



सत्यमेव जयते

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प्रमाणोक्तः राज्यासभे पेशः

(एन. व. चन्द्राशेकरा मुर्ति)
(M.V. Chandrasekhara Murthy)

REPORT OF THE
COMPTROLLER AND AUDITOR GENERAL
OF INDIA

PAPERS LAID ON THE TABLE
OF THE RAJYA SABHA
ON 10 MAY 1994

FOR THE YEAR ENDED 31 MARCH 1993
NO. 5 OF 1994

UNION GOVERNMENT
(REVENUE RECEIPTS- DIRECT TAXES)

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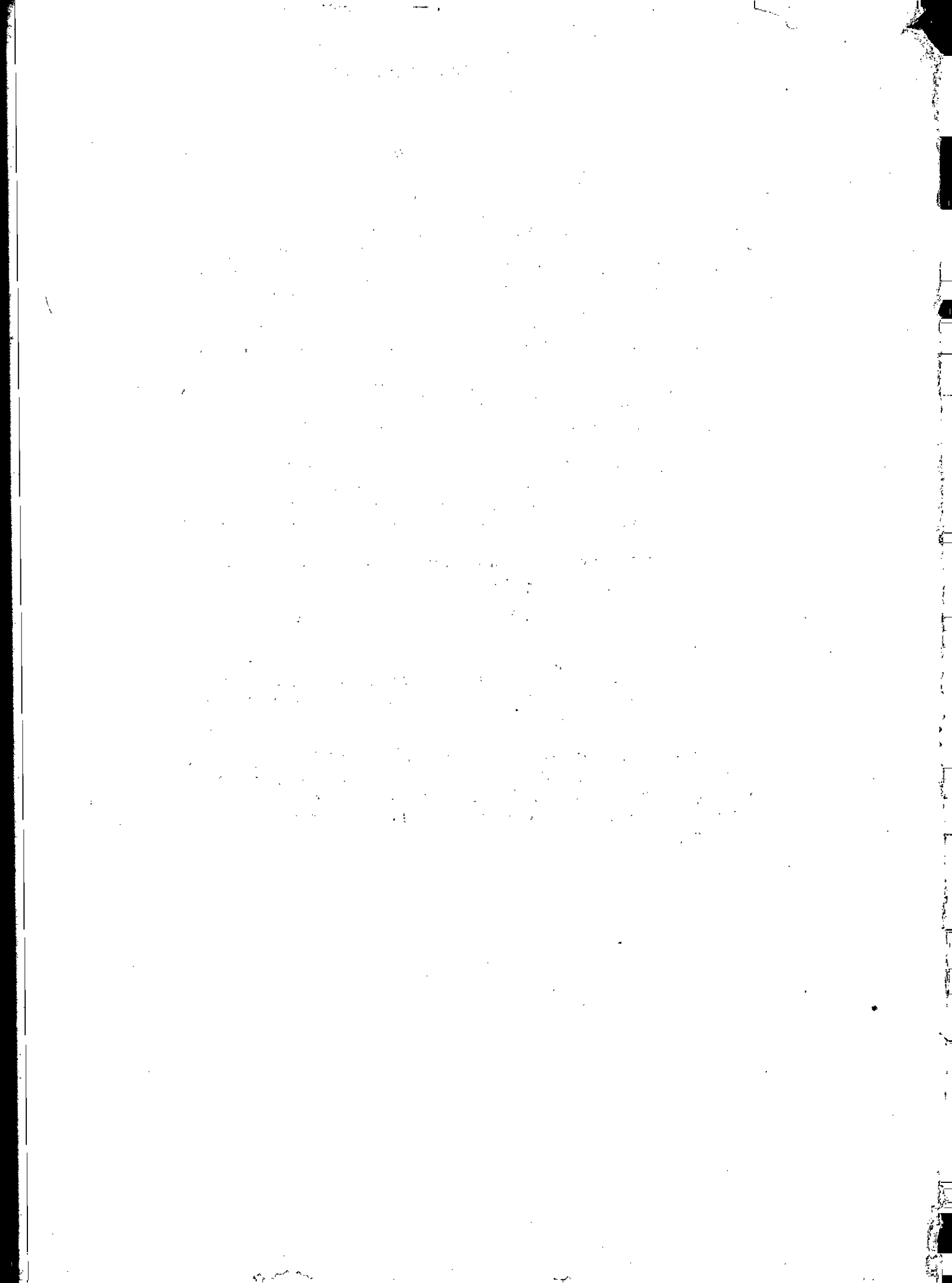
PREFATORY REMARKS

This Report for the year ended 31 March 1993 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, gift tax, expenditure tax and interest tax. The report is arranged in the following order:

- (i) Chapter I incorporates the statistical information regarding the working results of the tax administration and audit;
- (ii) Chapter 2 includes three system appraisals on 'Functioning of investigation circles', 'Exemption under section 80-O of the Income Tax Act, 1961' and 'Special provisions relating to minimum tax';
- (iii) Chapter 3 mentions the results of audit of corporation tax;
- (iv) Chapter 4 similarly mentions the results of audit of income tax; and
- (v) Chapter 5 covers issues arising from audit of wealth tax, gift tax, expenditure tax and interest tax.

The observations featured in this report are among those which came to notice during the course of test audit during 1992-93 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 200 paras bringing out audit observations involving a revenue effect of Rs.128.47 crores. Three system^o appraisals are also featured in this report.

2. An analysis of the trend of receipts has revealed an increase in gross receipts from direct taxes during 1992-93 over the previous year. The actual collection for the year was Rs.18,097.29 crores against the budget estimates of Rs.17,153 crores representing 17.95 percent increase over last year's collection of Rs.15342.36 crores. There was an increase in the number of assessees as well, which rose from 77.95 lakhs to 83.62 lakhs, an increase of about 7.27 per cent compared to last year.

3. The expenditure incurred for the collection of all direct taxes during the year 1992-93 was Rs.296.48 crores against Rs.256.46 crores incurred in the previous year. As a percentage of total collection, it came to 1.6 percent (against 1.7 per cent in 1991-92). 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.19,049.39 crores. The cost of collection in respect of income tax and corporation tax alone as a percentage of post assessment collections of these taxes was 14.02 per cent (against 16.35 per cent in 1991-92).

4. Overall pendency of assessments increased to 14.50 lakhs cases as on 31 March 1993 (from 13.21 lakhs cases as on 31 March 1992). This happened even though the Board had issued directions for 100 per cent disposal of summary assessment by 31 July 1992, and 10 per cent reduction in scrutiny assessments, brought forward at the beginning of the year.

5. Arrears of tax have also shown an increasing trend. Cumulative arrears of corporation tax and income tax increased from 8460.98 crores last year to 9,488.54 crores during the period ending 31 March 1993. Of these, in 3,364 cases alone, the arrears amounted to Rs.5767.04 crores with each of these cases having an arrear of more than Rs.25 lakhs. Arrears continue to mount, despite the Action Plan targets for reducing them. The Action Plan for 1992-93 envisaged an overall reduction of 20 per cent in the aggregate demand as compared to the previous year and remained an area of concern.

6. During the course of test audit, 13,916 audit observations involving underassessment of tax of Rs.3,490.62 crores were intimated to the department. Of these, only 200 paras feature in this Report, besides the following system appraisals:

- (a) Functioning of Investigation Circles.
- (b) Exemptions under section 80-O of Income Tax Act.
- (c) Special provisions relating to minimum tax.

System Appraisals

7. The important audit observations emanating from the system appraisals are briefly mentioned below:

Functioning of Investigation circles

(a) The Income Tax Act, 1961, empowers the departmental authorities to conduct searches in order to collect evidence of tax evasion and to seize unaccounted assets for early satisfaction of tax liabilities likely to arise as a result of such searches. Assessments in these cases are then framed in the Investigation circles. Some of the audit observations emerging from a test check of 165 Investigation circles, revealed the following:

(i) In 35.88 per cent of search and seizure cases where final assessments were completed, no concealed income was detected or established.

(ii) In 42 assessments, mistakes/omissions were noticed which resulted in non assessment/underassessment of income/wealth of Rs.3.34 crores with consequent non/short levy of tax of Rs.1.05 crores.

(iii) Inordinate delays were noticed in issue of notices for reopening cases where incriminating material was seized and also in completion of regular assessments in such cases.

(iv) Despite inclusion of search and seizure cases in the "Key Result Area" in successive Action plans of the department, these cases were not receiving due attention. While the pendency was increasing over the years, the success rate of additions made by the department in appellate proceedings was about 26.94 per cent.

(v) Large variations were noticed in the income estimated in preliminary orders passed for determining tax liability, appraisal reports of the Investigation wing which conducts the searches and income finally determined in regular assessment, suggesting that either the estimates were wild, or the assessments were not being carefully framed.

(vi) Even in cases where tax demand was raised, recovery was not being vigorously pursued. In one charge alone, tax of Rs.36.56 crores and penalty of Rs.3.04 crores were pending collection.

(vii) The department initiated prosecution proceedings in less than 3 per cent of cases assigned to Investigation circles, and only in a negligible number of cases could convictions be obtained.

(viii) The deficiencies and irregularities noticed would indicate the need for a critical review of the system of search and seizure to make it more effective. [Para 2.1]

**Exemption
under
Section 80-O
of Income
tax Act**

(b) In order to boost development of technical know-how in the country and its export abroad, thus augmenting the flow of foreign exchange into the economy, the Income Tax Act provides for fifty per cent deduction of income received by way of royalty, commission, fees etc. from foreign governments or foreign enterprises. A test check of 218 cases revealed omissions/mistakes involving tax effect of Rs.8 crores in 51 cases. Some important observations are:

(i) Income as computed in accordance with the provisions of Income Tax Act, and that which is included in the gross total income of the assessee alone qualifies for relief. Deductions allowed on gross income without reference to income included in the gross total income, resulted in undercharge of tax of Rs.266.57 lakhs in 28 cases.

(ii) Irregularities in approval of or non-observance of conditions of approval of agreements with foreign parties, resulted in under-charge of tax of Rs.185.26 lakhs in 13 cases. [Para 2.2]

Special provision relating to certain companies regarding minimum tax

(c) Section 115J of Income Tax Act which remained on the statute for a limited period of three assessment years (from 1988-89 to 1990-91), provided that where total income of a corporate assessee under the normal provisions of the Act was negative or less than 30 per cent of its book profits, the income chargeable to tax would be deemed to be 30 per cent of such profits. Some of the important observations based on a review of assessments involving these special provisions, are:

(i) Failure to invoke the special provisions in cases where incomes were shown at less than 30 per cent of book profits, resulted in short levy of tax of Rs.11 crores in 70 cases. On the other hand, erroneous recourse to these special provisions, where income under the normal provisions of the Act was more than 30 per cent of book profits, led to under charge of tax of Rs.2.36 crores in 15 cases.

(ii) In several cases, book profits were not increased as prescribed, by the amount of provisions for bad and doubtful debts, gratuity, estimated loss on stores, write back of depreciation etc. resulting in under charge of tax of Rs.23.32 crores in 67 cases.

(iii) In some other cases, book profits were incorrectly reduced by the amounts of export profits, transfers to special reserves, differences on account of exchange rate fluctuations although these were not admissible under the normal provisions of the Act. This led to short levy of tax of Rs.2.37 crores in 19 cases.

(iv) Cases were noticed where unabsorbed depreciation, investment allowance and losses

relating to earlier years were allowed to be set off, though nothing actually remained to be adjusted. This led to short levy of tax of Rs.4.74 crores in 13 cases.

(v) According to instructions issued by the Board, companies were allowed to set off against book profits, brought forward losses or unabsorbed depreciation whichever was less. Mistakes and omissions were noticed in implementing these instructions in 44 cases leading to short levy of tax of Rs.3.03 crores. [Para 2.3]

**Corporation
Tax**

8(i) Under-assessments of tax on account of avoidable mistakes continue to occur, despite Boards' instructions stressing the necessity for ensuring accuracy in the computation of income and tax, carry forward of figures etc. Arithmetical errors, double allowances and other similar omissions in 6 cases led to undercharge of tax of Rs.2.86 crores. [Para 3.6(i) to (iii)]

(ii) In Maharashtra charge, tax on a closely held domestic company was levied at 50 per cent of the total income instead of the correct rate of 55 per cent leading to short levy of tax of Rs.180.92 lakhs [Para 3.7.1].

(iii) In West Bengal charge, the allowance of provision for payment of gratuity amounting to Rs.396.88 lakhs to an unapproved gratuity fund resulted in excess carry forward of loss by an identical amount involving a potential tax effect of Rs.214.32 lakhs and additional income tax of Rs.42.86 lakhs [Para 3.10].

(iv) In Rajasthan charge, in the case of a banking company, failure to restrict the deduction of bad debts to the amount by which these exceeded the provision for bad and doubtful debts, led to under assessment of income of Rs.294.17 ^{lakhs} involving short levy of tax of Rs.154 lakhs [Para 3.11].

(v) In Maharashtra charge, in the case of a public sector undertaking the allowance of provisions for probable increase in liability due to future variation in rates of exchange and for depreciation in value of assets, led to under-assessment of income of Rs.195.95 lakhs involving short levy of tax of Rs.108.02 lakhs [Para 3.13.1(i)].

(vi) In West Bengal charge, sales tax collected but not paid to the government was not included in the total income, which led to short computation of income by Rs.406.54 lakhs involving undercharge of tax of Rs.390.23 lakhs [Para 3.14.1(i)].

(vii) In West Bengal charge, allowance of liability for provident fund contribution, not paid within the stipulated period resulted in excess determination of loss by Rs.21.50 lakhs with a potential tax effect of Rs.11.29 lakhs.[Para 3.14.1(ii)]

(viii) In West Bengal charge, in the case of a widely held company, the estimated excise duty included in differential price receivable on its products, was debited to profit and loss account. Failure to disallow the unpaid duty while computing total income resulted in underassessment of income of Rs.1398.64 lakhs involving undercharge of tax of Rs.992.91 lakhs. [Para 3.14.2(i)]

(ix) In Madhya Pradesh charge, failure to disallow notional loss on revaluation of investment in the case of a banking company, resulted in underassessment of income by Rs.118.12 lakhs involving short levy of tax of Rs.98.47 lakhs. [Para 3.16.1(i)]

(x) In Maharashtra and Orissa charges, in the case of two companies, depreciation was allowed on the notional additions to the cost of assets representing increase in liability of foreign loans on account of intermediate fluctuation in the rate of exchange. As the liability had not been actually discharged at the time of repayment of loans, the grant of depreciation on additional cost was irregular, resulting in excess allowance of depreciation by Rs.534.96 lakhs involving notional tax effect of Rs.280.86 lakhs. [Para 3.19(i)&(ii)]

(xi) In Tamil Nadu charge, an assessee company running two units, claimed depreciation in the transitional previous year for 21 months, though one of the units started only a few days before the end of the previous year. Failure to restrict the depreciation in respect of that unit to a normal period of 12 months resulted in excess depreciation allowance of Rs.241.91 lakhs involving short levy of tax of Rs.240.29 lakhs. [Para 3.22.(i)]

(xii) In Maharashtra charge, non exclusion of house property income, dividend and interest on securities from eligible profit resulted in excess grant of relief under the investment deposit account by Rs.2879 lakhs involving tax effect of Rs.2141 lakhs. [Para 3.24.2 A.2]

(xiii) In West Bengal charge, incorrect allowance of deduction towards investment deposit account in the assessment year 1991-92, when the provision was no longer operative, led to underassessment of income of Rs.167.50 lakhs involving short levy of tax of Rs.99.39 lakhs. [Para 3.24.3]

(xiv) In Maharashtra charge, failure to reduce loss under the head 'capital gains' by deductions specified in the Act, resulted in excess determination of loss by Rs.151.45 lakhs involving notional short levy of tax of Rs.87.08 lakhs. [Para 3.25]

(xv) In West Bengal charge, failure to include accrued income representing increased rate of power tariff in the total income resulted in underassessment of income of Rs.268.41 lakhs involving short levy of tax of Rs.134.21 lakhs (potential). [Para 3.26.1(ii)]

(xvi) In West Bengal charge, an assessee obtained interest subsidy of Rs.1588.21 lakhs in respect of liabilities allowed in earlier assessment years. Its non-inclusion in the computation of total income, in the year of receipt resulted in underassessment of income of Rs.809.57 lakhs with consequential undercharge of tax of Rs.833.81 lakhs, including potential tax effect of Rs.408.79 lakhs. [Para 3.26.3]

(xvii) In West Bengal charge, a deduction of Rs.869.03 lakhs, being 50 percent of the foreign income was incorrectly allowed to a closely held company from gross income before allowing depreciation of Rs.762.17 lakhs. This resulted in excess allowance of deduction of Rs.371.91 lakhs involving short levy of tax of Rs.252.11 lakhs. [Para 3.28.1(i)]

(xviii) In Maharashtra charge, a public sector corporation was incorrectly allowed Chapter VI-A deductions amounting to Rs.3.29 crores, though the gross total income of the assessee was nil. This resulted in incorrect

carry forward of loss of Rs.3.29 crores involving a potential short levy of tax of Rs.1.97 crores. [Para 3.28.1(ii)]

(xix) In Uttar Pradesh charge, allowance of deduction on account of export incentives in the absence of statutory report of an accountant and allowance of provision for bonus without evidence in support of its payment, led to under-assessment of income of Rs.100.65 lakhs involving short levy of tax of Rs.82.56 lakhs. [Para 3.29.3]

(xx) In West Bengal charge, irregular allowance of deduction on account of profits from foreign projects on gross incomes instead of the profits from such projects actually included in the gross total income resulted in aggregate excess deductions of Rs.1208.24 lakhs with consequent undercharge of tax of Rs.1022.41 lakhs. [Para 3.31]

(xxi) In West Bengal charge, a closely held company was allowed relief of Rs.362.05 lakhs paid as tax in foreign countries, on doubly taxed income of Rs.804.28 lakhs. Failure to restrict the relief to lower of the two average rates of tax chargeable in those countries and in India, resulted in excess relief of Rs.282.69 lakhs with consequent under-charge of tax of Rs.402.23 lakhs. [Para 3.34.1]

(xxii) In Tamil Nadu charge, a non resident shipping company was allowed deduction of Rs.123.70 lakhs being 50 per cent of the income tax levied on the Indian income in India, though such income did not suffer any tax in the foreign country. Incorrect allowance of relief resulted in under-charge of tax of Rs.123.70 lakhs. [Para 3.34.2]

(xxiii) In Maharashtra charge, failure to levy interest for the shortfall in payment of advance tax, resulted in under charge of tax of Rs.143.51 lakhs. [Para 3.38.1(i)]

(xxiv) In Bihar and West Bengal charges, in the case of a state financial corporation and a widely held company, non-levy of interest for non-payment/short payment of advance tax resulted in under charge of tax of Rs.732.79 lakhs. [Para 3.38.2(ii) &(iii)]

(xxv) In Tamil Nadu and West Bengal charges, in case of four assessee companies

omission to make surtax assessment led to non-levy of surtax of Rs.313.96 lakhs. [Para 3.42]

**Income Tax
other than
Corporation
Tax**

9(i) Avoidable mistakes like incorrect adoption of figures, totalling errors, double allowance, calculation errors and application of lower rate of tax in 9 cases led to undercharge of tax of Rs.58.32 lakhs. [Para 4.6]

(ii) In Gujarat and Kerala charges, in the case of three assesseees, failure to disallow unpaid liabilities representing interest on long-term loans, sales tax, bonus and non-consideration of subsidy received, in the computation of total income, resulted in underassessment of income of Rs.24.22 lakhs involving short levy of tax of Rs.13.35 lakhs. [Para 4.8.1]

(iii) In Kerala charge, a partnership firm engaged in the export of marine products, was incorrectly allowed purchase tax liability, though the assessee was not liable to pay any tax having made purchases for the purpose of export. This led to underassessment of income of Rs.86.15 lakhs involving short levy of tax of Rs.15.85 lakhs. [Para 4.8.5(i)]

(iv) In Maharashtra charge, in a case of a registered firm, failure to disallow payments in excess of Rs. 2500 made in cash, amounting to Rs.20.73 lakhs resulted in underassessment of income of Rs.20.73 lakhs involving short levy of tax of Rs.15.34 lakhs in the hands of the firm and partners. [Para 4.8.7]

(v) In Maharashtra charge, failure to tax capital gains on the sale of business premises, from which the assessee carried on profession, resulted in under-assessment of income of Rs.49.88 lakhs involving short levy of tax of Rs.26.94 lakhs. [Para 4.10.2]

(vi) In Punjab charge, incorrect exemption of share income of two individuals, deriving income from a registered firm located in free trade zone beyond a period of five initial assessment years, resulted in underassessment of income of Rs.110 lakhs involving short levy of tax of Rs.57.81 lakhs. [Para 4.14.1]

(vii) In Gujarat charge, incorrect allowance of deduction in respect of profits and gains derived from new industrial undertaking, beyond the eligible period led to aggregate underassessment of income of Rs.29.11 lakhs involving short levy of tax of Rs.23.05 in the hands of the firm and its partners. [Para 4.14.4]

(viii) In Bihar charge, in the case of a co-operative society, failure to disallow provision for unrealised overdue interest which was not actually written off and not considered bad, led to short levy of tax of Rs.18.17 lakhs. [Para 4.14.7]

Wealth Tax

10(i) In Tamil Nadu charge, a mistake in working out the break-up value of unquoted equity shares, resulted in underassessment of wealth of Rs.609.25 lakhs with consequent short levy of wealth tax of Rs.12.13 lakhs. [Para 5.5.2(a)]

(ii) In Tamil Nadu charge, a closely held company which owned a commercial complex in a metropolitan city, did not file its wealth tax returns for three years though the valuation cell had determined its value at Rs.342.11 lakhs as on 31 March 1988. Adopting the same value for subsequent three assessment years, the wealth which escaped assessment amounted to Rs.1026.33 lakhs involving non-levy of tax of Rs.20.79 lakhs. [Para 5.8.1(i)]

(iii) In Punjab charge, failure to include the value of land appurtenant to buildings, determined at Rs.186 lakhs/227 lakhs in the total wealth of a private limited company, resulted in underassessment of wealth of Rs.640 lakhs involving short levy of tax of Rs.12.82 lakhs in three assessment years. [Para 5.8.2]

Gift Tax

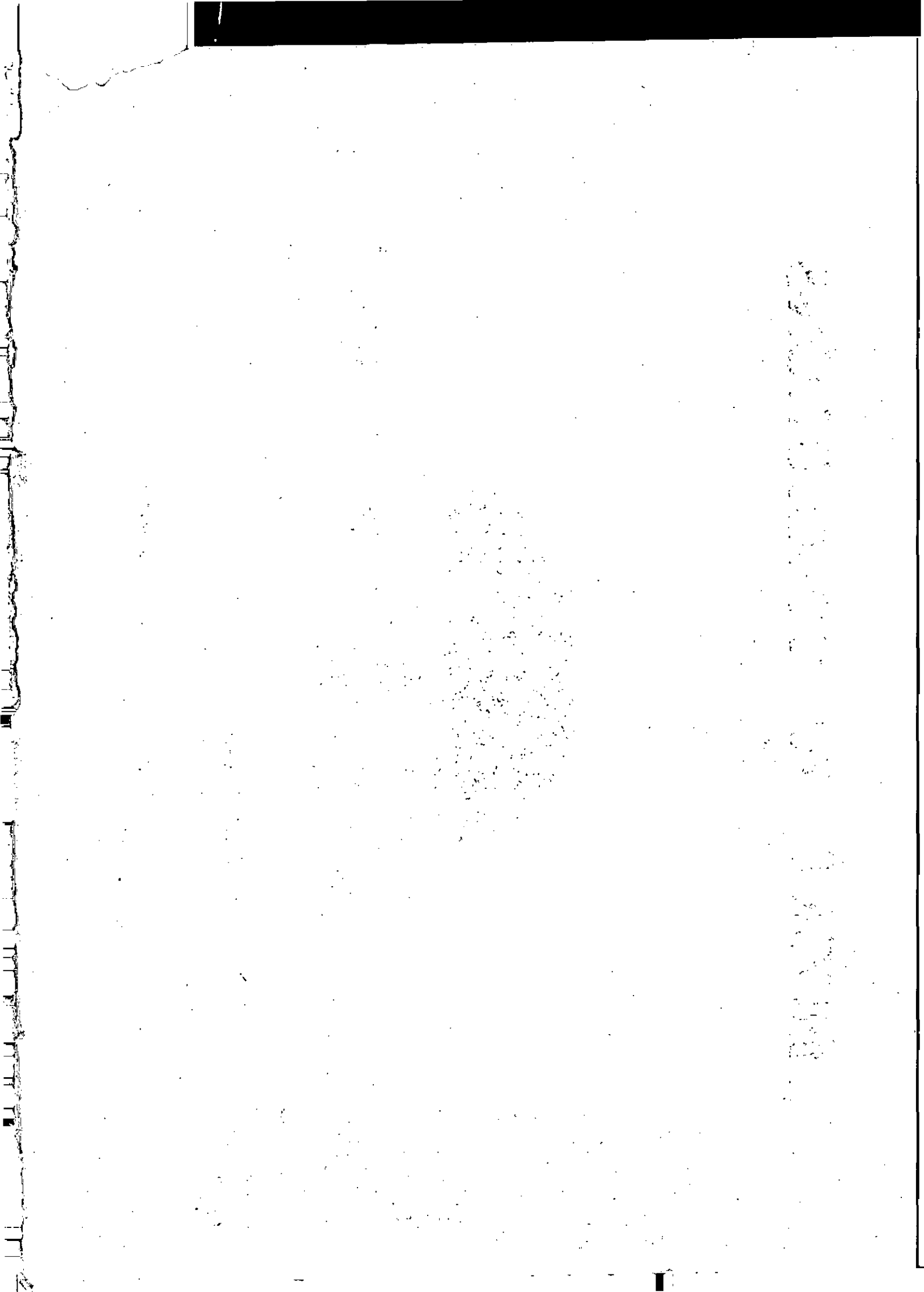
11 In Maharashtra charge, an assessee credited the accounts of his two minor sons with a sum of Rs.10 lakhs each and withdrew these amounts on the same day. Non-levy of gift tax on these amounts led to undercharge of Rs.7.06 lakhs. [Para 5.12]

Expenditure Tax

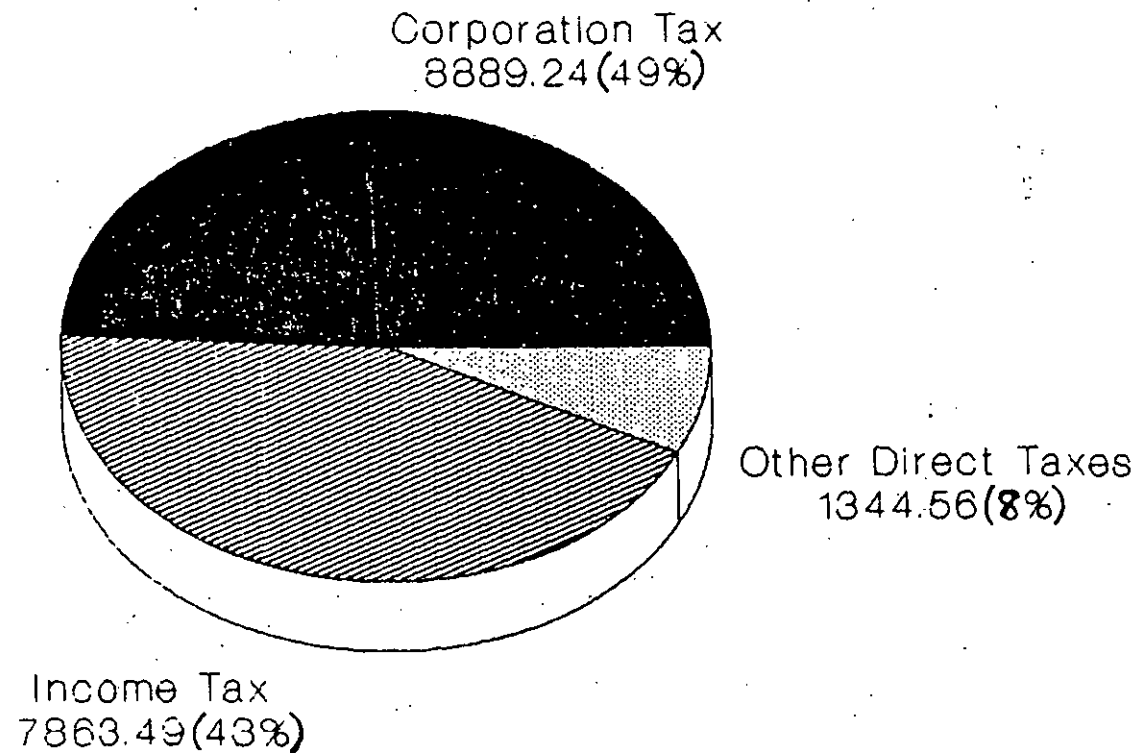
12 In Tamil Nadu charge, non-levy of interest on belated payment/non payment of tax to the credit of Central Government in the case of a closely held company, led to undercharge of tax of Rs.14.13 lakhs in three assessment years. [Para 5.14]

Interest Tax 13(i) In Karnataka charge, failure to revise the interest tax assessments, consequent upon revision of income tax assessment, led to non-levy of interest tax of Rs.107.21 lakhs. [Para 5.16]

(ii) In Maharashtra charge, the income tax assessment of a public sector bank disclosed interest income of Rs.2426 lakhs against Rs.2009 lakhs returned by the assessee. Short levy of interest tax amounted to Rs.14.60 lakhs. [Para 5.17]



INCOME TAX COLLECTIONS (1992-93)



(Figures in crores of rupees)

CHAPTER 1

GENERAL

Receipts under various Direct Taxes 1.1 The total proceeds from Direct Taxes for the year 1992-93* amounted to Rs.18,097.29 crores out of which a sum of Rs.6,059.45 crores was assigned to the States. The figures for the three years 1990-91, 1991-92 and 1992-93 are given below:

		(In crores of Rupees)		
		1990-91	1991-92	1992-93*
0020	Corporation Tax	5335.27	7867.67	8889.24
0021	Taxes on income other than Corporation-tax	5375.34	6705.80	7863.49
0023	Hotel Receipts Tax	1.30	1.24	0.37
0024	Interest Tax	(-) 0.86	305.04	714.70
0028	Other Taxes on Income and Expenditure	80.27	144.38	152.00
0031	Estate Duty	3.07	2.86	0.95
0032	Taxes on wealth	231.17	306.93	467.27
0033	Gift tax	3.38	8.44	9.27
	Gross Receipts	11028.94	15342.36	18097.29

Less share of net proceeds assigned to the States:

Income Tax	4,119.24	5,104.32	6059.45
Total	4,119.24	5,104.32	6059.45
Net Receipts	6,909.70	10,238.04	12037.84

* Figures furnished by the Controller General of Accounts are provisional

The gross receipts under Direct Taxes during 1992-93 went up by Rs.2754.93 crores compared with the receipts during 1991-92 against an increase of Rs.4313.42 crores in 1991-92 over those for 1990-91. Receipts under Corporation Tax registered an increase of Rs.1021.57 crores while receipts under Taxes on Income other than Corporation-tax increased by Rs.1157.69 crores.

Trend of collection

1.2(i) The trend in collection of Direct Taxes since 1989-90 has been as under:

Year	Collection (in crores of rupees)				Index taking 1988-89 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
1988-89	4407.21	4241.24	180.31	8828.76	100.0	100.0	100.0	100.0
1989-90	4728.92	5008.98	269.88	10007.78	107.3	118.1	149.7	113.4
1990-91	5335.27	5375.34	318.33	11028.94	121.1	126.7	176.6	124.9
1991-92	7867.67	6705.80	768.89	15342.36	178.5	158.1	426.4	173.8
1992-93*	8889.24	7863.49	1344.56	18097.29	201.7	185.4	745.6	204.9

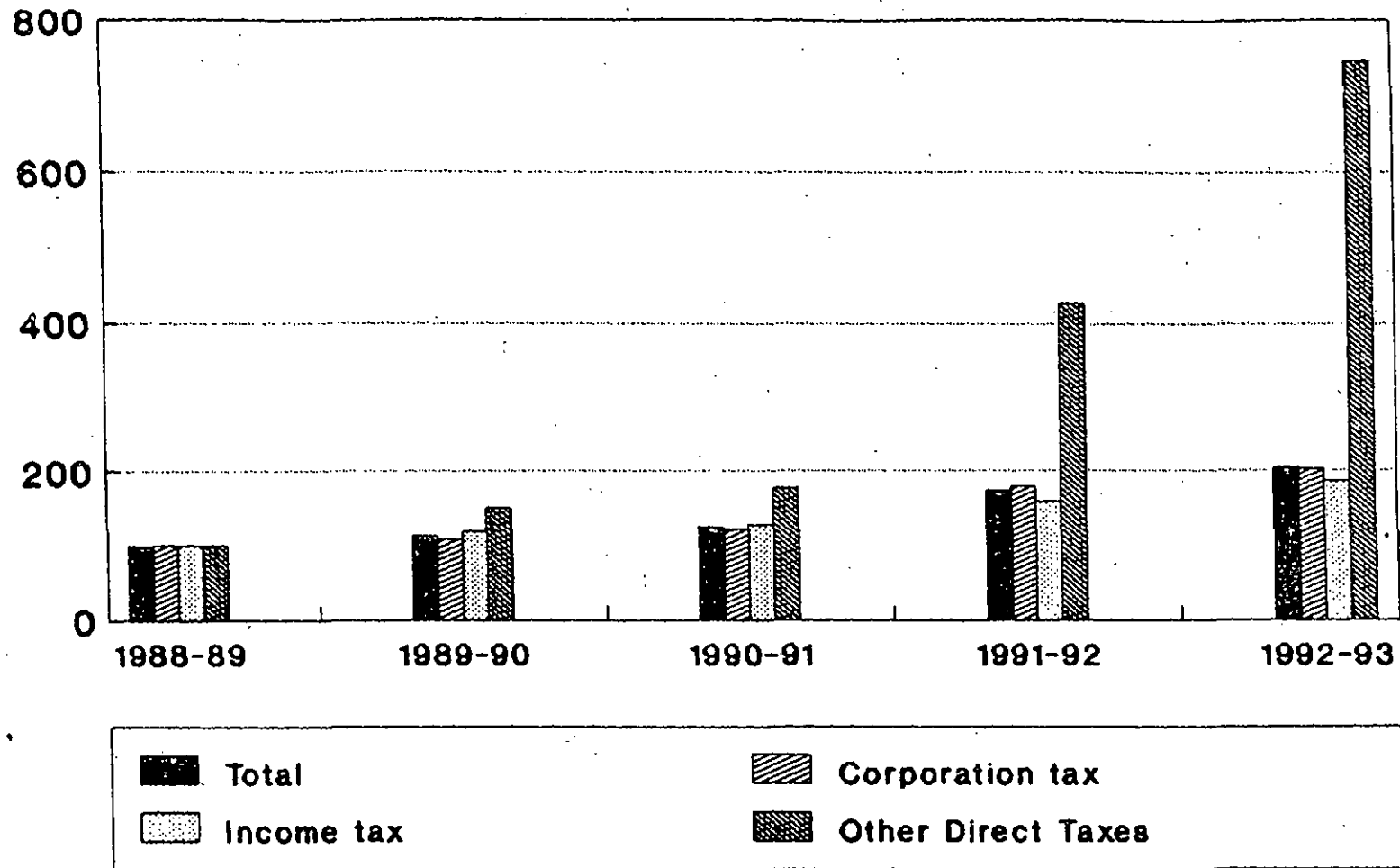
(ii)* Corporation Tax and income Tax collections since 1988-89 shown as percentage of the Gross Domestic Product is as follows:

Year	Corporation Tax	Income Tax other than Corporation Tax	G.D.P. at factor cost (current prices)**	Percent of G.D.P.	
				Corporation Tax	Income Tax
(Rupees in crores)					
1988-89	4407.21	4241.24	3,51,724	1.3	1.2
1989-90	4728.92	5008.98	3,95,143	1.2	1.3

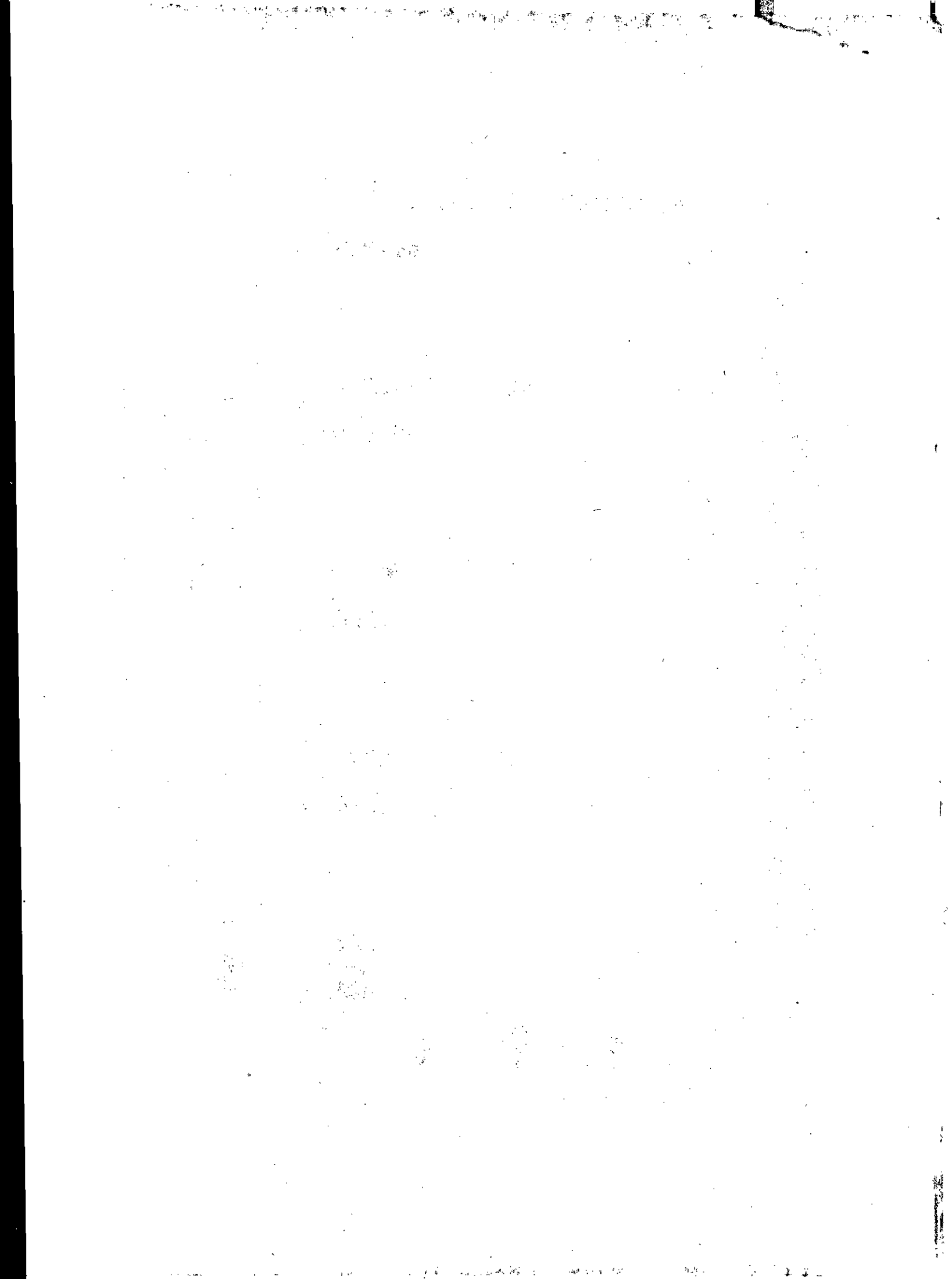
* Figures are provisional

** GDP Figures collected from National Accounts Statistics Organisation, Ministry of Planning. GDP figures for 1991-92 are as per estimates of NASO

TREND IN COLLECTION OF DIRECT TAXES OVER THE YEARS 1988-89 to 1992-93



(BASE YEAR 1988-89 - 100)



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

Variation between Budget estimates and Actuals

1.3.1 The comparative position of actual receipts vis-a-vis the budget estimates under the different heads are given below for the years 1988-89 to 1992-93:

Year	Budget Estimates	Actuals	Variation	Percentage of variation
(In crores of Rupees)				
0020- Corporation Tax				
1988-89	4,050.00	4,407.21	357.21	8.82
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
0021-Taxes on Income other than Corporation Tax				
1988-89	3,650.00	4,241.24	591.24	16.20
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
Other Direct Taxes##				
1988-89	133.25	137.99	4.74	3.55
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

*Figures furnished by the Controller General of Accounts are provisional
 ##includes Interest Tax, Estate Duty, Wealth Tax, Gift Tax. Details are given in Appendix I.

1.3

1.3.2 The details of variation under the heads subordinate to the Major Heads 0020 and 0021 for the year 1992-93* are given below:

	Budget Estimates	Actuals (In crores of Rupees)	Increase(+) Shortfall(-)	Percentage of variation	
0020-Corporation Tax					
(i)	Income Tax on companies	7132	8222.06	1090.06	15.28
(ii)	Surtax	10	1.17	(-)8.83	(-)88.3
(iii)	Surcharge	964	354.22	(-)609.78	(-)63.25
(iv)	Receipts awaiting transfer to other minor heads	-	244.92	244.92	
(v)	Other receipts	19.00	66.87	47.87	251.94
	Total	8125.00	8889.24	764.24	9.40
0021-Taxes on Income Tax other than Corporation Tax					
(i)	Income-tax	7341.00	7476.22	135.22	1.84
(ii)	Surcharge	485.00	109.69	(-)375.31	(-)77.34
(iii)	Receipts awaiting transfer to other minor heads	--	212.27	212.27	--
(iv)	Other receipts	44.00	65.31	21.31	48.43
(v)	Deduct share of proceeds assigned to States	5868.56	6059.45	190.89	3.25
	Total	2001.44	1804.04	(-)197.40	(-)9.86

**Analysis of
collection**

1.4.1* Under the provisions of the Income Tax Act, 1961, income-tax is chargeable for any assessment year in respect of the total income of

* Figures furnished by the Ministry of Finance are provisional

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, Surtax and Interest Tax from companies and taxes on income other than Corporation Tax from non-companies, at pre-assessment and post-assessment stages, during the year 1992-93 as furnished by the Ministry of Finance is given below:

	(In crores of rupees)					
	Company				Non-company	Grand Total
	Corporation Tax	Surtax	Interest Tax	Total	Income Tax	
Tax deducted at source	2321.19	--	--	2321.19	3888.34	6209.53
Advance Tax	6171.14	--	715.53	6886.67	3030.98	9917.65
Self-assessment	1032.48	--	--	1032.48	1005.38	2037.86
Regular assessment	1437.88	--	--	1437.88	676.60	2114.48
Other receipts including surcharge	423.69	1.17	--	424.86	459.49	884.35
Total collections	11386.38	1.17	715.53	12103.08	9060.79	21163.87
Refunds	2489.04	--	--	2489.04	1165.44	3654.48
Net collections	8897.34	1.17	715.53	9614.04	7895.35	17509.39 ^a

(ii) The sub-head wise break up of total income tax collections for companies, non companies and total thereof for the years 1988-89 to 1992-93, as furnished by the Ministry of Finance, is as follows:

^a Figures of collection as furnished by the Controller General of Accounts and those furnished by the Ministry of Finance, as appearing on page 2 do not tally and are under reconciliation

Tax collection

(In crores of rupees)

Year	Tax Deducted at source	Advance Tax	Self Assess- ment	Regular Assess- ment	Other Receipts	Total Collec- tions	Refunds	Net Collection
Company								
1988-89	841.12	3,347.50	337.10	501.92	123.67	5,151.31	744.75	4,406.56
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
Non-company								
1988-89	1,862.79	2,085.00	454.60	195.02	45.69	4,643.10	404.94	4,238.16
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
Total								
1988-89	2,703.91	5,432.50	791.70	696.94	169.36	9,794.41	1,149.69	8,644.72
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

1.4.2* The details of tax collections from Government companies, Corporations (including nationalised banks) and foreign companies out of the company assesseees in sub-para '1' above, during the year 1992-93, as furnished by the Ministry of Finance are as under:

(In crores of rupees)

	Government companies and corporations	Foreign companies	Others	Total
Advance Tax	1285.06	290.81	2021.47	3597.34
Self-assessment	369.14	9.17	358.28	736.59
Regular assessment	896.62	245.58	845.94	1988.14
Surtax	23.40	---	28.13	51.53
Interest Tax	207.16	67.77	90.45	365.38
Total	2781.38	613.33	3344.27	6738.98

*Figures furnished by the Ministry of Finance are provisional

Note: Information is still awaited from Lucknow, Patna and Ranchi charges.

1.4.3(i) The details of tax deduction at source during the year 1992-93 under broad categories are as under:

	Amount (in crores of rupees)
Salaries	1561.88
Interest on securities	1606.33
Dividends	366.28
Interest	887.19
Winnings from lottery or cross word puzzles	54.38
Winnings from horse races	9.02
Payments to contractors and sub-contractors	735.57
Insurance commission	75.11
Payment to non-residents and others	913.77
Total*	6209.93

(ii)* The details of tax deducted at source, the number of statements of tax deducted at source received and the tax actually remitted to Government account for the year 1992-93: under broad categories are as under:

Income	No. of statements received	Tax deducted as per statements	Tax remitted to Govt. Account	(Rupees in crores)	
				Balance due for remittance For the year 1992-93	Upto the end of the year 1992-93
(a) Salary	1,29,559	697.13	693.90	3.22	3.22
(b) Interest	2,02,538	379.93	379.88	0.05	0.05
(c) Contractors/sub-contractors	42,010	653.41	653.39	0.01	0.01
(d) Others**	35,270	689.53	689.48	0.06	0.06
Total	4,09,377	2420.00	2416.65	3.34	3.34

* Figures furnished by the Ministry of Finance are provisional.

