09,820
Total*	14,50,200	13,35.976

(v) Status-wise and year-wise break-up of pendency of income-tax assessments as on 31 March 1994 was as under:

	Status	1989-90 and earlier years	1990-91	1991-92	1992-93	1993-94	Total
(a)	Company assessments						
(i)	Regular	969	1710	3797	16,848	42,322	65,646
(ii)	Reopened/ set aside	596	508	329	215	139	1,787
(b)	Non-company assessments						
(i)	Regular	35,098	18,109	39,152	1,99,936	9,63,290	12,55,585
(ii)	Reopened/ set aside	2,705	2,772	1,976	1,436	4,069	12,958
	Total	39,368	23,099	45,254	2,18,435	10,09,820	13,35,976

The number of assessments pending as on 31 March 1994 was 13,35,976 as compared to 14,50,200 as on 31 March 1993 and 13,21,391 on 31 March 1992.

2.7.3 Wealth Tax and Gift Tax

Wealth Tax

(i) The number of wealth-tax assessments completed during the year 1993-94 was as follows :

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* These figures do not tally with those given in para 2.7.2 (i) and (iii), as figures of certain charges are not included and reconciliation is being done, according to Ministry of Finance.

Number of assessments

Due for disposal	Completed	Pending at the end of the year	Percentage of pendency
6,13.012	4,32,574	1,80,438	29.43

(ii) Status-wise break-up of the wealth tax assessments completed during the years 1992-93 and 1993-94 were as under:

	Status	No. of assessments completed during	
		1992-93	1993-94
(i)	Individuals	5,43,353	3,77,127
(ii)	Hindu undivided families	65,882	42,443
(iii)	Companies	15,163	13,004
(iv)	Others	607	-
	Total	6,25,005	4,32,574

(iii) Assessment year-wise position of pendency of assessments at the end of 1993-94 was not furnished by the Ministry of Finance.

Gift Tax

(iv) The number of gift tax assessments completed during the year 1993-94 was as under:

Number of assessments

Due for disposal	Completed	Pending at the end of the year	Percentage of pendency
36,478	28,489	7,989	21.90

(v) Assessment year wise position of pendency of assessments at the end of 1993-94 was not furnished by the Ministry of Finance.

Surtax and Interest Tax

(vi) The number of surtax and interest tax assessments completed during the year 1993-94 was as follows:

Number of assessments

	Due for disposal	Completed	Pending at the end of the year	Percentage of pendency
Surtax	1245	117	1128	90.60
Interest Tax	2381	395	1986	83.41

(vii) Assessment year-wise position of pendency of assessments in respect of sur tax and interest tax was not furnished by the Ministry of Finance.

Arrears of Tax Demands

2.8.1 The Income Tax Act, 1961, provides that when any tax, interest, penalty, fine or any other sum is payable in consequence of any order passed under the Act, a notice of demand shall be served upon the assessee. The amount specified as payable in the notice of demand has to be paid within 30 days unless the time for payment is extended by the assessing officer on application made by the assessee. The Act has been amended with effect from 1 October 1975 to provide that an appeal against an assessment order would be barred unless the admitted portion of the tax as per return has been paid before filing the appeal.

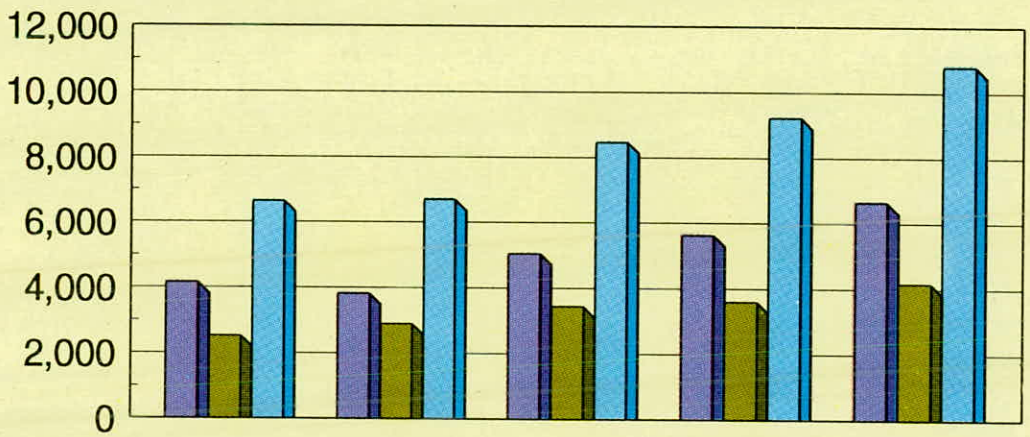
Corporation Tax (including surtax) and Income Tax

(i)(a) The total demand of tax raised and remaining uncollected as on 31 March 1994 was Rs.10780.13 crores, out of which arrears of Rs.6626.63 crores related to companies. The arrears included Rs.3969.33 crores which had not fallen due as on 31 March 1994, Rs.547.58 crores claimed to have been paid but remaining to be verified/adjusted, Rs.2160.35 crores stayed/kept in abeyance and Rs.98.50 crores for which instalments had been granted and instalments not fallen due. Arrears continue to mount despite directions of the Board for according priority to reduction of the arrear demand.

(b) The details of demands of income tax (including corporation-tax) stayed/kept in abeyance as on 31 March 1994 were as follows :

DEMANDS RAISED BUT NOT COLLECTED

Cumulative Uncollected Demand (Rs. in crores)



Year	1989-90	1990-91	1991-92	1992-93	1993-94
Companies	4,126.63	3,808.71	5,038.33	5,623.63	6,626.63
Non-companies	2,511.84	2,885.83	3,422.65	3,587.37	4,153.50
Total	6,638.47	6,694.54	8,460.98	9,211.00	10,780.13

(In crores of rupees)

(1)	By courts	188.60
(2)	Under Section 245(F)(2) (Application to Settlement Commission)	288.05
(3)	By Tribunals	194.99
(4)	By Income tax authorities due to	
	(i) Appeals and revisions	654.81
	(ii) Double income tax claims	1.07
	(iii) Restriction on remittances Sec.220(7)	32.80
	(iv) Other reasons	800.03
	Total	2160.35

(c)* The amounts of corporation tax, income tax, interest and penalty making up the arrears and the year wise details thereof are given below:

(In crores of rupees)

	Corporation Tax$	Income Tax$	Interest	Others**	Total
1.Over 1 year but less than two years.	757.55	271.54	798.71	158.03	1985.83
2.Over 2 years but less than 5 years	429.62	553.38	615.51	218.44	1816.95
3.Over 5 years but less than 10 years.	122.55	199.07	172.73	95.73	590.08
4. Over 10 years	33.78	87.01	69.59	41.04	231.42
Total#	1343.50	1111.00	1656.54	513.24	4624.28

(d) The following table gives the break up of the gross arrears of Rs.11365.33 crores by certain slabs of income:

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* Shillong charge is not included in these figures.

$ These figures include surcharge but not surtax/annuity deposits etc.

** Others include penalty, fees, fines,etc.

\# Figures do not tally with those given in para 2.8.(i)(a).

(Amount in Rs. crores)

	Company cases			Non-company cases			Total		
	No. of cases	Gross arrears	Net arrears	No. of cases	Gross arrears	Net arrears	No. of cases	Gross arrears	Net arrears##
Upto Rs.1 lakh in each case	117430	650.21	394.97	3978997	971.49	354.62	4096427	1621.70	749.59
Over Rs.1 lakh to Rs.10 lakhs in each case	12539	519.74	348.98	103164	499.86	305.00	115703	1019.60	653.98
Over Rs.10 lakhs to Rs.1 crore in each case	3537	1745.69	786.73	5764	1113.27	363.26	9301	2858.96	1149.99
Over Rs.1 crore in each case	707	4050.93	668.47	392	1814.13	904.38	1099	5865.06	1572.85
Total*	134213	6966.57	2199.15	4088317	4398.76	1927.26	4222530	11365.33	4126.41

(ii) The following table gives the year-wise arrears of demands outstanding under the two other direct taxes, **i.e.,** wealth tax and gift tax as on 31 March 1994.

(Amounts in crores of rupees)

	Wealth Tax Amount	Gift Tax Amount
Over one year but less than Two years	118.35	12.74
Over two years but less than five years	175.35	10.09
Over five years but less than 10 years	90.82	6.07
Over 10 years	38.76	2.91
Total	423.28	31.81

Net arrears represent gross arrears as reduced by demand not yet due, amounts claimed to have been paid but still to be verified, demand stayed and instalments granted but which have not fallen due.

* Figures do not tally with those given in para 2.8.1 (i)(a).

2.8.2 Under the provisions of the Income Tax Act, 1961 every demand of tax, interest, penalty or fine payable under the Act should be paid within thirty days of the service of notice of demand. On the default of an assessee in this respect, the assessing officer may forward a certificate specifying the demand of arrears to the Tax Recovery Officer for recovery of demand. The latter will serve a notice on the defaulter requiring him to pay the demand within fifteen days. If the amount mentioned in the notice is not paid within the time specified therein or within such further time as the Tax Recovery Officer may grant in his discretion, he shall proceed to realise the amount together with interest at the rate of 1.5 percent per month or part of month (from 1 April 1989) on the outstandings till the date of recovery by one or more of the following modes.

(a) by attachment and sale of the defaulter's movable property;

(b) by attachment and sale of the defaulter's immovable property;

(c) by arrest of the defaulter and his detention in prison;

(d) by appointing a receiver for the management of defaulter's movable and immovable properties.

(i) The number of officers engaged in tax recovery work during 1993-94 was as follows:

Category	Sanctioned strength	Working strength
Tax Recovery Officers	243	203

(ii) The tax demands certified to the Tax Recovery Officers and the progress of recovery to end of 1993-94 are given in the following table:

2.8

(In crores of rupees)

	At the beginning of the year *	Demand certified During the year	Total	Demand recovered during the year	Balance at the end of the year *
1989-90	959.85	218.77	1178.62	383.57	795.05
1990-91	795.05	322.15	1117.20	337.72	779.48
1991-92	776.97	606.35	1383.32	370.60	1012.72
1992-93	1023.79	506.06	1529.85	452.64	1077.21
1993-94	1025.19	1040.60	2065.79	519.33	1546.46

(iii) Year-wise break up of certificates pending on 31 March 1994 and amount of demand:

Year of receipt of recovery certificates	No. of certificates	Amount involved (In crores of rupees)
1989-90	935703	352.79
1990-91	23958	078.37
1991-92	37002	166.58
1992-93	19577	161.52
1993-94	26983	787.20
Total	1043223	1546.46

(iv) Tax-wise and amount-wise analysis of pending certificates:

(Amount in crores of rupees)

	Range of demand	Corporation Tax		Income Tax		Wealth Tax	
		No.	Amount	No.	Amount	No.	Amount
(a)	Upto Rs.10,000	26,347	6.82	7,26,401	465.15	1,09,644	16.39
(b)	Over Rs.10,000 and below Rs.1 lakh	4,846	7.71	1,05,316	109.67	14,081	23.64
(c)	Over Rs.1 lakh to Rs.5 lakhs	1800	18.96	11,752	184.04	1,752	22.29
(d)	Over Rs.5 lakhs to Rs.10 lakhs	308	14.33	3856	104.86	122	5.95
(e)	Over Rs.10 lakhs	451	98.90	3603	430.12	220	14.31
	Total	33,752	146.72	8,50,928	1,293.84	1,25,819	82.58

* Figures at the end of the year do not tally with the figures at the beginning of the next year and will be reconciled by the Ministry of Finance.

(Amount in crores of rupees)

	Range of demand	Gift Tax		Surtax		Others		Total	
		No.	Amount	No.	Amount	No.	Amount	No.	Amount
(a)	Upto Rs.10,000	27,033	2.99	3,459	5.31	802	0.40	8,93,686	497.07
(b)	Over Rs.10,000 and below Rs. 1 lakh	904	1.87	192	0.39	133	0.06	1,25,472	143.32
(c)	Over Rs.1 lakh to Rs.5 lakhs	132	1.41	32	0.79	----	----	15,468	227.49
(d)	Over Rs.5 lakhs	---	----	8	0.56	----	----	4,294	125.70
(e)	Over Rs.10 lakhs	9	2.85	20	6.27	----	0.42	4,303	552.88
	Total	28,078	9.12	3,711	13.32	935	0.88	10,43,223	1,546.46

(v) Details of disposal and pendency of attached property are indicated below :

A. Attachment of movable properties.

Particulars	No.of cases	Approximate value (in crores of rupees)
Pending cases in which attachment was made as on 1.4.1993	1430	32.06
Additions during the year	761	17.40
Total	2191	49.46
Not sold over six months	299	8.39

B. Attachment of immovable properties

Particulars	No.of cases	Immovable property	Approximate value (in crores of rupees)
Cases in which properties were attached as on 1.4.1993	2094	3594	270.47
Additions during the year	1194	1311	83.72
Total	3288	4905	354.19
Cases not sold for (a)over one year	834	1121	103.83
(b)Over 3 years	1158	1875	133.35

C. Sale of movable and immovable properties

Particulars	Movable property (value in crores of rupees)			Immovable property (value in crores of rupees)		
	No.of cases	No.of properties	Value	No.of cases	No.of properties	Value
Sale conducted	7	5,904	70.64	11	19	90.32

D. Cases in which receiver appointed

Number	Amount (in crores of rupees)
9	1.30

E. Defaulters against whom arrest proceedings initiated

Number	Amount (in crores of rupees)
246	7.67

Appeals, Revision Petitions and Writs

2.9 Under the provisions of the Income Tax Act, 1961 if an assessee is not satisfied with an assessment, a refund order etc. he can file an appeal to the Appellate Assistant Commissioner (now Deputy Commissioner (Appeals). The Act also provides for appeal by the assessee direct to the Commissioner (Appeals).

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

A taxpayer can approach the Commissioner of Income Tax to revise an order passed by an assessing officer or by an Appellate Assistant Commissioner within one year from the date of such orders. The Commissioner can also take up for revision an order which, in his view, is prejudicial to the interest of revenue.

(1) Income Tax including Corporation Tax

(a) Particulars of Income Tax appeals as on 31 March 1994 were as follows:

No. of income tax appeals pending with	
(a) Deputy Commissioner(Appeals)	93,504
(b) Commissioner of Income Tax (Appeals)	1,73,178
Total	2,66,682

(b)(i) Details of appeals pending with Deputy Commissioners (Appeals) upto 1993-94 were as under:

Appeals for disposal	Disposals	Closing balance
150629	57125	93504

(ii) Year-wise break-up of high demand (more than Rs. 1 lakh) appeals pending with Deputy Commissioners (Appeals) at the end of the year 1993-94 with reference to their year of institution was not furnished by the Ministry of Finance. However, the position as on 31 March 1994, was as under:

Opening Balance	Disposal	Balance
6272	3061	3211

(c)(i) Details of appeals pending with Commisioners of Income Tax (Appeals) at the end of 1993-94 were as under :

Opening balance	Additions	Disposal	Balance
1,64,557	97,235	88,614	1,73,178

(c)(ii) Year wise break-up of high demand (more than Rs. 1 lakh) appeals with Commissioners of Income Tax (Appeals) at the end of the year 1993-94 with reference to their year of institution was not furnished by the Ministry of Finance.

(c)(iii) Details regarding appeals, references and writs in Supreme Court, High Court and Income Tax Appellate Tribunal were as under:

	No. for Disposal	Disposal	Pending
Supreme Court	6,055	17	6,038
High Court	54,127	952	53,175
Income Tax Appellate Tribunal	1,26,747	5,819	1,20,928
Total	1,86,929	6,788	1,80,141

(2) Other Direct Taxes

Particulars of wealth tax and gift tax appeals pending with Deputy Commissioner (Appeals) and year wise pendency of high demand appeals (more than Rs.50,000) were not furnished by the Ministry of Finance.

Reliefs and refunds

2.10 Where the amount of tax paid exceeds the amount of tax payable, the assessee is entitled to a refund of the excess. If the refund is not granted by the department within three months from the end of the month in which the claim is made, simple interest at the prescribed rate becomes payable to the assessee on the amount of such refund (vide Section 237 read with Section 243 of the Income Tax Act). Information regarding the amount of relief and refunds given was not furnished by the Ministry of Finance, though called for.

Interest

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

Information relating to interest paid on refunds by Government was not furnished by the Ministry of Finance, though called for.

Cases settled by Settlement Commission

2.12 Under the provisions of the Income Tax Act, 1961, and the Wealth Tax Act, 1957, an assessee may at any stage of a case relating to him make an application to the Settlement Commission to have the case settled. The powers and procedures of the Settlement Commission are specified in the Act. Every order of Settlement passed by the Settlement Commission is conclusive as to the matter stated therein.

The number of cases settled by the Settlement Commission during the last five years was as under:

(i) Income Tax

Financial year	No. of cases for disposal	No. of cases disposed of	Percentage of cases disposed	No. of cases pending
1989-90	1993	355	17.81	1638
1990-91	2000	480	24.00	1520
1991-92	2014	457	22.69	1557
1992-93	2115	342	16.17	1773
1993-94	2439	403	16.52	2036

(ii) Wealth Tax

Financial year	No. of cases for disposal	No. of cases disposed of	Percentage of cases disposed	No. of cases pending
1989-90	537	92	17.13	445
1990-91	538	136	25.28	402
1991-92	479	166	34.66	313
1992-93	420	99	23.57	321
1993-94	385	52	13.51	333

(iii) No. of cases pending for admission before Settlement Commission as on 31.3.1994 825

(iv) No. of cases held up with Settlement Commission for want of comments of the department. 74

(v) Year-wise position of tax determined (including interest and penalty) in cases settled by Settlement Commission is given in Appendix III.

Penalties and prosecutions

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

(i) Income Tax and Corporation Tax

(a) Penalty proceedings initiated, disposed of and pending for each of the three years ending 1993-94 were as under:

Year	Opening balance	Additions	Total	Disposals	Closing balance
1991-92	1,92,597	70,723	2,63,320	96,878	1,66,442
1992-93	1,66,442	64,142	2,30,584	64,238	1,66,346
1993-94	1,66,346	1,49,306	3,15,652	83,491	2,32,161

(b) Details regarding prosecutions launched, convictions/ compoundings and acquittals for the three years ending 1993-94 were as under:

Year	Complaints filed during the year			Convictions	Compounding	Acquittal	Total
	For tax evasion	Others	Total				
1991-92	1234	1214	2448	165	153	169	487
1992-93	808	683	1491	102	391	808	1301
1993-94	552	389	941	57	507	570	1134

(c) Details relating to penalties regarding work load, disposal, pendency and imposed for the year 1993-94 are as follows :

Nature of penalty	Work Load	Disposal	Balance
For Concealment	1,26,029	26,527	99,502
Others	1,89,623	56,964	1,32,659
Total	3,15,652	83,491	2,32,161

Analysis of Pendency

Particulars	Less than 6 months	More than 6 months
For concealment	36,236	63,266
Others	41,771	90,888

Penalties imposed

(in crores of Rupees)

Particulars	No. of cases	Amount
For concealment	11,370	92.73
Others	27,802	55.70

Details of year wise pendency of penalties and composition money levied, collected and pending upto the year 1993-94 were not furnished by the Ministry of Finance.

Other Direct Taxes

(ii)(a) Penalty proceedings initiated, disposed of and pending for each of the three years ending 1993-94 are given below:

Year	Opening balance	Additions	Disposal	Closing balance
1991-92	49,029	16,735	21,328	44,436
1992-93	44,436	10,842	15,173	40,105
1993-94	40,105	27,310	13,896	53,519

(b) Details regarding prosecutions launched, convictions obtained and cases pending in courts of law regarding other direct taxes for the last three years were not furnished by the Ministry of Finance.

Searches and Seizures

2.14 Sections 132, 132-A and 132-B of the Income Tax Act, 1961 provide for search and seizure operations. A search has to be authorised by a Director of Income Tax, Commissioner of Income Tax or a specified Deputy Director of Income Tax or a Deputy Commissioner of Income Tax. Where any money, bullion, jewellery or other valuable article or thing is seized, the Assessing Officer has, after necessary investigations, to make an order with the approval of the Deputy Commissioner of Income Tax within 120 days of the seizures, estimating the undisclosed income in a summary manner on the basis of the material available with him and calculating the amount of tax on the income so estimated, specifying the amount that will be required to satisfy any existing liability, and retain in his custody such assets as are, in his opinion, sufficient to satisfy the aggregate of the tax demands and forthwith release the remaining portion, if any, of the assets to the persons from whose custody they were seized. The books of accounts and other documents cannot be retained by the authorised officer for more than 180 days from the date of seizure unless the Commissioner approved of the retention for longer period.

(i) The number of cases in which searches and seizures were conducted for the three years ending 1991-92 to 1993-94 were as under:

Year	Total No. of searches and seizures conducted	Value of assets seized (Rs. in Crores)
1991-92	3468	179.85
1992-93	4777	384.02
1993-94	5026	390.46

(ii)(a) Particulars of income determined, tax levied, balance tax outstanding after adjustment of value of assets retained on final assessment for the three years ending 1993-94 were as follows:

(Rupees in crores)

Year	No.of cases where final assessments were completed	Income determined	Demand raised			Demand adjusted out of retained assets	Balance pending recovery		
			Tax	Penalty	Total		Tax	Penalty	Total
1991-92	3751	3,674.29	2,077.29	261.94	2,339.24	366.47	1,712.61	260.14	1,972.75
1992-93	3412	623.94	289.79	12.97	302.76	191.63	98.61	12.51	111.12
1993-94	Information was not furnished by the Ministry of Finance, though called for								

(b) The number of cases of prosecutions launched, compounded and convictions obtained for the three years ending 1993-94 were as under:

Year	No.of prosecutions launched			No.of cases compounded	No.of cases in which convictions were obtained	No.of cases pending
	Opening balance	During the year	Total			
1991-92	17037	725	17762	154	67	17541
1992-93	17541	319	17860	118	472	17270
1993-94	17270	941	18211	507	57	17647

(c) Particulars of cases of assets returned, interest paid and cases pending for three years ending 1993-94 were as under:

Year	No.of cases where assets were due for return			No.of cases where assets returned	No.of cases where interest paid during the year	Balance cases pending
	Opening balance	Added during the year	Total			
1991-92	1443	392	1835	1098	--	737
1992-93	737	178	915	145	3	770
1993-94	Information was not furnished by the Ministry of Finance though called for.					

Survey

2.15(i) Number of cases where the powers of survey (other than those relating to ostentatious expenditure) were exercised for the three years ending 1993-94 as below.

Year	No. of premises surveyed under section 133A(1)	under section 133B
1991-92	3,566	9,93,963
1992-93	6,173	10,87,560
1993-94	6,329	1,14,601*

(ii) Number of cases where evidence about ostentatious expenditure was collected under Section 133A(5).

Year	No. of cases
1991-92	647
1992-93	664
1993-94	487

Purchase by Central Government of immovable properties in certain cases of transfer

2.16 With a view to countering tax evasion and to curb the circulation of black money in real estate transactions, a new Chapter XXC was inserted in the Income Tax Act, 1961, with effect from 1st October 1986 empowering the Central Government to purchase immovable properties in certain cases of transfer. To begin with, these provisions were made applicable to properties proposed to be transferred for an apparent consideration exceeding Rs.10 lakhs in each case in the metropolitan cities of Bombay, Calcutta, Delhi and Madras. It has been extended to 24 more cities upto 1 April 1991.

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* Information is provisional as conveyed by the Ministry of Finance.

During the financial year ended March 1994 details of properties purchased by the Central Government were as under:

	Calcutta	Madras	Ahmedabad	Delhi	Bombay	Total
(i)No. of statements received in Form 37-I	83	1006	1869	1191	2826	6975
(ii)No. of properties purchased	10	3	6	13	46	78
(iii) Value of properties purchased (Rs. in lakhs)	546	111	299	797	10732	12485
(iv)No. of properties where consideration exceeds Rs.50 lakhs	4	1	1	5	31	42

Functioning of Valuation Cells

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

(i) No. of valuation units/districts:

Year	No. of valuation units	No. of valuation districts
1989-90	70	13
1990-91	70	13
1991-92	70	13
1992-93	65	12
1993-94	64	12

(ii) No. of cases referred to valuation cells, disposed of and pending at the end of the each of three years ending 1993-94

	Year	Opening balance	No. of cases referred during the year	Disposal	Closing balance
(a) Income Tax	1991-92	958	8,426	8,445	939
	1992-93	894	7,832	7,905	821
	1993-94	1021	7,227	7,324	924
(b) Other Direct Taxes#	1991-92	1825	5713	6152	1386
	1992-93	1386	4067	4517	936
	1993-94	936	3338	3367	907

Revenue demands written off by the department

2.18* Details regarding amount written off for the year 1993-94 as furnished by the Ministry of Finance, were as under**

No. of cases Identified involving arrear demand of Rs. 10,000/- and below where recovery certificates were issued upto 31.3.79			(Amount in Rs. '000) Details of cases considered for write off during the year.		
No. of assessees	No. of entries	Total Amount involved(Rs.)	No. of assessees	No. of entries	Total amount involved(Rs.)
1.	2.	3.	4.	5.	6.
33305	41417	65521	17684	19498	18379

Details of cases written off during the year			Details of Balance of cases to be written - off		
No. of assessees	No. of entries	Total amount written-off (Rs.)	No. of assessees (1-7)	No. of entries (2-8)	Total amount for write off (Rs.)(3-9)
7.	8.	9.	10.	11.	12.
21774	24186	22092	11531	17231	43429

\# includes Wealth tax, gift tax and Estate Duty, Details are in Appendix IV

* Information as indicated in the proforma given in Appendix V was not furnished by the Ministry of Finance, though called for.

** The information is still awaited from the CCIT/CIT Jaipur, Allahbad, Tamil Nadu - II, Amritsar, Patna, Pune & Nasik, according to the Ministry of Finance.

Chapter 3

System Appraisal

3.1 Survey Operations under the Income Tax Act, 1961.

Introductory

3.1.1 Prevention of tax evasion and widening of tax base are the two most important attributes of a good tax administration. For the purpose of identifying new tax payers and for detecting tax evasion in the cases of existing assessees under the Income Tax Act, 1961 the department has been undertaking surveys.

The Government, in March 1970, appointed the Direct Taxes Enquiry Committee (Wanchoo Committee) to examine and suggest legal and administrative measures for countering evasion and avoidance of direct taxes. The Committee was of the opinion (December 1971) that an efficient machinery for collection, collation and dissemination of information is a sine qua non for an efficient tax administration and recommended that the Special Investigation Branch (SIB) should be made responsible to conduct adequate number of surveys to ensure that all persons having taxable income/wealth within their respective jurisdiction are brought on the registers of the department. Accordingly, looking into the need to expand the tax base, increase revenue and tackle the problem of unreported incomes, a large number of posts of Officers, Inspectors and other staff were sanctioned for this purpose, from the financial year 1986-87 onwards. The number of assessees which was 32.08 lakhs in 1971-72 has gone up to 93.07 lakhs in 1992-93. While in percentage terms the growth looks substantial, it has to be kept in view that in the meanwhile the number of persons gainfully employed in various kinds of income earning activities has also gone up similarly. While the Ministry attributes (Decemnber 1994) a significant part of the increase to surveys and their ripple effect, the effect has not been quantified. It also cannot be overlooked that many of them would have come under the tax net of their own volition. An attempt has been made by Audit in this review report to analyse the efficacy of survey operations to bring more assessees in the tax net and also generate additional revenue.

3.1

Surveys under the Income Tax Act are carried out under sections 133 A and 133 B of the Act. Surveys under section 133A are conducted for detecting evasion by existing assessees by keeping a watch over the business environment, collecting material facts in respect of specific cases and making enquiries about ostentatious expenditure on occasions such as marriage, birthdays, anniversaries etc. Survey under section 133B, introduced by the Finance Act, 1986, is done to identify and detect new and potential tax payers.

Organisational set up

3.1.2 The Central Information Branch functioning in the Investigation Wing of the department collects information from various internal and external sources, and passes these on to the assessing officers after verification through the Commissioners of Income-Tax for taking appropriate action. This process helps in locating new tax payers and also detecting tax evasion in the cases of existing assessees.

The work of administering the survey operations of Income Tax Act, 1961, is overseen by Member (Investigation) in the Central Board of Direct Taxes. The authorities empowered to carry out survey operations are the Deputy Commissioner, the Assistant Director, the Assessing Officer and the Inspector of Income Tax duly authorised for the purpose. These authorities act under the supervision and control of Chief Commissioner, the Director General or the Director of Income Tax, as the case may be. The Central Information Branch (CIB) functions under the Director of Income Tax (Investigation)

Law and procedure

Survey under section 133A

3.1.3(1) With a view to preventing tax evasion and widen the tax base, Finance Act, 1964, inserted a new section 133A with effect from 1 April 1964 conferring powers on the Income Tax authorities to conduct surveys. A Deputy Commissioner, an Assistant Director, an Assessing Officer and an Inspector of Income Tax duly authorised, is empowered to enter any place within the limits of the area assigned to him or any place occupied by any person in respect of whom he exercises jurisdiction. The

power to enter is limited to the place where business or profession is carried on or where books of account or other documents or any cash or stock or other valuable article or thing relating to the business or profession are kept. They are empowered to place marks of identification on the books of accounts or other documents inspected and can take extracts thereof but are not entitled to remove cash, stock or other valuable articles or things.

Survey under section 133A(5)

3.1.3(2) The Taxation Laws Amendment Act, 1975 enlarged the scope and powers of survey. Under section 133A(5), Income Tax authorities were empowered to require any person to furnish such information as may be necessary to work out the nature and scale of expenditure incurred by an assessee in connection with any function, ceremony or event. The purpose of the said survey is to have first hand information, as at a later point of time, it may be difficult for the department to prove the amount of expenditure incurred. During such proceedings, statements of the assessee as well as other persons, who might have information or material in their possession, can be recorded. Such statements can be used in evidence in any proceedings under this Act. Enquiries can be made from decorators, tent houses, caterers, hoteliers, photographers and such other persons. The purpose of the said survey is to curb wasteful expenditure which is usually met out of concealed income. The information so collected and statements so recorded have to be furnished to the assessee in the course of regular assessment proceedings.

Survey under section 133B

3.1.3(3) Finance Act, 1986 inserted this section with effect from May 1986 for conducting door to door survey. Income Tax authorities are empowered to enter any place where business or profession is carried on. The authorities can require a proprietor, employee or any other person who may at that time and place be attending or helping in carrying on such business/profession, to furnish such information as has been prescribed in Rule 112E and Form 45-D. It contains detailed information about the status and nature of business, books maintained, extent of investment etc. The Finance Act, 1986 also inserted a new section 272AA to provide for penalty extending upto Rs. 1000 for failure to comply with the provisions of Section 133B of the Act.

The Department had drawn up an Action Plan for this aspect of work for the period 1986-87 to 1989-90. Thereafter, a long term Action Plan for the financial years 1990-91 to 1993-94 was drawn up. The Action Plans give a codified list of heads of information. The Board specifies every year the particular codes to be taken up for extraction and verification. These codes can be varied according to local requirements. Field officers can also suggest new items for extraction and verification. The procedure for collection, collation and dissemination of information by the CIB has been laid down in Board's Instruction No. 1759 dated 11 June 1987.

Scope of the review

3.1.4 The insertion of sections 133A and 133B of the Act was aimed at detecting more assessees so as to broaden the tax base for mobilising additional revenue. This review is intended to evaluate the efficiency of the survey operations by scrutinizing relevant registers, records/reports with reference to the Action Plan, and to ascertain whether the legislative intent behind the insertion of the survey provisions in the Income Tax Act has been achieved or not and also to determine as to how far the department has been able to widen the tax net and mobilise additional revenue resources.

Constraints

3.1.5 Some of the key records relating to survey, especially survey reports sent by the Directorate of Investigation, alongwith Form 45-D to the assessing officers and records relating to receipts and disposal by the assessing officers, the staff deployed for survey operations and cost thereof as also CIB registers, were by and large not made available to Audit. These records indicate the extent of survey operations, their periodicity, the gain to revenue etc. and were, therefore, crucial for a proper evaluation of the efficacy of survey operations. The matter regarding non-furnishing of records was brought to the notice of the Board in January and April 1994. The Ministry has stated (December 1994) that the initial view that confidential folders and appraisal reports would not be made available to Audit was modified on November 29,1994 based on an assurance given to Public Accounts Committee in another case mentioned by Audit. However, as the instructions were issued very late, Audit had no option but to undertake the review based on the records made available to it. The results thereof are discussed in the following paragraphs.

Highlights

3.1.6(a) The Central Information Branch did not pass on 78 percent of the verified information to the assessing officers. Even in cases where information was passed on to the assessing officers, several instances were noticed where there was a failure to take action on the CIB information. [Para 3.1.7]

(b) From 37.78 lakh survey operations undertaken during the period 1989-90 to 1992-93 for detection of new assessees, only 23.69 lakh assessees could be detected. Further, even in these cases gains to revenue were nominal, either because new assessees filed returns of income which were below the taxable limit, or they could explain their income/wealth over a passage of time or the department failed to reopen assessments of existing assessees. [Para 3.1.8 and 3.1.9]

(c) Follow up action in most cases was tardy. The survey reports and material were either not made use of, or the cases were not diligently followed up so as to result in any substantial revenue yield. [Para 3.1.8(2)]

(d) Although survey operations are recognised to be a potent tool for aiding the tax administrator in the discharge of his duties, it was revealed that even in cases where survey reports had indicated large tax evasion no priority was accorded to finalisation of these cases. [Para 3.1.8(2)(iii)(c)]

(e) Although the Act provides for levy of penalty in cases of violations of survey provisions, this was often not made use of. This defeated the objective of giving a deterrent effect through penal provisions. [Para 3.1.8(2)(iii)(d)]

(f) The departmental registers and records were either defectively maintained or not maintained at all. As such, it could not be established whether revenue gains were commensurate with the efforts put in and whether the provisions had been properly implemented in tune with the legislative intent. [Para 3.1.10]

Working of the Central Information Branch (CIB)

3.1.7 Surveys are conducted based on information collected by different agencies. Central Information Branch (CIB) is one such agency which is required to collect information from external and internal sources and pass on the same to the assessing officers. The procedure for collection, collation and dissemination of information by the CIB has been laid down in Board's instruction No. 1759 of 11 June 1987.

