REPORT

OF THE

COMPTROLLER

AND

AUDITOR GENERAL

OF INDIA

FOR THE YEAR

1979-80

UNION GOVERNMENT (CIVIL)

REVENUE RECEIPTS

VOLUME II

DIRECT TAXES

ERRATA

Page	Para	Line	*For*	*Read*
3	1.02(ii)	13th and 14th from bottom	(iv) Other receipts Deduct share of proceeds assigned to States	(iv) Other receipts Deduct share of proceeds assigned to States
3	N.B.	2nd from bottom	'paragraps	paragraphs
21	1.11(i)	1st from top	Searches and Seizures	Searches and Seizures*
23	1.11(ii)(2)	2nd from bottom	8	87
25	1.12(7)	14th from top	Net available	Not available
27	1.13(ii)	9th and 10th from top	asse- ets	assets
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47	2.08(v)(a)	6th from top	manufacturig	manufacturing
50	2.08(ix)	4th from top	cost or acquisition	cost of acquisition
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83	2.28(vi)	9th from top	repectively	respectively
89	3.04(i)	13th from bottom	assesment	assessment
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101	3.11(iv)	9th from top	undrecharge	undercharge
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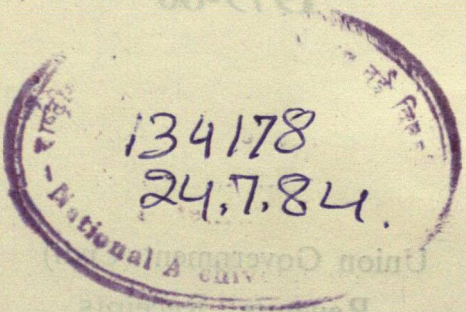
140	4.17(iii)	14th from top	years	year
147	4.24	8th from top	compay	company
148	4.24(i)	8th and 9th from top	break-the	break-up
149	4.25	17th from top	assesment	assessment



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PREFATORY REMARKS

As mentioned in the prefatory remarks of volume I of the Audit Report on Revenue Receipts of the Union Government, the results of audit of receipts under Direct Taxes are presented in a separate volume. In this volume, points arising from the audit of Corporation Tax, Income-tax, Wealth-tax, Gift-tax, Estate Duty and Interest—tax are included. The Report is arranged in the following order :—

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

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

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

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

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

VOLUME II

CHAPTER 1

GENERAL

1.01. *Receipts under various Direct Taxes*

The total proceeds from Direct Taxes for the year 1979-80 amounted to Rs. 2817.57* crores out of which a sum of Rs. 875.82 crores was assigned to the States. The figures for the three years 1977-78, 1978-79 and 1979-80 are given below :—

(In crores of rupees)

	1977-78	1978-79	1979-80
020 Corporation Tax	1220.77	1251.47	1391.90
021 Taxes on Income other than Corporation Tax	1002.02	1177.39	1340.31
028 Other Taxes on Income and Expenditure	115.84	24.53	0.01
031 Estate Duty	12.30	13.08	14.05
032 Taxes on Wealth	48.46	55.41	64.47
033 Gift Tax	5.55	5.85	6.83
Gross Total	2404.94	2527.73	2817.57
Less share of net proceeds assigned to the States			
Income-tax	675.44	706.62	864.88
Estate Duty	9.38	10.71	10.94
TOTAL	684.82	717.33	875.82
Net receipts	1720.12	1810.40	1941.75

The gross receipts under Direct Taxes during 1979-80 went up by Rs. 289.84 crores when compared with the receipts during 1978-79 as against an increase of Rs. 122.79 crores in 1978-79 over those for 1977-78. Receipts under Corporation Tax accounted for an increase of Rs. 140.43 crores and Taxes on income other than Corporation Tax Rs. 162.92 crores.

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

1.02. *Variations between Budget estimates and actuals*

(i) The actuals for the year 1979-80 under the Major heads '021—Taxes on Income etc.', '031—Estate Duty', '032—Taxes on Wealth' and '033—Gift Tax' exceeded the Budget estimates.

The figures for the years from 1975-76 to 1979-80 under the various heads are given below :—

Year	Budget estimates	Actuals	Variation	Percentage of variation
			(in crores of rupees)	
(1)	(2)	(3)	(4)	(5)
020—Corporation Tax				
1975-76	780.50	861.70	81.20	10.40
1976-77	1025.00	984.23	(—)40.77	(—)3.98
1977-78	1298.20	1220.77	(—)77.43	(—)5.96
1978-79	1441.90	1251.47	(—)190.43	(—)13.20
1979-80	1529.50	1391.90	(—)137.60	(—)8.99
021—Taxes on Income etc.*				
1975-76	791.00	1214.36	423.36	53.52
1976-77	957.00	1194.40	237.40	24.81
1977-78	1038.20	1002.02	(—)36.18	(—)3.48
1978-79	1134.80	1177.39	42.59	3.75
1979-80	1247.10	1340.31	93.21	7.47
031—Estate Duty*				
1975-76	9.25	11.65	2.40	25.95
1976-77	8.75	11.73	2.98	34.06
1977-78	10.75	12.30	1.55	14.42
1978-79	11.00	13.08	2.08	18.91
1979-80	12.00	14.05	2.05	17.08
032—Taxes on Wealth				
1975-76	43.00	53.73	10.73	24.95
1976-77	52.00	60.44	8.44	16.23
1977-78	54.90	48.46	(—)6.44	(—)11.73
1978-79	55.00	55.41	0.41	0.75
1979-80	60.00	64.47	4.47	7.45
033—Gift Tax				
1975-76	4.50	5.11	0.61	13.55
1976-77	4.75	5.67	0.92	19.37
1977-78	5.50	5.55	0.05	0.91
1978-79	5.75	5.85	0.10	0.18
1979-80	5.75	6.83	1.08	18.78

*Gross figures have been taken.

(ii) The details of variations under the heads subordinate to the Major Heads 020 and 021 for the year 1979-80 are given below :—

	Budget	Actuals	Increase(+) Short fall (—)	Percentage of variation
			(In crores of rupees)	
020—Corporation Tax				
(*i*) Income-tax on companies	1463.01	1300.04	(—)162.97	(—)11.13
(*ii*) Surtax	59.22	32.26	(—)26.96	(—)45.52
(*iii*) Surcharge	—	56.16	56.16	—
(*iv*) Receipts awaiting transfer to other Minor Heads	—	.01	.01	—
(*v*) Other receipts	7.27	3.43	(—)3.84	—52.82
	1529.50	1391.90	(—)137.60	(—)8.99
021—Taxes on Income other than Corporation Tax				
(*i*) Income-tax	1040.53	1130.57	90.04	8.65
(*ii*) Surcharge	189.57	183.60	(—)5.97	(—)3.14
(*iii*) Receipts awaiting transfer to other Minor Heads	—	14.61	14.61	—
(*iv*) Other receipts Deduct share of proceeds assigned to States	17.00	11.53	(—)5.47	(—)32.17
	812.58	864.88	(—)52.30	(—)6.43
	434.52	475.43	40.91	9.41

1.03. *Analysis of collections*

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

N.B. Figures appearing in paragraps 1.03, 1.04 and 1.06 to 1.15 have been furnished by the Ministry of Finance.

(i) The break-up of total collections of Corporation Tax and Taxes on income other than Corporation Tax, during 1979-80 as furnished by the Ministry of Finance, is as under :—

Pre-assessment and post-assessment collection of tax during 1979-80 :—

	(In crores of rupees)
(*i*) Deduction at source	643.06*
(*ii*) Advance tax (net)	1,778.51
(*iii*) Self—assessment	227.79
(*iv*) Regular assessment	288.38

Besides, the Ministry of Finance have intimated tax collection of Rs. 117.44 crores representing Surtax, Surcharge on 020-CT, Other Receipts and Receipts awaiting transfer to other Minor Heads, and Refunds of Rs. 323.09 crores.

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

	(In crores of rupees)
(*i*) Dividends distributed by companies	74.66
(*ii*) Salaries	233.25
(*iii*) Payments to contractors	77.94
(*iv*) Winnings from Lotteries and Crossword Puzzles	5.36

(iii) *Advance Tax—Demand and Collection.*

Demand raised (*i.e.* notices issued) and collected by way of advance tax during 1979-80 :—

	Number of cases	Amount (in crores of rupees)
(*i*) Demand raised	Not furnished	1891.67
(*ii*) Demand collected out of (i)	-do-	1798.46
(*iii*) Arrears under advance tax as on 31st March, 1980	-do-	93.21

*Inclusive of Surcharge (Union) in respect of 021—Taxes on income other than Corporation Tax.

1.04. *Interest*

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

The particulars of interest levied and interest paid by Government under different provisions of the Act are given below :—

	(In crores of rupees)
(*a*) The total amount of interest levied under the various provisions of the Income-tax Act during the year 1979-80	154.36
***(*b*) Of the amount of interest levied, the amount	
(1) Completely waived by the Department	5.38
(2) Reduced by the Department	12.05
(*c*) The total amount of interest paid	
(1) For delay in completion of assessments	7.74
(2) For delay in grant of refunds	1.03

1.05. *Cost of collection*

The expenditure incurred during the year 1979-80 in collecting Corporation Tax and Taxes on Income other than Corporation Tax, together with the corresponding figures for the preceding three years is as under :—

	(In crores of rupees)	
	Gross collections	Expenditure on collections
020—Corporation Tax		
1976-77	984.23	4.91
1977-78	1220.77	5.18
1978-79	1251.47	5.68
1979-80*	1391.90	5.93
021—Taxes on Income etc.		
1976-77	1194.40	34.38
1977-78	1002.02	36.28
1978-79	1177.39	**47.59
1979-80*	1340.31	41.48

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

**The final figure furnished by the Controller General of Accounts in October 1980 was Rs. 39.76 crores.

***Exclusive of figures of three Commissioners' charges.

1.06. *Total number of assessees*

Under the provisions of the Income-tax Act, 1961, tax is chargeable on the total income of the previous year of every person which term 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 and such person by whom tax is payable is called an assessee. For the assessment year 1979-80, no income-tax was payable on a total income not exceeding Rs. 10,000 except in the case of companies, co-operative societies and local authorities.

(i) The total number of assessees in the books of the department as on 31st March, 1980 was 41,75,615. As compared to the previous year ending 31st March, 1979 there was an increase of 2,05,650 assessees. The number of assessees status-wise as on 31st March, 1979 and 31st March, 1980 was as under :—

	As on 31st March, 1979	As on 31st March, 1980
Individuals	30,52,482	31,60,414
Hindu undivided families	2,11,036	2,35,935
Firms	6,11,088	6,72,817
Companies	41,532	42,581
Others	53,827	63,868
TOTAL	39,69,965	41,75,615

(ii) As for the category-wise break-up of the total number of assessees, the Ministry of Finance have explained that the categorisation according to different slabs of income as made till last year was dispensed with during the year 1979-80 as such categorisation "did not serve any useful purpose". They have given the break-up as between scrutiny assessment cases and summary assessment cases as under :

(*a*) Scrutiny assessment cases	10,56,634
(*b*) Summary assessment cases	31,18,981
Total	41,75,615

A summary assessment is an assessment made under Section 143(1) of the Income-tax Act, 1961 without requiring the presence of the assessee or the production by him of any evidence in support of the return made by him. During the financial year 1979-80, assessments in all non-company cases where the returned income in the assessment year and the assessed income in any of the two preceding years was less than Rs. 75,000 in the case of a registered firm or Rs. 50,000 in any other case were categorised as summary assessment cases. All company cases and other cases falling under certain specific categories such as new cases, search and seizure, investigation or prosecution cases etc. were treated as scrutiny cases irrespective of these monetary limits.

(iii) The total number of wealth-tax assessees in the books of the department as on 31st March, 1979 and 31st March, 1980 was as follows :—

	As on 31st March, 1979	As on 31st March, 1980
Individuals	2,73,482	2,98,375
Hindu undivided families	41,706	44,278
Others	3,262	3,638
TOTAL	3,18,450	3,46,291

(iv) The total number of gift-tax assessment cases for the years 1978-79 and 1979-80 was as follows :—

1978-79	60,546
1979-80	54,601

(v) The total number of estate duty assessment cases for the years 1978-79 and 1979-80 was as follows :—

1978-79	36,756
1979-80	39,63 0

1.07. *Arrears of assessments*

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

(i) Income-tax including Corporation Tax

(a) The number of assessment cases to be finalised as on 31st March, 1980 has increased as compared to that at the close of the previous year. The number of assessments pending as on 31st March, 1980 was 22.99 lakhs as compared to 19.26 lakhs as on 31st March, 1979 and 15.38 lakhs as on 31st March, 1978. Of the 22.99 lakhs of pending cases as many as 12.72 lakhs cases related to summary assessments.