** includes interest on securities, dividends etc, see Appendix II.

Advance Tax

1.4.4* Tax payable and collected by way of advance-tax during the year 1992-93 is as under:

(In crores of rupees)

	Company			Total	Non-company Income Tax	Grand Total
	Corporation Tax	Surtax	Interest Tax			
1. Arrear demand	19.44	--	--	19.44	2.83	22.27
2. Current demand	1497.93	--	35.30	1533.23	1309.59	2842.82
3. Collections:						
(a) Out of arrear demand	5.21	--	--	5.21	0.36	5.57
(b) Out of current demand.	1889.68	--	44.67	1934.35	1472.77	3407.12
(c) Total	1894.89	--	44.67	1939.56	1473.13	3412.69
4. Balance demand						
(a) Arrear	14.23	--	--	14.23	2.47	16.70
(b) Current	(-)391.75	--	(-)9.37	(-)401.12	(-)163.18	(-)564.30
(c) Total	(-)377.52	--	(-)9.37	(-)386.89	(-)160.71	(-)547.60

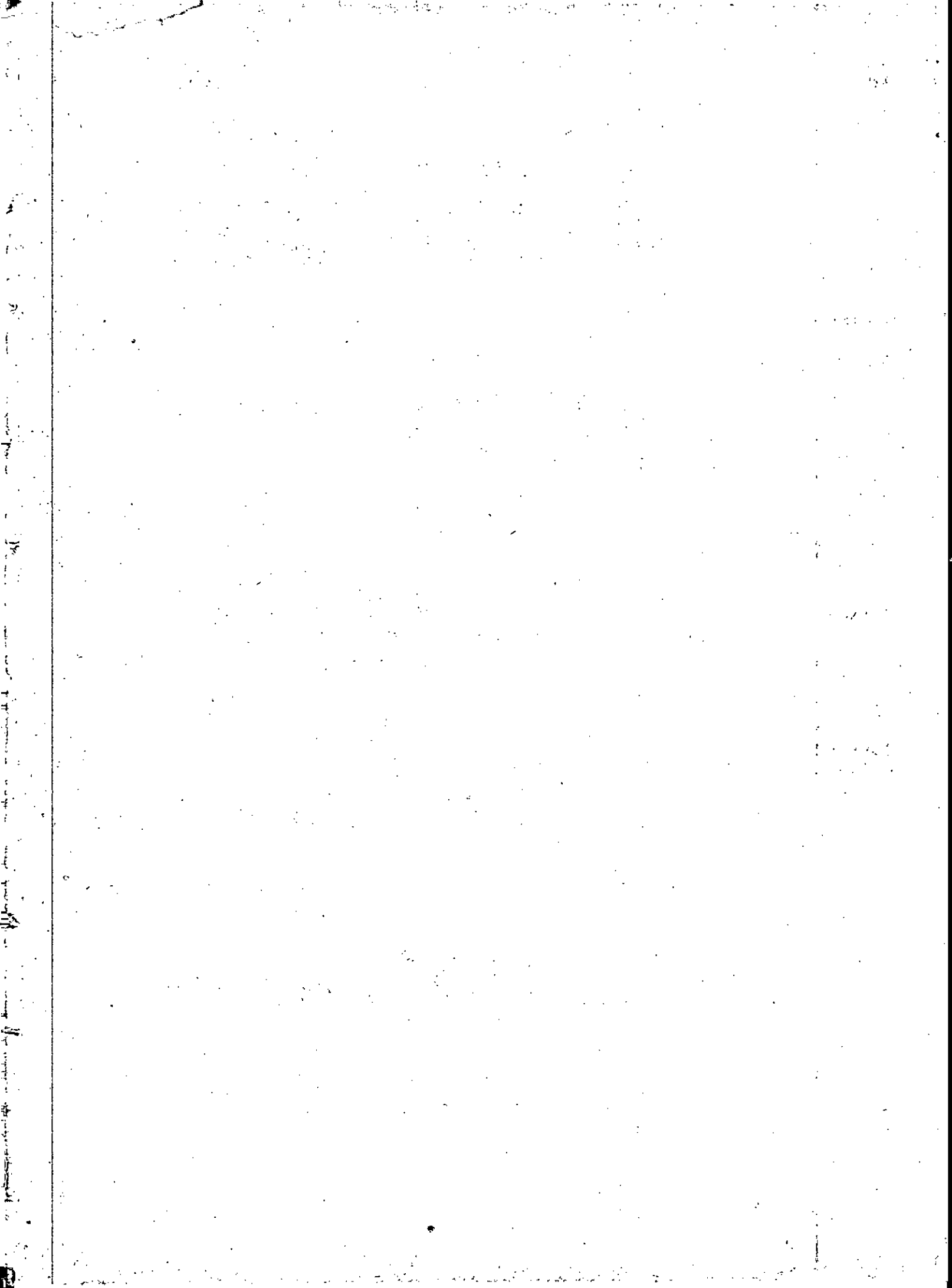
Cost of collection

1.5.1 The total expenditure incurred during the year 1992-93 and earlier three years in collecting the direct taxes are as under:

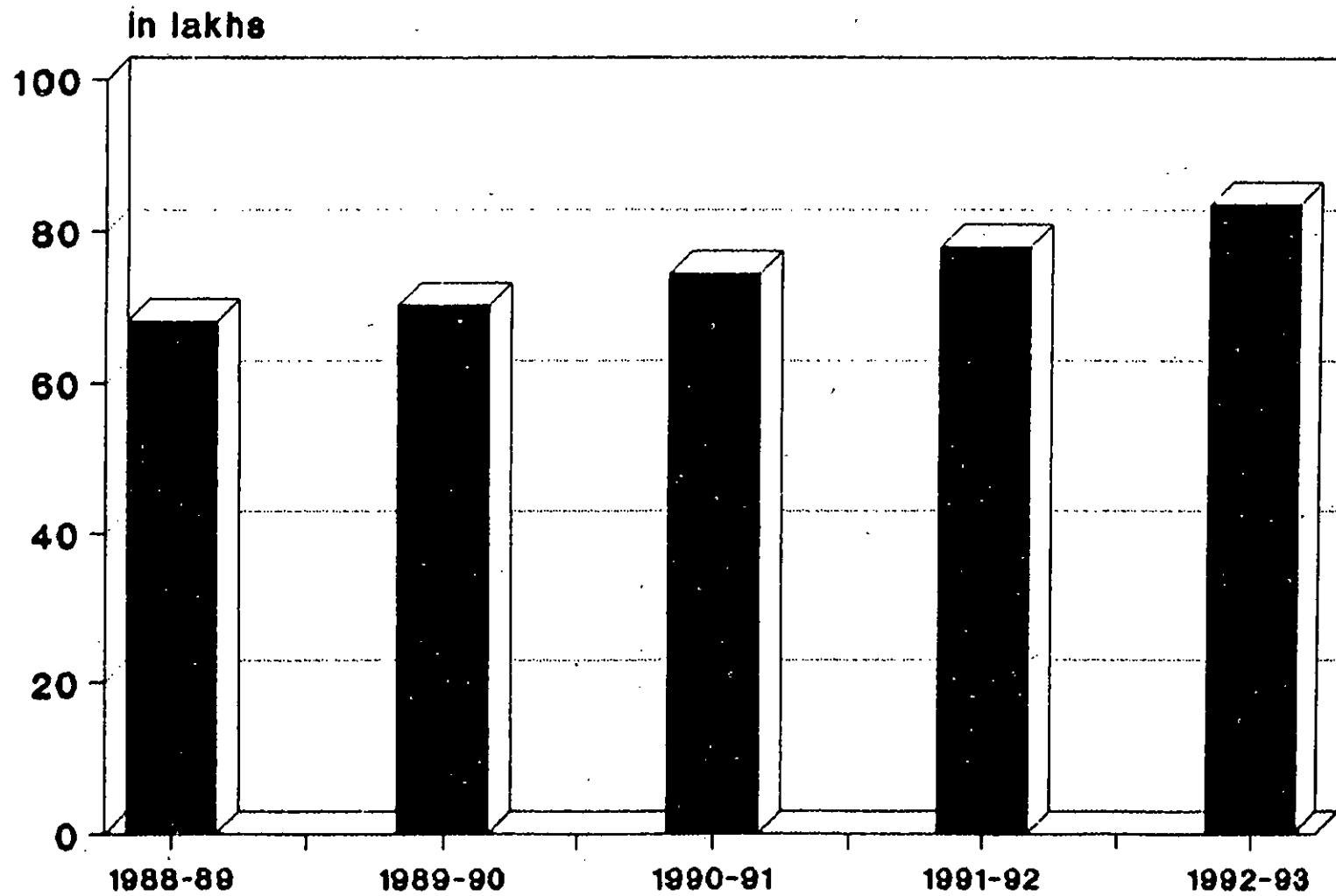
(In crores of Rupees)

Year	Collection	Expenditure	Percentage
1989-90	10,007.78	210.39	2.10
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

* Figures furnished by Ministry of Finance are provisional



Total number of Assesseees



1.5.2 The expenditure incurred during the year 1992-93 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 under:

	Collection	Expenditure on collection	Percentage
(In crores of Rupees)			
0020-Corporation Tax			
1989-90	4,728.92	25.24	0.53
1990-91	5335.27	27.62	0.52
1991-92	7867.67	30.77	0.39
1992-93*	8889.24	35.44	0.39
0021-Taxes on income etc.			
1989-90	5,008.98	164.10	3.28
1990-91	5,375.34	179.53	3.33
1991-92	6,705.80	200.02	2.98
1992-93*	7863.49	230.43	2.93
Other Direct Taxes#			
1989-90	266.42	21.05	7.90
1990-91	317.03	23.03	7.26
1991-92	767.65	25.67	3.34
1992-93*	1344.56	30.61	2.27

Number of assesses

1.6.1 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

For the assessment year 1992-93, no income-tax was payable on a total income not exceeding Rs.22,000 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 assesses in the books of the department was 83,62,738 as on 31st March 1993* as against 77,95,186 as on 31 March 1992. The break-up of the assesses on the said two dates was as under:

* Figures furnished by the Ministry of Finance are provisional

Includes interest tax, expenditure tax estate duty, wealth tax and gift tax.

For details, see Appendix III

	As on 31 March 1992	As on 31 March 1993
Individuals	58,78,404	64,34,540
Hindu undivided families	4,19,908	4,34,007
Firms	12,96,063	12,91,277
Companies	1,34,779	1,30,388
Trusts	41,049	34,816
Others	31,080	37,710
Total	77,95,186	83,62,738

(ii)* The following table indicates the break up of assesseees according to slabs of income:

Income	Individuals	Hindu undivided families	Firms	Companies	Others (including Trusts)	Total
(i) Below taxable limit	950217	76481	150295	32566	45037	1254596
(ii) Above taxable limit and upto Rs.1,00,000	5150722	332635	954603	59423	24554	6521937
(iii) Rs.1,00,001 to Rs.5,00,000	316665	23009	167910	22548	2082	532214
(iv) Above Rs.5,00,000	16936	1882	18469	15851	853	53991
Total	6434540	434007	1291277	130388	72526	8362738

Interest Tax 1.6.2 The number of assesseees for interest-tax in the books of the department as furnished by the Ministry of Finance for the last three years was as under:

Year ending	No. of assesseees
31 March 1991	44
31 March 1992	142
31 March 1993*	850

The information is provisional due to non-receipt of data from Patna, Ranchi, Lucknow.

Wealth Tax 1.6.3 Under the provisions of the Wealth Tax Act, 1957, wealth tax is levied for every assessment year on the net wealth of every

* Figures furnished by the Ministry of Finance are provisional

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 1992-93 no wealth tax was payable where the net wealth is less than Rs.2.50 lakhs.

(i) The number of wealth tax assessees in the books of the department as on 31st March 1992 and 31 March 1993 were as follows:

	As on 31 March 1992	As on 31 March 1993*
Individuals	5,91,681	5,98,011
Hindu undivided family	78,021	79,223
Companies	15,205	16,013
Others	502	197
Total	6,85,409	6,93,444

(ii)* The following table indicates the break up of assessees according to slabs of *wealth*:

	Individuals	Hindu undivided families	Companies	Others	Total
(i) Below taxable limit	78342	13181	2164	119	93806
(ii) Above taxable limit but upto Rs.5,00,000	349100	44695	10388	62	404245
(iii) Rs.5,00,001 to Rs.10,00,000	131316	16547	2321	11	150195
(iv) Rs.10,00,001 to Rs.15,00,000	25025	3221	722	1	28969
(v) Above Rs.15,00,000	14228	1579	418	4	16229
Total	598011	79223	16013	197	693444

*Figures furnished by the Ministry of Finance are provisional

Gift Tax

1.6.4 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 1992-93 no gift tax was payable where the value of taxable gifts did not exceed Rs.20,000.

The number of gift tax assessment cases for disposal for the years 1991-92 and 1992-93 were as follows:

1991-92	52,859
1992-93*	40,138

Arrears of assessment

1.7.1 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 1992 and 31 March 1993 were as under:

Nature of Posts	As on 31 March* 1992		As on 31 March 1993*	
	Sanctioned strength	Working strength	Sanctioned strength	Working strength
(a) Income Tax Officers on assessment duty	2,410	2,175	1734	1588
(b) Deputy Commissioner (Assessment)	253	253	407	425
(c) Asstt. Controllers of Estate Duty	36	28	207	192
Total	2,699	2,456	2348	2205

1.7.2 Income Tax including Corporation Tax

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

*Figures furnished by the Ministry of Finance are provisional.

Financial year	Number of assessments for disposal			Number of assessments completed			Percentage
	Scrutiny	Summary	Total	Scrutiny	Summary	Total	
1988-89	4,31,343	66,95,326	71,26,669	2,92,790	58,80,475	61,73,265	86.54
1989-90	4,44,724	64,42,103	68,84,856	2,97,543	54,01,950	56,98,310	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

Number of assessments pending at the end of the year

	Scrutiny	Summary	Total
1988-89	1,38,553 (14.53 %)	8,14,851 (85.47%)	9,53,404
1989-90	1,47,181 (12.40 %)	10,40,153 (87.60%)	11,86,546
1990-91	1,77,766 (13.86%)	11,04,436 (86.14%)	12,82,202
1991-92	2,27,679 (17.23%)	10,93,712 (82.77%)	13,21,391
1992-93*	2,23,539 (43.88)	12,26,661 (16.47)	14,50,200

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 between 12.40 per cent and 43.88 per cent during 1988-89 and 1992-93.

(ii) Status-wise break up of income tax assessments completed during the year 1991-92 and 1992-93 was as under:

	1991-92	1992-93*
(i) Individuals	51,85,928	49,90,063
(ii) Hindu undivided families	3,15,439	3,14,207
(iii) Firms	10,22,250	10,07,298
(iv) Companies	1,46,998	1,51,913
(v) Association of persons	42,799	39,462
Total	<u>67,13,414</u>	<u>65,02,943</u>

* Figures furnished by the Ministry of Finance are provisional.

(iii)* Status-wise and income range-wise break up of pendency of assessments as on 31 March 1993 was as under:

Sr. No.	Status	No. of pending assessments with income			
		Upto Rs.1,00,000	Rs.1,00,001 to Rs.5,00,000	Over Rs.5,00,000	Total
1.	Companies	34,242	18,546	20,130	72,918
2.	Firms	1,23,009	58,322	9,682	1,91,013
3.	Individuals	9,87,935	1,08,190	28,132	11,24,257
4.	Hindu undivided families	42,577	7,751	925	51,253
5.	Others	8,574	1,426	759	10,759
	Total	11,96,337	1,94,235	59,628	14,50,200

(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 1992	As on 31 March 1993
1988-89 and earlier years	11,594	5,974
1989-90	15,653	6,702
1990-91	2,33,369	29,553
1991-92	10,60,775	2,25,173
1992-93*	-----	11,82,798
Total	13,21,391	14,50,200

(v)* Status-wise and year-wise break-up of pendency of income-tax assessments as on 31st March 1993 was as under:

Status	1988-89 and earlier years	1989-90	1990-91	1991-92	1992-93	Total
(a) Company assessments						
(i) Regular	123	322	1527	18232	48452	68656
(ii) Reopened/set aside	1066	611	764	1040	2615	6096

*Figures furnished by the Ministry of Finance are provisional

(b) Non-company assessments						
(i) Regular	1034	2363	23819	202778	1125772	1355766
(ii) Reopened/ set aside	3751	3406	3443	3123	5959	19682
Total	5974	6702	29553	225173	1182798	1450200

The number of assessments pending as on 31st March 1993 was 14,50,200 as compared to 13,21,391 as on 31 March 1992 and 12,82,202 on 31 March 1991.

1.7.3 Wealth Tax, Gift Tax and Estate Duty

WEALTH TAX

(i)* The number of wealth-tax assessments completed during the year 1992-93 was as under:

Due for disposal	Number of assessments		
	Completed	Pending at the end of the year	Percentage of pendency
960692	625005	335687	35

(ii)* Status-wise break up of the wealth tax assessments completed during the years 1991-92 and 1992-93 were as under:

Status	No. of assessments completed during	
	1991-92	1992-93
(i) Individuals	6,02,885	5,43,353
(ii) Hindu undivided families	67,347	65,882
(iii) Companies	16,608	15,163
(iv) Others	318	607
Total	6,87,158	6,25,005

(iii)* Assessment year-wise position of pendency of assessments at the end of 1992-93 was as under:

Year	No. of assessments		Total
	Regular	Reopened	
1988-89 and earlier years	605	1379	1,984
1989-90	1,290	1079	2,369
1990-91	6,376	1294	7,670
1991-92	68,289	2143	70,432
1992-93	2,44,144	9,088	2,53,232
Total	3,20,704	14,983	3,35,687

* Figures furnished by Ministry of Finance are provisional

(iv)* Status-wise and wealth range-wise break up of pendency of wealth-tax assessments at the end of 1992-93 was as under:

Taxable Wealth-range	Number of pending assessments				
	Individual	HUFs	Companies	Others	Total
Up to Rs.2,50,000	40859	4995	299	16	48866
Rs.2,50,001 to Rs.5,00,000	140928	16134	3517	68	160647
Rs.5,00,001 to Rs.10,00,000	76608	9856	2101	20	88585
Rs.10,00,001 to Rs.15,00,00	19843	2197	505	31	22576
Over Rs.15,00,000	12922	1767	322	2	15013
Total	291160	34949	9441	137	335687

GIFT TAX

(v)* The number of gift tax assessments completed during the year 1992-93 was as under:

Due for disposal	Number of assessments		
	Completed	Pending at the end of the year	Percentage of pendency
40138	30170	9968	24.83

(vi)* Assessment year-wise position of pendency of assessments at the end of 1992-93 was as under:

Year	Number of assessments		Total
	Regular	Reopened	
1988-89 and earlier years.	78	23	101
1989-90	103	30	133
1990-91	377	30	407
1991-92	2400	28	2428
1992-93	6817	82	6899
Total	9775	193	9968

ESTATE DUTY

(vii)* The number of estate duty assessments completed during the year 1992-93 was as under:

* Figures furnished by the Ministry of Finance are provisional

Due for disposal	Number of assessments		Percentage of pendency
	Completed	Pending at the end of the year	
1192	614	578	48

(viii)* The number of assessments completed according to range of principal value of estate was as under:

Principal value of estate	Number of assessments completed
Up to Rs.5,00,000	452
Rs.5,00,001 to Rs.10,00,000	67
Rs.10,00,001 to Rs.15,00,000	86
Above Rs.15,00,000	9
Total	614

(ix)* Assessment year-wise position of pendency of assessments at the end of the year 1992-93 was as under:

Assessment Year	Number of assessments		Total
	Regular	Reopened/ set aside	
1988-89 and earlier years	343	166	509
1989-90	15	24	39
1990-91	18	2	20
1991-92	-	2	2
1992-93*	3	5	8
Total	379	199	578

(x)* Estate value-wise pendency of assessments at the end of the year 1992-93 was as under:

Principal value of estate	Number of assessments
Up to Rs.5,00,000	239
Rs.5,00,001 to Rs.10,00,000	252
Rs.10,00,001 to Rs.15,00,000	81
Above Rs.15,00,000	6
Total	578

SURTAX

(xi)* The number of surtax assessments completed during the year 1992-93 was as under:

* Figures furnished by the Ministry of Finance are provisional

Number of assessments

Due for disposal	Completed	Pending at the end of the year	Percentage of pendency
1648	170	1478	89.68

(xii)* Assessment year-wise position of pendency of assessments at the end of the year 1992-93 was as under:-

Assessment year	Number of assessments
1988-89 and earlier years	1174
1989-90	109
1990-91	88
1991-92	59
1992-93	48
Total	1478

INTEREST TAX (xiii)* The number of interest tax assessments completed during the year 1992-93 was as under:

Number of assessments

Due for disposal	Completed	Pending at the end of the year	Percentage of pendency
946	68	878	92.81

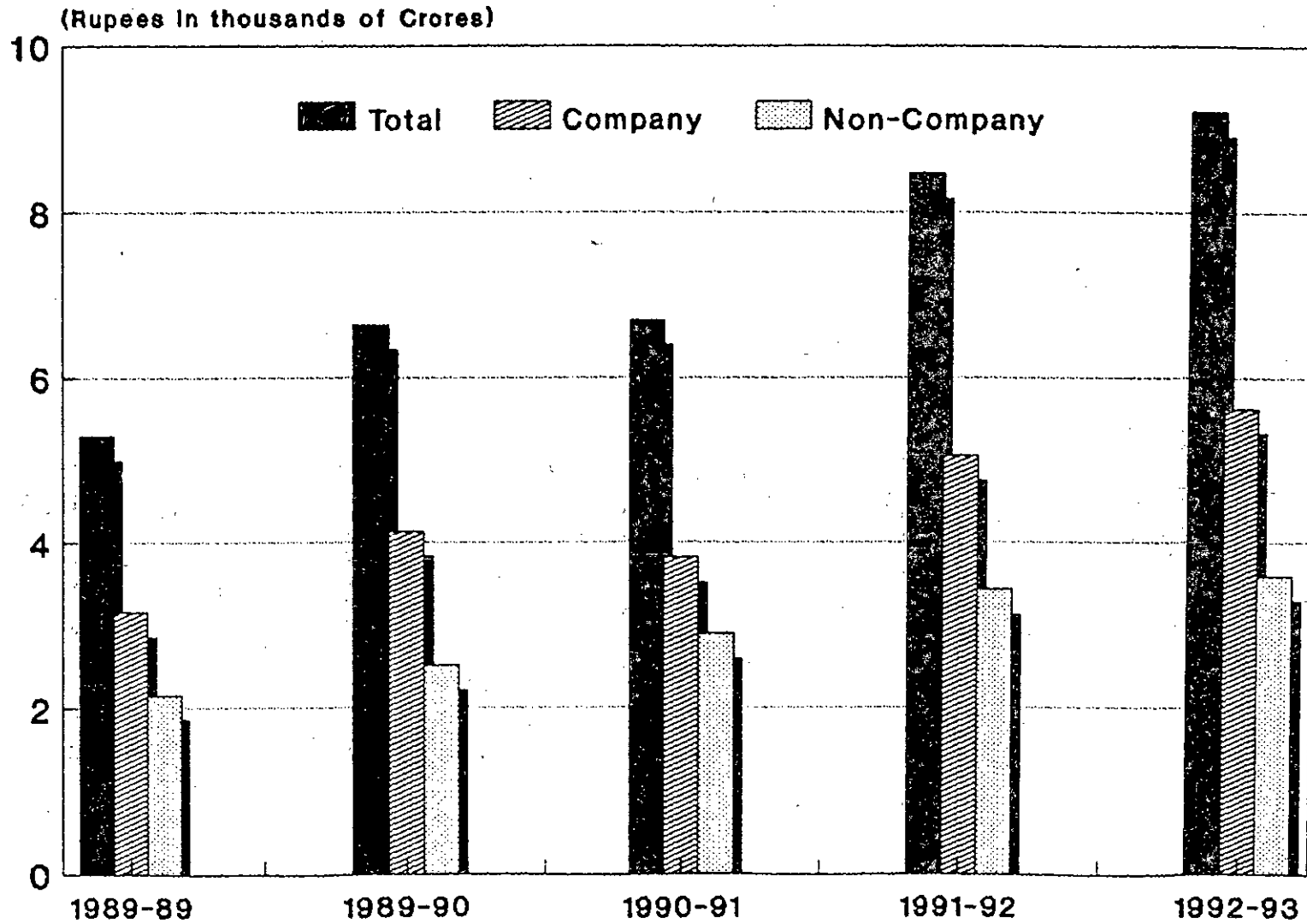
(xiv)* Assessment year-wise position of pendency of assessments at the end of the year 1992-93 was as under:

Assessment year	Number of assessments
1988-89 and earlier years	5
1989-90	12
1990-91	241
1991-92	620
1992-93	--
Total	878

Note : 1. Information is still awaited from Lucknow, Patna, Ranchi, Shillong.
2. Revised report is awaited from Kanpur.

*Figures furnished by the Ministry of Finance are provisional

DEMAND RAISED AND REMAINING UNCOLLECTED



**Arrears of
Tax Demands**

1.8.1 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 1993 was Rs.9211.00 crores, out of which arrears of Rs.5623.63 crores related to companies. The arrears included Rs.3740.03 crores in respect of which the permissible period of 30 days had not expired as on 31 March 1993, Rs.112.98 crores claimed to have been paid but remaining to be verified/adjusted, Rs.2090.12 crores stayed/kept in abeyance and Rs.183.22 crores for which instalments had been granted and instalments not fallen due.

(b)* The details of demands of Income-tax (including corporation-tax) stayed/kept in abeyance as on 31 March 1993 were as under:

(In crores of rupees)

(1)	By courts	219.95
(2)	Under Section 245(F)(2) (Application to Settlement Commission)	98.89
(3)	By Tribunals	99.96
(4)	By Income-tax authorities due to	
	(i) Appeals and revisions	751.76
	(ii) Double Income Tax claims	0.93
	(iii) Restriction of remittances Sec.220(7)	7.06
	(iv) Other reasons	911.57
	Total	2090.12

Note: Information does not include Lucknow, Ranchi, Patna and Shillong.
Revised information is still awaited from Delhi I and III, Jodhpur, Jaipur, Jalandhar, Agra, Allahabad, Ludhiana(C) and Madras(C I).

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

* Figures furnished by the Ministry of Finance are provisional

(In crores of rupees)

	Corporation Tax	Income Tax	Interest	Penalty	Total
1988-89 and earlier years	266.73	317.09	348.08	185.57	1117.47
1989-90	176.03	103.50	158.78	57.62	495.93
1990-91	174.62	182.75	252.14	95.87	705.38
1991-92	524.03	341.42	532.47	153.35	1551.27
1992-93	3058.31	1114.62	1304.03	141.53	5618.49
Total	4199.72	2059.38	2595.50	633.94	9488.54

(d)* The following table gives the break up of the gross arrears of Rs.9,488.54 crores by certain slabs of income.

	(Rupees in 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	104646	556.26	194.52	3657014	1275.55	631.33	3761660	1831.81	825.85
Over Rs.1 lakh to Rs.5 lakhs in each case	9340	225.16	114.85	23766	404.58	201.90	33106	629.74	316.75
Over Rs.5 lakhs to Rs.10 lakhs in each case	3333	218.83	100.80	4495	260.07	123.57	7828	478.90	224.37
Over Rs.10 lakhs to Rs.25 lakhs in each case	2042	388.60	141.65	2428	392.45	150.67	4470	781.05	292.32
Over Rs.25 lakhs in each case	1915	4309.27	1223.11	1449	1457.77	306.74	3364	5767.04	1529.85
Total	121276	5698.12	1774.93	3689152	3790.42	1414.21	3810428	9488.54	3189.14

Note: 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.

(e) Further details of classification of tax in arrears (Gross) are given in Appendix IV.

* Figures furnished by the Ministry of Finance are provisional.

(ii)* The amounts of interest tax in arrears and the year-wise break up thereof are given below:-

	No. of cases	Amount (In crores of rupees)
1988-89 and earlier years	82	23.36
1989-90	02	0.52
1990-91	--	--
1991-92	39	67.81
1992-93	55	4.06
Total	178	95.75

(iii)* The following table gives the year-wise arrears of demands outstanding and the number of cases relating thereto under the three other Direct Taxes, i.e., Wealth Tax, Gift Tax and Estate Duty as on 31st March 1993.

	(Amounts in crores of rupees)					
	Wealth Tax		Gift Tax		Estate Duty	
	Number	Amount	Number	Amount	Number	Amount
1988-89 and earlier years	98139	99.81	25365	7.44	14367	13.58
1989-90	25927	29.44	5230	2.24	397	1.80
1990-91	39534	43.99	5675	2.68	244	0.57
1991-92	49583	69.03	5472	3.49	57	0.45
1992-93	100516	67.33	11784	10.25	265	2.99
Total	313699	309.60	53526	26.11	19330	19.39

1.8.2 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 Tax Recovery Officer 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, the

* Figures furnished by the Ministry of Finance are provisional

Tax Recovery Officer 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 1992-93 was as follows:

Particulars	Sanctioned strength	Working strength
Tax Recovery Officers	178	175

(ii)* The tax demands certified to the Tax Recovery Officers and the progress of recovery to end of 1992-93 are given in the following table:

(In crores of rupees)

	Demand certified			Demand recovered during the year	Balance at the end of the year
	At the beginning of the year	During the year	Total		
1988-89	710.21	484.12	1194.33	287.78	906.55
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

(iii)* Year-wise break - up of certificates pending on 31 March 1993 and amount of demand:

* Figures furnished by the Ministry of Finance are provisional

Year of receipt of recovery certificates	No. of certificates	Amount involved (In crores of rupees)
1988-89	929852	348.85
1989-90	109566	88.54
1990-91	42813	92.54
1991-92	32839	246.13
1992-93	94746	301.15
Total	1209816	1077.21

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

Range of demand	(In crores of rupees)					
	Corporation Tax		Income Tax		Wealth Tax	
	No.	Amount	No.	Amount	No.	Amount
(a) Upto Rs.10,000	236011	74.23	664837	65.27	129206	20.26
(b) Over Rs.10,000 and below Rs.1,00,000	65939	82.30	43055	60.63	13846	24.90
(c) Over Rs.1 lakh	13600	361.00	7304	331.51	2356	40.56
Total	315550	517.53	715196	457.41	145408	85.72

Range of demand	Gift Tax		Estate Duty		Interest Tax		Total	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount
(a) Upto Rs.10,000	24475	2.59	7068	4.17	208	0.07	10618805	166.59
(b) Over Rs.10,000 and below Rs. 1 lakh	1048	1.15	514	0.30	114	0.22	124516	169.50
(c) Over Rs.1 lakh	84	5.14	18	1.33	133	1.58	23495	741.12
Total	25607	8.88	7600	5.80	455	1.87	1209816	1077.21

(v)* Year-wise disposal and pendency of attached property.

Year	(No. of properties)							
	Opening balance		Additions		Disposals		Closing balance	
	Movable	Immovable	Movable	Immovable	Movable	Immovable	Movable	Immovable
1988-89	2562	3455	808	1180	536	227	2834	4408
1989-90	2834	4408	693	763	1199	999	2328	4172
1990-91	2328	4172	1452	1057	1008	1635	2772	3594
1991-92	2772	3594	822	578	324	346	3270	3826
1992-93	3270	3826	880	476	894	190	3256	4112

*Figures furnished by the Ministry of Finance are provisional

1.8.3 Year-wise details of attached properties awaiting disposal at the end of 1992-93 as furnished by the Ministry of Finance were as under:

Year	Number of cases		(In crores of rupees)				Appointment of Receiver for management of properties	
			Total					
	Movable	Immovable	No.	Amount	No.	Amount	No.	Amount
1988-89	1095	20.25	1300	59.65	2395	79.90	1	0.01
1989-90	89	1.57	513	17.25	602	18.82	-	--
1990-91	547	9.21	792	41.90	1339	51.11	-	--
1991-92	545	54.94	624	87.61	1169	142.55	3	16.73
1992-93*	980	43.53	883	111.49	1863	155.02	158	11.81
Total	3256	129.50	4112	317.90	7368	447.40	162	28.55

Note:1) Does not include information from Patna, Ranchi and Lucknow
2) Closing balance and opening balance do not agree and are under verification.

Appeals, Revision Petitions and Writs

1.9 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 and revision petitions pending as on 31 March 1993 were as under:

(i) No. of income tax appeals pending with
(a) Appellate Assistant Commissioner
[Since redesignated as Deputy Commissioner
(Appeals)]

82802

865

*Figures furnished by the Ministry of Finance are provisional

(b) Commissioner of Income Tax (Appeals)	139564
(ii) No. of income tax revision petitions pending	9618
Total	2,31,984

(b)(i)* Year-wise details of appeals pending with Deputy Commissioner (Appeals) for the five years ending 1988-89 to 1992-93 were as under:

Financial year	Opening balance	Additions during the year	Disposals during the year	Closing balance
1988-89 and earlier years	84947	55814	59189	81572
1989-90	81645	59243	47188	93700
1990-91	97989	78609	64002	112596
1991-92	115634	60764	66655	109743
1992-93*	101108	40973	59279	82802

(ii)* Year-wise break up of high demand (more than Rs.1 lakh) appeals pending with Deputy Commissioner (Appeals) at the end of the year 1992-93 with reference to their year of institution was as under:

Year of institution	Number pending
1988-89 and earlier years	146
1989-90	245
1990-91	255
1991-92	1142
1992-93	2131
Total	3919

(c)(i)* Year-wise details of appeals pending with Commissioners of Income Tax (Appeals) for the five years ending 1988-89 to 1992-93 were as under:

Financial year	Opening balance	Additions during the year	Disposals during the year	Closing balance
1988-89	95708	68218	70301	93625
1989-90	92744	78578	71001	100321
1990-91	98922	83114	74663	107373
1991-92	107373	104633	75300	136706
1992-93*	136785	84534	81755	139564

* Figures furnished by the Ministry of Finance are provisional

(ii)* Year-wise break up of high demand (more than Rs.1 lakh) appeals pending with Commissioners of Income Tax (Appeals) at the end of the year 1992-93 with reference to their year of institution was as under:

Year of institution	Number pending
1988-89 and earlier years	888
1989-90	1770
1990-91	4850
1991-92	18079
1992-93*	11308
Total	36895

(d)(i) Particulars of revision petitions for the five years ending 1988-89 to 1992-93 were as under:

Financial year	Opening balance	Additions during the year	Disposal during the year	Closing balance
1988-89	14,219	7,766	7,465	14,520
1989-90	14,486	5,606	5,335	14,957
1990-91	14,959	4,851	7,819	11,991
1991-92	12,341	7,061	7,980	11,422
1992-93*	11,422	5,768	7,572	9,618@

(ii)* Year-wise break up of revision petitions pending at the end of the year 1992-93 with reference to their year of institution was as under:

Year of institution	Number pending
1988-89 and earlier years	2293
1989-90	973
1990-91	1222
1991-92	1730
1992-93*	3710
Total	9928@

(2) Other Direct Taxes

(a)* Particulars of Wealth Tax, Gift Tax and Estate duty appeals and revision petitions pending as on 31 March 1993 were as under:

@ Figures under reconciliation by the Ministry of Finance

* Figures furnished by Ministry of Finance are provisional

(d) * Year-wise pendency of revision petition with Commissioners:

Year of filing of petition	Number pending
1988-89 and earlier years	1,094
1989-90	382
1990-91	357
1991-92	571
1992-93	1,308
Total	3,712

(e) * Writ petitions pending:

	In Supreme Court	In High Court	Total
(i) On 31 March 1993	581	6740	7321
(ii) Out of (i) above			
Pending for:			
Over 5 years	133	2173	2306
3 to 5 years	166	1201	1367
1 to 3 years	261	2644	2905
Upto 1 year	21	722	743
Total	581	6740	7321

(f) * Cases pending with Courts of Law:

	In Supreme Court	In High Court	Total
(i) On 31 March 1993	5175	32647	37822
(ii) Out of (i) above			
Pending for:			
Over 5 years	1917	8841	10758
3 to 5 years	664	9160	9824
1 to 3 years	1065	10839	11904
Upto 1 year	1529	3807	5336
Total	5175	32647	37822

Reliefs and refunds

1.10 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).

(i) (a) The particulars of cases of direct refunds on which claims were made during 1988-89 to 1992-93 were as under:

Financial year	Opening Balance	Claims received during the year	Total	No. of refunds	Balance outstanding
1988-89	12,047	97,151	1,09,198	92,642	16,556
1989-90	16,556	81,547	98,103	73,494	24,609
1990-91	24,609	72,314	96,923	81,274	15,649
1991-92	15,649	97,486	1,13,135	96,470	16,665
1992-93*	16,665	90,402	1,07,067	91,249	15,818

(b)* Year-wise analysis of the outstanding direct refunds claims as on 31 March 1993.

Financial year in which application was made	No. of cases pending
1990-91 and earlier years	415
1991-92	1038
1992-93	14365
Total	15818

(ii) (a) The Act also provides for refund of any amount which may become due to an assessee as a result of any order passed in appeal or other proceedings without his having to make any claim on that behalf. Simple interest at the prescribed rate is payable to the assessee in such cases too.

Cases resulting in refund as a result of appellate orders and revision orders etc., during each of the five years ending 1992-93 were as under:

Financial year	Opening Balance	Additions	Disposal	Balance
1988-89	1,130	18,745	18,987	888
1989-90	888	20,046	19,673	1,261
1990-91	1,261	16,954	17,760	455
1991-92	455	17,459	17,655	259
1992-93*	259	16,366	16,046	579

(b)* Year-wise analysis of balance as on 31 March 1993 was as under:

Financial year	No. of cases pending*
1990-91 and earlier years	23
1991-92	01
1992-93	555
Total	579

* Figures furnished by the Ministry of Finance are provisional

Interest

1.11 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.

The particulars of interest paid on refunds by Government under the different provisions of the Act during the years 1990-91, 1991-92 and 1992-93 are given below:

(Amount in crores of rupees)

Section of Income Tax Act under which interest paid	1990-91		1991-92		1992-93*	
	No. of assess-ments	Amount	No. of assess-ments	Amount	No. of assess-ments	Amount
214	40211	17.06	22163	33.97	20092	6.97
243	466	0.27	279	0.47	1193	0.97
244	251306	77.25	308700	114.49	524509	134.07

Note: Information is still awaited from Lucknow, Patna, Ranchi and Shillong charges.

Cases settled by Settlement Commission

1.12 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	No. of cases pending
1988-89	1,897	243	12.81	1,654
1989-90	1,993	355	17.81	1,638
1990-91	2,000	480	24.00	1,520
1991-92	2,014	457	22.69	1,557
1992-93*	2,115	342	16.17	1,773

* Figures furnished by the Ministry of Finance are provisional.

1.12-1.13

(ii) Wealth Tax

Financial year	No. of cases for disposal	No. of cases disposed of	Percentage	No. of cases pending
1988-89	590	97	16.44	493
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

(iii)* No. of cases pending for admission before Settlement Commission as on 31.3.1993 865

(iv)* No. of cases held up with Settlement Commission for want of comments of the department. 131

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

Penalties and prosecutions 1.13 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 provide for levy of penalty and prosecution for failure to produce accounts and documents, failure to deduct or pay tax, etc.

Income Tax and Corporation Tax (i) (a) Penalty proceedings initiated, disposed of and pending for each of the three years ending 1992-93 were as under:

Year	Opening balance	Additions	Total	Disposals	Closing balance
1990-91	2,74,237	1,23,265	3,97,502	2,04,905	1,92,597
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

(b) Prosecutions launched, convictions/ compoundings and cases pending in the Courts for the three years ending 1992-93 were as under:

Year	Pending at the beginning of the year	Complaints filed during the year	Total	Convicted	No. of cases disposed			Total pending
					Compo- unded	Acqui- tted	Total	
1990-91	14,047	1,887	15,934	1,058	398	87	1,543	14,391
1991-92	14,391	1,541	15,932	180	131	61	372	15,560
1992-93*	15,560	789	16,349	175	366	306	847	15,502

* Figures furnished by the Ministry of Finance are provisional

(c) Penalty and composition money levied, collected and pending for the three years 1989-90 to 1992-93 were as under:

(Amount in crores of rupees)

Year	Opening Balance		Levied during the year		Collected during the year		Balance outstanding	
	Penalty	Composition money	Penalty	Composition money	Penalty	Composition money	Penalty	Composition money
1990-91	208.26	2.29	150.73	9.45	61.62	7.36	297.37	4.38
1991-92	297.37	4.38	94.60	17.09	67.77	15.49	324.20	5.98
1992-93*	324.20	5.98	109.22	2.06	44.27	1.66	389.15	6.38

Other Direct Taxes (ii) (a) Penalty proceedings initiated, disposed of and pending for each of the three years ending 1992-93 are given below:

Year	Opening balance	Additions	Disposals	Closing balance
1990-91	56,288	27,168	34,427	49,029
1991-92	49,029	16,735	21,328	44,436
1992-93*	44,436	10,842	15,173	40,105

(b) Prosecutions launched, convictions/compoundings and cases pending in the Courts of Law for the three years ending 1992-93 are given below:

Year	Pending at the beginning of the year	Complaints filed during the year	Total	Number of cases disposed of			Cases pending	
				Convicted	Compounded	Acquitted		
1990-91	725	12	737	60	1	37	98	639
1991-92	639	110	749	14	12	8	34	715
1992-93*	715	253	968	4	7	9	20	948

(c) Penalty and composition money levied, collected and pending for the three years 1990-91 to 1992-93 are given below:

Year	Opening balance		Levied during the year		Collected during the year		Balance outstanding	
	Penalty	Composition money	Penalty	Composition money	Penalty	Composition money	Penalty	Composition money
1990-91	15.61	0.08	8.66	0.001	6.47	0.004	17.81	0.08
1991-92	17.81	0.08	5.14	0.006	8.22	0.001	14.72	0.09
1992-93*	14.72	0.09	4.16	0.006	2.09	0.014	16.79	0.08

* Figures furnished by the Ministry of Finance are provisional

Searches and Seizures

1.14 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 1990-91 to 1992-93 was as under:

Year	No. of cases where cash jewellery etc., assets were seized		No. of cases where no assets were seized
	No.	Value	
	(in crores of rupees)		
1990-91	1,922	626.59	1,545
1991-92	1,631	238.90	696
1992-93*	4,252	983.87	472

(ii)(a) Particulars of orders under Section 132(5) passed during the three years ending 1992-93 were as under:

Year	Opening balance of cases	Search cases during the year	Total	No. of cases where orders were passed during the year	No. of cases pending at the end of the year
1990-91	932	2,195	3,127	2,243	884

*Figures furnished by the Ministry of Finance are provisional.

					1.14
1991-92	884	1,356	2,240	1,455	785
1992-93*	785	1,960	2,745	2,016	729

(b) Particulars of income determined in the orders under Section 132(5), tax involved therein, assets retained and assets returned over the three years ending 1992-93 were as under:

Year	No. of cases where orders were passed	Income determined in the orders	Tax involved therein	Value of assets retained	Value of assets returned
(Amount in crores of Rupees)					
1990-91	2,330	275.80	257.27	97.21	14.19
1991-92	1,299	329.63	238.96	63.62	12.98
1992-93*	1,964	590.67	564.86	262.97	36.84

(iii) (a) The number of search cases out of (ii) (b) where final assessments were completed and pending for the three years ending 1992-93 was as under:

Year	Opening balance of orders U/s 132(5)	Order U/s 132(5) passed during the year	Total	No. of cases where final assessments were completed			Cases where assessments are pending
				Where concealed income was found	With No concealed income	Total	
1990-91	2,602	2,368	4,970	1,502	1,013	2,515	2,455
1991-92	2,455	1,625	4,080	1,067	618	1,685	2,395
1992-93*	2,395	1,950	4,345	1,177	533	1,710	2,635

(b) Year-wise particulars of pendency of orders under Section 132(5) where final assessments were pending as on 31 March 1993 were as under:

Year in which summary assessments were made	No. of cases where final assessments were pending	Out of (2) no. of cases with Settlement Commission
1.	2.	3.
1990-91	1,499	50
1991-92	1,410	55
1992-93*	2,250	207

(c) Particulars of income determined, tax levied, balance-tax outstanding after adjustment of value of assets retained on final assessment for the three years ending 1992-93 were as under:

* Figures furnished by the Ministry of Finance are provisional

1.14-1.15

Year	No. of cases where final assessments were completed	Income determined	(Rupees in Crores)						
			Demand raised			Demand adjusted out of retained assets	Balance pending recovery		
			Tax	Penalty	Total		Tax	Penalty	Total
1990-91	4,956	2,612.83	1424.49	62.25	1,486.74	586.00	840.87	59.87	900.74
1991-92	3,751	3,674.29	2,077.29	261.94	2,339.24	366.47	1,712.61	260.14	1,972.76
1992-93*	3,412	623.94	289.79	12.97	302.76	191.63	98.61	12.51	111.12

(d) The number of cases of prosecutions launched, compounded and convictions obtained for the three years ending 1992-93 was 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			
1990-91	16,822	1,607	18,429	1,392	1,561	17,037
1991-92	17,037	725	17,762	154	67	17,608
1992-93*	17,608	319	17,927	118	472	17,809

(e) Particulars of cases of assets returned, interest paid and cases pending for three years ending 1992-93 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			
1990-91	483	1,140	1,623	180	-	1,443
1991-92	1,443	392	1,835	1,098	-	737
1992-93*	737	178	915	145	3	770

Note: Information is still awaited from Patna, Ranchi, Orissa and Shillong. Revised information is still awaited from Agra and Delhi (C)I.

Survey

1.15(i) Number of cases where the powers of survey (other than those relating to ostentatious expenditure) were exercised for the three years ending 1992-93 as below.

Year	No. of premises surveyed
1990-91	4,500
1991-92	2,930
1992-93*	4,798

* Figures furnished by the Ministry of Finance are provisional

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

Year	No. of cases
1990-91	426
1991-92	320
1992-93*	293

Note: Excluding charges of CCIT/CIT Lucknow, Patna, Ranchi, Shillong, Calcutta (C)I and II.

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

1.16 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 from 1 October 1987, 1 June 1989 and 1st April 1991.

During the financial year ended in March 1993 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	78	522	171	349	2348	3468
(ii) No. of properties purchased	13	7	4	8	46	78
(iii) Value of properties purchased (Rs. in lakhs)	253.52	505.48	106.56	262.04	3102.35	4229.95
(iv) No. of properties where consideration exceeds Rs.50 lakhs	1	4	-	1	21	27

*Figures furnished by the Ministry of Finance are provisional

**Functioning
of Valuation
Cells**

1.17 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
1988-89	71	13
1989-90	70	13
1990-91	70	13
1991-92	70	13
1992-93	70	13

(ii) No. of cases referred to valuation cells, disposed of and pending at the end of the each of three years ending 1992-93

	Year	Opening balance	No. of cases referred during the year	Disposals	Closing balance
(a) Income Tax	1990-91	959	7,551	7,552	958
	1991-92	958	8,426	8,445	939
	1992-93*	939	7,918	7,774	1,083
(b) Other Direct Taxes#	1990-91	3,098	7,440	8,713	1,825
	1991-92	1,825	5,713	6,152	1,386
	1992-93*	1,386	4,067	4,517	936

Revenue demands written off by the department

1.18* A demand of Rs.1173.52 lakhs in 71,625 cases was written off by the department during the year 1992-93. Details are given below category-wise:

includes Wealth tax, gift tax and Estate Duty, Details are in Appendix VI

* Figures furnished by the Ministry of Finance are provisional

		(Amount in lakhs of Rupees)					
		Company		Non-company		Total	
		No.	Amount	No.	Amount	No.	Amount
1. Income Tax							
I.	(a) Assesseees who have no assets or have become insolvent	28	3.44	331	2.06	359	5.50
	(b) Assesseees who have gone into liquidation or are defunct	6	1.38	2	0.06	8	1.44
	Total	34	4.82	333	2.12	367	6.94
II.	Assesseees being untraceable	39	0.19	7,883	54.88	7,922	55.07
III.	Assesseees having left India	-	-	72	30.00	72	30.00
IV.	Other reasons:						
	(a) Assesseees having no attachable assets	75	0.71	6,183	736.13	6,258	736.84
	(b) Amount being small, etc.	1	0.40	51,036	285.62	51,037	286.02
	(c) Amount written off as a result of scaling down of demand	-	-	4,413	47.19	4,413	47.19
	Total	76	1.11	61,632	1,068.94	61,708	1,070.05
V.	Amount written off on grounds of equity or as a matter of international courtesy or where time, labour and expenses involved in legal remedies for realisation are considered disproportionate to the amount of recovery.	-	-	1,556	11.46	1,556	11.46
	Grand Total	149	6.12	71,476	1,167.40	71,625	1,173.52

Note: Information not received in respect of Lucknow, Patna, Ranchi and Shillong charges.