Collection, collation and dissemination of information

3.1.7(1) The position of number of items of information received, verified and passed on to the Investigation wing during 1989-90 to 1992-93 as intimated by the Ministry is as follows:

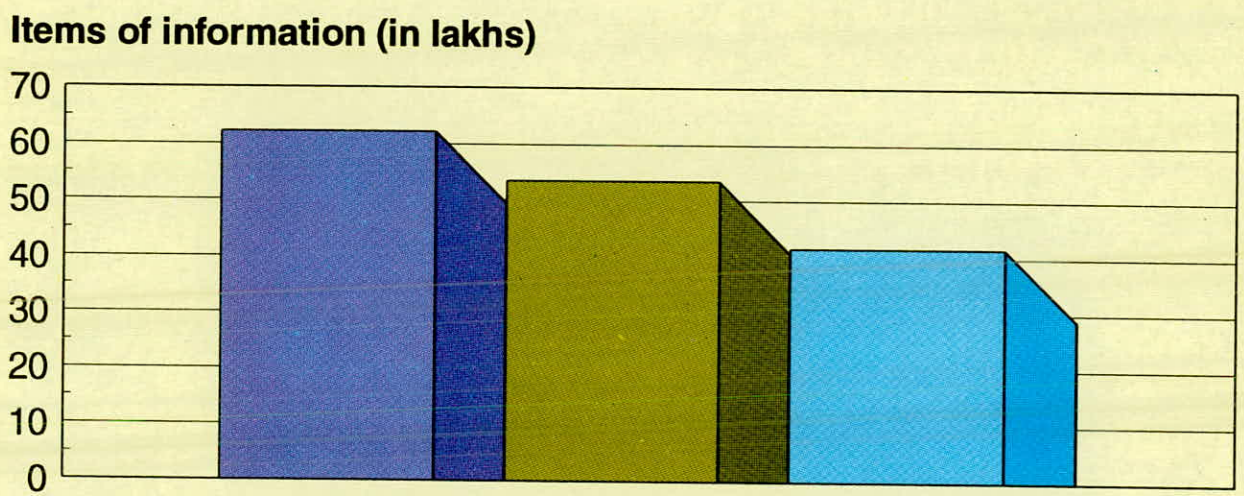
	(In lakhs)
Items of information collected	62.17
Items of information verified	53.48
Items of information passed on to the assessing officers	11.90

Thus around 78 percent of the verified information was not passed on to the assessing officers. Even in the verified items of information passed on by the Investigation Wing to the assessing officers, discrepancies were noticed as detailed below:

Name of charge	No. of items of verified information reportedly passed on to assessing officers by the Investigation Wing	No. of items of verified information actually received by the assessing officers	Percentage of items not received
	(figures in lakhs)		
Delhi	1.18	0.23	88
Gujarat	0.57	0.20	65
Orissa	1.10	0.03	97

Inspite of the wide gap in receipt of information no system of reconciliation of the discrepancies was found to have existed in any charge. Had there been such a system of reconciliation, it would have enabled the department to detect these discrepancies and take necessary action in the remaining cases.

ACTION ON INFORMATION COLLECTED BY CENTRAL INFORMATION BRANCH (1989-93)



	Items of information
Collected	62.17
Verified	53.48
Not sent to assessing units	41.58

Omission to take follow up action on CIB information

3.1.7(2) As and when the Central Information Branch comes to the conclusion that action is required to be taken by the assessing officers, information is forwarded to the latter after recording their findings and indicating the action to be taken. The information is also to be entered in the 'Register of verification of information in Central Information Branch' and necessary follow up action is required to be taken. In many cases, no follow up action was found to have been taken by the assessing officers on the CIB information. The Ministry has stated (December 1994) that the assessing officers are not bound by suggestions of CIB and they have to make assessment on the basis of available information and enquiries conducted by them. It is, however, felt that there should be sufficient reasons which should also be available on records for the assessing officer to disregard the suggestion of CIB. This was not so in many cases noticed in audit. Some illustrative cases are cited below:

(i) In Assam charge, 19 new cases (verification of information by CIB) were forwarded during 1989-90 and 1990-91 to the assessing officers but no case could be traced from the records of the assessing officers.

(ii) In Maharashtra charge, an assessee made an investment of Rs. 4.25 lakhs in a new flat in July 1987. This information was passed on by the C.I.B. in September 1991 to the assessing officer with specific comments "No details were enclosed with return for assessment year 1988-89. Hence action proposed". The relevant assessment was made under section 143(1) in January 1990 for taxable salary income of Rs. 31,210. The assessee had not returned any income from house property but stated that he had sold a flat for Rs. 1.80 lakhs and invested Rs. 1.78 lakhs in a new flat. The assessing officer had not taken any action on the basis of the C.I.B. information. There was nothing in the record to indicate that assessing officer was aware of the information passed on by C.I.B. Thus, income of Rs. 2.47 lakhs remained uninvestigated.

In the same charge, in two cases, the differences between sales disclosed to the Sales Tax Department and the sales shown in the accounts maintained by the assessees were intimated to the respective range Deputy

Commissioners in July 1992. In the first case the return for the relevant assessment year had been accepted under section 143(1)(a) and the suppressed sale of Rs. 3.77 lakhs escaped assessment involving short levy of tax of Rs.95,130 in the case of the firm alone. In the other case, the party was not assessed to tax at all. In both the cases the assessing officers were evidently unaware of the intimations from C.I.B.

Further, in Maharashtra charge, purchase of motor cars by four closely held companies was reported to the respective Deputy Commissioners in February 1990 and March 1990 for the reason that they were not filing the wealth tax returns. Verification of records revealed that necessary follow up action had not been taken in these 4 cases and the wealth represented by value of cars aggregating Rs. 9.86 lakhs had escaped assessment involving non-levy of tax of Rs. 43,160 upto assessment year 1992-93. In addition, the assessees were liable to penalty of Rs. 52,160, which was not levied.

(iii) In Gujarat charge, information in 832 cases received by the I.T.O. Survey cum CIB, Ahmedabad in February 1993, relating to purchase of sugar worth Rs. 5.33 crores could not be verified as complete addresses of the purchasers were not available. Further, in Baroda, information collected from 61 jewellers regarding sale/purchase of jewellery above Rs. 25,000, though selected for verification during the year 1989-90 had not been verified. It was filed in March 1990 without assigning reasons. Similarly, in Surat, information relating to transport, supply or service contract etc. for the year 1989-90 was received from 'Krishak Bharti Cooperative limited'. and enquiry letters were issued in January 1991. Replies received were however filed with the remarks 'Existing assessees.....P.A.No...../assessed in .....". The information was neither verified nor passed on to the assessing officers. Further, information relating to deposits above Rs. 50,000 was collected between November 1989 and February 1993 in 590 cases involving deposits of Rs. 2.95 crores. No action was taken except issuing reminders between August 1992 and February 1993.

Conducting of surveys

Number of surveys conducted and additional revenue realised

3.1.8(1) The survey records as per information furnished by the Ministry revealed that though about 21,770 surveys under section 133A(1) were conducted during the years 1989-90 to 1992-93, the additional revenue realised on this account could not be ascertained as the details thereof have not been recorded separately except in two charges viz Karnataka and West Bengal. In Karnataka charge, in assessment year 1989-90, out of the 1830 surveys conducted during the four year period between 1989-90 to 1992-93, additional revenue of Rs. 33.81 lakhs could be raised in 13 cases only. Similarly, in West Bengal charge, out of 407 surveys conducted during the period of four years, in 73 cases where assessments were completed, revenue of Rs. 47,000 only could be raised in 3 cases in the years 1991-92 and 1992-93.

Similarly, as per information furnished by the Ministry to Audit, 3,118 surveys were conducted under section 133A(5) but additional revenue raised on account of these surveys could not be ascertained, except in three charges, as the same was either not recorded separately or was not made available to Audit. In Andhra Pradesh, Rajasthan and Bihar charges, in 254 surveys conducted additional revenue of Rs.24.16 lakhs only was raised during 1989-90 to 1992-93.

According to the statistics furnished by the Ministry of Finance to the Standing Committee on Finance (1994-95), 10th Lok Sabha, the number of surveys conducted under section 133B during the period 1989-90 to 1992-93 and of new assessees added/detected was as follows:

	(In lakhs)
(1) Number of surveys conducted	37.78
(2) Number of new assessees added/ detected	23.69

The Department does not have a system of recording the new assessees added/detected as a result of surveys and consequently no correlation can be established between the

figures given at 1 and 2 above. This was also commented upon adversely by the Standing Committee on Finance (1994-95), Tenth Lok Sabha in its Eighth Report (August 1994). The Ministry has now informed (December 1994) that consequent to the recommendations of the Standing Committee, the proforma for statistics on survey and new assessees has since been modified with effect from August 1994 to indicate separately the number of new assessees detected on account of surveys. The Committee also observed that the Department has laid more emphasis on completion of quantitative targets for conducting surveys than on the qualitative aspects and results of such surveys. Many of the assessees would have filed returns of income on their own. The success rate of survey operations in adding new assessees during the years 1989-92 would at least appear to have been rather low.

Follow up action on surveys conducted

3.1.8(2) The success of survey operations depends on effective utilisation of the information gathered during the surveys, in assessments. Follow up action taken in most of the charges could not be ascertained as the relevant records/documents were not made available to audit. However, from the records made available to Audit cases of non-utilisation of such information were noticed. A few cases are discussed below:

Surveys under section 133 A(1)

(i)(a) In Kerala charge, information gathered during the course of survey was not utilised in 5 cases in the assessment of assessees concerned leading to non-assessment of income of Rs. 31.50 lakhs. For instance, in one case survey was conducted in March 1992 and information regarding concealment of income of Rs. 10 lakhs relating to assessment years 1991-92 and 1992-93 was passed on to assessing officer in April 1992. However, this was not made use of in the assessments made in January and February 1994 respectively. In another case, a firm agreed during survey to file a revised return of income for the assessment year 1989-90 enhancing income by Rs. 10 lakhs, but no return was filed.

(b) In Maharashtra charge, in two cases of a company and a firm, neither the assessees had returned the income aggregating Rs. 12.65 lakhs disclosed during survey operations nor was the

assessing officer aware of the survey action. Thus no action had been taken to bring to tax the income disclosed in the survey operation involving short levy of tax of Rs. 5.48 lakhs in both the cases. In another case, during survey operations in September 1990 concealment of Rs. 20.46 lakhs was reported, calculated at 12.26 per cent of the hawala sales amounting to Rs. 1.54 crores made by a firm for the period relevant to assessment years 1988-89 to 1991-92 including brokerage of Rs. 1.54 lakhs. The survey report was forwarded to the assessing officer in November 1990. However, in the assessment for assessment year 1990-91 completed in March 1993 after scrutiny, an addition of Rs. 9.82 lakhs only was made. The assessments for the years 1988-89 and 1989-90 were completed in a summary manner accepting the returned income and assessment for assessment year 1991-92 was completed after scrutiny without any addition to income. The assessee had also not declared the income disclosed during the survey. The assessments were also not reopened by the assessing officer. Thus the income disclosed amounting to Rs. 10.64 lakhs had escaped assessment resulting in short levy of tax of Rs. 2.05 lakhs in the hands of the firm alone. In yet another case, in a survey conducted in July 1992, an individual dealing in gold and diamond jewellery surrendered a sum of Rs. 5.07 lakhs on account of unaccounted income liable to be taxed in assessment years 1993-94, assessment of which was yet to be completed. The assessee also owned two shop premises in prime locations in Bombay. The survey report was forwarded to the range Deputy Commissioner in September 1992 specifically recommending verification of the source of investment in these shops. Assessments for assessment years 1990-91 and 1991-92 were completed after scrutiny in December 1992 and February 1994 i.e., after the survey report but there was no mention in assessment orders about the survey operations. The assessee had also declared an amount aggregating Rs. 7.69 lakhs on account of income from lotteries from assessment years 1989-90 to 1991-92 but there was no indication that either the survey unit or the assessing officer had investigated the genuineness of the investments.

In Tamil Nadu charge, in 4 cases, omission to take follow up action or taking partial action only resulted in non assessment of income of

Rs. 27.56 lakhs. An addition of Rs. 4.92 lakhs could only be made in cases where partial action was taken.

Surveys under section 133A(5)

(ii) The Central Board of Direct Taxes in November 1990 emphasised the need to make more effective and frequent use of provisions of section 133A(5) and a list of functions/ceremonies and events had been spelt out to be covered under section 133(A)(5). However, several cases indicating lack of follow up action in these surveys were noticed in audit. For instance in Maharashtra charge, in 6 cases no income tax/wealth tax proceedings were initiated by the assessing officers though the amount of expenditure aggregating Rs. 62.21 lakhs was admitted by the assessees themselves. Similarly, in Gujarat charge out of estimated expenditure of Rs. 62.62 lakhs in five cases, Rs. 11,200 only could be added back in one. The remaining cases were either not pursued by the department or the amounts disclosed were accepted by the assessing officer without further probe. In Assam charge, 4 cases were forwarded by the range Deputy Commissioner to the assessing officers in September 1992 but the receipt of cases and action taken thereon were not available from the records.

Two more illustrative cases of inadequate follow up action on survey reports are cited below:

(a) In Maharashtra charge, a survey was conducted after a marriage in December 1990 and the survey report was forwarded in March 1991 to the assessing officer where the uncle and guardian of the bridegroom were reportedly assessed. The assessing officer concerned had conducted enquiries and had accepted the assessee's contention that the total expenditure of Rs. 3.74 lakhs in the marriage was incurred by the bridegroom himself and the assessee had spent no amount. Thereafter, the survey report with enclosures was forwarded in October 1991 to the assessing officer where the bridegroom was assessed. However, enquiries by Audit revealed that the person was not assessed by that ward and the assessing officer was not aware of any such survey report. No action resulted from this survey report.

(b) In Gujarat charge, the expenditure incurred in a marriage held in December 1990, was estimated at Rs. 6.30 lakhs and the appraisal report was sent to the concerned assessing officer in March/April 1991. Audit scrutiny revealed that the return of income for the relevant assessment year was not filed with that assessing officer but it was filed with another assessing officer. The first assessing officer did not transfer the appraisal report to the second assessing officer and the latter was not aware of survey under section 133A(5). No action had thus been taken on the appraisal report.

Survey under section 133B

(iii) A scrutiny of the survey records maintained by the Deputy Director/Commissioners of Income tax and assessing circles/wards revealed:

Delay in submission/ forwarding of survey reports to the assessing officers.

(a) Inspectors deputed for survey work are required to prepare a summary of the work done during the period on the basis of entries in the area register. A copy of the summary together with the completed forms 45-D is required to be handed over to the officer authorising the survey. In Rajasthan, West Bengal, Assam, Gujarat, Kerala, Tamil Nadu and Maharashtra charges, it was noticed that in most of the cases no uniform procedure was followed with regard to issue and collection of information in Form 45-D which though distributed during the course of survey were not received back duly completed. No further action by way of reminders or other follow up action was indicated in the reports.

In Madhya Pradesh charge, it was noticed that 51 survey reports were submitted by the Inspectors after a delay of one to six months. In Delhi charge, in 6 units, survey reports were not submitted by the Inspectors to the concerned officers.

Further, the survey reports and Form 45-D are required to be sent by the survey unit to the assessing officers to enable them to take follow up action. This report is prepared by the officer authorising the survey after the receipt of Inspectors' diary alongwith Form 45-D. After exercising scrutiny of the

diaries, cases having revenue potential are selected and are required to be sent every month to the assessing officers concerned with a list of such cases in duplicate. One copy of the list is required to be sent to the Deputy Commissioner of Income Tax for monitoring and follow up.

Test check of records revealed that in Andhra Pradesh, Punjab, Madhya Pradesh, Assam, Delhi, Uttar Pradesh and Gujarat charges there were delays ranging from one month to 27 months in transmitting 12,667 survey reports by the Investigation Wing/Survey units to the concerned assessing officers.

In Gujarat charge, Form 45-D and survey reports were not being linked with the returns of income wherever filed. Further, the assessments were completed in summary manner rendering the whole exercise fruitless. In some cases entries in the register were closed and Form 45-D filed on the basis of assessee's replies that returns of income had been or would be filed. Some cases were closed as they pertained to other wards. No attempts were made to verify the correctness of the assessee's reply or to transfer the form to the other wards. Similarly, in some other cases assessees' replies that they did not have taxable income were accepted without verification and cases closed.

Non-utilisation of survey reports under section 133 B

(b) One of the objectives of surveys is to unearth black money and to book unaccounted/ unexplained expenditure. The review revealed that there was hardly any significant impact on unearthing black money as a result of these surveys. Only a fraction of estimated expenditure got included as income during assessments, as the assessees could, in most cases, get away by explaining the expenditure or the source of income. In some cases, the assessees themselves came forward with the amount of expenditure incurred out of unaccounted income and these were accepted without further probe. Thus very few effective assessees could be added to the number of assessees, resulting in little gain to revenue.

A few illustrative cases are discussed below:

(i) In Haryana charge, in 21 cases involving suspected concealment of income of Rs. 221.68 lakhs, no action was initiated by the assessing officer on receipt of information from the Investigation wing although a period of 1 to 3 years had already elapsed. Further, in 9 cases

involving concealment of income/wealth amounting to Rs. 348.44 lakhs, notices were issued during April 1992 to March 1993 but neither the assessees filed the returns nor any further action was taken by the assessing officers.

(ii) In Maharashtra charge, no follow up action was taken by the assessing officers in 18 cases on the information forwarded to them regarding investment in flats/shops, purchase of new cars, club membership, demurrage charges etc. involving escapement of income aggregating Rs.52.72 lakhs. For instance, an assessee company had invested Rs. 16.93 lakhs in four flats in January and March 1991. This information was passed on by the CIB to the assessing officer in May 1992 to investigate the source of investment, as the assessee company had not filed the details of investment. There was nothing on record to indicate that assessing officer was aware of the information passed on by the CIB. For the years 1989-90 to 1992-93 the CIB register was not maintained and the assessee's name did not appear in the register maintained for the subsequent years.

(iii) In Assam charge, in 522 new cases, verification of information by CIB/Form 45D were forwarded during 1989-90 and 1990-91 to the assessing officers by the Deputy Commissioner but neither the receipt of the cases by the assessing officers could be traced from their records nor was there indication of any action taken to issue notices etc.

(iv) In Karnataka charge, 1,36,960 Form 45-D were distributed by the Investigation Wing during the years 1991-92 to 1992-93 but only 7778 forms were reported to have been received by the assessing officers. Action taken in the remaining cases was not intimated to Audit.

(v) In Punjab charge, 32 cases involving concealed income of Rs. 158.94 lakhs were received by the Commissioner of Income Tax, Patiala through the Investigation wing, Chandigarh, who sent these cases between January 1990 to February 1993 to the range Deputy Commissioners for taking necessary action. No action was taken to finalise these cases till May 1994. In Tamil Nadu charge, during December 1992 to February 1993, 55 new cases were reported by the Investigation Wing, Coimbatore, to the assessing officer, Salem, for follow up action. However, none of the cases was found entered in the assessing

officers' control register. There was no evidence of issue of notice calling for return of income in respect of these cases. In Gujarat charge, out of 2876 Form 45-D received by the assessing officers, no follow up action was taken in 2178 forms. In some cases the forms were not traceable.

(vi) In West Bengal charge, while forwarding the information collected in form 45D, in 40 cases, the Inspectors suggested in a number of cases assessment for two or more consecutive assessment years as there was revenue potential for each of the years. However, notices were issued and assessment was done only for one assessment year instead of all the assessment years as suggested. In the same charge, in respect of six Commissioners of Income Tax in 27972 cases, survey cum C.I.B reports were not distributed to the assessing officers by the range Deputy Commissioner. A test check of the undistributed survey reports revealed that these were cases of revenue potential as reported by the survey wing. For instance, in 91 cases the assessing officers did not take action on the said reports even though in many cases the persons reported upon had taxable income, as mentioned in the survey reports. In a number of cases where the assessing officers issued notices to the persons reported upon as a result of survey u/s 133B, the notices could not be served by the postal authority as the persons were not traceable at the addresses given by them. It was noticed that the assessing officers did not take any further action on these cases.

The Ministry has informed (December 1994) that since last year the work of surveys under Section 133B has been entrusted to Chief Commissioner of Income Tax and it is hoped that the difficulties concerning follow-up of survey reports would be surmounted with this change.

Low priority accorded even to high value cases

(c)(i) In Punjab charge, two high revenue potential cases involving concealed income of Rs. 59.24 lakhs detected as a result of CIB verification were reported in September 1993 by the Investigation Wing, Chandigarh, to the Commissioner of Income tax, Patiala, for further action by the assessing officers concerned. The information from CIB had not been forwarded to the concerned assessing officers till May 1994.

(ii) In Delhi charge, 22 cases involving surrender of Rs. 244.90 lakhs were sent by the Director (Survey) to the Commissioner of Income Tax. Two cases involving surrender of Rs. 37.80 lakhs were still under process though these were sent to the concerned officers in January/March 1992.

Omission to levy penalty for failure to comply with provisions of section 133B

(d) Section 272 AA of the Income Tax Act, 1961, provides that if a person fails to comply with the provisions of section 133B of the Act, he shall, on an order passed by the Deputy Commissioner/Asstt. Director or the assessing officer, pay by way of penalty, a sum which may extend to Rs. 1000.

A test check of the survey reports under section 133B revealed that in Punjab, Union Territory of Chandigarh, Orissa, Tamil Nadu, West Bengal, Kerala and Madhya Pradesh charges, in 3071 cases where the persons either refused to sign Form 45D or the same were not returned back duly completed, no penalty proceedings under section 272 AA were initiated for failure to comply with the provisions of section 133B. In Madhya Pradesh, Bihar, Haryana and Uttar Pradesh penalty of a sum of Rs. 1.99 lakhs in 243 cases was imposed.

Results of survey

3.1.9 It was observed from survey records in Maharashtra, Andhra Pradesh, Bihar, Haryana, Chandigarh, Orissa and Madhya Pradesh charges that out of about 3.56 lakhs new cases detected during the year 1989-90 to 1992-93, notices calling for the returns were issued in 0.51 lakh cases i.e. in 14.30 percent of the cases. In 1.04 lakhs cases, assessees filed the returns of income, including some assessees who might have filed the returns voluntarily and paid income tax aggregating Rs. 1178.76 lakhs. About 2850 assessees filed wealth tax returns and paid wealth tax amounting to Rs. 58.62 lakhs. About 36,770 of these assessees filed their returns showing income/wealth below taxable limits. In West Bengal, Uttar Pradesh, Assam, Gujarat, J&K, Karnataka and Delhi charges, out of about 2.13 lakhs new cases discovered, notices were found to have been issued in 71,000 cases only. Other details regarding the number of assessees who had filed the income/wealth returns and paid tax thereon were not available from records. In Punjab,

Rajasthan and Tamil Nadu charges, the details were either not maintained separately or the records were not made available.

Cases were noticed where though the follow up action was taken by the assessing officers the survey operations resulted in meagre or no gain to revenue. For instance, in Tamil Nadu charge, as a result of detection of fictitious deposit in survey operation in November 1988, an assessee had himself disclosed an amount of Rs.7.38 lakhs representing interest income thereon and undisclosed distributor's commission for the assessment years 1981-82 to 1988-89. The case was, however, discussed by the assessing officer with assessee's representative and proceedings were dropped merely recording that the assessment is not likely to result in enhancement of income.

Maintenance of records

3.1.10 The state of maintenance of various records is discussed below:

For survey operations under sections 133A(1) and 133A(5)

(i) As per para 4.19 of the Survey Manual published by the Director of Income Tax (RSP & PR), a survey register is required to be maintained in each circle/ward in Annexure "H". This contains columns for date of survey, name, permanent account number and address of premises surveyed, result of survey in brief, relevant assessment years, date on which survey report was sent to the Deputy Commissioner, revenue results etc. This register is required to be maintained in two parts, one for survey under section 133A(1) and the other for survey under section 133A(5). Entries in this register are required to be made immediately after conclusion of the survey. Entries are to be reviewed by the assessing officer every month while sending the monthly report on survey. This register is required to be scrutinised by the Deputy Commissioner/Commissioner in the course of inspection of the work of the assessing officers to see whether the survey provisions have been effectively and properly put to use and that findings during the survey have been duly followed up.

The review revealed that in Maharashtra, Andhra Pradesh, West Bengal, Assam, Rajasthan, Tamil Nadu, Delhi, Madhya Pradesh charges, this register was not maintained in several circles/wards or was defectively maintained as some important columns viz results of survey, revenue results were left blank. In Uttar Pradesh, Gujarat, Jammu and Kashmir, Kerala, Bihar, Karnataka, Chandigarh and Orissa charges

the registers were either not maintained or were not produced to Audit despite request.

For survey under section 133-B

(ii) The following major records are required to be maintained:

Area Directory

(a) According to para 5.16 of Survey Manual, an Area Directory in Annexure "M" is required to be maintained for each area covered by the survey. This is a comprehensive and permanent record of areas taken up for surveys with description of the area with a sketch pen giving important landmarks, door numbers or plot numbers, name of survey personnel, period and duration of survey etc,. This helps in avoiding repetitive surveys and improper programming and in achieving optimum results.

Inspector's Diary

(b) This diary is required to be maintained by each of the Inspectors who conducts the survey. It contains the details of survey conducted and Form 45-D issued and those received back completed etc. This is required to be submitted to the officer authorising the survey, for scrutiny and further action.

Survey Reports - Annexure "N"

(c) According to para 5.19 of Survey Manual, a statement of survey report under Section 133-B has to be maintained. This register contains columns for recording name, addresses of the premises surveyed, action suggested in the survey report, date of receipt of survey report by the assessing officer, action taken and revenue results etc. This is the key record to evaluate the efficiency of survey work done.

The review revealed that the Inspectors Diary was not being maintained in most of the charges except in some units in Punjab and Delhi charges. The Area Directory (Annexure 'M') was not maintained in Orissa, Karnataka, Chandigarh, Rajasthan, Madhya Pradesh charges. However, it was maintained in some wards/circles in Maharashtra, Uttar Pradesh, West Bengal, Assam and Gujarat charges. The registers were however, not produced to Audit in Bihar, Kerala and Andhra Pradesh charges. Further, survey reports in Annexure 'N' was found to have been partially maintained in some wards/circles of Uttar Pradesh, Madhya Pradesh, West Bengal, Assam and Gujarat charges whereas in some other charges this was not properly maintained. In Karnataka, Tamil Nadu, Delhi,

Bihar this record was not produced to Audit. In Jammu and Kashmir, Orissa, Chandigarh and Rajasthan it was not maintained in any of the wards/circles. In Assam, Tamil Nadu, Rajasthan, Uttar Pradesh, Orissa, Karnataka, West Bengal and Maharashtra charges, registers maintained by the assessing wards/circles were not periodically scrutinised by the Director/Deputy Director to ensure necessary follow up action. In the absence of these registers and the relevant information, it could not be ascertained whether the survey provisions have been effectively and properly implemented and whether findings during the survey have been duly followed up to yield revenue results. For instance, in Uttar Pradesh charge, in one circle the register maintained for 1989-90 showed 979 cases as having been received but in no case was action taken noted. Similarly, in the register for 1991-92 in some cases, notices were issued after delays ranging from 6 to 10 months. Similarly, in Assam charge, 19 new cases were forwarded during 1989-90 and 1990-91 to the concerned assessing officers by the range Deputy Commissioner for verification of information. However, neither the receipt of the cases by the assessing officers could be traced from their records nor any records/register were maintained by the assessing officer showing action taken in such cases.

Maintenance of Records in CIB

(iii) Under the revised procedure which was introduced in June 1987, the Board has prescribed the maintenance of three registers, as below:

(a) Register of information receipts in Central Information Branch

This register records all information collected by the branch according to the monetary limits fixed by the Director of Inspection (Investigation) and the items selected for verification.

(b) Register of verification of information received in Central Information Branch

The final outcome or results of the verification of the information together with the potential revenue involved is required to be entered in this register.

(c) Register of cases of action proposed by the Central Information Branch

This register which is required to be maintained by the Commissioner of Income Tax will indicate the monthly reports received from the Central Information Branch and the action taken thereon by the assessing officers.

These registers, if maintained properly, could give complete data regarding collection and utilisation of information from various sources. They would also facilitate a quantitative analysis of dissemination and utilisation of information by the CIB as also by the assessing officers. For the purpose of the evaluation of the working of CIB by Audit, production of these registers for scrutiny was essential.

In Maharashtra, Punjab, Andhra Pradesh and Rajasthan charges, registers of receipt of information in CIB, register of verification of information, register of action proposed, were not found to have been maintained or defectively maintained with some important columns left blank. In Madhya Pradesh charge, the register of verification of information was not maintained. In Kerala, Karnataka and Jammu and Kashmir charges the relevant registers were not produced to Audit.

The register of action proposed by the CIB was either not maintained or maintained improperly by the assessing officers in West Bengal and Andhra Pradesh charges. In other charges viz. Kerala, Karnataka, Haryana, Union Territory of Chandigarh etc., the relevant registers were not produced to Audit stating that they were confidential in nature.

In the registers maintained and produced to Audit, some general deficiencies noticed were as follows:

(a) Items of information requiring verification were not being regularly reported every month to the Commissioner of Income Tax.

(b) The registers were not being completed regularly. For instance, columns regarding the total number of items of information received, the nature of information, cross reference, etc., in the register of information receipts, and month of reporting to Commissioner of Income Tax in the register of verification of information received were found left blank.

(c) There was no system of reconciling the receipts as per the relevant registers with the figures in the monthly progress reports.

The Ministry in its reply (December 1994) has said that the functions of CIB are proposed to be computerised. The proposed computerisation will lead to improvement in functions of CIB.

The review was referred to the Ministry in September 1994. The Ministry's reply received in December 1994 has been kept in view in making this report.

3.2 Administration of Tax Deduction Account Number

Introductory

3.2.1 Deduction of tax at source on the taxable income is a convenient method of tax collection since it effects early realisation and saves time and effort of the department. For better monitoring of deduction of tax at source and its deposit in Government accounts, the Finance Act, 1987, inserted a new provision in the Income Tax Act, 1961, with effect from 1 June 1987 which made it obligatory for all persons responsible for deducting tax at source to apply for allotment of a tax deduction account number and to quote the same in all challans, all certificates for tax deducted and all returns relating to collection and recovery of tax.

Organisational set up

3.2.2 In metropolitan charges at Bombay, Madras, Calcutta, Delhi, Ahmedabad, Bangalore, Hyderabad and Pune, the allotment of tax deduction account number(TAN) work is centralised with one circle called variously as 'EDP cell', 'Budget and statistics', 'systems', 'computers' or 'TDS'. In other charges the work has been assigned to either TDS ward(s) or jurisdictional assessing officers.

Law and Procedure

3.2.3 Section 203A of Income Tax Act, 1961 and Rule 114A of Income Tax Rules, 1962 provide that every person responsible for deducting tax from specified incomes at the time of their payment shall apply in form No. 49-B giving name, address, status, source of income, nature of payments from which tax is deductible etc. to the concerned assessing officer for the allotment of a tax deduction account number within the prescribed time limit. Where the function of allotment of tax deduction account

number has been assigned to any particular assessing officer, the said application shall be made to that officer and in other cases to the jurisdictional assessing officer of the applicant. The time limit prescribed was 30 September 1987 in the case of a person deducting tax prior to 1 June 1987 and in any other case it was 30 September 1987 or one month from the end of the month in which the tax was deducted, whichever happened to be later.

After the allotment of a tax deduction account number, such persons shall quote the allotted number in all the challans for the payment of tax deducted to the credit of Union Government, in all the tax deduction certificates issued to the payees of the incomes from which tax was deducted, in all the returns required to be delivered to the Income Tax Department and in all other documents pertaining to such transactions. Failure to comply with these provisions would make the defaulter liable to penalty which may extend upto a sum of Rs. 5,000 if such person has no reasonable cause for the default. The person on whom the penalty is proposed to be imposed shall, however, be given an opportunity of being heard in the matter.

Scope of the review

3.2.4 The review seeks to evaluate the working and effectiveness of the scheme of allotment of tax deduction account number, to ensure correct and timely deduction of tax, its prompt payment to Government account, correct credit to the person from whom tax is deducted and to prevent TDS frauds. A test check of records of the 165 TAN allotting authorities, TDS wards and assessment wards in all the charges was conducted for the years 1989-90 to 1992-93.

Highlights

3.2.5(i) The department did not have complete record of persons responsible for deduction of tax at source to ensure that TAN were obtained within the prescribed period in all cases. Even such records which were available with the department were not made use of effectively to detect defaulters and take coercive action against them as contemplated in the Income Tax Act. [Paras 3.2.6 and 3.2.7]

(ii) Persons responsible for deducting tax at the time of payment of specified incomes were required to do so and pay the deducted tax promptly to Central Government account in accordance with the provisions of the Act.

However, in 3 charges there was non deduction of tax and surcharge of Rs.26.24 lakhs in 13 cases and non payment of deducted tax of Rs.26.41 lakhs in 8 cases in 2 other charges. Delays ranging from 14 days to more than 7 years in the payment of tax to Central Government account were also noticed but evidence of any action having been initiated by the department against the defaulters was not found on record. [Paras 3.2.12.1(a) and (b)]

(iii) In accordance with the provision of the Act the tax deductors are required to furnish to the department statutory returns of the tax deducted and credited by them to Central Government account. One of the duties of ITO (TDS) is to ensure their timely receipt and take penal action against defaulters. In 8 charges, 39 percent of the statutory returns were not received (1,49,187 cases). In 954 cases these had been received after delays ranging from a few days to over 1160 days but no action was found to have been taken against the defaulters. [Para 3.2.13(1)]

(iv) For administrative reasons the allotment of TAN in metropolitan and some other charges was assigned to an officer not entrusted with TDS work. In such cases close coordination needs to exist between TAN allotting authority and TDS authority. However, test check revealed that in many charges the TAN authority was not intimating the TAN to TDS authority. Further, the TDS authority on verification of a return and finding that TAN had not been allotted, was not intimating this fact to the TAN allotting authority for taking appropriate punitive action. [Para 3.2.14]

(v) Cross verification by assessing officers of TDS certificates with the record of the ITO (TDS) is an important tool to prevent spurious credit for tax paid being allowed in assessment. The percentage of check to be prescribed was left to the discretion of Chief Commissioner/Commissioner of Income tax. Test check revealed that such percentage was not prescribed except in one case. [Para 3.2.15]

(vi) Records were not maintained in the manner prescribed resulting in reduced efficiency in implementing the scheme. [Para 3.2.18]

Allotment of TAN

Delay in making TAN application

3.2.6 As per provisions of the Act, all the tax deducting agencies as on 1 June 1987 were required to apply for allotment of tax deduction account number in Form 49-B to the assessing officers concerned upto 30 September 1987 and in other cases within one month from the date of deduction of tax at source. Failure to do so attracted penalty upto Rs.5,000. Test check of the 1074 applications produced to Audit in Haryana charge, revealed that in 160 cases applications were submitted late by tax deductors by 1 month to 61 months but no coercive action was taken by the Department for levy of penalty of Rs. 8 lakhs computed at maximum rates. In Assam charge, 1842 TAN applications were received during 1989-90 in 3 TDS wards, though these should have been received by 30 September 1987 or within one month of becoming a tax deductor. The action taken against the defaulters, if any, was not on record. In Bihar and Chandigarh charges the date of receipt of TAN application was not noted in the relevant records with the result that the delay, if any, in making TAN application was not ascertainable.