(b) The number of assessments completed out of arrear assessments and out of current assessments during the past five years is given below :—

Financial year	Number of assessments for disposal	Number of assessments completed: Out of current	Out of arrears	Total	Percentage	Number of assessments pending at the end of the year
1975-76	57,34,327	25,08,108	14,99,536	40,07,644	69.9	17,26,683
1976-77	56,90,717	24,88,743	14,60,136	39,48,879	69.4	17,41,838
1977-78	55,81,355	25,72,678	14,71,135	40,43,813	72.5	15,37,542
1978-79	52,35,891	21,07,544	12,02,783	33,10,327	63.2	19,25,564
1979-80	57,89,055	18,97,276	15,92,514	34,89,790	60.0	22,99,265

(c) Category-wise break-up of the total number of assessments completed during the years 1978-79 and 1979-80 is as under :—

	As on 31st March, 1979	As on 31st March, 1980
Scrutiny assessments	8,98,162	9,17,776
Summary assessments	24,12,165	25,72,014
TOTAL	33,10,327	34,89,790

(d) Status-wise break-up of income-tax assessments completed during the years 1978-79 and 1979-80 is as under :—

	1978-79	1979-80
(*i*) Individuals	25,49,938	26,61,417
(*ii*) Hindu undivided families	1,77,732	1,89,820
(*iii*) Firms	5,08,196	5,54,787
(*iv*) Companies	35,982	38,033
(*v*) Associations of persons	38,479	45,733
TOTAL	33,10,327	34,89,790

(e) The position of pendency of income-tax assessments for the last two years is as under :—

	As on 31st March, 1979	As on 31st March, 1980
1975-76 and earlier years	44,061	30,021
1976-77	61,185	18,648
1977-78	5,17,533	72,323
1978-79	13,02,785	6,48,858
1979-80	—	15,29,415
TOTAL	19,25,564	22,99,265

(f) Category-wise break-up of pending income-tax assessments as on 31st March, 1979 and 31st March, 1980 is as under :—

	As on 31st March, 1979	As on 31st March, 1980
Scrutiny assessments	9,09,533	10,27,300
Summary assessments	10,16,031	12,71,965
TOTAL	19,25,564	22,99,265

(g) Status-wise and year-wise break-up of pendency of income-tax assessments as on 31st March, 1980 is as under :—

Status	1975-76 and earlier years	1976-77	1977-78	1978-79	1979-80	Total
Individuals	20,255	12,657	51,490	4,51,814	11,59,790	16,96,006
Hindu undivided families	1,727	1,310	4,777	40,623	79,056	1,27,493
Companies	2,503	930	2,454	14,495	23,504	43,886
Firms .	4,445	3,229	12,014	1,23,867	2,37,491	3,81,046
Associations of persons	1,091	522	1,588	18,059	29,574	50,834
TOTAL	30,021	18,648	72,323	6,48,858	15,29,415	22,99,265

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

(a) Year-wise details of wealth-tax, gift-tax and estate duty assessments pending as on 31st March, 1980 are given below. The approximate amount of tax/duty involved therein has not been furnished by the Ministry of Finance :—

	Number of assessments pending		
	Wealth-tax	Gift-tax	Estate Duty
1975-76 and earlier years . . .	11,111	1,838	4,934
1976-77	51,213	3,102	3,443
1977-78	65,193	3,490	5,323
1978-79	1,01,878	7,228	7,366
1979-80	2,03,593	11,745	13,825
TOTAL	4,32,988	27,403	34,891

(b) The total number of wealth-tax assessments completed during the years 1978-79 and 1979-80 was as under :—

	1978-79	1979-80
Individuals	4,11,742	2,80,765
Hindu undivided families	60,545	41,456
Others	2,734	3,497
TOTAL	4,75,021	3,25,718

(c) The total number of gift-tax assessments completed during the years 1978-79 and 1979-80 was as follows :—

	1978-79	1979-80
Individuals	79,151	61,540
Hindu undivided families	2,167	1,358
Others	235	144
TOTAL	81,553	63,042

(d) The total number of estate duty assessments of individuals completed during the years 1978-79 and 1979-80 was as under :—

1978-79	37,038
1979-80	32,607

(e) The number of estate duty assessments completed during the year 1979-80 was as follows :—

Principal value of property	Number of assessments completed
(1) Exceeding Rs. 20 lakhs	6
(2) Between Rs. 10 lakhs and Rs. 20 lakhs	47
(3) Between Rs. 5 lakhs and Rs. 10 lakhs	360
(4) Between Rs. 1 lakh and Rs. 5 lakhs	6,013
(5) Between Rs. 50,000 and Rs. 1 lakh	5,583
TOTAL	12,009

1.08. *Arrears of tax demands*

The Income-tax Act, 1961 provides that when any tax, interest, penalty, fine or any sum is payable in consequence of any order passed under the Act, a notice of demand shall be served upon the assessee. The amount specified as payable in the notice of demand has to be paid within 35 days unless the time for payment is extended by the Income-tax Officer on application made

by the assessee. The Act has been amended with effect from 1-10-1975 to provide that an appeal against an assessment order would be barred unless the admitted portion of the tax has been paid before filing the appeal.

(i) Corporation Tax and Income-tax

(a) The total demand of tax raised and remaining uncollected as on 31st March, 1980 was Rs. 840.38 crores. This did not include Rs. 171.47 crores in respect of which the permissible period of 35 days had not expired as on 31st March but included Rs. 8.84 crores claimed to have been paid but pending verification/adjustment, Rs. 223.28 crores stayed/kept in abeyance and Rs. 18.62 crores for which instalments had been granted by the department and the Courts.

(b) Demands of Income-tax (including Corporation tax) stayed as on 31st March, 1980 on account of appeals and revision petitions were as under :—

	(In crores of rupees)
(1) By Courts	65.57
(2) Under Section 243F(2) (applications to Settlement Commission)	11.43
(3) By Tribunal	6.72
(4) By Income-tax authorities due to :—	
(*i*) Appeals and revisions	103.25
(*ii*) Double Income-tax claims	3.43
(*iii*) Restriction on remittances-Section 220(7)	1.67
(*iv*) Other reasons	31.21
TOTAL	223.28

(c) The figures of Corporation tax, Income-tax, interest and penalty comprised in the gross arrears of Rs. 1011.85 crores and the years to which they relate are shown below:—

	Corporation tax	Income-tax	Interest	Penalty	Total (in crores of rupees)
Arrears of 1969-70 and earlier years .	14.80	46.67	10.05	9.76	81.28
1970-71 to-1976-77 .	24.91	128.10	52.58	39.11	244.70
1977-78 . .	13.51	51.01	27.69	14.98	107.19
1978-79 . .	33.04	87.62	47.83	21.51	190.00
1979-80 . .	104.08	168.51	85.50	30.59	388.68
TOTAL .	190.34	481.91	223.65	115.95	1011.85

(d) The table below shows the number of assessees from whom gross arrears of Rs. 1011.85 crores were due :—

Arrear demands	Number of assessees	Total arrears of tax (in crores of rupees)
Upto Rs. 1 lakh in each case	27,52,283	489.54
Over Rs. 1 lakh upto Rs. 5 lakhs in each case .	6,736	122.13
Over Rs. 5 lakhs upto Rs. 10 lakhs in each case .	892	61.41
Over Rs. 10 lakhs upto Rs. 25 lakhs in each case .	494	78.30
Over Rs. 25 lakhs in each case	337	260.47
TOTAL	27,60,742	1011.85

(e) Where an assessee defaults in making payment of a tax, the Income-tax Officer may issue a certificate to the Tax Recovery Officer for recovery of the demand by attachment and sale of the defaulter's movable or immovable property, arrest of the defaulter and his detention in prison, appointing a receiver for the management of the defaulter's movable and immovable property etc. The tax demand certified to Tax Recovery Officers and State Government Officers for recovery and its year-wise particulars to the end of 1979-80 are as under: —

	Demand certified			Demand recovered	Balance
	At the beginning of the year	During the year	Total		
				(in crores of rupees)	
1969-70 . .	359.52	183.55	543.07	116.45	426.62
1970-71 . .	425.25	181.36	606.61	145.37	461.24
1971-72 . .	433.53	208.79	692.32	167.52	524.80
1972-73 . .	530.57	264.98	795.55	189.06	606.49
1973-74 . .	598.15	192.62	790.77	161.93	628.84
1974-75 . .	616.07	188.16	804.23	176.29	627.94
1975-76 . .	616.35	333.92	950.27	290.56	659.71
1976-77 . .	678.72	330.30	1009.02	370.67	638.35
1977-78 . .	638.00	258.00	896.00	244.00	652.00
1978-79 . .	655.00	309.00	964.00	267.00	697.00
1979-80 . .	703.96	323.65	1027.61	287.61	740.00

NOTE :—Recovery certificates were issued during the year 1979-80 in 5,57,764 cases

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

The following table shows 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, 1980 :—

(In crores of rupees)

	Wealth-tax		Gift-tax		Estate Duty	
	Number of cases	Amount Rs.	Number of cases	Amount Rs.	Number of cases	Amount Rs.
1975-76 and earlier years	52,445	11.23	12,850	1.51	5,244	5.39
1976-77	22,009	4.60	5,157	0.56	1,932	1.61
1977-78	30,991	14.51	8,240	1.20	2,441	2.15
1978-79	78,944	87.77	15,768	8.16	3,357	3.39
1979-80	88,090	62.42	18,424	4.34	6,263	4.69
TOTAL	2,72,479	180.53	60,439	15.77	19,237	17.23

1.09. *Appeals and Revision Petitions*

The Acts provide for appellate as well as revisionary proceedings.

(i) Particulars in respect of Income-tax appeals pending as on 31st March, 1980 are as under :—

	Income-tax appeals with Appellate Assistant Commissioners/ Cs. I.T. (Appeal)	Income-tax revision petitions with Commissioners of Income-tax
Number of appeals/revision petitions	2,53,381	10,457
(*a*) Out of appeals/revision petitions instituted during 1979-80	1,42,178	5,732
(*b*) Out of appeals/revision petitions instituted in earlier years	1,11,203	4,725

(ii) Particulars in respect of wealth-tax, gift-tax and estate duty appeals and Revision petitions pending as on 31st March, 1980 are as under :—

	Appeals with Asstt. Appellate Commissioners/ Cs. I.T. (Appeals)			Revision petitions with Commissioners of Income-tax		
	W.T.	G.T.	E.D.	W.T.	G.T.	E.D.
(*a*) No. of appeals/ revision petitions pending . .	87,525	4,328	5,740	2,785	122	Nil
(*b*) Out of appeals/ revision petitions instituted during 1979-80 . .	59,695	2,560	1,962	1,733	74	Nil
(*c*) Out of appeals/ revision petitions instituted in earlier years . . .	27,830	1,768	3,778	1,052	48	Nil

(iii) Year-wise break-up of Income-tax appeal cases and revision petitions pending with Appellate Assistant Commissioners and Commissioners of Income-tax (Appeals), and Commissioners of Income-tax for the periods ending 31st March, 1979 and 31st March, 1980 respectively with reference to the year of institution is as under :—

Years of institution	Appeals pending with Appellate Assistant Commissioners/Cs. I.T. (Appeals)		Revision petitions pending with Commissioners of Income-tax	
	31st March, 1979	31st March, 1980	31st March, 1979	31st March, 1980
1970-71 and earlier years .	155	119	89	83
1971-72	187	162	84	84
1972-73	563	452	89	75
1973-74	793	554	124	92
1974-75	1,846	1,306	177	116
1975-76	5,341	3,464	258	193
1976-77	19,521	10,284	689	432
1977-78	53,465	24,165	2,280	1,307
1978-79	1,41,141	70,697	5,672	2,343
1979-80	—	1,42,178	—	5,732
TOTAL	2,23,012	2,53,381	9,462	10,457

(iv) Year-wise break-up of wealth-tax, gift-tax and estate duty appeal cases and revision petitions pending with Appellate Assistant Commissioners and Commissioners of Income-tax for the period ending 31st March, 1980, with reference to the year of institution is as under :—

Years of institution	Appeals pending with Appellate Asstt. Commissioners			Revision petitions pending with Commissioners of Income-tax		
	W.T.	G.T.	E.D.	W.T.	G.T.	E.D.
1971-72 and earlier years . . .	55	..	21	57	..	..
1972-73 . . .	27	1	15	17	..	..
1973-74 . . .	56	5	11	48	..	..
1974-75 . . .	153	12	32	49	..	..
1975-76 . . .	713	27	187	66	3	..
1976-77 . . .	2,555	97	584	109	5	..
1977-78 . . .	6,121	408	1,198	267	15	..
1978-79 . . .	18,150	1,218	1,730	439	25	..
1979-80 . . .	59,695	2,560	1,962	1,733	74	..
TOTAL .	87,525	4,328	5,740	2,785	122	Nil

(v) The following table gives details of appeals/references disposed of during the years 1977-78, 1978-79 and 1979-80 :—

		1977-78	1978-79	1979-80
(1)(*a*)	No. of appeals filed before Appellate Assistant Commissioners . .	1,87,173	2,18,589	2,08,778
(*b*)	No. of appeals disposed of during 1979-80 by AACs . . .	64,289	1,63,510	1,55,319
(2)	No. of appeals filed before Income-tax Appellate Tribunals during 1979-80			
(*a*)	by the assessees	30,429	25,080	24,478
(*b*)	by the department . . .	16,981	17,089	18,354
(3)	No. of assessees' appeals decided by the Tribunal in favour of the assessees fully out of (2)(a) above. .	11,560	12,996	11,321
(4)	No. of departmental appeals decided by the Tribunals in favour of the department fully out of (2)(a) above	3,396	3,389	3,245

(5)	No. of references filed to the High Courts			
	(*a*) by the assessees	1,569	1,645	1,634
	(*b*) by the department	3,925	4,517	4,262
(6)	No. of references in the High Courts disposed of in favour of the			
	(*a*) assessees	99	260	228
	(*b*) department	293	616	566
(7)	No. of appeals filed to the Supreme Court			
	(*a*) by the assessees	26	36	46
	(*b*) by the department	146	65	60
(8)	No. of appeals disposed of by the Supreme Court in favour of the			
	(*a*) assessees	..	28	2
	(*b*) department	2	8	1

1.10. *Reliefs and Refunds*

Refunds

(i) 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.

Refunds under Section 237 :—

1. No. of applications pending on 1-4-1979	10,843
2. No. of refund applications received during the year 1979-80	1,25,927
3. No. and amount of refunds made during 1979-80	
(*a*) Out of (1) above	
(*i*) Number	10,838
(*ii*) Amount (in thousands of rupees)	37,99
(b) Out of (2) above	
(*i*) Number	1,10,663
(*ii*) Amount (in thousands of rupees)	9,40,59

4. No. of refund cases in which interest was paid under Section 243, the amount of such interest, and the amount of refund, on which such interest was paid during 1979-80 :

(*a*) Out of (1) above	
(*i*) Number	446
(*ii*) Amount of refund (in thousands of rupees)	4,53
(*iii*) Amount of interest paid (in thousands of rupees)	41
(*b*) Out of (2) above	
(*i*) Number	2,442
(*ii*) Amount of refund (in thousands of rupees)	19,55
(*iii*) Amount of interest paid (in thousands of rupees)	63

5. No. and amount of refunds made during 1979-80 on which no interest was paid :

(*a*) Number	1,18,613
(*b*) Amount (in thousands of rupees)	9,54,50

6. No. of refund applications pending as on 31-3-1980 . . 15,269

7. Break-up of applications mentioned at (6) above :

(*a*) Refund applications for less than a year	15,264
(*b*) Between 1 year and 2 years	5
(*c*) For 2 years and more	..

(ii) 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 in that behalf. Simple interest at the prescribed rate is payable to the assessee in such cases too.

The particulars of appeal/revision etc. effects, refunds under Section 240 and payment of interest under Section 244, as furnished by the Ministry of Finance for the year 1979-80, are given below:—

1. No. of assessments which were pending revision on account of appellate/revision etc. orders as on 1.4.1979	*6,528
2. No. of assessments which arose for similar revision in 1979-80	1,13,926
3. No. of assessments which were revised during 1979-80	
(*a*) Out of those pending as on 1-4-1979	5,725
(*b*) Out of those that arose during 1-4-1979 to 31-3-1980	1,05,407
4. No. of assessments which resulted in refunds as a result of revision and total amount of refund given :	

*The Ministry of Finance have revised the closing figure of 6,511 furnished for the year 1978-79.