Results of Test Audit in general

1.19 As a result of test audit conducted between 1 April 1992 to 31 March 1993 of the assessments completed by the Income Tax Department 13,916 cases of under-assessment involving a total revenue effect of Rs 3490.62 crores 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, 12,375 cases involving a tax effect of Rs.3470.66 crores were referred to the department. Of these cases, major audit observations were raised in 6,711 cases involving short levy of tax of Rs. 3455.33 crores. The remaining 5,644 cases accounted for underassessment of tax of Rs.15.33 crores.

The underassessment of tax of Rs.3,470.66 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	907	14.71
2. Failure to observe the provisions of the Finance Acts	728	110.19
3. Incorrect status adopted in assessments	136	1.20
4. Incorrect computation of income	146	0.64
5. Incorrect computation of income from house property	135	4.67
6. Incorrect computation of business income	2,638	296.04
7. Irregularities in allowing depreciation, investment allowance and development rebate	1,300	173.61
8. Irregular computation of capital gains	250	4.31
9. Mistakes in assessments of firms and partners	667	9.74
10. Income not assessed	1,291	2,415.29
11. Irregular set off of losses	348	41.08
12. Irregular exemptions and excess reliefs given	990	314.37
13. Non-levy/incorrect levy of interest for delay in submission of returns, delay in payment of tax etc.	1,256	31.56
14. Avoidable or incorrect payment of interest by Government	104	7.19
15. Omission/short levy of penalty	408	4.49
16. Other topics of interest (Miscellaneous)	1,071	41.57
Total	12,375	3,470.66

(ii) Wealth Tax

During test-audit of assessments made under Wealth Tax Act, 1957, 1,308 cases, involving short levy of Rs.11.74 crores were referred to the department.

The mistakes can be categorised under the following heads:

	No. of cases	Amount (in crores of rupees)
1. Wealth not assessed	312	6.14
2. Incorrect valuation of assets	282	1.53
3. Mistakes in computation of net wealth	165	0.71

4. Incorrect status adopted in assessments	77	0.18
5. Irregular/excessive allowances and exemption	116	0.31
6. Mistakes in calculation of tax	93	0.40
7. Non-levy or incorrect levy of additional wealth-tax	21	0.36
8. Non-levy or incorrect levy of penalty and non-levy of interest	151	0.56
9. Miscellaneous	91	1.55
Total	<u>1,308</u>	<u>11.74</u>

(iii) Gift Tax

During the test audit of gift-tax assessments, 233 cases involving short levy of Rs.8.21 crores, were referred to the department.

**Outstanding
audit
observations**

1.20 Assessments completed by the Income Tax department are subjected to audit by the Department's own Internal Audit and test checked by the Indian Audit and Accounts Department (Statutory Audit) under the direction of Comptroller and Auditor General of India. While the former conducts 100 percent audit of all immediate cases (as defined under departmental instructions of September 1990), the audit by I.A. & A.D. is carried out through test checks designed to verify the adequacy and efficiency of systems and procedures. According to the departmental instructions, observations of Internal Audit Department are to be attended to by the assessing officers within three months, whereas those of statutory audit are to be replied to within a period of six weeks.

During 1992-93, the total number of observations made by the Internal Audit Department was 12,815 with money value of Rs.252.11 crores, while those made by statutory audit were 13916 with money value of Rs.3490.61 crores.

On 31 March 1993, 1,07,135 audit observations made by both the Internal Audit and Statutory Audit, were pending settlement. Of these, 11,303 major cases (each with tax effect of Rs.10,000 and above relating to Income tax and Rs.1,000 and above under other direct taxes) accounted for Rs.467.81 crores and 21,811 other observations involving revenue effect of Rs.5.78 crores had been made by the Internal Audit. The remaining 74,021 cases relate to statutory audit and involve Rs.2,809.58 crores.

(i) Internal Audit

As per 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 1989-93 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)
1.	2.	3.	4.	5.
1989-90	18,578 (479.25)	8,907 (156.39)	48 (33)	9,671 (322.86)
1990-91	20,698 (1017.36)	10,044 (318.25)	49 (31)	10,650 (699.11)
1991-92	18,625 (936.61)	7,159 (570.50)	38 (63)	11,466 (366.11)
1992-93	18,053 (614.59)	6,750 (146.78)	37 (24)	11,303 (467.82)

Agewise analysis of the pending items at the end of 1992-93 and revenue effect involved are given below:

Year of the observation	No. of cases	Revenue effect (in crores of rupees)
1988-89 and earlier years	124	3.99
1989-90	1260	37.89
1990-91	1648	62.45
1991-92	2695	174.99
1992-93	5576	188.50
Total	11303	467.82

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 1989-90 and earlier years should have been settled by March 1993, which is not the case as shown above.

(ii) Statutory Audit

(a) On 31 March 1993, 74,021 observations involving a revenue of Rs.2,809.58 crores, were pending for final action. The year-wise particulars of the pendency are as follows:

Year	Income Tax		Other Direct Taxes (Wealth Tax, Gift Tax and Estate Duty)		Total	
	Items	Revenue effect (In crores of rupees)	Items	Revenue effect (In crores of rupees)	Items	Revenue effect (In crores of rupees)
Up to 1989-90 and earlier years	43,125	925.77	8,545	44.70	51,670	970.47
1990-91	9,630	717.06	1,223	10.27	10,853	727.33
1991-92	10,269	1101.35	1,229	10.43	11,498	1,111.78
Total	63,024	2,744.18	10,997	65.40	74,021	2,809.58

(b) There were 1881 pending audit observations (as against 1529 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	22	395.97
2.	Assam	32	1560.41
3.	Bihar	32	9540.51
4.	Delhi	273	54,555.49
5.	Gujarat	99	3,776.78

1.19

6.	Haryana	6	78.10
7.	Himachal Pradesh	1	18.04
8.	Karnataka	41	3,970.98
9.	Kerala	27	771.51
10.	Madhya Pradesh	167	19,216.27
11.	Maharashtra	559	75,536.94
12.	Orissa	16	772.31
13.	Punjab	12	320.40
14.	Rajasthan	15	874.71
15.	Tamil nadu	173	8,334.43
16.	Uttar Pradesh	44	9,175.05
17.	West Bengal	362	26,360.67
	Total	1,881	2,15,208.57

(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.	Delhi	7	80.69
2.	Gujarat	9	136.88
3.	Karnataka	3	21.32
4.	Madhya Pradesh	12	678.33
5.	Maharashtra	6	89.25
6.	Punjab	2	19.13
7.	Tamil Nadu	16	324.55
8.	West Bengal	10	159.77
	Total	65	1509.92

(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	4	121.25
2.	Assam	1	7.99
3.	Delhi	3	88.60
4.	Gujarat	12	212.98
5.	Haryana	1	32.98
6.	Karnataka	1	27.64
7.	Kerala	1	21.39
8.	Madhya Pradesh	1	7.05
9.	Maharashtra	8	449.73
10.	Orissa	1	184.97
11.	Tamil Nadu	13	343.91
12.	West Bengal	5	151.78
	Total	51	1650.27

(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.	Rajasthan	3	10.64
5.	Tamil Nadu	2	24.18
6.	West Bengal	2	11.30
	Total	16	770.63

Of 74,021 pending cases with revenue effect of Rs.2,809.58 crores, 1,969 cases (2.53 percent) accounted for Rs.2,099.65 crores (71.92 per cent). This underlines the need to assign priority to the settlement of observations with high money value.

(iii) Steps taken to settle audit observations

The Action Plan of the department for 1992-93 provided for 100 percent disposal of all pending major audit observations. In respect of current observations of statutory audit upto 31 December 1992 (i.e. period of reporting being 1992-93), replies are to be sent in 80 percent of the cases while the target fixed for major internal audit observations is 50 per cent.

(a) According to information furnished by the department in September 1993 relating to internal audit observations and Quarterly Reviews of Internal Audit and Statutory Audit major observations of the Directorate of Income Tax (Income Tax and Audit), for the quarter ending March 1993, the targets according to Action Plan and actual achievement in settlement of the major internal and statutory audit observations for the year 1992-93 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		Percentage of pendency
				cases	Percentage	
	1.	2.	3	4.	5.	6.
A. Internal Audit Observations						
Current	7,962 (229.52)	3,981 (50%)	2,386 (41.01)	1,595	40.06	70.03
Arrear	10,091 (385.07)	10,091 (100%)	4,364 (105.76)	5,727	56.75	56.75
B. Receipt Audit Observations						
Current	8,468 (15,024.35)	6,774 (80%)	3,720 (1,404.36)	3,054	45.08	56.07
Arrear	24,349 (1668.17)	24,349 (100%)	16,855 (1219.31)	7,494	30.77	30.77

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

(b) Remedial action barred by time

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 1992-93, a number of cases where remedial action became barred by limitation was noticed. The number noticed as a result of review of such cases and the tax effect involved in selected charges are as under :

Charge	Income Tax	
	Number of observations	Tax effect (in lakhs of rupees)
Haryana	50	11.41
Maharashtra	1890	103.56

(iv) Follow up on Audit Reports

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 were laid on the table of the House duly vetted by Audit. Such notes were required to be submitted even for paragraphs which were not selected by the Public Accounts Committee for detailed examination.

A review of the Audit Reports for the years 1989-90 to 1991-92 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
1989-90	698	60
1990-91	457	71
1991-92	362	40

(v) Non receipt of Board's comments on draft paragraphs

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 communicating their responses 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 3 Audit Reports:

Year of Report	<u>Number of draft paragraphs</u>		Replies received before finalisation of Audit Report	Percentage in which replies were received
	Issued	Period of issue		
1990-91	1,319	January-July 1991	535	40.56
1991-92	1,022	March-July 1992	136	13.30
1992-93	889	March-August 1993	629	70.75

Chapter 2

System Appraisal

2.1 Functioning of Investigation Circles

Introductory

2.1.1 Various measures including, inter-alia, conferring of powers of survey, search and seizure on the Income Tax authorities, have been introduced by the department, from time to time, to curb economic offences and combat tax evasion.

The efficacy of the measures to unearth black money and check evasion of taxes has been commented upon by various expert committees, as well as, the Public Accounts Committee. Measures such as, the voluntary disclosure schemes to combat tax evasion have not found favour with these committees. The Wanchoo Committee in their report on Black Money (December 1971) had strongly opposed the idea of introduction of any general scheme of disclosure of concealed income either now or in the future. A study conducted by the National Institute of Public Finance and Policy, in March 1985, had brought out that these schemes did not blunt the underlying causes of black money generation. All that they did was to provide a temporary fillip to revenue collections. The Public Accounts Committee in their 17th Report (1967-68) had also concluded that these schemes (1951 and 1965 schemes) had not achieved their objectives and recommended suitable drastic measures to tone up the Direct Taxes Administration. The Public Accounts Committee in their 123rd Report (1978-79) had again expressed their dismay that the problem of black money had not been tackled effectively and recommended that the Government should take suitable drastic measures to tone up the direct taxes administration. It is in this background, that the relevance of such extraordinary powers, like search and seizure, can be appreciated.

Organisa- tional set up

2.1.2 Search and seizure operations are conducted by the Investigation wing of the Income Tax department. This wing is entrusted with the responsibility of planning and executing search operations throughout the

country. For this purpose, there are ten regional Directorates of Investigation, whose work is monitored by five Directors General of Income Tax (Investigation). The assessment work is, however, assigned to the Investigation circles under the administrative control of the respective Commissioners of Income Tax. After the reorganisation of the Income Tax department in April 1988, the work of assessment of all search and seizure cases was transferred to Investigation circles headed by Assistant Commissioners, except those cases which are assigned to Central circles or to Deputy Commissioners of Income Tax (Assessment).

Law and Procedure

2.1.3. The powers of search and seizure under the Income Tax Act are vested in various Income Tax authorities. Sections 132 and 132A of the Act read with Rules 112, 112A, 112B, 112C and 112D of the Income Tax Rules prescribe the procedure for authorising and conducting a search, making seizures and dealing with the seized assets. Similar powers under the Wealth Tax Act, 1957, are conferred by section 37A and 37B read with Rules 10 and 10A of the Wealth Tax Rules.

Section 132 of Income Tax Act was intended to achieve two limited objectives:

(i) to get hold of evidence bearing on the tax liability of a person, which the said person is seeking to withhold from the assessing authority, and

(ii) to get hold of assets representing income believed to be undisclosed income and applying so much of them, as may be necessary, in discharge of the existing and anticipated tax liability of the person concerned.

The work of the assessing officer begins with the receipt of the appraisal report from the Investigation wing, alongwith the seized material. In all search and seizure operations undertaken by the Investigation wing, an appraisal report is required to be prepared, containing, interalia, details of seizure of assets, surrender made under section 132(4) of the Income Tax Act, outcome of the search, and it indicates the prosecution and concealment potential of the case, based on preliminary scrutiny of the seized

documents. This is sent to the assessing officer within one month (45 days from July 1991) of the date of search. The seized material is also to be handed over to the assessing officer within the specified time limit.

The assessing officer first passes an order under Section 132(5) of the Act in cases where any money, bullion, jewellery or other valuables are seized, estimating undisclosed income/wealth in a summary manner, after affording an opportunity to the person concerned for being heard, and calculates the amount of tax, determines the amount of interest payable and penalty imposable on the person, with the previous approval of the Deputy Commissioner of Income Tax. The assessing officer can retain in his custody such assets as would be sufficient to satisfy the aggregate amount of taxes, interest and penalties stated in the order, and is required to release the remaining assets, if any. After passing orders under Section 132(5), action for completion of regular assessment is taken up.

**Scope of
Audit Review**

2.1.4 This review seeks to evaluate the post-search performance of the department, particularly the working of the Investigation circles, and analyse the efficacy of the existing system. The audit observations incorporated in the subsequent paragraphs are based on the findings from test check of the records of 7,960 cases in 165 Investigation circles, functioning in 75 Commissioners charges in various parts of the country.

Constraints

2.1.5 The review was conducted in spite of extreme reluctance on the part of departmental authorities at various levels, to produce relevant records especially the appraisal reports, even after the Board has issued instructions in April, 1991 for making available all records, including appraisal reports. These instructions of the Board were later modified (March 1993) resulting in withholding of appraisal reports from Audit. The appraisal reports were to be examined with a view to ascertaining whether Board's instructions of July 1991, requiring recording of reasons for variations in assessment orders and findings in the appraisal reports were followed. Some instances, in which the appraisal reports were produced and where there were

substantial differences in the concealed income estimated therein and the assessments for which reasons were not recorded though required under the instructions of the Board, have been commented upon in paragraph 2.1.13 of this review.

Highlights

2.1.6(a) With a view to collecting evidence in respect of tax evasion and to withhold assets for early liquidation of tax liability, Income Tax Law empowers the department to undertake searches and to seize unaccounted assets like cash, jewellery etc. The task is undertaken by the Investigation wing of the department which prepares an appraisal report after search and forwards it to the Investigation Circles where search assessments are made. The department had been reluctant to produce complete records in many of the charges. In Tamil Nadu (some circles and some Commissioners of Income Tax), Uttar Pradesh and Kerala charges, the investigation circles refused to supply records and statistical information, especially the appraisal reports in Tamil Nadu and Uttar Pradesh charges. As availability of records is the prime necessity for conducting a review on a selected topic, the department's reluctance to produce the entire record hampered efforts to make a comprehensive appraisal of the entire scheme.

(b) An evaluation of available data on searches and seizures, including the statistics furnished by the Ministry of Finance for the years 1988-89 to 1992-93 revealed the following:-

(i) Out of a total number of 16,509 search cases during the five year period 1988-89 to 1992-93, orders under section 132(5) were passed in only 11,358* cases. The fate of the remaining 5,151 cases was not known.

(ii) The concealed income detected and assessed in 11,225* cases where interim orders were passed, worked out to Rs.1687.75 crores. There was no corresponding data on the income sustained in appeals.

(iii) Out of the total of 10,348 cases where final assessments were completed during the five-year period, 6,636 assessments (64.12 percent) were completed indicating some

*Variation in the figures to be reconciled by the Ministry

concealed income and in the rest of the 3,712 cases (35.88 per cent) no concealed income was detected or established.

(c) The Income Tax Act, provides for prosecution for certain defaults such as wilful attempt to evade tax, false statement in verification etc. As per statistical information furnished by 53 Commissioners' charges, prosecution proceedings were initiated in 173 cases as against 6,462 cases assigned to investigation circles during 1988-89 to 1992-93. Such a low number of prosecutions launched is a pointer to the fact that even after considering incriminating material in search cases, the department could not establish many cases of tax evasion.

(d) For completion of regular assessments in search and seizure cases, the department proposed Action Plan for each financial year, setting out the 'Key Result Areas' and targets. In the Action Plan for the year 1992-93, an annual target of disposal of a minimum of 50 core assessments was fixed and included as a Key Result Area. Similarly, targets were fixed for the years 1989-90 to 1991-92. The statistics furnished by the department revealed that in 14 charges completion of regular assessments of search and seizure cases was not receiving due attention in the Investigation circles, created with up-graded charges.

(e) A test check by Audit of the regular assessments has pointed out delays occurring at every stage of assessment. In cases where incriminating material or assets are seized, the departmental authorities are required to re-open the relevant assessment. In 161 assessments there were delays ranging from one month to 61 months in issue of notice for re-opening the assessments. In 69 cases test checked in seven charges, regular assessments were not completed and in 25 cases in 2 charges even assessment proceedings did not commenced within the two year period prescribed by executive instructions. In 364 cases, delay in completion of regular assessments ranged from 17 days to 5 years beyond the prescribed period of 2 years from the date of search in ten charges.

(f) One of the objectives for setting up the Investigation circles was to improve the quality of search assessments and ensure

quick follow-up action. A review of regular assessments revealed the following:-

(i) In 42 assessments, mistakes/omissions were noticed which resulted in non-assessment/underassessment of income/wealth of Rs.3.34 crores with consequent non/short levy of tax of Rs.1.05 crores.

(ii) There were large scale variations in the income estimated in orders passed under section 132(5)/appraisal reports and income finally assessed. Against an income of Rs. 13.54 crores determined initially in 15 cases, income of Rs.93.02 lakhs only was determined in the regular assessments. Further as against tax of Rs.2.82 crores initially determined in 35 cases, the amount finally determined was only Rs.42.00 lakhs. Similarly, the income shown in appraisal reports at Rs.806.90 lakhs in 25 cases was finally assessed at Rs.86.40 lakhs.

(iii) Even in cases where demands were raised, recovery was not being vigorously pursued. In West Bengal charge alone, tax of Rs.36.56 crores and penalty of Rs.3.04 crores was pending collection in case of assessments completed during the years 1988-89 to 1991-92.

(g) One of the measures of ascertaining the quality of assessments in Investigation circles was the success rate in appellate proceedings. The statistics furnished by 58 Commissioner's charges revealed that out of tax of Rs.467.47 crores determined in 2985 interim orders passed under section 132(5), tax of Rs.125.95 crores (26.94 percent) only, including interest and penalty was finally determined after appeal effect in regular assessments completed during the years 1988-89 to 1992-93. A test check in Madhya Pradesh and Tamil Nadu charges revealed that in 28 cases, out of assessed tax demand of Rs.14.59 crores raised in interim orders and regular assessments, in appeal, tax demand of Rs.6.15 crores (42.15 per cent), was deleted and tax demand of Rs.6.90 crores (47.31 per cent) was set aside. Similarly, in Madhya Pradesh, Karnataka, Chandigarh and Haryana charges, against income of Rs.448.41 lakhs estimated/assessed in 24 cases, amount of Rs.125.76 lakhs was deleted and Rs.256 lakhs was set aside in appeal.

(h) The registers and reports which were the

basis for monitoring of the functioning of the investigation circles, were either not maintained or improperly maintained. As these are important tools for close monitoring, this area requires special attention and care.

**Non-
production
of records/
information**

2.1.7 Besides the appraisal reports, in several charges, other records and statistical information was also not produced to Audit. For instance, in Andhra Pradesh, Gujarat, Chandigarh and Uttar Pradesh, no information was given regarding the number of cases assigned to Investigation Circles, number of cases in which interim orders were passed and cases in which regular assessments were framed thereafter. In Delhi (except one Commissioner of Income Tax) and Kerala charges, no information was furnished regarding monitoring of search assessments at various supervisory levels. In Rajasthan, Delhi (except one CIT) and Gujarat charges, information regarding achievement of Action Plan targets was not furnished. Similarly, in Delhi charge, the prescribed registers for search and seizure cases were not made available for audit scrutiny.

**Statistical
data**

2.1.8. The following statistical information furnished by the Ministry indicates various facets of 'search' and 'post search' functioning of the departmental machinery, for the years 1988-89 to 1992-93:

(i) The following are the particulars of the total number of cases where orders under section 132(5) were passed together with the tax involved:

Year	Opening balance of search cases	Searches during the year	Total	Number of cases where interim orders were passed during the year (percentage)	Number of cases pending at the end of each year (percentage)	Income determined in the orders passed (in crores of rupees)	Tax involved
1988-89	1,390	3,321	4,711	2,927 (62.13)	1,784 (37.87)	244.92	245.52
1989-90	1,786	1,900	3,686	2,717 (73.71)	969 (26.29)	246.71	225.31
1990-91	932	2,195	3,127	2,243 (71.73)	884 (28.27)	275.80	257.28

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1991-92	884	1,356	2,240	1,455 (64.95)	785 (35.05)	329.64	238.96
1992-93*	785	1,960	2,745	2,016 (73.44)	729 (26.56)	590.68	564.87
Total		10,732	16,509	11,358	5,151	1,687.75	1,531.94

Thus the pendency of assessments at the end of the respective years ranged from 26.29 to 37.87 per cent of the total number of cases to be assessed during that year.

(ii) Separate statistics furnished by the Ministry indicate that in the five years from 1988-89 to 1992-93*, out of a total of 10,348 search cases where final assessments were completed, in 3,712 cases (35.87 per cent), no concealed income was detected.

(iii) Out of 10,732 searches conducted between the period 1988-89 and 1992-93, the number of prosecutions launched, cases compounded and the number in which convictions were obtained for these five years, is mentioned below:

Year	Number of prosecutions launched			Number of cases compounded	Number in which convictions were obtained	Number of cases pending	Percentage of pending cases
	Opening balance	During the year	Total				
1988-89	9,062	4,447	13,509	262	52	13,247	98.06
1989-90	12,883	4,421	17,304	214	19	17,090	98.76
1990-91	16,822	1,607	18,429	1,392	1561	17,037	92.44
1991-92	17,037	725	17,762	154	67	17,608	99.13
1992-93*	17,608	319	17,927	118	472	17,809	99.34

(iv) According to information furnished to audit by 53 Commissioners' charges, 6,462 cases were assigned to Investigation Circles. Of these, prosecution proceedings were launched in 173 cases only during 1988-89 to 1992-93. Information in respect of remaining charges was not made available (December 1993).

* Provisional.

Non-achievement of Action Plan targets especially with regard to completion of regular assessments in search cases

2.1.9(a) Consequent on re-organisation of the department from 1 April 1988, the Investigation Circles were to be manned by senior officers for speedy and quality disposal of search and seizure assessments. Towards this end, the department proposed Action Plan for each financial year setting out 'Key Result Areas' and targets. In the Action Plan for the year 1992-93, an annual target of a minimum of 50 core assessments was fixed and included in the Key Result Area. Core assessment means assessment of the year to which seized material relates. Similarly, targets were fixed for the earlier years from 1988-89 to 1991-92. According to the Departmental statistics furnished the statement below indicates the targets, achievements and shortfalls of various charges in the country@.

Year	Targets Prescribed	Targets to be achieved	Achievements	Shortfalls
		(Number of assessments)		
1988-89	75 percent of the assessments to be completed by 31 March 1989, out of those brought forward as on 1 April 1988 which will get time barred after 1 April 1989 but on or before 31 March 1990.	6834	3923	2911
1989-90	Disposal of minimum 50 core assessments per annum per Asstt. Commissioner subject to the following: 1. Disposal of 100 percent assessments relating to searches conducted upto 31 March 1988. 2. Pendency to be carried forward as on 1 April 1990 should not be more than the pendency as on 1 April 1989.	8104	4991	3113
1990-91	Disposal of minimum 50 core assessments per annum per Asstt. Commissioner subject to the following:- 1. Disposal of 100 per cent assessments relating to searches conducted upto 31 March 1989.	6081	3735	2346

@except Rajasthan, Gujarat, and Delhi charges wherefrom information was not available. Information received from Karnataka was not furnished in the prescribed form.

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2. Pendency to be carried forward as on 1 April 1991 should be less than the pendency as on 1 April 1990.

1991-92 Disposal of minimum 50 core assessments per annum per Asstt. Commissioner subject to the following:-

6116	3811	2305
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1. Disposal of 100 per cent assessments relating to searches conducted upto 31 March 1990.
2. Pendency to be carried forward as on 1.4.1992 should be less than the pendency as on 1 April 1991.

1992-93

1. Minimum 50 core assessments.	2589	1487	1102
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2. 100 per cent disposal of assessments relating to searches conducted upto 31 March 1991 to be achieved by 31 December 1992.

A test check in Tamil Nadu, Madhya Pradesh, Bombay, Calcutta, Kerala and Orissa charges revealed that the completion of regular assessments of search and seizure cases was not receiving due attention in the Investigation circles, created with upgraded charges. Consequently, the desired objective underlying the formation of the circles, could hardly be achieved. The deficiencies noticed in achievement of various targets of Action Plan, are discussed in the succeeding paragraphs:-

(b) According to successive Action Plans, pending assessments at the end of the year, which are to be carried forward to the next year, should be less than those pending at the beginning of the year.

In Tamil Nadu charge, a test check of 4 Investigation circles under two Commissioners of Income Tax revealed non-achievement of these targets as illustrated below:-

CIT charge	Year	<u>No. of assessments pending completion</u>	
		At the beginning of the year	At the end of the year
A.	1988-89	8	16
	1989-90	16	29
	1990-91	29	38
B.	1991-92	158	206
	1992-93	206	289

(c) (1) Action Plan targets have also laid down that after a search is carried out the relevant assessment should be completed within two years. Thus for searches made up to 31 March 1990, assessment are required to be made up to 31 March 1992. A test check revealed that :

(i) In Calcutta charge, in 10 Investigation circles, the targeted disposal of 50 search and seizure assessment cases was not achieved by 5 circles and 7 circles could not attain the targeted disposal of the pending cases, for the years 1988-89 to 1992-93. The extent of shortfall noticed ranged from 4 per cent to 100 per cent. However, in most of the cases, the percentage ranged from 21 to 71.

(ii) In Bombay charge, the number of assessment cases which were more than 2 years old were 664 as on 31 March 1989, 2,484 as on 31 March 1991 and 2,098 as on 31 March 1992.

(2) Apart from Action Plan targets, the Board also issued instructions in July 1991, stressing the need to expedite disposal of search and seizure cases, and completion of search assessments within two years from the date of search.

In 12 charges test checked, audit scrutiny revealed that, in 69 cases, regular assessments had not been completed and in 25 cases assessments were not commenced within the prescribed period. In 364 cases, where these assessments were completed, there was delay in completion beyond the prescribed period of 2 years ranging from 17 days to 5 years.

Sl. No.	Charge	No. of cases where delay occurred beyond prescribed period	Period of delay (in days)	No. of cases where <u>assessments not</u> completed	commenced (Period of delay)
1.	Andhra Pradesh	38	17 to 1720	--	--
2.	Tamil Nadu	160	90 to 2070	04	--
3.	Karnataka	24	60 to 540	17	--
4.	Orissa	5	111 to 436	---	---
5.	Punjab	6	90 to 390	--	--

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6.	Assam	23	210 to 1050	19	20 (14 to 740 days)
7.	Madhya Pradesh	---	---	6	5 (2 years 5 months)
8.	West Bengal	43	76 to 315	11	--
9.	Delhi	18	150 to 1440	---	---
10.	Chandigarh(UT)	40	270 to 1470	---	---
11.	Kerala	7	60 to 720	5	--
12.	Rajasthan	---	---	7	--
	Total	<u>364</u>		<u>69</u>	<u>25</u>

(d) Action Plan targets also stipulated 100 per cent disposal of cases relating to the years 1989-90 to 1991-92, which were more than two years old.

A test check revealed that in Kerala charge the targets fixed for 100 per cent disposal of search and seizure cases for the year 1991-92 could not be achieved in 4 Investigation circles. In 2 Investigation circles under a Commissioner's charge, only 30 per cent targets could be achieved whereas in two other circles only 65 per cent and 70 per cent targets could be achieved.

Infirmities noticed in passing orders under section 132(5) of the Income Tax Act, 1961.

2.1.10 In cases of search and seizure, where any money, bullion, jewellery or other valuable article or thing has been seized, the assessing officer must make an estimate of the undisclosed income in a summary manner and pass an order under section 132(5), within 120 days of the date of seizure.

Test check revealed that in Maharashtra, Tamil Nadu, Andhra Pradesh and Gujarat charges, in 27 cases, there were delays ranging between 3 days to 870 days in passing such an order. Further, in 13 such orders passed, mistakes and infirmities, like under-estimation of income, omission to consider concealed incomes, non-imposition of penalty, interest etc. were noticed. Two cases of West Bengal charge are mentioned below, by way of illustrations:

(i) In a case, where search was made on 31 December 1991, the assessing officer, in his interim order passed on 20 May 1992, estimated Rs.14.32 lakhs as the concealed income and worked out tax liability of Rs.31.08 lakhs (including penalty). The Commissioner of Income Tax, in his orders dated 1 June 1992, held that the valuables seized should be returned to the assessee as the interim order passed suffered from legal infirmities and the notice issued in this connection, was also defective.

(ii) In another case, the assessee disclosed Rs.50 lakhs as concealed income, consequent on search operations. In the order passed under section 132(5), the assessing officer held that as the assessee did not pay any tax on the said disclosure, immunity from penalty was not available to him. However, while framing the order, he omitted to levy the penalty of Rs.26.03 lakhs.

Delay in re-opening of assessments after search and seizure operations.

2.1.11 Under the Income Tax Act, 1961, whenever a search is conducted in the premises of an assessee and incriminating assets are seized, the assessee is treated as one who had concealed income/wealth. Consequently, notices are issued for re-opening completed assessments. Executive instructions require such notices to be issued within six months from the date of search.

A test check in Tamil Nadu, Bihar, Karnataka, Assam, Delhi, Andhra Pradesh, Haryana and Orissa charges revealed that in 161 regular assessment cases, delay in issue of such notices ranged between one month to 61 months as shown in the statement below, leading to consequential delay in finalisation of the assessment proceedings:

Sl.No.	Charge	No.of assessments where delays were noticed	Period of delay
1.	Tamil Nadu	86	One month to 4 years
2.	Bihar	1	2 years
3.	Karnataka	12	2 months to over one year
4.	Assam	22	21 months to 42 months

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5.	Delhi	3	22 months to 43 months
6.	Andhra Pradesh	2	25 months and 49 months
7.	Haryana	9	35 months to 61 months
8.	Chandigarh(UT)	14	28 months
9.	Orissa	12	4 years 7 months
	Total	161	

Mistakes/ omissions resulting in under assessment of income and tax noticed in regular assessments

2.1.12 The order passed under section 132(5) is of an interim nature and as such, while finalising the regular assessment, the assessing officer is expected to make complete investigations and frame an assessment which can stand appellate scrutiny. In the Action Plans formulated by the Board, the objective of improving the quality of search and seizure assessments has been repeatedly stressed. However, many of these assessments continue to be made in a perfunctory manner.

In 42 cases test-checked in 12 charges, mistakes/omissions were noticed which resulted in non-assessment/underassessment of income/wealth of Rs.3.34 crores, with consequent non/short levy of tax of Rs.1.05 crores. In addition, avoidable payment of interest of Rs.20.59 lakhs was also noticed in one case.

A few cases are mentioned below, to illustrate the nature of these omissions:

Maharashtra Charge

(i) While completing the regular assessment of a firm for the assessment year 1990-91 in March 1993, the assessing officer determined that the assessee firm received 'unaccounted money' which was not spent on the project and not included in the books of accounts. However, he made an aggregate addition of Rs.44.08 lakhs to 'work in progress' and only 15 per cent over this amount i.e. Rs.6.61 lakhs was brought to tax. As the entire amount of unexplained money was required to be taxed in terms of section 69A of the Income Tax Act, 1961, the action of the assessing officer was not correct resulting in under-assessment of income of Rs.44.08

lakhs with consequent short levy of tax of Rs.29.06 lakhs.

Bihar Charge

(ii) In a search case, an assessee was found to have taxable net wealth for assessment years 1983-84 to 1989-90, but no wealth tax proceedings were initiated by the Department. The omission resulted in wealth of Rs.152 lakhs escaping wealth tax of Rs.2.35 lakhs (including interest).

Gujarat Charge

(iii) In the case of a private limited company, the return of income for assessment year 1989-90, was filed in March 1992. It was mentioned in the note attached with the computation of income filed along with the return that the return did not include the income of the assessee company disclosed during the search operation on 29 March 1989. The Director of the company declared, under section 132(4), an amount of Rs.33 lakhs as unaccounted income of the company. However, it was seen during the course of scrutiny of the assessment records of the assessee that the assessment had not been completed for the assessment year 1989-90, though the regular assessment for subsequent year 1990-91 was done on 10 March 1993. The time limit for completion of assessment for the assessment year 1989-90 expired on 31 March 1992 according to the provisions of the Income Tax Act, 1961. The assessment has thus become time barred and the undisclosed income of Rs.33 lakhs escaped assessment involving short levy of tax of Rs.19.05 lakhs.

Variations between the concealed income/wealth as mentioned in appraisal reports and as assessed in orders passed under Section 132(5) and thereafter in regular assessments

2.1.13 The Central Board of Direct Taxes issued instructions in July 1991 that the reasons for any variation between regular assessment order and appraisal reports as well as interim orders are required to be clearly recorded in regular assessment orders. During the course of audit it was noticed that in several cases there were substantial variations between income and tax determined in regular assessments and that worked out in appraisal reports and orders passed under Section 132(5).

In Maharashtra, Delhi, Gujarat, Tamil Nadu, Karnataka, Rajasthan, Haryana, Kerala, West Bengal, Assam, Punjab, Orissa and Andhra Pradesh charges, test check revealed that

against income of Rs.13.54 crores in 15 cases and tax of Rs.2.82 crores in 35 cases estimated in interim orders passed, the income and tax were determined at Rs.93.02 lakhs and Rs.42.00 lakhs respectively in the regular assessments. Similarly, against the income of Rs.806.90 lakhs estimated in appraisal reports in 25 cases, only Rs.86.40 lakhs was determined in regular assessments. No reasons were, however, assigned/recorded for variations for not considering/partly considering the income/tax in the completed regular assessments. Such abnormally large variations between the basic records such as appraisal reports and interim orders passed and regular assessments would imply that either highpitched estimates were made in appraisal reports and orders passed under Section 132 (5) or the regular assessments were highly defective.

A few illustrative cases are mentioned below:

Gujarat charge

(i) In the case of a group of assesseees, the group floated 3 investment companies. The total share capital of these companies was Rs.1.50 crores. The appraisal report mentioned that the public issue of share capital of Rs.1.50 crores by the three companies floated by the group, was benami and fictitious. According to the appraisal report in the cases of most of the shareholders, cash was first deposited in their accounts and subsequently the cheques were issued. Immediately after the search, statements of some of the shareholders were recorded. These persons filed an affidavit stating that they had not invested in the shares of the said companies. The amount was given to them by one of the members of this group. It was suggested in the appraisal report that the share-holding of the persons who filed an affidavit should be called for from the Registrar of companies and amount of such holdings was required to be added as unexplained investment to the total income of the person who gave them the money for investment. However, the assessing officer did not take any action in this regard and thus the potential tax liability on the benami and bogus investment of Rs.1.50 crores was not included in the assessable income.

Punjab Charge

(ii) During a search conducted (July 1990) at the business and residential premises of two assesseees, the investigation officers found evidence of undisclosed income of Rs.130 lakhs including cash, gold jewellery and substantial investment in house property. This was indicated in the appraisal report. In the regular assessments for the assessment years 1989-90 to 1991-92 completed during February 1991 to March 1992, the total income of the two assesseees was assessed at Rs.13.19 lakhs only. Thus undisclosed income amounting to Rs.116.81 lakhs remained unassessed resulting in loss of revenue of Rs.163.69 lakhs (including interest and penalty).

Kerala Charge

(iii) A search was conducted at the business premises of an individual assessee in September 1989. In interim order passed in January 1990, concealed income of Rs.20.18 lakhs was estimated for assessment years 1985-86 to 1989-90. However, in regular assessments for these years, income of Rs.2.90 lakhs only was assessed in the assessments completed in March 1991.

Department has stated that all the points in the appraisal report and order under section 132(5), have been examined while completing regular assessments. This was not borne out by the facts as per assessment records, obviously, either the assessment under section 143(3) or the order under section 132(5) was incorrect.

Defective assessments made in search and seizure cases which did not stand the test of appeal

2.1.14 One measure of determining the effectiveness of search and seizure operations is the establishment of the fact of concealed income and to see whether additions made on this score, stand the test of appeal. Cases were noticed where orders passed under section 132(5) were wholly or substantially deleted at subsequent stages. As per statistics furnished by 58 Commissioners charges, out of tax of Rs.467.47 crores demanded in 2985 interim orders passed under Section 132(5), tax of Rs.125.95 crores (26.94 per cent) only including interest and penalty was finally demanded, after appeal effect, in regular assessments completed during the years 1988-89 to 1992-93. Test check in Madhya Pradesh

and Tamil Nadu charges, revealed that out of 487 cases reviewed, in 28 cases, against the tax demand of Rs.1458.61 lakhs in orders passed under regular assessments, tax demand of Rs.614.82 lakhs (42.15 per cent) was deleted and tax demand of Rs.690.09 lakhs (47.31 per cent) was set aside in appeals. Similarly, in Madhya Pradesh, Karnataka, Chandigarh and Haryana charges, against income of Rs.448.41 lakhs estimated/assessed in 24 cases, amount of Rs.125.76 lakhs was deleted and Rs.256 lakhs was set aside in appeal. While deleting the additions, it was held by appellate authorities that either the seizure was fully and properly explained by the assessee or sufficient opportunity was not given by the assessing officers to them to explain discrepancies in accounts. Defects in framing the assessments were also pointed out.

Illustrative cases of this kind are mentioned below:

Madhya Pradesh Charge

(i) In the case of an assessee, as a result of search operations in August 1989, income for two assessment years 1987-88 and 1988-89 was assessed exparte as under:

Assessment year	Income assessed	Date of assessment
1987-88	Rs.31.70 lakhs	28 March 1990
1988-89	Rs.15.20 lakhs	27 March 1992

On assessee's appeal, the assessment for the assessment year 1987-88 was set aside by Income Tax Appellate Tribunal in May 1992 on the ground of denial of reasonable opportunity of being heard to the assessee. Assessment for assessment year 1988-89 was set aside by the Commissioner of Income Tax (Appeal) in July 1992, rejecting the contention of the assessing officer that non-attendance on the day of hearing, which was a Sunday, constituted non-compliance by the assessee. Thus in these two assessments, demand could not be raised, and these were still pending (January 1993). According to the appraisal report (August 1989) concealment was also noticed in respect of assessment year 1986-87. However, the assessing officer did not re-open the assessment for this year and thus concealed income for this year remained to be assessed.

Tamil Nadu Charge

(ii) Similarly, a review of 78 cases revealed that in 17 cases, the assessments were fully/partially knocked down at the appellate stage. Tax and interest amounting to Rs.873.92 lakhs levied by the department was reduced to Rs.153.70 lakhs in appeal, indicating that the assessments made in these cases were not carefully made. In one such case, a search was conducted in June 1988. The assessing officer completed exparte assessments for assessment years 1984-85 to 1988-89 in March 1991. In appeal, all these assessments involving tax and interest of Rs.128.40 lakhs, were completely set aside by Commissioner of Income Tax (Appeal) in February 1992 with the remarks that the assessments were done in a hurried manner.

Non-levy and short levy of penalty

2.1.15(a) Non-levy and short levy of penalty for concealment of income

Under the Income Tax Act, 1961, penalty is leviable where, in the course of a search, the assessee is found to be the owner of any unexplained or undisclosed money, bullion, jewellery or other valuable article or thing.

In Assam, West Bengal, Delhi and Tamil Nadu charges, in 9 cases test checked, penalty of Rs.30.24 lakhs leviable for concealment of income, was not levied/short levied on concealed income of Rs.55.40 lakhs (in two cases of Assam charge, amount not quantified).

(b) Penalty proceedings dropped without approval of Deputy Commissioner of Income Tax.

The Central Board of Direct Taxes issued instructions in July 1991 that where penalty for concealment of income under section 271(1)(c) is not initiated or is to be dropped after its initiation, it will be done only with the approval of Deputy Commissioner of Income Tax.

In 7 cases (Tamil Nadu charge) and in one case (West Bengal charge), penalty proceedings initiated for the assessment years 1980-81 to 1991-92 (relating to Tamil Nadu cases) and for 1989-90 (West Bengal case), involving penalty of Rs.28.22 lakhs, for concealed income, were dropped, without the approval of the competent authority.

**Tax/Penalty/
Interest
levied in
regular
assessments
lying
uncollected**

2.1.16 In cases where search assessments have been framed, demands raised in several cases remained uncollected. For instance, in West Bengal charge, tax of Rs.36.56 crores and penalty of Rs.3.04 crores determined in regular assessments of search cases during the years 1988-89 to 1991-92 remained uncollected. Similarly, in Tamil Nadu charge, in 14 cases relating to assessment years 1983-84 to 1992-93 completed between February 1989 and March 1993, collection of tax and interest of Rs.2.51 crores which was chargeable, was pending.

**Lack of
effective
monitoring**

2.1.17 With a view to ensuring adequate and proper follow up action in search cases, the Board have issued an instruction in July 1991 requiring each Commissioner and Deputy Commissioner of Income Tax to monitor at least 5/10 of the top search cases respectively, every year.

Test check by audit revealed that monitoring was either not being done or was being done partly.

For instance, in Tamil Nadu charge, one Commissioner of Income Tax monitored only 19 cases during the years 1991-92 and 1992-93. The other Commissioner of Income Tax did not furnish the details of monitoring and two Deputy Commissioner of Income Tax did not monitor any search cases. Similarly, in Bihar out of 2 Commissioner of Income Tax charges, in one charge no monitoring was done while in another charge only two cases were monitored during the 5 years period 1988-89 to 1992-93. In Calcutta charge, of the 52 search cases in one circle, only 3 cases were monitored by the Deputy Commissioner of Income Tax, during the year 1991-92. In Punjab charge out of 350 cases required to be monitored by seven Deputy Commissioners of Income Tax during 1988-89 to 1992-93, only 139 cases were monitored.

**Defective/
improper
maintenance
of records**

2.1.18(i) With a view to facilitating control, quick transmission of relevant data to various supervisory authorities as well as for quicker follow-up action, at least 5 registers are required to be maintained by assessing officers, dealing with search assessments.

A review of the maintenance of these registers revealed that most of the registers

were either not maintained or wherever maintained, these were not in the prescribed proforma or were otherwise incomplete. Many important columns in the registers were left blank. Submission of these registers to the competent authorities, wherever required, was also not regularly done.

The different types of deficiencies noticed in test check are mentioned below:

(a) Register of application, for relief against orders passed under section 132(5)

In Tamil Nadu charge, in one circle, the register was not maintained for four years and in 5 circles it was not maintained properly with many of the columns having been left blank. In Madhya Pradesh circles, the register was not submitted to the competent authority periodically. In Uttar Pradesh, its maintenance was not in the prescribed proforma.

(b) Register for granting extension of time for retention of seized records

In Tamil Nadu charge, the register was maintained in three circles but in one circle many columns were left blank. In Assam charge, it was not maintained in 3 circles and in 2 circles, it was not updated. In Uttar Pradesh and Kerala charges, it was not maintained in the prescribed proforma.

(c) Register for retention of books and documents under section 132(8)

In Tamil Nadu, in four circles, its maintenance was not in the prescribed format. In Assam, Uttar Pradesh and Kerala charges, the register was not maintained in almost all the circles test checked. Wherever it was maintained, its maintenance was not in the prescribed proforma. The registers were also not posted upto date.

(d) Register of inspection of seized books and documents

In Assam and Uttar Pradesh charges, the register was not maintained at all in the circles test checked. In Tamil Nadu, Kerala and Calcutta charges, it was not maintained in the prescribed proforma.

(ii) Non-preparation/submission of reports.

Test check revealed that the periodical reports, monthly as well as quarterly, which were prescribed and which were required to be submitted to the competent authorities, were not prepared at all and wherever prepared, these were not submitted to the concerned authorities in time. For instance, in Tamil Nadu circles a review of 306 monthly reports for the period April 1988 to March 1993, on the progress of assessments in cases having concealed income of Rs.10 lakhs or more, received from 7 Commissioner of Income Tax charges, disclosed that the submission of these reports was delayed upto 45 days in 140 reports. Further, a review of 100 quarterly reports of search and seizure assessments in 5 Commissioner of Income Tax charges pertaining to the period April 1988 to March 1993, revealed similar delays ranging from 3 days to 75 days in 46 such reports in four Commissioners' charges.

Other topics of interest**2.1.19(a) Lack of co-ordination in assessments**

The departmental 'Search & Seizure Manual 1989' mentions that in order to ensure that action is taken by all assessing officers on similar lines in respect of assessments of all assessees of a group, the assessing officer dealing with one assessee should keep in close touch with officers dealing with other assessees of the group.

(i) In West Bengal charge, in respect of one assessee of a group, the assessing officer, in the interim order passed, estimated income of Rs.13.35 lakhs being the assessee's share of undisclosed profit declared by a firm as concealed income. However, in the case of another assessee of the same group assessed in another circle, the assessing officer omitted to add Rs.26.71 lakhs being his share of profit in the said firm. Similarly, in another case, a sum of Rs.4 lakhs being 20 per cent share of undisclosed profit (Rs.20 lakhs) of a firm was added to the income of partners by one assessing officer, but during regular assessment the said disclosure of Rs.20 lakhs was not taken into account in the assessment of the firm. No reasons for exclusion were recorded in the assessment order.

(ii) In Gujarat charge, as per appraisal report in a case, land for a project was purchased in September 1986 and the cost of land was shown as Rs.38 lakhs in the accounts seized. In the audited accounts the cost of land was shown as Rs.29.64 lakhs only, implying that the difference of Rs.8.36 lakhs treated as undisclosed income was paid in cash outside the books of accounts to the land owners. This fact was also admitted by the assessee during the search. However, no action has been taken by the assessing officer to pass on this information to the assessing officer having jurisdiction over the owners of the land, so that the tax on capital gain could be levied on such amounts and penal action taken for not showing the amount in the books of accounts.

(b) Failure to co-ordinate with other departments on valuable information established during search

The Search and Seizure Manual, 1989, as well as departmental instructions, require the investigating wing of the department as well as the assessing officer to maintain co-ordination/liaison with other departments and enforcement agencies, like Revenue Intelligence, Enforcement Directorate, Customs and Central Excise department, Sales Tax department etc. Instances have come to notice where such other departments/agencies were not informed of violation of other laws. For example, in Gujarat charge, in case of an assessee who was found to have acquired gold ornaments worth Rs.82.05 lakhs out of unaccounted business transactions, no information was passed on to the Sales Tax department of the state.

The review was referred to the Ministry for comments in September 1993; their reply has not been received so far.