Non-detection of TAN Applications not made

3.2.7 As a measure of control to ensure that the tax deducting agencies applied for TAN within the prescribed time and also in order to effectively monitor the work relating to deduction of tax at source, the Board had prescribed the maintenance of TDS control registers and alphabetical register of employers, entries in which were to be made from diverse sources like blue books of company circles/central circles/special ranges, counterfoils of TDS challan or entries in the daily collection register, monthly certificate of TDS (Form 23), survey of persons responsible for deducting TDS etc. These registers were meant for watching the receipt and processing of annual returns/monthly statements and furnishing the various reports to the higher authorities. These registers and monthly progress reports were not made use of to detect defaulting TAN applicants. A few illustrative cases are as under:

(i) In Assam charge, 135 tax deductors did not apply for allotment of TAN although their names appeared in control registers. No coercive action was initiated for levy of penalty which could amount to Rs. 6.75 lakhs for non-compliance of the provisions of the Act. In

the same charge, there were over 150 assessee companies being assessed in special ranges but only 36 companies had applied for TAN. The actual number of companies responsible for TDS could have been ascertained from blue books of the respective range where the company assessments were made. Action taken, if any, for ascertaining the reasons for not applying for TAN was not available in records.

(ii) In Punjab charge, the number of tax deducting agencies as on 31 March 1993, was reported to be 6322 in one TDS ward, but TANs were allotted to only 3658 tax deductors. The details of remaining 2664 cases were not available. There was also no evidence of any action taken in this regard.

(iii) In the Union Territory of Chandigarh charge, the number of tax deducting agencies was reported in the monthly progress report as 2081 whereas TAN allotment register showed only 1334 TANs allotted, while penalty under section 272 BB was imposed in only 18 cases. In the remaining 729 cases whether TAN applications were made or any action was taken against the defaulters by the department was not on record.

(iv) In Rajasthan charge, 10 tax deductors did not apply for TAN in one TDS ward, though they were filing prescribed returns. Action taken to allot TAN to these tax deductors and to levy penalty under section 272BB was not on record.

(v) In Gujarat charge, as per the Registrar, Non Trading Corporation there were 6208 corporations as on 31 March 1993 in Gujarat state which carried out various types of contract work through contractors. From the works bills, tax was required to be deducted and credited to Government Account. Other requirements prescribed under Section 203-A, 206 etc. were also to be followed by them. However, it was seen that only 10 corporations had obtained TANs and filed Income Tax Annual Returns suo-moto. No action had been initiated in respect of the remaining corporations. On this being pointed out in audit, the Department had promised to obtain lists from the Registrar concerned and take necessary action in the matter.

Mistakes in formulating TAN

3.2.8 To bring uniformity in the allotment of TAN, Board issued instructions in October 1987 prescribing the manner in which TAN will be formulated. As per these instructions, TAN will contain the letter and serial number of the tax deducting agencies as entered in the Register for allotment of TAN, a check digit, a letter indicating the nature of payment and an abbreviation for station as standardised by Indian Railways. Any failure in following the prescribed procedure would render monitoring of tax deducting agencies difficult. The procedure was not being correctly followed as the following cases reveal:

(i) In Bihar charge, the nature of payment was incorrectly indicated as 'Y' instead of 'I' for interest other than interest on securities in 172 cases in one TDS ward. In 2 wards, in 73 cases the nature of payment was not indicated and in 147 cases the abbreviation for station was either not mentioned or mentioned incorrectly.

(ii) In Orissa charge, the serial number of TAN was not being allotted alphabetically but one serial number was continued for all the alphabets.

(iii) In Punjab charge, TAN did not contain either letter and serial number of the tax deducting agencies, or the check digit or the letter indicating the nature of payment or appropriate abbreviation for station in 935 cases in one TDS ward.

(iv) In West Bengal charge, the serial number of TAN was not identical in 7 cases in one ward with that of the Register required to be maintained.

Delay in allotment of TAN

3.2.9(i) No time limit has been fixed for allotment of TAN by the concerned authority. However, the work involved is to enter the TAN applications in a register and allot the numbers. In the background of the simple matter of operation, delays in allotment of a number of over 3 months after the receipt of an application may not be considered as reasonable. Any delay in allotment or intimation would result in TANs not being

quoted on all TDS certificates/returns/ challans delivered to the payees/department during the period of delay. However, in Assam, Bihar, Haryana, Punjab, Union Territory of Chandigarh and West Bengal charges, test check in selected wards revealed time ranging from over 3 to 36 months however, been taken in alloting TAN in 676 cases. The reasons for taking so much time were either not stated or were not on record in all the cases. In one ward in Punjab charge, the delay was stated to be due to staff shortage. In the same charge in one TDS ward, it was observed that though TANs were duly alloted during 1989-90 to 1992-93, intimation thereof was not sent to TAN applicants in 2617 cases. Consequently they could not quote TAN in the prescribed documents.

(ii) In Madhya Pradesh charge, the applications received by the concerned ITO (TDS)/ACIT (TDS) are forwarded to computer wing alongwith the list of the applications for allotment of TAN and the computer wing in turn forwards a copy of TAN directory to the ITO (TDS) concerned. But the TAN directory was not checked by concerned TDS ward with a view to ensuring that TANs were allotted in all the cases for which applications were forwarded to the computer wing. A test check revealed that this had led to non-allotment of tax deduction account number in 50 cases in four ranges under one CIT charge.

Allotment of multiple TAN

3.2.10 Every person deducting tax at source should be allotted only one TAN and in case where the applicant makes payment of more than one nature viz. salary, interest etc., TAN issuing authority can issue the main number with appropriate alphabet letters for different nature of payments which can be used in appropriate case of deduction. The Board had prescribed a Register for allotment of Tax deduction Account Number in their instructions issued in September 1990 to regulate and monitor the allotment of TAN.

Test check in 36 offices in Andhra Pradesh, Assam, Bihar, Bombay, Karnataka, Madhya Pradesh and Punjab charges, revealed that in 533 cases more than one TAN was allotted to the same tax deductor either for different nature of payments or against more than one applications made. On the other hand in 12 cases in Punjab charge the same TAN was issued to more than one tax deductor. This shows that either the prescribed register was not maintained properly

or due care was not taken while allotting the TAN. Allotment of more than one TAN to a tax deductor or allotment of one TAN to more than one tax deductors would make the task of monitoring the tax deductors difficult.

Improper maintenance of Register for allotment of TAN

3.2.11 For effectively monitoring the allotment of TAN, the Board had issued instructions in September 1990 requiring the TAN allotment authorities to maintain, in alphabetical order, a consolidated register for allotment of TAN for all kinds of payments which would be a permanent record. The format of the Register provided for the name and address of person responsible for tax deduction at source, dates of receipt of application, status, PA No., source(s) for which TAN is required, TAN allotted, date of issue of allotment letter etc.

However, in Jammu and Kashmir and Punjab charges (3 TDS wards), the register was not maintained in alphabetical order and in Punjab charge, the Register prior to 9 November 1989 was destroyed in one ward and in another certain portions of it were not available. In Assam, Bihar , Punjab and Union Territory of Chandigarh charges, in quite a large number of cases, the status of the applicant and the dates of receipt of application and allotment of TAN were not found noted in the register with the result that the delay in making an application and allotment of TAN could not be ascertained. In the absence of the information the incidence of penalty under section 272BB which could be levied for delay in making an application could not be worked out. The information as to the number of cases in which the penalty was imposed by the department and the amount thereof could not be provided by them.

Administration of TDS through TAN

3.2.12 One of the objectives in introducing TAN scheme was better monitoring of tax deducted at source and its timely deposit with Central Government. However, instances were noticed in audit of non-deduction of TDS, its non-payment/delayed payment into Government account going undetected etc. These are mentioned below:

3.2

Failure to deduct or pay tax

(1) Under the Income Tax Act, 1961, any person required to deduct any tax shall pay it to the credit of Central Government within the prescribed time. The time prescribed in the case of deduction by or on behalf of the Government is the same day. In other cases if the income is by way of interest or insurance commission or payment to non-resident, sportsmen or sports associations or commission, remuneration or prize on sale of lottery tickets, or commission or brokerage etc. and if the same is credited by a person carrying on a business or profession to the account of the payee as on the day of making up the accounts, it is within two months of the expiry of the month in which the said day falls. In any other case it is either one week from the last day of the month in which the deduction is made or within one week from the date of deduction. Failure to deduct or pay tax shall make the tax deductor an assessee in default and make him/it liable to levy of interest at fifteen percent on the amount of such tax from the date on which such tax was deductible to the date on which such tax is actually paid. When such a tax deductor is deemed to be in default and fails to satisfy the assessing officer that the default was for good and sufficient reasons he shall be liable to penalty, the amount of which the assessing officer may determine but which shall not exceed the amount of tax in arrears.

(a) In Gujarat, Kerala and Rajasthan charges, the non-deduction of TDS and surcharge on tax of Rs. 26.24 lakhs in case of 13 tax deductors from payment of interest, commission and contract payments were noticed. There was no evidence on record to show that the payees had furnished prescribed declaration of non-taxability of their total income and the tax deductor had delivered such declarations to the prescribed authority. The department had also not initiated any action against the defaulters. An illustrative case is as under:

In Kerala charge, a group of firms engaged in money lending business assessed to income tax in the same circle were paying interest on deposits among themselves. In 3 cases the interest paying firms made payment of Rs.131.58 lakhs but failed to deduct tax of Rs.14.38 lakhs at source. In the course of audit it was found that the assessing officer had neither levied interest under section 201(1A) for omission to deduct tax at source nor brought the matter to the notice of the ITO(TDS) concerned. Interest leviable for non-deduction

of tax at source worked out to Rs. 7.06 lakhs apart from penalties leviable under section 221.

(b) In Gujarat, Karnataka and Orissa charges, test check revealed that though there were delays ranging from 14 days to more than 7 years in crediting the TDS to Central Government account, interest leviable under section 201(1A) was not charged. Penalty proceedings were also not initiated. Further, there was also default in making the payment. Two illustrative cases are as under:

(i) In Karnataka charge, while certifying the annual accounts of Zilla Parishads for the years 1987-88, 1988-89 and 1989-90, irregularities were noticed in 9 Zilla Parishads in the matter of remittance of income tax amount recovered from the payments made to contractors/suppliers under section 194-C. Out of Rs. 74.89 lakhs recovered as TDS during financial years 1987-88 to 1989-90, only a sum of Rs. 49.86 lakhs was remitted which was delayed by 1 to 28 months. The balance of Rs. 25.03 lakhs was still to be remitted by 6 Zilla Parishads to Government account (April 1994). The interest leviable under section 201(1A) was not levied. It was seen that the annual returns for the years 1987-88 to 1989-90 had not been furnished to the Income Tax Department by the Zilla Parishads. Failure to credit the tax collected at source could have been detected, had the annual returns under section 206 of the Act been properly watched and action initiated under section 272(A.2)(c) for levying penalty in cases of non-receipt or delayed receipt. Prosecution proceedings under section 276B could have also been initiated for failure to credit the tax deducted at source to the credit of Central Government.

(ii) In Assam charge, verification of records in assessment circle and TDS/TAN ward revealed that two closely held companies who were allotted TAN deducted tax from contract payment made during 1979-80 to 1991-92 amounting to Rs.1.38 lakhs but did not pay it to Govt. account. Total interest and penalty leviable worked out to Rs. 3.01 lakhs which was not levied.

Irregularities in TDS certificates

(2) Under section 203 of the Income Tax Act, 1961, every person deducting tax in accordance with the provisions of the Act shall within one month (upto 30 September 1991) and one month and fourteen days (from 1 October 91) from the time of credit or payment furnish to the person to whose account such credit is given or payment is made, a certificate to the effect that the tax has been deducted giving PAN and TAN of the tax deductor, PAN of the employee and date of payment to Central Government account.

(i) During review of the records of TDS wards in Gujarat charge, it was seen that in 84 cases the TDS certificates were not furnished within the specified time to the person concerned. Penalty proceedings u/s 272(A)(2)(g) were not initiated in any case.

(ii) In 389 cases in Madhya Pradesh, Orissa and West Bengal charges, the TDS certificates did not bear the date of remittance of TDS into Government account.

(iii) In Madhya Pradesh charge, TAN was not found noted in 1663 TDS certificates in 21 assessment wards/circles but penalty proceedings U/s. 272 BB were not initiated in any case.

Annual returns of TDS

3.2.13 Under section 206 of Income Tax Act 1961, the persons responsible for deducting tax at source are required to furnish prescribed returns such as annual returns of tax deduction of tax from salary, interest, dividends, winnings from lotteries or crossword puzzles, winnings from horse races, payments to contractors, insurance commissions, payments in respect of deposits under National Savings Scheme etc. in the prescribed forms setting forth all prescribed particulars by the end of the month specified (April to June according to the nature of deduction). The prescribed returns have to be accompanied by the copies of challans through which the payments are made to the credit of Central Government and copies of TDS certificates issued to the payees.

In introducing the TAN scheme, the department expected better monitoring of the receipt and check of statutory return and follow up action thereon. But instances were noticed of non-receipt of statutory returns, non-verification and want of follow up action. These are mentioned below:

Non-receipt or delayed receipt of prescribed returns

(1) One of the duties of ITO(TDS) is to ensure that statutory returns are received within time and that the defaulters are duly penalised.

The number of TANs alloted, number of statutory returns required to be furnished(presuming only one return for one TAN in the absence of details from the department, though more than one may be required for different kinds of payment) and number of returns received are given below:

Charge	Year to which relate	No.of TAN alloted	No. of Returns due	No. of returns received
Andhra Pradesh	1991-92 & 1992-93	39,903	62,260	25,589
Assam	1989-90 to 1992-93	1827	4,887	1,383
Delhi	1992-93	45,609	47,802	46,832
Karnataka	1991-92 & 1992-93	N.A.	29,941	25,604
Kerala	1989-90 to 1992-93	5,420	18,587	11,067
Maharashtra	1992-93	95,718	95,718	45,785
Punjab	1990-91 to 1992-93	26,795	81,474	44,141
Tamil Nadu	Inf.in r/o 11 out of 27 wards	N.A.	42,431	33,512
	Total	2,15,272	3,83,100	2,33,913

Thus in 39 percent of cases returns due were not received. No action was found to have been taken by the department to call for the wanting returns or to ensure that no return was required to be filed by TAN holders in these cases. Besides, delays ranging from few days to more than 1160 days were noticed in 954 cases while checking the receipt of returns in Gujarat, Haryana, Karnataka, Madhya Pradesh, Orissa, Rajasthan, Tamil Nadu and West Bengal charges. However, evidence of initiation of penalty proceedings in these cases was not on record.

Non-quoting of TAN on returns, challans and TDS certificates

(2) Section 203A(2) provides that TAN allotted shall be quoted in all challans for the payment of TDS to Central Govt. in all tax deduction certificates issued to the person from whom tax deducted and in all returns delivered to the Income Tax Department. Failure to quote TAN may entail levy of penalty which may extend to five thousand rupees if such failure is not for reasonable cause.

Test check of annual returns in selected wards in Assam, Delhi, Haryana, Karnataka, Union Territory of Chandigarh and West Bengal charges revealed that TAN was not quoted in 1075 cases out of 13726 returns (7.8 per cent), in 228 out of 1774 TDS certificates (12.8 percent) and in 135 out of 675 challans (20 per cent) checked. In 103 cases out of 1707 TDS certificates checked the details of remittance of TDS amount to the credit of Central Government were not given. Penalty for default was reported to have been levied in 248 cases. In the remaining cases no action appears to have been taken to either call for the wanting details or to initiate penalty proceedings.

Verification of statutory returns/ statements.

(3) As per Board's instructions issued in September 1990, the statutory returns/ statements received should be checked to find out whether the tax has been correctly deducted from each payee, whether the tax deducted at source has been paid within the specified time, whether interest is payable under section 201(1A) and whether any penalty is leviable under section 272 A(2). The amount of short or non deduction of tax or short or non payment of tax to Central Government account has to be determined and recovered by I.T.O. (TDS) and action taken in accordance with law. The instructions provided that the payment of taxes claimed to have been made should be verified from the daily collection register in which all the challans relating to deduction of tax at source are entered. The returns/statements where no defect on verification is found should be kept separately in a bundle arranged alphabetically.

(i) Test check of selected TDS wards in Assam, Delhi, Maharashtra, Orissa, Tamil Nadu and West Bengal charges revealed that the cross verification of payments of TDS into Government accounts with bank scrolls/daily collection register was not being carried out. In Punjab charge, a sum of Rs.49,345 claimed to have been paid on 23 April 1992 by a tax deductor in one TDS ward was not traceable in the bank scroll.

(ii) In Rajasthan charge, TDS fell short by Rs. 59,000 in 7 cases but no follow up action was taken to recover it alongwith penalty and interest due.

(iii) Test check in Andhra Pradesh, Gujarat, Maharashtra and Tamil Nadu charges revealed that the amount of tax shown as deducted in monthly certificate of deduction of tax at source from income chargeable under the head 'Salaries' in Form 23 was not being verified with the departmental copy of challan/entry in the daily collection register and the total of tax paid shown in the monthly certificates in a year not reconciled with the total tax shown paid in the annual return in Form 24.

Irregularities in statutory returns

(4) The following irregularities were generally noticed while test checking statutory returns received in TDS wards:

- Annual returns were not checked in large number of cases.
- Interest and penalty for belated remittance of tax were not levied.
- PAN of the tax deductors/payees was not noted in the returns.
- Dates of issue of TDS certificates and payment to Govt. account were not indicated in some cases.
- Challans were not found attached in support of payment of tax to Govt. account in many cases.
- Returns were kept not in bundles but in loose condition.

Lack of co-ordination between TAN allotting authority and TDS authorities

3.2.14 When the scheme of TAN was introduced, the allotment work was intended to be entrusted to the officers handling TDS work. However, for administrative reasons the work had to be entrusted later on in some cases to officers not handling TDS work. As TAN was devised to help better administration of TDS, there should be close co-operation between the two authorities.

It was observed during test check in Bombay, Delhi, Gujarat, Haryana, Orissa and West Bengal charges, that neither the authority responsible for allotment of TAN, was intimating the allotment of TAN to the authority responsible

for TDS work nor were TDS authorities reporting to TAN allotting authority the cases where annual returns were received from the tax deductors but TAN had not been quoted in the said returns. This resulted, on one hand, in TAN not being allotted to certain tax deducting authorities and, on the other, in the possibility of prescribed TDS returns remaining undelivered to the department for exercising necessary checks on TDS recovery and credit to Central Government account.

Prescribing percentage check/cross verification of Tax Deduction Certificates by Chief Commissioner of Income Tax

3.2.15 Cross verification of TDS certificates by assessing officers with records of TDS wards is an important tool to check spurious credit for tax being claimed by the assessees and allowed by the department against the tax due. As per Central Board of Direct Taxes instructions issued in September 1988 and September 1990 the percentage of cross check of TDS certificates received by jurisdictional assessing officer alongwith the income tax returns of the assessees with the records of the Income Tax Officer (TDS) has to be prescribed, at the discretion of the Chief Commissioner/Commissioner of Income Tax (CCIT/CIT).

The information sought from assessing officers in this regard disclosed that in no CCIT/CIT's charge except Punjab, had such percentage been laid down. In Punjab also only one CIT had prescribed the percentage. In the absence of prescribed percentage most of the assessing officers whose assessment records were test checked conceded that such cross verification of TDS certificates was not carried out at all. The TDS Officers also confirmed that no request was received by them from assessing officers for the purpose. A few assessing officers, however, claimed that in selected cases especially involving larger amounts the TDS certificates were verified but no discrepancy was noticed. In Jammu and Kashmir charge, it was noticed that refunds exceeding Rs.2,500 were being granted after getting the correctness of tax deduction at source verified from the TDS wards. In the absence of cross verification, the possibility of frauds cannot be completely ruled out.

Internal and external surveys

3.2.16 With a view to ensuring that all the persons who are liable to deduct or collect tax within their jurisdiction are brought on TAN Directory, the Board had directed the Income Tax Officers (TDS) in September 1990 that they

would organise internal survey of important assessment records as also outdoor survey of organisations within their jurisdiction, viz., trade and commerce, accounts, Registrars of Companies, business houses, firms, companies, clubs, hospitals, educational institutions, etc. Further, for ascertaining that persons responsible for tax deduction were complying with the provisions relating to the deduction of tax at source, survey of such persons was also to be conducted by the Income Tax Officers (TDS).

Except in Andhra Pradesh, Gujarat, Madhya Pradesh and Tamil Nadu charges, no internal or external survey was reportedly undertaken by the TDS officers in any other charges to bring on books the defaulting TAN applicants. Survey was conducted in one ward in Andhra Pradesh and Tamil Nadu charges and 3 surveys in one CIT charge in Gujarat. In Madhya Pradesh charge the surveys were carried out in two stages - first, the information was collected from PAN directory, and second, field surveys were done from time to time. Results of these surveys were not on record to assess their effectiveness.

Internal Audit

3.2.17 One of the duties of Internal Audit is to check whether the tax demanded and collections/recoveries are correctly brought to account and the relevant records/accounts are maintained properly and also to verify :

(a) whether there is any inordinate delay on the part of employers to deduct TDS from salaries and whether interest under section 201(1A) was levied by Income Tax Officer?

(b) whether there has been any case where the employer has given a certificate to an assessee under Section 203 regarding the amount of salary paid and tax deducted at source while actually no tax was deducted at source?

Despite the codal provisions in this regard, it was seen in audit that no internal audit had been carried out in any of the wards covered by test check in Assam, Delhi and West Bengal charges. Most of the irregularities brought out in this review could have been detected in time, if internal audit of the TDS wards was conducted with a regular periodicity.

Maintenance of Registers

3.2.18 Board's instructions issued in September 1990, provided for the maintenance of following registers in TDS wards, apart from Register for allotment of TAN to tax deductors for TDS:

3.2

TDS control Register No.I (for offices of Government and local authorities) and 2 (for others).

(i) These registers contain the particulars of all persons responsible for deducting tax at source and serve as control registers for monitoring the receipt of the annual returns and follow up action thereon. These should be maintained in the prescribed proforma and alphabetically. The entries in these registers are required to be made from sources such as Blue Books of company circles/central circles/special range, counterfoils of TDS challans or entries in the daily collection register(TDS) and surveys etc. However, test check revealed that in many cases they were either not maintaiend at all or not posted upto date or not maintained separately and in the prescribed proforma. In most of the cases it was merely a return receipt register where statutory returns, as and when received were entered and did not serve as an instrument for better administration of TDS. The entries were not made from five sources mentioned in Board's circulars and all the columns were not found filled.

Demand and collection Register

(ii) This register keeps record of name and addresses of the persons responsible for TDS, amount of short deduction or no deduction of TDS detected from the checking of statutory returns, interest and penalty leviable, date of service of notice of demand, date on which demand is due and collection of demand and particulars thereof etc. Test check in Union Territory of Chandigarh charge revealed that Demand and collection Register did not indicate the dates on which demands were due to be paid with the result that the interest chargeable under section 201(1A) could not be worked out.

Alphabetical Register of employers

(iii) This register meant for employers responsible for deducting tax from 'salaries' records the receipt of monthly certificates of TDS in Form ITS 23 from them, shortfall of TDS if any, and action taken to recover the same. This register was not found maintained in many cases and where maintained it was not in the prescribed form. It merely served as an index register of TAN allottees.

Register of penalties under section 271C, 272A and 272BB and register of cases for prosecution proceedings under section 276B.

(iv) The register of penalties keeps record of initiation of penalty proceedings and indicates details like the person against whom penalty proceedings are initiated, date of service of show cause notice, limitation date, date of penalty order and amount of penalty imposed. Register of prosecutions records, the nature of default, the particulars of defaulters, date of CITs approval and date of filing prosecution proceedings etc. These were generally not found maintained and where maintained not updated in some cases

Daily Collection Register (TDS)

(v) In this register particulars of challans for TDS from all types of payments, interest and penalties in respective columns with cross reference of serial number in D&CR (TDS) are entered. Test check revealed that in Orissa charge this register was not being maintained.

Special Watch Register

(vi) In this register record is kept of statements in form No.21 in respect of salaries paid to the employees leaving service and of return in form No.22 furnished by trustees of an approved superannuation fund when they pay employer's contribution to an employee during his life time. This register was generally not found maintained in the wards test checked.

The reply from the Ministry of Finance to the audit observations has not been received so far.

3.3 Double Taxation Avoidance Agreements and Relief

Introduction

3.3.1 Transfer of technology and investment from other countries plays a vital role in the economic development of a country. A crucial factor which inhibits free transfer of technology and investment is the likelihood of double taxation of income. The agreements between different countries for double taxation relief are intended to provide relief against double or multiple taxation of the same income in the hands of the same assessee simultaneously under the taxation laws of the countries entering into such agreement. The taxability of an assessee in India on any source of income depends upon his residential status taken in conjunction with the places of

accrual or arisal or receipt of the particular income. The position in many other countries being also broadly similar, it frequently happens that a person may be found to be a resident in more than one country or that the same item of his income may be treated as accruing, arising or received in more than one country with the result that the same income becomes liable to tax in more than one country. It is to prevent this hardship to the assessee that India has also entered into agreements with different countries for avoidance of double taxation.

Law and Procedure

3.3.2 Tax treaties are entered into by the Government of India with the government of a foreign country for the following purposes:

(a) granting of relief in respect of income on which income tax has been paid under Indian tax laws and also in that country; or

(b) avoidance of double taxation of income under the tax laws of the two countries; or

(c) exchange of information for the prevention of evasion or avoidance of income tax chargeable under the tax laws of the two countries, or investigation of cases of such evasion or avoidance; or

(d) recovery of income tax imposed under the tax laws of the two countries.

The Central Board of Direct Taxes in their Circular No. 333 dated 12 April 1982 clarified that where a Double Taxation Avoidance agreement provides for a particular mode of computation of income, the same prevails over the general provisions contained in the Act. Where there is no specific provision in the agreement, the domestic law governs the taxation of income.

In order to avoid hardship in respect of doubly taxed incomes arising in countries with which there are no Double Taxation Avoidance agreements, section 91 of the Act provides for unilateral relief.

The conditions to be fulfilled for grant of such relief are:

(a) the assessee should be resident in India in the previous year.

(b) the income should have accrued or arisen to him outside India.

(c) the assessee should have paid tax in the foreign country. The tax could be paid either by way of deduction or otherwise under the law in force in the foreign country; and

(d) the income should be taxed both in India and in the foreign country with which India has no agreement for relief or avoidance of double taxation.

In such cases the assessee will be entitled to a deduction from the Indian income tax payable by him, of a sum calculated on such doubly taxed income at the Indian rate of tax or the rate of tax of the said country, whichever is lower or at the Indian rate of tax if both the rates are equal.

Scope and extent of audit

3.3.3 A test check of assessment records was conducted in audit with a view to examining whether Double Taxation Avoidance Agreements and also provisions providing unilateral relief where no such agreements exist were being applied correctly. Certain irregularities in these assessments were noticed in Karnataka, Kerala, Maharashtra, West Bengal and Tamil Nadu charges under the following broad categories:

(i) Mistake in computation of income

(ii) Omission to withdraw excess relief

(iii) Mistakes in grant of relief

(iv) Application of incorrect rates

A few illustrative cases under each of the above categories are mentioned in the succeeding paragraphs:

Mistake in computation of income

(i) The Agreement for avoidance of double taxation of income between the Government of India and Government of Malaysia stipulates that the income or profits of an enterprise of

one of the contracting States shall be taxable only in that contracting State unless the enterprise carries on business in the other contracting State through a permanent establishment situated therein, and if the enterprise carries on business as aforesaid, tax may be imposed in that other contracting State on the income or profit of the enterprise, but only on so much of that income or profits as is attributable to the permanent establishment in that country. It has been held by the Madras bench of the Tribunal in December 1982 that business profits arising in Malaysia through a permanent establishment in that country, cannot be taxed in India. This view was later endorsed by the Madras High Court in March 1994. On a similar analogy, losses arising in Malaysia are also required to be excluded from the total income brought to tax in India.

In Tamil Nadu charge, the assessments of a nationalised bank, having branches in Malaysia, for the assessment years 1988-89 to 1991-92 were completed after scrutiny between March 1991 and March 1994. Audit scrutiny revealed that though profits from branches in Malaysia for the previous year relevant to the assessment year 1988-89 were excluded in accordance with the terms of the Agreement, the amount of bad debts of Rs. 6.38 lakhs for assessment year 1988-89 and losses amounting to Rs, 2490 lakhs for assessment years 1989-90 to 1991-92 attributable to business in Malaysia were not excluded in the assessment for the respective assessment years resulting in excess carry forward of losses aggregating Rs. 2496.38 lakhs involving a potential tax effect of Rs. 1212.07 lakhs.

Omission to withdraw excess relief

(ii) Under the Income Tax Act, 1961, the Government of India may enter into an agreement with the government of any country outside India for granting relief in respect of income on which income tax has been paid both in India under the Act and in that country.

In Karnataka charge, in the assessment of a resident banking company for the assessment year 1989-90 completed after scrutiny in December 1990, the assessing officer allowed a

relief of Rs. 92.80 lakhs being income tax paid in the United Kingdom on the profits of Rs. 265.14 lakhs earned in London and taxed in that country. The company made a loss in the assessment year 1992-93 and opted for a backward set off of this loss against the income for the assessment years 1991-92 to 1989-90 in accordance with the laws of the United Kingdom. This resulted in reduction of the tax payable in that country for the assessment year 1989-90 to Rs. 24.80 lakhs. Hence, the consequential excess allowance of relief of Rs. 68.00 lakhs from the tax payable in India which was required to be withdrawn was not done by the assessing officer. This resulted in grant of excess relief of Rs. 80.24 lakhs including interest.

The audit observation, which was communicated to the department in February 1994, was accepted by them and the mistake rectified in April 1994.

Mistake in grant of relief

(iii) Under the Income Tax Act, 1961, a resident person is entitled to relief in respect of his foreign income, taxed both in India and in a foreign country. The quantum of relief is governed by agreements entered into by the two countries.

In West Bengal charge, a resident company was assessed for the assessment year 1990-91 after scrutiny in March 1993 at a total income of Rs. 15.36 lakhs allowing relief of Rs. 7.21 lakhs on account of tax paid in Libya on the income of Rs.27.44 lakhs. Audit scrutiny revealed that out of the total Libyan income of Rs. 27.44 lakhs, Rs. 13.29 lakhs was taxed in both the countries in the earlier assessment year 1989-90 and double taxation relief was granted. Hence, the assessee company was entitled to relief on the balance amount of Rs. 14.15 lakhs only for the assessment year 1990-91. The mistake resulted in excess allowance of relief of Rs. 3.50 lakhs.

Application of incorrect rates of tax

(iv) The Double Taxation Avoidance Agreements entered into by the Government of India with Austria, France, Germany, Japan, Nepal, Sweden and USA provide for different rates of taxation in the respective countries on income from technical fees, dividends, royalties, etc. In the following illustrative cases of companies, relating to assessment years 1983-84 to 1992-93, audit scrutiny revealed application of incorrect rates resulting in short levy of tax aggregating Rs. 363.25 lakhs:

3.3

S.No.	CIT Charge	Assess-ment year	Nature of mistake	Tax effect
				(In lakhs of Rs.)
1.	Trichy/ Coimbatore	1988-89 to 1992-93	The Double Taxation Avoidance Agreements with U.S.A. and Japan are applicable for income arising on or after 1 April 1991/1 April 1990. Accordingly, income by way of fees for technical services will be subject to tax at 20 percent. However in six cases, the income arising before that date was erroneously taxed at this rate instead of 30 percent as applicable under the Act.	277.76
2.	Tamil Nadu	1985-86 to 1987-88	In the assessment for the assessment year 1987-88, relief on account of tax paid in Thailand was allowed at 50 percent as per the Double Taxation Avoidance Agreement with Thailand which was applicable to assessment year 1988-89 and onwards instead of the correct rate of 35 percent applicable to the assessment year 1987-88. Further, for the assessment year 1985-86, relief was allowed at the rate of 43.20 percent instead of the correct rate of 40 percent	25.19
3.	Bombay City II	1990-91	As per Article VI of the Double Taxation Avoidance Agreement with Germany, the rate of tax leviable on shipping profits was 50 percent. However, tax was erroneously levied at 25 percent only	17.64
4.	WB I, Calcutta	1989-90	While giving effect to appellate orders, double taxation relief was allowed under the Double Taxation Avoidance Agreement with United Kingdom on the whole of dividend income of Rs. 191.94 lakhs instead of on Rs. 61.65 lakhs which alone was eligible for such relief.	13.03
5.	Trichy	1983-84	According to Article IX of Double Taxation Avoidance Agreement with Germany, tax on royalty arising after 1 April 1976 was leviable at 30 percent. Though the assesments for 1978-79 to 1982-83 and 1988-89 to 1990-91 were revised and tax was levied at 30 percent, no revision was made for assessment years 1983-84 to 1987-88.	12.75
6.	Bombay City II	1992-93	Relief on dividend was allowed at 15 percent in accordance with the terms of the Double Taxation Avoidance Agreement with U.S.A. instead of the correct rate of 25 percent as the company had a permanent establishment in India.	9.50

	Kochi	1988-89 1990-91	An amount of Rs. 23.45 lakhs was considered as technical fees and taxed at 20 percent according to the Double Taxation Avoidance Agreement with Germany instead of taxing it as royalty at the rate of 30 percent as provided in the Act.	4.02
8.	Kochi	1991-92	Tax on dividend of Rs. 6.72 lakhs was levied at the rate of 15 percent. As the assessee was a resident of Japan and carried on business through a permanent establishment in India, tax should have been levied at the rate of 65 percent.	3.36
				363.25

The reply from the Ministry of Finance to the audit observations has not been received so far.

CHAPTER 4

CORPORATION TAX

General

4.1 ** According to Department of Company Affairs, Ministry of Law, Justice and Company Affairs, there were 3,08,889 companies as on 31 March 1994. These included 565 foreign companies and 2350 associations functioning 'not for profit' but registered as companies limited by guarantee and 349 companies with unlimited liability. The remaining 3,05,625 companies with limited liability comprised 1,203 Government companies and 3,04,422 non-Government companies with paid up capital of Rs.64,027.58 crores and Rs.40,863.31 crores respectively. Among non-Government companies, over 87.71 per cent (267012) were private limited companies with a paid up capital of Rs.7,512.62 crores.

4.2 The number of companies on the books of the Income Tax Department during the last five years was as follows:

As on 31 March	Number
1990	1,10,514
1991	1,24,402
1992	1,34,779
1993	1,55,418
1994	1,61,075

4.3 The trend of receipts from corporation tax i.e., income tax and surtax payable by companies during the last five years was as follows:

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

Year	Receipts from Corporation tax	Gross collection of all direct taxes	Percentage of Corporation tax to gross collection
	(In crores of rupees)		
1989-90	4,728.92	10,007.78	47.25
1990-91	5,335.26	11,028.93	48.37
1991-92	7,867.67	15,342.36	51.28
1992-93	8,889.24	18,097.29	49.12
1993-94	10,060.06	20,298.24	49.56

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

Year	No. of assessments				Total demand		
	For disposal	Completed during the year	Pending at the close of the year	Percentage of pendency to total cases for disposal	Demand for collection	Collection during the year	Percentage of collection to total demand
					(In crores of rupees)		
1989-90	1,54,858	1,04,572	50,286	32.47	7680.61	4728.92	61.57
1990-91	1,76,338	1,19,265	57,073	32.36	7925.48	5335.26	67.32
1991-92	2,13,359	1,46,998	66,361	31.10	10938.21	7867.67	71.93
1992-93	2,26,665	1,51,913	74,752	32.98	13088.96	8889.24	67.91
1993-94	2,55,344	1,81,130	74,214	29.06	16686.69	10060.06	60.29

Results of Audit

4.5 A total number of 414 draft paragraphs involving tax effect of Rs.157.32 crores were issued to the Ministry of Finance for comments during March to September 1994. The Ministry of Finance have accepted the observations in 282 cases involving tax effect of Rs.88.12 crores. 136 illustrative cases involving tax effect of Rs.124.57 crores are indicated in the succeeding paragraphs. Out of these, the Ministry of Finance have accepted the observations in 105 cases involving tax effect of Rs.75.93 crores. Of these, 20 cases involving tax effect of Rs.7.02 crores were checked by the Internal Audit but the mistakes were not detected by it. The repetitive nature of the mistakes committed by the assessing officers indicates that adequate attention is not being given even to assessments involving substantial revenue.