	Number	Amount of refund
		(In thousands of rupees)
(a) Under item 3(a) above	1,745	1,47,27
(b) Under item 3(b) above	49,146	38,57,21
5. No. of assessments in which interest became payable under Section 244 and amount of interest :		
(a) Under item 4(a) above	260	6,23
(b) Under item 4(b) above	3,839	95,91
6. No. of assessments pending revision as on 1-4-1980 :		
(a) Out of (1) above	803	
(b) Out of (2) above	8,519	
7. Break-up of assessments mentioned at (6) above :		
(a) Pending for less than 1 year	8,519	
(b) Pending for more than 1 year and less than 2 years	802	
(c) Pending for more than 2 years	1	

1.11. *Searches, Seizures and Rewards*

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

(i) *Searches and Seizures*

	1977-78	1978-79	1979-80
(1) Total number of searches and seizure operations conducted . .	617	1345	2109
(2) Total amount each of money, bullion and jewellery or other valuable articles or things seized :			(In lakhs of rupees)
Cash	101	220	244.22
Jewellery and bullion . . .	119	261	551.25
Other assets	133	100	419.21
TOTAL	353	581	1214.68
(3) Particulars of concealed income estimated under Section 132(5) in (1) above			
(*a*) No. of cases out of these mentioned at (1) in which orders under Section 132(5) were passed by 31-3-1980. . .			359
(*b*) Amount of concealed income estimated in cases at (a) above.			1407
(*c*) Taxes payable in respect of (b)			1130
(*d*) Money value of assets retained against (c)			587
(*e*) Money value of assets released in these cases . . .			122
(4) (*a*) Total amount each of money, bullion and jewellery or other valuable articles or things released by 31-3-78/31-3-1979/ 31-3-1980			
Cash	23	32	108
Jewellery and bullion . .	31	45	156
Other assets . . .	11	9	71+ 272 Dollars
TOTAL	65	86	335 + 272 Dollars

*Figures furnished by the Ministry of Finance are provisional.

(*b*) Total amount of money, bullion and jewellery or other valuable articles or things held as on 31-3-1978/31-3-1979/31-3-1980 irrespective of the year of search . . .

Cash	410	477	537
Bullion and jewellery . .	1,004	983	1215 + 566.118 kg. silver
Other assets . . .	640	469	753
TOTAL	2,054	1,929	2505 + 566.118 kg. silver

(*c*) The earliest date from which any of these assets is still retained 4-6-1965

(*d*) The arrangements made for the safe custody of assets still held and for their physical verification . . . . Cash is deposited in the Personal Deposit Accounts of the Commissioners of Income-tax in the Reserve Bank of India. Other valuables are kept either in well-guarded strong-rooms in the office building or in the treasuries or in Bank vaults etc.

(5)	(*a*) No. of assessments involved in Search and Seizure operations pending as on 1-4-1979	4842
	(*b*) No. of assessments completed out of (a) above during 1979-80	2307
	(*c*) Taxes and penalties :	
	(i) Recovered	198
	(ii) Pending	995
	(*d*) Balance pending as on 31-3-1980.	2,535
(6)	(*a*) No. of assessment proceedings started during 1979-80	3,312
	(*b*) No. of assessments completed out of (a) above during 1979-80	1,143
	(*c*) Taxes and penalties :	
	(*i*) Recovered	74
	(*ii*) Pending.	65
	(*d*) Balance pending as on 31-3-1980	2169
(7)	(*a*) No. of prosecutions in search and seizure cases, launched during the year 1979-80.	37
	(*b*) No. of convictions obtained during the year.	5

(ii) *Rewards to informers :**

	Year	No. of cases	Amount (In lakhs of rupees)
(1) Total number of cases and amount of rewards (interim and final) sanctioned year-wise for the years 1977-78, 1978-79, and 1979-80	1977-78	218	467
	1978-79	207	41
	1979-80	207	69

		Amount of additional income assessed as a result of action taken on the informer's information	Additional tax collected
(2) In respect of cases at (1) above the amount of concealed or undisclosed income/recovery of tax that came to notice as per information furnished by the informers.	1977-78	305	144
	1978-79	366	106
	1979-80	376	8

*Figures furnished by the Ministry of Finance are provisional.

	1977-78	1978-79	1979-80
(3) (*a*) No. of cases where information regarding tax evasion was received by the intelligence wing	3,196	4,850	4,064
(*b*) No. of cases where action was taken out of (a) above either u/s 132 or otherwise. .	802	2,184	1,235
(*c*) No. of cases where the information did not result in an addition to income out of (b) above.	169	288	370

	Year	No. of cases
(4) Cases where the amount of rewards was drawn but remained undisbursed for more than one year.	1977-78	1
	1978-79	..
	1979-80	..

1.12. *Cases settled by Settlement Commission*

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

Particulars of cases settled by the Settlement Commission during the years 1978-79 and 1979-80 are given as under :—

		1978-79	1979-80
1. No. of cases disposed of by the Commission : . . .	I.T.	113	130
Income-tax/Wealth-tax . .	W.T.	68	42
2. No. of assessment years involved	I.T.	630	486
	W.T.	480	178
3. The amount offered for settlement (Rs. in crores) . .	I.T.	2.05	1.46
	W.T.	7.61	2.49
4. Actual income/wealth determined by the Commission (Rs. in crores)	I.T.	4.55	Rs. 2.38
	W.T.	26.61	Rs. 6.29
5. Tax on (4) above	Not available		Not available

	1978-79		1979-80	
	No. of cases	Amount Rs.	No. of cases	Amount Rs.
6. Penalty and Interest : . .				
(*a*) Penalties under Section 271(1)(c) of the IT Act, 1961	I.T. 1	5,000	3	1,26,832
	W.T. 2	38,183	1	12,000
(*b*) Other penalties . .	I.T. 1	27,753	19	1,68,839
	W.T. 3	37,812	2	8,168
(*c*) Interest levied . .	I.T. 16	13,25,534	48	5,81,223
	W.T.	—		—
(7) Recovery of tax, penalty and interest	Not available		Not available	
(8) Balance of tax outstanding.	Not available.		Not available	

1.13. *Revenue demands written off by the Department*

(i) A demand of Rs. 1053.02 lakhs in 1,81,413 cases was written off by the department during the year 1979-80. Of this, a sum of Rs. 325.81 lakhs relates to 149 company assessees and Rs. 727.21 lakhs to 1,81,264 non-company assessees.

		Companies		Non-companies		Total	
		No.	Amount Rs.	No.	Amount Rs.	No.	Amount Rs.
1	2	3	4	5	6	7	8
I.(*a*)	Assessees having died leaving behind no assets or gone into liquidation or become insolvent	..	..	834	1,34,73,214	834	1,34,73,214
(*b*)	Companies which are defunct though not gone into liquidation	100	2,33,91,948	..	..	100	2,33,91,948
	TOTAL	100	2,33,91,948	834	1,34,73,214	934	3,68,65,162

1	2	3	4	5	6	7	8
II.	Assessees being untraceable	12	36,15,494	44,240	1,72,06,214	44,252	2,08,21,708
III.	Assessees having left India.	10	48,21,339	1,061	75,07,000	1,071	1,23,28,339
IV.	Other reasons :						
	(*a*) Assessees who are alive but have no attachable assets	9	3,68,280	3,810	1,57,87,648	3,819	1,61,55,928
	(*b*) Amount being petty etc.	18	3,84,448	1,27,271	1,76,47,141	1,27,289	1,80,31,589
	(*c*) Amount written off as a result of settlement (cases of scaling down of demand)	..	..	..	..	..	..
	TOTAL	27	7,52,728	1,31,081	3,34,34,789	1,31,108	3,41,87,517
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	—	—	4,048	10,99,650	4,048	10,99,650
GRAND TOTAL		149	3,25,81,509	1,81,264	7,27,20,867	1,81,413	10,53,02,376

(ii) Wealth-tax, Gift-tax and Estate Duty demands written off by the department during the year 1979-80 are shown in the different categories as below :

	Wealth-tax		Gift-tax		Estate-Duty	
	No.	Amount Rs.	No.	Amount Rs.	No.	Amount Rs.
1 2	3	4	5	6	7	8
I. Assessees having died leaving behind no assets or have gone in liquidation or become insolvent.						
(*a*) Assessees having died leaving behind no asset. .	2	246	1	250	..	..
(*b*) Assessees having gone in liquidation. . . .	..	..	..	..	..	..
(*c*) Asseessees having become insolvent .	..	..	..	..	..	..
TOTAL : . .	2	246	1	250	..	..
II. Assessees being untraceable. . .	4	27	6	2	..	..
III. Assessees having left India. . . .	..	..	..	..	..	..
IV. Other reasons. . .						
(*a*) Assessees who are alive but have no attachable assets. .	—	..	..	..	..	..
(*b*) Amount being petty etc. .	39	109	19	369	..	..
(*c*) Amount written off as a result of settlement with assessees.	..	..	..	..	..	..
TOTAL .	39	109	19	369	..	..

1	2	3	4	5	6	7	8
V.	Amount written off on grounds of equity or as a matter of international courtsey or where the time, labour and expenses involved in legal remedies for realisation are considered disproportionate to the amount of recovery. .	..	..	..	..	..	..
	GRAND TOTAL . .	45	382	26	621	—	..

1.14 Penalties for concealment and prosecution

(i) Income-tax

(a) No. of orders of penalty under Section 18(1)(c)/271(1)(c) passed during 1979-80 28,851

(b) Concealed income involved in (a) above . . . Rs. 31.48 Crores

(c) Total amount of penalty levied in (a) above . . . Rs. 22.30 Crores

(d) Position of prosecution cases under the provisions of the Income-tax Act :

(1) No. of prosecutions pending before the courts on 1-4-79 673

(2) No. of prosecutions complaints filed during 1979-80 under Section 276(c) (Substituted w.e.f. 1-10-75), 276 CC, 276D, 277 and 278 122

(3) No. of prosecutions decided during 1979-80 . . 50

(4) No. of convictions obtained in (3) above . . 24

(5) No. of cases which were compounded before launching prosecutions 8

(6) Composition money levied in such cases [(5) above] (Amount in thousands) 75

(ii) *Wealth-tax and Gift—tax*

	*Wealth-tax	*Gift-tax
	(In thousands of Rs.)	
(a) No. of orders of penalty under Section 18(1)(c)/17(1)(c) passed during 1979-80 . . .	35,52	1,70
(b) Amount of concealed net wealth/value of gift involved in (a) above	7,03,10	20,86
(c) Total amount of penalty levied in (a) above .	4,84,10	13,68
(d) Position of prosecution cases under the provisions of Wealth/Gift-tax Act :		
(1) No. of prosecutions pending before the courts on 1-4-1979	1,40	..
(2) No. of prosecution complaints filed during 1979-80, under Sections 35A, 35B, 35C, 35D and 35F	64	..
(3) No. of prosecutions decided during 1979-80	1	..
(4) No. of convictions obtained in (3) above	..	..
(5) No. of cases which were compounded before launching prosecutions . .	..	..
(6) Composition money levied in such cases [(5) above]	..	..

1.15. *Results of functioning of the Valuation Cells*

The results of functioning of the Valuation Cells are detailed below :—

(i) No. of Valuation Units/Districts :

Year	No. of Valuation Units	No. of Valuation Districts functioning
1977-78	80	10
1978-79	80	10
1979-80	80	10

(ii) No. of cases referred to the Valuation Cells excluding cases brought forward from previous year :—

	Income-tax	Wealth-tax	Gift-tax	Estate duty
1977-78 and earlier years .	1,571	16,755	137	585
1978-79	1,525	19,193	162	296
1979-80	1,180	11,853	117	214

*Exclusive of figures of one Commissioner's charge.

(iii) No. of cases decided by the Valuation Cells and the total amount of valuation made by the Cells compared with the returned value in the decided cases

(In lakhs of rupees)

Year	Income-tax			Wealth-tax		
	No. of cases	Value returned	Value determined	No. of cases	Value returned	Value determined
1977-78	1,516	3,648.52	4,605.94	15,340	22,481.36	47,902.78
1978-79	1,620	2,997.06	4,825.49	26,152	38,924.70	1,09,733.96
1979-80	1,341	2,585.79	3,499.33	12,045	13,600.81	37,109.51

Year	Gift-tax			Estate Duty		
	No. of cases	Value returned	Value determined	No. of cases	Value returned	Value determined
1977-78	129	114.87	259.36	635	752.35	1,616.59
1978-79	252	683.69	1,056.05	321	356.04	821.77
1979-80	92	65.87	212.92	331	554.41	1,085.66

1.16. *Results of test audit in general*

(i) Corporation tax and Income-tax

During the period from 1st April, 1979 to 31st March, 1980, test audit of the documents of the income-tax offices revealed total under-assessment of tax of Rs. 2342.54 lakhs in 26,703 cases. Besides these, various defects in following the prescribed procedures also came to the notice of Audit.

Of the total 26,703 cases of under-assessment, short levy of tax of Rs. 1993.62 lakhs was noticed in 2,707 cases alone. The remaining 23,996 cases accounted for under—assessment of tax of Rs. 348.92 lakhs.

The under-assessment of tax of Rs. 2342.54 lakhs is due to mistakes categorised broadly under the following heads :—

(1)	No. of items (2)	Amount (In lakhs of rupees) (3)
1. Avoidable mistakes in computation of tax	2,304	74.95
2. Failure to observe the provisions of the Finance Acts	460	34.42
3. Incorrect status adopted in assessments	326	46.45
4. Incorrect computation of salary income	738	22.86
5. Incorrect computation of income from house property	1,241	37.86
6. Incorrect computation of business income	3,567	298.16
7. Irregularities in allowing depreciation and development rebate	1,496	353.07
8. Irregular computation of capital gains	2,299	193.33
9. Mistakes in assessment of firms and partners	302	438.16
10. Omission to include income of spouse/minor child etc.	709	53.99
11. Income escaping assessment	212	25.12
12. Irregular set off of losses	2,230	153.39
13. Mistakes in assessments while giving effect to appellate orders	184	37.68
14. Irregular exemptions and excess reliefs given	101	7.12
15. Excess or irregular refunds.	874	38.32
16. Non-levy/incorrect levy of interest for delay in submission of returns, delay in payment of tax etc.	2,578	78.80
17. Avoidable or incorrect payment of interest by Government	525	25.20
18. Omission/short levy of penalty	1,092	55.51
19. Other topics of interest/miscellaneous	5,333	321.43
20. Under-assessment of Surtax/Super Profits Tax	132	46.72
TOTAL	26,703	2342.54

(ii) *Wealth-tax*

During test audit of assessments made under the Wealth-tax Act, 1957, short levy of Rs. 403.45 lakhs was noticed in 6,871 cases.