2.2 Exemption under section 80-O

Introduction

2.2.1 The Income Tax Act, 1961 contains several provisions providing tax incentives to encourage the flow of foreign exchange into the economy. Section 80-O is one such provision, which was introduced with the

additional objective of developing technical know-how in the country, which could be made available to foreign governments and enterprises so as to boost foreign exchange earnings. The provisions introduced with effect from 1 April 1968 provide for exemption of income by way of royalties, commission, fees, etc. received in convertible foreign exchange for use outside India of any patent, invention, model, design, or secret formula etc. or information concerning industrial, commercial or scientific knowledge, experience or skill or in consideration of technical or professional services rendered outside India. The extent of exemption which was originally 60 per cent of the specified income, was raised to 100 per cent with effect from 1 April 1969, but was reduced to 50 per cent with effect from 1 April 1985. The benefit was available only to Indian companies up to 31 March 1992, but from 1 April 1992, non-corporate assesseees have also become entitled to the concession. Another major change, which has become effective from 1 April 1992 is that the benefit of section 80-O deduction has been extended even to professional services rendered abroad.

Procedure

2.2.2 For claiming deduction, the application for approval of agreement with a foreign party is required to be made to the Chief Commissioner or Director General of Income tax, in the prescribed form, before the first day of October of the assessment year for which the approval is first sought. The applications are entered in a register chronologically and a report about disposal of cases is to be sent to the Board every quarter. The grant of exemption was subject to the approval of the appropriate authority. From 1 April 1992 the condition regarding approval of the agreement, has been dispensed with.

Scope and extent of audit

2.2.3 The department does not maintain, in a centralised manner, any information regarding cases where the deduction under section 80-O has been claimed or the extent to which the deduction has been allowed. However, a test check was conducted in audit of 218 cases in which deduction under section 80-O was allowed in Andhra Pradesh, Bihar, Delhi, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Tamil Nadu and West Bengal, to examine whether the exemption under this section was correctly claimed and granted.

2.2.4 The test check revealed the following categories of mistakes and irregularities in granting the exemption under section 80-0 of the Income Tax Act, 1961:

(i) Irregularity in approval of agreement or non-observance of the conditions of approval.

(ii) Mistakes in allowance of deduction computed on the basis of gross receipts.

(iii) Other mistakes

The mistakes detected in 51 cases involved a total tax effect of Rs.8 crores. A few illustrative cases of each of these categories are mentioned below:

(i) Irregularity in approval of the agreements or non observance of conditions of approval.

Prior to 1 April 1992, one of the conditions for the grant of the deduction was that the agreement under which payments eligible for the deduction are received, should be approved by the competent authority. It has been judicially held* that where the testing and certification of samples were done in India and the results given to a foreign company, the assessee was not entitled to deduction of technical fees received. It has also been held@ that commercial services or managerial services rendered are not technical services which qualify for this deduction.

In 13 cases of Bombay, Delhi and West Bengal charges, irregularities in approval or non-observance of conditions of approval resulted in underassessment of income of Rs.314.24 lakhs with consequent under-charge of tax of Rs.185.26 lakhs involving assessment years 1985-86 to 1991-92.

A few illustrative cases are as under:

* 145-ITR-673 (Bom),
@ 118-ITR-312 (Bom)

2.2

Sl. No.	Charge/ Type of assessee	Assessment year	Under-assessment of income (in lakhs of rupees)	Undercharge of tax	Nature of Mistake
1.	WB.I Company	1989-90	9.45	9.39	The assessee being an agent of two principal banks, received non refundable grants and reimbursement of expenses which were not eligible for the deduction. Approval of the agreement was thus irregularly accorded.
2.	Bombay City II Company	1985-86 to 1989-90	126.64	74.45	Assessee company received testing charges, professional charges, inspection fees, export fees and other expenses for services such as physical tests, quantitative analytical tests, preparation of technical reports, obtaining certification of goods to be exported out of India etc. The Board, while approving the agreement specifically directed the assessing officer to determine the consideration attributable to activities which qualify under these provisions. However the assessing officer failed to ignore part of the professional charges of which only one-third was earlier held as eligible for the deduction)and omit the entire income by way of inspection fees, export fees and other charges.
3.	Bombay City II Company	1988-89 to 1990-91	166.28	97.61	Assessee received income by way of testing charges and professional charges which were not entitled for the deduction. The approval of the agreement was therefore irregular.

The reply of the department to the audit observations have not been received so far.

(ii) Mistake in allowance of deduction computed on gross receipts.

Where any deduction is required to be made in respect of any income which is included in the gross total income of the assessee, then for purpose of computing the deduction, the amount of income as computed in accordance with the provisions of the Income Tax Act shall alone be deemed to be the amount of income which is received by the assessee and which is included in his gross total income. It has been judicially held* that the relief is available with reference

to the net amount as computed for the purpose of assessment and not with reference to the gross amount received.

In 28 cases assessed in Bombay, Karnataka, Tamil Nadu and West Bengal charges, incorrect deductions of Rs.410.12 lakhs with consequent tax effect of Rs.266.57 lakhs involving assessment years 1984-85 to 1991-92 were noticed, where either the expenditure incurred in deriving the income was not considered or the deduction under section 80-O, was not regulated in accordance with the amount of income included in the gross total income. Some cases of this kind are as under:

Sl. No.	Charge/ Type of assessee	Assessment year	Under-assessment of income (in lakhs of rupees)	Undercharge of tax	Nature of Mistake
1.	WB I/ Company	1985-86 to 1989-90	168.01	118.91	Assessee had income which qualified for section 80-O deduction and also other business income but the common expenditure on account of salaries, provision for bonus, pension, gratuity and medical expenses were not apportioned to the two kinds of income, resulting in adoption of gross income for section 80-O deduction.
2.	WB III/ Company	1989-90	31.27	18.06	Employees of the assessee were sent abroad for rendering technical services but their salary and perquisites were not reduced from the amount of technical fees received.
3.	WB IV/ Company	1984-85 to 1989-90	78.18	56.69	Deductions allowed on the gross receipt on account of technical fees, etc. and not with reference to income actually included in the gross total income.
4.	CIT City V, Company	1989-90	31.54	16.56	Assessee had business income, part of which qualified for section 80-O deduction. The assessee was also allowed a deduction of 20 per cent of business profits towards investment deposit account. As this deduction was considered on the composite profit in respect of income from all activities, proportionate deduction should have been made from the income qualifying for deduction under section 80-O. This was not done.

5.	Bombay CIT City II Company	1989-90	49.11	25.78	Proportionate overseas tax of Rs.98.21 lakhs paid in various countries from consultancy income not reduced from income qualifying for section 80-D deduction.
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The reply of the department to the audit observation has not been received so far.

(iii) Other Mistakes

Representative cases of other types of mistakes noticed in the cases test-checked, are as under:

Sl. No.	Charge/ Type of assessee	Assessment year	Under-assessment of income (in lakhs of rupees)	Undercharge of tax	Nature of Mistake
1.	WBIV/ companies	1983-84	191.37	160.10	It has been held that if the receipts are fully covered by the provisions of section 80HHB (deduction in respect of profits and gains from projects outside India) the deduction under section 80HHB would prevail over the relief that might have been otherwise available. This would be so even if approval under section 80-D has been accorded. In case of two companies which were engaged in the execution of project outside India, the deduction was allowed under section 80-D at 100 per cent instead of at 25 per cent of such income under section 80HHB.
2.	Bombay CIT/City V and Company	1989-90 1990-91	112.81	60.05	Cash compensatory support amounting to Rs.114.68 lakhs and Rs.110.93 were irregularly considered for deduction.
3.	Bombay City I/ Company	1990-91	could not be computed by Audit	could not be computed by Audit	Even after the appropriate authority while according approval of the agreement, held that only 2 out of 9 types of services (i.e. about 20%) rendered by the assessee were eligible for the deduction, yet the assessing officer considered the entire receipts for deduction. In the absence of quantification of receipts from each type of services, the exact excess deduction allowed could not be worked out.
4.	Delhi City I/ Companies	1988-89	240.63	128.72	The Act allows the deduction only if amount is received in convertible foreign exchange in India within 6 months, or such extended period as allowed by the appropriate authority. In the case of 6 company assesseees of

Delhi charge, consultancy fees on which tax concession was given, was not received from either the foreign enterprise or government within the stipulated time.

The reply of the Ministry of Finance in respect of Serial No.1 has not so far been received. In case of the company(Sl.No.4) the department has accepted the audit observation. In other cases reply of the department has not been received.

Summing up

2.2.5 Test check by Audit revealed the following types of major mistakes and irregularities in the allowance of deductions granted under Section 80-0 of the Income Tax Act, 1961:

(i) Approval to agreements was accorded with scant regard to the eligibility of nature of receipt for relief under Section 80-0.

(ii) Relief was allowed on the gross income without reducing the direct and indirect expenses incurred in deriving such income.

(iii) Relief at a higher rate was allowed under Section 80-0, instead of at a lower rate, as correctly admissible under Section 80 HHB.

(iv) Evidence in support of receipt of convertible foreign exchange in the country was not insisted upon, leading to violation of provisions of the section.

The review was referred to the Ministry for comments in September 1993; their reply has not been received so far.

2.3 SPECIAL PROVISIONS RELATING TO MINIMUM TAX

Introductory

2.3.1 It is an accepted canon of taxation to levy tax on the basis of ability to pay. However, exemptions and reliefs, particularly in the corporate sector, are so extensive that many flourishing companies with disposable commercial profits and declaring attractive dividends could substantially reduce their tax liability by availing of the incentives and the concessions, within the framework of the Income Tax Act, 1961.

As a sequel to the recommendations of the Public Accounts Committee in their 143rd

report (7th Lok Sabha), that the impact of various tax exemptions granted, particularly to the corporate sector should be evaluated, and as a measure of equity a new chapter VIB was introduced by the Finance Act, 1983, with effect from 1 April 1984 so as to compel the high profit earning companies, which reduce their tax liability to zero or near zero level, to contribute to the national exchequer, by paying tax on at least 30 per cent of their profits. This provision was introduced in the form of Section 80VVA. However, its implementation revealed that it was inadequate, ineffective and had several incongruities in it. Consequently, a new provision, Section 115J was introduced in the Finance Act, 1987, with effect from assessment year 1988-89, for the levy of minimum tax on companies, (other than those generating power) which had disposable commercial or accounting profits, and yet were not paying any tax or paying only nominal tax, under the normal provisions of the Act.

The chief difference between section 80VVA and section 115J was that while in the former, most of the unadjusted deductions/tax concessions could be carried forward to subsequent years, in the latter case the unavailed allowance /tax incentives could not be carried forward to the following year. Further section 115J was based on book profits as computed under the Companies Act and it was to supersede all provisions of the Income Tax Act, wherever the taxable income was lower than 30 per cent of the book profits. In contrast, Sec. 80VVA was based on pre-incentive total income as computed under the Income Tax Act, requiring the aggregate amount of deductions to be limited to 70 per cent of the pre-incentive total income.

**Law and
Procedure**

2.3.2 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 per cent of its book profit, shall be deemed to be the amount equal to 30 per cent 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

the Companies Act, 1956, subject to certain additions/deletions as mentioned in the provision. Section 115J, therefore, involves a two-stage computation. First, an assessing authority has to determine the income of the company under the provisions of the Income Tax Act. Thereafter, the book profit is to be worked out in accordance with the Explanation to section 115J(1). Section 115J would be invoked if the income determined under the normal provisions is less than 30 per cent of the book profit. Explanation to sub-section(1) of section 115J gives the definition of the book profit by incorporating the requirements of section 205 of the Companies Act. In the computation of 'book profit', brought forward losses or unabsorbed depreciation, whichever is less, would be reduced. Sub-section(2) however, provides that the application of this provision would not affect the carry forward of unabsorbed depreciation, unabsorbed investment allowance and business losses to the extent not set off.

The computation of income liable to tax under the special provisions of section 115J, is based on 'book profits' after the adjustments mentioned above are made. Thus, the computation is dependent on what an assessee shows in the books of accounts as his profits for the year. The provisions of the Companies Act in relation to drawing up of profit and loss account are not very specific as to either cover all conceivable items of receipts or expenditure and the manner of their accounting. To cite only an example, a company could credit to either the general reserve or some other reserve, sums received by it on account of cash compensatory support. Another company may credit the same amount to the profit and loss account of the year. In both cases, companies would be deemed to have drawn up their accounts in accordance with the provisions of the Companies Act. The concept of book profit under the Companies Act thus being indefinite, the entire process of computation under section 115J was likewise indefinite. This led to varying interpretations and avoidable litigations.

Scope and extent of review 2.3.3 This review seeks to evaluate, in general, the objectives set forth in the legislation for augmenting revenue from the corporate sector particularly from the so called 'zero tax' companies. It also attempts

to assess the degree of compliance by the department with the law and procedural requirements and the manner of implementation of the scheme. Test check of assessments of companies for the assessment years 1988-89 to 1990-91 involving application of section 115J (deleted with effect from assessment year 1991-92) was carried out in audit for the purpose of this study in Maharashtra, West Bengal, Delhi, Assam, Gujarat, Madhya Pradesh, Punjab, Haryana, Himachal Pradesh, Bihar, Rajasthan, Uttar Pradesh, Karnataka, Kerala, Orissa and Tamil Nadu charges. The number of cases reviewed, aggregate of tax concession enjoyed, number of cases in which minimum tax was levied and the amount of tax levied is shown in the table below:

Assessment year	No. of cases test checked	No. of cases in which minimum tax was levied	Amount of minimum tax levied (in lakhs of rupees)	No. of cases in which mistakes were detected	Tax effect (in lakhs of rupees)
1988-89	3074	579	14,674.78	112	2183.90
1989-90	3797	883	12,631.54	143	1711.07
1990-91	3538	871	14,463.17	125	1820.12
Total	10409	2333	41,769.49	380	5715.09

The important findings of Audit are set out in the succeeding paragraphs.

Highlights

2.3.4(a) Section 115J of the Income Tax, Act, 1961, which was applicable to corporate assesseees from the assessment year 1988-89 to 1990-91 provides that where total income computed under normal provisions of the Act, is less than 30 per cent of its book profit, the income chargeable to tax is deemed to be 30 per cent of such book profit. The provision was required to be invoked even in cases where computation of income under the normal provisions of the Act results in 'Nil' income or a loss. Omission to invoke the provisions of minimum tax resulted in short levy of tax of Rs.1,100.83 lakhs in 70 cases.

(b) Where income chargeable under the normal provisions of the Act is more than that computed under the special provisions of the Act, the special provision is not required to be invoked. In 15 cases test-checked, income for the assessment years 1988-89 to 1990-91 under the normal provisions of the Act worked

out to be more than that computed by the assessing officer under the special provisions. The unwarranted application of special provisions in 15 cases led to under-assessment of income of Rs.310.76 lakhs involving under-charge of tax of Rs.235.71 lakhs .

(c) The special provisions require that net profit shown in the profit and loss account of the relevant previous year has to be increased by the amounts set aside as provisions made for meeting liabilities, other than ascertained liabilities. However, in 67 cases test-checked, the net profit as per the profit and loss account was not increased by the amount of provisions for bad and doubtful debts, gratuity, estimated loss on slow/non-moving/non-useable stores write back of depreciation excess provision of earlier years written back, etc. resulting in undercharge of tax of Rs.2,331.94 lakhs.

(d) Where a company has brought forward losses, as well as, unabsorbed depreciation to be set off against the book profit, the lesser of the two is required to be set off in accordance with clause (b) of the proviso to sub-section (1) of section 205 of the Companies Act 1956, and the Central Board of Direct Taxes instructions of September 1987. The mistake in applying the above provisions incorrectly, in 44 company cases, involved short levy of tax aggregating Rs.303.38 lakhs.

(e) In 13 cases, unabsorbed depreciation, unabsorbed investment allowance and losses relating to earlier years were allowed to be set off against the current year's income, even though these were already adjusted in the earlier years and nothing remained to be adjusted. The mistake resulted in short levy of tax of Rs.473.85 lakhs.

(f) For computing book profit, certain specified adjustments are required to be made. Where some deductions are not allowable to the assessee under the normal provisions of the Act, book profit is not required to be reduced by such inadmissible deductions. Incorrect reduction of book profits on account of deductions for export profits under section 80 HHC, deduction in respect of special reserves, exchange rate difference, etc. were allowed in some cases though the assessees were not eligible to these

deductions under the normal provisions of the Act. These omissions led to short levy of tax of Rs.237.12 lakhs in 19 cases.

(g) Liabilities relating to earlier years but debited to the profit and loss account of the current year are required to be added back to arrive at book profit for the purpose of section 115J. Omission to add back liabilities on account of gratuity, charity, donations and other business expenses relating to earlier years led to short levy of tax of Rs.134.46 lakhs in 6 cases.

(h) In cases where the assessee follows the mercantile system of accounting, their total income for any previous year will include all incomes from whatever sources derived, which is received or deemed to be received or which accrues or arises during such previous year. In 14 cases, income/receipts on account of excise duty refunds, share of income from registered firms, interest accrued on investments, short-term capital gains, etc. were excluded while computing book profits, resulting in undercharge of tax of Rs.59.82 lakhs.

(i) Omission to invoke the provisions of minimum tax by the assessing officers while rectifying the mistakes for giving effect to appellate orders, involved short levy of tax of Rs.63.69 lakhs in 13 cases.

Non-levy of minimum tax

2.3.5(a) Under the special provisions, where the total income computed under the normal provisions of the Income Tax Act, 1961, in the case of a company is less than 30 per cent of its book profit, the income chargeable to tax is deemed to be 30 per cent 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.

The assessments of 70 companies, for the assessment years 1988-89 to 1990-91, assessed in West Bengal, Bombay, Haryana, Kerala, Uttar Pradesh, Punjab, Bihar, Gujarat, Madhya Pradesh, Andhra Pradesh, Rajasthan, Karnataka, Assam, Delhi, Orissa and Tamil Nadu charges were completed at 'nil' income, or at a loss. However, the assessee companies had adjusted book profits assessable under

the minimum tax provisions, and in some cases, had offered the same for taxation. In these cases the assessing officers were required to levy minimum tax at 30 per cent of the book profit. Omission to do so resulted in short computation of book profit by Rs.7115.01 lakhs involving under-assessment of income aggregating Rs.2,102.41 lakhs with resultant short levy of tax of Rs.1100.83 lakhs (including additional tax and interest for default in payment of advance tax). An illustrative case is given below:

The assessment of a banking company in Tamil Nadu charge, was made for the assessment year 1988-89 under section 143(3), determining the taxable income at 'nil' and no levy was made under Section 115-J either at the time of original assessment made in March 1991, or in the revisions done in February 1992 and December 1992. It was noticed in audit that the net profit as computed in accordance with the Parts II and III of Schedule VI to the Companies Act, 1956 worked out to Rs.2,474.65 lakhs after including an amount of Rs.1915.65 lakhs representing provisions for doubtful debts, contingencies, income tax and excess depreciation (debited in accounts in excess of Schedule XIV of Companies Act, 1956), in the profit of Rs.558.98 lakhs as per Banking Act, 1946. The omission to invoke provision of Section 115-J resulted in underassessment of income of Rs.742.40 lakhs (being 30 percent of book profit computed at Rs.2474.65 lakhs) involving undercharge of tax of Rs.389.76 lakhs.

(b) 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.

While computing the taxable income in the case of 15 companies in West Bengal, Uttar Pradesh, Bihar, Delhi, Gujarat, Maharashtra and Tamil Nadu charges, for the assessment years 1988-89 to 1990-91, the assessing officers started with the net profits as shown in the profit and loss account and reduced therefrom higher amounts on account of depreciation and investment allowance, instead of the amount actually debited to the profit and loss account and thus determined the total taxable income for those years under special provisions of the Act. However

audit scrutiny revealed that the correct taxable income for these assessment years, without invoking the special provision of the Act, worked out to Rs.1486.21 lakhs, which was more than the income determined under the special provisions. The unwarranted application of the special provisions of the Act resulted in underassessment of income of Rs.310.76 lakhs involving undercharge of tax of Rs.235.71 lakhs (including additional tax and interest for short payment of advance tax). One major representative case is cited below:

A private limited company in Bihar charge, for the assessment year 1988-89, was assessed on taxable income of Rs.110.12 lakhs under section 144 of the Income Tax Act, 1961, in March 1991. Subsequently, as a result of appellate orders, the assessment was modified at a loss of Rs.21.88 lakhs without working out book profit in accordance with the provisions of section 115J. The book profit for the previous year relevant to the assessment year 1988-89 worked out to Rs.13.22 lakhs. In arriving at this book profit, the amount of Rs.7.69 lakhs carried to investment allowance reserve and debited to the relevant profit and loss account was added back to the net profit of Rs.5.74 lakhs and the brought forward unabsorbed depreciation of Rs.20,471 relating to the assessment year 1985-86 was deducted. 30 per cent of the book profit viz. Rs.3.97 lakhs being higher than the taxable income (loss of Rs.21.88 lakhs) should have been taken as deemed income of the assessee company under Section 115J for the assessment year 1988-89.

However, as per assessment order of March 1991, the total taxable income was determined under section 144 after allowing depreciation of Rs.34.56 lakhs on fixed assets. On the other hand, the appellate order under reference allowed depreciation of Rs.82.44 lakhs besides other reliefs to the tune of Rs.5 lakhs. The depreciation allowed in assessment dated March 1991 should have been added back to the total taxable income before allowing appellate relief. Instead, the assessing officer deducted the depreciation of Rs.34.56 lakhs again before allowing appellate reliefs. The mistake resulted in grant of excess depreciation of Rs.69.12 lakhs. The correct taxable income would, therefore, come to Rs.47.24 lakhs (Rs.69.12 minus Rs.21.88 lakhs) which is higher than the deemed income

of Rs.3.97 lakhs brought to tax under section 115J. The mistake led to undercharge of tax of Rs.57.83 lakhs (including interest and potential tax of Rs. 13.78 lakhs).

**Incorrect
computation
of book
profit**

2.3.6(a) 'Book profit' has been explained 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 the assessment of 67 companies, for the assessment years 1988-89 to 1990-91 assessed in West Bengal, Maharashtra, Uttar Pradesh, Kerala, Punjab, Bihar, Madhya Pradesh, Karnataka, Assam, Delhi, Gujarat and Tamil Nadu charges, provisions for bad and doubtful debts, redemption of debentures, estimated loss on slow/non moving/non-usable stores, gratuity, transfer to molasses storage reserve fund, provisions for interest on sugar prices, leave salary, building, bonus, income tax unconfirmed expenditure on purchase of scrap, amounts representing write back of depreciation, excess provision of earlier years written back, difference in depreciation on revaluation of assets, etc. amounting to Rs.12,696.41 lakhs charged to the profit and loss account of the relevant previous years were not added back to arrive at the correct amount of 'book profit'. Omission to add back the amounts set apart for unascertained liabilities resulted in short computation of 'book profit' by an identical amount leading to underassessment of income of Rs.3822.04 lakhs with undercharge of tax of Rs.2331.94 lakhs (including interest for short payment of advance tax). Three illustrative cases are mentioned below:

(i) The assessment of a banking company in Tamil Nadu charge, for the assessment years 1988-89 to 1990-91, was made in a scrutiny manner determining the taxable income at "nil" and deemed income under section 115 J was determined at Rs.673.28 lakhs, Rs.482.85 lakhs and Rs.593.16 lakhs respectively. It was noticed in audit that provision for contingent liabilities and depreciation claimed in excess of that prescribed under the Companies Act, were not added back to the book profits leading to underassessment of deemed income aggregating Rs.1,873.09 lakhs

involving under charge of tax of Rs.1,004.13 lakhs for the three years.

(ii) In Delhi charge, the assessment of a scheduled bank, for the assessment year 1988-89, was completed, after scrutiny, at a loss of Rs.63.57 lakhs. It was observed that net book profit as per profit and loss account was Rs.49.40 lakhs. Considering the provisions for building (Rs. 1.50 lakhs), income tax (Rs.15.00 lakhs), doubtful debts (Rs.284.32 lakhs), gratuity (Rs.85.15 lakhs), bank robbery (Rs.3.63 lakhs) and fraud cases (Rs.2.86 lakhs), the total book profit works out to Rs.441.87 lakhs. Thus deemed taxable income amounting to Rs.132.56 lakhs, 30 per cent of Rs.441.87 lakhs escaped assessment involving a tax effect of Rs.89.73 lakhs (including of interest for short/non-payment of advance tax).

(iii) In West Bengal charge, the regular assessment of a widely held company for the assessment year 1989-90, was made in February 1992 computing loss on account of unabsorbed depreciation at Rs.621.91 lakhs and unabsorbed investment allowance at Rs.1466.66 lakhs. A sum of Rs.233.05 lakhs was taken as the chargeable income, being 30 per cent of the book profit of Rs.776.86 lakhs.

It was noticed in audit that during the relevant previous year, the company had derived profit on sale of assets (Rs.1458.10 lakhs). While determining 'book profit', the company had deducted Rs.1,171.39 lakhs representing write back of depreciation provided in the books in respect of sold assets (up to 30 September 1987). As the amount represented profit on sale of assets and not provision for depreciation written back, it was not deductible from the book profit in the absence of any enabling provision in the Act. The incorrect reduction of book profit by Rs.1,171.39 lakhs resulted in short computation of profit by a like amount leading to underassessment of chargeable income by Rs.351.42 lakhs (30 per cent) with consequent undercharge of tax of Rs.184.49 lakhs for the assessment year 1989-90.

(b) 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 section 205 of the Companies Act, 1956. The Board also issued instructions in September 1987 on similar lines.

In the case of 44 companies assessed in Delhi, Haryana, Bihar, Rajasthan, Orissa, Gujarat, Tamil Nadu, Kerala and Assam charges, while computing the book profit, the amount of unabsorbed depreciation of earlier years and brought forward losses amounting to Rs.2364.98 lakhs were reduced from the book profits whereas the correct amount of unabsorbed depreciation of earlier years and brought forward losses amounting to Rs.750.13 lakhs (nil in some cases) were required to be reduced from the book profits in accordance with the legal position mentioned above considering the lesser of the two amounts. The mistakes resulted in short computation of book profit of Rs.1,475.39 lakhs involving underassessment of income of Rs.442.48 lakhs with undercharge of tax of Rs.303.38 lakhs for the assessment years 1988-89 to 1990-91 (including additional tax and interest under Section 234B). Two such cases are mentioned below, as illustrations:

(i) The assessment of a company in Bihar charge, for the assessment year 1990-91, was completed in a scrutiny manner, in March 1993, on taxable income of Rs.138.89 lakhs, based on book profit of Rs.462.97 lakhs computed under section 115J of the Income Tax Act, 1961. While computing the book profit, the assessing officer allowed set off of carried forward unabsorbed depreciation of Rs.604.11 lakhs (total carried forward loss including aforesaid depreciation being Rs.2024.78 lakhs). However, as per details furnished by the assessee company in the return of income for the assessment year under reference, the total carried forward losses amounted to Rs.1467.65 lakhs which included unabsorbed depreciation of Rs.404.32 lakhs. The assessee company was, therefore, entitled to set off Rs.404.32 lakhs instead of Rs.604.11 lakhs being lesser of the two amounts. Grant of excess set off of depreciation resulted in reducing, the book profit by Rs.199.79 lakhs leading to under charge of income by Rs.59.94 lakhs with consequent short levy of tax of Rs.53.31 lakhs (including interest for non payment of advance tax).

(ii) The assessment of a company in Tamil Nadu charge, was made for the assessment year 1989-90, in December 1991, determining the deemed income at Rs.279.38 lakhs. The 'book profit' of Rs.931.27 lakhs was arrived at after deducting the depreciation of Rs.201.39 lakhs debited to the profit and loss account for the accounting year 1987-88 relevant to the assessment year 1988-89. Audit scrutiny revealed that as per the balance sheet of the company for the year 1987-88, there was no unabsorbed loss or unabsorbed depreciation to be carried forward in the year 1988-89. Hence the deduction of Rs.201.39 lakhs from the profits of the company for 1988-89 (relevant to assessment year 1989-90) for computation of 'book profits' was not in order. The mistake resulted in short computation of total income by Rs.60.42 lakhs leading to a short levy of tax of Rs.52.65 lakhs.

(c) 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 provisions applicable to normal computation of total income. However, it was noticed in some cases that the provisions regarding carry forward and set off of unabsorbed allowance/losses were not properly followed, thereby adversely affecting the revenue realisable in subsequent years.

In the cases of 13 companies in Karnataka, Gujarat, Maharashtra and Tamil Nadu charges, unabsorbed depreciation, unabsorbed investment allowance and losses relating to earlier years were allowed to be set off against the current years' income although these amounts were already adjusted in the earlier years and there was nothing left to be set off. The mistakes resulted in under assessment of income of Rs.890.65 lakhs leading to undercharge of tax of Rs.473.85 lakhs. Two illustrative cases are given below:

(i) The assessments for the assessment years 1988-89, 1989-90 and 1990-91 of a company, in Tamil Nadu charge, were made allowing the assessee to carry forward losses of Rs.272.18 lakhs, Rs.725.47 lakhs and Rs.13.83 lakhs and determining the deemed income under section 115J at Rs.97.70 lakhs, Rs.121.21 lakhs and Rs.95.41 lakhs respectively. The assessment

for assessment year 1991-92 was made determining the taxable income at 'nil'. It was noticed in audit that the assessee claimed carry forward for these years at Rs.369.88 lakhs, 846.68 lakhs and Rs.109.25 lakhs increasing the loss to be carried forward under the normal provisions of the Act by the deemed income assessed for these years under section 115J(Rs.97.70 lakhs, Rs.121.21 lakhs and Rs.95.42 lakhs respectively), which is not in accordance with the provisions of Section 115J(2). The excess carry forward of Rs.314.33 lakhs, in aggregate, resulted in potential tax effect of Rs.144.59 lakhs.

(ii) The assessment of a widely held company in Tamil Nadu charge, for the assessment year 1989-90, was completed in March 1992, on a total income of Rs.146.82 lakhs after setting off unabsorbed investment allowance of Rs.57.40 lakhs relating to the assessment year 1986-87. Audit scrutiny revealed that the total income for the assessment year 1988-89 had been computed in February 1989 at Rs.88.65 lakhs after setting off all the unabsorbed allowance upto the assessment year 1987-88. The total income for the purpose of levy of tax for the assessment year 1988-89 was however determined at Rs.146.05 lakhs at 30 per cent of the book profit, since this was greater. The assessee's request for the carryforward of the difference of Rs.57.40 lakhs (Rs.146.05 lakhs minus Rs.88.65 lakhs) as unabsorbed investment allowance was also negatived by the assessing officer in the assessment order of February 1989 for the assessment year 1988-89 as being beyond the provisions of the Act. The set off of Rs.57.40 lakhs in the assessment for the assessment year 1989-90 was, therefore, incorrect. The mistake resulted in short levy of tax of Rs.48.00 lakhs (including interest for default in payment of advance tax).

(d) For computing book profit under section 115J, certain specified adjustments are required to be made. Where, however, some deductions are not allowable to the assessee under normal provisions of the Act, the book profit is not required to be reduced by such inadmissible deductions.

In the case of 19 companies in Maharashtra, Assam, Delhi, Gujarat, Tamil Nadu and Rajasthan charges, while computing book profits for the assessment years 1988-89 to

1990-91, amounts representing deductions for export profit under section 80HHC, deduction in respect of special reserves created by a financial corporation, capital expenditure on account of exchange rate difference due to the fluctuation in foreign exchange, technical know-how fee, good-will written off, etc. were reduced from the book profits, though the assessees were not eligible for these deductions under the normal provisions of the Act. The incorrect reduction of book profits by the amount of ineligible deductions, resulted in short computation of book profit by Rs.1297.83 lakhs involving underassessment of income of Rs.422.22 lakhs with undercharge of tax of Rs.237.12 lakhs (including additional tax and interest). Two illustrative cases are given below:

(i) An assessee company in Gujarat charge, debited an amount of Rs.318.28 lakhs representing exchange rate difference due to fluctuation in the rate of foreign exchange on cost of plant and machinery, to its profit and loss account of the previous year relevant to assessment year 1989-90. While computing income under the normal provisions of the Act, the expenditure was treated as capital expenditure. However, while computing book profits under the special provisions of the Act, the same was not added back. The mistake resulted in short computation of book profit by Rs.318.28 lakhs, leading to under-assessment of income of Rs.95.48 lakhs with short levy of tax of Rs.50.13 lakhs.

(ii) The assessment of an assessee company in Tamil Nadu charge, for 1989-90, was made, allowing the assessee to carry forward loss of Rs.613.70 lakhs, and determining the deemed income under section 115J, at Rs.186.24 lakhs. It was noticed in audit that the deemed income under section 115J worked out to Rs.228.54 lakhs. In computing "book profits" the assessee claimed a deduction of Rs.141 lakhs towards export profits eligible for deduction under section 80HHC(3). However, income under the head "profits and gains of business or profession" was determined at a loss of Rs.613.70 lakhs; and therefore the assessee was not eligible for deduction under section 80HHC(3). The mistake of reducing a deduction of Rs.141 lakhs on account of export profits, from book profits resulted in underassessment of deemed income

by Rs.42.30 lakhs i.e. (228.54 lakhs minus 186.24 lakhs) and led to a short levy of tax of Rs.22.21 lakhs.

(e) While computing the income of an assessee, the assessing officer normally proceeds with the income as computed by the assessee as the starting point and then makes necessary adjustments by way of additions or deletions as required by the provisions of the Act and rules to arrive at the total taxable income. Liabilities relating to earlier years but debited to the profit and loss account of the current year are required to be added back to arrive at the book profits for the purpose of section 115J.

In the case of 6 companies, assessed in Uttar Pradesh, Punjab and Gujarat charges and following the mercantile system of accounting, liabilities aggregating Rs.695.18 lakhs on account of gratuity, charity, donations and other business expenses relating to earlier years were debited to the profit and loss accounts for the assessment years 1988-89 to 1990-91. As the liabilities related to the earlier years, the same were required to be added back to arrive at the correct amount of chargeable book profits. The mistakes resulted in under-assessment of income of Rs.208.56 lakhs (being 30 per cent of Rs.695.18 lakhs) leading to undercharge of tax of Rs.134.46 lakhs (including interest). One such case is cited below:

In a case of public limited company in Uttar Pradesh charge, assessment, for the assessment year 1989-90, was completed, after scrutiny in March 1991. It was noticed in audit that the assessee, following the mercantile system of accounting, had debited a sum of Rs.50.85 lakhs under the head 'gratuity' in profit and loss account. Out of this amount, liability of Rs.39.20 lakhs pertained to earlier years and should have been disallowed. As such the book profit for assessment year 1989-90 was reduced to that extent, resulting in short computation of deemed taxable income of Rs.11.76 lakhs (30 per cent of Rs.39.20 lakhs), involving tax liability of Rs.7.41 lakhs (including interest for short payment of advance tax).

(f) Where the assessee follows the mercantile system of accounting, his total income for any previous year will include all

incomes from whatever sources derived, which is received or deemed to be received or which accrues or arises during such previous years.

In the case of 14 companies assessed in Kerala, Gujarat, Madhya Pradesh, Rajasthan, Maharashtra and Tamil Nadu charges, receipts/incomes aggregating Rs.505.74 lakhs received/accrued during the previous years relevant to assessment years 1988-89 to 1990-91 on account of refund of excise duty, share of income from registered firm, interest accrued on investments, sale of grass considered as a revenue receipt, unpaid amount of sale tax collected but not treated as trading receipt, income-tax refund, short-term capital gains, etc., though initially credited to the profit and loss account were excluded while computing book profits for the purpose of section 115J. The mistake resulted in short computation of book profits in the above cases by Rs.505.74 lakhs involving under assessment of income of Rs.99.43 lakhs, after adjusting income already assessed with resultant tax effect of Rs.59.82 lakhs. One such illustrative case is mentioned below:

In the case of a widely held company in Gujarat charge, the income tax assessment for assessment year 1988-89 was completed after scrutiny in January 1991, determining the deemed total income, based on book-profit, as Rs.1.90 lakhs, since the total income computed under normal provisions was less. The assessee received an amount of Rs.50.66 lakhs as refund of central excise duty in the relevant previous year, which was not credited to the profit and loss account on the ground that the refund had not become final since the Central Excise Department had filed an appeal against the refund. This amount was however, included in the total income computed under normal provisions of the Income-tax Act. However, for computation of book-profit, the amount of the refund of duty was not considered. The incorrect exclusion of this amount resulted in short computation of deemed income by Rs.15.20 lakhs and short levy of tax of Rs.7.98 lakhs.

**Omission to
invoke
provisions
of minimum
tax while
giving
effect to
appellate
orders**

2.3.7 In 13 cases of West Bengal, Gujarat, Andhra Pradesh, Karnataka, Assam, Kerala and Tamil Nadu charges, the assessing officers ignored the minimum tax provisions while rectifying the mistakes in original assessment, giving effect to appellate orders though in some cases the assessee themselves had filed statements showing the adjusted book profit. Omission to invoke the provisions of Section 115J while rectifying the mistakes resulted in under-assessment of income totalling to Rs.79.16 lakhs with the resultant tax effect of Rs.63.69 lakhs for the assessment years 1988-89 and 1990-91 (including interest for default for payment of advance tax).

The review was forwarded to the Ministry on 27 September 1993. The legal position as emerging out of irregularities and mistakes pointed out in the review was accepted by the Ministry in principle. One of the illustrative cases cited in the review was also accepted. Replies in respect of other cases are awaited.

CHAPTER 3

CORPORATION TAX

General

3.1 ** According to Department of Company Affairs, Ministry of Law, Justice and Company Affairs, there were 2,78,792 companies as on 31 March 1993. These included 529 foreign companies and 2,262 associations functioning 'not for profit' but registered as companies limited by guarantee and 337 companies with unlimited liability. The remaining 2,75,664 companies with limited liability comprised 1,190 Government companies and 2,74,474 non-Government companies with paid up capital of Rs.60,476.6 crores and Rs.30,485.6 crores respectively. Among non-Government companies, over 87.07 per cent (2,40,925) were private limited companies with a paidup capital of Rs.5,149.5 crores.

3.2 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
1989	96,176
1990	1,10,514
1991	1,24,402
1992	1,34,779
1993*	1,30,388

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

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

Year	Receipts from Corporation tax (in crores of rupees)	Gross collection of all direct taxes	Percentage of Corporation tax to gross collection	Number of assess- ments completed
1988-89	4,407.21	8,828.76	49.91	1,21,595
1989-90	4,728.92	10,007.78	47.25	1,04,572
1990-91	5,335.26	11,028.93	48.37	1,19,265
1991-92	7,867.67	15,342.36	51.28	1,46,998
1992-93*	8,889.24	18,155.32	48.96	1,51,913

* Figures furnished by the Ministry of Finance/Controller General of Accounts are provisional

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

Year	No. of assessments		Percent- age	Amount of demand	
	completed during the year	pending at the close of the year		collected during the year	in arrears at the close of the year
1988-89	1,21,595	41,421	34.06	4407.21	2169.41
1989-90	1,04,572	50,286	48.08	4728.92	2951.69
1990-91	1,19,265	57,073	47.85	5335.26	2590.22
1991-92	1,46,998	66,361	45.14	7867.67	3070.54
1992-93*	1,51,913	74,752	49.20	8,889.24	4,199.72

Results of Audit

3.5 A total number of 511 draft paragraphs involving tax effect of Rs 165.85 crores were issued to the Ministry of Finance for comments during March to August 1993. The Ministry of Finance have accepted the observations in 279 cases involving tax effect of Rs.65.47 crores. 106 illustrative cases involving tax effect of Rs.120.98 crores are indicated in the succeeding paragraphs. Out of these, the Ministry of Finance have accepted the observations in 57 cases involving tax effect of Rs.39.44 crores. Of these, 7 cases involving tax effect of Rs.3.15 crores were checked by the Internal Audit but the mistakes were not detected by it. The audit observations in respect of scrutiny and summary assessment cases have been included separately under these heads. 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.

Avoidable mistakes in computation of income and tax

3.6 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

*Figures furnished by the Ministry of Finance are provisional

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 required 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 under-assessed (in lakhs of rupees)
1988-89	679	1,121.38
1989-90	880	960.63
1990-91	1,153	1,135.00
1991-92	878	8,857.00
1992-93	907	1,470.48

The types of mistakes noticed are:

- (i) Incorrect adoption of figures
- (ii) Double allowance
- (iii) Arithmetical errors
- (iv) Calculation errors and other omissions and mistakes.

Some important cases noticed in test check are given below:

Sl. No.	State/Commissioners charge	Assessment year/Date of assessment	Section under which assessed	Nature of mistake	Tax effect/ Revenue implications (In lakhs of rupees)
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(i) Incorrect adoption of figures

	West Bengal/ W.B.II, Calcutta	1989-90 February 1992	143(3)	In arriving at the income from business the assessing officer started with net profit shown in the profit and loss account and deducted, inter alia, Rs.18.56 lakhs instead of Rs.3.94 lakhs actually credited to the profit and loss account for separate consideration.	14.70 (including interest)
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The Ministry has accepted the audit observation.

(ii) Arithmetical error

1.	West Bengal/ W.B.II, Calcutta	1989-90 December 1991	143(3)	Omission to add back Rs.4894.77 lakhs to net profit being depreciation allowance debited to profit and loss account.	62.61
2.	West Bengal/ W.B.III, Calcutta	1988-89 March 1992	143(3)	Total disallowance was worked out at Rs.1700.71 lakhs instead of the correct amount of Rs.1786.71 lakhs.	71.68

The reply of the Ministry has not been received so far.

(iii) Calculation errors and other omissions

1.	Maharashtra/ Bombay city III	1989-90 December 1990	143(3)	Net capital gains of Rs.195.41 lakhs as returned was accepted instead of the correct capital gain of Rs.341.97 lakhs.	76.94 (Potential*)
2.	West Bengal/ W.B.IV, Calcutta	1989-90 December 1991	143(3)	The assessing officer disallowed Rs.5.01 lakhs towards conversion charges for the period ended 31 March 1989 in the absence of supporting evidence, but omitted to disallow a similar sum of Rs.33.13 lakhs relating to the period ended 30 June 1988.	19.13 (Potential*)
3.	West Bengal/ W.B.-VI	1989-90 November 1991	143(1)	Omission to deduct dividend and interest income of Rs.64.74 lakhs by the assessee, separately from book loss.	40.79

The Ministry has accepted the audit observation at Sr.No.1.

The reply of the Ministry in respect of other observations has not been received so far.

* The term potential indicates the possible tax which could have accrued.

**Application
of incorrect
rate of tax**

3.7.1 Under the provisions of Finance Act, as applicable to the assessment year 1989-90, closely held domestic companies in which public are not substantially interested, are chargeable to tax at 55 per cent, whereas companies in which public are substantially interested are charged at 50 per cent of the total income.

The assessment of a company in which the public are not substantially interested for the assessment year 1989-90, was completed in March 1992 and tax was levied at 50 per cent of the total income instead of the correct rate of 55 per cent. The levy of tax at incorrect rates resulted in short levy of tax of Rs.180.92 lakhs, including interest.

The Ministry has accepted the audit observation.

3.7.2 Under the Finance Act, 1988 and 1989, a domestic company, engaged in trading activities in which public are not substantially interested is chargeable to income tax at the rate of 60 per cent on the total income and surcharge at the rate of 5 per cent on the income tax, if total income exceeds fifty thousand rupees.

In the assessment of two closely held domestic companies, engaged in trading business for the assessment years 1988-89 and 1989-90 completed in September 1991 and February 1992, income tax of Rs.180.11 lakhs was charged in one case at the rate of 60 percent of the total income of Rs.300.19 lakhs, but the department did not levy surcharge of Rs.9.00 lakhs leviable at the rate of 5 per cent and in the other case levied income tax at 50 per cent and surcharge at 5 per cent of the income tax instead of the correct rate of income tax at 60 per cent and surcharge at 5 percent thereof. The omission resulted in undercharge of tax of Rs.34.24 lakhs (including interest).

The Ministry has partly accepted the audit observation in one case.

**Incorrect
allowance of
expenditure
on know-how**

3.8 Under the Income Tax Act, 1961, as inserted by the Finance Act, 1985, with effect from 1 April 1986, where an assessee has paid, in any previous year, any lump sum

consideration for acquiring know-how for the purpose of his business, one-sixth of the amount so paid shall be deducted in computing the business income for that year and the balance amount shall be deducted in equal instalments in each of the five immediately succeeding years. In view of the specific provision, the expenditure on technical know-how would not qualify for depreciation, investment allowance, etc.

(i) In the assessment of a public limited company, for the assessment year 1988-89 completed in a scrutiny manner in January 1990, an expenditure of Rs.59.39 lakhs on 'knowledge and foreign consultancy' debited to the profit and loss account, was incorrectly allowed by the assessing officer in full instead of Rs.9.90 lakhs during the year being one-sixth of the expenditure and spreading over the balance in five succeeding years. The mistake resulted in computation of excessive business loss of Rs.49.49 lakhs involving potential short levy of tax of Rs.25.98 lakhs.

The Ministry has accepted the audit observation.

(ii) In the case of an assessee company, for the assessment year 1989-90, completed in March 1992, an amount of Rs.40.00 lakhs was paid as 'technical fees'. The same was capitalised and depreciation on it was claimed and was allowed. As technical know-how cannot be treated as forming part of a capital asset from assessment year 1986-87, no depreciation was allowable on technical know-how. The entire amount was required to be added back and one-sixth therefrom was to be allowed as a deduction. The incorrect allowance resulted in underassessment of income of Rs.34.16 lakhs leading to short levy of tax of Rs.19.73 lakhs (potential).

The Ministry has accepted the audit observation.

Incorrect allowance of preliminary expenses

3.9 Under the provisions of the Income Tax Act, 1961, the admissible expenditure towards preliminary expenses incurred prior to commencement of business or in connection with the extension of an industrial undertaking is limited to 2.5 per cent of cost of the project or capital employed and is allowed in equal instalments spread over ten years.

In the assessment of three public limited companies for the assessment years 1986-87 to 1988-89 it was noticed that Rs.71.39 lakhs being preliminary expenses incurred on issue of debentures/bonds, was debited to profit and loss account in the relevant previous years. The entire amount was allowed as deduction though these amounts were allowable in equal instalments spread over ten years. Thus Rs.7.14 lakhs only qualified for deduction. The excess deduction resulted in underassessment of income of Rs.64.25 lakhs involving short levy of tax of Rs.32.61 lakhs (including potential tax effect of Rs.3.54 lakhs).

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

Incorrect allowance of contribution to gratuity fund

3.10 Under the Income Tax Act, 1961, no deduction shall be allowed in respect of any provision for gratuity to employees on retirement or on termination of employment for any reason, unless it is by way of contribution towards an approved gratuity fund or for payment of gratuity that has become payable during the previous year. Further, with effect from the assessment year 1989-90, the assessing officer while processing the return of income under the summary assessment scheme, has to disallow any deduction claimed in the return, which on the basis of the information available in such returns and the accounts and documents accompanying it, is prima facie inadmissible. Any such disallowance attracts levy of additional tax also.

B-Summary Assessment

In processing the return of income of a widely held company, for the assessment year 1990-91 in a summary manner in November 1991, a sum of Rs.396.88 lakhs, debited in the accounts for the relevant previous year as provision for payment of gratuity, was allowed as a deduction. Audit scrutiny of the notes to accounts and balance sheet of the company revealed that the assessee did not have an approved gratuity fund. The deduction of Rs.396.88 lakhs was thus, not in order. As the mistake was apparent from accounts and notes accompanying the return of income, the amount of Rs.396.88 lakhs was required to be added back to income, by making the prescribed adjustments. Omission to do so resulted in excess computation and consequent excess carry forward of loss by an identical amount involving a potential tax effect of

Rs.214.32 lakhs. Besides additional income tax of Rs.42.86 lakhs was also leviable.