4.6

Avoidable mistakes in computation of income and tax

4.6 Under the Income Tax Act, 1961, an assessment may be completed in a summary manner after, inter alia, rectifying any arithmetical error in the return, accounts and accompanying documents. In a scrutiny assessment, the assessing officer shall make a correct assessment of the total income or loss of the assessee and determine the correct sum payable by him or refundable to him on the basis of such assessment. While computing the income chargeable to tax, the assessing officer takes the profit or loss as per the profit and loss account of the assessee as the starting point and then adds back or deducts the amount not allowable or which requires special consideration. The Central Board of Direct Taxes have, from time to time, issued instructions stressing the necessity for ensuring accuracy in the computation of income and tax, carry forward of figures etc. Underassessments of tax of substantial amounts on account of avoidable mistakes, attributable to negligence on the part of assessing officers were reported year after year in the reports of the Comptroller and Auditor General of India. Despite this and issue of repeated instructions by the Central Board of Direct Taxes, such mistakes continue to occur. The extent of such mistakes noticed during test check of the assessments completed by the assessing officers during last five years was as under:

Year	No. of Items	Amount of tax underassessed (Rs. in lakhs)
1989-90	880	960.63
1990-91	1,153	1,135.00
1991-92	878	8,857.00
1992-93	907	1,470.48
1993-94	1140	2,101.49

The various types of mistakes noticed are:

- incorrect adoption of figures
- double allowance of deductions
- arithmetical errors

- calculation errors and other omissions and mistakes.

Some important cases of each type noticed in test check are given below:

Sr. No.	State/CIT's charge	Asstt. year Date of Asstt.	Section under which assessed	Nature of mistake	Tax effect (Rs. in lakhs)
(i) Incorrect adoption of figures					
1.	West Bengal/W.B.IV	1990-91 February 1993	143(3)	In computing the loss, depreciation of Rs.218.60 lakhs debited to profit and loss account was added to net loss instead of deducting it from the loss.	236.09(P)
2.	Andhra Pradesh/ Vishakhapatnam	1990-91 February 1993	143(3)	Income of Rs.36.31 lakhs was erroneously adopted as a loss.	43.13 (including potential tax of Rs.18.12 lakhs)
3.	West Bengal/W.B.VI	1990-91 July 1992	143(3)	Amount of Rs.864.48 lakhs was erroneously adopted as net loss instead of the correct figure of Rs.825.36 lakhs.	21.13(P)
4.	West Bengal/W.B.II	1991-92 March 1993	143(3)	Though there was a profit of Rs.6.52 lakhs, income was computed at a loss of Rs.3.30 lakhs.	6.69 (including interest)
(ii) Arithmetical errors					
1.	Bihar/Ranchi	1984-85 January 1993	143(3)	Several arithmetical mistakes in the assessment order resulted in short computation of income by Rs.655.40 lakhs leading to excess carry forward of loss.	378.49(P)
2.	Karnataka/ Kar-I,Bangalore	1990-91 July 1992	143(3)	Aggregate amount of disallowed items was arrived at Rs.14250.26 lakhs instead of	159.38(P)

The Ministry has accepted the audit observation at Sl. Nos. 1,2&3. Their response to the remaining case has not been received.

(P) denotes potential. In such cases there may be no actual demand being loss cases.

				correct figure of Rs.14545.41 lakhs.	
3.	Rajasthan/ Jaipur	1992-93 March 1993	143(3)	Deduction of Rs.249 lakhs was allowed towards depreciation as against the correct amount of Rs.229 lakhs	10.35

The Ministry has accepted the audit observations.

(iii) Double allowance of deductions, calculation errors and other mistakes

1.	Maharashtra/ Bom. city III	1990-91 August 1991 March 1993	143(3)	In the revised assessment, while giving credit for the taxes paid, the refund of Rs.56.20 lakhs allowed to the assessee in the earlier assessment was omitted to be considered.	56.20
2.	West Bengal/ W.B.V, Calcutta	1990-91 March 1993	143(3)	Omission to disallow Rs.74.15 lakhs on account of investment written off in the actual computation of income though considered for disallowance in the discussions of assessment order. Further, the amount of refund and interest thereon was not reduced due to reduced tax effect.	47.90
3.	Karnataka/ Kar.I, Bangalore	1988-89 October 1989	143(3)	Omission to disallow Rs.80.77 lakhs being 'payment and provisions for employees' and prior period expenses already adjusted by the assessee.	47.40(P)
4.	Tamil Nadu TN IV,Madras	1990-91 February 1993	115J/143(3)	Tax payable was worked out on income of Rs.23.66 lakhs computed under special provisions instead of on the income of Rs.55.11 lakhs computed under normal provisions.	28.88 (including interest)
5.	West Bengal/ W.B.III	1990-91 March 1993	143(3)	Claim of depreciation of Rs.42 lakhs was rejected in assessment order but while computing total income it was allowed.	22.68(P)
6.	Tamil Nadu/ T.N.III, Madras	1989-90 March 1992	143(3)	Investment allowance of Rs.17.44 lakhs already claimed by assessee was again allowed by the assessing officer.	15.75 (including interest)

7.	Maharashtra/ Bom. city III	1990-91 January 1993	143(3)	Omission to disallow un-absorbed liability of Rs.15.41 lakhs relating to royalty payments.	15.38 (including interest)
8.	West Bengal W.B.III	1990-91 March 1993	143(3)	Deduction of Rs.20.62 lakhs towards municipal tax and corporation tax was allowed again though already debited to profit and loss account.	13.36
9.	West Bengal/ W.B.III	1990-91 March 1993	143(1)	In the assessment order Rs.13.58 lakhs relating to prior period expenses was disallowed but in the actual computation of income the amount was allowed as deduction.	12.61 (including interest)
10.	West Bengal/ W.B.I, Calcutta	1990-91 March 1993	143(3)	Omission to disallow depre-ciation of Rs.21.07 lakhs already allowed in earlier assessment years.	11.38
11.	Maharashtra/ Bom. city V	1990-91 March 1993	143(3)	In the assessment order short term capital gains of Rs.4.42 lakhs arising on sale of flats was determined to be included in the total income but in the actual computation this was not done.	4.52 (including interest)

The Ministry has accepted the audit observation in all the cases.

Application of incorrect rate of tax

4.7 In Uttar Pradesh charge, the assessment of a company in which the public are not substantially interested, for the assessment year 1987-88, was completed after scrutiny in March 1990 and revised in March 1993, wherein tax was levied at 50 percent of the total income instead of the correct rate of 60 percent. The levy of tax at incorrect rates resulted in short levy of tax of Rs. 18.65 lakhs including interest.

The Ministry has accepted the audit observation.

Incorrect allowance of capital expenditure

4.8 Under the provisions of Income Tax Act, 1961, any expenditure not being expenditure of a capital nature laid out or expended wholly or exclusively for the purpose of the business is allowable as deduction in computing income chargeable under the head 'Profits and gains of business or profession'.

In Maharashtra charge, the assessment of a company for the assessment year 1990-91 was completed in March 1992 in a scrutiny manner at a taxable income of Rs.5.52 lakhs. The income was computed under the special provisions of the Act, as that computed under the normal provisions of the Act was a loss. Audit scrutiny revealed that the assessee company had debited its 'profit and loss account of the relevant previous year by an amount of Rs.23.92 lakhs being the value of assets written off. The loss which was capital in nature should have been disallowed. Failure to do so resulted in computation of excess loss by Rs.23.92 lakhs involving potential short levy of tax of Rs.13.82 lakhs (after adjusting the depreciation).

The reply of the Ministry to the audit observation has not been received.

Incorrect allowance of bad debts

4.9 Under the Income Tax Act, 1961, as applicable for assessment year upto 1988-89, the amount of any debt or part thereof which is established to have become bad in the previous year is allowable as deduction in computing the income chargeable to tax under the head 'profits and gains of business or profession'. However, in the case of a bank to which provision for bad and doubtful debts is allowable, the amount of deduction shall be limited to the amount by which such debt or part thereof exceeds the 'credit balance in the provision for bad and doubtful debts' account made under the Act.

In Tamil Nadu charge, the assessment of a bank for the assessment years 1986-87 to 1988-89 was completed between February 1989 and November 1990 after scrutiny. Audit scrutiny revealed that deduction of Rs. 36.28 lakhs, Rs. 48.85 lakhs and Rs. 56.92 lakhs respectively towards bad debts written off were allowed though sums of Rs. 21.14 lakhs, Rs. 32.75 lakhs and Rs. 40 lakhs were available in the relevant assessment years in the provision for bad and doubtful debts. The deduction allowed in respect of bad debts, however, should have been limited to the amount by which the same exceeded the amount allowed towards provision for bad and doubtful debts. Omission to restrict the deduction resulted in underassessment of income by Rs. 93.89 lakhs involving short levy of tax aggregating Rs.47.95 lakhs in three years.

The Ministry has not accepted the audit observation on the ground that proviso to

section 36(1)(vii) was not attracted in the case as provision for bad and doubtful debts was created and claimed in respect of certain identified debts under sec.36(1)(viia) of the Income Tax Act, 1961. The Ministry has further stated that there was no nexus between items in respect of which provison was made under section 36(1)(viia) and items of debt actually written off. The reply is not tenable in view of the specific provisions in the Act for regulating the allowance of claim towards bad and doubtful debts in respect of banks. Further, in March 1993 the Board has also clarified that the provision under section 36(1)(viia) merely takes into account the quantum of the aggregate average advances of the rural branches for the purpose of quantifying the deduction allowable under that section but all the bad debts of both urban and rural branches of the bank should be first set off against the provision made under section 36(1)(vii a) and excess only, if any, should be allowed to be deducted under section 36(1)(vii). There is thus a definite nexus between the two sections. It may be incidentally added that a similar observation featured as paragraph 3.11 of the Report of the Comptroller and Auditor General of India on Direct Taxes for the year 1992-93 was accepted by the Ministry.

Incorrect computation of income of a financial corporation

4.10 Under the Income Tax Act, 1961, financial corporations engaged in providing long term finance for industrial or agricultural development in India, are entitled to special deduction of an amount transferred by them out of their profits to a special reserve account, up to an amount not exceeding 40 per cent of their total income as computed before making any deduction under Chapter VI – A. The deduction is to be limited to the amount of special reserve actually created in the accounts of the relevant previous year.

In Tamil Nadu charge, the assessment of a company engaged in promotion of small scale industries for assessment year 1992-93 was completed in a summary manner by computing 'nil' income after claiming the special deduction of Rs.57.49 lakhs. Audit scrutiny revealed that the assessee was allowed adjustment of brought forward losses of Rs. 99.64 lakhs and carry forward of remaining loss of Rs. 372.04 lakhs. Since the special deduction was to be allowed only on the income computed after setting off the losses of earlier years but before allowing any deduction

under chapter VI-A, the deduction availed by the assessee, which was apparent from return and documents accompanying it, was irregular. The incorrect allowance of deduction resulted in excess carry forward of Rs. 57.49 lakhs involving potential tax effect of Rs.29.75 lakhs besides levy of additional tax of Rs.5.95 lakhs.

The Ministry has not accepted the observation on the ground that the assessment was completed in a summary manner. The reply is not tenable since the information that there were losses of earlier years for set off against current year's income was available in the return of income. Further, section 36(1)(viii) specifically provides that this deduction shall be computed on the amount of total income and after setting off carried forward losses, before allowing deductions under Chapter VI-A.

Incorrect allowance of provisions

4.11 Under the Income Tax Act, 1961, losses other than capital losses that arise out of and are incidental to the business are allowable deductions in the computation of the profits and gains of the business. It has been judicially held* that in order that a loss be deductible, it must have actually arisen and been incurred and not merely anticipated as certain to occur in future. 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.

(i) In Gujarat charge, in the assessment of a widely held company for the assessment year 1988-89 completed after scrutiny in March 1991, the assessee claimed and was allowed a deduction of Rs.58.49 lakhs in respect of provisions for unserviceable or damaged stores and spare parts. As it was only a provision for anticipated loss and not an actually incurred loss, it should have been disallowed. Failure to do so resulted in under assessment of income of Rs.58.49 lakhs with consequent short levy of tax of Rs.30.71 lakhs.

The Ministry has accepted the audit observation.

(ii) In West Bengal charge, the assessments of a public sector company for assessment years 1990-91/1991-92 were completed in March 1993/July 1992 in a scrutiny/summary manner. Audit scrutiny revealed that the assessing officer had allowed deductions on account of

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* CIT vs. Indian Overseas Bank (1985) - 151 ITR 446(Mad)

provisions for doubtful debts, loss of assets and loss of stores aggregating Rs. 411.08 lakhs and Rs. 2324.48 lakhs respectively in two assessment years. As the provisions for bad debts and loss of stores were not ascertained liabilities and the loss on sale of fixed assets was to be absorbed within the relevant block of assets and treated as capital loss, these were not allowable deductions on the basis of information available in the accounts accompanying the return of income. Omission to disallow the deduction resulted in underassessment of income/overcomputation of loss by Rs. 411.08 lakhs/Rs. 2324.48 lakhs involving positive/potential tax effect of Rs.221.98 lakhs/Rs. 1069.26 lakhs for the two years respectively and non-levy of additional tax of Rs. 185.96 lakhs for assessment year 1991-92.

The reply of the Ministry to the audit observation has not been received.

Incorrect deduction in respect of reserve for shipping business

4.12 Under the Income Tax Act 1961, with effect from 1 April 1990, a public company formed and registered in India with the main object of carrying on the business of operation of ships is eligible for a deduction of an amount not exceeding the total income as debited to the profit and loss account of the previous year and credited to a reserve account. The total income for this purpose has to be computed after setting off all unabsorbed losses, allowance etc.of the earlier years.

In Tamil Nadu charge, the assessment of a company engaged in shipping business for the assessment year 1990-91 was completed in a scrutiny manner in January 1993 allowing the entire income of Rs.191.25 lakhs as deduction in respect of the reserve for shipping business. Audit scrutiny revealed that the assessee company had been allowed to carry forward unabsorbed losses, depreciation and investment allowance in the earlier assessment year amounting to Rs. 57 crores and hence the total income after setting off of part unabsorbed losses for the purpose of the deduction was 'nil'. The mistake of allowing the deduction resulted in excess carry forward of unabsorbed depreciation of Rs.191.25 lakhs involving a potential tax effect of Rs.103.28 lakhs.

The Ministry has accepted the audit observation.

Incorrect allowance of liability

4.13 Under the Income Tax Act, 1961, as applicable from the assessment year 1984-85, a deduction otherwise allowable under the Act in respect of any sum payable by the assessee by way of tax or duty, under any law for the time being in force, shall be allowed in computing the business income of that previous year in which such sum is actually paid by him and not merely on the basis of accrual of the liability. From 1 April 1988, tax or duty actually paid by the assessee on or before due date applicable in his case for furnishing the return of income shall also be allowed as deduction. From 1 April 1989, cess, fee or any sum payable by an assessee as employer by way of contribution to any provident fund, superannuation fund or gratuity fund etc. or any sum payable to an employee as bonus or commission for services rendered or any sum payable as interest on any loan from any public financial institution are also deductible on actual payment basis. No deduction in respect of contribution to the above funds is allowable unless such sum has actually been paid before the stipulated due date as specified under the relevant statute governing the funds. It has been judicially held* that the amount of sales tax collected by a trader in the course of business constitutes his trading or business receipts and as such is liable to be included in his business income.

(i) The assessment of a company in West Bengal charge, in which public are substantially interested for the assessment year 1990-91 was completed after scrutiny in March 1993 at a loss of Rs.169.65 lakhs. Audit scrutiny of the tax audit report and accounts submitted with the return of income revealed that Rs.64.57 lakhs debited to profit and loss accounts as taxes and duties for the previous year relevant to the assessment year 1990-91, was not paid within the relevant previous year or within the due date of submission of the return of income. However, the unpaid liability was omitted to be disallowed by the assessing officer. The omission resulted in excess computation and carry forward of loss by Rs.64.57 lakhs involving potential tax effect of Rs.34.87 lakhs.

The Ministry has accepted the audit observation.

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* Chowringhee Sales Bureau Pvt.Ltd.vs.CIT WB 87-ITR 542(SC), Sinclair Murray and Co. Pvt.Ltd. vs. CIT (1974) 97-ITR-615(SC)

(ii) The assessment of a public sector undertaking in West Bengal charge, for the assessment year 1990-91 was completed after scrutiny in March 1993. Audit scrutiny revealed that the amount of Rs. 1608.99 lakhs debited to the profit and loss account as taxes and cess for the previous year relevant to the assessment year 1990-91 was allowed as deduction though the same was not paid within the relevant previous year or within the due date allowed for furnishing the return of income. Omission to disallow the amounts led to overassessment of loss by Rs.1608.99 lakhs involving potential tax effect of Rs. 868.86 lakhs.

The reply of the Ministry to the audit observation has not been received.

(iii) In Kerala charge, in the assessment of a closely held company, for the assessment year 1990-91, completed in March 1993 after scrutiny, a deduction of Rs.41.43 lakhs towards disallowed liability of earlier year paid during the previous year relevant to the assessment year 1990-91 was allowed. Audit scrutiny revealed that out of the above deduction Rs.40.44 lakhs represented arrears of employer's contribution to provident fund relating to the accounting year 1988-89, paid on various dates between June and November 1989. Since the payments in question had not been remitted to the fund by the due dates prescribed under the relevant statute governing the funds, the deduction of Rs.40.44 lakhs should not have been allowed. Besides, the assessee was erroneously allowed a deduction of Rs.29.60 lakhs being employees' contribution to provident fund on the ground that the amount treated as income in earlier year under the Act was credited to the relevant welfare fund during the previous year relevant to the assessment year. Since the contribution had not been credited to the relevant fund by the due date prescribed, the allowance of expenditure of Rs.29.60 lakhs was also not in order. As the assessee was carrying on the business of growing and manufacturing tea, these mistakes resulted in underassessment of income of Rs.28.02 lakhs (40 percent of Rs.70.04 lakhs) involving short levy of tax of Rs.23.52 lakhs (including interest).

The Ministry has accepted the audit observation.

(iv) In West Bengal charge, the assessment of a closely held tea company for the assessment

year 1990-91 was completed after scrutiny in February 1993. Audit scrutiny revealed that out of Rs.359.97 lakhs debited to the profit and loss account on account of salaries, wages and bonus etc, Rs.59.72 lakhs was on account of unpaid bonus. Since there was no evidence that the amount was paid by the date of submission of return, it should have been disallowed. However, this was not done. As the assessee was a tea company, omission to disallow Rs.59.72 lakhs resulted in 40 per cent thereof (Rs.23.89 lakhs) escaping tax. The consequential short levy of tax was Rs.14.19 lakhs.

The Ministry has accepted the audit observation.

(v) In West Bengal charge, the assessment of a widely held banking company for the assessment year 1989-90 was completed in a summary manner in June 1990. Audit scrutiny revealed that Rs.193 lakhs towards provision for bonus payable to employees was allowed as deduction although there was no indication of the liability having been discharged within the relevant previous year or within the due date allowed for furnishing the return of income. Omission to disallow the unpaid liability resulted in underassessment of income by Rs.193 lakhs with a consequential undercharge of tax of Rs.121.59 lakhs including non levy of additional tax of Rs.20.26 lakhs.

The Ministry has accepted the audit observation.

(vi) In West Bengal charge, the assessment of a widely held company for assessment year 1989-90 was completed in June 1990 in a summary manner determining the loss at Rs.1919.32 lakhs. Audit scrutiny revealed that unpaid interest amounting to Rs.94.34 lakhs payable to different public financial institutions was debited to profit and loss account and allowed as deduction. There was no evidence of the liability having been discharged before the due date of filing the return. The unpaid liability, therefore, should have been disallowed. Failure to do so resulted in excess computation of loss by an identical amount involving a potential tax effect of Rs.49.53 lakhs and consequent non-levy of additional tax of Rs.9.91 lakhs.

The Ministry has accepted the audit observation.

(vii) In Kerala charge, in the assessments of a

company for the assessment years 1989-90 and 1990-91, completed in a summary manner in June and July 1991 respectively, interest amounting to Rs.52.28 lakhs and Rs.46.86 lakhs payable to public financial institution was allowed as deduction. Audit scrutiny revealed that the assessee company had not paid these amounts during the relevant previous years or by the due date of submission of returns of income. The amount of unpaid interest should, therefore, have been disallowed. Omission to do so resulted in excess carry forward of loss amounting to Rs.52.28 lakhs and Rs.46.86 lakhs for the assessment years 1989-90 and 1990-91 respectively involving a potential tax effect of Rs.52.62 lakhs and non levy of additional tax of Rs.10.52 lakhs in aggregate for the two assessment years.

The Ministry has accepted the audit observation.

(viii) In West Bengal charge, the assessment of a widely held company for the assessment year 1990-91 was completed in December 1991 in a summary manner computing income of Rs.220.01 lakhs being 30 percent of the book profit under special provision of the Act, as against the income of Rs.166.43 lakhs computed under the normal provision of the Act. Audit scrutiny revealed that an amount of Rs.68.46 lakhs being sales tax collected from the customers and not paid to Govt. account, had not passed through the relevant profit and loss account but appeared as a liability in the balance sheet. There was, however, no evidence on record of the liability having been discharged before the due date for filing of the return. Omission to treat the trading receipt as income resulted in underassessment of income by Rs.14.88 lakhs being the difference between the income calculated under normal and special provisions of the Act involving undercharge of tax of Rs.13.01 lakhs (including interest and additional tax).

The Ministry has not accepted the observation on the ground that the assessment was completed in a summary manner. While under the summary assessment scheme additional information may not be called for from the assessee, it cannot be the legislative intent that the information available in the records of the department should be ignored. In the present case the information that tax was collected but was neither paid to government account nor treated as income was available from the documents accompanying the return of income. To exclude

such receipt from the scope of summary assessment even though information was available in the records cannot be in conformity with the legislative intent.

Incorrect valuation of closing stock

4.14 Under the Income Tax Act, 1961, where the accounts are correct and complete, but the method employed is such that the income cannot properly be deduced therefrom, the computation will be made upon such basis and in such manner as the assessing officer may determine. If closing stock does not include any element of cost correctly, the assessing officer should conclude that the account does not reflect the true profits and should bring the under valuation of stock to tax. As per accounting principles, the stock of raw materials and finished goods at the close of an accounting year becomes opening stock in the succeeding accounting year.

(i) In Maharashtra charge, the assessment of a company for assessment year 1990-91 was completed after scrutiny in January 1993 computing income of Rs.314 lakhs. Audit scrutiny revealed that for the purpose of valuing finished goods and work in progress, the overhead absorption rate of 15 months was applied. Since the previous year comprised 12 months and all expenditure and income of those 12 months had been taken into account in computing taxable income, the overhead absorption rate of 12 months should have been applied. The omission led to value of inventories being lower by Rs.14.17 lakhs than that which should have been taken and consequential underassessment of income by a like amount leading to short levy of tax of Rs.12.85 lakhs (including interest).

The reply of the Ministry to the audit observation has not been received.

(ii) In West Bengal charge, the assessment of a company for the assessment year 1989-90 was completed after scrutiny in March 1993. Audit scrutiny revealed that while the closing stock figure on 31st December 1987 was shown as Rs.31.66 lakhs, the opening stock on 1 January 1988 was taken as Rs.41.56 lakhs. The higher valuation of opening stock by Rs.9.90 lakhs led to consequential underassessment of income to the same extent involving undercharge of tax by Rs. 11.20 lakhs (including interest).

The reply of the Ministry to the audit observation has not been received.

Other mistakes in the computation of business income

4.15(a) Under the Income Tax Act,1961, any sum paid by way of tax levied on the profits and gains of any business is not an allowable deduction.

The total income of a widely held company in Tamil Nadu charge for the assessment year 1990-91, was computed after scrutiny in November 1993 at a loss of Rs.76.24 lakhs after taking into account previous year's expenses of Rs.129.32 lakhs and receipts of Rs.20.59 lakhs. Audit scrutiny revealed that the previous years' expenses included provision of Rs.69.37 lakhs for income tax for the assessment years 1984-85, 1987-88 and 1989-90 and similarly the previous year's receipts included Rs.1.87 lakhs being excess income tax provision withdrawn. As tax on business profits is not an admissible deduction, the difference of Rs.67.50 lakhs should have been disallowed in computing the business income. Omission to do so, resulted in excess carry forward of loss by a like amount involving potential tax effect of Rs.36.45 lakhs.

The Ministry has accepted the audit observation.

(b) Under the Income Tax Act, 1961, depreciation on building, plant and machinery owned and used by the assessee for the purpose of his business is an allowable deduction. The Act further provides that from 1 April 1986 the expenditure on knowhow shall be deducted in equal instalments spread over six years and that expenditure in connection with travelling shall be allowed to the extent and subject to the prescribed conditions.

In Andhra Pradesh charge, the assessment of a widely held company for the assessment years 1989-90 and 1990-91 were completed after scrutiny in March 1992 computing losses at Rs.254.94 lakhs and Rs.728.03 lakhs respectively. Audit scrutiny revealed that the deductions aggregating Rs.33.49 lakhs and Rs.16.22 lakhs respectively and representing excess allowance of travelling expenses and expenditure on technical knowhow, and depreciation on damaged building, plant and machinery not used in the business of the assesee were allowed in two assessment years.

The erroneous allowance resulted in over computation of loss by identical amounts involving potential tax effect of Rs.26.34 lakhs in the aggregate.

The reply of the Ministry to the audit observation has not been received.

(c) Under the Income Tax Act, 1961, income under the head "profits and gains of business and profession" shall be computed in accordance with the method of accounting regularly employed by the assessee. Where an assessee follows mercantile system of accounting, the annual profits are worked out on due basis i.e., after providing all expenses for which a legal liability has arisen and taking credit for all receipts that have become due regardless of their actual receipt or payments.

(i) In Bihar charge, in the assessment of a public limited company for the assessment year 1990-91, the assessment of which was completed after scrutiny in March 1993, an amount of Rs.494.37 lakhs being expenditure relating to earlier years was debited to the profit and loss account of the relevant previous year. As the assessee was following mercantile system of accounting, the amount should have been disallowed and added back while determining taxable income of the assessee company. Omission to do so resulted in excess computation of loss of Rs.494.37 lakhs involving potential tax effect of Rs.227.41 lakhs.

The Ministry has accepted the audit observation.

(ii) In Gujarat charge, in the assessment of a widely held company for the assessment year 1989-90 completed in December 1991, the assessee claimed and was allowed a deduction of Rs.29.11 lakhs being rebate and adjustments of earlier years. There was no evidence on record to show that the said liabilities crystallised in the relevant year. This resulted in underassessment of income of Rs.29.11 lakhs with consequent short levy of tax of Rs.15.28 lakhs.

The Ministry has accepted the audit observation.

(d) Under the Income Tax Act, 1961, financial corporations engaged in providing long term finance for industrial development in India are entitled to a special deduction of an amount

transferred by them out of their profits to a special reserve account, not exceeding 40 percent of their total income as computed before making any deduction under this clause and Chapter VI of the Act. The Act also provides that deduction in respect of investment deposit account is not admissible unless the accounts of the business of the assessee for the previous year relevant to the assessment year for which deduction is being claimed have been audited by an accountant and the assessee furnishes, alongwith the return of income, the report of such audit in the prescribed form duly signed and verified by such accountant.

In Himachal Pradesh charge, in the assessments of a State Financial Corporation, for assessment years 1987-88 and 1988-89, completed in summary manner, audit scrutiny revealed that aforesaid special deduction of Rs.150.64 lakhs was erroneously allowed whereas the deduction actually worked out was Rs.96.87 lakhs (40 percent of business income of Rs.242.16 lakhs). The assessee was allowed further deduction of Rs.44.18 lakhs on account of investment deposit account though the prescribed audit report had not been furnished with the return. The mistake resulted in underassessment of income of Rs.97.95 lakhs involving tax effect of Rs.50.49 lakhs.

The Ministry has accepted the audit observation in full. However, on an appeal filed by the assessee against the additional demand of Rs.50.49 lakhs, the appellate authority deleted the addition made under section 32 AB. The additional demand has been consequently reduced to Rs.16.02 lakhs. Of this, Rs.10.76 lakhs is reported to have been collected.

Mistakes in the allowance of depreciation

4.16 Under the Income Tax Act, 1961, in computing the business income of an assessee, a deduction on account of depreciation on plant and machinery or other assets is admissible at the prescribed rates provided these are owned by the assessee and used for the purpose of his business during the relevant previous year. Depreciation on buildings and 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 Rules, 1962. Special rates of depreciation ranging from 15 to 100 percent are prescribed for certain specified items of machinery and plant. A general rate of 10 percent (15 percent from assessment year 1984-85) is prescribed in

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respect of machinery and plant for which no special rate has been prescribed.

From the assessment year 1988-89, the Taxation Laws (Amendment and Miscellaneous Provisions) Act, 1986 has prescribed same percentage of depreciation for assets falling under respective block of assets i.e. building, machinery, plant or furniture. For plant and machinery, the rates of depreciation are 33.33 percent and 50 percent depending on the category and for buildings for low paid employees of industrial undertakings, 20 percent as against the general rate of 5 percent for residential buildings and 10 per cent for non residential buildings. With the upward revision in the rates of depreciation, the extra shift allowance admissible on some items of plant and machinery has been discontinued. From the assessment year 1991-92, the Taxation Laws (Amendment) Act, 1991 has restricted the allowance of depreciation to seventy five percent of the amount admissible.

(i) In Tamil Nadu charge, in the assessment of a company for the assessment year 1990-91 completed in March 1993, depreciation of Rs.342.13 lakhs was allowed. While allowing depreciation, the assessing officer excluded from the cost of new machinery purchased during the previous year, a sum of Rs.14.87 lakhs relating to unused or uninstalled machineries, the particulars of which were furnished along with the return of income. Audit scrutiny revealed that according to these particulars, the cost of new machinery not installed/used was Rs.55.69 lakhs. Accordingly depreciation should have been disallowed on this amount. The mistake resulted in excess allowance of depreciation of Rs.13.61 lakhs, involving a short levy of tax of Rs.12.65 lakhs (including interest).

The Ministry has accepted the audit observation.

(ii) In Uttar Pradesh charge, the assessment of a company for the assessment year 1989-90 was completed after scrutiny in January 1992 allowing depreciation on buildings at the rate of 33.33 percent instead of the admissible rate of 10 per cent. The mistake resulted in excess carry forward of depreciation of Rs.49.10 lakhs involving potential tax effect of Rs.25.77 lakhs.

The Ministry has accepted the audit observation.

(iii) In Assam, Tamil Nadu and Karnataka charges, while completing the assessments of four companies for the assessment year 1991-92 between March 1992 to March 1993, depreciation in respect of block of assets was not restricted to seventy five percent as required under the Act resulting in excess allowance of depreciation/under assessment of income of Rs.282.04 lakhs involving tax effect of Rs.131.05 lakhs (including interest).

The Ministry has accepted the audit observations in all the cases.

(iv) In Uttar Pradesh charge, while completing the assessment of a company for the assessment year 1991-92 in a summary manner in March 1992, depreciation of Rs.2.65 crores was allowed which included depreciation on floating equipment. Audit scrutiny revealed that depreciation on floating equipments was allowed at the rate of 50 per cent instead of 33.33 per cent and the amount of depreciation was not restricted to 75 percent of the admissible amount as required under the Act. The mistakes resulted in excess allowance of depreciation by Rs.51.37 lakhs involving a potential tax effect of Rs.23.63 lakhs and non-levy of additional tax of Rs.4.72 lakhs.

The reply of the Ministry to the audit observation has not been received.

(v) In West Bengal charge, while completing the assessments of five companies for the assessment year 1991-92 between July 1992 to December 1992 depreciation in respect of block of assets was not restricted to the seventy five percent as required under the Act resulting in excess allowance of depreciation of Rs.249.35 lakhs involving potential tax effect of Rs.124.29 lakhs and additional tax of Rs.24.86 lakhs.

The Ministry has accepted the audit observations in four cases. Their response to other case has not been received.

Erroneous allowance of depreciation on fluctuations in exchange rates

4.17 Under the Income Tax Act, 1961, where an assessee has acquired any asset from a country outside India for the purpose of his business or profession and in consequence of a change in rate of exchange at any time after the acquisition of such asset, there is an increase or reduction in the liability of the assessee,

as expressed in Indian currency, for making payment towards the whole or a part of the cost of asset, the amount by which the liability aforesaid is so increased or reduced during the previous year shall be added to or reduced from the actual cost of the asset. Ministry of Law has since clarified in October 1984, that the benefit of addition to the actual cost of asset on change in the rate of exchange of currency is admissible only at the time of actual repayment of foreign currency loans and not on the outstanding balances of loans at any time. Any intermediate fluctuations in the rate of exchange would not be relevant for this purpose.

In Maharashtra, Madhya Pradesh and Gujarat charges, assessments of eight companies for the assessment years 1987-88 to 1991-92 were completed between February 1990 to March 1993. The assessees had made adjustments to the cost of plant and machinery on account of fluctuations in exchange rate and were allowed depreciation and investment allowance of Rs.309.38 lakhs on the enhanced cost. As the additions were on account of intermediate fluctuations in the rateof exchange and not at the time of repayment of loan, the depreciation and investment allowance allowed was irregular and resulted in short levy of tax of Rs.166.97 lakhs (including interest).

The Ministry has accepted the audit observation in all the cases.

Mistake in computing the written down value

4.18 Under the Income Tax Act, 1961, in computing the business income of an assessee, a deduction on account of depreciation on plant and machinery or other assest is admissible at the prescribed rates. Depreciation on buildings, plant and machinery is calculated on their cost or written down value according to the rates prescribed in the Income Tax Rules, 1962. Written down value means the actual cost of the assets to the assessee in the case of new assets acquired during the year or the actual cost less depreciation allowed(including additional depreciation as well as extra shift depreciation) in the case of an asset acquired in earlier years.

In Tamil Nadu charge, during the previous year relevant to the assessment year 1989-90, a widely held company had capitalised interest and commitment charges aggregating Rs.1186.83 lakhs on plant and machinery relating to

assessment years 1987-88 to 1989-90 and claimed depreciation thereon. Subsequently the assessee company requested the assessing officer to treat the above sum as revenue expenditure and withdraw depreciation thereon. In the assessment completed after scrutiny in March 1992, the assessing officer allowed Rs.969.82 lakhs as revenue expenditure for that year, the balance having been already allowed in the assessments of the respective assessment years and disallowed depreciation of Rs.692.25 lakhs on the capitalised amount. Audit scrutiny revealed that corresponding reduction in the closing written down value amounting to Rs.494.58 lakhs was not made by the assessing officer in the assessment order ibid. The mistake resulted in adoption of excess opening written down value by a like amount in the assessment for assessment year 1990-91 completed in March 1993 determining excess unabsorbed depreciaion by Rs.164.86 lakhs involving a potential tax effect of Rs.89.03 lakhs.