The under-assessment of tax of Rs. 403.45 lakhs was due to mistakes categorised broadly under the following heads :—

	No. of items	Amount (In lakhs of rupees)
1. Wealth escaping assessment	942	69.08
2. Incorrect valuation of assets	1,032	98.22
3. Mistakes in computation of net wealth	646	21.60
4. Incorrect status adopted in assessments	99	4.44
5. Irregular/excessive allowances and exemptions	1,059	30.93
6. Mistakes in calculation of tax	1,189	34.80
7. Non-levy or incorrect levy of additional wealth-tax	362	74.15
8. Non-levy or incorrect levy of penalty and non-levy of interest	424	32.01
9. Miscellaneous	1,118	38.22
TOTAL	6,871	403.45

(iii) *Gift-tax*

During the test audit of gift-tax assessments it was noticed that in 1,260 cases there was short levy of tax of Rs. 288.96 lakhs.

(iv) *Estate Duty*

In the test audit of estate duty assessments it was noticed that in 374 cases there was short levy of estate duty of Rs. 25.95 lakhs.

CHAPTER 2

CORPORATION TAX

2.01 Corporation tax is the major source of proceeds under Direct Taxes. The trend of recovery of Corporation tax during the last five years was as follows :—

Year	Amount (In crores of rupees)
1975-76	861.70
1976-77	984.23
1977-78	1220.77
1978-79	1251.47
1979-80	1391.90

2.02 The number of companies on the books of the department for the last five years was as follows :—

As on 31st March	Number
1976	40,055
1977	40,237
1978	42,084
1979	41,532
1980	42,581*

As on 31st March, 1980 there were 57,620 companies. These included 315 foreign companies and 1,447 associations not for profit registered as companies limited by guarantee and 78 companies with unlimited liability. The remaining 55,780 companies comprised 825 Government companies and 54,955 non-Government companies with paid-up capitals of Rs. 9,753 crores and Rs. 3,658 crores respectively. Among non-Government companies over 85 per cent were private limited companies**.

*Figures furnished by the Ministry of Finance.

**Figures given by the Department of Company Affairs, Ministry of Law, Justice & Company Affairs.

2.03 The arrears outstanding under Corporation tax during the last five years, together with the number of assessments completed and assessments pending at the end of each year were as follows :—

Year	No. of assessments		Amount of demands	
	Completed during the year	Pending at the close of the year	Collected during the year	In arrears at the close of the year
			(In crores of rupees)	
1975-76	40,327	31,613	861.70	192.11
1976-77	41,878	34,008	984.23	146.38
1977-78	41,533	34,864	1220.77	185.96
1978-79	35,982	40,563	1251.47	168.04
1979-80	38,033	43,886	1391.90	190.34

2.04 Some instances of mistakes noticed in company assessments are given in the following paragraphs.

2.05 *Avoidable mistakes in the computation of tax*

Under-assessments of taxes of substantial amounts have been noticed, year after year, on account of avoidable mistakes resulting from carelessness or negligence. The position of such cases reported by Audit in the Audit Reports for the years 1963 to 1971-72 was reviewed by the Public Accounts Committee in 1975 and their recommendations are contained in their 186th Report (Fifth Lok Sabha).

In spite of remedial action taken by the department such mistakes continue to occur. As already pointed out in paragraph 1.16(i) of Chapter I, 2,304 cases of avoidable mistakes involving short levy of tax of Rs. 74.95 lakhs were noticed in test audit during the year 1979-80 under Corporation tax and Income-tax. Some of the important mistakes relating to Corporation tax are given below :—

(i) Under the provisions of the Income-tax Act, 1961, the Income-tax Officer is authorised to make provisional assessment of the sum refundable to the assessee when tax paid in advance

and collected at source exceeds the tax payable on the basis of income returned. After a regular assessment has been made, the sum so refunded on provisional assessment shall be deemed to be tax payable by the assessee.

In two cases, the assessee-companies furnished their returns of income for the assessment year 1976-77 in September 1976 declaring incomes of Rs. 21,10,390 and Rs. 7,81,310 and claiming credits of Rs. 17,74,000 and Rs. 16,55,000 as advance tax and Rs. 14,889 and Rs. 21,486 as tax deducted at source respectively. As the amounts of advance tax paid together with tax deducted at source exceeded the tax payable on the basis of income returned, the department made provisional assessments in April 1977 and refunded in May 1977 sums of Rs. 5,70,140 and Rs. 12,23,652 respectively, being the excess tax paid. The regular assessments were completed later in September 1979 on total incomes of Rs. 38,60,970 and Rs. 43,17,930 and tax demands aggregating Rs. 12,66,955 were raised against the assessees after adjustment of the entire advance tax of Rs. 34,29,000. The fact that sums amounting to Rs. 17,93,792 had already been refunded to the assessees through the provisional assessments made earlier in April 1977 was lost sight of. As a result, there was an aggregate tax undercharge of Rs. 17,93,792 for the assessment year 1976-77.

While accepting the objection the Ministry of Finance have stated that the assessments in question have been revised raising additional demands of tax amounting to Rs. 17,93,792.

(ii) The accounts of an assessee-company for the assessment year 1975-76 exhibited a loss of Rs. 50,58,65,564. While completing the assessment in August 1978, the department determined the loss at Rs. 39,81,71,486 after disallowing certain expenses aggregating Rs. 11,06,93,976, which were, however, incorrectly taken at Rs. 10,76,94,078 due to a totalling mistake. This resulted in excess computation and carry forward of loss of Rs. 29,99,898.

The Ministry of Finance have accepted the objection. As a result of revision of the assessment in question, the loss to the extent of Rs. 29,99,898 has been reduced.

(iii) While computing income, the assessing officer proceeds from the net profit or loss as per the profit and loss account as the starting point and adds back inadmissible expenses and the amount of depreciation actually charged in the account. The amount of depreciation admissible under the Income-tax Act, 1961, and the Rules framed thereunder is thereafter allowed as a deduction.

(a) In the case of a public sector company for the assessment year 1973-74, depreciation of Rs. 3,50,44,720 charged to the account was added back to the loss of Rs. 5,45,18,123 shown in the account but the total was erroneously struck as minus Rs. 8,95,62,843 instead of minus Rs. 1,94,73,403. This resulted in excess computation of loss by Rs. 7,00,89,440.

As there was no chargeable profit, depreciation allowance of Rs. 19,57,69,760 and tax holiday concession of Rs. 10,76,62,512 should have been carried forward as unabsorbed. Instead, the Income-tax Officer amalgamated the business loss with the unabsorbed depreciation allowance and tax holiday concession and showed the total amount as net loss in the assessment order. Similarly, in the assessment years 1974-75 and 1975-76, unabsorbed depreciation was amalgamated with the business loss in the assessment orders.

The above mistakes resulted in excess carry forward of loss of Rs. 7,00,89,440 and irregular amalgamation of unabsorbed depreciation of Rs. 80,07,20,879 and tax holiday concession of Rs. 10,76,62,512 with the business loss.

While accepting the objection the Ministry of Finance have stated that the assessment for the assessment year 1973-74 had been set aside by the Appellate Assistant Commissioner on 16th February, 1978 on the question of computation of depreciation.

(b) In the case of another assessee-company for the assessment year 1975-76, depreciation of Rs. 6,14,087 already charged to the account for the relevant previous year was omitted to be added back although depreciation for a sum of Rs. 8,89,478 as admissible under the Act was allowed separately. The mistake resulted in excess allowance of depreciation of Rs. 6,14,087 with consequent tax undercharge of Rs. 3,54,637.

While accepting the objection, the Ministry of Finance have stated that the assessment in question has been revised and that the amount of additional demand of Rs. 3.54,637 has been raised and collected.

(c) In computing the total income of still another assessee-company for the assessment year 1976-77, the assessing Officer started from the net loss as shown in the profit and loss account and assessed a total loss of Rs. 30,60,113. In the assessment order the assessing officer disallowed some items of inadmissible expenses amounting to Rs. 6,75,570. The said amount of Rs. 6,75,570 instead of being deducted from the net loss figure of the profit and loss account, was incorrectly added thereto. The mistake resulted in excess computation of carry forward of business loss of Rs. 13,51,140 for the assessment year 1976-77.

The Ministry of Finance have accepted the objection.

(iv) An assessee-company claimed extra shift allowance of Rs. 20,145 in respect of the previous year relevant to the assessment year 1978-79. While allowing depreciation the department incorrectly allowed the allowance at Rs. 2,01,452 instead of Rs. 20,145. The mistake resulted in excess allowance of depreciation of Rs. 1,81,307 with excess computation and carry forward of loss of Rs. 1,81,307.

The Ministry of Finance have accepted the objection.

(v) In the assessment of an assessee-company for the assessment year 1976-77 completed in January 1979, the assessing officer while computing the total income, considered

in the assessment order certain items of expenses aggregating Rs. 61,662 as inadmissible and decided to add back the same to the total income of the assessee. The said amount, however, instead of being added to, was incorrectly deducted from the total income. The mistake resulted in under-assessment of business income by Rs. 1,23,324 with consequent tax undercharge of Rs. 96,859 including penal interest for late submission of return and short payment of advance tax on estimate.

The Ministry of Finance have accepted the objection.

(vi) While computing the income from house property of a non-resident banking company for the previous year relevant to the assessment year 1973-74, the total of the rental income from four properties was incorrectly arrived at Rs. 1,38,421 instead of Rs. 55,598. This led to an over-assessment of income by Rs. 82,823. Further, an expenditure of Rs. 1,86,436 incurred by the assessee-company on up-keep of air conditioning plant in one of its house properties was allowed twice leading to under-assessment of income by Rs. 1,86,436. The net under-assessment of income of Rs. 1,03,613 on account of these two mistakes led to undercharge of tax of Rs. 76,160.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been rectified and that the amount of additional tax of Rs. 76,160 has been raised.

(vii) In the income-tax assessment of an assessee-company for the assessment year 1974-75 finalised in May 1978 an amount of Rs. 1,90,334, being the loss for the assessment year 1973-74 carried forward, was allowed as set off. The assessment for the assessment year 1973-74 was subsequently revised in January 1979 when the income was assessed at Rs. 9,85,340 as against the loss of Rs. 1,90,334 assessed earlier. Consequently, the amount of loss already set off against income in the assessment for the assessment year 1974-75 was required to be withdrawn. However, it was neither withdrawn when the assessment for the year was revised in February 1979 on some other account nor was it withdrawn subsequently. Omission to do so resulted in

under-assessment of income of Rs. 1,90,334 for the assessment year 1974-75 with consequent tax undercharge of Rs. 1,09,917.

The Ministry of Finance have accepted the objection in principle.

(viii) While passing a rectificatory order in January 1978 in the case of an assessee-company for the assessment year 1969-70, the starting point was taken as a loss of Rs. 83,59,125 representing unabsorbed depreciation instead of the correct figure of Rs. 81,69,804. Consequently, in the rectification order, the unabsorbed depreciation to be carried forward was quantified at Rs. 82,59,125 instead of the correct amount of Rs. 80,69,804. The excessive depreciation of Rs. 1,89,321 carried forward resulted in under-assessment of income to the same extent in the assessment year 1975-76 when the company had taxable income with consequent undercharge of tax of Rs. 1,09,332.

The Ministry of Finance have accepted the objection.

(ix) In the case of an assessee-company deriving income both from business and house property, the assessments for the years 1974-75 and 1975-76 were computed at a loss of Rs. 25,73,534 and Rs. 16,42,254 respectively. While computing the income from house property, municipal tax of Rs. 56,575 was deducted from the amount of rent received in each of the two years but the said amounts already debited to the profit and loss accounts of respective years were not deducted for separate consideration from the net loss as shown in the profit and loss accounts. The double allowance of municipal tax resulted in excess computation and excess carry forward of business loss aggregating Rs. 1,13,150 for the two assessment years.

While accepting the objection the Ministry of Finance have stated that the assessments in question have been revised and that the loss has been reduced to the extent of Rs. 1,13,150.

(x) In the original assessment of an assessee-company for the assessment year 1973-74, completed in March 1976, the total income was determined at a loss of Rs. 13,20,951. Subsequently,

pursuant to an appellate order of December 1978 directing the Income-tax Officer to enhance the business loss by Rs. 93,916, the assessment was revised in February 1979. In the revised assessment, however, the total loss was computed as Rs. 15,14,867 instead of the correct amount of Rs. 14,14,867. The mistake resulted in excess computation of loss of Rs. 1,00,000.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been revised and that the excess carry forward of loss to the extent of Rs. 1,00,000 has been reduced.

2.06 *Failure to observe the provisions of the Finance Acts*

(i) Under the provisions of the Finance Act applicable to the assessment year 1974-75, an industrial company in which the public are not substantially interested was liable to income-tax at the rate of 50 per cent on so much of the total income as does not exceed Rs. 2 lakhs and at 60 per cent on the balance, if any, of the total income. The corresponding provisions of the Finance Acts applicable for the earlier years 1969-70 to 1973-74, however, prescribed a rate of 55 per cent in case the total income of such company did not exceed Rs. 10 lakhs.

In the case of such an industrial company for the assessment year 1974-75, the total income was determined at Rs. 7,83,650 on which tax (including surcharge) of Rs. 4,83,200 was chargeable. The department, however, erroneously applied the rates applicable for the earlier assessment years and levied tax of Rs. 4,52,558. The mistake resulted in tax undercharge of Rs. 41,322 including short levy of interest of Rs. 10,680, for the assessment year 1974-75.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been revised and that the amount of additional tax raised is Rs. 41,322.

(ii) Under the Finance Act, 1975, a domestic company in which public are not substantially interested and which is mainly engaged in industrial activity is chargeable to tax at the rate of

55 per cent on the first two lakhs of rupees of its total income and at 60 per cent on the excess over Rs. 2 lakhs.

In the assessments of two private companies for the assessment year 1975-76, the total incomes were computed at Rs. 9,74,930 and Rs. 5,00,000 respectively. Income-tax was charged at a flat rate of 55 per cent on the entire total income in either case. Since, however, the assessees were industrial companies in which public were not substantially interested, income-tax was leviable at the slab rate of 60 per cent on the excess of income over Rs. 2 lakhs as provided in the Finance Act. The mistakes led to an aggregate tax undercharge of Rs. 66,513 including penal interest for belated submission of return of income and short payment of advance tax on estimate.

The Ministry of Finance have accepted the objection.

2.07 *Incorrect status adopted in assessments*

The Income-tax Act, 1961, provides that a company which is treated as one in which the public are substantially interested suffers lesser tax liability in comparison with a company which is not so treated. To be so treated, a company shall, among other things, fulfil the conditions that it is not a private company, and that its shares are listed in a recognised stock exchange in India or its shares carrying more than 50 per cent of the voting power were at no time during the relevant previous year, controlled or held by five or less persons. In computing this number, persons who are relatives of one another are treated together as a single person.

(i) In the assessments of an industrial company for the assessment years 1974-75 to 1978-79, the status of the company was taken as one in which the public were substantially interested and tax was levied accordingly. It was, however, noticed in audit that the shares of the company were not listed in a recognised stock excange in India and shares carrying more than 60 per cent of the company's total voting power were held or controlled by

five or less persons all along during the relevant previous years. The company was, therefore, to be treated as an industrial company in which the public were not substantially interested. The mistake in determining the status of the company led to total tax undercharge of Rs. 1,07,072 in the five assessment years commencing from 1974-75.