The Ministry has accepted the audit observation.

Incorrect allowance of bad debts

3.11 Under the Income Tax Act, 1961, as amended from April 1989, the amount of any bad debt or part thereof which is written off as irrecoverable in the accounts for 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 case of a banking company the amount of deduction relating to any such debt or part thereof shall be limited to the amount by which such debts or part thereof exceed the credit balance in the provision for bad and doubtful debts account, made under the Act.

In the assessment of a banking company, for the assessment year 1988-89, completed in a scrutiny manner in December 1989, deduction of Rs.294.72 lakhs was allowed towards bad and doubtful debts. As the deduction allowed in respect of bad debts should have been limited to the amount by which these exceeded the amount credited as provisions for bad and doubtful debts, a sum of Rs.55,437 only (Rs.294.72 lakhs minus Rs.294.17 lakhs) was allowable. Failure to restrict the allowance of bad debts written off resulted in under-assessment of income of Rs.294.17 lakhs with short levy of tax of Rs.154 lakhs.

The Ministry has accepted the audit observation.

Incorrect computation of income of a scheduled bank.

3.12 In the case of scheduled banks engaged in banking operations outside India which are approved by the Government for the purpose, the Income Tax Act, 1961, provides for a special deduction in the computation of their taxable income of the amounts transferred by them out of such 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 these provisions and under Chapter VIA of the Act.

The assessment of a nationalised bank for the assessment year 1987-88 was initially concluded after scrutiny in December 1988 after allowing the above deduction. This assessment was revised in February 1990 to

set off the carried forward loss, pertaining to the assessment year 1986-87 determined at Rs.136.05 lakhs in October 1989 while giving effect to appellate orders for that assessment year. However, the amount of special deduction was not revised on the basis of the total income as reduced by the loss. The mistake resulted in excess deduction of Rs.54.42 lakhs (40 per cent of Rs.136.05 lakhs) involving short levy of tax of Rs.27.21 lakhs.

The Ministry has accepted the audit observation.

Incorrect allowance of provisions

3.13.1 Under the Income Tax Act, 1961, a provision made in the accounts for an accrued or known liability is an admissible deduction, while other provisions made do not qualify for the deduction. A provision made in the accounts for doubtful debts is not an allowable deduction.

A-Scrutiny Assessment

(i) The assessments of a public sector undertaking engaged in life insurance business and other insurance business like capital redemption insurance for the assessment years 1989-90 and 1990-91, were completed in May 1990 and March 1992 respectively. The profits from capital redemption business based on actuarial valuation was computed after excluding the amounts of Rs.92.95 lakhs and Rs.103 lakhs in the two assessment years for probable increase in liability due to future variation in rates of exchange and for depreciation in the value of assets. As these amounts were in the nature of provisions towards future contingent liabilities, these were required to be included in the profit from capital redemption business. The failure to include these amounts resulted in underassessment of income of Rs.195.95 lakhs in the two assessment years 1989-90 and 1991-92 leading to an aggregate short levy of tax of Rs.108.02 lakhs.

The Ministry has accepted the audit observation.

(ii) A public limited company debited in its account in respect of the assessment year 1989-90 provisions for bad and doubtful debts of Rs.60.11 lakhs and Rs.28.07 lakhs, the latter amount being shown under the head miscellaneous expenditure. In the assessment made in March 1992. while the assessing

officer disallowed the amount of Rs.60.11 lakhs, he did not disallow the provision of Rs.28.07 lakhs included under the head 'miscellaneous expenditure'. This resulted in underassessment of income of Rs.28.07 lakhs and short levy of tax of Rs.26.23 lakhs (including interest).

The department has accepted the audit observation.

(iii) A public limited company, engaged in the manufacture of scooters, made a provision of Rs.22.87 lakhs in the accounts of the previous year relevant to the assessment year 1989-90 for meeting a liability on account of warranty claims. While completing the assessment in a scrutiny manner in February 1992, the assessing officer allowed the claim. As the warranties by nature are contingent and not ascertainable, the provision therefor was not an allowable deduction and should have been disallowed. Failure to do so resulted in under-assessment of income of Rs.22.87 lakhs involving short levy of tax of Rs.17.53 lakhs (including interest of Rs.5.52 lakhs).

The Ministry has accepted the audit observation.

(iv) A company, in its profit and loss accounts for the previous year relevant to the assessment year 1990-91, made a provision of Rs.26.69 lakhs for probable encashment of leave with wages and salaries on the basis of the leave earned but unavailed during the year. While completing the assessment in November 1991, the assessing officer allowed the said provision as a deduction. As the provision for probable encashment of leave is not an allowable deduction, there was consequent excess computation of loss by Rs.26.69 lakhs involving potential short levy of tax of Rs.15.85 lakhs.

The Ministry has accepted the audit observation.

B-Summary Assessment

3.13.2 Under the Income Tax Act, 1961, with effect from the assessment year 1989-90 the assessing officer while processing the return of income under the summary assessment scheme, has to disallow any deduction claimed in the return, which on the basis of the information available in such returns and the accounts and documents accompanying it, is

prima facie inadmissible. Any such disallowance attracts levy of additional tax also.

(i) The assessment of a Government company for the assessment year 1990-91 was completed in a summary manner in June 1991. The Auditor's report and documents accompanying the return indicated that the assessee had made a provision of Rs.138.33 lakhs in the relevant accounts to cover possible deterioration in stock in future years and doubtful debts. As the aforesaid provision made in accounts was not for accrued or known liability, the deduction was prima facie inadmissible. However, the assessing officer did not disallow the same leading to underassessment of income and consequent excess set off of losses of earlier years to the extent of Rs.138.33 lakhs involving potential tax effect of Rs.74.70 lakhs and non-levy of additional tax of Rs.14.94 lakhs.

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

(ii) The assessment of a widely held company, for the assessment year 1989-90 was completed in November 1991, in a summary manner at a loss of Rs.4646.37 lakhs. Audit scrutiny revealed that the assessing officer had allowed a deduction of Rs.96.83 lakhs in respect of provisions for doubtful debts, contingency, subsidy and loss on realisation of finished goods as claimed by the assessee. As these were mere provisions and not for ascertained liabilities, the amount of Rs.96.83 lakhs was not an allowable deduction. The information being readily available from the accounts and documents submitted with the return of income, the amount should have been disallowed while making the prescribed adjustments. Omission to do so resulted in excess carry forward of loss of Rs.96.83 lakhs involving a potential undercharge of tax of Rs.50.83 lakhs. Besides, additional income tax of Rs.10.17 lakhs was also leviable.

The Ministry has accepted the audit observation.

(iii) In the assessment of a company, for the assessment year 1991-92, completed in January 1992 under the summary assessment scheme, the company was allowed an amount of Rs.87.69 lakhs debited towards provision for trade

guarantees. As the guarantee is of contingent nature, the provision made therefor in the accounts was prime facie disallowable. Omission to do so resulted in underassessment of income of Rs.87.69 lakhs leading to short levy of tax of Rs.48.40 lakhs (including additional tax of Rs.8.07 lakhs).

The Ministry has accepted the audit observation.

(iv) The assessment of a widely held company, for the assessment year 1990-91, was completed in November 1991 in a summary manner, at a loss of Rs.8708.75 lakhs. An audit note accompanying the return revealed that provisions for 'doubtful advances' etc. of Rs.57.38 lakhs and for 'loss of stores' of Rs.9.78 lakhs were included in the amount of Rs.1300.93 lakhs debited under the head 'other expenses'. The above two items being mere provisions and not known or ascertained liabilities, were not admissible deductions. Failure to disallow the inadmissible provisions charged to accounts led to excess carry forward of loss of Rs.67.16 lakhs with consequent potential tax effect of Rs.36.27 lakhs and non-levy of additional income tax of Rs.7.25 lakhs.

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

3.13.3 The Income Tax Act, 1961, provides for allowance of deduction in respect of provisions for bad and doubtful debts made by a bank incorporated outside India of amount not exceeding five per cent of the total income.

In the assessment of a closely held company for the assessment year 1990-91, completed in August 1991 in a summary manner at Rs.29.77 lakhs, it was noticed from the accounts submitted by the assessee along with the return of income, that a sum of Rs.50.96 lakhs had been debited in the profit and loss accounts under the head 'operating expenditure' as per actuarial valuation on account of 'goods claim for losses and damages against the company, under litigation'. The amount, being of a contingent nature, should not have been allowed by the assessing officer till finalisation of the litigation. Omission to disallow the amount led to underassessment of income of Rs.50.96

lakhs with the resultant under-charge of tax of Rs.36.32 lakhs (including additional tax).

The Ministry has not accepted the audit observation on the ground that the assessment was completed in a summary manner. The reply is not tenable as the information regarding the claims being under litigation was available from the documents accompanying the return of income.

Incorrect allowance of liability

3.14.1 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 provident fund, etc. is allowable unless such sum has actually been paid before the stipulated due date. 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.

A-Scrutiny assessment

(i) The assessment of a widely held company for the assessment year 1989-90 was completed in March 1992 at a total income of Rs.1665.68 lakhs. Audit scrutiny revealed that sales tax of Rs.406.54 lakhs collected from customers, but remaining unpaid to government, was not included in computing the business income of the assessee. As the amount was not paid to government account during the relevant previous year or before the filing of the relevant return of income, it should not have been allowed as a deduction. The mistake led

* 87-ITR-542 (SC), 97-ITR-615 (SC)

to short computation of income by Rs.406.54 lakhs involving undercharge of tax of Rs.390.23 lakhs (including interest).

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

(ii) In the assessment of a widely held company, for the assessment year 1988-89, completed in March 1991 at a loss of Rs.311.69 lakhs, a liability for provident fund contribution amounting to Rs.21.50 lakhs was charged to the accounts of the relevant previous year. Audit scrutiny revealed that the sum was not deposited with the appropriate authority within the stipulated period and should therefore have been disallowed. Omission to disallow the unpaid liability led to excess determination of loss and its carry forward amounting to Rs.21.50 lakhs with a potential tax effect of Rs.11.29 lakhs.

The Ministry has accepted the audit observation.

(iii) In the assessment of a public sector company for the assessment year 1985-86, completed in August 1988 at a loss of Rs.3615.19 lakhs, an amount of Rs.54.87 lakhs debited in the profit and loss account towards 'provision for sales tax set off' was allowed as a deduction while computing the business income. As the amount debited in accounts was not towards actual payment of sales tax it should have been disallowed. Omission to do so resulted in under-assessment of income of Rs.54.87 lakhs involving a notional short levy of tax of Rs.27.43 lakhs.

The Ministry has accepted the audit observation.

(iv) The assessment of a company for the assessment year 1986-87 was completed in a scrutiny manner in March 1989. Audit scrutiny revealed that a provision of Rs. 38.66 lakhs was made in the accounts for the year towards set off of sales tax. As these amounts were not paid during the relevant previous year, it was not an allowable deduction in the computation of income. The incorrect allowance resulted in under-assessment of income of Rs. 38.66 lakhs leading to potential short levy of tax of Rs. 20.30 lakhs.

Subsequent to the audit observation, the assessment has been rectified.

(v) In the assessments of a company for the assessment years 1987-88 and 1988-89, completed in March 1990 and February 1991 respectively, unpaid liabilities on account of West Bengal luxury tax, amounting to Rs.12.37 lakhs and Rs.15.65 lakhs respectively were not brought to tax. Omission to do so resulted in excess computation of loss of Rs.12.37 lakhs in assessment year 1987-88 and underassessment of income by Rs.15.65 lakhs in the assessment year 1988-89 leading to aggregate tax effect of Rs.19.68 lakhs in the two years.

The department has accepted the audit observation.

**B-Summary
Assessment**

3.14.2(i) In the accounts for the previous year corresponding to the assessment year 1989-90, a widely held company credited the profit and loss account with a notional income of Rs.6477.81 lakhs, representing the differential price receivable on its product, subject to its later ratification. This was not finalised till the end of the previous year. It was also seen from the tax audit report that a sum of Rs.1398.64 lakhs, representing estimated excise duty on the notional value, was included in the aforesaid sum of Rs.6477.81 lakhs and was debited to the profit and loss account, as estimated liability for excise duty. The said duty was neither finalised nor paid within the accounting year nor was there any evidence of finalisation and payment of the excise duty up to the date of submission of return. The assessment for the aforesaid assessment year was completed in a summary manner in September 1990 and later rectified in November 1990 at Rs.726.69 lakhs. While doing so the assessing officer did not disallow the said liability of Rs.1398.64 lakhs which led to under-charge of tax of Rs.992.91 lakhs (including additional tax and interest).

The Ministry has accepted the audit observation.

(ii) The assessments of a widely held company, for three assessment years 1987-88 to 1989-90, were completed in a summary manner in February 1990 computing losses at Rs.92.91 lakhs, Rs.141.73 lakhs and Rs.92.27 lakhs respectively. The accounts and audit

report available in the relevant assessment records revealed that provident fund dues of Rs.36.52 lakhs for the assessment year 1987-88, Rs.37.83 lakhs for the assessment year 1988-89 and Rs.98.20 lakhs for the assessment year 1989-90 were not deposited by the assessee company with the trustees of the fund during the relevant previous years. Moreover, sales tax of Rs.95.22 lakhs and employees' state insurance dues of Rs.78.70 lakhs for the assessment year 1989-90 were also not deposited with the respective authorities within the stipulated due date. Thus, the aforesaid amounts were required to be disallowed while computing income for the relevant assessment years. Omission to do so resulted in irregular carry forward of loss of Rs.36.52 lakhs, Rs.37.83 lakhs and Rs.272.12 lakhs in assessment years 1987-88, 1988-89 and 1989-90 involving an aggregate potential under-charge of tax of Rs.170.71 lakhs for the above three assessment years and positive under-charge of tax of Rs.41.10 lakhs (including additional tax and interest).

The Ministry has accepted the audit observation.

(iii) Assessment of a widely held company, for the assessment year 1989-90 was completed in April 1990 in a summary manner. Audit scrutiny revealed that an amount of Rs.68.36 lakhs debited to profit and loss account under the head contribution to provident fund, pension and welfare fund for the extended previous years from 1 August 1987 to 31 March 1989, was not paid to the credit of respective authorities within the prescribed dates. Thus, the amount of Rs.68.36 lakhs was required to be disallowed. Omission to do so resulted in excess computation and consequent excess carry forward of loss by Rs.68.36 lakhs involving a potential tax effect of Rs.35.89 lakhs and additional tax of Rs.7.18 lakhs.

The Ministry has accepted the audit observation.

(iv) In the assessment of a widely held company for the assessment year 1989-90, completed in a summary manner, at a loss of Rs.8835.05 lakhs in March 1990 (revised in February 1991), provisions for provident fund contribution of Rs.50 lakhs, electricity consumption tax of Rs.13.16 lakhs and customs

duty of Rs.11.23 lakhs were allowed. Audit scrutiny revealed that the above dues were not actually paid either in the relevant previous year or before the due date for filing the return of income. The tax audit report also specifically mentioned about the non-payment of statutory dues. Omission to disallow these amounts resulted in excess carry forward of loss by Rs.74.42 lakhs involving tax effect of Rs.46.88 lakhs (additional tax of Rs.7.81 lakhs and potential tax of Rs.39.07 lakhs).

The Ministry has accepted the audit observation.

(v) In the assessment of a widely held company, for the assessment year 1986-87, completed in a summary manner, in March 1989, a sum of Rs.35.25 lakhs was allowed by the assessing officer on account of taxes and duties, though the amount was not paid to the concerned authorities within the stipulated period. The amount was, therefore, required to be added back to the income of the assessee. Omission to do so resulted in excess computation and consequent excess carry forward of loss of Rs.35.25 lakhs involving a potential tax effect of Rs.18.50 lakhs.

The Ministry has accepted the audit observation.

3.14.3 Under a scheme envisaged in a notification of 1979 under the Customs Act, an assessee can import goods without payment of customs duty on fulfilment of certain prescribed conditions. Breach of the stipulated conditions by the importer entails payment of customs duty on such imported goods.

The assessment of a company for the assessment year 1989-90 was completed in February 1990 under the summary assessment scheme. Audit scrutiny revealed that during the relevant previous year, the company had imported polyester fibre without payment of customs duty under the duty exemption scheme. As per the tax audit report filed along with the return, the company had made a provision of Rs.52.53 lakhs towards customs duty that would be payable in the eventuality of the conditions for exemption not being

fulfilled. Since the duty of Rs.52.53 lakhs was not actually paid, the provision thereof was prima facie inadmissible and should have been disallowed. Omission to do so resulted in underassessment of income of Rs.52.53 lakhs involving potential short levy of tax of Rs.30.33 lakhs, apart from additional tax of Rs.6.06 lakhs.

The Ministry has accepted the audit observation.

Incorrect valuation of closing stock

3.15 Under the Income Tax Act, 1961, the income of an assessee from business or profession shall be computed in accordance with the method of accounting regularly employed by the assessee. Where the accounts are correct and complete to the satisfaction of the assessing officer, 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 he may determine. If closing stock does not include any element of cost which should be taken into account, the assessing officer should conclude that the accounts do not reflect the true profit and should bring the undervaluation of stock to tax.

The assessment of a closely held company, dealing in real estate, for the assessment year 1989-90, was completed in a scrutiny manner in March 1992 at a loss of Rs.106.76 lakhs. Audit scrutiny revealed that the closing stock included a property acquired at Rs.188.81 lakhs. This value was worked out after taking into account the cost of land, building, construction expenses and sanction fee to the municipal authority, but excluding the amount of Rs.104 lakhs paid to the tenants towards compensation for vacating the premises and surrender of their tenancy rights. As the said amount of Rs.104 lakhs was debited to profit and loss accounts and was part of the cost of acquisition of the right on the property its exclusion from the value of closing stock resulted in excess carry forward of loss by an identical amount involving potential tax effect of Rs.65.52 lakhs.

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

Other mistakes in the computation of business income

3.16.1 Under the Income Tax Act, 1961, any expenditure incurred wholly and exclusively for the purposes of business is allowable as deduction in computing the business income of an assessee provided the expenditure is not in the nature of capital or personal expenses of the assessee. It has been judicially held* that the entire price paid for securities is a capital outlay. Consequently, the Board's circular issued in April 1991 treating securities held by a banking company as its stock-in-trade, instead of investment and allowing loss on revaluation in the computation of business income debited to books of accounts were withdrawn in August 1991.

A-Scrutiny Assessment

(i) A banking company, revalued its investments at the end of the previous year and debited the loss on revaluation amounting to Rs.118.12 lakhs to its accounts. The claim was allowed in assessment for the assessment year 1983-84 completed in March 1986 treating the same as a business loss. It was pointed out in audit that the loss was not an actual loss but was a notional one on capital account which was required to be disallowed. Omission to disallow the same resulted in under-assessment of income by Rs.118.12 lakhs with short levy of tax of Rs.98.47 lakhs (including interest on short payment of advance tax).

Subsequent to the audit observation, the department disallowed the amount in the fresh assessment.

(ii) The assessment of a public limited company, for the assessment year 1989-90, was completed in March 1992 at an income of Rs.54.07 lakhs. Audit scrutiny revealed that the assessee company had paid lump sum contribution of Rs.42.67 lakhs to Bhilwara Export Development Fund and debited it to the relevant profit and loss account which was allowed as revenue expenditure by the assessing officer. As the contribution made to Export Development Fund was not an expenditure incurred for business consideration, the expenditure was not allowable. Omission to disallow the same resulted in underassessment of income of Rs.42.67 lakhs and short levy of tax of Rs.22.40 lakhs.

* 187-ITR-541(SC)

The department has accepted the audit observation.

**B-Summary
Assessment**

3.16.2 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 profit as a deduction from the total income.

In the assessment of a company, for the assessment year 1990-91, completed in February 1991 under the summary assessment scheme, the assessee company claimed deductions of Rs.46.94 lakhs and Rs. 1.78 lakhs being the amounts of tax paid in the assessment years 1988-89 and 1989-90, under the special provisions for levy of minimum tax on companies on their book profits. As the Act did not provide for deduction of such amounts in the following years, the claim should have been disallowed. Failure to do so resulted in underassessment of income of Rs.48.72 lakhs leading to short levy of tax of Rs.31.57 lakhs, including additional tax.

The Ministry has not accepted the audit observation on the ground that the income was determined under regular provisions and not under section 115J of the Income Tax Act, 1961. The reply is not tenable. Under section 40(ii) of the Act deduction of the tax paid in any earlier assessment year under the special provision of the section 115J cannot be allowed in the computation of business income.

**Mistakes in
the
allowance of
depreciation**

3.17 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 per cent to 100 percent are prescribed for certain specified items of machinery and plant. A general rate of 10 percent (15 per cent from assessment year 1984-85) is prescribed in 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 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 calculated at the percentage, on the written down value of such assets, prescribed under this Act immediately before the commencement of the Taxation Laws (Amendment) Act, 1991.

A large number of mistakes in the computation and application of the law on depreciation in the assessments of companies were noticed in test audit during the year. The important among such mistakes noticed are shown below:

Sl. No.	CIT charge	Assessment year	Section under which assessed	Nature of mistake	Tax effect (in lakhs of rupees)
1.	Ranchi	1988-89	143(3)	Grant of depreciation of Rs.58.95 lakhs at 50 per cent on plant and machinery instead of the correct amount of Rs.39.30 lakhs. Underassessment Rs.19.65 lakhs.	10.61 (P)
2.	Tamil Nadu IV Madras	1989-90	143(3)	Grant of higher rate of depreciation of 50 percent instead of 33.33 percent. Under-assessment of Rs.19.53 lakhs.	10.26 (P)

The reply of the Ministry has not been received so far.

Allowance of depreciation though the assets not used for business

3.18 It has been held judicially* that the expression 'used for the purpose of business' means that the asset must be used by the owner for purpose of carrying on the business and earning profit therefrom. If the assets have not at all been used for any part of the accounting year, no depreciation can be claimed.

The assessment of a widely held company for the assessment year 1989-90 was completed in February 1992, in a scrutiny manner, determining taxable income at Rs.22.79 lakhs and unabsorbed depreciation of Rs. 561.75 lakhs was allowed to be carried forward. The unabsorbed depreciation included depreciation allowed to the assessee for additions to plant and machinery of the aggregate value of Rs.124.56 lakhs made during the previous year relevant to the assessment year 1989-90. It was admitted by the assessee in January 1990, that he had put to use plant and machinery valued at Rs.70.85 lakhs only during the relevant previous year, leaving a balance of Rs.53.71 lakhs which was the value of machinery not put to use at all. As depreciation is allowed only when there is actual use of the plant and machinery in business, depreciation of Rs.22.38 lakhs allowed on plant and machinery of the value of Rs.53.71 lakhs was irregular. This led to excess carry forward of depreciation of Rs.22.38 lakhs involving potential tax effect of Rs.11.75 lakhs.

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

Erroneous allowance of depreciation on fluctuations in exchange rates

3.19 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 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.

(i) The assessment of a company, for the assessment year 1989-90, was completed in January 1992, computing taxable income of Rs.1425.12 lakhs under the special provisions of the Act. It was seen from the notes forming part of the accounts that the additions to the assets on which the depreciation was claimed, included Rs.1269.37 lakhs towards increase in liability on foreign loans on account of exchange rate difference. This liability, not having been discharged, should neither have been added to the cost of asset nor depreciation allowed on such additions. The addition of Rs.1269.37 lakhs to the cost of machinery resulted in excess allowance of depreciation of Rs.444.28 lakhs leading to potential short levy of tax of Rs.233.25 lakhs.

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

(ii) Assessment of a widely held domestic company, for the assessment year 1989-90, was completed in March 1992, allowing depreciation of Rs.460.02 lakhs, as claimed by the assessee. The company had made additions of Rs.141.95 lakhs in the assessment year 1989-90 to the cost of plant and machinery on account of increase in liability payable in foreign currency, consequent upon change in the rate of exchange. On the enhanced cost of Rs.141.95 lakhs, the assessee was allowed depreciation of Rs.90.68 lakhs. As the additions to the cost of plant and machinery were made on account of intermediate fluctuations in the rate of exchange and not at the time of repayment of loan, depreciation allowance allowed was irregular and resulted in excess carry forward of loss of Rs.90.68 lakhs involving potential tax effect of Rs.47.61 lakhs.

The Ministry has accepted the audit observation.

Allowance of depreciation in excess of the cost of assets

3.20.1 Under the Income Tax Act, 1961, in computing the business income of an assessee, a deduction on account of depreciation is admissible at the prescribed rates on plant and machinery and other assets, provided these are owned by the assessee and used for the purpose of his business during the relevant previous year. From 1 April 1989, the financial year uniformly became the relevant previous year. As a transitional arrangement, it was provided that for the assessment year 1989-90, depreciation can be proportionately increased if income under the head 'profits and gains of business or profession' included in the total income is for a period of thirteen months or more. This increase is, however, not admissible where 100 percent depreciation is allowed on any block of the assets as per the rates schedule. The Board, in circular issued in October 1989, clarified that while allowing depreciation, the total amount of depreciation allowed during the extended transitional previous year, including the depreciation allowed in earlier years, should not exceed the actual cost of the asset.

A-Scrutiny Assessment

In the case of a widely held company, the assessment for assessment year 1989-90 was completed in March 1992 in a scrutiny manner. The assessee company's transitional previous year covered 17 months. The company made additions to energy saving machinery at a cost of Rs.69.64 lakhs, during the previous year, for which depreciation at the rates of 100 per cent, has been prescribed in the Rules. Audit scrutiny revealed that the assessee was allowed proportionate increase in the amount of depreciation in respect of this block of assets also, even though the depreciation thereby exceeded the cost of the assets. The mistake resulted in excess grant of depreciation of Rs.29.02 lakhs involving short levy of tax of Rs.15.23 lakhs.

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

B-Summary Assessment

3.20.2 The assessment of a company for the assessment year 1989-90, was completed in a summary manner, in September 1990. The assessee company's transitional previous year comprised 15 months. The company made additions to plant and machinery at a cost of Rs.177 lakhs during the previous year, for

which depreciation at the rate of 100 per cent has been prescribed in the Rules. Audit scrutiny revealed that the assessee was allowed proportionate increase in the amount of depreciation in respect of this block of assets also, even though the depreciation thereon exceeded the cost of the assets. The mistake resulted in excess grant of depreciation of Rs.44 lakhs involving short levy of tax of Rs.36 lakhs including additional tax and interest.

The department has accepted the audit observation.

**Mistake in
written down
value**

3.21 Under the Income Tax Act, 1961, depreciation on building, 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. From assessment year 1984-85, initial depreciation allowed on hotel buildings is deductible in determining the written down value of the buildings.

A widely held company, engaged in the business of running hotels, was allowed initial depreciation aggregating Rs.270.24 lakhs during the assessment years 1973-74 to 1978-79. In the assessment for the assessment year 1986-87, as revised in March 1992, the assessing officer allowed depreciation without deducting the initial depreciation granted in the earlier assessment years, as required under the amended provisions of the Act. The omission led to excess allowance of depreciation of Rs.24.12 lakhs with consequent underassessment of an identical amount involving under-charge of tax of Rs.12.66 lakhs.

The Ministry has not accepted the audit observation on the ground that initial depreciation will not reduce the written down value of the assets but will be taken into account in the year in which the asset is sold, demolished or destroyed. The argument is not tenable as according to the amended provision of section 32(i)(v) of the Income Tax Act 1961, effective from April 1, 1984, and also Board/s circular of October 1983, the initial depreciation allowed has to be taken into account in determining its written down value.

**Depreciation
for
transitional
period**

3.22 The Direct Tax Laws (Amendment) Act, 1987, provided for certain special provisions for the computation of total income of the transitional previous year relevant to the assessment year 1989-90, which may, in certain circumstances exceed twelve months. It provided, inter alia, for the allowance of increased depreciation in respect of the block of assets and where more than one period in respect of income under the head 'profits and gains of business or profession' are included, the depreciation allowance shall be calculated separately for each such period and increased, where necessary, by multiplying it by a fraction of which the numerator is the number of months in such period and the denominator is 12. The intention was to remove hardships faced by tax payers for compulsory change over of the previous year and accordingly, assets in use for 13 months or more in the relevant previous year would get the benefit of proportionately higher depreciation and where these are used for less than 13 months, the benefit would be restricted to 12 months only.

(i) A closely held company, running a distillery unit, was regularly closing its accounts on 30th June every year. During February 1989, the company started a textile unit. As per the amended provisions of the Act, the company furnished its return of income for the transitional previous year relevant to the assessment year 1989-90, admitting income from the distillery business for 21 months from 1 July 1987 to 31 March 1989 and income from the textile business for 45 days from 15 February 1989 to 31 March 1989. The assessment was completed in March 1992 on a total income of Rs.204.89 lakhs. Audit scrutiny revealed that the assessee company was allowed depreciation for 21 months involved in the previous year in respect of the assets of both the units. The amount included depreciation of Rs.564.46 lakhs relating to the textile unit. As the textile unit was started only in February 1989, the assessee was eligible for depreciation in respect of the assets of the textile unit for only twelve months which worked out to Rs.322.55 lakhs. The mistake resulted in underassessment of income of Rs.241.91 lakhs involving short levy of tax of Rs.240.29 lakhs including interest.

(ii) A widely held company, having five independent units consisting of sugar, distillery, hybrid seed, etc., was regularly closing its accounts on 30th September every year. In March 1989, the company started a new sugar unit at Sivaganga. As per the amended provisions of the Act, the company furnished its return of income for the transitional previous year relevant to the assessment year 1989-90, admitting income from the five units for 18 months from October 1987 to March 1989 and from the newly started sugar unit for 12 days from 20 March 1989 to 31 March 1989. In the assessment completed in March 1992, depreciation was allowed on all the assets of all the units for 18 months including the new unit at Sivaganga. As the new unit had worked only for 12 days, depreciation was to be allowed for 12 months as per the amended provisions. The excess depreciation allowed worked out to Rs.268.96 lakhs resulting in a potential tax effect of Rs.141.20 lakhs.

The Ministry has not accepted the audit observation stating that the depreciation was correctly allowed under section 32(1)(ii) read with section 3(2) and 3(3) of the Act and rule 5 of 10th schedule to the Act. The argument is not tenable as the new units of the assessee came into operation only in the previous year 1988-89, relevant to assessment year 1989-90. In such case, in terms of section 3(3), Rule 5 of tenth schedule will not apply, and hence depreciation will have to be restricted to 12 months only.

Incorrect grant of deduction in respect of investment allowance/ deposit account

3.23 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 in the previous year of first usage, of a sum equal to 20 per cent (25 per cent up to the assessment year 1988-89) of the actual cost of the machinery to the assessee.

The regular assessment of a closely held company, for the assessment year 1989-90, was completed in March 1992, allowing carry forward of unabsorbed loss of Rs.371.92 lakhs for future set off. While completing the assessment, investment allowance of Rs.75 lakhs was allowed at the rate of 25 per cent, on machinery worth Rs.299.99 lakhs as against the admissible amount of Rs.60 lakhs, the rate

of 20 per cent of the cost of the plant and machinery. This resulted in excess allowance of investment allowance of Rs.15 lakhs involving a tax effect of Rs.16.19 lakhs, including interest.

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

**Non-creation
of reserve**

3.24.1 Under the Income Tax Act, 1961, a deduction by way of investment allowance is allowed at the rate of twenty per cent of the actual cost of new machinery and plant installed during the relevant previous year in any industrial undertaking and used for the purpose of the business by the assessee. The Act also provides that the admissible investment allowance shall be an amount which is sufficient to reduce the said total income to nil, provided seventyfive per cent of the allowance claimed as deduction is debited to the profit and loss account, and credited to a reserve account.

In the assessment of a company in which public are not substantially interested, for the assessment year 1989-90, completed in March 1992, the assessing officer allowed investment allowance of Rs.20.09 lakhs. Audit scrutiny revealed that a reserve of Rs.20.24 lakhs was created by debiting the profit and loss appropriation account instead of the profit and loss account. Hence the investment allowance of Rs.20.09 lakhs was erroneously allowed, resulting in short levy of tax of Rs.11.61 lakhs.

The reply from the Ministry has not been received so far.

3.24.2 Under the Income Tax Act 1961, a tax-payer 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 with the prescribed Development Bank within a period of six months from the end of previous year or before the submission of the return, whichever was earlier, or had utilised any amount during the previous year for the purchase of new ship, new aircraft, new machinery, or plant, 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.

Some major cases of mistakes resulting in substantial tax effect are shown below:

Sl. No.	Commissioner's charge	Assessment year	Nature of mistakes	Tax effect (in lakhs of rupees)
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A-Scrutiny Assessment

1.	West Bengal III Calcutta	1990-91	Eligible profit included tax-free interest of Rs.226.54 lakhs and dividend income of Rs.339.14 lakhs. Underassessment of income Rs.112.44 lakhs.	90.47
2.	Bombay city III Bombay	1987-88	Eligible profit included income from house property of Rs. 40.81 lakhs, dividends of Rs.105.00 lakhs and interest from securities of Rs.17752.00 lakhs. Underassessment Rs.2879.00 lakhs.	2141.00
3.	West Bengal III Calcutta	1988-89 1989-90	Eligible profits included income from investments of Rs.338.46 lakhs. Underassessment of Rs.50.73 lakhs.	26.79

B-Summary Assessment

4.	Patiala	1990-91	Amount of Rs.321.14 lakhs credited in profit and loss account towards excess provision written back and dividend income were not considered while calculating eligible profit. Underassessment of Rs.43.10 lakhs.	23.28
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The Ministry has accepted the audit observation at Sl.No.1 & 3. The Ministry has not accepted the audit observation at Sl. No. 4 on the ground that the assessment was completed under the summary assessment scheme. The reply is not acceptable as the method of calculation has been clearly provided in the provision itself and a prima facie adjustment should have been made.

3.24.3 Under the Income Tax Act 1961, while computing the business income of an assessee, a deduction by way of investment deposit account, of a sum equal to the amount deposited and utilised in the prescribed manner or twenty per cent of the profits of business or profession, whichever is less is allowed as a deduction. However this deduction was withdrawn under the provisions of the Finance Act 1990, with effect from 1 April 1991.

B-Summary Assessment

In the assessment of a widely held tea company for the assessment year 1991-92, completed in a summary manner in January

1992, deduction towards investment deposit account of Rs.418.76 lakhs was claimed and allowed. However, the assessee was not entitled to the same for the assessment year 1991-92, as the provision for the deduction was no longer operative. The incorrect grant of deduction resulted in underassessment of income by Rs.167.50 lakhs (being 40 per cent of Rs.418.76 lakhs) involving short levy of tax of Rs.99.39 lakhs, including additional tax and interest.

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

3.24.4 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 the deduction is claimed, have been audited by an accountant and the assessee furnishes, along with the return of income, the report of such audit in the prescribed form duly signed and verified by such accountant.

In the assessments of a state financial corporation, for the assessment years 1987-88 and 1989-90, completed in March 1992, deduction towards investment deposit amount amounting to Rs.28.00 lakhs and Rs.37.60 lakhs respectively was allowed by the assessing officer on the basis of computation chart signed by the Managing Director of the company. Audit scrutiny revealed that the audit reports in the prescribed form duly signed and verified by the accountant as required under the provisions of the Act were not furnished along with the returns of income. Accordingly, the deduction was wrongly allowed. The mistake resulted in under-assessment of income of Rs.65.60 lakhs and short levy of tax of Rs.59.55 lakhs (including interest).

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

**Incorrect
computation
of capital
loss**

3.25 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 deemed to 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. These deductions shall be made also for the purposes of computing any loss under the head 'capital gains'.

In the assessment of a company for the assessment year 1991-92, completed in March 1992, the loss under the head 'capital gains' was computed without reducing the loss by the deductions specified under the Act. The loss worked out to Rs.100.90 lakhs as against Rs.252.35 lakhs actually allowed. The excess allowance of loss of Rs.151.45 lakhs resulted in potential short levy of tax of Rs.87.08 lakhs.

The Ministry has accepted the audit observation.

Income not assessed

3.26.1 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 employed by the assessee. Where an assessee follows the 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 all expenditure incurred and the liability relating to the period regardless of their actual receipt or payment. It has been judicially held* that interest on 'sticky' advances that had accrued according to mercantile system of accounting is to be treated as income and brought to tax.

(i) In the assessment for the assessment year 1990-91 in respect of a public sector company engaged in general insurance business, accrued interest of Rs.466.00 lakhs on 'sticky loans' was not credited to the profit and loss account. The amount was also not included in the total income and brought to tax. The omission resulted in under-assessment of income of Rs.466.00 lakhs involving short levy of tax of Rs.252.15 lakhs.

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

* 158-ITR-102

(ii) The income tax assessment of a widely held company for the assessment year 1987-88 was completed in May 1989 at a total loss of Rs.1137.08 lakhs being unabsorbed depreciation. Notes on accounts for the previous year ending 31 March 1987 relevant to the assessment year 1987-88 indicated that power sales of the assessee company during the relevant previous year did not include the sum of Rs.268.41 lakhs realisable from a State Electricity Board on account of increased rate of tariff effected by the assessee company with effect from 1 December 1982 as the same was not accepted by the State Electricity Board. The dispute with regard to increased tariff from 1 December 1982 was, however, settled through a memorandum of agreement reached between the two parties on 7 September 1987 deciding that the increased rate of tariff would be effective from the consumption month of August 1985. Thus the increase in the rate of tariff was effective during the entire previous year (1986-87) of the assessee company. The assessment for the assessment year 1987-88 was completed in May 1989 subsequent to signing of the memorandum of agreement. Since the assessee company was maintaining mercantile system of accounting, the accrued income of Rs.268.41 lakhs should have been taken into account in the computation of income of the assessee company for the assessment year 1987-88. Omission to do so resulted in under-assessment of income of Rs.268.41 lakhs in the assessment year 1987-88 leading to excess computation of loss representing excess carry forward of unabsorbed depreciation by a like sum involving a potential tax effect of Rs.134.21 lakhs.

The Ministry has accepted the audit observation.

3.26.2 It has been judicially held* that the amount of sales tax collected by a trader in the course of business constitutes his trading receipts and is to be included in his total income. If and when the assessee paid the amount so collected to State Government or refunded any part thereof to the purchaser, the assessee would be entitled to claim deduction of the sum paid or refunded.

* 87-ITR-542

The assessment of a company for the assessment year 1989-90 completed under the summary scheme in February 1990 was rectified in March 1991 to include an amount of Rs.30.85 lakhs being excise duty collected but not paid to Government account. Additional tax of Rs.3.84 lakhs was also levied for omission to include the amount collected as taxes. However, in the scrutiny assessment completed in March 1992, the above amount of Rs.30.85 lakhs was not included in the taxable income though the additional tax of Rs.3.84 lakhs was levied. The mistake resulted in excess computation of loss of Rs.30.85 lakhs leading to potential short levy of tax of Rs.17.82 lakhs.

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

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

The assessee, a widely held company, had obtained loans from Government, the accrued interest on which, was regularly debited to the profit and loss accounts of the relevant previous year and on the other hand, the interest subsidy received or receivable from Government was credited to such account. The profit and loss appropriation account for the previous year ending 31 March 1988, relevant to the assessment year 1988-89 had a credit of Rs. 666.20 lakhs described as adjustment of earlier year's income and expenditure which was not included in the assessment for the assessment year 1988-89. The break-up of the credit showed earlier year's income of Rs. 1887.26 lakhs and expenses of Rs. 1221.06 lakhs. Further, the income of Rs. 1887.26 lakhs included the amount of interest/ interest subsidy receivable from Government to the extent of Rs. 1588.21 lakhs. The assessment records indicated that the interest subsidy was in respect of the amount

of accrued interest liability charged to accounts of the previous years relevant to the assessment years 1985-86, 1986-87 and 1987-88 and allowed as deduction in the computation of income of these assessment years. The grant of the interest subsidy wiped off the interest liability of the assessee for the aforesaid assessment years to the extent of Rs. 1588.21 lakhs. As the assessee obtained the benefit in respect of a liability by way of cessation of the same through grant of the subsidy, the benefit so obtained should be deemed to be profit and gains of business, and charged to income-tax as income of the previous year ending 31 March 1988 relevant to assessment year 1988-89. Due to the omission of the assessing officer to do so, there was an underassessment of Rs. 809.57 lakhs and irregular carry forward of loss of Rs. 778.64 lakhs. This led to consequential undercharge of tax of Rs. 425.02 lakhs and potential tax effect of Rs. 408.79 lakhs aggregating Rs.833.81 lakhs.

The Ministry has accepted the audit observation.

**Incorrect
set off and
carry
forward of
losses**

3.27.1 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 under any other head of income, so much of the loss as has not been set off shall, subject to other provision of the Act, be carried forward for adjustment in the following assessment year. Where any part of the business of a company (other than an investment, a banking or a financial company) consists in the purchase and sale of shares of other companies, such company shall be deemed to be carrying on a speculation business to the extent to which the business relates to purchase and sale of shares.

**A-Scrutiny
Assessment :**

(i) In the assessment of a private limited company for assessment year 1988-89, completed in February 1991 in a scrutiny manner, total loss of Rs.67.72 lakhs was allowed to be carried forward for set off against future income out of which loss of Rs 1.29 lakhs related to the current assesment year 1988-89 and the balance of Rs 66.43

lakhs to the earlier years. Scrutiny in audit disclosed that earlier assessments were completed on positive incomes and there was no loss left to be carried forward for set off against future income. Carry forward of the amount of Rs.66.43 lakhs being loss pertaining to earlier years was therefore incorrect. The mistake resulted in excess carry forward of business loss of Rs.66.43 lakhs with potential short levy of tax of Rs.38.36 lakhs.

The department has accepted the audit observation.

(ii) No loss under the head 'profit and gains of business or profession' is allowed to be carried forward from 1 April 1985 for set off unless the assessee had filed the return of loss voluntarily within the due date or within such further time as may be allowed by the assessing officer.

In the case of a closely held company whose previous year in respect of assessment year 1985-86 ended in December 1984, the stipulated date of submission of return was 30 June 1985. The assessee however submitted the return on 19 February 1986 and the belated submission was not covered by extension of time. In the assessment completed in May 1987, the business loss of Rs.16.60 lakhs was allowed to be carried forward. As the loss was not determined in pursuance of a return submitted within the stipulated time as prescribed in the Act, the carry forward of loss allowed in the aforesaid assessment was irregular. This led to a potential tax effect of Rs.10.46 lakhs.

The Ministry has accepted the audit observation.

**B-Summary
Assessment**

3.27.2 Under the amended provision of the summary assessment scheme, applicable with effect from 1 April 1989, adjustment shall be made to the income of the assessee, inter-alia, in regard to any loss carried forward, deduction allowance or relief, which is prima facie admissible or inadmissible. Though the provisions of the Act required adjustments to be made on account of brought forward losses and allowances which needed reference to assessment records of earlier years, these could not be carried out as the Act does not provide for reference to such earlier records. The anomaly needs to be resolved.

(i) The return filed by a widely held company for the assessment year 1990-91 in December 1990, was processed under the summary assessment scheme in June 1991 determining a loss of Rs.708.11 lakhs which was allowed to be carried forward. The above loss included, inter alia, Rs.61.29 lakhs relating to the assessment year 1988-89 which had not been allowed by the assessing officer to be carried forward. Thus the loss of Rs.61.29 lakhs disallowed in 1988-89 was irregularly allowed in the assessment year 1990-91. This led to potential revenue effect of Rs.33.10 lakhs apart from non-levy of additional income-tax of Rs.6.62 lakhs.

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

(ii) A widely held company filed its return of loss of Rs.38.89 lakhs for the assessment year 1988-89 on 29 July 1988 against the due date of 30 June 1988 without seeking extension of time. The business loss was assessed under the summary assessment scheme at Rs.38.90 lakhs which was allowed to be carried forward for set off against future profits. As the return of loss was filed beyond the prescribed due date, the benefit of carry forward of loss was not admissible. The irregular carry forward involved potential tax effect of Rs.20.42 lakhs.

The Ministry has accepted the audit observation.

(iii) The total income of a closely held company for the assessment year 1990-91 was determined at Rs.26.00 lakhs by processing the return of income considering set off of loss of Rs.15.65 lakhs pertaining to the assessment year 1989-90. The assessment for the assessment year 1989-90 was, however, revised in March 1992 determining a total income of Rs.1.03 lakhs as against the loss of Rs.15.65 lakhs arrived at earlier by processing the return of income for that year in June 1990. Since the assessment for the assessment year 1989-90 was revised at a total income of Rs.1.03 lakhs subsequent to the filing of the return for the assessment year 1990-91, the income processed for the year 1990-91 was required to be revised as a result of aforesaid variation and a revised intimation sent as per provision of the Act. Omission to do so resulted in under-assessment of income of Rs.15.65 lakhs with

consequent under-charge of tax of Rs.12.27 lakhs (including interest of Rs.2.97 lakhs for short payment of advance tax).

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

3.27.3 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.

Assessment of a widely held company for the assessment year 1990-91 was completed in June 1991 in a summary manner. In the assessment an unabsorbed loss of Rs. 544.10 lakhs was allowed to be carried forward. The above loss included unabsorbed business loss of Rs. 9.73 lakhs and unabsorbed depreciation of Rs. 12.93 lakhs for the assessment year 1989-90. However, in the order of scrutiny assessment for the assessment year 1989-90 made in January 1992, there being no business loss, unabsorbed depreciation of Rs. 1.03 lakh only was allowed to be carried forward for future set off. Since scrutiny assessment for the assessment year 1989-90 was completed after the date of filing of return of income for the assessment year 1990-91 in December 1990, the order determining the total loss processed as per return for the assessment year 1990-91 was required to be revised to incorporate unabsorbed depreciation of Rs. 1.03 lakhs only and a fresh intimation sent under the provisions of the Act. Omission to revise the same resulted in excess carry forward of loss of Rs. 21.63 lakhs in the

assessment year 1990-91 involving potential tax-effect of Rs. 11.68 lakhs.

The Ministry has not accepted the audit observation on the ground that the assessment was completed under summary assessment scheme. The argument is not tenable. Under the amended provisions of the summary assessment scheme applicable with effect from 1 April 1989 adjustments shall be made to the income of the assessee, inter alia, in regard to any loss carried forward, deduction, allowance or relief which is prima facie admissible or inadmissible. In the instant case, though the provisions of the Act required adjustments to be made on account of brought forward losses and allowances which need reference to previous year's assessment records, these could not be carried out as the Act does not provide for reference to such earlier records. The anomaly needs to be resolved.

Mistakes in allowing deduction under Chapter VIA

3.28.1 Under the provisions of Chapter VIA 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 of the Act before making the deductions under Chapter VIA. 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 VIA is admissible.

A-Scrutiny assessment

(i) The assessment of a closely held company, for the assessment year 1989-90, was completed in March 1992, at a loss of Rs.371.91 lakhs. However, minimum tax was levied on the book profit of Rs.118.11 lakhs. In the assessment, a deduction of Rs.869.03 lakhs, being 50 per cent of the foreign project income was allowed as a deduction from the gross income of Rs.1259.29 lakhs before allowing depreciation of Rs.762.17 lakhs. This led to the allowance of depreciation of Rs.390.26 lakhs (gross income Rs.1259.29 lakhs minus Rs.869.03 lakhs being the deduction for foreign project income) leaving unabsorbed

depreciation of Rs.371.91 lakhs (Rs.762.17 lakhs minus Rs.390.26 lakhs) which was carried forward for set off against the profit for the assessment year 1990-91. The deduction in respect of foreign project income was allowable on the gross total income of Rs.497.12 lakhs (Rs.1259.29 lakhs minus Rs.762.17 lakhs) and not against gross income before other allowances. The assessee was, therefore, entitled to a deduction on foreign project income to the extent of Rs.497.12 lakhs instead of Rs.869.03 lakhs allowed. This led to excess allowance of deduction of Rs.371.91 lakhs. The incorrect deduction led to irregular carry forward of depreciation of Rs.371.91 lakhs to the assessment year 1990-91 with consequent short levy of tax of Rs.252.11 lakhs (including interest).