The Ministry has accepted the audit observation.

Incorrect grant of deduction in respect of investment allowance

4.19(a) Under the Income Tax Act, 1961, in respect of machinery owned by the assessee and used for the purpose of business carried on by him, a deduction by way of investment allowance shall be allowed to the assessee of a sum equal to 20 percent (25 per cent up to the assessment year 1988-89) of the actual cost of the machinery in the previous year of installation or in the previous year of first usage. Where for any assessment year, unabsorbed investment allowance cannot be set off against any other income in relevant year such unabsorbed investment allowance shall be carried forward to the following assessment year and shall be set off against profit and gains of business or profession of that year and if there is no positive income in that year also, it can be carried forward to the subsequent year for set off upto a maximum of eight assessment years immediately succeeding the assessment year for which the loss was first computed.

(i) In Bihar and West Bengal charges, the assessments of three widely held companies for the assessment year 1990-91 were completed after scrutiny in March 1993 after allowing deduction of Rs.3736.33 lakhs by way of

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investment allowance at the rate of 25 percent of the cost of the plant and machinery instead of the correct rate of 20 percent. This resulted in excess grant of investment allowance/excess carry forward of loss of Rs.746.46 lakhs involving tax effect of Rs.415.95 lakhs(including potential tax effect of Rs.386.09 lakhs and interest).

The Ministry has accepted the audit observation in all the cases.

(ii) In Karnataka charge, in the assessment of a closely held company for the assessment year 1989-90 completed after scrutiny in March 1992 an amount of Rs.87.01 lakhs being the unabsorbed investment allowance relating to the assessment year 1980-81 was allowed to be carried forward. As the unabsorbed investment allowance for the assessment year 1980-81 could not be carried forward beyond the assessment year 1988-89, the carry forward of unabsorbed investment allowance in the assessment year 1989-90 was not in order. The mistake resulted in excess carry forward of investment allowance of Rs.87.01 lakhs involving potential short levy of tax of Rs.50.25 lakhs.

The Ministry has accepted the audit observation.

(iii) In Karnataka charge, in the assessment of a widely held company for the assessment year 1991-92, completed in a summary manner in July 1992, and subsequently revised in November 1993, unabsorbed investment allowance of Rs.20.49 lakhs pertaining to assessment years 1987-88 to 1989-90 had been adjusted. The assessment for the assessment year 1990-91 was completed in March 1993 and the unabsorbed investment allowance of Rs.20.49 lakhs was allowed to be set off against the income of the assessment year 1990-91. Accordingly, the adjustment of unabsorbed investment allowance made in the assessment for the assessment year 1991-92 was required to be withdrawn. Failure to do so resulted in underassessment of income of Rs.20.49 lakhs and short levy of tax of Rs.12.44 lakhs.

The Ministry has accepted the audit observation.

(iv) In West Bengal charge, the assessment of a domestic company for the assessment year 1992-93 completed in a summary manner, at an income of Rs.2.53 lakhs in January 1993, unabsorbed investment allowance of Rs.132.97

lakhs relating to assessment years 1986-87 to 1990-91 was fully allowed as deduction instead of restricting the allowance to two-third of the amount. The excess allowance of deduction resulted in under assessment of income by Rs.44.32 lakhs with consequential undercharge of tax by Rs.27.52 lakhs (including additional tax of Rs.4.59 lakhs).

The Ministry has accepted the audit observation.

(b) The Ministry of Law clarified in April 1988 that no investment allowance is admissible to an assessee who has transferred his eligible assets to somebody else on hire/mortgage basis, whether as a solitary case or as a business activity.

In Gujarat and Madhya Pradesh charges, in the assessments of two companies for the assessment years 1989-90 and 1990-91, completed in March 1992 and March 1993 investment allowance amounting to Rs.15.05 lakhs was allowed on leased out plant and machinery resulting in underassessment of income by a like amount involving short levy of tax of Rs.12.46 lakhs including interest.

The Ministry has accepted the audit observations.

Incorrect grant of deduction in respect of investment deposit account

4.20(a) Under the Income Tax Act, 1961, in the case of an assessee whose total income includes 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 maintained by him with the Development Bank within a period of six months from the end of the previous year or before furnishing the return of income whichever is earlier, or has utilised any amount during the previous year for the purchase of any ship, new air craft, new machinery or plant without depositing any amount in a deposit account, is allowed a deduction equal to the amount deposited and/or any amount so utilised. The amount of deduction is, however, limited to 20 per cent of the profits of eligible business or profession as per audited accounts. The Act further provides that where separate accounts for eligible business are not maintained or are not available, the profits of eligible business shall be such amount which bears to the total

profits of business of the assessee, the same proportion as the total sales, turnover or gross receipts of the eligible business bears to the total sales turnover or gross receipts of the business carried on by the assessee.

The profits of the eligible business computed in accordance with the provisions of Companies Act, 1956, are increased/decreased by certain specified items debited/credited in the profit and loss account. The amount of depreciation debited to the relevant profit or loss account is one such item which is required to be added to the net profits. The amounts withdrawn from reserves or provisions credited to the profit and loss account are required to be deducted from the net profits. One of the purposes for utilisation of such amount specified under the scheme is repayment of the principal amount of term loans contracted after 31 March 1986, and taken for a period of three years or more, from institutions specified therein.

(i) In West Bengal charge, the assessments of two companies for the assessment year 1990-91 were completed after scrutiny in March 1993 allowing deduction of Rs.213.06 lakhs towards investment deposit account. Audit scrutiny revealed that Rs.110.25 lakhs being interest income from tax free bonds was wrongly included for computing the profits of eligible business. The omission resulted in excess allowance of deduction of Rs.11.25 lakhs involving short levy of tax of Rs.10.45 lakhs (including interest).

The Ministry has not accepted the audit observation stating that the Act did not prescribe any adjustment to exclude tax free interest from the eligible business profit for computing allowable deduction on account of investment deposit account. The reply is not tenable as the incentive deduction is allowed from the taxable income in terms of the Act and not from exempted income.

(ii) In Maharashtra charge, the assessment of a company for the assessment year 1990-91 was completed after scrutiny in February 1991 allowing deduction of Rs.29.64 lakhs towards investment deposit account. Audit scrutiny revealed that the assessee had total sale of Rs.4028 lakhs of which Rs.435 lakhs was attributed to eligible trading business. The profit of the business according to the audit report was Rs.457 lakhs. The assessee was thus entitled to a deduction of Rs.9.90 lakhs being 20 percent of the pro-rata profit of the

eligible business as against Rs.29.64 lakhs allowed. The excess allowance of deduction resulted in underassessment of income of Rs.19.74 lakhs involving short levy of tax of Rs.14.89 lakhs (including interest).

The Ministry has accepted the audit observation.

(iii) In West Bengal charge, the assessment of a widely held domestic company for the assessment year 1990-91 was completed after scrutiny in March 1993 allowing a deduction of Rs.3.28 crores under the investment deposit account. The assessing officer in computing the profit of eligible business for such deduction increased the profit by the amount of depreciation of Rs.18.24 crores which included Rs.5.49 crores representing transfer from revaluation reserve instead of restricting the amount of depreciation to Rs.12.75 crores debited to the relevant profit and loss account. Thus, the profit was incorrectly increased by Rs.5.49 crores. The incorrect increase led to excess allowance of deduction of Rs.1.10 crores involving short levy of tax of Rs.1.02 crores (including interest).

The reply of the Ministry to the audit observation has not been received.

(iv) In Maharashtra charge, the assessment of a company for the assessment year 1990-91 was completed after scrutiny in March 1993 allowing a deduction of Rs.168.08 lakhs on account of investment deposit account. Audit scrutiny revealed that while determining the eligible profits an amount of Rs.101.34 lakhs withdrawn from provisions for accumulated privilege leave made in the earlier years and credited to profit and loss account of the relevant previous year was not reduced from the net profit. After reducing the aforesaid amount, the eligible profits would work out to Rs.748 lakhs and the allowable deduction to Rs.149.76 lakhs as against Rs.168.08 lakhs allowed. This resulted in underassessment of income by Rs.18.32 lakhs involving short levy of tax of Rs.24.48 lakhs (including interest).

The Ministry has accepted the audit observation.

(b) Under the Income Tax Act, 1961, the eligible business means business other than the business of construction, manufacture or production of any article or thing specified in the list in the Eleventh Schedule, carried on

by an industrial undertaking, which is not a small scale industrial undertaking. The Act further stipulates that an industrial undertaking shall be deemed to be a small scale industrial undertaking if the aggregate value of the machinery and plant (other than tools, jigs and moulds) installed as on the last day of the previous year, where the previous year ends after the 17th day of March 1985, does not exceed thirty five lakh rupees.

In West Bengal charge, assessment of a closely held industrial company for the assessment year 1989-90 was completed after scrutiny in March 1992. The company engaged in the manufacturing of pilfer proof caps and having aggregate value of plant and machinery of Rs.55.95 lakhs was allowed a deduction of Rs.11.47 lakhs towards investment deposit account. A further deduction of Rs.9.55 lakhs was allowed in respect of profits and gains from industrial undertaking set up after 31 March 1981. As the plant and machinery was not used in a small scale industrial undertaking but used in the manufacturing of an item listed in the Eleventh Schedule to the Act, grant of the deduction was not in order. The mistake resulted in under assessment of income of Rs.21.02 lakhs involving short levy of tax of Rs.18.08 lakhs, (including interest).

The Ministry has not accepted the audit observation on the ground that the value of plant and machinery was beyond the specified amount because of the addition of cost of vehicles used in a separate 'truck division' and the rest of the machinery falls within the specified limits. Further, the assessee was registered as a small scale unit and the benefits of section 80-I could not be denied only because the articles manufactured were listed in the Eleventh Schedule and also that the year of allowability of the deductions for the first time was not assessment year 1989-90 but an earlier assessment year and the deductions allowed during this period were allowed only according to the extent of carry forward allowable. The reply of the Ministry is not tenable in view of the fact that the assessee company does not maintain separate accounts treating the truck division as a separate unit and the value of plant and machinery exceeded the prescribed limit of Rs. 35 lakhs. Further, neither the assessee company nor the assessing officer computed income for the assessment year 1989-90 separately. Moreover, deductions under sections 80-I and 32-AB were claimed and allowed on profits of

the business as a whole and no carry forward of allowances granted under two sections was involved in this case.

(c) The Board clarified in March 1988 that profits and losses of different units are to be considered together so that the deduction is available only on overall profits of the assessee.

In Haryana charge, the assessment of a widely held company, for the assessment year 1987-88, was completed in March 1989. Audit scrutiny revealed that the company had been allowed a deduction of Rs.256.39 lakhs on account of investment deposit account by limiting the deduction to 20 percent of the profits of two units only ignoring profits and losses of other three units for which new machinery was purchased. The omission to consider the trading results of all the five units resulted in excess deduction of Rs.40.27 lakhs involving undercharge of tax of Rs.20.13 lakhs.

The reply of the Ministry to the audit observation has not been received.

(d) Where there has been an amalgamation of a company owning an industrial undertaking or a ship with another company, and the Central Government, on the recommendation of the Specified Authority*, is satisfied that conditions specified in this behalf are fulfilled, the Central Government may make a declaration to that effect and thereupon, not withstanding anything contained in any other provisions of the Act, the accumulated loss and unabsorbed depreciation of the amalgamating company shall be deemed to be the loss or, as the case may be, allowance for depreciation of the amalgamated company for the previous year in which the amalgamation was effected and other provisions of the Act relating to carry forward and set off of loss and allowance for depreciation shall apply accordingly.

In Andhra Pradesh charge, the assessment of a widely held company, for the assessment year 1990-91, was completed in a summary manner in December 1991. The company had a taxable income of Rs.560.85 lakhs. During the relevant previous year, two sick companies were amalgamated with the assessee company. Audit scrutiny revealed that the assessee company was

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* "Specified authority" means such authority as the Central Government may, by notification in the official Gazette, specify for the purposes of the section.

erroneously allowed a deduction towards investment deposit account of Rs.135.85 lakhs and the balance income of Rs.425 lakhs was set off against the accumulated losses of the companies amalgamated during the previous year, instead of considering the total accumulated losses of Rs.584.41 lakhs Irregular deduction on account of investment deposit account of Rs.135.85 lakhs resulted in excess carry forward of an identical amount of loss involving potential tax effect of Rs.73.36 lakhs and non-levy of additional tax of Rs.14.67 lakhs.

The Ministry has accepted the audit observation.

Non creation of reserve

4.21 Under the Income Tax Act, 1961, in computing the business income of an assessee, a deduction is allowed by way of investment allowance at the rate of twenty per cent of the actual cost of new machinery or plant installed during the previous year, subject to the condition that an amount equal to seventy five percent of the allowance to be actually allowed is debited to the profit and loss account and credited to a reserve account.

(i) In Karnataka charge, in the assessment of a leasing company for the assessment years 1984-85 and 1985-86, investment allowance of Rs.6.27 lakhs and Rs.24.96 lakhs was allowed without creating the necessary reserve subsequent to appellate orders. The assessee company was allowed to carry forward the investment allowance. In the assessment year 1987-88 also the assessee did not create any reserve but claimed investment allowance of Rs.10.01 lakhs. The unabsorbed investment allowance of earlier years was set off against taxable income for the assessment year 1986-87 to 1988-89 and 1991-92 respectively. Audit scrutiny revealed that although the assessee company had made profits in assessment years 1986-87 to 1988-89 and 1991-92, it had not created sufficient reserves. The assessee was, therefore, not entitled to set off the unabsorbed investment allowance. The incorrect set off resulted in underassessment of income of Rs.22.69 lakhs for the assessment years 1986-87 to 1988-89 and 1991-92 with a short levy of tax of Rs.14.20 lakhs (including potential tax effect of Rs.3.18 lakhs).

The Ministry has accepted the audit observation. The assessments for the assessment years 1988-89 and 1991-92 have been rectified. For the assessment years 1986-87 and 1987-88, set off of unabsorbed investment allowance has been allowed against the reserve created in the assessment year 1993-94.

(ii) In Tamil Nadu charge, the assessment of a closely held company for assessment year 1990-91 was completed in March 1993 on a total income of Rs.14.46 lakhs under the special provisions relating to companies. While computing the income under the normal provisions of the Act, the assessing officer allowed the investment allowance of Rs.28.34 lakhs relating to assessment year 1989-90. Audit scrutiny revealed that the assessee had not created any reserve during assessment years 1989-90 and 1990-91. The mistake resulted in underassessment of income of Rs.24.78 lakhs involving short levy of tax of Rs.14.72 lakhs.

The reply of the Ministry to the audit observation has not been received.

Incorrect computation of capital gains

4.22 Under the Income Tax Act, 1961, as amended by the Finance Act, 1987 and effective from 1 April 1988, 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 the income of the previous year in which the transfer took place. For computing the long-term capital gains, the Act provides for certain deductions. The Central Board of Direct Taxes has also clarified that provisions relating to the exemptions will have to be applied first and the deductions of Rs.10,000 plus a percentage of the excess over Rs. 10,000 will be applied on the remaining part of the capital gains.

In Tamil Nadu charge, a closely held company sold 1.65 lakhs shares held by it in two other companies for a consideration of Rs.190.50 lakhs in the previous year relevant to assessment year 1990-91. The cost of acquisition of the shares was Rs.59.35 lakhs. Audit scrutiny revealed that the assessee company had disclosed income of Rs.1.55 lakhs from capital gains computed by first claiming the deduction of Rs.10,000 plus 30 percent of the excess over Rs.10,000 and then claiming the deduction towards the deposits made in

specified assets on the balance amount. This was not correct. The exemptions were to be allowed first and on the balance only the deduction of Rs.10,000 plus a percentage of the excess over Rs.10,000 was allowable. The taxable capital gain would correctly work out to Rs.28.60 lakhs as against Rs.1.55 lakhs brought to tax. The mistake resulted in an underassessment of income of Rs.27.05 lakhs involving a short levy of tax of Rs.39.63 lakhs(including interest).

The Ministry has accepted the audit observation.

Income not assessed

4.23(a) Under the Income Tax Act, 1961, any expenditure or trading liability incurred for the purpose of business carried on by the assessee is allowed as a deduction in the computation of business income. Where on a subsequent date, the assessee obtained any benefit in respect of such expenditure or trading liability allowed earlier, by way of remission or cessation thereof, the benefit that accrues thereby, shall be deemed to be profits and gains of business or profession to be charged to tax as the income of the previous year in which such remission or cessation takes place.

In Delhi charge, the assessment of a private limited company for assessment year 1988-89 was completed after scrutiny in May 1991 and revised in February 1993. Audit scrutiny revealed that out of a total refund of Excise Duty of Rs.124.56 lakhs received by the assessee, only Rs.32.11 lakhs was credited to profit and loss account and assessed as income. The balance of Rs.92.45 lakhs was treated as a current liability being amount refundable to customers. Since the liability for Excise Duty was allowed as deduction in earlier assessment year, the entire refund of Rs.124.56 lakhs should have been treated as income and assessed to tax. Omission to do so resulted in underassessment of income of Rs.92.45 lakhs involving short levy of tax of Rs.78.10 lakhs.

The Ministry has accepted the audit observation.

(b) Under the Income Tax Act, 1961, income chargeable under the head 'profits and gains of business or profession' is computed in accordance with the method of accounting

regularly employed by the assessee. Where an assesseee follows mercantile system of accounting, the net profit or loss is calculated after taking into account all the income actually received or accrued or deemed to have accrued as well as expenditure incurred and liabilities relating to the period, regardless of their actual receipt or payment. It has judicially been held* that income is accrued when the assessee has acquired a right to receive it.

A large number of mistakes were noticed in test audit during the year. Brief particulars of three representative cases are given below:

Sr. No.	State/CIT's charge	Asstt. year Date of Asstt	Section under which assessed	Nature of Mistake	Tax effect (in lakhs of rupees)
1.	West Bengal/ W.B.I	1989-90 & 1990-91 March 1992	143(3)	Accrued income of Rs.1215.23 lakhs from sale of power to State Electricity Boards on account of increased rate of tariff was not included in total taxable income. Incorrect carry forward of unabsorbed depreciation was also allowed.	806.14(P)
2.	Assam NE Region Shillong	1990-91 March 1993	144	Subscribed share capital was raised in the case of five companies. Assessing officer established the fact that additions could not be explained satisfactorily the investments be charged to tax. However, this was not done in the assessment resulting in underassessment of income of Rs.244 lakhs.	231.31 (including interest)
3.	West Bengal W.B.V	1990-91 Nov.1993	143(3)	Rs.79.13 lakhs realised by way of encashing suppliers' performances guarantee bond due to non-performance of contract by supplier was not brought to tax.	73.50

The reply of the Ministry to the audit observations has not been received.

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* CIT vs. Ashokbhai Chimanbhai (1965) 56 ITR 42(SC)

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(c) Under the Income Tax Act 1961, the income liable to tax under the head 'profits and gains of business or profession' shall be computed in accordance with the method of accounting regularly employed by the assessee. The Act also provides that total income of any previous year of a person who is a resident includes besides income earned in India, also the income that accrues or arises to him outside India during such year. The provisions of the Companies' Act was amended with effect from June 1988 to make it obligatory on the part of the companies to maintain their accounts on mercantile basis.

(i) In Maharashtra charge, the assessments of a company executing contracts abroad, for the assessment years 1989-90 and 1990-91 were completed after scrutiny in February 1992 and March 1993 respectively. Audit scrutiny of the assessment records revealed that the assessee was accounting for only those receipts which were actually remitted to India and not the entire receipts which were deposited in banks in Iran. This was accepted by the assessing officer. Since the income of Rs.438.03 lakhs and Rs.388.67 lakhs had accrued and was deposited in banks in Iran during the relevant previous years, it should have been included in the total income and brought to tax. Omission to do so resulted in underassessment of income aggregating Rs.826.70 lakhs leading to short levy of tax of Rs.439.83 lakhs for the assessment years 1989-90 and 1990-91.

The reply of the Ministry to the audit observation has not been received.

(ii) In Maharashtra charge, the assessment for assessment year 1990-91 of a company executing contracts abroad was completed in a scrutiny manner in January 1993. Audit scrutiny revealed that income realisable in foreign exchange was accounted for only to the extent it was actually received in India and income to the extent of Rs.34.89 lakhs pertaining to the relevant previous year was not accounted for. As the assessee was following mercantile system of accounting, accrued income of Rs.34.89 lakhs should have been brought to tax. Omission to do so resulted in underassessment of income by an identical amount involving short levy of tax of Rs.20.73 lakhs.

The reply of the Ministry to the audit observation has not been received.

(iii) In West Bengal, Delhi and Haryana

charges, the assessments of five assessee companies for the assessment years 1989-90 to 1992-93 were completed under summary assessment scheme in July 1991 to March 1993. Audit scrutiny revealed that while processing the return in the summary manner, the assessing officer omitted to consider sums aggregating Rs.90.13 lakhs representing amount of interest income, amount of award received in arbitration proceedings, accrued interest on deposits kept with the bankers, surplus grant received from government and amount of cash compensatory support, though the same were apparent from the auditor's report and other documents furnished with the return of income. Omission to do so resulted in underassessment of income aggregating Rs.90.13 lakhs involving short levy of tax of Rs.35.25 lakhs and potential tax effect of Rs.27.84 lakhs (including additional tax and interest).

The reply of the Ministry to the audit observation has not been received.

Incorrect set off and carry forward of losses

4.24(a) Under the provisions of the Income Tax Act, 1961, any profit or gains arising from the transfer of a capital asset is chargeable to income tax as 'capital gains' in the previous year in which the transfer took place. However, if there is a loss under the head 'capital gains' which cannot be set off in the relevant assessment year, it can be set off against income under the head 'capital gains' of the subsequent year or years upto eight assessment years.

In West Bengal charge, the assessment of a widely held company for the assessment year 1990-91 completed after scrutiny in March 1993 was revised in June 1993 at a total income of Rs.16.98 lakhs. Audit scrutiny revealed that the capital gains of Rs.37.71 lakhs earned by the assessee company during the previous year relevant to the assessment year 1990-91 was fully set off with the capital loss of Rs.50.60 lakhs of the assessment year 1987-88. It was noticed from the assessment records for the assessment year 1987-88 that the capital loss of Rs.50.60 lakhs claimed by the assessee company for the assessment year 1987-88 was disallowed by the assessing officer and this disallowance was further confirmed by CIT (Appeals) in his order of December 1992. As there was no capital loss, irregular set off of

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capital loss of Rs.37.71 lakhs of the assessment year 1987-88 with the capital gains of the assessment year 1990-91 resulted in under assessment of income by an identical amount involving undercharge of tax of Rs.35.43 lakhs (including interest).

The Ministry has accepted the audit observation.

(b) Under the provisions of the Income Tax Act, 1961, where the net result of the computation under the head 'Profits and gains of business or profession', is a loss to the assessee and such loss cannot be wholly set off against income under any other head of the relevant year, so much of the loss as has not been set off shall be carried forward to the following assessment year/years to be set off against the profits and gains of business or profession of those years.

(i) In West Bengal charge, the assessment of a widely held company for the assessment year 1990-91 was completed in March 1993 after scrutiny after setting off business loss of Rs.119.69 lakhs relating to assessment year 1987-88. Audit scrutiny revealed that the total loss of Rs.940.42 lakhs claimed by the assessee company for the assessment year 1987-88 was disallowed by the assessing officer. Since no loss for the assessment year 1987-88 was allowed to be carried forward, the incorrect set off of loss of Rs.119.69 lakhs against the income of assessment year 1990-91 resulted in underassessment of income to the same extent involving potential tax effect of Rs.64.63 lakhs.

The Ministry has accepted the audit observation.

(ii) In Tamil Nadu charge, the assessment of a company for the assessment year 1991-92, completed in January 1993 after scrutiny, the assessing officer computed 'nil' income after setting off inter alia, unabsorbed business loss of Rs.65.89 lakhs relating to assessment year 1984-85 and unabsorbed depreciation of Rs.11.84 lakhs relating to assessment years 1979-80 and 1980-81. Audit scrutiny however, revealed that for the assessment year 1984-85 a positive total income had been determined in the revision order of August 1987 instead of a loss and also the unabsorbed depreciation relating to assessment years 1979-80 and 1980-81 had already been fully set off against the income of the assessment year 1986-87 as

per the revision order in September 1992. The mistake of setting off these allowances again in the assessment year 1991-92 resulted in excess carry forward of unabsorbed depreciation of Rs.77.73 lakhs relating to assessment year 1988-89 involving a potential tax effect of Rs.35.76 lakhs.

The Ministry has accepted the audit observation.

(iii) In Tamil Nadu charge, in the assessment of a widely held company for assessment year 1990-91 completed after scrutiny in March 1993, a sum of Rs.17.15 lakhs being interest received by the assessee in advance from IDBI on capital gains bonds was included in the total business income of Rs.142.19 lakhs which was fully set off against the carried forward business loss aggregating Rs.147.47 lakhs. Audit scrutiny revealed that the aforesaid interest of Rs. 17.15 lakhs was correctly assessable under the head 'Income from other sources' and its set off against brought forward business losses was not proper. The mistake resulted in underassessment of income of Rs.17.15 lakhs involving undercharge of tax of Rs.10.26 lakhs (including interest).

The Ministry has accepted the audit observation.

(c) No loss shall be carried forward for more than eight assessment years immediately succeeding the assessment year for which the loss was first computed.

In Delhi charge, the assessment of a public limited company for the assessment year 1990-91 was completed after scrutiny in July 1992. Audit scrutiny revealed that sums of Rs.62.96 lakhs and Rs.7.87 lakhs representing business loss for the assessment years 1982-83 and 1986-87 respectively were incorrectly allowed to be set off from the positive income of Rs.70.83 lakhs, whereas only Rs.6.71 lakhs and Rs.3.86 lakhs representing unabsorbed depreciation for the assessment years 1982-83 and 1986-87 respectively should have been set off in the computation of business income of the assessee. The mistake resulted in under assessment of income of Rs.60.26 lakhs involving short levy of tax of Rs.50.76 lakhs(including interest and potential tax effect of Rs.46.76 lakhs).

The reply of the Ministry to the audit observation has not been received.

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(d) No loss under the head 'Profits and gains of business or profession' is allowed to be carried forward from 1 April 1985, 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 assessing officer.

(i) In Gujarat charge, assessment of a widely held company for the assessment year 1991-92, was completed in May 1992, after scrutiny allowing the carry forward of unabsorbed depreciation and business losses of Rs.233.78 lakhs pertaining to the assessment years 1984-85 to 1991-92. Audit scrutiny revealed that the said unabsorbed business loss inter-alia included Rs.33.30 lakhs relating to assessment year 1985-86, the return of which was voluntarily filed after expiry of due date prescribed for filing the same. There was nothing on record about seeking extension of time for filing of return by the assessee. The incorrect allowance of carry forward of business loss, resulted in underassessment of income of Rs.33.30 lakhs with potential short levy of tax of Rs.17.23 lakhs.

The Ministry has accepted the audit observation.

(ii) In West Bengal charge, in the case of a widely held company, engaged in the agency business of scooter and auto rickshaw, the assessment for the assessment year 1990-91 was completed in November 1992 after scrutiny determining 'nil' income after adjusting a loss of Rs.14.78 lakhs pertaining to earlier years. Audit scrutiny of the assessment records revealed that the loss of Rs.14.78 lakhs was incurred by the assessee in the business of manufacturing wool and yarn, which was discontinued in the previous year relevant to the assessment year 1990-91. The incorrect set off of loss of discontinued business against the income of another business resulted in underassessment of income of Rs.14.78 lakhs with consequential short levy of tax of Rs.11.46 lakhs (including interest).

The Ministry has accepted the audit observation.

(iii) In Himachal Pradesh charge, in the assessment of a company for the assessment year 1988-89 completed in December 1989, the assessing officer allowed the entire brought forward loss of Rs.21.64 lakhs pertaining to assessment years 1985-86 to 1987-88 to be

carried forward alongwith the current year's loss of Rs.6.64 lakhs. Audit scrutiny of the assessment records revealed that consequent upon the CIT(A)'s order, the assessment for the assessment year 1985-86 was framed denovo at a loss of Rs.3.53 lakhs and assessments for the assessment years 1986-87 and 1987-88 were treated as *non-est* and infructuous. The brought forward loss of Rs.3.53 lakhs only was, therefore, required to be allowed as carry forward and not Rs.21.64 lakhs for years prior to 1988-89. Consequently in the assessment year 1988-89, the assessee was entitled to carry forward total accumulated losses of Rs.10.17 lakhs and not Rs.28.28 lakhs as allowed by the assessing officer. The mistake resulted in excess carry forward of loss of Rs. 18.11 lakhs involving potential tax effect of Rs.10.46 lakhs.

The Ministry has accepted the audit observation.

(e) Under the Income Tax Act, 1961, as applicable from the assessment year 1989-90, where as a result of an order of scrutiny assessment or best judgement assessment or on revision, rectification or on settlement relating to any earlier assessment year and passed subsequent to the filing of the return of income processed under the summary assessment scheme for any subsequent year, there is any variation in the carry forward of loss, deduction, allowance or relief claimed in the return and as a result of that if any tax or interest is found due, an intimation shall be sent to the assessee specifying the sum so payable and such intimation shall be deemed to be a notice of demand and all the provisions of the Act shall apply accordingly and if a refund is due, it shall be granted to the assessee. Further, the intimation for any tax or interest due shall not be sent after the expiry of four years from the end of the financial year in which any such order was passed.

In Madhya Pradesh charge, the assessments of a company for the assessment years 1987-88 and 1988-89 were completed in November 1988 under summary assessment scheme allowing carry forward of unabsorbed business losses and

depreciation aggregating Rs.419.86 lakhs pertaining to assessment years 1981-82 to 1986-87. Audit scrutiny revealed that assessment for the assessment year 1986-87 was later revised in January 1992 determining the loss at 'nil' by disallowing the carry forward of unabsorbed business losses and depreciation of the above years. Consequently, assessment for the assessment years 1987-88 and 1988-89 which were required to be revised were not revised. The omission resulted in excess computation of loss by Rs.240.67 lakhs in assessment year 1988-89 involving potential tax effect of Rs.126.35 lakhs.

The Ministry has not accepted the audit observation on the ground that the mistake could have been rectified by the assessing officer on 31 March 1993 and that it was rectified on 16 March 1993. However, the fact remains that action was initiated by the assessing officer when it was brought to his notice by audit on 24 September 1992. Further, but for audit pointing out the omission, it was likely that its rectification would have been barred by limitation of time.

Mistakes in allowing deduction under Chapter VI-A

4.25 Under Chapter VI-A of the Income Tax Act, 1961, certain deductions are admissible from the gross total income of an assessee in arriving at the net income chargeable to tax. The overriding condition is that the total deduction should not exceed the gross total income of the assessee. Gross total income has been defined in the Act as the total income computed in accordance with the provisions in the Act before making the deductions under Chapter VI-A but after setting off unabsorbed losses, depreciation, investment allowance etc. of earlier years. Where the set off of unabsorbed loss, depreciation, investment allowance etc. of earlier years results in reducing the total income to 'nil' or to a loss, no deduction under Chapter VI-A is admissible.

In Madhya Pradesh charge, in the assessments of two private limited companies, for the assessment years 1991-92 and 1992-93 completed in March 1993, deductions of Rs.39.45 lakhs and Rs.47.71 lakhs were allowed towards their

profits and gains from newly established industrial undertaking in backward areas. Audit scrutiny revealed that while computing these deductions, the deductions of Rs.16.30 lakhs and Rs.23.15 lakhs allowed on account of brought forward unabsorbed investment allowance and depreciation respectively, allowed in the two assessment years were not reduced. The assessees were thus entitled to aggregate deductions of Rs.63.83 lakhs as against Rs.87.16 lakhs allowed. The mistake resulted in underassessment of income of Rs.23.33 lakhs with consequent short levy of tax of Rs.17.38 lakhs, including interest.

The Ministry has accepted the audit observations.

Incorrect deduction in respect of profits and gains from newly established industrial undertakings in backward areas

4.26 Under the Income Tax Act, 1961, where the gross total income of an assessee includes any profits and gains derived from an industrial undertaking in a backward area, there shall be allowed, in computing the total income of the assessee, a deduction from such profits and gains of an amount equal to twenty percent of the profits and gains. A further deduction at twenty five percent is admissible if the industrial undertaking goes into production within a period of ten years from 1 April 1981. One of the conditions for the grant of deductions is that the industrial undertaking is not formed by transfer of machinery and plant previously used for any purpose.

In Madhya Pradesh charge, a private limited company, engaged in dairy business, was allowed deductions of Rs.2.36 lakhs, Rs.2.38 lakhs and Rs.1.61 lakhs in assessment years 1989-90 to 1991-92, from its profits and gains as applicable for a newly established industrial undertaking in a backward area and of Rs.2.94 lakhs and Rs.2.98 lakhs in assessment years 1989-90 and 1990-91 respectively as applicable to a new industrial undertaking going into production after 31 March 1981. Audit scrutiny revealed that the assessee was disallowed investment allowance in the first assessment year 1983-84 itself as it had transferred to the new industrial undertaking machinery and

plant previously used by other persons and the disallowance had been upheld in appeal. Accordingly, both the above deductions were also not admissible to the industrial undertaking. The incorrect allowance of aggregate deductions of Rs.12.27 lakhs resulted in short levy of tax aggregating Rs.13.67 lakhs (including interest).

The Ministry has accepted the audit observation.

Incorrect allowance of deduction in respect of profits and gains from newly established small scale industrial undertakings in certain areas

4.27 Under the Income Tax Act, 1961, where the gross total income of an assessee includes any profits and gains derived from a small scale industrial undertaking, a deduction from such profits and gains of an amount equal to twenty percent thereof is allowed. For this purpose, an industrial undertaking is deemed as a small scale industrial undertaking, if the aggregate value of the machinery and plant installed for the purposes of the business does not exceed Rs.35 lakhs as on the last day of the previous year and for this purpose the value of any machinery or plant shall be the actual cost thereof to the assessee.

In Madhya Pradesh and Maharashtra charges, in the assessments of two companies for the assessment years 1991-92 and 1992-93 completed in a summary manner in March 1993, deduction of Rs.46.62 lakhs was allowed in respect of the newly established industrial undertaking. Audit scrutiny revealed that the aggregate value of plant and machinery on the last day of the relevant previous years exceeded Rs.35 lakhs and by virtue of the definition in the Act, the company was not a small scale industrial undertaking and as such the assessees were not entitled to the deduction. The mistakes resulted in underassessment of income of Rs.46.62 lakhs with consequent short levy of tax of Rs.36.85 lakhs (including interest and additional tax).