The Ministry of Finance have accepted the objection.

(ii) In the assessment of another assessee-company for the assessment year 1976-77, the status of the company was treated by the department as one in which the public are substantially interested and tax was levied accordingly. In the return of income furnished by the assessee for that year the status was, however, shown as one in which the public are not substantially interested. Further, the assessee claimed and was allowed in that assessment year, deduction on account of export markets development allowance at the rate of one and one-third times the amount of the qualifying expenditure as applicable to a company in which the public are not substantially interested. The incorrect determination of the status of the company and application of concessional rate of tax in the assessment year 1976-77 led to short levy of tax of Rs. 93,272.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been rectified and that an additional demand of Rs. 93,272 has been raised.

2.08 *Incorrect computation of business income*

Under the Income-tax Act, 1961, any expenditure laid out or expended wholly or exclusively for the purposes of the business is allowable as a deduction.

(i) Any sum paid by an employer by way of contribution towards an approved gratuity fund created by him for the exclusive benefit of his employees under an irrevocable trust is admissible as a deduction while computing income from business. In September 1970, the Central Board of Direct Taxes issued

instructions that the provision made by the assessee in his accounts on a scientific basis in respect of estimated service gratuity payable to employees is admissible as deduction, even though the assessee might not have created a fund under an irrevocable trust and obtained recognition for it. The said instructions were cancelled by the Board in September 1974 stating that such provisions for gratuity should not be allowed in any pending and future assessment.

With a view to mitigating hardship in cases where provisions had been made by the assessees in their accounts for the previous years relevant to the assessment years 1973-74 to 1975-76 on the basis of their understanding of the law and the clarification given by the Board in 1970 and to put matters beyond doubt, the Income-tax Act, 1961 was amended in 1975 to provide specifically that no deduction shall be allowed in the computation of business income, in respect of any provision made by an assessee for the payment of gratuity to his employees. The provisions for gratuity made during the assessment years 1973-74 to 1975-76 were, however, saved by the amendment, if such provisions were made in accordance with an actuarial valuation of the liabilities of the assessee for payment of gratuity to his employees and the assessee had created an approved gratuity fund and transferred the amount of such provisions to such fund before 1st April, 1977 in the manner prescribed.

(a) In the case of an assessee-company for the assessment year 1973-74, a deduction of Rs. 7.86 lakhs was allowed by the department in March 1977 on account of uptodate accrued gratuity liability to the employees of the company, on the basis of an actuarial valuation. In the assessment order for the assessment year 1974-75, made in August 1977, deduction of Rs. 6,264 was allowed towards further gratuity liability incurred by the assessee during the relevant previous year, as certified by an actuary. However, in the same order, the department allowed the assessee's claim for deduction of a sum of Rs. 10.80 lakhs towards accumulated gratuity liability. This was not in order, as the entire admissible deduction for gratuity liability had already

been allowed. The erroneous allowance resulted in short levy of income-tax and surtax of Rs. 7.60 lakhs.

The Ministry of Finance have accepted the objection.

(b) In the profit and loss account of a company for the year relevant to the assessment year 1975-76, a sum of Rs. 17,13,796 was debited on account of provision for gratuity on the basis of actuarial valuation. It was, however, noticed that the assessee did not have any approved gratuity fund till the close of the previous year ended 31st March, 1975. The assessee in its application of December 1975 sought for the Commissioner's approval to the creation of the gratuity fund from 1st April, 1975. The relevant trust deed also indicated that the proposed gratuity fund should be deemed to have been established from 1st April, 1975. As the assessee did not have any approved gratuity fund during the previous year ending 31st March, 1975 relevant to the assessment year 1975-76, the aforesaid provision of Rs. 17,13,796 was not an admissible deduction and should have been disallowed while completing the assessment. It was also noticed that in the assessment year 1976-77, a total provision of gratuity amounting to Rs. 25,21,796 which included the aforesaid provision of Rs. 17,13,796 was allowed in full. There was thus an under-assessment of business income by Rs. 17,13,796 in the assessment year 1975-76 leading to tax undercharge of Rs. 9,89,716.

The paragraph was sent to the Ministry of Finance in July 1980 ; their reply is awaited (December 1980).

(ii) Interest on borrowings not expended for the purpose of the business would not be allowable in the computation of business income.

In the case of a company it was noticed that huge amounts of loans were granted to its directors free of interest although the company had no sufficient funds of its own to run the business and had to incur heavy loans from banks and to pay substantial

amounts of interest thereon which was claimed and allowed as deductible business expenditure in the respective assessments. The loan funds so diverted to the personal use of the directors could not be said to have been utilised wholly for the purpose of business and proportionate interest payable to the banks should have been disallowed while computing the business income of the company. The omission to do so led to under-assessment of income by Rs. 5,66,910 in the assessment years 1971-72 to 1978-79.

Further, an amount of Rs. 3,92,951 was advanced free of interest to the estate of a deceased person of which one of the directors of the company was the residual legatee. Accordingly, proportionate interest payable to the banks in respect of funds diverted to the estate was diallowable, as not being utilised for the purpose of business. Failure to do so resulted in further undercharge of income by Rs. 4,41,177.

The two mistakes led to total tax undercharge of Rs. 6,35,244 in the assessment years 1974-75 to 1978-79, there being losses in the assessment years 1971-72 to 1973-74.

The paragraph was sent to the Ministry of Finance in July 1980; their reply is awaited (December 1980).

(iii) Under the provisions of the Income-tax Act, 1961, as applicable to the assessment year 1977-78, in the case of a foreign company which receives from an Indian concern any royalty or fees for technical services in pursuance of agreements made before 1st April, 1976, the aggregate of the various deductions admissible in computing the business income by way of royalty or technical fees shall not exceed twenty per cent of the gross amount of such royalty or fees as reduced by any lump sum consideration received for transfer of know-how abroad.

In the assessment of a foreign company for the assessment year 1977-78, the aforesaid ceiling limit of deductions was applied

in respect of the expenses incurred from 1st June, 1976 to 30th November, 1976 and not from 1st April, 1976 to 30th November, 1976 in computing the income although the previous year relevant to the assessment year 1977-78 commenced from 1st April, 1976. The erroneous allowance of full expenses incurred during the period from 1st April, 1976 to 31st May, 1976 resulted in under-assessment of income by Rs. 4,39,287 with consequent short levy of tax of Rs. 2,30,626 in the assessment year 1977-78.

The Ministry of Finance have accepted the objection.

(iv) The Act further provides that any expenditure incurred by a company which results directly or indirectly in the provision of any remuneration, benefit or amenity to a director or to a person who has a substantial interest in the company or to a relative of the director or of such person, as the case may be, is not allowable as deduction from the business income to the extent such expenditure or allowance is in excess of Rs. 72,000 during a previous year comprising more than eleven months or where such expenditure relates to a period not exceeding eleven months, an amount calculated at the rate of Rs. 6,000 for each month or part thereof comprised in that period.

In computing the business income of two assessee-companies the entire expenditure incurred on the remuneration, bonus, commission, salary and perquisites amounting to Rs. 1,71,056, Rs. 1,15,628 and Rs. 1,50,646 of the directors in the previous years relevant to the assessment years 1973-74, 1976-77 and 1977-78 respectively, was allowed as deduction in full instead of limiting it to Rs. 72,000 in each of the three assessments. This led to excess allowance of deduction of Rs. 2,21,330 with undercharge of tax of Rs. 1,40,656.

The Ministry of Finance have accepted the objection.

(v) Under the Income-tax Rules, 1962, only 40 per cent of the income derived from the sale of tea grown and manufactured by a seller in India is deemed to be income derived

from manufacturing and selling operations of the assessee and hence liable to income-tax, the remaining 60 per cent being deemed to relate to the cultivation of tea, income from which is agricultural in nature and hence not liable to income-tax.

(a) In the assessment of a company carrying on the business of growing and manufacturig tea in India for the assessment year 1972-73 completed in February 1979, the entire loss of Rs. 3,76,738 computed on account of manufacture and sale of tea was incorrectly carried forward instead of only 40 per cent thereof as prescribed under the rules. Further, while computing the aforesaid loss, an interest income of Rs. 26,358 duly credited in the relevant profit and loss account was not separately assessed under the head 'other sources'. The two mistakes resulted in excess carry forward of loss of Rs. 2,41,858 for the assessment year 1972-73.

The Ministry of Finance have accepted the objection.

(b) In the case of two other tea companies, income from interest on fixed deposits in banks, on loans and advances and from the Income-tax department, received in India in the years relevant to the assessment years 1975-76 and 1976-77 was assessable as income from other sources and was taxable in full under the provisions of the Act. The department, however, adjusted the amount of interest payable on loan relating to tea business against the aforesaid gross interest receipts and taxed the net interest receipts only. The aggregate tax undercharge on this account amounted to Rs. 1,48,484 for the two assessment years 1975-76 and 1976-77.

The paragraph was sent to the Ministry of Finance in July 1980; their reply is awaited (December 1980).

(vi) In the computation of its business income for the assessment year 1976-77, an assessee-company engaged in sale of liquor/resin in wholesale, claimed and was allowed as depreciation the whole amount of the cost of aluminium drums

purchased by it as the actual cost of each drum did not exceed seven hundred and fifty rupees, although the company had not written off the cost of the drums in its profit and loss account for the previous year relevant to the assessment year 1976-77. The company finally wrote off the book value of the drums amounting to Rs. 1,02,355 in its accounts for the previous year relevant to the assessment year 1978-79. While computing the business income of the company for the assessment year 1978-79, the assessing officer omitted to disallow the amount so written off although the original cost of the drums had already been allowed in the assessment for the year 1976-77. This resulted in under-assessment of income of Rs. 1,02,355 and tax under-charge of Rs. 69,857.

The Ministry of Finance have accepted the objection.

(vii) In the case of two assessee-companies sums of Rs. 3,01,970 and Rs. 2,34,704 which related to the assessment year 1975-76, were debited to the profit and loss accounts of the previous year relevant to the assessment year 1976-77 under 'Special benefit to workers'. Even though the book profit was adopted in each case as the basis for assessment of income for the assessment year 1976-77, deductions of further sums of Rs. 3,01,970 and Rs. 2,34704 were allowed on the same account while computing the income. This resulted in double allowance of deductions of Rs. 3,01,970 and Rs. 2,34,704 which in fact related to the assessment year 1975-76. The assessments finalised in March 1978 were rectified in August 1978 withdrawing the amounts of Rs. 3,01,970 and Rs. 2,34,704 respectively stating that the expenditure related to the assessment year 1975-76 wherein the deductions had been allowed. In spite of this rectification, the amounts of Rs. 3,01,970 and Rs. 2,34,704 already debited to the profit and loss accounts for the assessment year 1976-77 remained to be withdrawn. This led to excess computation of total loss of Rs. 5,36,674 for the assessment year 1976-77.

The Ministry of Finance have accepted the objection.

(viii) The Act provides that any loss computed in respect of a speculation business, can be set off only against profits and gains, if any, of another speculation business. A speculative transaction is defined in the Income-tax Act, 1961 as one in which a contract for the purchase or sale of any commodity is periodically or ultimately settled otherwise than by the actual delivery of the commodity or scrips but hedging contracts entered into by manufacturers and merchants to guard against loss through future price fluctuations are not to be deemed to be a speculative transaction. It has also been judicially held that compensation received for breach of contract of sale is not receipt from a speculative transaction.

A company manufacturing rice bran oil during the accounting year relevant to the assessment year 1975-76 received a compensation of Rs. 2,00,146 from two parties who failed to take delivery of the oil despatched to them. It also received damages to the extent of Rs. 26,740 from a supplier who failed to supply the entire contracted quantity. These receipts were of the nature of business income and any speculation losses of earlier years could not be adjusted against this income. But the entire amount of Rs. 2,26,886 was adjusted against the speculation loss of the previous year relevant to the assessment year 1975-76 and earlier years. The incorrect classification of business income as speculation profits and erroneous adjustment of speculation losses of earlier years against this income resulted in tax undercharge of Rs. 1,42,976.

The Ministry of Finance have stated that there is no agreement among the High Courts regarding the extent of application of the relevant provisions of the Act and the action of the Income-tax Officer would find support in the view taken by one High Court. They have not indicated what action they propose to take to set at rest the resultant controversy.

(ix) The Income-tax Rules, 1962 framed under the Income-tax Act, 1961 provide that in computing the profits and gains of the business of distribution of feature films carried on by a person, the deduction in respect of the cost or acquisition of a feature film is allowable in the manner prescribed thereunder. The cost of acquisition for the purpose of such deduction, however, does not include the amount of expenditure incurred by the film distributor for the preparation of the positive prints of the film.

An assessee-company carried on the business of film distribution. In its assessment for the assessment year 1975-76 the department while computing the business income allowed a deduction of an amount of Rs. 3,91,251 on account of amortisation of a feature film as claimed by the assessee. The said sum, however, included an amount of Rs. 1,25,000, being the cost of additional prints. The incorrect inclusion of the cost of additional prints in the total cost of the feature film for working out the deduction on account of amortisation thus resulted in excess allowance of deduction by Rs. 1,25,000 with consequent tax undercharge of Rs. 72,459 including incorrect payment of interest on excess payment of advance tax.

Final reply of the Ministry of Finance is awaited (December 1980).

(x) According to the provisions of the Income-tax Act, 1961, introduced in 1968, with a view to curbing tax evasion, payments made by an assessee to his close associates for supply of goods, services or facilities should be disallowed in the computation of his business income, to the extent such payments are excessive or unreasonable, having regard to the fair market value of the goods, services or facilities. Payments made by a company to another company where one of them is substantially interested in the other or payments made to a company, one of the directors of which is substantially interested in the company making the payment, would be covered by these provisions.

During the accounting year relevant to the assessment year 1973-74, two private industrial companies made payments of Rs. 3.96 lakhs and Rs. 1.00 lakh to another private company, closely connected with them, as consultancy fees. The assessees claimed full deduction for the payments on the ground that the recipient company rendered services to the assessees in the conduct of business, on income-tax matters, training of personnel, labour relations, etc. But the precise nature and extent of the services rendered was not known from the records. In fact, the assessees did not produce to the department any claim bills issued by the recipient company detailing the activities for which the payments had been made by the assessees. However, the assessments of both the companies for the assessment year 1973-74 were completed in September 1976 by the department admitting the claim in full. It was pointed out in audit (November-December 1977) that, in the context of the close relationship between the assessees and the payee-company, the department should have examined, as statutorily required, how far the payments of Rs. 3.96 and Rs. 1.00 lakh towards consultancy fees were reasonable and disallowed the payments to the extent found excessive or unreasonable. Initially, the department contended that there was no material on record to hold that the payments were excessive or unreasonable. However, subsequently (September 1979), the assessment of one of the companies was revised disallowing the payment to the extent of Rs. 2.98 lakhs (out of the total payment of Rs. 3.96 lakhs), one of the grounds for the disallowance being that the Company Law Board had found the payment to be excessive. Part of the consequential additional demand of Rs. 1,87,953 has been collected by adjustment of refund due to the assessee and report of collection of the balance of Rs. 1,35,547 is awaited.