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

(ii) The assessment of a public sector corporation, for the assessment year 1986-87, was completed in February 1989, and was revised in July 1990, computing taxable income of Rs.13.36 crores being 30 per cent of the pre-incentive total income of Rs.44.92 crores. The company was also allowed carry forward of deduction of Rs.3.29 crores under Chapter VIA which was allowed to be set off in the following assessment year. Audit scrutiny revealed that the gross total income of the company for the assessment year 1986-87 was 'Nil' and hence no deduction under Chapter VIA was allowable. The incorrect allowance resulted in incorrect carry forward of loss of Rs.3.29 crores involving potential short levy of tax of Rs.1.97 crores.

The Ministry has accepted the audit observation.

**B-Summary
Assessment**

3.28.2 Under the Income Tax Act, 1961, in the case of a domestic company, when the gross total income includes any income by way of dividends from another domestic company, there shall, in accordance with and subject to the provision of the Act be allowed, in computing the total income of such domestic company, a deduction of an amount equal to so much of the amount of income by way of dividends from another domestic company as

does not exceed the amount of dividend distributed by the recipient company on or before furnishing the return of income.

While processing the return of income of a widely held company, for the assessment year 1991-92, in February 1992, under the summary assessment scheme, loss of Rs.1.08 crores (consisting of unabsorbed business loss of Rs.67.37 lakhs and unabsorbed depreciation of Rs.40.84 lakhs of earlier years) was computed. In doing so, the assessing officer allowed a deduction of Rs.33.89 lakhs on account of inter-corporate dividend received from other domestic companies before setting off the business loss of Rs.93.13 lakhs and unabsorbed depreciation of Rs.40.84 lakhs brought forward from earlier years. As per provisions of the Act, the assessee company would be entitled to the deduction only after setting off the said loss and the unabsorbed depreciation. Since there was no positive gross total income for the assessment year 1991-92 after setting off unabsorbed business loss of earlier years, the deduction allowed was erroneous. Further, there was no evidence to suggest the distribution of dividend before the due date of furnishing the return of income. The incorrect allowance of deduction of Rs.33.89 lakhs resulted in excess carry forward of loss by an identical amount with consequent potential tax effect of Rs.15.59 lakhs and non-levy of additional income tax of Rs.3.12 lakhs.

The Ministry has accepted the audit observation.

Incorrect allowance of relief in respect of export turnover

3.29.1 Under the Income Tax Act, 1961, as amended by the Finance Act, 1988, with effect from 1 April 1989, an assessee being an Indian company or other assessee resident in India engaged in export business is entitled to a deduction equal to the profit derived from the export of goods or merchandise other than the exempted items if the sale proceeds thereof are received in convertible foreign exchange. Where the business of the assessee does not consist exclusively of export 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, according to

the Act, only business income derived from export of goods or merchandise qualifies for deduction and thus income not derived from the export of goods is required to be excluded while arriving at the business income.

**A-Scrutiny
assessment**

(i) The assessment of a company for the assessment year 1990-91 was completed in December 1991, determining the taxable income at Rs.54.30 lakhs computed under the special provisions of the Act, as the income computed under the normal provision of the Act was 'Nil'. The income under the normal provisions of the Act was computed at 'Nil' after allowing a deduction of Rs.209 lakhs towards export profits and after adjusting brought forward business losses to the extent of Rs.122 lakhs. The company was allowed to carry forward unabsorbed business loss and unabsorbed depreciation aggregating Rs.62 lakhs, relating to the earlier previous year. Audit scrutiny revealed that the total turnover for the relevant previous year was Rs.3655 lakhs and the export turnover was Rs.2,305 lakhs. The profit of the business, after adjusting unabsorbed losses of Rs.184 lakhs, was Rs.146 lakhs and the deduction allowable would be Rs.92 lakhs as against of Rs.209 lakhs allowed by the department. The assessing officer had worked out the deduction of Rs.209 lakhs on the total profit of the business of Rs.331 lakhs before setting off aggregate unabsorbed losses of Rs.184 lakhs relating to the earlier previous year. The mistake resulted in computing the income under normal provision as 'Nil' instead of Rs.54.08 lakhs and an incorrect carry forward of losses aggregating Rs.62 lakhs, involving potential short levy of tax of Rs.37 lakhs.

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

(ii) The assessment of a company for the assessment year 1989-90 was completed in March 1992 allowing a deduction of Rs.88.99 lakhs towards export profits. Audit scrutiny revealed that the total turnover for the previous year relevant to the assessment year 1989-90 was Rs.61,903 lakhs and the export turnover was Rs.2,110 lakhs. The assessing officer adopted an amount of Rs.2610 lakhs as profits of the business for computing the

deduction which was arrived at before setting off the unabsorbed depreciation and investment allowance of the earlier assessment years. As the deduction is to be computed with reference to the business profits as computed under the head 'profits and gains of business' after adjusting the unabsorbed depreciation and investment allowance, the business profits would work out to Rs.1,203 lakhs and the amount of admissible deduction will be Rs.41 lakhs as against Rs.88.99 lakhs incorrectly allowed. The mistake resulted in grant of excess deduction of Rs.47.98 lakhs with consequent short levy of tax of Rs.25.19 lakhs.

The Ministry has accepted the audit observation in principle.

3.29.2 Under the Income Tax Act, 1961, for claiming a deduction for export incentives, for the assessment years 1986-87 to 1988-89, the assessee is required to create a reserve by debiting the profit and loss account and crediting to a reserve account by an amount equal to the amount of deduction. Thus where the reserve created falls short of the amount of deduction to which the assessee is eligible, the deduction allowed is to be restricted to the amount of reserve created.

The assessments of two tea companies, for the assessment year 1987-88, were completed in July 1989 and March 1990, allowing deductions of Rs.28.35 lakhs and Rs.23.86 lakhs respectively, by way of export incentives. Audit scrutiny revealed that the assessee companies created reserve of Rs.13.65 lakhs and Rs.11.50 lakhs respectively by debiting the profit and loss account. Omission to restrict the deduction to the amount of reserve created resulted in excess deduction of Rs.14.70 lakhs and Rs.12.36 lakhs respectively leading to underassessment of income of Rs.27.05 lakhs in aggregate with consequent short levy of tax of Rs.13.53 lakhs.

The department has accepted the audit observation in one case.

**B-Summary
Assessment**

3.29.3 The Central Board of Direct Taxes clarified in September 1990 that furnishing of evidence along with the return of income is a necessary requirement for claiming

exemptions or deduction under certain specified sections of the Act.

An assessee company, engaged exclusively in the business of export out of India, claimed the whole of its income of Rs.48.69 lakhs in the assessment year 1989-90 and Rs.51.16 lakhs in the assessment year 1990-91, as a deduction on account of export incentives which was accepted by the department, while completing the assessments in a summary manner, in January 1990 and 1991. The assessee, however, did not file the report of an accountant in the prescribed form, with the return of income, for both the assessment years and hence the deduction allowed to the assessee was irregular. Further, the assessee has shown Rs.70,000 and Rs.80,000 in the balance sheet relevant to the assessment years 1989-90 and 1990-91, as 'provisions for bonus' but evidence in support of payment of those amounts before the due date of filing of income tax return, was not filed along with the return. Thus the assessee was not entitled to a deduction on this account also, The aforesaid irregular deductions resulted in underassessment of income aggregating Rs.100.65 lakhs with consequent short levy of tax of Rs.82.56 lakhs (including interest).

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

3.29.4 Under the Income Tax Act, 1961, as amended from 1 April 1989, where an assessee, being an Indian company or a person, other than company, resident in India, is engaged in the business of export out of India of any goods or merchandise other than mineral oil, minerals and ores, there shall, subject to other provisions, be allowed, in computing the total income of the assessee, a deduction of the profits derived by the assessee from the export of such goods or merchandise. The Act further imposes certain conditions, nonfulfilment of which would render the assessee ineligible for the aforesaid deduction. One such condition is that the report of an accountant certifying that the deduction has been correctly claimed on the basis of the amount of export turnover should be furnished in the prescribed form along with the return of income.

**B-Summary
Assessment**

(i) The assessment of a closely held company for the assessment year 1989-90 was completed in a summary manner in August 1990 and

subsequently rectified in March 1991. The assessing officer allowed deduction of Rs.16.50 lakhs on export profits though the assessee company did not furnish the report of an accountant in the prescribed form along with the return of income. The irregular deduction, resulted in underassessment of income of Rs.16.50 lakhs involving undercharge of tax of Rs.12.47 lakhs (including additional tax).

The Ministry has accepted the audit observation.

(ii) While processing the return of income of a widely held tea growing and manufacturing company for the assessment year 1990-91 in the summary manner in April 1991 (rectified in November 1991), the assessing officer allowed deduction of Rs.101.25 lakhs on export profits in respect of one of its tea estates though the assessee failed to furnish the report of an accountant in the prescribed form for such deduction along with the return. It was however noticed that the assessing officer, in computing the total income of the relevant assessment year, had disallowed similar deduction pertaining to another tea estate belonging to the assessee company for want of the requisite certificate from the accountant. The irregular deduction resulted in under-assessment of income of Rs.40.50 lakhs (40 per cent of Rs.101.25 lakhs, the assessee being a tea company) with consequent under-charge of tax of Rs.26.24 lakhs (including additional tax of Rs.4.37 lakhs). The assessee company was allowed refund of Rs.60.42 lakhs including interest instead of Rs.41.51 lakhs refundable to him. The aforesaid omission led to an excess allowance of refund of Rs.18.91 lakhs.

The Ministry has accepted the audit observation.

Incorrect allowance of relief in respect of export turnover from tea business

3.30 Under the Income Tax Act, 1961, where during the previous year relevant to the assessment year 1988-89, an assessee, being an Indian company, exports out of India any goods or merchandise, there shall be allowed in computing the taxable income, a deduction of an amount equal to the aggregate of four per cent of net foreign exchange realisation and fifty per cent of profit from export in excess of four per cent of the net foreign exchange realisation. In a case where the

business carried on by the assessee does not consist exclusively of export out of India of the goods to which these provisions apply, the profit derived from the export of goods shall be the amount which bears to the profits and gains of business the same proportion as the amount of export turnover bears to the total turnover of the business. Under the Income Tax Rules, in the case of tax-payers engaged in the business of growing and manufacturing tea, for computing the income chargeable to tax from the sale of tea grown and manufactured in India, the composite income is first determined as if it were income derived from business and forty per cent of such income is deemed to be the income liable to tax. The Central Board of Direct Taxes clarified in May 1991 that in case of tea companies, export incentive deduction should be allowed after the income chargeable to tax under the head profits and gains of business or profession has been computed according to the Income Tax Rules.

The assessments of three tea companies for the assessment year 1988-89 were completed in March 1991 allowing deductions of Rs.108.97 lakhs in respect of export turnover calculated at the prescribed rates. Audit scrutiny revealed that proportionate deduction on export turnover was calculated with reference to the total composite income of Rs.1,222.38 lakhs instead of forty per cent of the income of Rs.489.17 lakhs liable to income tax. On the aforesaid basis, the deduction for export turnover at the prescribed rates would work out to Rs.63.17 lakhs. The mistake resulted in excess allowance of deduction of Rs.45.80 lakhs with consequent short levy of tax of Rs.24.94 lakhs in aggregate (including interest).

The Ministry has accepted the audit observation.

Mistake in allowance of deduction in respect of profits and gains from project outside India

3.31 Under the Income Tax Act, 1961, where the gross total income of an Indian company or a person resident in India, includes any profits and gains derived from the business of execution of a foreign project under a contract or of execution of any work as forming part of a contractual foreign project work undertaken by any other person, there shall be allowed a deduction from such profits (subject to other provisions of the Act), in computing the total income of the

assessee, of an amount equal to twenty five per cent (fifty per cent from 1 April 1987) thereof. The basic conditions for such deduction are (a) that the contract should be with the government of a foreign state or any statutory authority or agency in a foreign state or a foreign enterprise and (b) the consideration is payable in convertible foreign exchange. Further, it has been judicially held* that the deductions under Chapter VIA of the Act, will be computed on income which actually stands included in the gross total income and not on income capable of being included therein.

The assessments of a closely held company, for the assessment years 1985-86, 1986-87, 1987-88 and 1989-90 were completed in March 1992 (revision), August 1989 (rectification), December 1989 and March 1992 respectively allowing deductions at 25 per cent in assessment years 1985-86 and 1986-87 and at 50 per cent in assessment years 1987-88 and 1989-90 amounting to Rs.464.22 lakhs, Rs.506.34 lakhs, Rs.191.93 lakhs and Rs.869.03 lakhs respectively on the gross income from foreign project of Rs.1856.88 lakhs Rs.2025.38 lakhs, Rs.383.86 lakhs and Rs.1738.06 lakhs. Audit scrutiny revealed that the profits from foreign projects in those years were Rs.712.86 lakhs, Rs.932.83 lakhs, Rs.326.62 lakhs and Rs.497.12 lakhs respectively and the deductions at the rate of 25 per cent for assessment years 1985-86 and 1986-87 and 50 per cent for assessment years 1987-88 and 1989-90 would work to Rs.178.21 lakhs, Rs.233.20 lakhs, Rs.163.31 lakhs and Rs.248.56 lakhs. Thus the irregular allowance of deduction on gross incomes from foreign projects instead of the profit from such projects actually included in the gross total income resulted in excess deductions aggregating to Rs.1208.24 lakhs with consequent total under-charge of tax of Rs.1022.41 lakhs (including interest).

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

* 155-ITR-120(SC), 181-ITR-79(SC)

Incorrect allowance of deduction in respect of certain inter-corporate dividends

3.32 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.

The assessment of a widely held company, for the assessment year 1988-89, was completed under scrutiny, in March 1991 and the return for the assessment year 1989-90 was processed in June 1990 in a summary manner determining the income at Rs.107.25 lakhs and Rs.603.40 lakhs respectively. Audit scrutiny revealed that gross dividend of Rs.109.84 lakhs and Rs.55.11 lakhs were reduced by loss on sale of units amounting to Rs.59.15 lakhs and Rs.19.09 lakhs respectively. The net income from dividends included in the total income after these adjustments was Rs.50.69 lakhs and Rs.36.02 lakhs respectively. The assessing officer, however, allowed deductions of Rs.65.90 lakhs and Rs.33.06 lakhs (60 percent of Rs.109.84 lakhs and Rs.55.11 lakhs) instead of Rs.30.41 lakhs and Rs.21.61 lakhs respectively (60 per cent of Rs.50.69 lakhs and Rs.36.02 lakhs). The incorrect deduction thus resulted in underassessment of income of Rs.46.94 lakhs with consequent undercharge of tax of Rs.35.80 lakhs (including additional tax and interest).

The Ministry has accepted the audit observation.

Incorrect deduction of profits derived from services provided to foreign tourists

3.33 Under the Income Tax Act, 1961, as applicable from the assessment year 1989-90 where an assessee, being an Indian company or a person resident in India, is engaged in the business of hotel or tour operator approved by the prescribed authority there shall be allowed, in computing the total income of the assessee, a sum equal to the aggregate of 50 per cent of the profit derived from services provided to foreign tourists and so much of the amount out of the remaining profits

derived as such, as is debited to the profit and loss account and credited to a reserve account to be utilised by the assessee for the purpose of his business under the conditions prescribed in the Act. For this purpose, the profits derived from services provided to foreign tourists shall, in case where the business of the assessee does not consist exclusively of services provided to foreign tourists resulting in receipts in convertible foreign exchange, be the amount which bears to the profit of the business as computed under the head 'profits and gains of business or profession' under the provisions of the Income Tax Act, the same proportion as the receipts in convertible foreign exchange on account of services provided to the foreign tourists bear to the total receipts of the business carried on by the assessee.

**B-Summary
Assessment**

In the assessment of a company, for the assessment year 1989-90, completed in September 1990, in a summary manner, the company was allowed a deduction of Rs.549.32 lakhs in respect of profits derived from services rendered to foreign tourists as claimed. The profit from foreign tourists services of the assessee's hotel business as certified by the auditor of the company was determined at Rs.598.64 lakhs on the total income of Rs.1159.63 lakhs. The total business receipts were Rs.10565.04 lakhs apportioned between foreign receipts of Rs.5404 lakhs and other receipts of Rs.5161.04 lakhs. Assessment records revealed that the assessee company was allowed a deduction of Rs.211.29 lakhs in respect of investment deposit account from the income of the hotel business. This deduction was not considered in arriving at the profits derived from services provided to the tourists, eligible for deduction. Consequently, the income should have been determined at Rs.490.57 lakhs (Rs.598.64 lakhs minus Rs.108.07 lakhs being the deduction under section 32AB computed in the ratio of foreign receipts to total receipts) instead of Rs.598.64 lakhs from foreign tourist services as determined by the department and the allowable deduction in respect of profits derived from services to foreign tourists would work out to Rs.490.57 lakhs (being 50 per cent of Rs.490.57 lakhs plus Rs.245.28 lakhs for creating a reserve of Rs.250 lakhs with the total deduction being limited to the profits) instead of Rs.549.32 lakhs allowed

by the assessing officer. The mistake resulted in excess allowance of deduction of Rs.58.75 lakhs leading to under-charge of tax of Rs.37.01 lakhs (including short levy of additional tax of Rs.6.17 lakhs for understatement of income in the assessment year 1989-90).

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

Incorrect allowance of double income tax relief

3.34.1 Under the Income Tax Act, 1961, a resident person is entitled to a relief in respect of his foreign income, taxed both in India and in a foreign country. The quantum of relief is governed by agreements entered into by the two countries. In cases where there is no agreement between the Government of India and the Government of a foreign country for either affording double taxation relief or avoiding double taxation in respect of income tax in both the countries, the Act provides for a unilateral relief by way of allowance of tax relief to the extent of tax calculated on the doubly taxed income at the average rate of tax in India or the average rate of tax in the foreign country, whichever is lower.

The assessment of a closely held company, for the assessment years 1985-86 to 1987-88, were revised/rectified in March 1992, December 1989 and June 1990 respectively. The assessee had income in Iraq and Algeria on which taxes aggregating Rs. 362.05 lakhs were paid in those countries during the assessment years 1985-86 to 1987-88. In the assessments, the aforesaid taxes paid in Iraq and Algeria were allowed as relief instead of restricting those to lower of the two average rates of tax chargeable in those countries and in India. Audit scrutiny revealed that the net income arising in Iraq which was taxed in India (and therefore entitled to aggregate tax relief) was Rs.804.28 lakhs in the aforesaid assessment years. The average rate of tax in Iraq was 5.22 percent in 1985-86, 11.60 percent in 1986-87 and 14.05 percent in 1987-88. The Indian average rate of tax for these years were 63 per cent (1985-86), 57.75 per cent (1986-87) and 55 per cent (1987-88). The assessee was, therefore, entitled to double income tax relief on Iraqi income at 5.22 per cent, 11.60 percent and 14.05 percent for these assessment years which worked out to

Rs.81.08 lakhs instead of Rs. 344.32 lakhs allowed which resulted in excess relief aggregating Rs. 263.24 lakhs in the aforesaid three assessment years. The Algerian income for assessment years 1986-87 and 1987-88 taxable in India was 'nil' after allowing deductions. Hence the tax relief of Rs. 17.73 lakhs allowed on Algerian income was irregular. Further, for assessment year 1985-86 the Algerian income taxed in India was Rs. 5.53 lakhs. The tax on the aforesaid income at Indian rates would work out to Rs.3.32 lakhs against Algerian rates being Rs. 5.04 lakhs. The lower of these two rates was Rs. 3.32 lakhs which was required to be allowed. The aforesaid mistakes/omissions thus resulted in excess relief of Rs.282.69 lakhs with consequent under-charge of tax of Rs. 402.23 lakhs(including interest of Rs.119.55 lakhs).

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

3.34.2 Under the Double Taxation Avoidance Agreement between India and Japan, where a resident enterprise of Japan derives profit through shipping operation in India, the tax leviable on such profit in India shall be reduced by an amount equal to 50 per cent thereof, provided the income so charged to tax in India is also charged to tax in Japan. The agreement further provided that the amount of tax paid on Indian income shall be allowed credit against the tax payable in Japan. Further, it has been judicially held* that in order to get the benefit of double taxation, income assessed to tax in one country is required to be assessed in the other country as well.

In the assessments of a non-resident shipping company for the assessment years 1989-90 and 1990-91 completed in January 1992, deduction aggregating Rs.123.70 lakhs, being 50 per cent of the income tax levied in India on the Indian income, was claimed and allowed as per the Double Taxation Avoidance Agreement existing between India and Japan. Audit scrutiny revealed that the company, which is a resident of Japan incurred world losses upto assessment year 1988-89 running to several crores of Japanese Yen and as such the Indian income for the assessment years 1989-90 and 1990-91 did not suffer any tax in

* 58 -ITR-468 (Bombay), 61-ITR-632 (Madras)

Japan. Since the income earned in India was not charged to tax in Japan on account of losses in Japan, granting of 50 per cent deduction under the Double Taxation Avoidance Agreement was irregular. The mistake resulted in an under charge of tax of Rs.123.70 lakhs.

The Ministry has not accepted the audit observation on the ground that the income of the Japanese resident in India will be subject to taxation in accordance with the Income Tax Act and the Double Taxation Avoidance Agreement and the effect of the provisions of the said Agreement will have to be given in India irrespective of the fact whether the said assessee is assessed at positive or negative income in Japan. The Ministry's reply is not acceptable in the light of the Bombay High Court decision in the case of C.I.T. Vs. Citizen Bank of India Ltd. and another (58 ITR 468) wherein it has been held that for double taxation relief income tax should have been paid both in India and in the other State for the same corresponding year and income on which tax has been paid in the other State, should have entered into the computation of the Indian income and augmented the Indian income by its inclusion.

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

3.35 Under the Income Tax Act, 1961, where in any assessment year, full effect of admissible allowance of depreciation and relief, like development rebate and investment allowance cannot be given out of the income of the relevant assessment year, the same is carried forward for adjustment against income of the following assessment years. While development rebate and investment allowance can be carried forward for eight assessment years only, after the end of the initial assessment year, there is no such restriction on carrying forward of unabsorbed depreciation allowance. The Central Board of Direct Taxes clarified in July 1976 that brought forward unabsorbed depreciation gets priority for adjustment over unabsorbed development rebate and investment allowance. Further, under the Act, as applicable to the assessment years 1984-85 to 1987-88, where, in case of a company, the aggregate amount of deduction admissible under certain specified provisions of the Act, exceeds 70 per cent of amount of the

total income computed before making such deduction and known as 'pre-incentive income', the amount to be deducted in the relevant assessment year is to be restricted to 70 per cent of the total pre-incentive income and balance carried over to the following assessment year. Development rebate and investment allowance are in the nature of such specified deductions, for the purpose of applying the aforesaid restrictions.

The assessment of a company, for the assessment year 1984-85, made in March 1987 at 'nil' income was revised to loss of Rs.52.63 lakhs in December 1990 after first allowing the deductions of Rs.25.55 lakhs and Rs.47.06 lakhs for current and brought forward investment allowance and then a deduction of Rs.371.26 lakhs for unabsorbed depreciation allowance. Audit scrutiny further indicated that in arriving at the loss of Rs.52.63 lakhs, the assessing officer neither applied the prescribed priority for adjustment of unabsorbed deductions, nor restricted the deductions/reliefs to 70 per cent of the total 'pre-incentive income'. The order of priority in adjustment of depreciation/relief was also not applied in the assessments for the earlier assessment years, from 1978-79 onwards. After adjustment of unabsorbed depreciation of Rs.191.33 lakhs out of the profit of Rs.391.24 lakhs for the assessment year 1984-85, an amount of Rs.199.91 lakhs would have been the pre-incentive income and deduction on account of unabsorbed development rebate/investment allowance was required to be further restricted to 70 per cent thereof i.e. Rs.139.94 lakhs. After reducing this amount, the income for the assessment year 1984-85 worked out to Rs.59.97 lakhs, instead of the loss of Rs.52.63 lakhs determined by the department. The aforesaid mistake resulted in non-assessment of income of Rs.59.97 lakhs with consequent short levy of tax of Rs.34.63 lakhs.

The Ministry has accepted the audit observation.

**Excess
refund of
tax**

3.36 Under the Income Tax Act, 1961, where as a result of any order passed in 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 same against outstanding dues of the assessee.

The assessment of a widely held company for the assessment year 1984-85 was completed in March 1987 at an income of Rs.169.71 lakhs and the amount of Rs.18.50 lakhs found refundable was refunded in July 1987. In a subsequent revision of assessment in November 1990, the income was determined at Rs.178.50 lakhs and the refund due was determined at Rs.13.45 lakh which was refunded in September 1990 and April 1991 through adjustment and cash refund respectively. Audit scrutiny revealed that while determining the refundable amount of Rs.13.45 lakhs in November 1990, the tax refund of Rs.18.50 lakhs already allowed in July 1987 was not considered. As a result, there was short demand of tax of Rs.5.05 lakhs, apart from the irregular refund of Rs.13.45 lakhs. The total tax effect involved is thus Rs.18.50 lakhs.

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

Non-levy of interest for delay in filing of return

3.37 Under the Income tax Act, 1961, where the return for an assessment year is furnished after the specified due date, the assessee shall be liable to pay simple interest at fifteen per cent per annum (from the assessment year 1989-90, two per cent for every month or part thereof) from the date immediately following the specified due date to the date of furnishing the return on the amount of tax determined on regular assessment as reduced by the advance tax, if any, paid and any tax deducted at source. The mistakes in the levy of interest noticed in test check are given in the table below:

Sl. No.	State/Commissioner charge/Name of assessee	Assessment year/Date of assessment	Assessed income (in lakhs of rupees)	Section under which assessed	Specified due date/Date of filing the return	Tax due	Tax paid	Non levy/short levy of interest (in lakhs of rupees)
1.	Uttar Pradesh Lucknow Company	1989-90/ January 1992/ March 1992	91.35	143(3)	31 Dec.1989/ 31 Dec. 1990	47.96	Nil	6.71
2.	Delhi/Central I Company	1989-90 March 1992	32.98	143(3)	31 Dec.1989/ 4 Jan. 1991	2.07	1.05	4.73

The Ministry has accepted the audit observations.

**Interest for
short
payment of
advance tax**

3.38.1 Under the Income Tax Act, 1961, where in any financial year, the advance tax paid by an assessee on his current income on or before the 15th day of September is less than twenty percent of the tax due on the returned income or the amount of such advance tax paid on or before the 15th day of December is less than fifty per cent of tax due on the returned income, the assessee shall be liable to pay simple interest at the rate of one and one half percent per month of the short fall for a period of three months on the amount of the shortfall from twenty percent or as the case may be, fifty percent of the tax due on the returned income.

(i) In the case of a public sector corporation engaged in insurance business, the assessments for the assessment years 1989-90 and 1991-92 were completed in May 1990 and March 1992 respectively. Audit scrutiny revealed that on a returned income of Rs.1192.40 crores and Rs.1800 crores, the corporation was liable to pay advance tax of Rs.25.04 crores and Rs.51.62 crores as the first instalment and Rs.32.60 crores and Rs.129.00 crores as the second instalment in the two respective assessment years. However, the corporation paid only Rs.21.01 crores and Rs.44.57 crores as first instalment and Rs.31.52 crores and Rs.73.74 crores as the second instalment respectively. The department did not levy any interest for the short fall in payment of advance tax. Non-levy of interest on the shortfall in the payment of first and second instalments of advance tax resulted in undercharge of interest of Rs.143.51 lakhs (Rs.63.46 lakhs and Rs.80.05 lakhs respectively for the assessment years 1989-90 and 1991-92).

The Ministry has accepted the audit observation.

(ii) In the re-assessment of a closely held company for the assessment year 1986-87 completed in March 1992, an additional demand of Rs.64.18 lakhs was raised. Audit scrutiny revealed that the assessing officer did not charge interest for short payment of advance tax though such interest was levied in the original assessment completed in December 1990. The omission resulted in short levy of interest of Rs.14.30 lakhs for the period from 1 April 1986 to 31 October 1987.

The Ministry has accepted the audit observation.

3.38.2 Under the Income Tax Act, 1961, where an assessee company has paid advance tax for any financial year on the basis of its own estimate and the advance tax so paid falls short of eighty-three and one third per cent (ninety per cent with effect from 1 April 1989) of the tax determined on regular assessment, interest at the rate of fifteen per cent per annum 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 regular assessment.

(i) In the assessment of a non-resident company for the assessment year 1987-88 completed in March 1990, the total income was computed at Rs.589.93 lakhs. The advance tax paid by the assessee was only Rs.101.21 lakhs which was less than eighty three and one third per cent of the assessed tax of Rs.360.92 lakhs. As against the correct amount of Rs.105.47 lakhs, the department incorrectly levied interest of Rs.90.22 lakhs for short payment of advance tax. This resulted in short levy of interest of Rs.15.15 lakhs for the assessment year 1987-88.

The Ministry has accepted the audit observation.

(ii) In the assessment of a State Financial Corporation, for the assessment year 1989-90, the regular assessment was completed in March 1992 and tax of Rs.1360.99 lakhs was levied. As no advance tax was paid by the assessee, interest for non-payment of advance tax was levied upto the date of processing under section 143(1)(a) (March 1990) instead of upto the date of regular assessment (March 1992). The mistake resulted in short levy of interest of Rs.645.50 lakhs for the assessment year 1989-90.

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

(iii) The return of income of a widely held company for the assessment year 1989-90, initially processed in June 1990, was subsequently revised in March 1992 computing total income at Rs.231.86 lakhs and tax payable at Rs.121.23 lakhs after adjustment

of Rs.49,180 for tax deducted at source. Since the assessee company paid no advance tax, it was liable to pay interest of Rs.87.29 lakhs, calculated at the rate of two per cent per month for 36 months from 1 April 1989 to the end of March 1992. The assessing officer, however, did not levy interest for non-payment of advance tax.

The Ministry has accepted the audit observation.

(iv) The return of income of a widely held assessee company for the assessment year 1989-90, initially processed in June 1990, was subsequently scrutinised in March 1992 computing total income at Rs.748.55 lakhs and tax at Rs.392.99 lakhs. The company paid Rs.215.52 lakhs, by way of advance tax and tax deducted at source and Rs.60.00 lakhs as self-assessment tax on 30 May 1989. Since advance tax paid fell short of ninety per cent of the assessed tax, the assessee company was liable to pay interest of Rs.86.98 lakhs calculated at the rate of two per cent per month for 36 months from 1 April 1989 to the date of regular assessment on 3 March 1992, in place of Rs.35.29 lakhs levied by the department for 14 months from 1 April 1989 to 1 June 1990 (the date of determining the income by processing the return). The omission led to short levy of interest of Rs.51.69 lakhs.

The Ministry has accepted the audit observation.

(v) The assessment of a company, for the assessment year 1989-90, was originally completed in June 1990 under the summary assessment scheme. The regular assessment, after the scrutiny of the records, was completed in March 1992 levying tax of Rs.220 lakhs. It was seen in audit that the advance tax paid fell short of ninety per cent of the assessed tax and hence the company was liable to pay interest for a period of 36 months from 1 April 1989 to 30 March 1992 that is upto the date of regular assessment. However, the assessing officer levied interest for a period of 15 months from 1 April 1989 to 28 June 1990 that is the date on which the summary assessment was completed. Consequently, an amount of Rs.31.48 lakhs was levied as interest as against Rs.73.95 lakhs leviable. The mistake resulted in short levy of interest of Rs.42.47 lakhs.

The Ministry has accepted the audit observation.

(vi) The return of a non-resident company, for the assessment year 1989-90, initially processed in July 1990, was subsequently assessed under scrutiny in March 1991 and revised in December 1991 finally determining the tax payable at Rs.228.32 lakhs. The assessee had paid advance tax of Rs.152.58 lakhs and self-assessment tax of Rs.0.16 lakhs. As the advance tax paid fell short of ninety per cent of the assessed tax, the company was liable to pay interest of Rs.36.31 lakhs for the period from 1 April 1989 to the date of regular assessment in March 1991. No interest was, however, levied.

The department has accepted the audit observation.

(vii) The assessment of a widely held company, for the assessment year 1989-90, was completed in March 1992. Audit scrutiny revealed that as against the assessed tax of Rs 42.93 lakhs as per the regular assessment order, the assessee company had paid advance tax of Rs 8.26 lakhs. As the advance tax paid was less than ninety per cent of the assessed tax, the assessee was liable to pay interest of Rs 24.96 lakhs for the default.

The Ministry has accepted the audit observation.

Interest for delay in payment of tax demand

3.39 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 fifteen per cent per annum (one and one half per cent 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.

The assessment of a company, for the assessment year 1986-87 was originally

completed in March 1989 and later revised in June 1989 to August 1991 with reduced demand of Rs. 42.51 lakhs. The demand notice was served on 31, March 1989. The assessee paid Rs. 5197 in January 1989, Rs. 5.00 lakhs each in January 1990 and March 1990 and Rs.7.93 lakhs in March 1991, aggregating Rs.17.98 lakhs. The assessee was therefore in default in respect of the tax demand. However interest for delay in payment amounting to Rs. 10.95 lakhs was not charged.

The Ministry has accepted the audit observation adding that there is no possibility of collecting the demand as the company is a sick unit.

**Incorrect
payment of
interest by
Government**

3.40 Under the Income Tax Act, 1961, where the advance tax paid by an assessee during any financial year exceeds the amount of assessed tax, the Government is liable to pay interest at the rate of fifteen per cent on the amount of excess advance tax so paid from 1 April of the assessment year to the date of regular assessment.

The assessment of a company for the assessment year 1987-88 was originally completed in March 1989. In pursuance of the appellate orders the assessment was revised in July 1991, determining a refund of Rs.74.55 lakhs after adjusting advance tax of Rs.32.54 lakhs and tax deducted at source amounting to Rs.54.01 lakhs. The company was allowed interest of Rs.22.36 lakhs on the refund of Rs.74.55 lakhs. As the interest was payable only on the excess payment of advance tax of Rs.32.54 lakhs, the allowance of interest of Rs.22.36 lakhs on the entire refund of Rs.74.55 lakhs was not in order. The mistake resulted in excess payment of interest of Rs.12.60 lakhs.

The Ministry has accepted the audit observation.

**Omission to
levy
additional
tax**

3.41 Under the provisions of 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 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 per cent of tax payable on such excess amount.

(i) Adjusted income of a widely held assessee company, for the assessment year 1989-90 was determined by the assessing officer, in a summary manner at Rs.367.34 lakhs in the revised assessment made in December 1991 against the returned income of Rs.239.46 lakhs. Although the department rightly levied income tax of Rs.192.85 lakhs on the adjusted income of Rs.367.34 lakhs, it did not levy additional income tax of Rs.13.43 lakhs calculated at the rate of twenty per cent on the income tax of Rs.67.13 lakhs chargeable for addition of Rs.127.88 lakhs to the returned income. This led to non-levy of additional income tax of Rs.13.43 lakhs.

The Ministry has accepted the audit observation.

(ii) The assessment of a company for the assessment year 1991-92 was completed in January 1992 under the summary assessment scheme. The assessing officer computed taxable income at Rs.60.59 lakhs after making an addition of Rs.156.18 lakhs to the returned loss of Rs.95.59 lakhs. However, additional tax was levied only on the tax payable on the income of Rs.60.59 lakhs computed, though it was correctly leviable on the amount of tax of Rs.89.80 lakhs payable on such additions. This mistake resulted in short levy of additional tax of Rs.10.99 lakhs.

The Ministry has accepted the audit observation.

**Omission to
make
assessment
of surtax**

3.42 Under the Companies (Profits) Surtax Act, 1964, there is no statutory time limit for completion of surtax assessment. 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 along with income tax assessments. The Board further laid down that the surtax assessments 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 income tax and surtax assessments should not ordinarily exceed a month, unless there were special reasons justifying the delay. Noticing the persistent delays or omissions in completing the surtax

assessments despite the above recommendations and issue of instructions by the Board, the Public Accounts Committee recommended in paragraphs 3.3 to 3.10 of their 85th Report (Seventh Lok Sabha) that a statutory time limit for completion of surtax assessments under the Surtax Act should be prescribed. The need for a statutory time limit for completion of surtax assessment was again stressed by the Public Accounts Committee in para 1.6 of their 193rd Report (Seventh Lok Sabha).

Test audit revealed that in 11 cases, either the assessee company had not filed the surtax return or the department had not initiated any proceedings for making surtax assessment. The omission in not making surtax assessment in these cases resulted in a non-levy of surtax of Rs.360.26 lakhs. The following cases are illustrative of the omissions:

Sl. Commissioner's No. charge	Assessment year	Date of completion of Income Tax Assessment	Total income assessed (in lakhs of rupees)	Surtax leviable (in lakhs of rupees)
1. West Bengal III, Calcutta	1987-88	21.9.1990	1282.04	167.14 (including interest)
2. Central II, Madras	1985-86	23.3.1988	241.77	53.18
3. Central II, Madras	1985-86 1987-88	18.3.1991 30.3.90/26.11.92	51.04 128.37	50.58 (including interest)
4. West Bengal IV Calcutta.	1985-86	24.3.1988	252.75	43.06

The audit observation at serial number 2 has been accepted by the department.
The Ministry has accepted the audit observation at Sl.No.1,3 & 4.

CHAPTER 4

INCOME TAX

General

4.1 Income Tax collected from persons other than companies is booked under the major head '0021 Taxes on income other than corporation tax'. Eighty-five per cent 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.

4.2 The trend of receipts from income tax during the last five years was as follows:

Year	Total collection of all Direct Taxes	Amount of Income tax	Percentage of Income tax to total collection
	(in crores of rupees)		
1988-89	8,828.76	4,241.24	48.04
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

4.3 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 collec- tion of tax (per capita) (in thousands of rupees)
1989	67,15,127	6.31
1990	69,16,640	7.24
1991	73,22,010	7.34
1992	77,60,407	8.66
1993*	83,62,738	9.40

* Provisional

4.4 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	Amount of demand		Percentage of arrears to total collection
	Completed during the year	Pending at the close of the year		Collected during the year	In arrears at the close of the year	
1988-89	60,51,670	9,11,983	13.10	4,241.24	1,173.67	27.79
1989-90	55,93,738	11,36,260	16.88	5,008.98	1,409.99	28.15
1990-91	62,68,326	12,28,905	16.39	5,375.34	1,534.59	28.55
1991-92	65,66,416	12,55,030	16.05	6,729.18	2,398.70	35.65
1992-93*	65,02,943	14,50,200	18.23	7,863.49	2,059.38	26.19

Results of audit

4.5 A total number of 270 draft paragraphs involving tax effect of Rs.13.79 crores were issued to the Ministry of Finance for comments during March to August 1993. The Ministry has accepted the observations in 142 cases involving tax effect of Rs.5.37 crores. 68 illustrative cases involving tax effect of Rs.6.10 crores are given in the following paragraphs. Out of these, the Ministry has accepted the observations in 42 cases involving tax effect of Rs.3.04 crores. Out of these 4 cases involving tax effect of Rs.25 lakhs were checked by the Internal Audit but the mistakes were not detected by it.

Avoidable mistakes in computation of income and tax

4.6 Underassessment of tax of substantial amounts on account of avoidable mistakes attributable to negligence on the part of assessing officers has 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,

*Provisional

double allowance, calculation errors and application of lower rate of tax. Brief particulars of nine representative cases involving short levy of tax of Rs.58.32 lakhs are given below:

Sr. No.	State/Commissioner's charge/Assessee	Assessment year/Date of Assessment	Nature of mistake	Tax effect/Financial implication (in lakhs of rupees)
A.Scrutiny Assessment				
1.	Maharashtra Bombay Registered firm	1989-90 December 1991	The relevant previous year of the assessee comprised seventeen months ending on 31 March 1989. While calculating the rental income from the house property, annual value was calculated for twelve months at Rs.29.75 lakhs instead of for seventeen months at Rs.42.14 lakhs.	9.75 (including interest)
2.	West Bengal W.B. IV, Calcutta Unregistered firm	1989-90 February 1992	Omission to add back Rs. 7.59 lakhs determined to be disallowable.	6.78 (including interest)
3.	Maharashtra City IV, Bombay Charitable trust (AOP)	1989-90 August 1990	Omission to add back contribution of Rs.14.75 lakhs received from a company for reservation of seats for the children of its employees in an educational institution run by the assessee, contribution having been considered as consideration for the services rendered by the assessee.	6.87 (including additional tax and interest).
4.	Maharashtra City XI, Bombay Individual	1986-87 March 1992	The total income was taken at Rs.1.13 lakhs instead of the correct amount of Rs.7.73 lakhs.	5.21 (including interest)
5.	Rajasthan Jaipur Individual	1989-90 March 1992	Omission to add back Rs.5 lakhs to the total income determined by the assessing officer on account of receipt of whole-sale business conducted by the assessee.	5.09 (including interest)

6.	West Bengal W.B.-IV, Calcutta Unregistered firm	1989-90 February 1992	Omission to add back provision for bonus of Rs.13.82 lakhs debited to profit and loss account determined by the assessing officer as disallowable.	4.93 (including interest)
7.	Bihar Patna Individual	1989-90 March 1992	Assessing officer considered income of Rs.4.30 lakhs from undisclosed sources to be included in the total income. However, while totalling figures of income in the assessment order, the amount was not included.	4.41 (including interest)
8.	West Bengal W.B.-I, Calcutta Unregistered firm	1989-90 March 1992	Due to incorrect application of rate of tax, arithmetical error and incorrect levy of interest, the tax payable on total income of Rs.13.86 lakhs was determined at Rs.7.95 lakhs (including interest) instead of the correct amount of Rs.12.14 lakhs.	4.19 (including interest)

B-Summary Assessment

9.	Maharashtra Nasik A.O.P.	1989-90 March 1992	The additional tax payable was wrongly determined at Rs.1.24 lakhs instead of the correct amount of Rs.12.33 lakhs.	11.09
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The Ministry has accepted the audit observation in respect of Sl. Nos. 1 to 6, 8 and 9. The reply of the Ministry for the remaining case has not been received so far.

Application of incorrect rate of tax

4.7 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.

The assessments of a firm for the assessment years 1987-88 and 1988-89 were completed ex-parte in March 1992 at a total income of Rs.5 lakhs and Rs.3 lakhs. The assessee firm was denied continuation of registration as the firm did not file application for the same. The assessing officer, therefore, treated the assessee firm as an unregistered firm. However, the tax payable by the firm was charged at the rates applicable to a registered firm resulting in short levy of

tax of Rs.4.54 lakhs, including interest for non-filing of the return for two years.

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

4.8 INCORRECT COMPUTATION OF BUSINESS INCOME

Incorrect allowance of liabilities

4.8.1 Under the Income Tax Act, 1961, as amended by the Finance Act 1983 with effect from the assessment year 1984-85, in computing the business income of an assessee, a deduction allowable in respect of any sum payable by way of tax or duty, or any sum payable as an employer by way of contribution to any provident fund, superannuation fund etc. 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. However, deduction in respect of tax or duty will be allowed if it is actually paid on or before the due date for furnishing the return of income.

The assessments of three assessees (a registered firm, one domestic private limited company and a partnership firm) for the assessment years 1987-88, 1989-90 and 1990-91 were completed between November 1990 and January 1992 in the charges of two different Commissioners of Income tax. Audit scrutiny revealed that an amount of Rs.23.76 lakhs was debited to the profit and loss account towards unpaid liabilities of interest on long-term loans, interest and sales tax and bonus which were not actually paid before the filing of returns of income and thus should have been disallowed by the assessing officer. Further, in one case, though there was evidence to show that the assessee had received subsidy of Rs.45,930 during the previous year relevant to the assessment year 1990-91, this was neither taken as receipt nor reduced from the actual cost of the related asset and the depreciation regulated accordingly. These mistakes resulted in underassessment of income of Rs.24.22 lakhs involving short levy of tax of Rs.13.35 lakhs in aggregate in the hands of assessees and partners.

The Ministry has partly accepted the audit observations in one case. The reply of the Ministry for the remaining cases has not been received so far.

Mistakes in computation of business income

4.8.2 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 assessee follows mercantile system of accounting, the net profit or loss is calculated after taking into account all incomes actually received, accrued or deemed to accrue, as well as, expenditure and the liability incurred relating to the period, regardless of their actual receipt or payment.

A- Scrutiny assessment

The assessment of an assessee co-operative society following mercantile system of accounting for the assessment year 1991-92 was completed, in December 1991, at a loss of Rs.16.68 lakhs. Audit scrutiny revealed that an amount of Rs.15.40 lakhs, being expenses pertaining to earlier years, was debited to the profit and loss account of the relevant previous year. Since the assessee was following mercantile system of accounting, expenses pertaining to earlier years were not allowable in computing income/loss of the current year. Omission to disallow the expenses resulted in underassessment of income of Rs.15.40 lakhs with potential short levy of tax of Rs.6.04 lakhs.

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

4.8.3 Under the provisions of the Income Tax Act, 1961, for determination of income in the case of an assessee, being a person other than a public sector company, obtaining in any sale by way of auction, tender or any other mode conducted by any other person, any goods in the nature of alcoholic liquor for human consumption (other than Indian made foreign liquor) or any forest produce, a sum equal to forty per cent of the amount paid or payable by the buyer as purchase price in respect of such goods shall be deemed to be the profits and gains of the buyer from the business of trading in such goods chargeable to tax under the head 'profits and gains of business or profession'. In view of the judicial decisions against this provision, the Central Board of Direct Taxes in Instruction No.1814 has confirmed the applicability of the provisions of the Act in the States other than the States where the

judicial decisions are applicable and had filed a special leave petition in the Supreme Court.

**B-Summary
Assessment**

The assessment of a firm (a country liquor contractor) for the assessment year 1990-91, was completed in a summary manner in February 1991, at an income of Rs.82,610. Audit scrutiny revealed that the total purchase of liquor during the assessment year amounted to Rs.21.18 lakhs (excluding excise duty). The income of the assessee thus worked out to Rs.8.47 lakhs (40 per cent of Rs.21.18 lakhs). The mistake resulted in underassessment of income of Rs.7.64 lakhs involving short levy of tax of Rs.4.44 lakhs in the hands of firm and its partners.

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

4.8.4 The Income Tax Act 1961, was amended retrospectively with effect from 1 April 1967 by the Finance Act 1990 to bring to tax cash incentives received or receivable by any person against exports under any scheme of the Government of India. The Central Board of Direct Taxes, vide their circular No.564 dated 5 July 1990 has also clarified that the export incentives would have to be included in the profits of the business for computing the deduction under section 80HHC of the Act as they are revenue receipts.

An assessee deriving income from export business, returned losses of Rs.4.34 lakhs and Rs.2.33 lakhs for the assessment years 1988-89 and 1989-90 in December 1988 and March 1990 respectively. These losses were accepted as such by the assessing officer in the assessments completed in a summary manner in February 1989 and March 1992 respectively. It was noticed in audit that while computing the losses, the assessee had not taken into consideration the cash compensatory receipts of Rs.5.29 lakhs and Rs.5.27 lakhs received during the relevant previous years on the plea that these constituted capital receipts. The omission to treat cash compensatory receipts as income resulted in under-assessment of income of Rs.8.80 lakhs (after allowing deductions in respect of profit retained from export business) involving a total tax effect of Rs.4.57 lakhs (potential tax effect Rs.3.06 lakhs and positive tax

effect Rs.1.51 lakhs), including additional tax and interest for short payment of advance tax.