The Ministry did not accept the audit observation in the case of Maharashtra charge on the twin grounds that as per balance sheet the value of plant and machinery was Rs.31.26 lakhs which was less than Rs.35 lakhs and the issue involved was beyond the purview of prima facie adjustments to be made under section

143(1)(a). The reply of the Ministry is not tenable as the Act provides that for working out the value of the plant and machinery the actual cost to the assessee has to be determined and not the depreciated value. This was more than Rs.35 lakhs. Being an incorrect deduction allowed it would also come within the purview of prima facie adjustments. The Ministry has accepted the audit observation in the case of Madhya Pradesh charge.

Incorrect deduction in respect of profits from new industrial undertakings established after 31 March 1981

4.28(a) Under the Income Tax Act, 1961, where the gross total income of an assessee includes any profits and gains derived from a newly established industrial undertaking which goes into production after 31 March 1981, the assessee is entitled to a deduction of 25 percent of such profits provided the industrial undertaking does not manufacture or produce any article or thing specified in the Eleventh Schedule. It has been judicially held* that the use of the term 'derived from' in the relevant provisions of the Act indicates the restricted meaning given by the legislature to cover only the profits and gains directly accruing from the conduct of the business undertaking.

In Tamil Nadu charge, a widely held company engaged in the manufacture and sale of personal computers was also engaged in the trading of other finished goods such as printers, plotters, monitors, floppy discs, key boards etc. For the assessment years 1988-89 and 1990-91, the total turnover of the assessee company was Rs.1608.98 lakhs and Rs.6010.50 lakhs respectively which included the turnover of Rs.616.82 lakhs and Rs.1271.80 lakhs respectively relating to its trading activity. Audit scrutiny revealed that in the assessment for the assessment years 1988-89 and 1990-91, completed in March 1991 and February 1993, the assessee was allowed a deduction towards profits and gains from newly established undertakings at 25 percent of the entire profit of the business including the profits relating to the trading activities. As the deduction was admissible only in respect of the profits derived by the assessee from its manufacturing activity, the deduction allowed in respect of the entire profits was not in order. In the absence of separate accounts for the industrial undertaking, the profits have been worked out

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* Cambay Electric Supply Industrial Co.Ltd. vs. CIT Gujarat II - 113 ITR 84 (SC).
Sterling Foods vs. CIT Karnataka - 150 ITR 292 (Kar).

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on pro-rata basis indicating excess allowance of deduction of Rs.61.35 lakhs for these two years with consequent short levy of tax aggregating Rs.51.74 lakhs (including interest).

The Ministry has accepted the audit observation.

(b) Under the Income Tax Act, 1961, where the gross total income of an assessee being a company, includes any profits and gains derived from an industrial undertaking which goes into production within a period of nine years next following 31 March 1981, the assessee is entitled to a deduction of twenty five percent of such profits and gains for a period of eight years including the year in which he begins to manufacture or produce articles or things subject to the condition that the industrial undertaking is not formed by the transfer to a new business of machinery or plant previously used for any purpose and if so formed, the total value of the old machinery so transferred to the new business does not exceed twenty per cent of the total value of the machinery or plant used in the business.

In Tamil Nadu charge, in the assessments of two closely held companies for the assessment years 1990-91 and 1991-92, deduction of Rs.18.27 lakhs was allowed in respect of profits and gains from new industrial undertaking established after 31 March 1981. Audit scrutiny revealed that the industrial undertakings were formed in the previous years relevant to the assessment years 1983-84 and 1984-85 with old machinery constituting more than twenty percent and seventy seven percent respectively of the total value of the machinery used in the business. The assessees were not, therefore, entitled to the deduction allowed. The incorrect deduction resulted in undercharge of tax of Rs.16.56 lakhs (including interest).

The Ministry has accepted the audit observations.

(c) Under the Income Tax Act, 1961, prior to its amendment by Finance Act, 1980, with effect from assessment year 1981-82, where the gross total income of an assessee included any profits and gains derived from a newly established industrial undertaking which went into production before 1 April 1981, the assessee was entitled to tax relief in respect of such profits and gains upto 6 percent per annum of the capital employed in the

undertaking, in the assessment year in which the undertaking began to manufacture or produce articles and in each of the four succeeding assessment years. Where, however, such profits and gains fall 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. Further, under the Act as applicable to the assessment years 1984-85 to 1987-88, where in the case of a company, the aggregate amount of deductions admissible under certain specified provisions of the Act exceed seventy percent of the amount of the total income, the amount to be deducted is restricted to seventy percent of the total income.

In Gujarat charge, a closely held industrial company, claimed relief amounting to Rs.16.93 lakhs in respect of two plants established in the previous year relevant to assessment years 1983-84 and 1986-87. Owing to deficiency of profits in assessment years upto 1985-86, this set off was allowed in assessment years 1986-87 and 1987-88. However, this was not admissible since manufacturing operations started after 31 March 1981. Further, the assessee's total income for the assessment year 1986-87 was computed at 'nil' without restricting the deductions in respect of certain specific items of deductions to seventy percent of the pre-incentive total income, as required under the Act. In addition, the assessee company was also allowed deduction of Rs.2.58 lakhs in assessment year 1987-88, in respect of brought forward investment allowance of assessment year 1985-86, which was however fully adjusted in assessment year 1986-87. The aforesaid mistakes resulted in underassessment of income aggregating Rs.23.08 lakhs with consequent short levy of tax of Rs.12.80 lakhs.

The Ministry has accepted the audit observation.

Incorrect allowance of relief in respect of export turnover

4.29(a) Under the Income Tax Act, 1961, an assessee being an Indian company or other assessee, resident in India, engaged in export business, is entitled to a deduction equal to the profits derived from the export of all goods or merchandise other than the exempted items, if the sale proceeds thereof are received or are receivable in convertible foreign exchange. Where the business of the assessee does not consist exclusively of export

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of goods/merchandise, profit derived from export shall be the amount which bears to the profit of the assessee as computed under the head 'profits and gains of business or profession' the same proportion as export turnover bears to the total turnover. Further, in cases where the income chargeable under the normal provisions of the Act is more than that computed under the special provisions of the Act, the special provisions are not required to be invoked. The Act further provides that where the assessee is a supporting manufacturer exporting goods or merchandise through export/trading house, the deduction shall be allowed subject to the condition that a certificate in the prescribed form has been issued by the export/trading house specifying the amount of export turnover and such a certificate has been furnished alongwith the return of income by the supporting manufacturer. For this purpose in a case where the business carried on by the supporting manufacturer does not consist exclusively of sale of goods or merchandise to one or more export house, profits derived by it from the sale of goods or merchandise shall be the amount which bears to the profits of the business as computed under the head 'profits and gains of business or profession' the same proportion as the turnover in respect of sale to the respective export house bears to the total turnover of its business.

(i) In Maharashtra charge, in the assessment of a company, for the assessment year 1989-90, completed in March 1992 after scrutiny, a deduction of Rs. 398 lakhs in respect of export turnover was allowed as claimed by the assessee. Audit scrutiny revealed that the export turnover of the company during the relevant previous year was Rs. 1365 lakhs against total turnover of Rs. 7018 lakhs. Profits of the business as computed by the assessee company were Rs. 2047 lakhs. In pursuance of an appellate order, the assessment was revised in October 1992 and subsequently in May 1993 whereby the profits of the business computed under the normal provisions were reduced to Rs. 1572 lakhs before allowing other deductions under Chapter VI-A, but the deduction in respect of export turnover was not revised on pro rata basis by reducing the same to Rs. 306 lakhs as against Rs. 398 lakhs allowed. Considering the deduction of Rs. 306 lakhs alongwith other admissible deductions under Chapter VI A, the income computed under the normal provisions of the Act would be Rs. 642 lakhs which was required to be taxed

instead of the income of Rs. 610 lakhs computed under the special provisions of the Act. The omission resulted in underassessment of income of Rs. 31.75 lakhs with consequent short levy of tax of Rs. 18.33 lakhs.

The Ministry has accepted the audit observation.

(ii) In Maharashtra charge, the assessment of an assessee company, for the assessment year 1991-92, was completed in January 1992 after scrutiny allowing a deduction of Rs.36.74 lakhs in respect of export profits. Audit scrutiny revealed that during the previous year relevant to the assessment year 1991-92, the company had made total exports of Rs.724.78 lakhs which comprised direct export of Rs.67.37 lakhs and export of Rs.657.41 lakhs through other export houses. According to the auditor's report, the profit derived by the assessee as a supporting manufacturer from export through export houses, was Rs.33.33 lakhs. The assessee had filed certificates showing an export of Rs.27.48 lakhs only. In the absence of a certificate in respect of export of Rs.629.92 lakhs, the proportionate profit of Rs.31.93 lakhs attributable to export through export houses, should not have been allowed as deduction. The incorrect allowance resulted in underassessment of income of Rs.31.93 lakhs with consequent short levy of tax of Rs.18.36 lakhs.

The Ministry has accepted the audit observation.

(iii) In Tamil Nadu charge, an assessee company, having two separate units (one for local sales and the other exclusively for exports) and maintaining separate accounts, claimed the entire profit of the export unit of Rs.88.20 lakhs for the assessment year 1989-90, as deduction in respect of export turnover. The assessing officer, in the assessment completed in March 1992, in a summary manner, however, computed the export profit on pro-rata basis and allowed the deduction at Rs.51.82 lakhs. Details for working out the deduction were not available in the assessment records. Audit scrutiny revealed that the export turnover was 27.25 percent of the total turnover. The export profit, applying this percentage on the total business profits of Rs.150.40 lakhs worked out to Rs.40.99 lakhs. Similarly, the assessee claimed the entire profit of Rs.209.23 lakhs relating to the export unit for the assessment year 1991-92. The claim was allowed by the assessing officer completing the assessment in

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a summary manner in August 1992. In that year according to the details furnished in the return, the export turnover was 34.05 percent of the total turnover and on this basis, the admissible deduction towards export turnover worked out to Rs.91.31 lakhs. The aggregate excess deductions for the two assessment years thus worked out to Rs.128.75 lakhs with consequent short levy of tax of Rs.92.10 lakhs (including levy of additional tax for assessment year 1991-92 and interest).

The Ministry has accepted the audit observation.

(b) It has been judicially held* that Central Excise Duty and Sales Tax collected form part of the turnover of manufacturer.

In Maharashtra charge, in the assessment of two companies for the assessment years 1990-91 and 1992-93 completed in February and March 1993, deductions aggregating Rs.191.60 lakhs were allowed in respect of export profits. Audit scrutiny revealed that the total turnover of the companies aggregating Rs. 52.07 crores considered for computing the deduction in respect of such profits of the business did not include Central Excise Duty and Sales Tax included in total sale value of the goods. Considering the total turnover of Rs.60.42 crores including Central Excise Duty and Sales Tax, the aggregate deduction allowable would work out to Rs.115.87 lakhs as against Rs.141.60 lakhs allowed by the department. The incorrect allowance of deduction resulted in underassessment of income of Rs.25.73 lakhs with consequent short levy of tax of Rs.16.28 lakhs (including additional tax and interest)

The Ministry has not accepted the audit observation in one case on the ground that the issue raised is debatable and could not be taken care of at the time of processing the return under summary scheme. The reply is not tenable in view of the Supreme Court decision cited above and the fact that information relating to Central Excise Duty and the Sales Tax paid was available in the documents accompanying the return. Their response to the remaining case has not been received.

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* Mc Dowell & Co. Ltd. vs. C.T.O - 154 ITR 148(SC)

Incorrect deduction in respect of inter-corporate dividends

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

(i) In West Bengal charge, the assessment of a widely held company, for the assessment year 1990-91, was completed in March 1993 after scrutiny, at a loss of Rs.3.36 lakhs after allowing a deduction of Rs. 19.88 lakhs(60 percent of Rs.33.14 lakhs) towards inter-corporate dividends. Audit scrutiny revealed that as the assessee company had unabsorbed losses of Rs.129.53 lakhs pertaining to the assessment year 1989-90 the deduction for inter-corporate dividend was required to be allowed from the income arrived at after setting off the losses. Considering the brought forward losses, the income of the assessee company would result in a loss of Rs.113.01 lakhs and no deduction for inter-corporate dividend was admissible. The incorrect deduction led to excess carry forward of loss by Rs.19.88 lakhs with consequent potential tax effect of Rs.10.74 lakhs.

The Ministry has accepted the audit observation.

(ii) In Gujarat charge, in the assessment of an assessee company, for the assessment year 1991-92, completed in a summary manner in January 1992, a deduction of Rs.155.47 lakhs was allowed in respect of inter-corporate dividend, being 60 per cent of the gross amount of dividend of Rs.259.11 lakhs. This was done before deducting therefrom the amount claimed as deduction in respect of special reserve of 40 percent, amounting to Rs.103.64 lakhs. This resulted in excess deduction of Rs. 62.19 lakhs with consequent short levy of tax of Rs.34.33 lakhs (including additional tax).

The Ministry did not accept the audit observation on the ground that the assessment was completed in a summary manner. The reply

is not tenable. Being an incorrect deduction it would come within the purview of prima facie adjustments.

Non levy of minimum tax due to omission to restrict certain deductions

4.31 Under the Income Tax Act, 1961, as applicable to the assessment years 1984-85 to 1987-88, where in the case of a company, the aggregate amount of deductions, admissible under certain specified provisions of the Act, exceed seventy percent of the amount of the total income, the amount to be deducted is restricted to seventy percent of the total income.

In Maharashtra and Uttar Pradesh charges, the assessments of two companies for the assessment year 1987-88 were revised in January 1991 and March 1992. Similarly, in Karnataka charge, the assessment for assessment year 1985-86 of a company was revised in January 1992. Audit scrutiny revealed that the maximum permissible deductions under Chapter VI-A were not restricted to seventy percent of the pre-incentive total income under the special provisions of the Act in these three cases. The omissions resulted in underassessment of income aggregating Rs. 48.38 lakhs with consequent non-levy of minimum tax of Rs. 34.64 lakhs (including interest).

The Ministry has accepted the audit observation in two cases. Their response for the remaining one case has not been received.

Mistakes in levy of minimum tax on book profits of companies

4.32 Under the Income Tax Act, 1961, with effect from the assessment year 1988-89 to 1990-91, the income chargeable to tax of any company other than a company engaged in the business of generation of electricity, whose total income as computed under the normal provisions of the Act in respect of any previous year is less than 30 percent of its book profit, shall be deemed to be the amount equal to 30 percent of such book profit. For this purpose book profit means the net profit shown in the profit and loss account for the relevant previous year prepared in accordance with the provisions of Companies Act, 1956, subject to certain additions/deletions as mentioned in the provision on computation of income under the normal provision.

A review of assessments of companies for the assessment years 1988-89 to 1990-91 involving

application of section 115-J was carried out during 1992-93, and important findings including non-levy of minimum tax, incorrect computation of book profits and omission to invoke provisions of minimum tax while giving effect to appellate orders were featured in para 2.3 of the Report of the Comptroller and Auditor General of India for the year ended 31 March 1993 (Revenue Receipts-Direct Taxes). The legal position as emerging out of irregularities and mistakes pointed out in the review was accepted by the Ministry in principle. Some more mistakes in application of the provisions of this section are illustrated in the succeeding paragraphs.

(a) Under the special provisions, where the total income as computed under normal provisions of the Act in respect of any previous year is less than 30 percent of its book profit, the income chargeable to tax shall be deemed to be the amount equal to 30 percent of such book profit. The provision is required to be invoked even in cases where computation of income under the normal provisions of the Act results in 'nil' income or loss.

(i) The assessments of 5 companies, for the assessment years 1989-90 and 1990-91, assessed in Orissa, Delhi, Uttar Pradesh and Gujarat charges, were completed between June 1990 and November 1992 at 'nil' income though the companies had book profits aggregating Rs. 98.27 lakhs. Similarly, in case of 2 companies assessed in Gujarat charge, the assessments for the assessment years 1988-89 and 1989-90, were completed in March 1991 and May 1990 respectively at total income aggregating Rs. 5.66 lakhs though the companies had book profit aggregating Rs. 56.37 lakhs. In all these cases the assessing officers were required to levy minimum tax at 30 percent of the book profits. Omission to do so resulted in under assessment of income aggregating Rs.40.73 lakhs with consequent short levy of tax of Rs.30.29 lakhs (including interest).

The Ministry has accepted the audit observation in one case of Gujarat charge. Their response to the remaining cases has not been received.

(ii) In Maharashtra charge, the assessment of a company for the assessment year 1989-90, was completed in February 1992 on a total income of Rs. 61.68 lakhs under the normal provisions of the Act, as the income computed under the special provisions of the Act was Rs. 46.38 lakhs. The assessment was revised in February

1993 to allow a relief amounting to Rs. 21.85 lakhs pursuant to appellate orders and the revised total income was worked out at Rs. 36.24 lakhs which was brought to tax. This was not in order as the amount computed under the special provision of the Act was more and was required to be taxed. The omission resulted in under assessment of income by Rs.10.13 lakhs with consequent short levy of tax of Rs.7.32 lakhs (including interest).

The Ministry has accepted the audit observation.

(b) 'Book profit' means the net profit shown in the profit and loss account for the relevant previous year prepared in accordance with the provision of the Companies Act, 1956, subject to certain additions/deductions. The profit and loss account of the company shall give a true and fair view of the profit and loss of the company for the relevant financial year.

In Tamil Nadu charge, the assessment of a public company, engaged in the business of civil and mechanical works, drilling of development wells for ONGC etc., for the assessment year 1990-91, was completed at 'nil' income as returned under the special provisions of the Act in March 1993 since the income computed under the normal provisions was also a loss. Audit scrutiny revealed that an amount of Rs. 1209.38 lakhs towards debenture issue expenses, shown as capital expenditure in the company's printed accounts, was shown as revenue expenditure in the profit and loss account for income tax purposes, which clearly did not give the true and fair view of the company's profit and loss account. Disallowance of this expenditure would have resulted in a profit of Rs. 607.29 lakhs and 30 percent thereof i.e., Rs. 182.19 lakhs was liable to be assessed as income instead of 'nil' income as adopted. Accordingly there was a short levy of tax of Rs. 161.37 lakhs (including interest).

The Ministry has accepted the audit observation.

(c) 'Book profit' has been defined in the Act, as the net profit shown in the profit and loss account of the relevant previous year, as increased by the amount or amounts set aside as provisions made for meeting liabilities other than ascertained liabilities.

In Karnataka and Maharashtra charges, in the assessment of two companies, for the assessment year 1990-91, provision for estimated arrears of salary and for interest on scooter booking advance etc., amounting to Rs. 1194.45 lakhs charged to profit and loss account of the relevant previous years were not added back to arrive at the correct amount of 'book profit'. The omission to add back the amounts set apart for unascertained liabilities resulted in short computation of 'book profit' by an identical amount resulting in underassessment of income of Rs. 358.33 lakhs with consequent short levy of tax aggregating Rs.276.27 lakhs (including interest).

The Ministry has accepted the audit observation in the case of Karnataka charge. Their response to the remaining case has not been received.

(d) In cases where the company has brought forward business losses, as well as unabsorbed depreciation to be set off against the book profit, the lesser of the two will be set off in accordance with clause (b) of the first proviso to sub-section (1) of the section 205 of the Companies Act, 1956. The Board has also issued instructions in September 1987 on similar lines.

In Gujarat and Delhi charges, while computing the book profit in case of two companies, for the assessment year 1989-90, in January 1991 and February 1991, unabsorbed depreciation of earlier years amounting to Rs. 33.03 lakhs was reduced from the book profit though the companies had no unabsorbed business loss. Similarly, in the case of another company in Gujarat charge, in the assessment for the assessment year 1989-90 completed in March 1991, book profit was reduced by an amount of Rs. 2.62 lakhs of investment allowance though the company had unabsorbed depreciation of Rs. 32.60 lakhs and unabsorbed business loss was 'nil'. Accordingly, the lesser of the two amounts was to be deducted while computing the book profits. The omission resulted in short computation of book profit of Rs.35.65 lakhs involving under assessment of income of Rs.12.53 lakhs with consequent short levy of tax of Rs.9.28 lakhs (including interest).

The Ministry has accepted the audit observation in the case of Gujarat charge. Their response to the remaining case has not been received.

(e) Under the Act, it has been specifically provided that the provision regarding minimum tax on book profit would not affect the carry forward of unabsorbed depreciation, investment allowance, business losses etc. to the extent not set off. These would be governed by the provision applicable to normal computation of total income.

In Tamil Nadu charge, the assessment of a widely held company, for the assessment year 1990-91, was completed in November 1992, on a taxable income of Rs. 4326.75 lakhs. This was arrived at after deducting a sum of Rs. 2377.79 lakhs being the carried forward unabsorbed depreciation, investment allowance etc, of assessment years 1985-86 to 1988-89. Audit scrutiny revealed that for the assessment year 1989-90, the income was computed in March 1990 at Rs. 33.81 crores by the assessee but it had set off only Rs. 15.47 crores leaving a sum of Rs. 23.78 crores to be carried forward for the next year on the ground that tax had been paid on the income of Rs. 18.34 crores under the special provisions and that this would not be set off against past losses. It was further observed that assessment for the assessment year 1988-89 was completed in January 1990 determining the past losses to be carried forward at Rs.30.49 crores. Taking into account the unabsorbed allowances as per the completed assessment for assessment year 1988-89, the entire loss of Rs.30.49 crores was capable of being absorbed by the income of Rs.33.81 crores computed for the assessment year 1989-90. No amount was, therefore, to be set off against the income of assessment year 1990-91. The incorrect set off of Rs.23.78 crores in assessment year 1990-91 resulted in undercharge of tax of Rs.17.73 crores including withdrawal of interest granted on the refund and levy of interest for short payment of advance tax.

The Ministry has accepted the audit observation.

Excess refund of tax

4.33 Under the Income Tax Act, 1961, where as a result of any order passed in assessment, appeal, revision or any other proceedings under the Act, refund of any amount becomes due to the assessee, the assessing officer may grant the refund in cash or adjust or set off the refund against outstanding dues of the assessee.

(i) In West Bengal charge, the return of a widely held company for the assessment year 1990-91 was initially processed in February 1991 determining tax of Rs.123.96 lakhs refundable to the assessee of which, a sum of Rs.77.58 lakhs only was refunded through adjustment against the demand for the assessment year 1989-90. The assessment for the assessment year 1990-91 was subsequently scrutinised in March 1993 computing income at Rs.957.21 lakhs and tax at Rs.516.89 lakhs. On adjustment of prepaid taxes of Rs.520.73 lakhs (advance tax Rs.518 lakhs and tax deducted at source Rs.2.73 lakhs), a sum of Rs.3.84 lakhs was computed as refundable to the assessee. However, in doing so, the amount of Rs.77.58 lakhs already refunded by adjustment against the demand for the assessment year 1989-90, was not considered. The mistake resulted in excess grant of refund of Rs.73.74 lakhs for the assessment year 1990-91 made by way of adjustment against the demand for the assessment year 1989-90.

The Ministry has accepted the audit observation.

(ii) In West Bengal charge, in the assessment of a non-resident company for the assessment year 1987-88 originally completed in March 1990 and subsequently revised in July 1991, a demand of Rs.51.16 lakhs was raised. Audit scrutiny revealed that out of the said demand, the assessing officer adjusted Rs.8.41 lakhs only along with another demand of Rs.1.94 lakhs pertaining to the assessment year 1988-89, against a refund of Rs.115.84 lakhs due to the assessee and a net refund of Rs.105.49 lakhs was granted to him in March 1992. Failure to adjust the entire demand of Rs.51.16 lakhs pertaining to assessment year 1987-88 against the refund due resulted in excess refund of Rs.42.75 lakhs.

The Ministry has accepted the audit observation.

(iii) In West Bengal charge, the assessment of a widely held company for assessment year 1990-91 initially processed in a summary manner in November 1991 was completed after scrutiny in March 1993. Audit scrutiny revealed that while raising demand, the assessing officer omitted to withdraw Rs.12.87 lakhs being interest paid to the assessee. The mistake resulted in excess payment of interest of Rs. 12.87 lakhs to the assessee.

The Ministry has accepted the audit observation in principle.

(iv) In Karnataka charge, the assessment of a widely held company for the assessment year 1989-90 completed in October 1991 after scrutiny was revised in March 1992 to give effect to an appeal order. Audit scrutiny revealed that taking into account the tax due and also the refunds already granted, the assessee company was entitled to a refund of only Rs.159.16 lakhs as against Rs.169.41 lakhs authorised in March 1992. The mistake resulted in excess refund of Rs.10.25 lakhs.

The Ministry has accepted the audit observation.

Short levy of interest for short payment of advance tax

4.34 Under the Income Tax Act, 1961, where in any financial year, an assessee who is liable to pay advance tax, has failed to pay such tax or where the advance tax paid by such assessee is less than ninety percent of the assessed tax, the assessee shall be liable to pay simple interest at the rate of two percent for every month or part of a month comprised in the period from 1 April next following such financial year to the date of determination of total income on regular assessment or to the date on which the tax is so paid by way of self assessment tax on the amount equal to the assessed tax, or as the case may be, on the amount by which the advance tax paid falls short of the assessed tax.

(i) In West Bengal and Uttar Pradesh charges, the assessments of five companies for the assessment years 1989-90 and 1990-91 were completed/revised between March 1990 to March 1993 with a tax demand of Rs.149.41 lakhs. Audit scrutiny revealed that the advance tax paid by the assessees fell short of ninety percent of the assessed tax. The assessees were thus liable to pay interest calculated at the rate of two percent for every month or part of a month comprised in the period from first day of April next following the relevant financial year to the date of regular assessment. Omission to do so led to non-levy of interest of Rs.26.66 lakhs.

The Ministry has accepted the audit observation in all cases.

(ii) In Andhra Pradesh charge, assessments of four widely held companies for the assessment year 1990-91 were completed after scrutiny in March 1993. Audit scrutiny revealed that interest for short payment of advance tax was calculated upto the date of completion of summary assessments instead of till the date of completion of scrutiny assessments resulting in short levy of interest of Rs. 43.64 lakhs.

The Ministry has accepted the audit observation.

Interest for delay in payment of tax demand

4.35 Under the Income Tax Act, 1961, as amended from 1 April 1989, any demand for tax should be paid by an assessee within thirty days (thirty-five days prior to the assessment year 1989-90) of service of notice of the relevant demand. Failure to do so would attract interest at twelve percent per annum (fifteen percent per annum from 1 October 1984 and one and one half percent per month or part thereof from 1 April 1989) from the date of default till actual payment. In November 1974, the Central Board of Direct Taxes issued instructions that interest for belated payment of tax should be calculated and charged within a week of the date of final payment of the tax demand. It issued further instructions in June 1991 that demand for such interest should be raised before 30 April on the balance of demand due from the assessee as on 31 March of the year.

(i) In Tamil Nadu charge, the assessment of a widely held company for the assessment years 1988-89 and 1989-90 were revised in November 1991 and October 1992 computing income of Rs.194.54 lakhs and Rs.581.92 lakhs and the demands payable worked out to Rs.33.56 lakhs and Rs.184.88 lakhs respectively, which were not paid by the assessee company. Audit scrutiny revealed that though the instructions of the Board require the assessing officer to calculate the interest payable on such demand upto the end of the financial year, interest was calculated only upto November 1991 for assessment year 1988-89 and no interest was levied for assessment year 1989-90. This resulted in short levy of interest of Rs.38.56 lakhs for the two assessment years.

The Ministry has accepted the audit observation. Interest due is yet to be quantified.

(ii) In West Bengal charge, the assessments of a widely held company for the assessment year 1985-86 was originally completed in March 1988 and demand of Rs.11.32 lakhs was raised. The demand was increased to Rs.13.54 lakhs after re-assessment proceedings in March 1992, and was adjusted against refunds due. As the demand was paid beyond the permissible period of 35 days from the date of service of demand notice, the assessee company was liable to pay interest amounting to Rs.11.83 lakhs, which was not levied.

The Ministry has accepted the audit observation.

(iii) In Tamil Nadu and West Bengal charges, the assessments of three companies for the assessment years 1984-85, 1986-87, 1987-88 and 1989-90 were completed/revised between July 1986 to March 1992. The demands were reduced/increased after giving effect to appellate orders. Audit scrutiny revealed that demands were paid beyond the permissible period from the date of service of the demand notices resulting in short levy of interest of Rs.19.84 lakhs.

The Ministry has accepted the audit observation in all the cases.

Incorrect payment of interest by government to assessees

4.36 Under the Income Tax Act, 1961, as applicable from assessment year 1989-90 onwards, where any refund is due to an assessee out of any tax collected at source or paid by way of advance tax, during the financial year immediately preceding the assessment year, he shall be entitled to receive in addition to the said amount, simple interest thereon at the rate of one and half percent (one percent from 1 October 1991) for every month or part of a month comprised in the period from April of the assessment year to the date on which the refund is granted. The Act also provides that no interest shall be payable if the amount of refund is less than ten percent of the tax determined under summary or regular assessment. The Act further provides that if as a result of an order of rectification, revision, appeal or settlement, the amount on which interest was payable has been increased or reduced, the interest shall be increased or reduced accordingly.

(i) Some of the cases revealed during test check where mistakes were committed in calculating interest payable by the assessees while completing the assessment under section 143(3) of the Act, are given below:-

Sr. No.	State/CIT's charge	Asstt. year Date of Asstt.	Tax effect (in lakhs of rupees)
1.	West Bengal/ W.B.-I	1989-90 July 1991/Feb.1992	29.90
2.	West Bengal/ Central II	1990-91 March 1991/.Dec. 1991	11.03
3.	Maharashtra/ Bom. city IX	1989-90 March 1992/Jan.93	3.59

The Ministry has accepted the observation at Sl. Nos. 1 & 3. Their response to the remaining case has not been received.

(ii) In Karnataka charge, the assessment of a widely held company for the assessment year 1989-90 was revised in March 1992 to give effect to an appellate order. After giving credit to the tax deducted at source and also the advance tax paid, the assessee company became entitled to a refund of Rs. 685.62 lakhs and also interest thereon of Rs. 123.41 lakhs. Audit scrutiny revealed that the interest allowed in the revised order was only Rs. 94.02 lakhs. Mistake in calculation of interest resulted in short payment of interest to the assessee company to the extent of Rs. 29.39 lakhs.

The Ministry has accepted the audit observation.

Omission/ incorrect levy of penalty

4.37(i) Under the Income Tax Act, 1961, if the assessing officer in the course of any proceedings under this Act, is satisfied that any person has concealed the particulars of his income or furnished inaccurate particulars of such income, he may direct that such person shall pay by way of penalty, in addition to any tax payable by him, a sum which shall not be less than, but not exceeding twice, the amount of tax sought to be evaded by reason of the concealment of particulars of his income or furnishing of inaccurate particulars of such income.

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In Madhya Pradesh charge, the assessment of a company was completed after scrutiny for assessment year 1985-86 in March 1988, at a total income of Rs.25.56 lakhs as against income of Rs.3.70 lakhs declared in the return. Audit scrutiny revealed that the assessee had claimed depreciation of Rs.17.23 lakhs and investment allowance of Rs.11.49 lakhs on certain machinery. Consequent upon an enquiry by the assessing officer, this claim was however withdrawn by the assessee by filing a revised return in March 1988 because the machinery was neither installed nor put to use during the relevant previous year. The assessing officer levied a penalty of Rs.0.48 lakh after working out concealment of income of Rs.0.67 lakh. As the assessee company had made a false claim of deduction in the original return, the assessee company was liable for penalty of Rs.32.69 lakhs being twice the amount of tax of Rs.16.58 lakhs sought to be evaded on concealment of income of Rs.28.72 lakhs. The omission resulted in short levy of penalty of Rs.32.69 lakhs.

The reply of the Ministry to the audit observation has not been received.

(ii) Under the Income Tax Act, 1961, after 30 June 1984 no person should take or accept any loan or deposit of Rs.20,000 or more otherwise than by an account payee cheque or an account payee bank draft. For contravention of this provision, such a person is liable to pay fine equal to the amount of such loan or deposit. The Central Board of Direct Taxes issued instructions that in cases where the Income Tax Officer did not initiate penalty proceedings, he should record reasons for not doing so.

In Gujarat charge, in the assessment of an assessee company for the assessment year 1990-91, completed in March 1991 in a summary manner, it was noticed that the assessee had accepted an amount of Rs.70 lakhs in cash as security deposit. The assessing officer did not initiate penalty proceeding nor did he record any reasons for not doing so. Thus a fine upto Rs.70 lakhs was leviable in this case.

The Ministry has accepted the audit observation.

Omission to levy additional tax

4.38 Under the Income Tax Act, 1961, as applicable from 1 April 1989 where as a result of adjustments, the returned income of the assessee is increased or loss decreased by any amount, the assessing officer shall increase the amount of tax payable by the assessee by an amount of additional tax calculated at the rate of twenty percent of tax payable on such excess amount.

(i) In West Bengal charge, the assessment of a widely held company for the assessment year 1990-91 was made in a summary manner in February 1993 after making the prescribed adjustments amounting to Rs.945.38 lakhs. Audit scrutiny revealed that the additional tax of Rs.94.54 lakhs leviable under the provisions of the Act was not levied by the assessing officer.

The Ministry has accepted the audit observation.

(ii) In West Bengal charge, the assessment of a widely held company for the assessment year 1990-91 was completed in November 1991 in a summary manner at a total income of Rs.1502.08 lakhs after adding back a sum of Rs.745.08 lakhs by way of prescribed adjustments to the returned income of Rs.757 lakhs. Audit scrutiny revealed that though an additional tax of Rs.74.51 lakhs was required to be levied, the assessing officer levied additional tax of Rs.6.56 lakhs only. The mistake resulted in short levy of additional tax of Rs.67.95 lakhs.

The reply of the Ministry to the audit observation has not been received.

Omission to make surtax assessment

4.39 Under the Companies (Profits) Surtax Act, 1964, there was no statutory time limit for completion of surtax assessments. Pursuant to the recommendations of the Public Accounts Committee in Para 6.7 of their 128th Report (Fifth Lok Sabha), the Central Board of Direct Taxes issued instructions in October 1974 that surtax assessment proceedings should be initiated alongwith the income tax assessments. The Board further laid down that the surtax assessment should not be kept pending on the ground that the additions made in the income tax assessments were disputed in appeal and the time lag between the date of completion of

4.39

income tax assessments and surtax assessments should not ordinarily exceed a month, unless there were special reasons justifying the delay.

The income tax assessments of a closely held company for the assessment years 1985-86 and 1986-87 were completed/revised between March 1989 and September 1992 determining total income at Rs.5280.30 lakhs and Rs.4157.27 lakhs on the basis of which the net chargeable profits for the levy of surtax worked out to Rs.1656.46 lakhs and Rs.1506.29 lakhs respectively. After allowing statutory deduction from the chargeable profits, surtax should have been levied at Rs.625.64 lakhs and Rs.557.39 lakhs at the prescribed percentage. Audit scrutiny revealed that although the assessee company had submitted its surtax returns for the aforesaid two assessment years in October 1985 and November 1987 and paid advance surtax of Rs.36.58 lakhs and Rs.30.42 lakhs respectively, the surtax assessments for both the assessment years were not completed till the date of audit. The omission resulted in non realisation of surtax of Rs.1116.04 lakhs in aggregate for the two assessment years.