Final reply of the Ministry of Finance is awaited (December 1980).

2.09 *Irregularities in the allowance of Head Office expenses*

Under the provisions of the Income-tax Act, 1961, any expenditure other than capital expenditure and personal expenses of the assessee, laid out or expended wholly and exclusively for the purpose of the business is an allowable deduction in the computation of the business income of an assessee. In the case of foreign companies doing business in India, a portion of the administrative expenses of their Head Offices becomes an allowable deduction. Till 1975 the checks exercised by the department on allowing claims towards Head Office expenses were inadequate. Pursuant to the recommendations made by the Public Accounts Committee in paragraph 9.13 of their 176th Report (Fifth Lok Sabha) and paragraph 3.38 of their 187th Report (Fifth Lok Sabha), detailed guidelines on the subject were issued by the Central Board of Direct Taxes in June 1975 and the law was also amended by the insertion of a new Section 44C in the Income-tax Act, 1961, with effect from 1st June, 1976. This new Section fixed a ceiling limit on the deduction on account of Head Office expenses as the least of the following three items :—

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

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

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

In the assessment of a non-resident company for the assessment year 1977-78, completed in September 1978, it was seen in audit in September 1979 that the aforesaid ceiling limit in respect of the head office expenditure had not been applied though the provisions relating thereto were effective from the assessment year 1977-78. This led to an under-assessment of income of Rs. 20,81,501 and consequent short levy of tax of Rs. 15,29,903

apart from short levy of interest of Rs. 2,60,241 for non-payment in full of advance tax due.

The paragraph was sent to the Ministry of Finance in July 1980; their reply is awaited (December 1980).

Irregularities in allowing depreciation and development rebate

2.10 *Depreciation*

The Income-tax Act, 1961 provides for grant of depreciation on buildings, plant and machinery owned by the assessee and used for the purpose of his business in computing the income from business if the prescribed particulars have been furnished by the assessee in respect of such buildings, plant and machinery. The Rules prescribed in this regard, provide for specified rates of depreciation for certain items of plants and machinery and a general rate of 10 per cent for the remaining items of plant and machinery on the actual cost or the written down value of the assets, as the case may be.

(i) In respect of first class substantial buildings of selected materials, depreciation is admissible at 2.5 per cent of the actual cost. While assessing the income of an assessee-company running a hotel for the assessment years 1975-76 and 1976-77, during September and October 1978 respectively, depreciation at the rate of 5 per cent instead of 2.5 per cent was allowed on the cost of the hotel building though it was a first class building constructed using selected materials. The application of incorrect rate of depreciation resulted in total excess allowance of depreciation of Rs. 76,535. There was no positive income during the years concerned and hence excess depreciation carried forward amounted to Rs. 76,535.

The Ministry of Finance have accepted the objection.

(ii) In the case of a non-resident company engaged in air transport business, depreciation on air crafts was allowed in the

assessment years 1973-74 and 1974-75 at 40 per cent against 30 per cent as admissible under the Rules. This led to excess allowance of depreciation and consequent excess computation and carry forward of loss of Rs. 6,23,402 in the two assessments.

The Ministry of Finance have partly accepted the objection

(iii) In respect of ships owned by an assessee and used for the purpose of his business or profession, the rate of depreciation is 5 per cent for ocean going ships, not being fishing vessels, and 10 per cent for vessels other than "speed boats" ordinarily plying on inland waters.

In its assessment for the year 1975-76, a shipping company was allowed depreciation on two barges at the rate applicable to vessels other than "speed boats" at the rate of 10 per cent in the original assessment completed in September 1978. Since the barges were treated as 'vessels' and not as 'ships', the assessee's claim for development rebate which was admissible only on 'ships' was not allowed by the department. On an appeal, however, the assesse's claim for dvelopment rebate was allowed by the appellate authority (February 1979) holding the barges as 'ships'. While giving effect to the appellate orders in March 1979, however, the higher rate of depreciation of 10 per cent originally allowed, treating the barges as 'vessels' was not reduced an dthe correct rate of depreciation of 5 per cent applicable to 'ships' was not applied. This resulted in the grant of excess depreciation of Rs. 2,88,221 and short levy of tax of Rs. 1,81,580.

The paragraph was sent to the Ministry of Finance in August 1980; their reply is awaited (December 1980).

(iv) It has been judicially held that several persons having specified fractional shares in a depreciable asset cannot claim proportionate fractional depreciation in respect of the same depreciable asset. According to the High Court concerned, a

fractional share in the asset will not suffice for granting depreciation allowance.

A company constructed a multi-storeyed building equipped with various utilities *viz.*, air conditioning plant, lifts and tubewell etc. on its own land under co-ownership with 24 other companies who contributed towards the cost of construction of the building. The aforesaid company leased out office flats in the building to the 24 co-owners according to their share of contribution towards construction retaining a certain portion for itself. In terms of the lease deed executed, the co-owners owned their respective office flats and also various utilities in the proportion of office flats owned by them. In the assessment of the aforesaid company for the assessment years 1973-74 and 1974-75, depreciation allowance of Rs. 89,368 and Rs. 77,924 respectively, calculated on the assessee's share of the value of utility assets *viz*, air conditioning plant, lifts and tubewells were allowed by the department as claimed. Since the assessee did not own the assets exclusively but was only a co-owner of a fractional share in the said asset, no depreciation allowance was admissible in terms of the judicial pronouncement which held that fractional share would not suffice for granting an allowance of depreciation on an asset. The incorrect allowance resulted in total tax undercharge to the extent of Rs. 96,611 for the two assessment years.

The Ministry of Finance have stated that the case was not well argued before the court and hence, it cannot be said that the decision lays down a binding precedent.

(v) The Rules prescribe a rate of 30 per cent for earth-moving machinery employed in heavy construction works such as dams, tunnels, canals, etc.

During the year ended 31st March, 1974 relevant to the assessment year 1974-75, a private company acquired a crane at a cost of Rs. 20,86,664 for its contract business of dredging and removal of earth from sand bars in the Bay of Bengal. For

the assessment years 1974-75 and 1975-76, the assessee claimed depreciation in respect of the crane at the special rate of 30 per cent which was allowed by the department. As the crane was not an earth-moving machine, it was not entitled to the higher rate (30 per cent) of depreciation. Only the general rate of 10 per cent was admissible. The department's omission to disallow the claim for the higher rate of depreciation for the two assessment years 1974-75 and 1975-76 resulted in under-assessment of income of Rs. 4,17,333 and Rs. 2,50,401 leading to short levy of income-tax of Rs. 3,30,555 and Rs. 2,16,044 respectively.

Final reply of the Ministry of Finance is awaited (December 1980).

(vi) While assessing the income of an assessee-company for the assessment year 1976-77, the total amount of depreciation admissible was worked out at Rs. 14,56,100 comprising initial depreciation of Rs. 3,83,235 and other depreciation of Rs. 10,72,865. This amount of depreciation was adjusted against the income of Rs. 59,856 and the amount of unadjusted depreciation to be carried forward for set off during subsequent years correctly worked out to Rs. 13,96,244. However, the assessing officer quantified the amount of unadjusted depreciation to be carried forward at Rs. 13,96,244 in addition to initial depreciation of Rs. 3,83,235. Since the former amount of Rs. 13,96,244 already included the amount of initial depreciation, this resulted in excess carry forward of unadjusted depreciation of Rs. 3,83,235.

The Ministry of Finance have accepted the objection in principle.

2.11 *Development rebate*

Under the Income-tax Act, 1961, if any machinery or plant or ship on which development rebate was allowed in any earlier assessment is sold before the expiry of eight years from the end

of the previous year in which it was installed or acquired, the development rebate so granted should be deemed to have been allowed wrongly and the total income should be recomputed withdrawing the development rebate originally allowed.

(i) During the previous year relevant to the assessment year 1974-75 a shipping company sold its ship acquired in the previous year relevant to the assessment year 1967-68. As the ship was sold within the prohibited period of eight years, the development rebate of Rs. 85,342 allowed in the assessment year 1972-73 when the company had sufficient profits to allow the rebate relating to the assessment year 1967-68, should have been withdrawn. As the rebate allowed in the assessment year 1967-68 was not withdrawn, there was an under-assessment of income by Rs. 85,342 with undercharge of tax of Rs. 56,859.

The Ministry of Finance have accepted the objection.

(ii) In another case for the assessment year 1977-78, an assessee-company sold certain machinery on which development rebate of an amount of Rs. 87,697 had earlier been allowed in the assessment for the assessment year 1974-75. As the machinery was sold within the prohibited period of eight years, the income for the assessment year 1974-75 should have been recomputed by withdrawing the development rebate earlier allowed. Failure to do so led to under-assessment of business income by Rs. 87,697 with consequent tax undercharge of Rs. 65,330 in the assessment year 1974-75.

The Ministry of Finance have accepted the objection.

(iii) The Act also provides that no deduction by way of development rebate is allowable in respect of any machinery or plant installed after 31st March, 1965, in any office premises or any residential accommodation, including any accommodation in the nature of a guest house.

In the case of two electric supply companies, development rebate on meters and indicators installed in the office premises and residential accommodations of their customers was allowed for the assessment years 1966-67 to 1969-70. This led to incorrect allowance of development rebate of Rs. 2,48,493 with tax undercharge of Rs. 1,26,289 in the assessment years 1966-67 to 1969-70.

The paragraph was sent to the Ministry of Finance in August 1980; their reply is awaited (December 1980).

Irregular exemptions and excess reliefs given

2.12 *Incorrect allowance of deductions in excess of the gross total income*

Chapter VI A of the Income-tax Act, 1961 provides for certain deductions in the computation of total income. The aggregate amount of deductions to be made under the provisions of that Chapter should not, in any case, exceed the gross total income. The 'gross total income' means the total income computed under the Act before making the deductions under Chapter VI A.

In the case of three assessee-companies their income was determined for the assessment years 1969-70 and 1976-77 at a loss of Rs. 4,45,910, Rs. 2,00,564 and Rs. 79,619 before making the aforesaid deductions under the Act. Accordingly, no deductions under Chapter VI A were admissible as there was no positive income. The department, however, allowed deductions of Rs. 1,57,793, Rs. 1,02,710 and Rs. 59,850 in respect of royalties received from certain foreign enterprises in one case and dividend received from domestic companies in the other two cases. This resulted in excess computation and excess carry

forward of loss of Rs. 1,57,593, Rs. 1,02,710 and Rs. 59,850 in the three cases respectively.

The Ministry of Finance have accepted the objections.

2.13 *Irregular allowance of relief in respect of newly established undertakings*

Under the provisions of the Income-tax Act, 1961, where the gross total income of an assessee includes any profits and gains derived from a newly established industrial undertaking, the assessee becomes entitled to tax relief in respect of such profits and gains upto six per cent per annum of the capital employed in the industrial undertaking, in the assessment year in which the undertaking begins to manufacture or produce articles and also in each of the four assessment years immediately succeeding the initial assessment year. The Rules framed under the Act provide that any borrowed money and debt due by the person carrying on the business shall be deducted from the value of assets in the computation of capital for this purpose.

(i) In the case of an assessee-company which started a new industrial unit in the previous year relevant to the assessment year 1975-76, while computing the capital, the department did not deduct, from the value of the assets, the proportionate amounts of other debts relatable to the unit out of the total debts incurred by the company. This resulted in excess computation of capital to the extent of Rs. 71,81,884 in the assessment year 1975-76 and consequent excess allowance of relief of Rs. 4,30,913. In the absence of profit in the new industrial undertaking the excess relief of Rs. 4,30,913 was allowed to be carried forward.

The Ministry of Finance have accepted the objection.

(ii) A new industrial undertaking of an assessee-company which was entitled to the relief in the previous year relevant to the assessment year 1970-71 had suffered a loss of Rs. 2,98,511 as per the profit and loss account of the year, and was not,

therefore, entitled to the relief. In the statement claiming the relief the assessee, however, showed the figure of loss as profits and on the basis of that statement the department incorrectly allowed a relief of Rs. 2,98,511 leading to undercharge of tax of Rs. 1,64,181 and excess refund of tax to that extent.

The Ministry of Finance have accepted the objection.

2.14 *Irregular exemptions given*

The Income-tax Act, 1961 provides that financial corporations engaged in providing long-term finance for industrial or agricultural development in India are entitled to a deduction, in the computation of their taxable profits of the amount transferred by them out of such profits to a special reserve account, upto a specified percentage of their total income as computed before making any deduction under Chapter VI A of the Act. The Board issued instructions in November, 1969 to the effect that this deduction is to be calculated by applying the specified percentage to the total income arrived at after the deduction. Subsequently, the Board issued a clarification to the Department of Banking in November 1973 to the effect that the percentage should be applied to the total income computed before making the said deduction. The clarification being contrary to law was not accepted in audit and the matter was taken up with the Board in December 1975. In January 1977 the Board stated that the viewpoint expressed by Audit was acceptable to them. Necessary instructions in this respect were, however, issued only in August 1979. In the meantime, the assessing officers continued to act upon the Board's clarification of November 1973. This accounted for a number of costly mistakes.

Mention of such irregularities has been made in paragraph 25(iii) of Audit Report 1975-76 and paragraph 29(i) of Audit Report 1978-79. Further mistakes noticed in audit are as under :—

In the case of eight corporations in 6 Commissioners' charges, it was observed that during the assessment years 1971-72 to

1978-79, this deduction was worked out at the prescribed percentage of the income of the corporations before deducting this allowance. This resulted in under-assessment of income of Rs. 62,35,816 with resultant tax undercharge of Rs. 36,57,826.

The Ministry of Finance have stated that the very fact that the Board had to issue instructions on this point three times shows that the matter was not so obvious or clear. The assessments in question have, however, been revised by the department for some years and the action is pending in the others.

2.15 *Irregular computation of capital gains*

Under the provisions of the Income-tax Act, 1961, any profit or gain arising from the transfer of a capital asset is chargeable to tax as income. The capital gain is determined by deducting the cost of acquisition of the asset and of any improvements thereto, from the value of the consideration received or accruing on the transfer. Where the capital asset became the property of the assessee or of the previous owner before 1st January, 1954, the fair market value of the asset as on that date is allowed to be substituted at the option of the assessee, for the actual cost of acquisition for determining the amount of capital gain. In the case of an asset for which depreciation has been allowed in computing income, the cost of acquisition of the asset would be its written down value as adjusted. It has been judicially held that, in respect of depreciable assets, the concession of substituting the fair market value as on 1st January, 1954 is available only if the asset becomes the property of the assessee by gift or will or on distribution of assets on partition of a Hindu undivided family or dissolution of a firm or by other specified modes and not if such assets were acquired by the assessee by purchase.