The Ministry has accepted the audit observation.

Incorrect allowance of provision

4.8.5 Under the Income Tax Act, 1961, 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 purposes of the business or profession shall be allowed in computing the income chargeable under the head 'profits and gains of business or profession.'

A-Scrutiny Assessment

(i) In the case of a partnership firm engaged in the export of marine products for the assessment years 1980-81, 1981-82 and 1982-83, during the period October 1982 to March 1983, Rs.25.20 lakhs, Rs.24.44 lakhs and Rs.36.51 lakhs respectively, were debited in the profit and loss account towards purchase tax payable and outstanding in the balance sheet and were allowed as deduction. Audit scrutiny revealed that the goods were purchased in the course of export and the assessee had no liability to pay purchase tax under the Central Sales Tax Act, 1956. Thus the deductions allowed were not in order. The mistake resulted in underassessment of income of Rs.86.15 lakhs in aggregate involving short levy of tax of Rs.15.85 lakhs in the hands of the firm alone for the three assessment years.

The Ministry has accepted the audit observation.

(ii) The assessment of an individual for the assessment year 1989-90, was completed in January 1992. The assessee was a partner in a firm upto 10 December 1987. On the death of one of the two partners, the business was taken over by the assessee with effect from 11 December 1987. In the assessment for the assessment year 1989-90 in the case of the assessee, a sum of Rs.12.57 lakhs representing commission payment which was disallowed in the assessment of the firm for assessment year 1988-89 as it pertained to the assessment year 1989-90 and a sum of Rs.45,262, a revenue receipt, were excluded for the reason that these amounts were taxed in the earlier assessment year 1988-89. As these adjustments were made during the assessment year 1988-89 in the case of the

firm, the deduction should also have been allowed only to the firm and not to the partner. The mistake resulted in underassessment of income of Rs.13.02 lakhs involving short levy of tax of Rs.7.03 lakhs.

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

(iii) The assessment of a co-operative society engaged in the business of manufacture and sale of yarn, for the assessment year 1989-90 was completed in March 1990. It was seen from the profit and loss account that the assessee had debited an amount of Rs.16.49 lakhs towards cotton development expense, out of which Rs.15.70 lakhs was paid to cotton grower members as incentive for implementation of cotton development in the working area of the mill. Obviously, the incentive paid was not related to the business of the assessee and was not allowable. Considering the fact that the society wanted to help its members in cotton development, this expenditure should have been treated as capital expenditure and disallowed as revenue expenditure. The omission to disallow this expenditure resulted in excess carry forward of depreciation of Rs.15.70 lakhs involving potential short levy of tax of Rs.6.60 lakhs.

The Ministry has accepted the audit observation and rectified the assessment.

B-Summary Assessment

4.8.6 The assessment of a registered firm, engaged in the business of purchasing vacant land and selling it after developing, for the assessment year 1988-89 was completed in March 1990 under the Summary assessment scheme. Audit scrutiny revealed that the assessee firm had debited an amount of Rs.4.85 lakhs and credited it to a fund account, viz. 'Development Fund'. As the development fund was not created under the provisions of any statute and did not represent any expenditure, but was in the nature of an appropriation, the amount was required to be added back to taxable income. Failure to add back the same resulted in underassessment of income of Rs.4.85 lakhs involving short levy of tax of Rs.3.44 lakhs in the hands of the firm and its partners, including interest.

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

Other mistakes in the computation of business income

4.8.7 The Income Tax Act, 1961, provides for disallowance of expenditure incurred in business or profession for which payment is made for any amount exceeding Rs.2,500 (Rs.10,000 with effect from 1 April 1989), otherwise than by a crossed cheque or crossed bank draft. This provision was designed to counter evasion of tax through claims for expenditure shown to have been incurred in cash with a view to frustrating proper investigation by the department as to the identity of the payee and the reasonableness of the amount. A residuary provision made in this regard stipulates that exemption could be allowed, subject to satisfactory explanation being furnished to the assessing officer about the genuineness of the payment and the identity of the payee. The exemption could also be allowed if the assessing officer was satisfied about the exceptional and unavoidable circumstances due to which the payments could not be made by crossed cheques/draft and any other difficulties having regard to the nature of the transaction and the necessity of expeditious settlement thereof.

Further, under the Act, as made applicable from the assessment year 1985-86, assessee carrying on business or profession, would file in respect of their accounts for each previous year if their total sales, turnover or gross receipts exceeded the specified limit, an audit report furnished by a chartered accountant in the prescribed form which provided for the auditor to list out payments in excess of Rs.2,500 (Rs.10,000 from 1 April 1989) made otherwise than by crossed cheque or crossed bank draft.

The assessment of a registered firm for the assessment year 1986-87, was completed in March 1992. It was seen in audit that the assessee had made payments in excess of Rs.2,500 in cash which amounted to Rs.20.73 lakhs and were not disallowed by the assessing officer. Failure to do so resulted in underassessment of income of Rs.20.73 lakhs involving short levy of tax of Rs.15.34 lakhs in the hands of the firm and its partners.

Subsequent to the audit observation, the department/initiated action to set aside the assessment.

4.9 IRREGULARITIES IN ALLOWING DEPRECIATION AND INVESTMENT ALLOWANCE

Mistakes in the allowance of depreciation

4.9.1 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 per cent to one hundred per cent are prescribed for certain specified items of machinery and plant. Where the actual cost of any machinery or plant does not exceed five thousand rupees, the actual cost thereof is allowed as deduction in respect of the previous year in which such machinery or plant is first put to use.

(i) In the assessment of a registered firm running a lodging complex, for the assessment year 1989-90, completed in February 1992, the assessing officer allowed the entire cost of T.V. sets and audio decks of Rs.7.91 lakhs as deduction towards depreciation. Audit scrutiny revealed that out of Rs.7.91 lakhs, Rs.7.84 lakhs represented cost of T.V. sets, each costing more than Rs.5,000. The assessee was, therefore, entitled to depreciation on T.V. sets at the prescribed rate of thirty-three and one-third per cent only. The mistake resulted in underassessment of income of Rs.5.23 lakhs and short levy of tax of Rs.3.37 lakhs in the hands of the firm and its partners.

The Ministry has accepted the audit observation.

(ii) In the assessment of a co-operative society, for the assessment year 1988-89, completed after scrutiny in March 1992, due to incorrect application of rate of depreciation allowance on furniture, there was an excess allowance of depreciation of Rs.9.46 lakhs with consequential excess determination of loss of Rs.9.46 lakhs resulting in potential tax effect of Rs.3.97 lakhs.

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

Excess set off of unabsorbed depreciation

4.9.2 Under the Income Tax Act, 1961, when for any assessment year, unabsorbed depreciation under the head 'profits and gains of business or profession' cannot be set off against any other income in the relevant year, such unabsorbed depreciation shall be carried forward to the following assessment year for set off against profits 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.

In the assessment of an assessee, a registered firm, for the assessment year 1985-86, revised in March 1992, unabsorbed depreciation of Rs.59.35 lakhs in respect of the assessment years 1982-83 and 1984-85 was set off. It was, however, noticed in audit that as per the revision order of March 1992 for the assessment year 1984-85, the carried forward unabsorbed depreciation for the assessment years 1982-83 and 1984-85 was only Rs.50.34 lakhs. The excess set off of Rs.9.01 lakhs resulted in underassessment of income by a like amount in the assessment year 1985-86 involving short levy of tax of Rs.6.50 lakhs in the hands of the firm and its partners.

The Ministry has accepted the audit observation.

Incorrect grant of investment allowance

4.9.3 Under the Income Tax Act, 1961, no deduction on account of investment allowance is admissible in respect of road transport vehicles. The Central Board of Direct Taxes have decided that cranes mounted on mobile transport vehicles should be classified as motor vehicles other than those used in a business of running them on hire qualifying for depreciation at a higher rate.

A-Scrutiny Assessment

In the assessment of a registered firm for the assessment year 1986-87, completed in December 1988, the assessing officer granted deduction of Rs.11.52 lakhs on account of investment allowance on mounted cranes costing Rs.46.10 lakhs. It was, however, noticed in audit that the assessee was also allowed depreciation on these cranes at the rate applicable to road transport vehicles treating them as such. As road transport vehicles do not qualify for investment allowance, no investment allowance should have been allowed. The mistake resulted in

underassessment of income of Rs.11.52 lakhs involving short levy of tax of Rs.6.79 lakhs in the hands of the firm and its partners.

The Ministry has not accepted the audit observation stating that the admissibility of investment allowance on a particular asset depends upon its use or utilisation and the cranes were used by the assessee as plant and machinery in its manufacturing activities. The argument is not tenable. As the depreciation on cranes was allowed treating them as transport vehicles, investment allowance cannot be granted for the same asset treating it as machinery used for the purpose of manufacture. It has also been held judicially[@] that Revenue cannot take an inconsistent stand in allowing depreciation and investment allowance.

**B-Summary
Assessment**

4.9.4 Under the Income Tax Act, 1961, in respect of machinery owned by an assessee and used for the purpose of business carried on by him, a deduction, by way of investment allowance, shall be allowed, in the previous year of installation or in the previous year of first usage, of a sum equal to twenty-five per cent (reduced to twenty per cent in respect of machinery installed after 31 March 1988) of the actual cost of the new machinery to the assessee. No investment allowance is admissible on machinery or plant which are not used in an industrial undertaking for the purpose of the business of manufacture or production of any article or thing. It has been judicially held* that a hotel is mainly a trading concern and the preparation of articles of food from raw materials did not constitute manufacture or processing. The Central Board of Direct Taxes have also issued instructions (January 1986) that investment allowance is not admissible to a hotel as no manufacture or processing of goods is involved. The amended provisions of the summary assessment scheme were applicable with effect from 1 April 1989. Under the amended provisions, adjustments shall be made to the income of the assessee, inter alia, in regard to any loss, carry forward, deduction, allowance or relief which is prima facie admissible or inadmissible.

For the assessment year 1990-91, a registered firm engaged in the business of running

[@] 165-ITR-160(Guj)

* 154 ITR 53(Kar), 91-ITR-286(Kerala)

hotels returned 'nil' income after setting off unabsorbed investment allowance of Rs.26.85 lakhs relating to the assessment year 1987-88 and claimed further carry forward of Rs.5.21 lakhs, being the balance of unabsorbed investment allowance. While sending the intimation of tax payable/refundable in March 1991 under the summary assessment scheme, the assessing officer accepted the 'nil' income returned by the assessee. However, in view of the judicial decisions and also the Board's instructions, the claim of the assessee for investment allowance should have been disallowed as prima facie inadmissible and the adjustment contemplated in the Act should have been effected. The omission to do so resulted in undercharge of income of Rs.21.64 lakhs involving short levy of tax of Rs.8.68 lakhs in the hands of firm and its partners, including additional tax, interest for default in payment of advance tax and belated filing of return. Further, a sum of Rs.84,060 being interest allowed to the assessee in July 1991 on refund of advance tax should also have been withdrawn. Incidentally, it was seen in audit that the claim of the assessee for carry forward of investment allowance was not allowed by the assessing officer in the assessment for the assessment year 1987-88.

The Ministry has not accepted the audit observation stating that the assessment was completed in a summary manner under section 143(1)(a) of the Act. Since even the assessment under section 143(1)(a) is required to be completed in accordance with law as established by judicial decision and the Board's instructions requiring the assessing officers not to allow investment allowance in respect of a hotel, this is a case of failure to carry out the prescribed adjustment.

4.10 COMPUTATION OF CAPITAL GAINS

Incorrect computation of capital gains

4.10.1 Under the Income Tax Act, 1961, any profits or gains arising from the transfer of a capital asset shall be chargeable to income tax under the head 'capital gains'. The Act also provides that while computing capital gains in case of a depreciable asset, the written down value of the asset at the beginning of the previous year is to be considered for arriving at the capital gains

and such gains, if any, are to be treated as short-term capital gains.

**A- Scrutiny
Assessment**

The assessment of a registered firm, engaged in the business of transport, for the assessment year 1989-90, was completed, after scrutiny, in August 1990 at a total income of Rs.90,982. The assessee firm had its business at various places. During the previous year relevant to the assessment year 1989-90, the firm sold its building at Bombay for a consideration of Rs.29.50 lakhs. An amount of Rs.3.16 lakhs being long-term capital gains was offered for taxation after claiming exemption of Rs.20.64 lakhs, on account of investment in Industrial Development Bank of India bonds and Rs.3.26 lakhs under the provisions of the Act. Scrutiny in audit revealed that assessee had claimed and was allowed depreciation in the past on the property which was sold. As the asset was a depreciable asset, the entire amount of capital gain of Rs.26.79 lakhs was required to be assessed as short-term capital gain, without allowing any exemption/deduction applicable to long-term capital gains. The omission resulted in underassessment of income of Rs.21.23 lakhs and short levy of tax of Rs.12.53 lakhs.

The Ministry has accepted the audit observation.

**B-Summary
Assessment**

4.10.2 The amended provisions of the summary assessment scheme were applicable with effect from 1 April 1989. Under the amended provisions adjustments shall be made to the income of the assessee, inter alia, in regard to any loss carried forward, deduction, allowance or relief which is prima facie admissible or inadmissible.

The assessment of a doctor, for the assessment year 1990-91, was completed in a summary manner in October 1991. The assessee was carrying on professional practice in a flat which was sold for Rs.51 lakhs. As the entire sale proceeds were invested in Industrial Development Bank of India bonds by the assessee, the capital gain arising from the sale of flat was exempted, treating it as long-term capital gain. Audit scrutiny revealed that the flat sold by the assessee was a business asset. The assessee had claimed and was allowed depreciation on it for the assessment years 1973-74 to 1985-86. The assessee had not claimed depreciation on it

from the assessment year 1986-87 onwards but continued to carry on professional practice in the premises till the assessment year 1989-90. Thus the capital gain on the sale of business premises should have been assessed to tax as short-term capital gain without allowing any exemption applicable to long-term capital gains. The mistake resulted in underassessment of income of Rs.49.88 lakhs and short levy of tax of Rs.26.94 lakhs.

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

4.10.3 The mode of computation of capital gains under the Act in respect of a capital asset provides for deduction, from the consideration received, of the cost of the asset and the cost of its improvement. In addition, the Act also provides for a deduction of Rs.10,000 (Rs.15,000 from the assessment year 1992-93) plus a percentage of the excess over Rs.10,000 or Rs.15,000 depending upon the class of the asset, in respect of long-term capital gains. 'Long-term capital gains' means capital gains arising from the transfer of a capital asset held by an assessee for more than thirty-six months immediately preceding the date of its transfer. From the assessment year 1988-89, capital asset being equity or preference shares in a company would be treated as short-term capital asset, if it is held by an assessee for not more than twelve months immediately preceding the date of their transfer. The capital gains arising out of transfer of such shares would be treated as short-term capital gains and no deduction would be admissible.

The assessment of an individual for the assessment year 1989-90 was completed, after scrutiny in November 1990 accepting the returned income of Rs.24.23 lakhs. It was noticed in audit that the assessee was holding debentures of a company. These debentures were converted into shares during the previous year relevant to the assessment year 1989-90 and the assessee sold the shares in the same previous year. However, the assessee treated the above income as long-term capital gains and offered an amount of Rs.5.03 lakhs for taxation. As the asset was not held by the assessee for more than twelve months immediately preceding the date of its transfer, the capital gains should have been treated as short-term capital gains and the

entire amount of Rs.8.07 lakhs should have been taxed. Failure to treat the income as short-term capital gains resulted in underassessment of income of Rs.3.04 lakhs and short levy of tax of Rs.1.60 lakhs.

The Ministry has accepted the audit observation.

4.10.4 The Act further provides that capital gains arising from the transfer of a long-term capital asset other than a residential house is exempt from tax to the extent mentioned therein, if the assessee has, within one year before or two years after the date of transfer, purchased or has within a period of three years after that date constructed a residential house, provided the assessee did not own any other residential house on the date of transfer of the capital asset.

(i) The assessments of two co-owners for the assessment year 1989-90 were completed, after scrutiny, in March 1991, determining the taxable capital gains arising from the transfer of capital asset other than a residential house at Rs.3.32 lakhs each after allowing exemption of Rs.2.63 lakhs in each case on the amount utilised on the construction of a residential house. It was noticed in audit (January 1992) that the assessees owned on the date transfer a residential house, the income from which was chargeable to tax under the head 'income from house property'. Accordingly, they were not eligible for the exemption allowed. The incorrect grant of exemption resulted in aggregate short computation of income of Rs.5.25 lakhs involving a total short levy of tax of Rs.4.21 lakhs, including interest for belated filing of returns and default in payment of advance tax in the two cases.

The Ministry has accepted the audit observation.

(ii) The assessment of two individuals for the assessment year 1989-90 was completed, after scrutiny, in September 1990. The assessees became the joint owners of a warehouse and a residential building after the demise of their father. By an agreement dated 7 March 1988 the assessees agreed to vest all rights in respect of the warehouse to the purchaser for developing the property for a consideration of Rs.23 lakhs. In

terms of the provisions of the Act, the transfer of warehouse property by the assesseees to the purchaser-developer was complete for the purpose of capital gain assessable in the hands of the assesseees. The assesseees claimed exemption from capital gains tax on transfer of capital asset to the extent of the amount invested in a residential house and the claim was allowed by the assessing officer. Since the assesseees owned a residential building on the date of transfer of the original asset, the assesseees were not eligible for exemption from capital gains tax. Thus the incorrect allowance of exemption from capital gains tax resulted in underassessment of income of Rs.5.89 lakhs and short levy of tax of Rs.3.09 lakhs in the hands of both the assesseees.

Subsequent to the audit observation, the department has set aside the assessments.

4.10.5 Under the Income Tax Act, 1961, as applicable from the assessment year 1988-89, any profits and gains arising from the transfer of a capital asset shall be chargeable to income tax under the head 'capital gains' and are taxable in the year in which the transfer took place. The mode of computation of capital gains in respect of long-term capital asset provides for deduction, from the consideration received, of the cost of the asset and the cost of its improvement. In addition, the Act provides for a deduction of Rs.10,000 plus a percentage of the excess over Rs.10,000 depending upon the class of the asset. The Act also provides that these specified deductions shall also be made for the purposes of computing any loss under the head 'capital gains' in so far as it pertains to any long-term capital asset.

**B-Summary
Assessment**

The assessment of an assessee individual for the assessment year 1991-92 was completed in a summary manner in February 1992. Scrutiny in audit revealed that during the previous year relevant to the assessment year the assessee exchanged 5,10,212 equity shares of the cost price of Rs.51.02 lakhs for a consideration of Rs.20.41 lakhs with 1,72,850 equity shares of another company resulting in long-term capital loss of Rs.30.61 lakhs. This long term capital loss was allowed in full as claimed by the assessee. The long-term capital loss was required to be allowed,

after scaling it down by the deductions specified under the provisions of the Act, which would work out to Rs.12.20 lakhs. The mistake resulted in determination of excess loss of Rs.18.41 lakhs with the consequent potential tax effect of Rs.10.06 lakhs and non-levy of additional tax of Rs.2.01 lakhs.

The Ministry has accepted the audit observation.

4.11 ASSESSMENT OF FIRMS

Mistakes in assessments

4.11 Under the Income Tax Act, 1961, in the case of an unregistered firm, the assessing officer may treat the firm as registered firm and assess as such, if the aggregate amount of tax payable by the firm and its partners individually, if it were assessed as a registered firm, would be greater than the aggregate amount of tax payable by the firm and its partners as an unregistered firm.

In the assessment of an assessee firm for the assessment year 1990-91 completed ex-parte in March 1992, the status of the firm was determined as unregistered firm and assessed as such. Audit scrutiny revealed that the aggregate amount of tax payable by the firm and its partners individually, if it had been assessed as a registered firm, would have been more than the amount of tax payable by the firm and its partners as an unregistered firm. Thus the firm should have been assessed as a registered firm. The omission to do so resulted in short levy of tax of Rs.11.31 lakhs, including interest for belated filing of the return and default in payment of advance tax, in the hands of the firm and its partners.

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

4.12 INCOME ESCAPING ASSESSMENT

Income not assessed

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

(i) Audit scrutiny of the assessment records of a firm for the assessment year 1981-82 revealed that as per an agreement of 27 January 1981 the firm had paid to an individual a sum of Rs.5.50 lakhs during the previous years relevant to the assessment year 1981-82 (Rs.75,000) and 1982-83 (Rs.4.75 lakhs) in consideration of withdrawal by the individual of a suit filed in a court of law against a company, from whose estates the firm was engaged in cutting and removing timber. Although the amount so received constituted taxable income, no action was taken by the assessing officer to tax it. The omission resulted in non-levy of tax of Rs.14.73 lakhs, including interest in the hands of the individual for the assessment year 1981-82.

The Ministry has accepted the audit observation.

(ii) Audit scrutiny of the assessment of an assessee individual for the assessment year 1991-92 completed after scrutiny in October 1991 revealed that assessee had shown Rs.2.82 lakhs and Rs.4.30 lakhs pertaining to the assessment years 1984-85 and 1987-88 respectively as liability on the plea that the settlement of compensation received by the assessee was sub-judice. Accordingly, these amounts were not brought to tax in the relevant assessment years. The action was not correct as these amounts were actually received by the assessee. This resulted in underassessment of aggregate income of Rs.7.12 lakhs and short levy of tax of Rs.3.62 lakhs for two years.

The Ministry has accepted the audit observation.

(iii) An association of persons, consisting of seven co-owners of a commercial complex was assessed for the assessment year 1989-90 in March 1991 and the income from house property was allocated to the co-owners for assessment in their hands. Scrutiny in audit revealed that the association of persons had received during the previous year relevant to the assessment year 1989-90, refunds of municipal tax amounting to Rs.2.71 lakhs and interest from a scheduled bank amounting to Rs.9.72 lakhs. These two receipts had not been allocated to the co-owners as income to be taxed in their hands. The omission resulted in underassessment of income of Rs.12.43

lakhs in the hands of seven co-owners. The short levy of tax in the hands of four co-owners having substantial share in the property worked out to Rs.5.91 lakhs.

The Ministry has accepted the audit observation.

(iv) In the assessment of an assessee individual for the assessment year 1986-87, completed in March 1989, receipt of Rs.7.37 lakhs was shown from a number of provident funds as part payments during the previous year relevant to the assessment year 1986-87. Audit scrutiny revealed that there was no evidence to show that the funds were recognised and that the assessee had rendered continuous service for five years or more with her employers. Further, the assessee had received a sum of Rs.1.20 lakhs from various superannuation funds as part payments in the same year. Since the case of the assessee did not fall under the circumstances specified in the Act, this receipt was liable to tax. However, these amounts were not brought to tax. There was consequent underassessment of income of Rs.8.57 lakhs with short levy of tax of Rs.4.71 lakhs.

The department has accepted the audit observation.

Lack of correlation with the records of other taxes

4.12.2 The need for proper co-ordination among 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. Mention in this respect may be made of paragraphs 4.12 and 4.13 of 186th Report (Fifth Lok Sabha) and paragraph 1.19 of the 61st Report (Sixth Lok Sabha) of the Public Accounts Committee. The Central Board of Direct Taxes have also issued instructions, from time to time, for carrying out such correlation with other relevant records. Despite these instructions, instances of under-charge of tax resulting from omission to utilise information already available in the assessment records of other direct taxes continue to be noticed.

(i) A comparison of the wealth tax assessment records of an individual for the assessment years 1985-86 and 1986-87 showed that, during the calendar year 1985, he had made investments totalling Rs.13.22 lakhs, although the funds available therefor, as per

his income tax assessment records for the assessment year 1986-87, could not have been more than Rs.3.84 lakhs. However, no action was taken by the assessing officer to bring to tax the excess amount of Rs.9.38 lakhs as income of the assessee.

The Ministry has accepted the audit observation and raised demand of Rs.5.03 lakhs.

(ii) In the wealth tax assessment of an assessee individual for the assessment year 1985-86 completed in April 1987, the assessing officer disallowed Rs.4.03 lakhs out of the debts claimed by the assessee as deemed dividend received from a private limited company in which the assessee had substantial interest as managing director. The company had sufficient accumulated profits and its equity shares of Rs.10 each were valued at Rs.290.72 as on 31 March 1985 by the department. Since the debts to the extent of Rs.4.03 lakhs claimed in the wealth tax return were treated as deemed dividend in the wealth tax assessment the said sum was also includible as deemed dividend in the income tax assessment of the assessee for the assessment year 1985-86 completed after scrutiny in March 1988. Omission to do so resulted in underassessment of income by the identical sum involving undercharge of tax of Rs.3.80 lakhs, including interest for belated filing of return and short payment of advance tax.

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

Mistakes in giving effect to appellate orders

4.12.3 Under the Income Tax Act, 1961, any interest paid by a partner of a firm out of his determined share income, on the amount of capital borrowed by him for the purposes of investment in the firm, is deductible in computing the income from 'profits and gains of business or profession' In case the amount borrowed is found not invested in the firm, such deduction is not allowable.

(i) An assessee who was a partner in a registered firm, claimed payment of interest out of his determined share income on the capital borrowed from his family members in the assessment years 1981-82 to 1988-89. The deduction claimed was at nine per cent of the capital standing in his personal set of books if the determined share in the firm remained

up to Rs.75,000. In case the amount of share income determined exceeded Rs.75,000, payment by way of additional interest at twenty per cent of such excess to his wife, at twenty per cent to his minor son and at ten per cent of such excess to his minor daughter was claimed according to the terms of the agreement. In the original assessment for the assessment year 1981-82 completed in March 1984, the assessing officer did not allow the deduction, observing that funds of family members were not found invested in the firm but were invested elsewhere, as the credit balance invested with the firm on 31 December 1980 was only Rs.4.34 lakhs, whereas as per his personal set of accounts, his own funds were Rs.7.83 lakhs. This position was upheld by the Commissioner of Income tax (Appeals). In the second appeal by the assessee, the Tribunal observed that in case funds of the family members were found to be utilised elsewhere than in the firm, the assessee was not entitled to the impugned deduction by way of additional interest and referred back the case to Commissioner of Income tax (Appeals) for verification of the above fact. Verification was, in turn, entrusted by the Commissioner of Income tax (Appeals) to the assessing officer, who examined the position of investments in the firm from 1970 to 1979 and on the basis of this, reframed assessments for the assessment years 1981-82 to 1988-89 in which additional interest as originally claimed by the assessee on the basis of the agreement referred to above, was allowed. Audit scrutiny, however, revealed that the position of investment of funds of the family members, as well as, funds of the assessee himself as prevailing on 31 December 1980, was holding good even on 31 December 1987. According to the balance sheet of the assessee on this date, the credit balance invested in the firm was only Rs.14.10 lakhs, while as per the personal set of accounts, the assessee's own funds available were Rs.18.40 lakhs and the funds of family members were to the tune of Rs.21.89 lakhs. Thus funds of the family members could not be said to have been invested in the firm. Thus, in view of the Tribunal's directions, the assessee was not entitled to the deduction of additional interest beyond the normal interest at nine per cent already allowed by the Commissioner of Income tax (Appeals). As such the re-assessments on account of allowing the aforesaid deduction of additional interest were contrary to the

orders of the appellate authority which led to underassessment in all the eight assessment years. Consequent short charge aggregated Rs.23.72 lakhs.

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

(ii) Assessment of a registered firm for the assessment year 1984-85 was completed in March 1987 at a total income of Rs.24.22 lakhs. Appeal of the assessee was partly allowed and the assessment on certain points was set aside. The assessment was revised to give effect to appellate order in part in January 1990, leaving the issues which needed recomputation after further scrutiny, and the revised income was computed at Rs.24.06 lakhs. The revised assessment was again rectified in March 1991 to withdraw the investment allowance of Rs.14.83 lakhs granted to the assessee in the assessment year 1984-85 as the plant and machinery was sold before the stipulated period, and income computed at Rs.38.89 lakhs. It was, however, noticed in audit that while completing the reassessment in March 1992 to consider the issue of brokerage which was earlier set aside by the Commissioner of Income tax (Appeals), the rectification order passed in March 1991 withdrawing the investment allowance was ignored and the income of Rs.24.06 lakhs instead of Rs.38.69 lakhs was adopted as the starting point for the recomputation. The mistake resulted in underassessment of income of Rs.14.83 lakhs and short levy of tax of Rs.10.09 lakhs in the hands of the firm and its partners.

The Ministry has accepted the audit observation.

4.13 SET OFF OR CARRY FORWARD OF LOSSES

**Incorrect
set off or
carry
forward of
losses**

4.13.1 Under the Income Tax Act, 1961, where a change has occurred in the constitution of a firm due to the death or retirement of a partner, the loss of the previous year proportionate to the share of the deceased or retired partner, computed under the provisions of the Act, if any, shall not be allowed to be carried forward for set off against the income of the firm in the subsequent year.

In the assessment of an unregistered firm for the assessment year 1988-89 completed in

March 1989, the entire income of Rs.49.67 lakhs was set off against the business loss of Rs.122.02 lakhs pertaining to the assessment years 1986-87 and 1987-88 and the balance of Rs.72.35 lakhs was allowed to be carried forward. Audit scrutiny revealed that two of the five partners enjoying the aggregate share of 30 per cent had retired from the partnership with effect from 1 April 1987. The proportionate share of loss of Rs.36.60 lakhs of the retired partners was set off against their proportionate share of profit of Rs.11.18 lakhs for the period up to 31 March 1987. The balance amount of Rs.25.42 lakhs was set off in the assessment of the firm for the assessment year 1989-90 completed in February 1992. The incorrect set off of loss of Rs.25.42 lakhs resulted in undercharge of tax of Rs.21.16 lakhs in the hands of the firm and its partners in the assessment year 1989-90, including interest in the hands of the firm for default in payment of advance tax.

The Ministry has accepted the audit observation.

4.13.2 Under the Income Tax Act, 1961, loss of an unregistered firm is not to be allocated amongst the partners of the firm, as they are not entitled to set off such loss against their personal income but shall be carried forward and set off against the income of the firm in the subsequent assessment years.

The assessment of an assessee firm for the assessment year 1989-90 was completed, after scrutiny, in February 1992. As the assessee had not filed the necessary documents, registration was not granted and the assessee's status was treated as an unregistered firm under the relevant provisions of the Act. However, it was seen in audit that the loss of the unregistered firm was allocated amongst the two partners of the firm and the allocated loss was partly set off against other income and the balance was carried forward in one of the partners' cases made available to audit. The firm having been assessed in the status of unregistered firm, the loss should have been carried forward and set off in the hands of the firm only. The mistake resulted in incorrect carry forward of loss in respect of two partners to the extent of Rs.10.91 lakhs with potential tax effect of Rs.5.80 lakhs in

the hands of two partners.

The Ministry has accepted the audit observation.

4.14 IRREGULAR EXEMPTIONS AND EXCESS RELIEFS GIVEN

Incorrect relief in respect of profits from industrial undertaking set up in free trade zones.

4.14.1 The Income Tax Act, 1961, provides for complete tax exemption in respect of the profits and gains derived from an industrial undertaking set up in any Free Trade Zone for a period of initial five assessment years.

In completing the assessment of two assessee individuals, deriving share income from a registered firm in Kandla Free Trade Zone, for the assessment year 1988-89 in February 1989 and November 1990, the assessing officer allowed exemption of Rs.55.06 lakhs to each assessee. Audit scrutiny revealed that as the first assessment year for which tax exemption was allowed was 1983-84, the exemption was admissible only up to the assessment year 1987-88 and not for the assessment year 1988-89. The incorrect allowance of exemption for the assessment year 1988-89 thus resulted in underassessment of income of Rs.110 lakhs with consequent short levy of tax of Rs.57.81 lakhs in respect of the two assessees, besides interest for non-payment of advance tax.

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

Mistakes in allowing deduction under Chapter VI-A

4.14.2 Chapter VI-A of the Income Tax Act, 1961, allows certain deductions 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 of the Act before making the deductions under chapter-VIA, but after setting off unabsorbed losses, depreciation etc. of earlier years.

In the assessment of a registered firm for the assessment years 1988-89 and 1990-91, completed in December 1991, the gross total income was computed at Rs.13.64 lakhs and Rs.9.44 lakhs respectively and deduction of Rs.5.46 lakhs and Rs.3.77 lakhs respectively

were allowed under chapter VI A. However, as per the provisions of the Act, the gross total income, computed after setting off unabsorbed depreciation of Rs.13.29 lakhs and Rs.7.31 lakhs (net), worked out to only Rs.35,863 and Rs.2.13 lakhs respectively. The assessee was thus entitled to deduction of Rs.14,345 and Rs.85,130 respectively under chapter VI A of the Act for assessment years 1988-89 and 1990-91, as against Rs.5.46 lakhs and Rs.3.77 lakhs allowed. These mistakes resulted in aggregate excess allowance of deduction of Rs.8.24 lakhs involving short levy of tax of Rs.4.54 lakhs in the hands of the firm and its partners.

The Ministry has accepted the audit observation.

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

4.14.3 Under the Income Tax Act, 1961, where the gross total income of an assessee 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 per cent of such profits and gains for a period of eight years including the year in which the assessee begins to manufacture or produce articles or things. Where the assessee is also entitled to deduction in respect of profits and gains from newly established industrial undertaking in backward areas in addition to the deduction mentioned above, effect shall first be given to the latter deduction before allowing the former deduction.

A-Scrutiny Assessment

While completing the assessment of a co-operative sugar mill for the assessment year 1989-90 in December 1990 and subsequently revising it in February 1991, the assessee co-operative society was allowed deduction of Rs.76.79 lakhs in respect of profits and gains of a new industrial undertaking. The assessee was also allowed deduction of an equal amount in respect of new industrial undertaking established in backward areas. Both the deductions were worked out at twenty per cent of the profits and gains. However, the deduction in respect of profits and gains from new industrial undertaking established after 31 March 1981 should have been calculated after allowing deduction in respect of new industrial undertaking established in backward areas. On this basis

the assessee was entitled to a deduction of Rs.61.43 lakhs as against Rs.76.79 lakhs allowed. The mistake resulted in short levy of tax of Rs.9.16 lakhs (including interest).

The department has accepted the audit observation.

**B-Summary
Assessment**

4.14.4 The amended provisions of the summary assessment scheme were applicable with effect from 1 April 1989. Under the amended provisions, adjustments shall be made to the income of the assessee, inter alia, in regard to any loss carried forward, deduction, allowance or relief, which is prima facie admissible or inadmissible.

In the assessment of an assessee registered firm for the assessment years 1987-88 and 1989-90 completed, in a summary manner in March 1990, the assessing officer allowed, in computing the taxable income, a deduction aggregating Rs.26.47 lakhs in respect of profits and gains derived from new industrial undertaking. Scrutiny in audit revealed that the industrial undertaking came into existence prior to the assessment year 1975-76 and thus was not eligible for deductions in these assessment years. Further, the assessee was allowed a deduction of Rs.2.64 lakhs and Rs.10.57 lakhs at twenty per cent of the profits of Rs.13.20 lakhs and Rs.52.85 lakhs for the assessment year 1987-88 and 1989-90 respectively in respect of profits and gains derived from new industrial undertaking established in backward area. Identical amount of deduction was also allowed for the two assessment years in respect of profits derived from new industrial undertaking established after 31 March 1981. As the assessee was allowed both the deductions, the one in respect of profits and gains from new industrial undertaking established after 31 March 1981 should have been allowed at twenty per cent on the profits and gains as reduced by the deduction allowed in respect of profits and gains from new industrial undertaking established in backward area. The admissible deduction would thus work out to Rs.2.11 lakhs and Rs.8.46 lakhs at twenty per cent on the balance of profits of Rs.10.56 lakhs and Rs.42.28 lakhs for the assessment years 1987-88 and 1989-90 respectively as against which the deduction of Rs.2.64 lakhs and 10.57 lakhs was allowed resulting in the grant of excess relief

aggregating Rs.2.65 lakhs for two years. The total underassessment of income worked out to Rs.29.11 lakhs with consequent short levy of tax of Rs.23.05 lakhs in the hands of the firm and its partners for two years.

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

Incorrect allowance of relief in respect of export turnover

4.14.5 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. In a case where the business carried on by the assessee does not consist exclusively of export out of India of goods or merchandise (other than mineral oil and mineral ores), 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.

A-Scrutiny Assessment

(i) The assessment of a registered firm for the assessment year 1989-90 was completed, after scrutiny, in March 1992, at a total income of Rs.28.85 lakhs after allowing deduction of Rs. 116.56 lakhs in respect of export profit. The assessee's main business was export of diamonds and it had also income from trading service charges, commission on labour charges, premium on sale of licence, etc. Audit scrutiny revealed that the assessee was in the practice of accounting the net receipts under some of these accounts. The assessee had received premium of Rs.63.92 lakhs on sale of licences, while the profit and loss account was credited with the amount of Rs.2.53 lakhs. Similarly, net receipts only were accounted under labour charges received, exchange rate difference, etc. By exhibiting the net figures under these account heads, the amount of total turnover for the purpose of deduction in respect of export turnover was understated to the extent of Rs.288.30 lakhs. This had the effect of enhancement in the claim for deduction for export business profit to the extent of Rs.14.64 lakhs which was admitted

by the assessing officer. The mistake resulted in underassessment of income of Rs.14.64 lakhs and short levy of tax of Rs.14.16 lakhs in the hands of the firm and its partners.

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

(ii) Assessments of two registered firms for the assessment year 1990-91 were completed, after scrutiny, in March 1991. Both the assesseees had maintained their respective combined accounts for export turnover as well as local turnover. The statutory accountants of the firms furnished certificates in the prescribed form determining the proportionate profits attributable to the export turnover in respect of the two assessee firms separately and thereto added amounts of Rs.2.46 lakhs and Rs.2.31 lakhs respectively on account of sales tax paid in India, to arrive at the total deductions allowable from the income derived from the export business. The calculations were accepted in both these cases by the assessing officer. However, addition of sales tax to the relief allowable in respect of export turnover on the ground that the export turnover is exempt from sales tax is not correct as the amount adopted as total turnover to arrive at the combined profits derived already included sales tax. The incorrect accounting of sales tax twice in computing the profits derived from exports resulted in short levy of tax aggregating Rs.3.38 lakhs in the hands of both the firms and their partners.

The Ministry has accepted the audit observation.

**B-Summary
Assessment**

4.14.6(i) In the assessment of a registered firm for the assessment year 1990-91 completed under the summary assessment scheme in March 1991, the assessee was allowed a deduction of Rs.70.85 lakhs. From the computation it was seen in audit that export turnover included 'import licence premium' and 'cash assistance' aggregating Rs.40.96 lakhs. Since the income of the assessee was not exclusively from export business, he would be entitled to a proportionate deduction excluding receipts from import licence premium and cash assistance, as provided in the Act. The allowable deduction

on account of profits from export would thus work out to Rs.59.51 lakhs instead of Rs.70.85 lakhs allowed by the assessing officer. The mistake resulted in excess allowance of deduction of Rs.11.34 lakhs leading to underassessment of income by an identical amount involving undercharge of tax of Rs.9.96 lakhs, including additional tax in the hands of the firm and its partners.

The Ministry has accepted the audit observation.

(ii) A registered firm, engaged in the business of trading in automobile spare parts, had offices at Bombay and Baroda. The business at Bombay consisted exclusively of export out of India, while there were only local sales at Baroda. For the assessment year 1990-91, the entire export profit from Bombay amounting to Rs.38.25 lakhs was claimed as deduction in respect of export turnover and income of Rs.12.95 lakhs from business at Baroda only was returned for taxation. While completing the assessment in a summary manner in February 1991, the returned income was accepted by the department allowing the deduction claimed. The total turnover of the assessee firm for the previous year relevant to the assessment year 1990-91 was Rs.354.45 lakhs and the turnover for export of goods and merchandise qualifying for deduction was Rs.172.49 lakhs. The taxable profits of the business was Rs.51.19 lakhs. The assessee firm was, therefore, entitled to a deduction of Rs.24.98 lakhs in respect of export turnover as against Rs.38.25 lakhs claimed by the assessee and allowed by the assessing officer. The mistake resulted in underassessment of income of Rs.13.26 lakhs involving short levy of tax of Rs.8.74 lakhs in the hands of the firm and its partners.

The Ministry has accepted the audit observation.

Incorrect exemption in the case of co-operative society.

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

**A-Scrutiny
Assessment**

An assessee being a co-operative society had debited Rs.100.81 lakhs, Rs.187.54 lakhs, Rs.270.33 lakhs and Rs.272.25 lakhs in its profit and loss account for the previous years relevant to the assessment years 1985-86, 1986-87, 1987-88 and 1988-89 respectively as provision for unrealised overdue interest and the same was allowed as a deduction by the assessing officer in the assessment completed in March 1991. The provisions made by the assessee in the accounts relevant to a particular assessment year was actually written off in the accounts of the following assessment year. The provision which was not actually written off and not considered bad was not deductible. Omission to disallow the provision resulted in excess computation of proportionate expenditure in working out income from interest on term deposits (in the absence of separate accounts) with consequent short levy of tax of Rs.18.17 lakhs, including interest for delay in filing the return and non-payment of advance tax.

The Ministry has accepted the audit observation.

4.14.8 Under the Income Tax Act, 1961, the whole amount of the profits and gains of a co-operative society attributable to certain specified activities are allowed as deduction in computing its taxable income. Accordingly, a co-operative society carrying on the business of banking or providing credit facilities to its members is entitled to the aforesaid deduction. Further, income by way of interest or dividends derived by a co-operative society, would be entitled to such exemption from tax. However, the Act does not provide for full exemption from tax of the profits and gains of such co-operative societies derived from activities other than those specified therein. The provisions in this regard restrict the deduction to twenty thousand rupees in the case of non-specified activities (forty thousand rupees in the case of a consumers' co-operative society).

**B-Summary
Assessment**

An assessee co-operative society was engaged in carrying on banking business and providing credit facilities to its members. During the previous year relevant to the assessment year 1989-90, the assessee received Rs.14.49 lakhs on account of interest on fixed deposit kept with an electric supply company. The deposit was made out of surplus fund of the society.

In the assessment for the assessment year 1989-90, completed in December 1989 in a summary manner, the total income of the assessee society was computed at 'nil' after accepting the claim of the assessee for exemption of the entire interest income. As the money was kept in fixed deposit with a company (not a co-operative society) for earning interest income only and not utilisable for specified activities of a co-operative credit society, the assessee was not eligible for full exemption of the aforesaid income, but for only twenty thousand rupees thereof, the income being from 'other sources' and not attributable to specified activities. The omission to restrict the deduction to twenty thousand rupees resulted in underassessment of income by Rs.14.29 lakhs involving under-charge of tax of Rs.7.80 lakhs, including additional tax and interest for non-payment of advance tax.

The Ministry has accepted the audit observation.

Incorrect deduction in respect of professional income from foreign sources in certain cases

4.14.9 Under the Income Tax Act, 1961, before its amendment by Finance Act, 1990, with effect from 1 April 1991, where the gross total income of an individual resident in India, being an author, playwright, artist, musician, actor or sportsman, includes any income derived by him in the exercise of his profession from the Government of a foreign State or any person not resident in India and such income is received in or brought into India by him or on his behalf in accordance with the Foreign Exchange Regulation Act, 1947 and any rules made thereunder, there shall be allowed a deduction from such income of an amount equal to twenty-five per cent of the income so received or brought in, while computing the total income of the individual.

In the case of two individual assesseees, the assessing officer, while completing the assessments for the assessment years 1988-89 and 1989-90 in a summary manner between July 1989 and February 1990, allowed deduction of Rs.2.80 lakhs and Rs.6.22 lakhs out of their share of income from the firm which was engaged in the profession of photography. The irregular deduction resulted in under-assessment of income of Rs.9.02 lakhs and short levy of tax of Rs.5.72 lakhs, including additional tax and interest.

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

4.15 NON-LEVY OR INCORRECT LEVY OF INTEREST AND PENALTY

Interest for delay in payment of tax demand

4.15.1 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 a 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 the demand. 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.

Four illustrative cases involving non-levy of interest aggregating Rs.15.10 lakhs for delay in payment of tax demand are given below:

Sl. No.	State/Commissioners' charge/Name of the assessee	Assessment year/date of assessment	Brief facts	Non-levy of interest (in lakhs of rupees)
1.	Andhra Pradesh Central II, Madras Two Individuals	1986-87/1989-90 February 1991/ March 1991	Tax demands of Rs.8.61 lakhs and Rs.32.26 lakhs respectively were raised in February 1991 and April 1991. The entire demand was paid by one assessee between March 1991 and March 1992, while only a part of the demand was paid by the second assessee between March 1991 and March 1992.	5.62
2.	Tamil Nadu Madurai/ Individual	1988-89 August 1991	Refund of Rs.7.63 lakhs for the assessment year 1988-89 including interest of Rs.2.32 lakhs payable by Government was adjusted against demand aggregating Rs.6.83 lakhs for the assessment years 1980-81 to 1986-87 raised between March 1986 and February 1989 which remained unpaid.	5.52

3.	Tamil Nadu Central II, Madras Individual	1984-85 March 1987	In the assessment completed in March 1987 the tax payable was computed at Rs.33.28 lakhs which was later reduced to Rs.33.13 lakhs in the appellate revision in May 1988. The entire demand of tax less tax paid in advance was paid by the assessee between October 1987 and October 1988.	3.96
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The Ministry has accepted the audit observations.

Interest for delay in filing the return

4.15.2 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, if any, paid and the tax deducted at source, if any. In other words, interest payable is calculated on the balance of tax payable after adjusting the advance tax paid and tax deducted at source.

(i) The returns of income for the assessment years 1986-87 and 1987-88 were submitted by an assessee unregistered firm on 21 August 1990, in response to a notice issued by the assessing officer in August 1988. The assessments were completed in February 1991 and March 1991 respectively. The specified due dates for the submission of the returns were 30 June 1986 and 31 July 1987. The assessee was, therefore, in default as regards submission of the returns and was liable to pay interest of Rs. 10.04 lakhs and Rs.5.54 lakhs respectively. Audit scrutiny revealed that the assessing officer levied interest of Rs.4.71 lakhs and Rs.3.54 lakhs respectively for the assessment years 1986-87 and 1987-88. The mistake resulted in short levy of interest aggregating Rs. 7.33 lakhs for the two assessment years. Further, it was noticed that the assessing officer had levied interest of Rs.9.84 lakhs for default in

payment of advance tax for the assessment year 1986-87 instead of the correct amount of Rs.11.89 lakhs. Thus the total tax effect worked out to Rs.9.38 lakhs.

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

(ii) The return for the assessment year 1989-90 was submitted by an assessee co-operative society on 31 October 1990. The assessment was completed, after scrutiny, in March 1992 at a total income of Rs.36.16 lakhs. The specified due date for submission of the return was 31 October 1989. The assessee had, therefore, defaulted in submitting the return for the period from November 1989 to October 1990 and was liable to pay interest. The assessing officer, however, failed to levy the interest of Rs.3.63 lakhs which was payable.

The Ministry has accepted the audit observation.

Interest for short payment of advance tax

4.15.3 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 per cent (ninety per cent from 1 April 1989) of the tax determined on regular assessment, interest at fifteen per cent per annum (two per cent 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. It has been judicially held* that the initial order of assessment gets effaced by appellate or revision order and the only effective order is the ultimate order of the superior authority. The original order of assessment becomes part of the entire proceedings culminating in the ultimate order which, for all practical purposes, should be treated as an order of regular assessment. The Court further held that the provisions under which interest is payable by the assessee or Government were comparable and there was substantial reciprocity between the class of tax payers and the Government in these provisions. It has also been held that as both the

*179-ITR-580 (Cal), 183-ITR-299 (Kar)

provisions cover two aspects of the same situation, logically both of them should bear the same meaning.