The Ministry has accepted the audit observation.

CHAPTER 5

INCOME TAX

General

5.1 Income Tax collected from persons other than companies is booked under the major head '0021 Taxes on income other than corporation tax'. Eighty five percent of the net proceeds of this tax, except in-so-far as these are attributable to Union emoluments, Union Territories and Union surcharge is assigned to the States in accordance with the recommendations of the Finance Commission.

5.2 The trend of receipts from income tax during the last five years is shown below:

Year	Total collection of all Direct Taxes	Amount of Income tax	Percentage of Income tax to total collection
	(in crores of rupees)		
1989-90	10,007.78	5,008.98	50.05
1990-91	11,028.94	5,375.34	48.74
1991-92	15,324.07	6,729.18	44.56
1992-93	18,097.29	7,863.49	43.45
1993-94	20,298.24	9,122.62	44.94

5.3 The number of assessees (other than companies) borne on the books of the Income tax department during the last five years was as follows:

As on 31 March	Number	Average collection of tax (per capita) (in thousands of rupees)
1990	69,16,640	7.24
1991	73,22,010	7.34
1992	76,60,407	8.78
1993	82,32,350	9.55
1994	94,15,102	9.69

5.4 The following table indicates the progress in the completion of assessments and collection of demand under income tax (excluding corporation tax) during the last five years:

Year	No. of assessments			Percentage of pendency to total cases for disposal	Total Demand		Percentage of collection to total demand
	For disposal	Completed during the year	Pending at the close of the year		Demand for collection	Collected during the year	
					(in crores of rupees)		
1989-90	67,29,998	55,93,738	11,36,260	16.88	6,418.97	5,008.98	78.03
1990-91	74,97,231	62,68,326	12,28,905	16.39	6,909.93	5,375.34	77.79
1991-92	78,21,446	65,66,416	12,55,030	16.04	9,127.88	6,729.18	73.72
1992-93	77,28,312	63,51,030	13,77,282	17.82	9,922.87	7,863.49	79.24
1993-94	85,10,569	72,42,046	12,68,523	14.90	12,403.40	9,122.62	73.55

Results of audit

5.5 A total number of 146 draft paragraphs involving tax effect of Rs.14.67 crores were issued to the Ministry of Finance for comments during March to September 1994. The Ministry has accepted the observations in 99 cases involving tax effect of Rs.5.49 crores. 53 illustrative cases involving tax effect of Rs.4.63 crores are given in the following paragraphs. Out of these, the Ministry has accepted the observations in 39 cases involving tax effect of Rs.3.66 crores. Of the cases accepted by the Ministry, nine cases involving tax effect of Rs.0.89 crores were checked by the Internal Audit but the mistakes were not detected by it.

Avoidable mistakes in computation of income and tax

5.6 Underassessment of tax of substantial amounts on account of avoidable mistakes attributable to negligence on the part of assessing officers have been mentioned year after year in the reports of the Comptroller and Auditor General of India. Despite this and issue of repeated instructions by Government, such mistakes continue to occur suggesting the need for close supervision and control. The various types of mistakes noticed included, inter-alia, incorrect adoption of figures, totalling errors, double allowance, application of lower rate of tax etc. Brief particulars of five representative cases involving short levy of tax of Rs. 34.70 lakhs are given below.

Sl.No.	State/Commissioner's charge/Assessee	Assessment Year/Date of Assessment	Section under which assessed	Nature of mistake	Tax effect (in lakhs of rupees)
1.	Haryana Rohtak Co-operative Society	1992-93 March 1993	143(1)	The assessee society while computing the loss of Rs. 115.11 lakhs in the return had increased the loss by Rs. 25.04 lakhs on account of depreciation instead of reducing the loss by an equivalent amount. The assessee also claimed inadmissible deduction of Rs. 26,006 under Sec. 80P. The assessing officer omitted to make these adjustments resulting in excess computation of loss.	19.69 (potential) 3.94 (additional tax)
2.	Orissa Unregistered firm	1992-93 December 1992	143(1)(a)	Tax was erroneously calculated at Rs. 76,550 instead of the correct amount of Rs. 4.87 lakhs, resulting also in incorrect calculation of surcharge and interest.	5.85 (including interest)
3.	Orissa Individual	1990-91 March 1993	143(3)	Tax on total income of Rs. 4.98 lakhs was erroneously determined as Rs. 1.28 lakhs instead of the correct amount of Rs. 2.28 lakhs.	1.85 (including interest)
4.	Madhya Pradesh Jabalpur HUF(specified)	1987-88 March 1993	143(3)	Total income was determined at Rs. 20.28 lakhs, whereas the tax was calculated on the total income of Rs. 17 lakhs.	1.80
5.	Rajasthan Jodhpur Individual	1987-88 1989-90 March 1993	144	Total income was erroneously worked out as Rs. 2.03 lakhs and Rs. 6.32 lakhs instead of the correct total income of Rs. 2.28 lakhs and Rs. 7.14 lakhs respectively resulting in underassessment of income aggregating Rs. 1.07 lakhs for two years.	1.57 (including interest)

The Ministry has accepted the audit observations in the cases at S.Nos.1,2,3 and 5. Their reply to the remaining observation has not been received.

Application of incorrect rate of tax

5.7 The Income Tax Act, 1961, provides that income tax is chargeable for every assessment year in respect of the total income of the previous year of a person according to the rates prescribed under the particular Finance Act.

(i) In Maharashtra charge, the assessment of an individual assessee, for the assessment year 1990-91 was completed after scrutiny in March 1993, at a total income of Rs.7.81 lakhs. According to the rates applicable to an individual for the relevant assessment year, the assessee was liable to pay tax of Rs.3.99 lakhs. Instead he was incorrectly charged tax of Rs.1.87 lakhs at the rates applicable to a registered firm. The mistake resulted in short levy of tax of Rs.4.45 lakhs (including interest).

The reply of the Ministry to the audit observation has not been received.

(ii) In West Bengal charge, the assessment of a firm for the assessment year 1990-91 was completed ex-parte after scrutiny in March 1993 treating the firm as an unregistered firm, on a taxable income of Rs.10 lakhs. The tax payable by the assessee firm in the status of an unregistered firm was Rs.5.17 lakhs. However, while calculating tax on total income, the department levied tax of Rs.2.44 lakhs only as leviable in the case of a registered firm resulting in under charge of tax of Rs.2.73 lakhs. There was also a consequential short levy of interest of Rs.2.17 lakhs for short payment of advance tax. Accordingly, there was an aggregate under charge of tax of Rs.4.90 lakhs.

The Ministry has accepted the audit observation.

(iii) Under the Income Tax Act, 1961, as applicable from 1 April 1989, tax is chargeable on the income of an association of persons or body of individuals at the same rate as is applicable in the case of an individual where

the individual shares of the members are determinate and known. Where, however, the total income of any member or members thereof is or are chargeable to tax at a rate or rates which is or are higher than the maximum marginal rate, tax will be charged on that portion or portions of the total income of the association or body which is or are relatable to the share or shares of such member or members at such higher rate or rates, as the case may be, and the balance of the total income of the association or body will be taxed at the maximum marginal rate.

In Maharashtra charge, the assessments of four associations of persons for the assessment year 1990-91 were completed after scrutiny in March 1993 at a total income of Rs. 83.95 lakhs, 68.93 lakhs, Rs. 62.84 lakhs and Rs. 100.75 lakhs respectively and tax was charged at the maximum marginal rate of fifty four percent. Audit scrutiny revealed that some of the members of these associations with 38 to 61 percent shares in the association had income chargeable to tax at 64.8 percent. Accordingly, the total income of these associations relatable to the shares of such members should have been taxed at such higher rate and the balance alone should have been taxed at the maximum marginal rate of fifty four percent. Failure to do so resulted in short levy of tax aggregating Rs. 46.57 lakhs, including interest for default in filing the return and in payment of advance tax.

The Ministry has accepted the audit observations in three cases. Their response to the remaining case has not been received.

Incorrect computation of income

5.8 Under the Income Tax Act, 1961, in computing the income chargeable under the head 'income from other sources', any expenditure not being in the nature of capital expenditure or personal expenses of the assessee laid out or expended wholly and exclusively for the purpose of making or earning such income shall be allowed as a deduction.

In Maharashtra charge, the assessment of an individual for the assessment year 1991-92 was completed after scrutiny in November 1991 and income was determined at Rs.31.10 lakhs. This income included Rs.27.04 lakhs under the head 'income from other sources' which was computed after allowing interest of Rs.5.68 lakhs on

funds borrowed from a financial corporation. Audit scrutiny, however, revealed that the moneys borrowed were mainly utilised for meeting the personal expenses of the assessee. Thus allowances of deduction of interest paid on borrowed funds was irregular. The mistake resulted in under assessment of income of Rs.5.68 lakhs involving short levy of tax of Rs.3.18 lakhs.

The Ministry has accepted the audit observation.

5.9 INCORRECT COMPUTATION OF BUSINESS INCOME

Incorrect allowance of liability

5.9.1 Under the Income Tax Act, 1961, in computing the business income of an assessee, a deduction for any sum payable by the assessee by way of tax or duty under any law for the time being in force or for any sum payable by him as an employer by way of contribution to any fund for the welfare of the employees or any sum payable by the assessee as interest on any loan or borrowing from any public financial institution or a state financial corporation, 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. Thus, these deductions are admissible only on actual payment and not on accrual basis.

In Punjab charge, in the assessments of two individuals for the assessment years 1991-92 and 1992-93 completed after scrutiny and in a summary manner in March 1992 and February 1993 respectively, the assessing officer allowed deduction of Rs. 4.26 lakhs and Rs. 10.91 lakhs respectively on account of liability towards purchase tax exhibited in balance sheet but not actually paid during the previous years relevant to the assessment years. Omission to disallow the statutory liability not actually discharged resulted in underassessment of income aggregating Rs. 15.17 lakhs involving short levy of tax aggregating Rs. 8.54 lakhs.

The Ministry has accepted the audit observation in one case. Their response to the remaining case has not been received.

Incorrect allowance of provisions

5.9.2 Under the Income Tax Act, 1961, for computing the taxable income, certain deductions and reliefs are prescribed. However, there is no provision to allow the tax levied on income as a deduction from the total income.

In Maharashtra charge, the assessment of a registered firm for the assessment year 1990-91 was completed after scrutiny in March 1993. Audit scrutiny revealed that taxable income had been computed after allowing provision for income tax of Rs.3.65 lakhs. As this provision is not an admissible deduction,this was required to be added back to the assessee's taxable income. Failure to do so resulted in underassessment of income of Rs.3.65 lakhs involving short levy of tax of Rs.4.14 lakhs in the hands of both the firm and its partners (including interest).

The Ministry has accepted the audit observation.

Incorrect allowance of expenditure relating to previous accounting year

5.9.3 Under the Income Tax Act, 1961, income under the head 'profits and gains of business or profession' is computed in accordance with the method of accounting regularly employed by the assessee. Where the assessee follows mercantile system of accounting, the annual profits are worked out on due or accrual basis i.e. after providing for all expenses for which a legal liability has arisen and taking credit for all receipts that have become due regardless of their actual receipt or payment. Only such expenses are allowable as deduction from a previous year's income as are relevant to that year.

In Maharashtra charge, the assessment of an assessee firm for the assessment year 1990-91 was completed in March 1993 in a scrutiny manner. Audit scrutiny revealed that the assessee had changed the method of accounting during the relevant previous year and debited Rs. 9.31 lakhs representing expenses relating to earlier years to the profit and loss account of the subsequent year. Incorrect allowance of the claim by the assessing officer resulted in underassessment of income of Rs.9.31 lakhs and short levy of tax of Rs.4.15 lakhs (including interest).

The Ministry has accepted the audit observation.

Mistake in the valuation of the closing stock

5.9.4 According to the principles of accounting, the closing stock at the end of a previous year is computed by including the quantity of additions in the form of purchases and manufactured goods to the opening stock and deducting the quantity of goods consumed from such figure.

In Delhi charge, the assessment of a registered firm for the assessment year 1990-91 was completed in December 1992 after scrutiny. Audit scrutiny of the assessment records revealed that opening stock of 58,160 kgs of a certain raw material worth Rs. 12.80 lakhs was not accounted for while valuing closing stock. The assessing officer should have increased the value of closing stock by a like amount. Omission to do so resulted in underassessment of income of Rs. 12.80 lakhs involving short levy of income tax of Rs. 5.77 lakhs(including interest).

The reply of the Ministry to the audit observation has not been received.

5.10 IRREGULARITIES IN ALLOWING DEPRECIATION

Mistakes in the allowance of depreciation

5.10.1 Under the Income Tax Act, 1961, in computing the business income of an assessee, a deduction on account of depreciation on plant and machinery or other assets is admissible at the prescribed rates provided these are owned by the assessee and used for the purpose of his business during the relevant previous year. Apart from the general rate, special rates of depreciation ranging from fifteen percent to one hundred percent are prescribed for certain specified items of machinery and plant.

In Karnataka charge, in the assessment of a registered firm for the assessment year 1990-91 completed after scrutiny in March 1993, depreciation at 100 percent on a steel reactor valued at Rs.25 lakhs was allowed as against the admissible rate of 33.33 percent. The incorrect application of rates resulted in short computation of income of Rs.16.67 lakhs involving short levy of tax of Rs.7.40 lakhs in the hands of the firm and its partners.

The Ministry has accepted the audit observation.

Excess carry forward and set off of unabsorbed depreciation

5.10.2 Under the Income Tax Act, 1961, where in the assessment of an assessee, full effect cannot be given to depreciation allowance in any previous year owing to there being no profits or gains chargeable for the previous year or profits or gains chargeable to other provisions of law, the allowance or part of the allowance to which effect has not been given, shall be deemed to be part of the allowance for

the following year and so on. It has been judicially held* that in the case of registered firms, depreciation should be adjusted against business income and against other heads of income of the firm and that portion, if any, which remains unabsorbed would be allocated to the partners for adjustment against the business and other income of each of the partners. If full effect cannot still be given to the depreciation allowance of the assessee firm by the above process in the hands of its partners and some amount still remains unadjusted, the assessee firm would carry it forward to the succeeding assessment year.

The assessment of a registered firm of Gujarat charge, for the assessment year 1990-91, was completed after scrutiny in December 1991. Audit scrutiny revealed that unabsorbed depreciation of Rs.13.08 lakhs was allowed to be carried forward without first allocating it to partners. Out of this amount, a sum of Rs.3.22 lakhs was set off in the assessment for the assessment year 1991-92, completed after scrutiny in March 1992. The mistake resulted in short levy of tax of Rs.3.39 lakhs (potential) and Rs.1.80 lakhs (positive) for the assessment years 1990-91 and 1991-92 respectively.

The Ministry has accepted the audit observation.

5.11 COMPUTATION OF CAPITAL GAINS

Incorrect computation of capital gains

5.11.1(i) Under the Income Tax Act, 1961, any profits or gains arising from the transfer of a capital asset effected during 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. The term 'transfer' includes any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882. The Act further provides for the exemption of capital gains arising from the transfer of a long-term capital asset if the assessee has, within a period of six months after the date of such transfer, invested or deposited the whole or any part of the net consideration in any

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* CIT vs. Trivedi Sons (1990) - 183 ITR 420(AP)
CIT vs. Srinivasa Sugar Factory (1988) - 174 ITR 178(AP)
CIT vs. Madras Wire Products (1979) -119 ITR 454(Mad)
Ballarpur Colleries Co. vs. CIT (1973) - 92 ITR 219(Bom).

'specified' asset and the exemption shall be allowed in proportion to the cost of the new asset.

In Tamil Nadu charge, an individual sold a property in a metropolitan city in April 1988 for a net consideration of Rs. 60.85 lakhs and invested Rs. 48.37 lakhs out of the same in 'specified' assets under the capital gains scheme and Rs. 12.48 lakhs on the purchase of a new house property and claimed exemption of the entire amount from capital gains tax which was allowed in the assessment for the assessment year 1989-90 completed after scrutiny in March 1993. The agreement for the sale was entered into on 16 April 1988 and the possession of the property was handed over to the transferee on the same date after receiving an advance of Rs.20 lakhs. Audit scrutiny revealed that the investment of Rs.48.37 lakhs in specified assets was made by the assessee only in November 1989, which was beyond the period of six months from the date of transfer of the assets. As the investment in specified assets was not made within the time limit prescribed in the Act, the exemption granted was not in order. The irregular exemption resulted in underassessment of income of Rs.19.68 lakhs involving short levy of tax of Rs.20.41 lakhs including interest for belated filing of return and default in payment of advance tax.

The reply of the Ministry to the audit observation has not been received.

(ii) The Act further provides that while computing capital gains in case of depreciable assets, the written down value of the asset at the beginning of the previous year is to be considered as the cost of acquisition of the assets for arriving at the capital gains and such gains, if any, are to be treated as short-term capital gains.

In Maharashtra charge, the assessment of an individual for the assessment year 1988-89 was completed after scrutiny in January 1991 at a net taxable income of Rs.2.74 lakhs. The assessee was engaged in hotel business during the relevant previous year. The assessee sold his hotel for a consideration of Rs.23 lakhs and claimed exemption applicable to long term capital gain on account of investment in specified assets. The department allowed the claim and assessed a net capital gain of Rs.1.64 lakhs. As the asset was a depreciable asset, the gains arising from the sale of the same should have been taxed as short term

capital gain without allowing any deduction/ exemption. The omission resulted in underassessment of income of Rs.20.77 lakhs involving short levy of tax of Rs.15.44 lakhs (including interest).

The Ministry has accepted the audit observation.

(iii) The Act further provides that specified asset includes, inter alia, deposits for a period of not less than three years with any nationalised bank.

In Rajasthan charge, in the assessment of an individual for the assessment year 1991-92 completed in December 1991 in a summary manner, the assessing officer exempted the entire consideration amount of Rs. 11.87 lakhs from tax. Audit scrutiny revealed that the assessee had sold her house property in June 1990 for Rs. 15.92 lakhs, the cost of acquisition of which was Rs. 4.05 lakhs resulting in a net consideration of Rs. 11.87 lakhs. The assessee was allowed the exemption even when the net consideration was kept in a saving bank account and short term deposit account. The exemption allowed was irregular as the amount invested or deposited under these accounts does not qualify for exemption under the provisions of the Income Tax Act. This mistake resulted in under computation of income by Rs. 5.14 lakhs involving short levy of tax of Rs. 3.62 lakhs (including additional tax and interest).

The Ministry has accepted the audit observation.

Omission to levy tax on capital gains

5.11.2 Under the Income tax Act, 1961, any profits and gains arising from the transfer of a capital asset are chargeable to tax under the head 'capital gains' except in certain specified cases.

In Uttar Pradesh charge, audit scrutiny of assessment records of an assessee individual revealed that a property consisting of a house and land appurtenant thereto, of which the assessee had one-third share, was sold in May 1989 for a consideration of Rs.48.65 lakhs. Taking the cost of acquisition at Rs.1.87 lakhs as shown in the wealth tax assessment records, the capital gains on the transfer of the property would work out to Rs. 23.34 lakhs after allowing the statutory deductions, of

which the assessee's share would work out to Rs.7.78 lakhs. The assessee was liable to pay tax of Rs.3.97 lakhs on the capital gains for the assessment year 1990-91 which was not levied.

The reply of the Ministry to the audit observation has not been received.

Loss of revenue due to application of wrong provisions of law

5.11.3 Under the Income Tax Act, 1961, any profits or gains arising from the transfer of a capital asset effected in the previous year is chargeable to income tax under the head 'capital gains' and is deemed to be the income of the previous year in which the transfer took place. In the case of capital gains arising from the transfer of buildings or lands appurtenant thereto and being a residential house, no capital gains is chargeable to tax, if the full value of consideration received does not exceed Rs. 2 lakhs. However, if the full value of consideration exceeds Rs. 2 lakhs, so much of the capital gains as bears to the whole of capital gains the same proportion as the amount of Rs. 2 lakhs bears to the amount of consideration is not charged to tax.

In Madhya Pradesh charge, two individuals having forty percent share each in land appurtenant to a building, sold it during the previous year relevant to assessment year 1986-87 for a consideration of Rs. 2.43 lakhs each, involving capital gains of Rs. 2.33 lakhs each. In the assessments for the assessment year 1986-87 completed after scrutiny in December 1988, deduction of Rs. 1.92 lakhs was allowed individually for computing capital gains. The assessments were subsequently rectified in June 1991 to withdraw the deduction allowed on the ground that the assessees were in possession of their respective share in the residential building and the deduction was admissible in respect of capital gains arising on transfer of residential building. In an appeal filed by the assessees, the Commissioner of Income Tax (Appeals) in his order of February 1993 cancelled the rectification order on the ground that under section 53 of the Act, the capital gains arise from the transfer of long term asset being building or land appurtenant thereto and thus on the sale of land appurtenant to the residential building deduction from capital gains was correctly allowed. Further, a mere change of opinion was not a mistake apparent from record and thus section 154 of the Act was not applicable. The department did not file a second appeal. The

non-filing of a second appeal resulted in loss of revenue of Rs. 2 lakhs in the two cases.

The reply of the Ministry to the audit observation has not been received.

5.12 INCOME ESCAPING ASSESSMENT

Income not assessed

5.12.1 Under the Income Tax Act, 1961, as applicable from 1 April 1967, cash assistance (by whatever name called) received or receivable by any person against exports under any scheme of the Government of India is chargeable to income tax under the head 'profits and gains of business or profession'.

In Maharashtra charge, in the assessment of a registered firm, for the assessment year 1989-90, completed after scrutiny in March 1992, cash assistance received for exports amounting to Rs.4.47 lakhs during the relevant previous year and accounted for in the balance sheet was not included in the taxable income. The omission resulted in underassessment of income of Rs.4.47 lakhs with consequent short levy of tax of Rs.3.73 lakhs, including interest in the hands of the firm and its partners.

The Ministry has accepted the audit observation.

Lack of correlation with the records of other taxes

5.12.2 The Central Board of Direct Taxes in their instructions issued in November 1974, stressed the need to have proper liaison with Sales Tax Authorities so that various matters arising from proceedings under the Sales Tax Act which have a bearing on the income tax assessment are taken due note of by the Income Tax Authorities in the relevant assessment proceedings. The need for a proper co-ordination of the assessment records pertaining to Direct Taxes to ensure an overall improvement in the administration of these taxes has been repeatedly emphasised by the Public Accounts Committee in their 186th Report (Fifth Lok Sabha) and 61st Report (Sixth Lok Sabha). The Central Board of Direct Taxes have also issued instructions from time to time, the latest being in April 1979 for carrying out such correlation.

In Orissa charge, the assessments of two registered firms for assessment year 1989-90 were completed after scrutiny in January 1990 and March 1992 respectively. In the assessment of one of the firms the assessing officer had enhanced the returned income by Rs. 20 lakhs

considering the suppression of sales as per sale tax assessment and computed the sales turnover at Rs. 217.59 lakhs. Audit scrutiny revealed that the Sales Tax Authorities had estimated the sales turnover at Rs. 236.27 lakhs which included the aforesaid Rs. 20 lakhs included in the taxable income by the assessing officer. In the case of another firm, Sales Tax Authorities had enhanced the gross turnover by Rs.7 lakhs determining it at Rs. 161.69 lakhs. The assessing officer should have adopted in both the cases the turnover of Rs. 236.27 lakhs and Rs. 161.69 lakhs as determined by the sales tax authorities instead of Rs. 217.59 lakhs and Rs. 154.69 lakhs respectively actually taken for the purposes of computation of taxable income. Omission to do so resulted in underassessment of income aggregating Rs.25.68 lakhs involving short levy of tax aggregating Rs.12.38 lakhs, including interest, in the hands of the firms and their partners.

The reply of the Ministry to the audit observations has not been received.

Mistakes in assessments while giving effect to appellate orders

5.12.3 In Tamil Nadu charge, the assessments of an individual, for assessment years 1982-83 and 1983-84 were revised in March 1993 to give effect to appellate orders determining the losses at Rs. 4.79 lakhs and Rs. 5.83 lakhs respectively which were allowed to be carried forward for set off in the subsequent years. Consequential revision of assessment for the assessment year 1984-85 was made in March 1993 wherein the entire carried forward loss of Rs. 4.79 lakhs pertaining to assessment year 1982-83 and loss relating to assessment year 1983-84 amounting to Rs.1.49 lakhs was set off. The balance of Rs.4.34 lakhs was set off in the assessment for the assessment year 1985-86. Audit scrutiny revealed that while revising the assessment for the assessment year 1984-85, losses pertaining to assessment years 1982-83 and 1983-84 already set off in the earlier revision of August 1992 aggregating Rs.10.39 lakhs were omitted to be added back. The mistake resulted in an underassessment of income of Rs.4.72 lakhs and Rs.4.34 lakhs for assessment years 1984-85 and 1985-86 respectively involving short levy of tax aggregating Rs.9.95 lakhs for two years, including interest for belated filing of return and non-filing of estimate.

The Ministry has accepted the audit observation. Additional demand of Rs. 5.62 lakhs has been raised after recomputing the income for assessment year 1984-85 and after waiving interest leviable for assessment years 1984-85 and 1985-86.

5.13 SET OFF OR CARRY FORWARD OF LOSSES

Incorrect set off and carry forward of losses

5.13(a) Under the Income Tax Act,1961, where for any assessment year, the net result of the computation under the head 'profits and gains of business or profession' is a loss to the assessee, not being a loss sustained in speculation business and such loss cannot be or is not wholly set off against income from any other head of income, so much of the loss as has not been set off shall, subject to other provisions of the Act, be carried forward for adjustment in the following assessment year.

In Punjab charge, in the assessments of an assessee co-operative society for the assessment years 1991-92 and 1992-93 completed in December 1992 and February 1993 respectively, the assessing officer computed the loss to be carried forward at Rs.696.15 lakhs for the assessment year 1991-92. Audit scrutiny revealed that instead of carrying forward the computed loss of Rs.696.15 lakhs, the loss actually carried forward was Rs.826.61 lakhs. The excess carry forward of loss of Rs.130.46 lakhs resulted in potential short levy of tax of Rs.51.10 lakhs.

The Ministry has accepted the audit observation.

(b) Under the Income Tax Act, 1961, where for any assessment year, the net result of the computation under the head 'profits and gains of business or profession' is a loss to the assessee not being a loss sustained in speculation business, and such loss cannot be wholly set off against income under any other head of income during that year, the whole of such loss is entitled to be carried forward to the following assessment year and shall be set off against profit and gains of business or profession carried on by him and assessable for that assessment year provided the business or profession for which the loss was originally computed continues to be carried on by him in the previous year relevant to the said assessment year.

In Karnataka charge, in the assessments of a registered firm, for the assessment years 1987-88 and 1988-89, completed after scrutiny in March 1991, the losses of a proprietary concern run by one of the partners of the firm, amounting to Rs.4.82 lakhs in the assessment year 1987-88 and Rs.7.17 lakhs in assessment year 1988-89 were allowed for set off against the income of the firm. As there is no provision for set off of losses of a proprietary concern against the income of a registered firm, the set off of losses aggregating Rs.11.99 lakhs was not in order. Incorrect set off of losses led to underassessment of income of like amount and under-charge of tax of Rs.7.25 lakhs in the hands of the firm and its partners.

The Ministry has accepted the audit observation.

5.14 IRREGULAR EXEMPTIONS AND EXCESS RELIEFS GIVEN

Incorrect allowance of relief in respect of export turnover

5.14.1(a) Under the Income Tax Act, 1961, as applicable from the assessment year 1989-90, an assessee being an Indian company or a person other than a company, resident in India and engaged in the business of export out of India, of any goods or merchandise other than mineral oil, minerals and ores, during the previous year, is entitled to a deduction of the profits derived from such business. The Central Board of Direct Taxes in their circular dated 22 May 1984 have clarified that the export of cut and polished diamonds and gem stones will not amount to export of 'minerals and ores' and hence will qualify for relief. The Act was amended with effect from 1 April 1991 to extend the benefit of deduction in cases of export of processed minerals and ores.

In Maharashtra charge, the assessment of a registered firm engaged in the business of excavation and export of granite stones, for the assessment year 1989-90, was completed after scrutiny in October 1990 allowing deduction of Rs. 54.95 lakhs in respect of profit from export of granite stones. As the granite stones are classifiable as minerals and ores, the deduction allowed was irregular. The mistake resulted in underassessment of income of Rs. 54.95 lakhs involving short levy of tax of Rs. 35.42 lakhs.

The Ministry has accepted the audit observation.

(b) Under the Income Tax Act, 1961, as applicable from the assessment year 1989-90, an assessee being an Indian company or a person other than a company, resident in India and engaged in the business of export out of India, of any goods or merchandise during the previous year, is entitled to a deduction of the profits derived from such business if the sale proceeds thereof are received in convertible foreign exchange. In a case where the business carried on by the assessee does not consist exclusively of export out of India of goods or merchandise, the profits derived from export of goods or merchandise shall be the amount which bears to the profits of the assessee as computed under the head 'profits and gains of business or profession' the same proportion as the amount of export turnover bears to the total turnover of the business carried on by the assessee.

In Karnataka charge, in the assessment of a registered firm for the assessment year 1991-92 completed after scrutiny in June 1992, a deduction of Rs.54.23 lakhs was allowed in respect of export profits. Audit scrutiny revealed that the profits of the business arrived at by the assessee firm included a sum of Rs.2.03 lakhs being interest received on 'bank deposits' which did not represent sale proceeds of goods exported received in convertible foreign exchange. It was also noticed that the export turnover included a sum of Rs.5.45 lakhs representing credit balance/liability written off and another sum of Rs. 40,000 representing training fees received, which also did not represent the sale proceeds of goods exported out of India and received in convertible foreign exchange. In determining the export incentive allowance, the sum of Rs.2.03 lakhs and Rs. 5.85 lakhs should have been deducted from the 'business income' and the 'export turnover' respectively. Omission to deduct the above sums resulted in excess allowance of deduction of Rs.4.66 lakhs leading to an underassessment of income by an identical amount involving under-charge of tax of Rs.1.27 lakhs in the hands of the firm and Rs.2.08 lakhs in the hands of its partners.

The Ministry has accepted the audit observation.

Incorrect exemption in the case of co-operative society

5.14.2 Under the Income Tax Act, 1961, the income of a co-operative society attributable to certain specified activities is wholly exempt. Income derived from activities other than the specified ones is also exempt to a

limited extent, subject to the fulfilment of prescribed conditions. In the case of a co-operative society or an urban consumers' society, any income from house property is exempt only if the gross total income does not exceed rupees twenty thousand.

In Uttar Pradesh charge, in the case of a co-operative society engaged in marketing of agriculture produce, in the computation of income for the assessment year 1989-90, assessment for which was completed after scrutiny in March 1992, the amount of Rs.23.13 lakhs being income from property, was considered as exempt. However, as the assessee was neither a housing society nor an urban consumers' society and its gross total income was in excess of rupees twenty thousand, the income from property did not qualify for exemption. The erroneous exemption resulted in under assessment of income by Rs.23.13 lakhs with consequent undercharge of tax of Rs.16.64 lakhs, including interest of Rs.6.96 lakhs for non payment of advance tax.

The reply of the Ministry to the audit observation has not been received.

5.15 NON-LEVY OR INCORRECT LEVY OF INTEREST AND PENALTY

Interest for delay in payment of tax demand

5.15.1 Under the Income Tax Act, 1961, any demand for tax should be paid by an assessee within thirty five days (thirty days with effect from 1 April 1989) of service of notice of the relevant demand and failure to do so would attract interest at the rate of fifteen per cent per annum with effect from 1 October 1984 and one and one half per cent for every month or a part thereof from 1 April 1989 from the date of default till the actual date of payment of demands. The Central Board of Direct Taxes issued instructions in November 1974 that interest for belated payment of tax should be calculated and charged within a week of the date of final payment of tax demand. The Central Board of Direct Taxes in their instructions issued in June 1991 have further emphasised that the assessing officer should calculate such interest at the end of each financial year even if the amount of tax etc. in respect of which interest is payable has not been paid in full before the end of any such financial year and issue the demand notice accordingly.

Test check revealed cases in which such interest was not levied, some of which

are detailed below:

Sl. No.	State/Commissioner's charge/Status of the assessee	Assessment year/date of assessment	Brief facts	Non-levy/short levy of interest (in lakhs of rupees)
1	Tamil Nadu, Coimbatore Co-operative Sugar Mills	1989-90 August 1991/ January 1992 1990-91 February 1991/ March 1992/ August 1992	For assessment year 1989-90 tax demand notice of Rs. 31.48 lakhs was served in September 1991 and additional demand of Rs. 1 lakh was raised in January 1992. The assessee paid Rs. 19.86 lakhs between December 1991 and September 1992. Demand of Rs. 73.45 lakhs for the assessment year 1990-91 was raised in February 1991 which was increased to Rs. 87.61 lakhs in March 1992 and was finally reduced to Rs. 75.38 lakhs in August 1992 after giving effect to appellate orders. The assessee paid Rs. 60 lakhs between November 1992 and March 1993. No interest on outstanding demand was charged.	29.90
2	Kerala Kochi Individual	1986-87 to 1989-90 Between March 1989 and March 1992/October 1989 and December 1992	Out of the aggregate demand of Rs. 35.08 lakhs raised between April 1989 and March 1992, the assessee paid Rs. 10.76 lakhs between August 1989 and January 1993. Interest on delayed payment/ non-payment of tax demand was not levied.	8.89
3.	Tamil Nadu Coimbatore Industrial Co-operative Society	1983-84 1989-90 November 1991 September 1991 February 1992/ August 1992	The original demands of Rs. 5.83 lakhs and Rs. 33.31 lakhs raised in November 1991 and September 1991 were revised to Rs. 3.90 lakhs and Rs. 24.54 lakhs in February 1992 and August 1992. The assessee paid the demands in instalments between March 1992 and March 1993. Interest on belated payment of tax was not levied.	3.74
4.	Tamil Nadu Coimbatore Hindu Undivided family (specified) Individual	1986-87 March 1989/ November 1989 1985-86 1986-87 October 1988 March 1989/ November 1989	As against the demand of Rs. 3.26 lakhs raised in March 1989 the assessee Hindu Undivided family had paid Rs. 38,593 upto March 1993. Similarly as against the demand of Rs. 1.99 lakhs and Rs. 1.46 lakhs respectively for two years raised in November 1989 the assessee made payments of Rs. 1.97 lakhs and Rs. 31,844. Interest on belated payment of tax demand was not levied.	3.55

The Ministry has accepted the audit observations at Sr.No.1 to 3 and 4(in the case of individual). Their response to remaining case has not been received.

Interest for delay in filing the return

5.15.2 Under the Income Tax Act, 1961, where the return for any assessment year is furnished after the specified due date, the assessee shall be liable to pay interest at fifteen per cent per annum from 1 October 1984 and two per cent per month or part thereof from 1 April 1989, from the date immediately following the specified due date to the date of filing the return or where no return is furnished, to the date of completion of regular assessment on the amount of tax determined on regular assessment as reduced by the advance tax paid and the tax deducted at source, if any.

(i) In West Bengal charge, the assessment of an individual, for the assessment year 1987-88, completed ex-parte after scrutiny in March 1990 was set aside. The assessment was revised in March 1993 at the original total income of Rs.22.77 lakhs and tax at Rs.11.18 lakhs. Audit scrutiny revealed that the assessee furnished the return of income on 21 March 1990, whereas the specified due date for furnishing the return was 31 July 1987. The assessee was, therefore, liable to pay interest of Rs.4.33 lakhs for default in furnishing the return of income in time from 1 August 1987 to 21 March 1990 against which the assessing officer levied only Rs.55,906. The mistake resulted in short levy of interest of Rs.3.77 lakhs.

The Ministry has accepted the audit observation.

(ii) In Gujarat charge, in the assessment of a registered firm, for the assessment year 1988-89, completed after scrutiny in March 1992, interest for default in filing the return and in payment of advance tax was erroneously levied at Rs.17.23 lakhs instead of the correct amount of Rs.20.76 lakhs. The mistake resulted in short levy of interest of Rs.3.53 lakhs.

The reply of the Ministry to the audit observation has not been received.

Interest for non-payment or short payment of advance tax

5.15.3 Under the Income Tax Act, 1961, where an assessee has paid advance tax for any financial year on the basis of his own estimate and the advance tax so paid falls short of seventy five percent (ninety percent from 1 April 1989) of the tax determined on regular assessment, interest at fifteen percent per annum (two percent for every month or a part thereof from 1 April 1989) is payable by the assessee on the amount by which the advance tax paid falls short of the assessed tax from the first day of the next financial year to the date of determination of total income in a summary manner or regular assessment.

A few examples of the mistakes in the levy of interest noticed in test check are given in the following table:

S. No.	State/Commissioner's charge	Status of the assessee	Assessment year Date of assessment	Section under which assessed	Period for which interest was leviable	Correct amount of interest leviable	Interest levied	Short levy of interest
						(in lakhs of rupees)		
1.	West Bengal WB-VI Calcutta	Unregistered firm	1990-91 November 1990 March 1993	144	1 April 1990 to March 1993	24.80	nil	24.80
2.	Maharashtra City V, Bombay	Individual	1989-90 February 1992	143(3)	1 April 1989 to 29 February 1992	14.35	5.06	9.29
3.	Orissa Orissa	Individual	1990-91 March 1993	143(3)	1 April 1990 to 31March 1993	10.23	5.12	5.11
4.	Maharashtra City I, Bombay	Association of persons	1990-91 December 1992	143(3)	1 April 1990 to December 1992	6.73	2.45	4.28
5.	Maharashtra City II, Bombay	Individual	1989-90 March 1993	143(3)	1 April 1989 to March 1993	16.77	12.58	4.19
6.	Karnataka Kar III, Bangalore	Unregistered firm	1990-91 March 1993	143(3)	1 April 1990 to March 1993	3.75	0.37	3.38
7.	Andhra Pradesh Hyderabad	Individual	1989-90 March 1993	143(3)	1 April 1989 to January 1993	2.72	0.23	2.49
8.	Maharashtra City XI, Bombay	Two individuals	1989-90 1990-91 March 1992/ March 1993	143(3)	1 April 1989 to March 1992 1 April 1990 to March 1993	11.01	7.90	3.11

9. Gujarat III, Ahmedabad	Three registered firms and one individual	1989-90 1990-91 March 1992 and February 1992 respectively	143(3)	1 April 1989 to March 1992 and 1 April 1990 to February 1992	6.25	3.15	3.10

The Ministry has accepted the audit observations in the cases at Sl. No. 1 to 7 and 8(in one case). Their response to the remaining cases has not been received.

Interest for failure to deduct tax at source

5.15.4(i) Under the Income Tax Act, 1961, a person other than an individual or Hindu undivided family, who is responsible for paying to a resident any income by way of interest is required to deduct income tax at source at the rates in force at the time of credit of such income to the account of the payee or at the time of payment thereof in cash, cheque etc. Failure to deduct such tax or after deducting it, failure to pay the same as required under the Act makes him liable for the levy of interest at 15 percent per annum on the amount of tax from the date on which such tax was deductible to the date on which it is actually paid.

In Tamil Nadu charge, a registered firm, for the previous year ending 31 March 1990 relevant to assessment year 1990-91 debited Rs.67.65 lakhs towards payment of interest which included, inter alia, interest payments aggregating Rs.59.65 lakhs made by the assessee firm to its sister concerns. This expenditure was allowed in the assessment completed in December 1992, determining a loss of Rs.12.09 lakhs. Audit scrutiny revealed that on such interest payments, no tax was deducted by the assessee firm as required under the Act. Copies of accounts of the sister concerns also confirmed this position. The assessee firm was, therefore, liable to pay interest for failure to deduct tax at source amounting to Rs.3.54 lakhs for the period from 1 April 1990 to 30 November 1993 which was not levied.

The Ministry has accepted the audit observation.

(ii) Under the Income Tax Act, 1961, if any person fails to deduct the whole or any part of the tax as required by or under the provisions of Chapter XVII-B of the Act he shall be liable to pay, by way of penalty, a sum equal to the amount of the tax which he failed to deduct as aforesaid. The Act further provides that if any

person who is required to deduct tax at source does not deduct or after deducting, fails to pay the tax as required by or under the Act, he shall be liable to pay simple interest at fifteen per cent per annum on the amount of such tax from the date on which such tax was deductible to the date on which such tax is actually paid.

In Madhya Pradesh charge, a registered firm paid interest of Rs.8.30 lakhs to two domestic companies on loans taken from them and Rs.4.63 lakhs to two sub-contractors for works got executed through them during the previous year relevant to the assessment year 1991-92. Audit scrutiny revealed that no tax was deducted at source by the assessee firm from these payments, although the total tax deductible at source worked out to Rs.1.96 lakhs. For failure to deduct tax at source from these payments the assessee firm was liable to pay interest of Rs.1.11 lakhs from 1 April 1991 to 31 August 1993 and penalty of Rs.1.96 lakhs, which were not levied by the assessing officer. The aggregate tax effect worked out to Rs.3.07 lakhs.

The reply of the Ministry to the audit observation has not been received.

Omission to levy penalty

5.15.5(a) Under the Income Tax Act, 1961, no person shall, after 30 June 1984, take or accept from any other person any loan or deposit of Rs. 10,000 (Rs. 20,000 from 1 April 1989) or more, otherwise, than by account payee cheque or bank draft, subject to certain exceptions. Similarly, no person shall repay in cash to any person any deposit or deposit with interest if the amount is Rs. 10,000 or more. Prior to 1 April 1989 the assessee contravening these provisions was liable for imprisonment for a term which could extend to two years and was also liable to pay a fine equal to the amount of such deposit. After 1 April 1989 an assessee contravening these provisions without reasonable cause is liable to pay by way of penalty, a sum equal to the amount of such loan or deposit. The Central Board of Direct Taxes had also directed that in cases where the assessing officer does not initiate penalty proceedings, he should record the reasons for not doing so.

A few examples of the mistakes in non-levy of penalty noticed in test check are given in the following table:

5.15

Sl. No.	State/ Commissioner's charge	Status of assessee	Assessment year and date of assessment	Section under which assessed	Nature of mistake	Penalty not levied
						(in lakhs of rupees)
1.	Gujarat Baroda	Three registered firms	1989-90 & 1990-91 Nov. 1989 February 1990 March 1991	143(1)(a)	Assessee accepted/repaid deposits amounting to Rs. 1.58 lakhs, Rs. 3.36 lakhs & Rs. 1.90 lakhs in cash. Assessing officer did not levy penalty for which no reasons were recorded.	6.84
2.	Gujarat Surat III-Ahmedabad	Two registered firms and one individual	1989-90 & 1992-93 Nov. 1991 March 1992 & March 1993	143(3)	Assessee accepted/repaid deposits aggregating Rs. 2.53 lakhs, Rs. 1.17 lakhs and Rs. 1.18 lakhs in cash. Assessing officer did not levy penalty for which no reasons were recorded.	4.88

The Ministry has accepted the audit observations in all the cases.

(b) The Income Tax Act, 1961 as amended from the assessment year 1985-86 and onwards has made it obligatory for every assessee, whose total sales, turnover, or gross receipts in business exceed forty lakhs rupees, in any previous year, to get his accounts audited by an authorised accountant before the specified due date for submission of return of income and obtain the report of such audit in the prescribed form within the specified date. Failure to comply with these provisions renders the assessee liable to a penalty equivalent to one half percent of the total sales/ turnover/gross receipts or one lakh rupees, whichever is lower. The Central Board of Direct Taxes had issued instructions, from time to time, that where the assessing officer did not initiate penalty proceedings in any case, he should record the reasons for not doing so.

In Gujarat charge, the assessments of an association of persons, for the assessment years 1989-90 to 1991-92 were completed between January 1991 and February 1992. Though the turnover of the assessee during these years was Rs.702.04 lakhs, Rs.459.46 lakhs and Rs.372.29 lakhs, the accounts were not got audited

nor did the assessee submit the report in the prescribed form alongwith the returns of income for the periods under review. Failure to comply with the statutory provisions rendered the assessee liable to penalty of rupees one lakh for each assessment year aggregating Rs. 3 lakhs. However, no penalty was imposed and no reason thereof was recorded by the assessing officer.

The reply of the Ministry to the audit observation has not been received.

5.16 OTHER TOPICS OF INTEREST

Omission to take action on internal audit observation

5.16.1 According to the executive instructions issued by the Board in 1977, mistakes pointed out by internal audit parties of the department should be rectified by the assessing authorities promptly. The remedial action should be initiated within a month and completed as far as possible within three months of the report of internal audit.

In Tamil Nadu charge, for the assessment year 1990-91, an individual filed a return of income admitting Rs.5.44 lakhs as income which included Rs.2.17 lakhs being capital gains on the sale of a property computed, interalia, after claiming a deduction of Rs.40.34 lakhs towards investment in specified assets out of the total sale consideration of Rs.56.69 lakhs. This was accepted by the department in March 1992. While checking the above assessment in September 1992, the Special Audit Party observed that as only a part of the sale consideration was invested in specified assets, the deduction towards the investment should be allowed only proportionately. Audit scrutiny, however revealed (January 1994) that this point was not taken note of in the revision of assessment made in December 1992 and September 1993. The omission resulted in the short computation of capital gains by Rs.4.25 lakhs involving a short levy of tax of Rs.4.17 lakhs including interest for belated filing of the return and default in payment of advance tax respectively besides additional income-tax leviable under the Act.

The Ministry has accepted the audit observation.

Mistake in demand notice

5.16.2 Under the Income Tax Act, 1961, when any tax, interest, penalty, fine or any other sum is payable in consequence of any order

passed under the Act, the assessing officer shall serve upon the assessee a notice of demand in the prescribed form specifying the sum so payable.

In West Bengal charge, the assessment of two individuals for the assessment year 1992-93 was completed under section 144 of the Act in January 1993, at a total income of Rs.17.10 lakhs each and tax at Rs.12.49 lakhs each, including interest for late filing of return and short payment of advance tax. Audit scrutiny revealed that the demand notices were issued for Rs.9.10 lakhs each instead of the correct demand of Rs.12.49 lakhs each. The mistake resulted in short demand of tax aggregating Rs.6.80 lakhs in two cases.

The Ministry has accepted the audit observations.

Incorrect adoption of previous year

5.16.3 Under the Income Tax Act, 1961, previous year in relation to the assessment year commencing on first day of April 1989 means the period which begins with the date immediately following the last day of the previous year relevant to the assessment year commencing on the first day of April 1988 and ends on 31 March 1989. The Act further provides that where the assessee has adopted more than one period as the previous year in relation to the assessment year commencing on the first day of April 1988 for different sources of his income, the previous year in relation to the assessment year commencing on the first day of April 1989 shall be reckoned separately in the manner aforesaid in respect of each such source of income and the longer or the longest of the period so reckoned shall be the previous year for the said assessment year.

In Maharashtra charge, the assessment of an assessee individual for the assessment year 1989-90 was completed, after scrutiny, in July 1991 at a total income of Rs.16.72 lakhs. Audit scrutiny revealed that the assessee had adopted more than one period as the previous year for different sources of income ranging from twelve months to twenty-three months. The period of twenty-three months being the longest one, should have been reckoned as the previous year for the relevant assessment year and income and tax should have been computed

accordingly. The total income for twenty-three months worked out to Rs. 21.54 lakhs and tax thereon worked out to Rs. 10.89 lakhs. However, the assessing officer determined the income for twelve months and levied tax of Rs. 8.56 lakhs. The mistake resulted in short levy of tax of Rs. 3.63 lakhs (including interest).

The Ministry has accepted the audit observation.

CHAPTER 6

OTHER DIRECT TAXES

A - WEALTH TAX

General

6.1 The following table gives a time series analysis of wealth tax receipts as against budget estimates during 1989-90 to 1993-94:

Year	Budget Estimates	Actuals	Variation	Percentage Variation
		(In crores of rupees)		
1989-90	120.00	178.51	58.51	48.75
1990-91	175.00	231.17	56.17	32.09
1991-92	255.00	306.93	51.93	20.36
1992-93	300.00	467.27	167.27	55.75
1993-94	200.00	153.98	(-)46.02	(-)23.01

6.2 Particulars of assessments completed, assessments pending and demands in arrear for the last five years ending 31 March 1994 are given below:

Year	Number of assessments completed during the year	Number of cases pending assessment at the end of the year	Arrear of demands at the end of the year (in crores of rupees)
1989-90	5,23,897	3,55,756	402.26
1990-91	5,96,411	3,61,114	429.52
1991-92	6,87,158	3,28,041	473.28
1992-93	6,25,005	3,35,687	309.61
1993-94	4,32,574	1,81,177	423.28

Results of Audit

6.3 During the test audit of assessments completed under the Wealth Tax Act, 1957, conducted during the period 1 April 1993 to 31 March 1994, short levy of wealth tax of Rs. 8.46 crores was noticed in 1318 cases.

A total number of 53 draft paragraphs involving tax effect of Rs.164.91 lakhs were issued to the Ministry of Finance for comments during March to September 1994. The Ministry of Finance has accepted the observations in 40 cases involving tax effect of Rs.112.13 lakhs. In the succeeding paragraphs 18 illustrative cases involving tax effect of Rs.69.79 lakhs have been discussed. While paragraphs 6.4 to 6.7 are on wealth tax on assessees other than companies, paragraph 6.8 relates to company cases. Out of these, the Ministry of Finance has accepted the observations in 16 cases involving tax effect of Rs.65.80 lakhs. 2 cases involving tax effect of Rs.11.82 lakhs were checked by the Internal Audit of the department but the mistakes were not detected by them.

Wealth not assessed

6.4 Under the Wealth Tax Act, 1957, wealth tax on assessees other than companies is chargeable in respect of each assessment year on the net wealth of the assessees as on the valuation date relevant to that assessment year at the rates prescribed in the Schedule to the Act. Net wealth means the aggregate value of all assets wherever located belonging to the assessee as reduced by the aggregate value of all admissible debts owed by him on the valuation date. The Act also provides that where an assessee is a partner in a firm, the value of his interest in the net assets of the firm is to be included in his net wealth.

In Assam charge, the income tax assessment records of two assessees for the assessment years 1989-90 to 1992-93 revealed that they returned rental income ranging between Rs. 2.76 lakhs and Rs. 3.41 lakhs from let out house properties during the relevant previous years. The net maintainable rent after deducting outgoings therefrom ranged between Rs. 2.26 lakhs and Rs. 2.80 lakhs. The fair market value of the properties under the rent capitalisation method ranged between Rs. 28.20 lakhs and Rs. 34.90 lakhs for which the assessees were liable to wealth tax. However, neither the assessees filed any wealth tax returns nor did the department initiate any wealth tax proceedings.

The omission resulted in wealth aggregating Rs.135.84 lakhs escaping assessment with consequent non-levy of wealth tax of Rs.3.22 lakhs (including interest and penalty).

The reply of the Ministry to the audit observation has not been received.

Incorrect valuation of unquoted equity shares

6.5 Under the Wealth Tax Rules, 1957, prior to their amendment with effect from 1 April 1989, the value of unquoted equity shares of a company is determined on the basis of the net value of the assets of the business as a whole having regard to its balance sheet. Under Rule 1D of the Wealth Tax Rules, 1957, any amount representing provision for taxation (other than the amount paid on advance tax under the relevant provisions of the Income Tax Act) to the extent of the excess over the tax payable with reference to book profits in accordance with the law applicable thereto, will not be treated as a liability while computing the break up value of the unquoted equity shares.

In West Bengal charge, in the wealth tax assessments of two individuals for the assessment years 1985-86 and 1986-87, completed in March 1990, the value of 11250 unquoted equity shares of a private limited company owned by the assessees, was declared by them at Rs.1495 and Rs.1830 per share, for the assessment years 1985-86 and 1986-87 respectively, which was accepted as such by the assessing officer. Audit scrutiny revealed that in arriving at the break up value, the entire provision for taxation as per balance sheets of the relevant financial years was incorrectly deducted from the value of assets instead of the actual amount of provision for taxation deductible under the prescribed rules. On this basis, the value of each share worked out to Rs.1915 and Rs.2246 per share for the aforesaid two assessment years respectively. The mistake in computation of value of shares resulted in their undervaluation by Rs.420 and Rs.416 per share leading to total under assessment of wealth of Rs.94.05 lakhs with consequent short levy of tax aggregating Rs.2.97 lakhs.

The Ministry has accepted the audit observations in both cases.

Mistake in application of rate of tax

6.6 From the assessment year 1974-75, the Schedule I to the Wealth Tax Act, 1957, was amended to provide for a higher rate of tax for every Hindu undivided family of the specified category, having at least one member with

assessable net wealth exceeding Rs.1 lakh upto assessment year 1979-80, Rs.1.50 lakhs from the assessment year 1980-81 to 1985-86 and Rs. 2.50 lakhs from the assessment year 1986-87 and subsequent years. Other cases of Hindu undivided families attract tax at lower rates.

In Tamil Nadu and Andhra Pradesh charges, audit scrutiny revealed that in the wealth tax assessments of three Hindu undivided families (specified), for the assessment years 1986-87 to 1989-90 and 1990-91 completed in March 1992 and 1993, tax was levied incorrectly at the rates applicable to Hindu undivided family (ordinary) instead of at the higher rates applicable to Hindu undivided family (specified). The mistake resulted in short levy of tax aggregating Rs. 7.67 lakhs.

The Ministry has accepted the audit observations.

Non/short levy of interest for belated submission of return

6.7 Under the Wealth Tax Act, 1957, where the return of net wealth for any assessment year is furnished after the specified due date or is not furnished, the assessee shall be liable to pay simple interest at the rate of two percent for every month or part of a month from the date immediately following the due date to the date of filing the return, on the amount of tax determined in regular assessment.

Four illustrative cases involving non-levy/ short levy of interest on tax determined on regular assessments aggregating Rs. 3.75 lakhs for delay in filing the returns by 5 assessees are given below:

(Amount in lakhs of rupees)

Sl. No.	State/Commissioner charge/status of assessees	Assessment year/Date of assessment	Section under which assessed	Specified due date/Date of filing the return	Tax due	Interest levied	Non/ short levy of interest
1.	Tamil Nadu/ T.N.III/Madras Individual	1989-90 & 1990-91/ January 1993	16(3)	31 October 1989 & 31 October 1990/ 31 March 1992	6.28	0.84	1.82
2.	West Bengal/WB.IX Calcutta/ Individual and H.U.F	1990-91/ January and March 1993	16(3)	31 August 1990/ December 1991 & February 1992	2.29	-	0.77

3.	Uttar Pradesh Meerut H.U.F.	1990-91 March 1993	16(3)	31 August 1990/ 1 October 1991	2.41	-	0.58
4.	Andhra Pradesh/ A.P. Hyderabad/ Individual	1990-91 March 1993	16(3)	30 June 1990/ 30 June 1992	1.34	0.06	0.58

The Ministry has accepted the audit observations at Sl. Nos. 1,3 & 4. Their response to the remaining case has not been received.

Wealth tax on companies

6.8 Under the provisions of section 40 of Finance Act, 1983, with effect from the assessment year 1984-85, companies other than those in which the public are substantially interested are liable to wealth tax at a flat rate of 2 percent (plus 10 percent surcharge for the assessment year 1988-89 only) of the net wealth comprising the aggregate market value of the specified assets belonging to the company reduced by the debts owed by the company pertaining to such assets on the valuation date.

Non-levy of wealth tax

6.8.1(i) In West Bengal, Kerala, Karnataka, Madhya Pradesh and Bihar charges, scrutiny of the income tax assessment records of 8 closely held companies for the assessment years 1984-85 to 1991-92 revealed that the companies owned let out immovable properties and motor cars which were chargeable to wealth tax. However, neither did assessee companies file their returns of net wealth nor did the department initiate any wealth tax proceedings. The omissions resulted in aggregate gross wealth of Rs. 773.78 lakhs escaping assessment with consequent non-levy of wealth tax of Rs. 15.73 lakhs. Brief particulars of these cases are given below:

(Amount in lakhs of rupees)

S.No.	State/ Commissioner's charge	Assessment year	Type of assets owned	Gross rent received from let out property	Value of assets	Tax effect
1.	West Bengal WB III Calcutta	1984-85 to 1987-88	Godowns, land and Motor cars	25.66	244.79 (including value of land and motor cars)	4.68
2.	Kerala Trivandrum	1986-87 to 1989-90	Buildings and Motor cars	16.73	168.06 (including value of motor car)	3.21

3.	West Bengal WB V & III Calcutta (Two companies)	1989-90 to 1991-92	Buildings	14.53	128.89	2.52
4.	Karnataka Kar I Banglore	1990-91	Buildings	13.68	107.45	2.11
5.	Bihar Ranchi	1989-90 to 1991-92	Building & land appurtenant thereto	4.17	41.56	1.11 (including interest)
6.	West Bengal W.B. II Calcutta	1989-90 and 1990-91	Building & Motor car	5.19	56.17 (including value of motor car)	1.09
7.	Madhya Pradesh Bhopal	1988-89 to 1990-91	Buildings	2.54	26.86	1.01 (including interest)

The Ministry has accepted the audit observations in all the cases.

(ii) Under the Act ibid the specified assets include building or land appurtenant thereto other than building or part thereof used by the assessee as factory, godowns, warehouse, hotel or office for the purposes of its business or as a hospital, creche, school, canteen, library, shelter, rest room or lunch room mainly used for the welfare of its employees.

In Kerala charge, the income tax assessment records of a closely held company for the assessment years 1987-88 to 1991-92 disclosed that the assessee company owned building and land appurtenant thereto used as a hospital, valued at Rs.67.63 lakhs, Rs.68.11 lakhs, Rs.93.97 lakhs, Rs. 90.93 lakhs and Rs.83.33 lakhs during the relevant previous years respectively. Audit scrutiny revealed that the building and land appurtenant thereto owned by the assessee company was not used as a hospital mainly for the welfare of its employees and as such, the assets constituted wealth of the company. However, neither the assessee company had filed the returns of wealth nor did the department initiate any wealth tax

6.8

proceedings.The omission resulted in aggregate wealth of Rs.236.59 lakhs escaping assessment with consequent non-levy of wealth tax of Rs.4.73 lakhs.

The Ministry has accepted the audit observation.

(iii) In West Bengal charge, the income tax assessment records of a closely held company for the assessment year 1991-92, completed in December 1992 disclosed that the assessee company acquired a plot of land on lease basis in July 1983, in a metropolitan city for 999 years from the state government at a cost of Rs. 24.61 lakhs. As this asset was a specified asset owned by the company, the assessee was liable to wealth tax from the assessment year 1984-85 onwards. Audit scrutiny revealed that the department did not initiate any wealth tax proceedings for the assessment years 1984-85 to 1991-92 against the assessee company. The omission resulted in non-levy of wealth tax aggregating Rs. 3.65 lakhs.

The Ministry has accepted the audit observation.

(iv) In Maharashtra charge, scrutiny of income tax assessment records of a company for the assessment year 1989-90, completed in February 1991, disclosed that the assessee company claimed long term capital loss on sale of land owned by it from assessment year 1984-85 at Rs. 1.90 lakhs. The value of land as on 31 March 1974, as per the valuation report dated 1 January 1990 of the approved valuer was Rs. 22.87 lakhs. The value of the land constituted wealth of the company. However, the company did not file the returns of net wealth for assessment years 1984-85 to 1988-89 nor did the department initiate any wealth tax proceedings. The omission resulted in wealth aggregating Rs. 114.35 lakhs escaping assessment with consequent non levy of tax of Rs. 2.74 lakhs.

The Ministry has accepted the audit observation.

(v) In Maharashtra charge, a private limited company owned a flat which was assessed to wealth tax at Rs.33 lakhs for the assessment years 1988-89 and 1989-90, in March 1992. Audit scrutiny revealed that the assessee owned this flat from the assessment year 1984-85 onwards. However, the assessee company did not file the returns of wealth nor did the

department initiate any wealth tax proceedings. The omission resulted in aggregate wealth of Rs.132 lakhs escaping assessment with consequent non-levy of wealth tax of Rs.2.64 lakhs.

The Ministry has accepted the audit observation.

Incorrect valuation of immovable properties

6.8.2 Under section 40 of the Finance Act, 1983, companies other than those in which public are substantially interested are liable to wealth tax at a flat rate of two percent on the value of assets specified in the Wealth Tax Act. Prior to its amendment by Finance (No. 2) Act, 1991 from assessment year 1992-93, the value of such specified assets shall be estimated to be the price which in the opinion of the Wealth Tax officer, these would fetch if sold in the open market on the valuation date.

In Tamil Nadu charge, the wealth tax assessments of five closely held companies for the assessment years 1989-90 to 1991-92 were completed between August 1991 and March 1993 adopting an aggregate value of nine immovable properties at Rs. 164.44 lakhs as per Schedule III to Wealth Tax Act, 1957. Audit scrutiny revealed that in the case of three companies the aggregate market value of six immovable properties worked out to Rs. 682.55 lakhs for assessment years 1989-90 and 1990-91 on the basis of value adopted in assessment for assessment year 1988-89. In the case of the two other companies, the market value of three immovable properties was determined by the Departmental Valuation Officer at Rs. 398.57 lakhs in the case of one company and at Rs. 93.26 lakhs and Rs. 43.35 lakhs for two properties in the case of another company. Omission to adopt the market value of the properties as determined by Departmental Valuation Officer and the value as estimated by the assessing officer in assessment year 1988-89 resulted in underassessment of wealth aggregating Rs. 1157.01 lakhs with consequent short levy of tax of Rs. 22.69 lakhs.

The Ministry has accepted the audit observation.

B - GIFT TAX

General

6.9 In the financial years 1989-90 to 1993-94, gift receipts vis-a-vis the budget estimates were as given below:

Year	Budget Estimates (in crores of rupees)	Actuals	Variation	Percentage variation
1989-90	9.50	8.07	(-)1.43	(-)15.05
1990-91	9.00	3.38	(-)5.62	(-)62.44
1991-92	9.00	8.44	(-)0.56	(-)6.22
1992-93	5.00	9.27	4.27	85.40
1993-94	10.00	4.99	(-)5.01	(-)50.10

6.10 Particulars of assessments completed, assessments pending and demands in arrear for the last five years ending 31 March 1994 were as given below:

Year	No.of assessments completed during the year	No. of cases pending assessment at the end of the year	Arrear of demands at the end of the year (in crores of rupees)
1989-90	52,560	18,683	62.61
1990-91	46,621	15,951	54.49
1991-92	42,176	10,683	37.86
1992-93	30,170	9,968	26.12
1993-94	29,489	7,989	31.81

Results of Audit

6.11 During the test audit of assessments made under the Gift Tax Act,1958, conducted during the period 1 April 1993 to 31 March 1994 short levy of gift tax of Rs. 8.38 crores was noticed in 171 cases.

A total number of 7 draft paragraphs involving tax effect of Rs.12.60 lakhs was issued to the Ministry of Finance for comments during March to August 1994. The Ministry of Finance has accepted the observations in 6 cases involving tax effect of Rs.10.72 lakhs. three illustrative cases involving tax effect of Rs. 7.99 lakhs are given in the following paragraphs. The Ministry of Finance has accepted the audit observations in these cases.

Non-levy of tax on deemed gift

6.12 Under the Gift Tax Act, 1958, when property is transferred otherwise than for adequate consideration, the amount by which the market value of the property on the date of transfer exceeds the value of the consideration shall be deemed to be a gift made by the transferor. The Act also provides that the value of the property shall be estimated to be the price which it would fetch if sold in the open market on the date on which the gift was made.

(i) In Gujarat charge, the income tax assessment records of an assessee for the assessment year 1986-87, revealed that the assessee sold land and building in November 1985 for a consideration of Rs.1.52 lakhs. Audit scrutiny revealed that the departmental valuation officer determined the value of the aforesaid property at Rs.12.52 lakhs as on November 1985. The difference of Rs.11 lakhs between the market value and value at which the aforesaid property was sold constituted deemed gift attracting levy of gift tax. However, neither the assessee filed any gift tax return nor did the department initiate any gift tax proceedings. The omission resulted in non-levy of gift tax of Rs.3.24 lakhs.

The Ministry has accepted the audit observation.

(ii) From 1 April 1989, Schedule II of the Gift Tax Act,1958, provides that the value of gift of shares or debentures of companies will be taken as per Schedule III to the Wealth Tax Act.

In Maharashtra charge, audit scrutiny of the income tax assessment records of an individual, for the assessment year 1991-92, revealed that the assessee had sold, in the relevant previous year, 20,925 shares of three companies at Rs.10 each, for a total consideration of Rs.2.09 lakhs. The value of each share of these companies worked out to Rs.42.47, Rs.25.66 and Rs.54.55 under the valuation rules prescribed in Schedule III of the Wealth Tax Act. On this basis, the total value of 20,925 shares sold by the assessee worked out to Rs.10.24 lakhs. Thus the difference of Rs.8.15 lakhs between the value as worked out under the provisions of the Gift Tax Act and the sale consideration, constituted deemed gift attracting levy of gift tax. However, neither the assessee filed any gift tax return nor did the department initiate any gift tax proceedings. The omission resulted

in non-levy of gift tax aggregating Rs.2.45 lakhs.

The Ministry has accepted the audit observation.

(iii) In Gujarat charge, the wealth tax assessment records of an individual for the assessment year 1990-91 disclosed that the assessee had sold three plots of land for a consideration of Rs.5.07 lakhs. Audit scrutiny revealed that the value of the said plots as on 31 March 1990 was determined by the departmental valuation officer in January 1992 at Rs.12.92 lakhs. The difference of Rs.7.85 lakhs between the market value and the value at which the property was sold constituted deemed gift attracting levy of gift tax. However, neither the assessee filed any gift tax return nor did the department initiate any gift tax proceedings. The omission resulted in non-levy of gift tax of Rs.2.30 lakhs.

The Ministry has accepted the audit observation.

A K Banerjee

(A.K. BANERJEE)
Principal Director of Receipt Audit
(Direct Taxes)

New Delhi
The 23 FEB 1995

Countersigned

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

New Delhi
The 01 MARCH 1995

APPENDIX I

Reference : (Paragraph 2.3.(i) of the Report)

Variation between Budget estimates and actuals

Year	Budget Estimates	Actuals	Variation	Percentage of of variation
	(In crores of Rupees)			
024-Interest Tax				
1990-91	----	(-)0.86	(-)0.86	---
1991-92	535.00	305.04	(-)229.96	(-)42.98
1992-93	800.00	714.70	(-)85.30	(-)10.66
1993-94	900.00	727.58	(-)172.42	(-)19.38
0032-Taxes on Wealth				
1990-91	175.00	231.17	56.17	32.09
1991-92	255.00	306.93	51.93	20.36
1992-93	300.00	467.27	167.27	55.75
1993-94	200.00	153.98	(-)46.02	(-)23.01
0033-Gift Tax				
1990-91	9.00	3.38	(-)5.62	(-)62.44
1991-92	9.00	8.44	(-)0.56	(-)6.22
1992-93	5.00	9.27	4.27	85.40
1993-94	10.00	4.99	(-)5.01	(-)50.10
0028- Other taxes on income and expenditure				
1992-93	50.00	152.00	102.00	20.40
1993-94	150.00	228.75	78.75	52.50

APPENDIX II

(Reference: Paragraph 2.5.2 of the Report)

Cost of collection

	Collection	Expenditure on collection	Percentage
	(In crores of Rupees)		
0024-Interest Tax			
1990-91	(-)0.86	0.02	0.02
1991-92	305.04	0.03	0.01
1992-93	714.70	0.03	0.01
1993-94	727.58	0.03	0.01
0028- Other taxes on income and expenditure			
1990-91	80.27	1.61	2.00
1991-92	144.38	1.79	1.24
1992-93	152.37	3.11	2.04
1993-94	228.75	2.34	1.02
0032-Taxes on wealth			
1990-91	231.17	18.41	7.96
1991-92	306.93	20.52	6.68
1992-93	467.27	23.63	5.05
1993-94	153.98	26.69	17.33
0033-Gift Tax			
1990-91	3.38	2.30	68.04
1991-92	8.44	2.56	30.33
1992-93	9.27	2.95	31.82
1993-94	4.99	3.34	66.93

APPENDIX III

(Reference : Paragraph 2.12(v) of the Report)

Year-wise position of tax determined (including interest and penalty) in cases settled by Settlement Commission

Financial year	Income Tax		Wealth Tax	
	(In lakhs of rupees)			
	Addl.tax collected/ collectable on admission of applications	Gross demand created in respect of cases settled	Addl. tax collected/ collectable on admission of applications	Gross demand created in respect of cases settled
1990-91	764.62	938.41	4.71	55.73
1991-92	864.17	1,593.93	22.70	101.97
1992-93	1,795.71	1,895.67	11.53	781.68
1993-94	2,547.85	3,773.15	125.45	90.22

APPENDIX IV

(Reference: Paragraph 2.17(ii) of the Report)

Functioning of Valuation cells- Cases referred, disposed of and pendency in respect of other Direct Taxes

	Year	No. for disposal at the beginning of the year	No. of cases referred during the year	Disposed of during the year	Pending at the end of year
(a) Wealth Tax	1990-91	3,047	7,319	8,571	1,795
	1991-92	1,795	5,644	6,067	1,372
	1992-93	1,372	4,014	4,470	916
	1993-94	916	3,259	3,310	865
(b) Gift Tax	1990-91	25	76	75	26
	1991-92	26	53	67	12
	1992-93	12	47	44	15
	1993-94	15	78	51	42
(c) Estate duty	1990-91	26	45	67	4
	1991-92	4	16	18	2
	1992-93	2	6	3	5
	1993-94	5	1	6	0

APPENDIX V

(Reference : Paragraph 2.18 of the Report)

Revenue demands written off by the Department

Category	
I. (a)	Assessees who have no assets or have become insolvent.
(b)	Assessees who have gone into liquidation or are defunct.
	Total.
II.	Assessees being untraceable.
III.	Assessees having left India.
IV.	Other reasons :
(a)	Assessees having no attachable assets.
(b)	Amount being small, etc.
(c)	Amount written off as a result of scaling down of demand.
	Total.
V.	Amount written off on grounds of equity or as a matter of international courtesy or where time, labour and expenses involved in legal remedies for relisation are considered disproportionate to the amount of recovery.
	Grand Total.