**A-Scrutiny
Assessment**

(i) In the assessment of an assessee, an individual, for the assessment year 1989-90 completed after scrutiny in March 1992, it was noticed in audit that the assessing officer calculated interest for default in payment of advance tax on the assessed tax of Rs.11.81 lakhs for the period from 1 April 1989 to the date of processing the return in November 1989 instead of up to the date of regular assessment in March 1992. The mistake resulted in short levy of interest of Rs.6.43 lakhs.

The Ministry has accepted the audit observation.

(ii) The assessment of an assessee, association of persons, for the assessment year 1989-90 was completed at a total income of Rs.38.11 lakhs. As the advance tax paid fell short of the ninety per cent of the tax determined on regular assessment, interest of Rs.3.96 lakhs was levied by the assessing officer. However, the correct amount of interest leviable was Rs.9.36 lakhs. There was thus short levy of interest of Rs.5.40 lakhs.

The Ministry has accepted the audit observation.

(iii) Assessments of two assessee individuals, for the assessment year 1989-90 were completed in March 1992. It was noticed in audit that interest of Rs.4.26 lakhs and Rs.96,096 was levied for failure to file the estimates of advance tax and for non-payment of advance tax, instead of the correct amount of Rs.6.66 lakhs and Rs.2.47 lakhs respectively. There was thus aggregate short demand of interest of Rs.3.92 lakhs.

The Ministry has accepted the audit observation.

(iv) In the assessment of an individual for the assessment year 1989-90 completed after scrutiny, in March 1992, the assessing officer had levied interest of Rs.1.66 lakhs for non payment of advance tax, from 1 April 1989 to the month of processing of the return

in a summary manner in February 1990. Interest was however, chargeable at Rs.5.45 lakhs for a period of 36 months from 1 April 1989 to 31 March 1992. The mistake resulted in short levy of interest of Rs.3.79 lakhs.

The Ministry has accepted the audit observation.

**B-Summary
Assessment**

4.15.4 In the assessment of an 'association of persons' for the assessment year 1990-91 completed in a summary manner, in September 1991, the assessing officer made an addition of Rs.146.89 lakhs to the income returned by the assessee and tax payable was worked out. Scrutiny in audit revealed that interest for short payment of advance tax was, however, not levied on the plea that unabsorbed depreciation and losses of earlier years were to be considered at a later stage by issue of notice to the assessee. It was noticed from the computation of income filed by the assessee along with the return that there was no unabsorbed depreciation or loss to be adjusted against the current years profit. Thus the interest for default in payment of advance tax should have been levied. Omission to do so resulted in non-levy of interest of Rs.19.64 lakhs.

The Ministry has accepted the audit observation.

**Omission to
levy penalty**

4.15.5 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 lakh 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 due date. The specified due date for filing the return for business cases where the assessee is a company is 31 December and in any other case 31 October of the assessment year. Failure to get the accounts audited and to obtain the audit report within the due dates renders the assessee liable to penalty equivalent to one half per cent of the turnover 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.

(i) Out of eleven cases relating to the assessment years 1989-90 to 1991-92 where total sales in the relevant assessment years exceeded Rs.40 lakhs, it was seen that in one case, audit had not at all been conducted, in another case audit report was not signed by the authorised accountant and in the remaining nine cases audit reports were not obtained before the specified due date. The assesseees were liable to pay penalty aggregating Rs.9.03 lakhs.

The department has accepted the audit observation in five cases. The Ministry has accepted the audit observation in one case.

(ii) In the assessment of four registered firms, for the assessment years 1986-87 to 1989-90 completed between March 1988 and January 1990, it was seen in audit that although the assesseees were required to get their accounts audited by an authorised accountant and furnish the reports of such audit in the prescribed form within the specified due date, such audit reports were neither furnished within the specified date, nor insisted upon by the assessing officer. The assesseees were therefore liable to pay penalty of Rs.3.94 lakhs.

The department has accepted the audit observation.

4.15.6 Under the Income Tax Act, 1961, if the assessing officer is satisfied in the course of any proceedings under the Act, that the assessee has concealed the particulars of income or furnished inaccurate particulars thereof 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 the amount of tax sought to be evaded. Further, when the person liable to such penalty is a registered firm or an unregistered firm which has been assessed as registered firm under the provisions of the Act, the penalty imposable shall be the same amount as would be imposable on that firm as if that firm were an unregistered firm.

The assessments of two registered firms, one for the assessment year 1987-88 and another for the assessment years 1987-88 and 1989-90 were completed, after scrutiny, in March 1990 and February 1991 respectively. The income concealed by the first firm for the assessment year 1987-88 was Rs.14.48 lakhs

and by the other firm for the two assessment years 1987-88 and 1989-90 was Rs.1.90 lakhs. The assessing officer in his order passed in April 1991 and January 1992 levied a penalty of Rs.3.48 lakhs on the first firm and Rs.41,370 on the other firm respectively. However, it was seen in audit that while calculating the amount of tax sought to be evaded, the tax was calculated as if the firms were registered instead of treating them as unregistered. The total short levy of penalty thus worked out to Rs.4.27 lakhs.

The Ministry has accepted the audit observation.

4.16 OTHER TOPICS OF INTEREST

Unexplained investment

4.16.1 Under the Income Tax Act, 1961, where in the financial year immediately preceding the assessment year, the assessee has made investments which are not recorded in the books of account and the assessee offers no explanation about the nature and source of the investments or the explanation offered by him is not found satisfactory, the value of such investments may be deemed to be the income of the assessee.

During the assessment proceedings of an individual, for the assessment year 1986-87, it was noticed that the assessee had constructed a cinema building, the cost of which was disclosed by him at Rs.6.59 lakhs. On a reference, the departmental valuer in his report of January 1987 estimated the cost of the building at Rs.16.33 lakhs and the period of construction from March 1977 to March 1983. As the assessments for the assessment years 1978-79 to 1983-84 based on the returned investments of Rs.6.59 lakhs had already been completed in 1983-84 and 1984-85, the assessing officer obtained the permission of the Commissioner of Income tax in March 1987 to initiate proceedings for making out fresh assessments after incorporating the additions of Rs.9.74 lakhs to the taxable income on account of the difference between the cost of construction as estimated by the departmental valuer and the cost as disclosed by the assessee. The difference in the cost of construction, which remained totally unexplained, was liable to be taxed in the hands of the assessee as per the provisions of the Act. It was, however,

noticed that the assessing officer, while making fresh assessments for the assessment years 1978-79 to 1983-84 in January 1990, made additions aggregating Rs.54,000 only as against Rs.9.74 lakhs initially proposed to be taxed as unexplained investments without recording any reason. This resulted in escapement of income of Rs.9.20 lakhs involving tax effect aggregating Rs.13.27 lakhs over the assessment years 1978-79 to 1983-84.

Subsequent to the audit observation, the department has passed orders cancelling the earlier assessments.

Incorrect allowance of contribution to gratuity fund

4.16.2 Under the Income Tax Act, 1961, no deduction shall be allowed in respect of any provision for gratuity to employees on retirement or on termination of employment for any reason, unless it is by way of contribution towards an approved gratuity fund or for payment of gratuity that has become payable during the previous year.

While processing in a summary manner, the return of income of an association of persons, for the assessment year 1989-90, in March 1990, the assessing officer allowed Rs.15 lakhs towards contribution to gratuity fund, as a deduction. It was, however, noticed from the comments included in 'Auditor's Notes' to the relevant accounts that there was no approved gratuity fund of the assessee during the previous year relevant to assessment year 1989-90 and therefore the allowance of gratuity provision of Rs.15 lakhs in the assessment year 1989-90 was not in order. The mistake resulted in underassessment of income of Rs.15 lakhs involving a total revenue effect of Rs.11.34 lakhs, including additional tax and interest for short payment of advance tax.

The department has accepted the audit observation.

CHAPTER 5

OTHER DIRECT TAXES

A - WEALTH TAX

General

5.1 In the financial years 1988-89 to 1992-93, wealth tax receipts as against budget estimates were as given below:

Year	Budget Estimates (In crores of rupees)	Actuals	Variation	Percentage
1988-89	120.00	122.48	02.48	02.06
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

*Provisional

5.2 Particulars of assessments completed, assessments pending and demands in arrear for the last five years ending 31 March 1993 were as 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)
1988-89	6,95,326	3,19,267	406.78
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

* Provisional

Results of Audit

5.3 During the test audit of assessments completed under the Wealth Tax Act, 1957, conducted during the period 1 April 1992 to 31 March 1993, short levy of wealth tax of Rs.11.74 crores was noticed in 1308 cases.

A total number of 86 draft paragraphs involving tax effect of Rs.176.93 lakhs were issued to the Ministry of Finance for comments during March to August 1993. The Ministry of Finance have accepted the observations in 46 cases involving tax effect of Rs.67.01 lakhs. 21 illustrative cases involving tax effect of Rs.105.10 lakhs are

given in the succeeding paragraphs. While paragraphs 5.4 to 5.7 are on wealth tax on assesseees other than companies, paragraph 5.8 relates to company cases. Out of these, the Ministry of Finance have accepted the observations in 11 cases involving tax effect of Rs.36.58 lakhs . 2 cases involving tax effect of Rs.8.94 lakhs were checked by the Internal Audit of the department but the mistakes were not detected by them.

**Wealth tax
on assesseees
other than
companies**

5.4 Under the Wealth Tax Act, 1957, wealth tax on assesseees other than companies is chargeable in respect of each assessment year on the net wealth of the assesseees 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.

**Wealth not
assessed**

5.4.1 The wealth tax assessments for the assessment years 1982-83 and 1983-84, of an individual (who was the beneficial owner of a firm) were completed in March 1987 and March 1988 at total wealth of Rs.63.37 lakhs and Rs.66.00 lakhs respectively. Audit scrutiny revealed that while finally revising (March 1990) the assessments of the firm, additions aggregating Rs.27.04 lakhs and Rs.70.45 lakhs on account of certain bogus transactions (including unexplained purchase of demand draft of Rs. 1 lakh in 1983-84) were made in assessment years 1982-83 and 1983-84 respectively. Since these additions constituted a part of the capital of the firm for the respective assessment years and the assessee himself was the beneficial owner of the firm, these should have been included in the assessable wealth of the assessee. Omission to re-open the wealth tax assessments for the assessment years 1982-83 and 1983-84 resulted in the aggregate non-assessment of wealth of Rs.97.49 lakhs with consequent short levy of tax of Rs.4.65 lakhs.

The Ministry has accepted the audit observation.

5.4.2 The Act also provides for the levy of penalty, inter-alia, if an assessee has, without reasonable cause, failed to furnish the wealth tax return within the prescribed time or concealed the particulars of any asset or furnished inaccurate particulars of any asset or debt.

Audit scrutiny of income tax returns of an assessee, for the assessment years 1983-84 to 1989-90, disclosed that the assessee owned wealth consisting of jewellery, house property, cash and capital investment in a partnership firm, of a gross value of Rs.176.52 lakhs which was liable to wealth tax under the Act. The assessee did not file any return of wealth nor did the department initiate wealth tax proceedings. The omission resulted in non-assessment of net wealth aggregating Rs.152.54 lakhs (after the initial basic exemption) with consequent non-levy of wealth tax of Rs.2.35 lakhs (including interest). Further, penalty provisions for non-filing of return and concealment of wealth were also attracted.

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

5.4.3 The Central Board of Direct Taxes issued instructions (November 1973, April 1979 and September 1984) for proper co-ordination amongst assessment records pertaining to different direct taxes, with a view to bringing to tax, cases of evasion of tax.

In the wealth tax assessment of an individual, for the assessment year 1979-80, completed in March 1985, the assessing officer observed that the assessee received compensation of Rs.13.82 lakhs including interest on solatium in February 1982 and added an amount of Rs.11.33 lakhs, being compensation receivable, to the wealth declared for the assessment year 1979-80 after giving discount for three years, as per the order of Commissioner of Income Tax (Appeals). The income tax assessment records of the assessee for the assessment year 1986-87 disclosed that the assessee received an additional compensation of Rs.10.72 lakhs in the year 1985. Audit scrutiny revealed that this additional compensation and interest thereon should also have been included in the wealth of the assessee for the assessment years 1979-80 to 1983-84. However, the

assessee did not return the aforesaid amount in his wealth tax returns nor did the department include the same in the wealth in the assessments completed between 1985 and 1988. The omission resulted in under assessment of wealth of Rs.48.30 lakhs with consequent short levy of tax of Rs.2.18 lakhs.

Subsequent to the audit observation, the department initiated remedial action.

5.4.4 Under the Wealth Tax Act, 1957, in the case of assets held by a trustee on behalf of another person, wealth tax shall be levied upon and recoverable from the trustee in like manner and to the same extent as it would be leviable upon and recoverable from the person on whose behalf the assets are held.

A private trust was created in August 1980 by an individual for the benefit of another member of his family. It had two trustees. Audit scrutiny of the income tax assessment records of the trust for the assessment year 1990-91 and earlier years revealed that the total value of its assets (Rs.49.14 lakhs as on 31 March 1990, Rs.60.16 lakhs as on 31 March 1989, and Rs.44.82 lakhs as on 31 December 1987) far exceeded the exemption limit for wealth tax. However, the assessee had not filed any wealth tax return for any of the assessment years. The department too did not initiate any wealth tax proceedings. The omission resulted in non-levy of wealth tax aggregating Rs.3.89 lakhs.

The Ministry has accepted the audit observation.

**Incorrect
valuation of
assets**

5.5.1 Immovable properties

Under the Wealth Tax Act, 1957, the wealth tax officer shall estimate the value of any asset (other than cash) to be the price which in his opinion it would fetch, if sold in the open market on the valuation date. With effect from 1 April 1989, the value on the valuation date of any immovable property, being a building or land appurtenant thereto, shall be the amount arrived at by multiplying the net maintainable rent by the figure 12.5. The Act further provides that the net

maintainable rent shall be derived from the gross maintainable rent by deducting therefrom the amount of taxes levied by a local authority in respect of the property and a sum equal to fifteen per cent of the gross maintainable rent.

**A-Scrutiny
assessment**

(i) The wealth tax assessments of an individual, for the assessment years 1989-90 and 1990-91, were completed in October 1991, adopting the value of a building situated in a metropolitan city at Rs.50.75 lakhs, as returned by the assessee. Audit scrutiny revealed that the said property was let out by the assessee on a monthly rent of Rs.1.40 lakhs. Calculated on the basis of the Schedule to the Act, the value of the property worked out to Rs.194.44 lakhs. Omission to adopt this value in the assessments resulted in underassessment of wealth of Rs.287.38 lakhs involving short levy of wealth tax aggregating Rs.6.76 lakhs, including interest for the two assessment years.

The Ministry has not accepted the audit observation on the ground that wealth tax assessments are in consonance with the income tax assessments, wherein the lease rent has been assessed under the head 'other sources'. The reply is not tenable in view of the valuation provisions under Rule 3 read with Rule 5(2) of Schedule III of the Wealth Tax Act which are mandatory and binding from 1 April 1989 and according to which rent shall include all payments for the use of the property by whatever name called.

(ii) The Wealth Tax Act, 1957, provides that the assessing officer may make a reference to the Departmental Valuation Officer for valuation of the assets. The Act also provides that the order of the valuation officer in respect of the value of the asset would be binding on the assessing officer.

An individual and a Hindu undivided family, each having 7/32 share in a registered firm which owned a building complex in a city, filed wealth tax returns for the assessment years from 1983-84 to 1987-88. The share interest of 7/32 as returned by the assessee was based on the fair market value of the building complex at Rs.130.23 lakhs, Rs.134.63 lakhs, Rs.135.24 lakhs, Rs.138.66 lakhs and Rs.157.38 lakhs, respectively for the assessment years 1983-84 to 1987-88.

Before completing the assessments, the assessing officer made references in March and July 1989, to the valuation officer, for valuation of the building complex. However, before the valuation officer made his report, the value as returned by the assessee was accepted and assessments were completed between October 1989 and February 1990. The valuation officer in his report dated 28 March 1990 determined the value of the building complex at Rs.155 lakhs, Rs.173 lakhs, Rs.169 lakhs, Rs.181 lakhs and Rs.186 lakhs as on the valuation dates relevant to assessment years 1983-84 to 1987-88. Audit scrutiny revealed that the assessing officer had not initiated any action to re-open and revise the assessments for the earlier years on the basis of the value as determined by the valuation officer. Omission to do so resulted in aggregate underassessment of wealth of Rs.68.02 lakhs with consequent short levy of tax of Rs.2.30 lakhs.

The Ministry has accepted the audit observation.

**B-Summary
Assessment**

(iii) In the wealth tax assessment of a Hindu undivided family for the assessment years 1985-86 and 1986-87, completed in March 1990 in a summary manner, the value of immovable property was adopted at Rs.31,000 and Rs.6.75 lakhs respectively, instead of Rs.35.20 lakhs as determined by the Departmental Valuation Officer, as on 31 March 1985. Omission to adopt the valuation of Rs.35.20 lakhs resulted in underassessment of wealth of Rs.63.34 lakhs with consequent short levy of tax of Rs.2.41 lakhs in aggregate.

The Ministry has not accepted the audit observation on the ground that assessments were completed under the summary assessment scheme. The argument is not tenable in view of the fact that the report of the valuation officer which was binding on the assessing officer in respect of the value computed, was available. However, there was an omission in not adopting this value.

5.5.2 Unquoted equity shares

(a) Under the Wealth Tax Act, 1957, from 1 April 1989, the value of any asset other than cash, shall be its value, as on the valuation date, determined in the manner laid down in

Schedule III of the Act. Further, the value of an unquoted equity share of a company other than an investment company shall be equal to 80 per cent (85 per cent upto assessment year 1988-89) of the break-up value. The break-up value shall be determined by dividing the value of all assets in excess of all liabilities as shown in the balance sheet by the total amount of its paid-up equity share capital and by multiplying the result by the paid-up value of each equity share.

**A-Scrutiny
Assessment**

In the wealth tax assessments of an individual, for the assessment years 1988-89, 1989-90 and 1990-91, completed in December 1991, the assessing officer adopted the value of 45 unquoted equity shares held by the assessee in a company at Rs. 6,752, Rs. 12,679 and Rs. 13,796 per share respectively under the prescribed break-up value method, as returned by the assessee. Audit scrutiny of the balance-sheet of the company revealed that the capital of the company consisted of 4482 numbers of 4 per cent preference shares of Rs. 100 each and 110 equity shares of Rs. 100 each fully paid up. While working out the value of unquoted equity share under the break-up value method, the net excess of assets over liabilities of the company was divided erroneously by the total number of shares including 4482 preference shares instead of 110 equity shares alone. The mistake led to incorrect computation of the value of shares resulting in aggregate under assessment of wealth of Rs. 609.25 lakhs with consequent short levy of tax aggregating Rs. 12.13 lakhs.

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

**B- Summary
Assessment**

(b) The net wealth of an individual for the assessment year 1990-91, computed in December 1990, in a summary manner, included, inter alia, 36,984 unquoted equity shares of a company. Audit scrutiny revealed that while working out the value of unquoted shares, advance tax amounting to Rs. 344.33 lakhs paid by the company was reduced from the total assets to arrive at the value of shares. However, while working out the value of liabilities, provision for taxes amounting to Rs. 388.48 lakhs was not reduced as laid down in the Wealth Tax Act. The incorrect valuation of shares resulted in under

assessment of wealth of Rs. 124.25 lakhs with consequent short levy of wealth tax of Rs. 2.92 lakhs, including additional tax.

The Ministry has not accepted the audit observation on the ground that assessment was completed under the summary assessment scheme and prima facie adjustments cannot be made. The reply is not acceptable in view of the instructions issued on the subject by the Central Board of Direct Taxes on 5 December 1990 which requires that cases involving valuation of assets under Schedule III to Wealth Tax Act warrant prima facie adjustments.

5.5.3 Gold jewellery and silver utensils

(i) The wealth tax assessments of an individual assessee, for the assessment years 1984-85 and 1985-86 were completed between March 1989 and March 1990. The assessing officer had adopted the value of gold ornaments and silver utensils at Rs.10 lakhs and Rs.2 lakhs respectively in both the assessments which represented the value adopted in the wealth tax assessment completed for the assessment year 1974-75. Since the value of gold ornaments and silver utensils had increased 3.60 times and 2.82 times respectively for assessment year 1984-85 and 3.95 times and 3.23 times respectively for assessment year 1985-86, there was apparent under-valuation of assets and consequent under assessment of wealth of Rs.63.67 lakhs. There was thus short levy of tax aggregating Rs.5 lakhs for two assessment years.

The Ministry has accepted the audit observation.

(ii) In the wealth tax assessment of an individual for the assessment years 1978-79, 1979-80, 1981-82, 1983-84 and 1984-85 (assessments completed in March 1992) the value of jewellery was taken at Rs.6 lakhs for the assessment year 1978-79 and Rs.5 lakhs for other assessment years. Audit scrutiny revealed that the value of jewellery was taken at Rs.8 lakhs for the assessment year 1974-75. As there was no transfer of jewellery during the years subsequent to assessment year 1974-75, the value estimated in the assessments should have been valued on the market rate of gold on the relevant valuation dates. Omission to do so resulted

in short computation of wealth by Rs.85.85 lakhs involving aggregate short levy of wealth tax of Rs.3.89 lakhs.

The Ministry has accepted the audit observation.

Incorrect exemption in respect of equity shares

5.6 Under the Wealth Tax Act, 1957, the value of any equity share in any company, established with the main object of carrying on business of manufacture or production of any one or more of the articles or things specified in the list in the Ninth Schedule to the Income Tax Act, where such share forms part of the initial issue of equity share capital made by the company after 28th day of February 1975, for a period of five successive assessment years commencing with the assessment year next following the date on which such shares were first issued, shall not be included in net wealth of the assessee and wealth tax shall not be payable by an assessee in respect of such shares.

Five individuals, holding shares of an industrial undertaking, manufacturing synthetic yarn, claimed exemption from wealth tax in their wealth tax returns filed for the assessment years 1989-90 and 1990-91. While completing these assessments between January and March 1991, the assessing officer allowed the exemption. As synthetic yarn is not an item specified in the Ninth Schedule to the Income Tax Act, no exemption was allowable. The mistake resulted in under assessment of wealth of Rs.203.19 lakhs with consequent short levy of tax of Rs.3.46 lakhs.

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

Mistake in application of rate of tax

5.7 Under the Wealth Tax Act, 1957, prior to its amendment with effect from 1 April 1989, where assets chargeable to tax are held by an association of persons other than a company or co-operative society and the individual shares of the members thereof in the income or assets or both of the said association on the date of its formation or at any time thereafter, are indeterminate or unknown, wealth tax shall be levied on and recovered from such association in like manner and to the same extent as it would be leviable on and recoverable from an individual who is a

citizen of India and resident in India, at the rates specified in Part I of Schedule I or at the rate of three per cent, whichever course would be more beneficial to the revenue.

The wealth tax assessments of an 'association of persons' for the assessment years 1986-87, 1987-88 and 1988-89 were completed in March 1991 on a net wealth of Rs.54.61 lakhs, Rs.59.10 lakhs and Rs.68.94 lakhs respectively, and aggregate wealth tax of Rs.2.98 lakhs was levied. Levy of tax at the flat rate of three per cent would have been more beneficial to revenue as on this basis, the tax leviable worked out to Rs.5.48 lakhs. Failure to adopt the flat rate, resulted in short levy of tax of Rs.2.50 lakhs in the aggregate.

The Ministry has accepted the audit observation.

**Wealth tax
on companies**

5.8 Under the provisions of Section 40 of Finance Act, 1983, companies other than those in which public are substantially interested, are liable to wealth tax from the assessment year 1984-85, at a flat rate of two per cent of the market value of the specified assets including buildings or land appurtenant thereto, other than building or part thereof used by the assessee as factory, godown, warehouse, hotel or office for the purposes of its business, and their value is estimated to be the price which, in the opinion of the wealth tax officer, they would fetch, if sold in the open market on the valuation date.

5.8.1 Non-levy of wealth tax

(i) A closely held company owned a commercial complex in a metropolitan city (which was leased out to a co-operative society) and some lands in a village, which were assessed to wealth tax for the assessment years 1984-85 to 1986-87. For the assessment year 1987-88, the assessee company did not file any wealth tax return, but the assessing officer completed the assessment in March 1991, based on the wealth assessed for assessment year 1986-87. Audit scrutiny revealed that for the assessment years 1988-89 to 1990-91, though the relevant income tax

assessments were completed between September 1988 and January 1991, wealth tax returns were neither filed by the assessee company nor called for by the department. Based on the report of the valuation cell of the department in March 1990, the value of the above properties on 31 March 1988 aggregated Rs.342.11 lakhs. Adopting the same value for all the three years, the wealth escaping assessment amounted to Rs.1026.33 lakhs involving aggregate short levy of tax of Rs.20.79 lakhs.

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

(ii) Two companies, in which public were not substantially interested, derived rent from lease of buildings owned by them. The rental income of the companies was assessed to income tax as income from house property. The value of the buildings, calculated on rent capitalisation method, worked out, in the case of the first company to Rs.20.56 lakhs, Rs.21.71 lakhs and Rs.29.43 lakhs for the assessment years 1989-90, 1990-91 and 1991-92. The value of a building and free hold land held by the other company worked out to Rs.19.51 lakhs, Rs.23.73 lakhs, Rs.15.85 lakhs and Rs.19.33 lakhs for the assessment years 1988-89 to 1991-92 respectively. However, the assessee companies did not file the returns of net wealth nor did the department initiate any wealth tax proceedings. The omission resulted in aggregate wealth of Rs.150.12 lakhs escaping assessment with consequent non levy of wealth tax of Rs.2.98 lakhs.

The Ministry has accepted the audit observation in one case.

(iii) The income tax assessment records of a closely held company, for the assessment years 1984-85 to 1988-89 revealed that the company owned buildings which had been let out, and that the rent received therefrom had been assessed as income from house property. The value of these buildings, according to the rent capitalisation method, ranged from Rs.10.92 lakhs to Rs.22.99 lakhs during the relevant period. The buildings, evidently, had not been used for any of the specified business purposes, and as such, were chargeable to wealth tax. However, no returns of wealth were filed by the assessee for any of the five assessment years, nor did

the department initiate wealth tax proceedings against the assessee company. The omission resulted in non-levy of wealth tax of Rs.2.09 lakhs.

The Ministry has accepted the audit observation.

(iv) The income tax assessment records of a closely held company relating to the assessment years 1984-85 and 1989-90 revealed that the company was also the owner of land and building valued at Rs.12.40 lakhs and Rs.5.58 lakhs respectively. These immovable assets were not used in the business of the assessee company. Accordingly, the assessee company was liable to wealth-tax on these assets. Audit scrutiny revealed that the assessee company had not filed any wealth tax return, nor did the assessing officer initiate assessment proceedings. The omission resulted in wealth aggregating Rs.107.89 lakhs escaping assessment with consequent non-levy of wealth tax of Rs.2.05 lakhs.

The Ministry has accepted the audit observation.

5.8.2 Wealth not assessed

Under the Wealth Tax Act, 1957, companies other than those, in which the public are substantially interested, are liable to wealth tax from the assessment year 1984-85 at a flat rate of two per cent of the market value of the specified assets including building or land appurtenant thereto, other than a residential building for its employees provided each such employee is an employee whose income chargeable under the head 'Salaries' under the Income Tax Act, does not exceed Rs.18,000 per annum upto the assessment year 1989-90.

A private limited company in its wealth tax returns for the assessment years 1984-85 to 1986-87, did not include the value of land measuring 39,241 square yards appurtenant to buildings meant for occupation by its senior officers such as Directors and Managers. Audit scrutiny revealed that while completing the assessments in March 1989 and 1990, the assessing officer also did not include the aforesaid land valued at Rs.186 lakhs for the assessment year 1984-85 and Rs.227 lakhs for each of the assessment years 1985-86 and 1986-87. The omission resulted in under

assessment of wealth aggregating Rs.640 lakhs with consequent short levy of tax of Rs.12.82 lakhs.

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

5.8.3 Incorrect valuation of assets

(a) The Act further provides that the assessing officer may make a reference to the departmental valuation officer, for the valuation of an asset, if in his opinion, the fair market value of the asset exceeds the value of the asset as returned by more than 33.33 per cent or Rs. 50,000 whichever is less. The value so estimated by the valuation officer shall be binding on the assessing officer.

In the wealth tax assessment of a closely held company for the assessment year 1985-86 completed in March 1990 and revised in March 1991, the value of two properties on the outskirts of a metropolitan city was adopted at Rs. 21.02 lakhs and Rs. 5.72 lakhs based on earlier year's value. Similarly in the case of another company, the assessment for the assessment year 1989-90 was completed in August 1991 and revised in October 1992 by adopting the value of two properties at Rs. 6.71 lakhs and Rs. 14.27 lakhs. Audit scrutiny revealed that both the cases were referred to the departmental valuation officer. While in the first case, the value of the properties was determined by the valuation officer in his report of March 1991 at Rs. 145.25 lakhs and Rs. 39.53 lakhs, in the second case it was determined (March 1992) at Rs. 18.70 lakhs and Rs. 34.06 lakhs. Omission to revise the assessments in the two cases on the basis of valuation as determined by the departmental valuation officer resulted in underassessment of wealth of Rs. 158.04 lakhs and Rs. 31.78 lakhs respectively involving short levy of wealth tax aggregating Rs. 3.72 lakhs.

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

(b) Under the Wealth Tax Act, 1957, the assessing officer shall estimate the value of a vacant land to be the price which it would, in his opinion, fetch if sold in the open market on the valuation date.

In the wealth tax assessment of a closely held company for the assessment years 1986-87 to 1989-90, completed in March 1992, the assessing officer adopted the value of vacant lands measuring 43.12 acres, 35.78 acres, 29.84 acres and 24.36 acres at Rs.90,000, Rs.1 lakh, Rs.1 lakh and Rs.1.20 lakhs per acre as on the respective valuation dates. Audit scrutiny revealed that out of the above lands, the assessee company had periodically sold certain portion during the previous years relevant to the assessment years 1986-87 to 1989-90 at Rs.1.75 lakhs, Rs.1.75 lakhs, Rs.2.74 lakhs and Rs.3.62 lakhs per acre respectively. Omission to adopt these values, which represented the market value of lands owned by the assessee, for the various years in the assessments completed, resulted in underassessment of wealth of Rs.174.41 lakhs in aggregate for the assessment years 1986-87 to 1989-90 with consequent short levy of tax aggregating Rs.3.52 lakhs.

The Ministry has accepted the audit observation.

(c) Under Section 40 of the Finance Act, 1983, any asset which is required or represented by a debt secured on any one or more of the assets specified in the Act, is also an asset owned by a company for wealth tax purposes. The Central Board of Direct Taxes issued instructions (November 1973, April 1979 and September 1984) for proper co-ordination amongst assessment records pertaining to different direct taxes with a view to bringing to tax cases of evasion of tax.

In the wealth tax assessment of a closely held company, for the assessment years 1984-85 to 1986-87 completed in July and October 1987, the value of the immovable property (land) was adopted at Rs.97,888 as returned by the assessee on the basis of a registered valuer's certificate. The income tax assessment records of the assessee for the assessment year 1987-88 disclosed that in the previous year relevant to the assessment year 1986-87, the earnest money deposit received against the sale of the aforesaid land was shown in the balance sheet of the company at Rs.45.33 lakhs which should at least have been adopted. Non-adoption of market value of the land in the aforesaid three assessment years resulted in underassessment of wealth

aggregating Rs.133.65 lakhs with consequent short levy of tax of Rs.2.69 lakhs.

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

B - GIFT TAX

General

5.9 In the financial years 1988-89 to 1992-93, gift tax receipts vis-a-vis the budget estimates were as given below:

Year	Budget Estimates (in crores of rupees)	Actuals	Variation	Percentage variation
1988-89	10.00	6.74	(-)3.26	(-)32.60
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

*Provisional

5.10 Particulars of assessments completed, assessments pending and demands in arrear for the last five years ending 31 March 1993 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)
1988-89	70,642	21,327	24.53
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

*Provisional

Results of Audit

5.11 During the test audit of assessments made under the Gift tax Act, 1958, conducted during the period 1 April 1992 to 31 March 1993 short levy of gift tax of Rs.8.21 crores was noticed in 233 cases.

A total number of 19 draft paragraphs involving tax effect of Rs.39.93 lakhs was issued to the Ministry of Finance for comments during March to August 1993. The

Ministry of Finance have accepted the observations in 8 cases involving tax effect of Rs.17.34 lakhs. 4 illustrative cases involving tax effect of Rs.20.68 lakhs are given in the following paragraphs. Out of these, the Ministry of Finance have accepted the observations in 2 cases involving tax effect of Rs.10.23 lakhs. one case involving tax effect of Rs.6.23 lakhs was checked by the Internal Audit of the department but the mistakes were not detected by it.

Gift not assessed

5.12 Under the Gift Tax Act, 1958, gift means the transfer by one person to another of any existing movable or immovable property made voluntarily and without any consideration in money or money's worth.

A father of two minor sons filed two income tax returns for the assessment year 1986-87 on 30 September 1986 for Rs.10 lakhs each and the returns were filed under the 'Amnesty scheme' introduced by the Board. He opened savings bank accounts in the names of the two minors on 27 February 1986 with Rs.100 each. On the same day he credited each account with Rs.10 lakhs in cash and withdrew Rs.10 lakhs from each account on that very day by cheque drawn in favour of a firm. This disclosure by father in the names of minor sons attracted levy of gift tax but the assessee had neither filed a return of gift nor did the department initiate any gift tax proceedings. The non-assessment of gift of Rs.20 lakhs resulted in non-levy of gift tax of Rs.7.06 lakhs.

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

Non-levy of tax on deemed gift

5.13.1 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 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) The income tax assessment records of a private limited company, for the assessment year 1989-90, disclosed that the assessee company had sold 50,820 sq.yards of land for a consideration of Rs.1.90 lakhs in March

1989. Audit scrutiny revealed that value of the said land as on 31 March 1974 was determined at Rs.22.87 lakhs by an approved valuer. The sale value of the land should have been taken at least at Rs.22.87 lakhs as per the valuation report, if not higher. On account of inadequate consideration, the sale of land at a lower value attracts levy of gift tax of at least Rs.6.23 lakhs which was not levied.

The Ministry has accepted the audit observation.

(ii) The income tax assessment records of a partnership firm, for the assessment year 1985-86, revealed that one of the partners had been gifted by his uncle, two plots of lease-hold lands along with incomplete construction thereon in July 1976. The donee constituted a partnership firm (April 1981) taking three partners with shares of 30 per cent, 20 per cent and 20 per cent retaining 30 per cent share for himself, in order to complete construction of the building for commercial purposes. The firm was assessed to tax on rental income from the house properties under the amnesty scheme for the assessment years from 1982-83 to 1985-86. For the assessment year 1986-87, the firm disclosed gross annual rental income of Rs.2.97 lakhs of which the net maintainable rent worked out to Rs.2.42 lakhs. In the previous year relevant to assessment year 1987-88, the properties were stated to have been transferred to the promoter partner who was the donee. The market value of the property so transferred worked out to Rs.24.18 lakhs on the basis of income capitalisation method. As the market value, thus worked out, exceeded the book value of the building of Rs.6.06 lakhs as shown in the firm's balance sheet for the year ended 31 March 1986, the differential amount of Rs.18.12 lakhs constituted deemed gift attracting levy of gift tax in the hands of the other three partners. Gift tax returns were neither filed by the three partners, nor did the Gift Tax Officer initiate any gift tax proceedings. The omission resulted in non-levy of gift tax of Rs.3.39 lakhs.

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

5.13.2 Under the Gift Tax Act, 1958, the value of transactions such as release,

discharge, surrender, forfeiture or abandonment of any debt, contract, actionable claim or of any interest in property if not bonafide, is deemed to be a gift chargeable to gift tax.

A closely held investment company, holding 1,80,150 shares of the face value of Rs. 10 per share in a sister concern, renounced its right to receive 81,550 right shares offered by the latter in the previous year relevant to the assessment year 1986-87. It, however, received premium on the renunciation of the right of shares to the extent of Rs.3.08 lakhs. The market value of the share so renounced was Rs.20.50 per share according to the details in balance sheet as on 31 March 1986, available in the income tax assessment records of the assessee company. Accordingly, the value of the shares renounced stood at Rs.16.72 lakhs. As the right to receive the shares valued at Rs.16.72 lakhs was transferred at a consideration of Rs.3.08 lakhs only, the difference amounting to Rs.13.64 lakhs constituted 'deemed gift' by the assessee company attracting levy of gift tax. The assessee company did not file any gift tax return, nor did the department initiate any gift tax proceedings. The omission led to non-levy of gift tax of Rs. 4 lakhs.

The Ministry has accepted the audit observation.

C - Expenditure Tax

Omission to levy interest for delayed payment of expenditure tax

5.14 The Expenditure Tax Act, 1987, provides for the levy of tax at 20 per cent on the expenditure incurred in a hotel wherein the room charges for any of the residential accommodation, at the time of incurring such expenditure, exceed Rs.400 (Rs.1200 or more with effect from 1 June, 1992) per day per individual. Under the Act, an assessee has to remit the tax collected during any calendar month to the credit of the Central Government by the 10th day of the succeeding month and if any person responsible for collecting such tax fails to collect it, he shall be liable to pay the tax to the credit of the Central Government within the said period. The Act

further provides that if an assessee fails to credit the tax to the account of the Central Government within the period specified above, he shall be liable to pay simple interest at the rate of one and one half per cent for every month or part thereof during which the default continues.

The assessments of a closely held company, engaged in the business of running a hotel, for the assessment year 1988-89 to 1990-91, were completed in January 1991, December 1991 and March 1992 respectively, and the tax payable was computed at Rs.2.68 lakhs, Rs.12.41 lakhs and Rs.15.71 lakhs respectively. Audit scrutiny revealed that though the assessee was liable for the levy of interest on the belated payment/non payment of tax to the credit of the Central Government aggregating Rs.14.13 lakhs for the three years (upto the period ending March 1992) it was not levied by the department.

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

D - Interest Tax

General

5.15 Under the Interest Tax Act, 1974, read with the Finance Act, 1983, interest tax was levied at the rate of three and half per cent (seven per cent upto 31 March 1983) on the total amount of interest received by scheduled banks on loans and advances made in India. Interest on Government securities as also debentures and other securities issued by local authorities, companies and statutory corporations are not, however, included in the tax base. Interest received on loan and advances made to other scheduled banks are also, like wise exempted from the levy. The levy of interest tax was extended to the specified All India Industrial Finance Institutions in respect of interest accruing or arising after 30 June 1980. The interest tax was abolished with effect from 1 April 1985 and was reintroduced with effect from 1 October 1991.

5.15.1 Particulars of assessments completed, assessments pending and demands in arrear for the last five years ending 31 March 1993 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)
1988-89	163	278	6.89
1989-90	314	21	27.11
1990-91	23	10	11.22
1991-92	3	45	10.79
1992-93*	68	878	0.96

* Provisional

Two important cases noticed during test check of assessments of interest tax during 1992-93 are given in the following paragraphs. These audit observations were referred to the Ministry of Finance for comments during March to August 1993.

Delay in revision of assessments

5.16 Under the Interest Tax Act, 1974, as it existed prior to its amendment by the Finance (No.2) Act, 1991, there was no statutory time limit prescribed for completion of interest tax assessments and re-assessments. The Central Board of Direct Taxes issued instructions in December 1981 that interest tax assessment should, as far as possible, be completed along with the income tax assessments.

The income tax assessments of a nationalised bank for the assessment years 1983-84 and 1984-85, which were originally completed in January 1986 and October 1986 respectively, were re-opened under the orders of Commissioner of Income tax to consider inter alia 'interest on sticky loans and advances', which was not returned by the assessee in the returns of income and not considered in previous assessments. The re-assessments were completed in October 1989 by making additions to the extent of Rs.891.52 lakhs and Rs.1,280.02 lakhs representing interest on sticky loans for the assessment years 1983-84 and 1984-85 respectively. Audit scrutiny revealed that taking into account the interest on sticky loans assessed as income

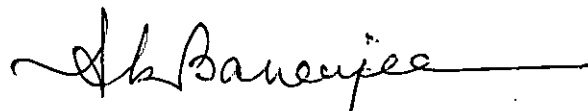
in October 1989, the assessee bank was liable to pay further interest tax of Rs.107.21 lakhs for these two assessment years. However, no action was taken to revise the interest tax assessments. Omission to do so resulted in postponement of tax collection of Rs.107.21 lakhs.

The Ministry has accepted the audit observation in principle.

**Incorrect
computation
of
chargeable
interest**

5.17 The Interest Tax assessment of a public sector bank, for the assessment year 1984-85, was completed in July 1989 accepting the interest income of Rs.2009 lakhs returned by the assessee bank. It was seen in audit that the interest income earned in India as per the income tax assessment was Rs.2426 lakhs. While completing the assessment under the Interest Tax Act, the department did not correlate the returns and omitted to bring to tax the entire income of Rs.2426 lakhs. The failure resulted in underassessment of interest income of Rs.417 lakhs involving short levy of interest tax of Rs.14.60 lakhs.

The Ministry has accepted the audit observation.



(A.K. BANERJEE)

Principal Director of Receipt Audit
(Direct Taxes)

New Delhi
The 7th February, 1994

Countersigned



(C.G. SOMIAH)

New Delhi
The 10 FEB 1994 Comptroller and Auditor General of India

APPENDIX I

Reference : Paragraph 1.3.1 of the Report)

Variation between Budget estimates and actuals

Year	Budget Estimates (In crores of Rupees)	Actuals*	Variation	Percentage of of variation
024-Interest Tax				
1988-89	----	2.73	2.73	---
1989-90	----	3.94	3.94	---
1990-91	----	(-)0.86	(-)0.86	---
1991-92	535.00	305.04	(-)229.96	(-)42.98
1992-93*	800.00	714.70		
0031-Estate Duty				
1988-89	3.25	6.04	2.79	85.84
1989-90	3.10	4.27	1.17	37.74
1990-91	3.50	3.07	(-)0.43	(-)12.28
1991-92	2.30	2.86	0.56	24.34
1992-93*	3.00	0.95		
0032-Taxes on Wealth				
1988-89	120.00	122.48	2.48	2.06
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
0033-Gift Tax				
1988-89	10.00	6.74	(-)3.26	(-)32.60
1989-90	9.50	8.07	(-)1.43	(-)15.05
1990-91	9.00	3.38	(-)15.62	(-)62.44
1991-92	9.00	8.44	(-)0.56	(-)6.22
1992-93*	5.00	9.27	4.27	85.40
0023- Hotel Receipts Tax				
1992-93	--	0.37		
0028- Other taxes on income and expenditure				
1992-93	50.00	152.00	102.00	

*Figures furnished by Ministry of Finance are provisional

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APPENDIX II

(Reference: Paragraph 1.4.3(ii) (d) of the Report)

Tax deducted at source*

Income	No. of statements received	Tax deducted as per statements	Tax remitted to Govt. Account	(Rupees in crores)	
				Balance due for remittance For the year	Upto the end of the year
(a) Interest on Securities	2,103	203.58	203.58	0.01	0.01
(b) Dividends	12,325	168.94	168.94	0.04	0.04
(c) Lotteries and Crossword Puzzles	262	77.55	77.55	--	--
(d) Winnings from horse races	1,229	3.21	3.21	--	--
(e) Insurance Commission	5,843	47.42	47.41	--	--
(f) Payment to non-resident	9,897	164.94	164.94	0.01	0.01
(g) Others	3,611	23.89	23.89	--	--
Total	35,270	689.53	689.48	0.06	0.06

* Figures furnished by Ministry of Finance are provisional

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APPENDIX III

(Reference: Paragraph 1.5.2 of the Report)

Cost of collection

	Collection	Expenditure on collection	Percentage
	(In crores of Rupees)		
0024-Interest Tax			
1989-90	3.94	0.02	0.50
1990-91	(-)0.86	0.02	0.02
1991-92	305.04	0.03	0.01
1992-93*	714.70	0.03	0.01
0028- Other taxes on income and expenditure			
1989-90	71.63	1.47	2.05
1990-91	80.27	1.61	2.00
1991-92	144.38	1.79	1.24
1992-93*	152.37	3.11	2.04
0031-Estate Duty			
1989-90	4.27	0.63	14.75
1990-91	3.07	0.69	22.47
1991-92	2.86	0.77	26.92
1992-93*	0.95	0.89	93.68
0032-Taxes on wealth			
1989-90	178.51	16.83	9.42
1990-91	231.17	18.41	7.96
1991-92	306.93	20.52	6.68
1992-93*	467.27	23.63	5.05
0033-Gift Tax			
1989-90	8.07	2.10	26.02
1990-91	3.38	2.30	68.04
1991-92	8.44	2.56	30.33
1992-93*	9.27	2.95	31.82

*Figures furnished by Ministry of Finance are provisional

APPENDIX IV

(Reference : Paragraph 1.8.1(i)(e) of the Report)

Details of classification of tax in arrears (Gross)

		Amount(in crores of rupees)		
		Arrears	Current	Total
1(a)	Due from companies in liquidation			
	(i) Pending consideration of write-off/ scaling down petitions	4.97	--	4.97
	(ii) Others	3.00	10.72	13.72
	(iii) Total	7.97	10.72	18.69
(b)	Due from non-company assesseees involved in insolvency proceedings			
	(i) Pending consideration of scaling down petitions/write off	2.33	--	2.33
	(ii) Others	27.88	16.35	44.23
	(iii) Total	30.21	16.35	46.56
(c)	Total of (a) (iii)and (b)(iii)	38.18	27.07	65.25
2(a)	Due from assesseees who have left India and who have no known assets	1.96	---	1.96
(b)	Due from assesseees who are not traceable and or who have no known assets			
	(i) Pending consideration of write off/ scaling down petitions	11.21	---	11.21
	(ii) Others	12.18	---	12.18
	(iii) Total	23.39	---	23.39
(c)	Total (a) and (b)(iii)	25.35	---	25.35
3.	Amounts due from undertakings which have been nationalised or taken over by the Government where the erstwhile owners do not have enough assets to pay the tax			
	(i) Pending consideration of scaling down petitions/write off	0.19	--	0.19
	(ii) Others	---	---	---
	(iii) Total	0.19	---	0.19
4.	All other amounts in arrears			
	(i) Pending consideration of scaling down petitions/write off	3.47	0.36	3.83
	(ii) Which are not being realised for various reasons for genuine hardships	292.15	203.31	495.46
	(iii) Balance being the realisable amount	3400.52	5220.40	8620.92
	(iv) Total	3696.14	5424.07	9120.21
	(v) Total of 1(c), 2(c), 3(iii) and 4(iv)	3759.86	5451.14	9211.00

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APPENDIX V

(Reference: Paragraph 1.12(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
1989-90	582.37	940.72	16.56	51.24
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

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*Figures furnished by Ministry of Finance, are provisional

APPENDIX VI

(Reference: Paragraph 1.17.1(ii) (b) 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 ^a	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
(b) Gift Tax	1990-91	25	76	75	26
	1991-92	26	53	67	12
	1992-93*	12	47	44	15
(c) Estate duty	1990-91	26	45	67	4
	1991-92	4	16	18	2
	1992-93*	2	6	3	5

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^a Figures are under reconciliation by Ministry of Finance

* Figures furnished by the Ministry of Finance are provisional