(i) In the case of a company, for the assessment year 1974-75 completed in August 1977, capital gain of Rs. 2,09,316 was determined in respect of a factory building which was sold for Rs. 15,61,644. The capital gain was arrived at by taking the

fair market value of the building as Rs. 13,52,328 as on 1st January, 1954. As the assessee acquired the building by purchase and as depreciation was allowed thereon from year to year, the assessee was not entitled to substitute the fair market value on 1st January, 1954 as his cost of acquisition. As provided in the statute, the cost of acquisition in this case would work out to Rs. 59,050, taking into account the written down value of Rs. 17,114 as adjusted by the terminal profit of Rs. 41,936 at the time of the sale. Since the factory building was sold for Rs. 15,61,644, the capital gain involved would work out to Rs. 15,02,594 and not Rs. 2,09,316 as assessed by the department. The incorrect substitution of the fair market value resulted in short levy of tax of Rs. 5,81,975. Further, the terminal profit representing the difference between the cost of the asset and its written down value was also assessable as business income of the assessee. Omission to do so resulted in under-assessment of business income of Rs. 41,936 and short levy of tax of Rs. 24,218. The total short levy of tax amounted to Rs. 6,06,193.

The paragraph was sent to the Ministry of Finance in September 1980 ; their reply is awaited (December 1980).

(ii) An assessee-company was assessed on a capital gain of Rs. 20,55,067 on the sale of shares of a foreign company in the assessment year 1976-77. While computing the capital gains, the company was allowed substitution of the fair market value of the relevant shares as on 1st January, 1954 but the value of the shares expressed in pound sterling was converted at the rate of Rs. 18 per pound sterling although the correct rate applicable on 1st April, 1954 was Rs. 13.33 per pound sterling. The application of the incorrect rate led to over-computation of the cost of acquisition of the shares by Rs. 3,93,641 and undercharge of tax of Rs. 2,27,327 in the assessment year 1976-77.

The paragraph was sent to the Ministry of Finance in August 1980 ; their reply is awaited (December 1980).

2.16 *Income escaping assessment*

(i) In consequence of devaluation of Indian currency in June 1966 an assessee-company made a provision of Rs. 19,48,067 in its accounts for the previous year relevant to the assessment year 1967-68 to meet the increase in liability for payment of the cost of goods purchased outside India. The provision which was originally disallowed by the department was, however, allowed in the revised assessment made in August 1972 on the orders of the appellate authorities.

As a result of devaluation of pound-sterling in November 1967, the rupee liability of the company for payment of the above cost of goods was reduced by Rs. 8,08,341 and a credit for the sum was made by the company in its accounts for the previous year relevant to the assessment year 1969-70. In computing the business income of the company for the assessment year 1969-70 in March 1971, the department did not take into account the amount of Rs. 8,08,341 on the ground that the additional liability of Rs. 19,48,067 was not allowed in the assessment year 1967-68. On the revision of the assessment for 1967-68 in August 1972 for allowance of the liability for Rs. 19,48,067, the assessment for 1969-70 was required to be revised to bring to tax the reduction of liability of Rs. 8,08,341 credited in the accounts of the relevant previous year. Omission to do so led to a total undercharge of income-tax, surtax and interest amounting to Rs. 4,87,687 in the assessment year 1969-70.

The Ministry of Finance have accepted the objection.

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

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

A sum of Rs. 14,43,562 was written back in the accounts of an assessee-company for the year relevant to the assessment year 1976-77 on account of gratuity provision made in earlier years. It was noticed in audit that provision for gratuity liabilities to the extent of Rs. 1,04,642 had earlier been allowed in the assessments for the assessment years 1971-72 and 1972-73. Accordingly, an amount of Rs. 1,04,642 was required to be treated as income chargeable to tax in the assessment year 1976-77. This having not been done, there was escapement of income by Rs. 1,04,642 in the assessment year 1976-77 with consequent tax undercharge of Rs. 65,924 together with penal interest of Rs. 21,755 for short payment of advance tax on estimate.

The Ministry of Finance have accepted the objection.

(iii) The Act further provides that if an assessee receives a refund of expenditure in respect of which deduction has already been made in the assessment for any year, the refund is chargeable to income-tax as the income of the year in which the refund is received. A case of non-disclosure of refunds of Central Excise duty was earlier examined by the Public Accounts Committee and their recommendations are contained in paragraph 1.44 of their 51st Report (Sixth Lok Sabha).

During the previous year relevant to the assessment year 1977-78, an assessee-company received a sum of Rs. 1,09,037 as refund of sales tax and another sum of Rs. 36,188 as refund of excise duty. As the payments of sales tax and excise duty had been allowed as admissible expenditure in the assessments of the previous years concerned, the amounts of refunds should have been treated as income and assessed to tax in the year of the refund. Failure to do so resulted in undercharge of tax of Rs. 83,864.

The paragraph was sent to the Ministry of Finance in July 1980 ; their reply is awaited (December 1980).

(iv) Under the Income-tax Act, 1961, income under the head 'Profits and gains of business or profession' is computed in accordance with the method of accounting regularly employed by the assessee. If the mercantile method of accounting is followed by an assessee, all income is required to be accounted for on accrual basis and assessed to tax.

In the case of two assessee-companies following mercantile system of accounting, the accounting method was changed from accrual to cash basis during the previous years relevant to the assessment years 1973-74 to 1975-76 in respect of only one isolated item of interest receivable on loan advanced to a sister concern. This irregular change in the system of accounting by the assessees resulted in escapement of interest income by an aggregate sum of Rs. 7,91,790 with consequent tax undercharge of Rs. 4,56,958 in the three assessment years 1973-74 to 1975-76.

The paragraph was sent to the Ministry of Finance in September 1980 ; their reply is awaited (December 1980).

(v) Under the provisions of the Income-tax Act, 1961, the total income of a person should include all income that accrues to or is received by him during the year. Where an assessee maintains his accounts on the mercantile system, the income computed for assessment should be the income actually earned, though not realised, bringing into credit what is due immediately it becomes legally due, even though it is not actually received in the year.

In the case of an assessee-company, the business of generation and supply of electricity to two towns was taken over by the State Electricity Board on the expiry of period of licence. As a consequence of Court orders of September 1969 and July 1972, the assessee-company became entitled to interest on unpaid amounts of compensation. Although the company maintained its accounts on mercantile system, except for a part amount in the

assessment year 1973-74, the company did not return and the assessing officer also did not bring to assessment the accrued interest in the assessment years 1970-71 to 1977-78. As a result, the total amount of Rs. 6,00,390 escaped assessment leading to short levy of tax of Rs. 3,51,590.

The paragraph was sent to the Ministry of Finance in August 1980 ; their reply is awaited (December 1980).

2.17 *Irregular set off of losses*

(i) Under the provisions of the Income-tax Act, 1961, where in respect of any assessment year the net result of the computation under any head of income other than capital gains is a loss and the assessee had income under capital gains, such loss may be set off against the income under any head including capital gains assessable for that assessment year. Where the assessee exercises an option, such loss can only be set off against the income from short-term capital gains and income under any other head.

A company received a compensation of Rs. 6,90,743 in the previous year relevant to the assessment year 1973-74 in respect of pieces of land costing Rs. 1,16,590 acquired by a State Government and an Improvement Trust. The company preferred a reference application in the court of law against the award and pending settlement kept the amount of the compensation award under other liabilities. The capital gains of Rs. 5,74,153 arising out of the compensation award was not returned by the company and the department also did not assess it.

In the absence of an option by the company, the capital gain of Rs. 5,74,153 assessable in the previous year relevant to the assessment year 1973-74 was required to be set off against the business loss of the year. Omission to do so led to excess computation and carry forward of business loss of Rs. 5,74,153.

The paragraph was sent to the Ministry of Finance in July 1980 ; their reply is awaited (December 1980).

(ii) The Act further provides that a company whose business mainly consists in dealing in shares is a trading company and any loss incurred by it in purchase and sale of shares of other companies is speculation loss and such loss shall not be set off except against profits and gains, if any, of another speculation business of the company. In the case of an investment company or a company the principal business of which is the business of banking or the granting of loans and advances, the business of purchase and sale of shares of other companies is, however, not speculation business.

In the assessment of a company, the total loss for the previous year relevant to the assessment year 1978-79 was computed at Rs. 2,17,989 including a loss of Rs. 2,00,400 on account of speculation business. From the details furnished by the assessee-company it was noticed that it had a further loss of Rs. 1,93,266 on account of purchase and sale of shares. The company being a trading company whose business mainly consisted in dealing with shares, the loss of Rs. 1,93,266 was speculation loss and was not adjustable against the business income of the company. As the department did not compute the loss of Rs. 1,93,266 as speculation loss, there was under-assessment of total income of Rs. 1,60,154 with undercharge of tax of Rs. 92,489 in the assessment year 1978-79.

In another case, the assessee-company was a grower and manufacturer of tea. The company purchased in February 1976 shares of another company at a cost of Rs. 2,85,000. In March 1976 the company sold the shares at Rs. 2,15,175, thereby incurring a loss of Rs. 69,825. The assessee not being an investment company, the amount of Rs. 69,825 was a loss in speculation business and it could not be set off except against profits and gains, if any, of another speculation business. The department, however, assessed the loss as short-term capital loss and allowed it against the business income of the assessee. This led to under-assessment of income by Rs. 69,825 in the assessment year 1977-78 with undercharge of tax of Rs. 40,327 and consequent

short levy of interest of Rs. 2,823 on account of delay in submission of the return of income and non-payment of advance tax.

The paragraph was sent to the Ministry of Finance in September 1980 ; their reply is awaited (December 1980).

(iii) Under the provisions of the Income-tax Act, 1961, as it stood prior to 1st April, 1978, accumulated business loss and unabsorbed depreciation allowance of a company which merges with another company under a scheme of amalgamation cannot be carried forward and set off by the latter company against its profits.

During the assessment year 1977-78 a company was merged with another company under a scheme of amalgamation. While computing the total income of the latter (amalgamated) company for this assessment year the department set off against its profits unabsorbed business loss and depreciation allowance of earlier years in respect of both the companies amounting to Rs. 1,89,950 out of which a sum of Rs. 1,15,126 related to the amalgamating company. The set off of the aforesaid loss of Rs. 1,15,126 was not correct and this led to under-assessment of income by the same amount with consequent tax undercharge of Rs. 72,272 in the assessment year 1977-78.

The Ministry of Finance have accepted the objection.

2.18 *Mistake in assessments while giving effect to appellate orders*

(i) In the case of an assessee-company for the assessment year 1972-73, the contention that the value of the closing stock of cotton should be taken at the market value of Rs. 11,30,123 instead of at the book value of Rs. 13,15,249 was upheld by the Income-tax Appellate Tribunal. The order of the Tribunal was given effect to on 20th September, 1978, thereby reducing the income by Rs. 1,85,126. However, the assessment for the succeeding assessment year *i.e.* 1973-74, already finalised on the basis of the value of the opening stock of cotton at Rs. 13,15,249 instead

was not revised, taking into account the modified value of the opening stock of cotton though the assessment was revised on some other grounds on 28th September, 1978. The omission resulted in under-assessment of income of Rs. 1,85,126 for the assessment year 1973-74 with consequent undercharge of tax of Rs. 1,06,910.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been revised raising an additional demand of Rs. 1,06,910.

(ii) An assessee-company incurred expenditure of Rs. 2,05,066 and Rs. 49,108 on research and development during the previous years relevant to the assessment years 1969-70 and 1970-71 respectively. In the income-tax assessments of both the assessment years the Income-tax Officer treated the said expenditure as capital expenditure and disallowed the same. Separately, depreciation was allowed on the expenditure capitalised in the income-tax assessments for the assessment years 1969-70 to 1975-76 and the total amount of depreciation allowed was Rs. 1,75,333. Subsequently, the assessments for the assessment years 1969-70 and 1970-71 were revised during November 1978 to give effect to the orders of the Appellate Assistant Commissioner who held that the amounts of expenditure of Rs. 2,05,066 and Rs. 49,108 were to be treated as revenue expenditure and allowed as deductions in computing the income of the assessee. Consequently, the depreciation allowed thereon for the assessment years 1969-70 to 1975-76 was required to be withdrawn. The depreciation allowed for the assessment years 1969-70 and 1970-71 only was, however, withdrawn. Thus, depreciation of Rs. 1,39,393 was allowed in excess for the assessment years 1971-72 to 1975-76. This resulted in undercharge of tax of Rs. 80,501.

The Ministry of Finance have accepted the objection. The assessment in question has been revised and the additional tax of Rs. 80,501 has been raised.

(iii) While assessing the income of an assessee-company for the assessment year 1974-75 the Income-tax Officer disallowed

an amount of Rs. 2,08,610 debited to the profit and loss account treating it as capital expenditure incurred on plant and machinery, and allowed deductions of Rs. 52,157 towards development rebate and Rs. 41,722 towards depreciation. On appeal by the assessee, the Appellate Assistant Commissioner upheld the contention of the assessee that the expenditure was of revenue nature and was, therefore, deductible in computing the income. While giving effect to the appellate orders on 27th March, 1978 the deductions originally allowed towards depreciation and development rebate were not withdrawn. This resulted in under-assessment of income by Rs. 93,879 with consequent tax undercharge of Rs. 54,216.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been rectified and that the amount of additional tax raised and collected is Rs. 54,216.

(iv) While computing the income of an assessee-company for the assessment year 1971-72 deduction was allowed in respect of research contribution payable by the company and also income-tax of Rs. 1,28,593 payable thereon and paid by the assessee-company. Subsequently, on the basis of the orders of the Income-tax Appellate Tribunal who held that no tax was payable on research contribution, the assessee received refund of tax of Rs. 1,28,593 during the previous year relevant to the assessment year 1975-76. In view of this the department re-opened the assessment for the assessment year 1971-72 in July 1977 and withdrew the deduction of Rs. 1,28,593 allowed to the assessee. This was, however, deleted by the Appellate Assistant Commissioner in February 1978 who held that the refund was to be taxed in the year of its receipt *i.e.* in the assessment year 1975-76. But while finalising the assessment of the assessment year 1975-76 in March 1978 the refund of Rs. 1,28,593 received during the relevant previous year, was not included in the total income. This resulted in under-assessment of income of Rs. 1,28,593 with consequent excess computation of loss to the same extent.

The paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

2.19 *Excess or irregular refunds*

The Income-tax Act, 1961 lays down that while making a provisional assessment for refund, adjustment to the income or loss declared in the return could be made by the Income-tax Officer to the extent laid down in the Act. Though the Act provides for the adjustment of the brought forward unadjusted loss, there is no provision for allowing the loss relating to earlier previous years in respect of which assessments were still pending. The Act also provides for disallowance of items which are *prima facie* inadmissible.

In the provisional assessment of an assessee-company for the assessment year 1977-78, completed in January 1978, the assessee's claim for set off of loss of Rs. 9,22,835 being the loss as per the return relevant to the assessment year 1976-77 was allowed and a refund of Rs. 2,87,420 was made to the assessee. The adjustment of the loss relating to the assessment year 1976-77, when the regular assessment for that year was still pending was not in order. Also, an amount of Rs. 1,38,135 being the depreciation claimed by the assessee on cost of machinery, which was allowed as deduction as capital expenditure on scientific research and development in earlier years was not disallowed though *prima facie* inadmissible. Further, the amount of Rs. 1,54,640 shown as provision for gratuity was not disallowed even though the provision for gratuity was being regularly disallowed in the hands of the assessee in earlier years. Had the provisional assessment been made in accordance with the law, the refund of Rs. 2,87,420 made to the assessee for the assessment year 1977-78 would not have arisen.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been rectified and that the amount of additional tax raised and collected is Rs. 2,87,420.

2.20 *Non-levy of interest/penalty*

(i) Under the provisions of the Income-tax Act, 1961, any person responsible for paying any sum exceeding Rs. 5,000 to any resident contractor for carrying out any work including supply of labour in pursuance of a contract between the contractor and the company shall at the time of credit of such sum to the account of the contractor or at the time of payment thereof, whichever is earlier, deduct an amount equal to 2 per cent of such sum as income-tax. Failure to deduct the tax shall make the company liable to interest at 12 per cent per annum on the amount of such tax from the date on which such tax was deductible to the date on which such tax is actually paid. The company is also liable, in such a case, to pay such amount of penalty as the Income-tax Officer may direct but not exceeding the amount of tax in arrears.

A company which made a total payment of Rs. 2,15,95,733 to its resident contractors during the previous years relevant to the assessment years 1973-74 to 1975-76 did not deduct tax of Rs. 4,31,915 from such payments. Failure to do so rendered the company liable to penal interest and penalty aggregating Rs. 3,02,009. The mistake was pointed out by Audit in April 1978 and remedial action was taken in May 1979.

While accepting the objection the Ministry of Finance have stated that the interest of Rs. 2,58,819 has been levied and penalty of Rs. 43,190 imposed.

(ii) Under the provisions of the Income-tax Act, 1961, where the amount specified in a notice of demand is not paid within thirty-five days of the service of the notice, the assessee is liable to pay interest at the prescribed rates from the day commencing after the end of the said period of thirty-five days till the date of payment of tax. Further, the said interest is required to be calculated at the end of each financial year if the amount of tax or other sum in respect of which such interest is payable has not been paid in full before the end of any such financial year.

An assessee-company did not pay the income-tax demanded from it for the assessment year 1970-71 within the specified period of thirty-five days. As the assessee was in default, interest to the extent of Rs. 5,92,660 for belated/non-payment of tax was chargeable for the period ending 31st December, 1979 which the department did not levy. The mistake was pointed out by Audit in January 1980.

The paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

Other topics of interest

2.21 *Non-completion of re-opened or cancelled assessments*

Under the provisions of the Income-tax Act, 1961, for and upto the assessment year 1970-71, no time limit for making fresh assessment under Section 146 of the Act or in pursuance of an order in appeal or revision, setting aside or cancelling an assessment, was prescribed.

The assessments of a company for the assessment years 1963-64, 1964-65, 1966-67 and 1969-70 were completed on 6th March, 1968, 26th March, 1969, 10th March, 1971 and 6th March, 1972 as best judgment assessments on total incomes of Rs. 13,21,016, Rs. 50,000, Rs. 18,52,338 and Rs. 3,49,415 raising demands of Rs. 7,67,758, Rs. 25,300, Rs. 15,23,997 and Rs. 2,70,660 respectively. The assessments for the assessment years 1965-66, 1967-68, 1968-69 and 1970-71 were completed as regular assessments on 12th March, 1970, 24th February, 1972, 24th February, 1972 and 19th September, 1973 on total incomes of Rs. 23,10,840, Rs. 16,02,252, Rs. 11,36,478 and Rs. 84,970 raising demands of Rs. 17,21,000, Rs. 10,41,460, Rs. 7,38,712 and Rs. 71,863 respectively. The assessments for all these years were either re-opened or set aside during the period January 1969 to March 1975. It was seen in audit in January 1980 that fresh assessments had not been made in any of these cases. As a result, income of the assessee for

the assessment years 1963-64 to 1970-71 had remained unassessed and total demand of nearly Rs. 61.61 lakhs raised against the assessee for different years had remained unrealised for periods ranging from 5 to 11 years, reckoned from the dates of original assessments. The assessee had not paid any tax on regular assessments ever since the first year of its accounts ended 31st May, 1962 relevant to the assessment year 1963-64.

The paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

2.22 *Set off of horse race losses*

Under the provisions of the Income-tax Act, 1961, as it existed for the assessment year 1974-75, any loss arising from races, including horse races, assessable under the head "income from other sources" could be set off against income, if any, from the same source but not against income from any other source or against income under any other head.

In the case of a private limited company, the original assessment for the assessment year 1974-75 was completed in January 1975 in which a loss of Rs. 17,126 from horse racing was not allowed to be set off against business income. The assessment was later rectified in June 1976 to give effect to the order of the Appellate Assistant Commissioner, who permitted loss of Rs. 77,521 from horse racing not only of the previous year relevant to the assessment year 1974-75 but also of earlier previous years to be fully set off against the assessee's business income of Rs. 77,521, thereby reducing its total income to nil. on further appeal by the department, the Appellate Tribunal, in its order of January 1978, reversed the decision of the Appellate Assistant Commissioner and restored the order of the Income-tax Officer denying set off of losses from horse racing against business income. No action to give effect to the Tribunal's order was, however, initiated by the department for

over 1½ years until it was pointed out by Audit in October 1979. The collection of a sum of Rs. 52,908 recoverable as a result of the Tribunal's order was delayed.

The Ministry of Finance have accepted the objection.

2.23 *Non-production of records to Revenue Audit for scrutiny*

The programme of local audit of Income-tax offices is drawn up sufficiently in advance and, at least one month before the local audit, intimation is given to the department with a view to enabling them to keep the relevant records ready for audit scrutiny. According to the Board's instructions of October 1968, reiterated in April 1970, the records requisitioned for local audit should be made available by the Income-tax offices on the day the audit commences and, if any particular record is not available, the reasons should be specifically stated in a note and the records should on no account be withheld by the Income-tax Officers on flimsy grounds. The position about non-production of records for scrutiny by audit during 1973-74 was commented upon in paragraph 46 of the Audit Report 1973-74. The Central Board of Direct Taxes issued further instructions in the matter in May 1975, June 1977 and March 1979.

A review of the position regarding the production of documents to Audit in 1979-80 in seven Commissioners' charges in Tamil Nadu, however, indicated that the position had not improved. Even after making allowance for cases where the records could not be made available to Audit due to their being held up with appellate authorities or having been transferred to other assessing authorities consequent on change of jurisdiction, the number of assessment cases not produced in 146 income-tax wards in 1979-80 was as high as 2,064 as indicated below :—

Not produced during current audit in 1979-80	1,128
Not produced during last audit in 1978-79 and the current audit in 1979-80	870
Not produced during last two audits or earlier and the current audit in 1979-80	66
TOTAL : . . .	2,064

The reasons for non-production were generally stated to be (i) the records were not readily traceable in the income-tax wards, or (ii) the records were being scrutinised by the Internal Audit Wing of the department. As the programme of audit was communicated sufficiently in advance, the department could keep all the files ready for scrutiny by Audit. Such delays in production of records for audit would frustrate audit scrutiny by shutting out any possible rectification/revision with the expiry of the prescribed period of limitation for such action.

The non-production of the files in each ward had been brought to the notice of the department through the local audit reports of the respective wards.

The Ministry of Finance have stated that the records could not be supplied for various reasons and that the Commissioners of Income-tax had assured that there was no intention to withhold records from Audit.

SURTAX

2.24 *Surtax*

To act as 'a disincentive to excessive profits' and 'to help to keep down the prices', a special tax called super profits tax was imposed on companies making excessive profits during the assessment year 1963-64 under the Super Profits Tax Act, 1963. This tax was replaced, from the assessment year 1964-65, by surtax levied under the Companies (Profits) Surtax Act, 1964. Surtax is levied on the 'chargeable profits' of a company in so far as they exceed the statutory deduction, which is an amount equal to 10 per cent (15 per cent from 1st April, 1977) of the capital of the company or Rs. 2 lakhs, whichever is greater.

During the period under review, under-assessment of super profits tax/surtax of Rs. 46.72 lakhs was noticed in 132 cases. A few illustrative cases are given in the following paragraphs.

2.25 *Incorrect computation of chargeable profits*

Under the provisions of the Companies (Profits) Surtax Act, 1964, surtax is leviable on the amount by which the chargeable profits of a company exceed the statutory deduction, which is an amount equal to 10 per cent (15 per cent from 1st April, 1977) of the capital of the company or Rs. 2 lakhs, whichever is greater. The chargeable profits of any year for this purpose are computed with reference to the total income assessed for levy of income-tax for that year after making certain prescribed adjustments. One such adjustment is that any interest payable by the company in respect of amounts, if any, borrowed on long-term basis, from certain notified financial institutions is to be added back to the total income.

(i) During the previous year relevant to the assessment year 1975-76, an assessee-company had borrowed money, on long-term basis, from two notified financial institutions and incurred an expenditure of Rs. 1,78,168 towards interest thereon. The interest payment was duly allowed as deduction in computing the total income of the company for that year for charging income-tax. Further, in computing the capital base for the same year for the purposes of surtax levy, the department had rightly included the aforesaid long-term borrowal and allowed the statutory deduction on that basis. But, in determining the chargeable profits (September 1978) as Rs. 1,63,820, the department omitted to adjust the total income assessed for income-tax purposes, as statutorily required, by adding back the interest payment of Rs. 1,78,168. The omission resulted in under-assessment of the chargeable profits by an equal amount and short levy of surtax of Rs. 57,740.

The Ministry of Finance have accepted the objection.

(ii) In the case of another company, while computing its chargeable profits for the levy of surtax for the assessment year 1975-76 the income-tax payable was taken as Rs. 91,97,480 and was allowed as a deduction, ignoring a refund of Rs. 3,64,030 which had been made to the assessee for that assessment year.

Thus, income-tax payable amounted to Rs. 88,33,450 only. Failure to adopt the correct amount of tax payable by the assessee resulted in under-assessment of chargeable profits to the extent of Rs. 3,64,030 leading to a short levy of surtax of Rs. 1,45,612.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been revised and that the additional tax of Rs. 1,45,612 has been raised and collected.

(iii) In the case of still another assessee-company, while computing its chargeable profits for the levy of surtax for the assessment year 1973-74, it was allowed a deduction of Rs. 4,77,721 on account of management compensation. However, while allowing the deduction towards income-tax payable, the entire income-tax of Rs. 31,03,318 payable on the total income was allowed as deduction without disallowing the income-tax of Rs. 2,75,886 payable on Rs. 4,77,721 on account of management compensation excluded from income. This resulted in under-assessment of chargeable profits to the extent of Rs. 2,75,886 leading to a short levy of surtax of Rs. 82,765.

The Ministry of Finance have accepted the objection.

2.26 *Incorrect computation of capital*

Under the provisions of the Companies (Profits) Surtax Act, 1964, any amount standing to the credit of any account in the books of a company, which is of the nature of liability or provision, shall not be regarded as a reserve for the purposes of computation of capital. Where no specific provision is made for payment of dividends and the proposed dividends are to be paid out of the general reserve, the general reserve is to be reduced by such proposed dividends, since to that extent it is not a free reserve. Further, in terms of the instructions issued by the Central Board of Direct Taxes in November 1974 'debenture sinking fund' or 'debenture redemption reserve' is only a 'provision' and not a 'reserve' and as such, it is not to be included in computing the capital.

(i) In computing the capital of an assessee-company for the purpose of levy of surtax for the assessment year 1975-76, it was noticed that debenture stock redemption reserve and dividends proposed to be paid out of general reserve amounting to Rs. 48,32,250 were incorrectly taken into account. This resulted in excess computation of capital and statutory deduction with consequent undercharge of surtax of Rs. 2,29,532 in the assessment year 1975-76.

The Ministry of Finance have accepted the objection.

(ii) In the case of a non-resident tea company, a sum of £ 4,22,311 representing Revenue Reserve/Retained Profits on the first day of the previous year relevant to the assessment year 1975-76 was included by the department in the capital of the company. The sum was merely surplus of the profit and loss account and was, therefore, required to be excluded from computation of the capital. Inclusion of the aforesaid sum led to excess computation of capital and statutory deduction with consequent undercharge of surtax of Rs. 1,40,826 in the assessment year 1975-76.

In the case of another non-resident tea company, a reserve of £ 9,05,192 was included in the capital although in the accounts of the company for the previous year relevant to the assessment year 1975-76 the sum was shown as £ 5,82,370. From the details furnished by the company it was noticed that the sum of £ 3,22,822 representing the difference between the reserve taken by the department and the reserve shown in the accounts was the net effect of losses adjusted against the reserve of £ 9,05,192. Inclusion of £ 9,05,192 instead of the adjusted net reserve of £ 5,82,370 in the capital led to excess computation of capital and statutory deduction with consequent undercharge of surtax of Rs. 1,15,149 in the assessment year 1975-76.

The paragraph was sent to the Ministry of Finance in September 1980 ; their reply is awaited (December 1980).

(iii) In the case of still another company, while computing the capital the department incorrectly included in the assessment years 1975-76 to 1978-79, the surplus balance of the profit and loss accounts. This led to excess computation of capital of Rs. 61,43,754 in the four assessment years with resultant undercharge of surtax of Rs. 1,08,248.

The Ministry of Finance have accepted the objection.

2.27 *Omission to make provisional surtax assessment*

The Companies (Profits) Surtax Act, 1964, provides that, pending a regular assessment, the department can make a provisional assessment, in a summary manner, of the chargeable profits of a company and raise a demand for surtax. The provision is designed to realise Government revenue as early as possible.

For the assessment year 1976-77, a company in which the public were substantially interested, filed a surtax return in September 1976, admitting chargeable profit of Rs. 7,14,302 and surtax liability of Rs. 1,78,625. On the basis of the return, the department could have raised a provisional demand of surtax but it did not do so. Consequently, surtax admittedly due from the assessee remained unrealised for over three years, without the assessee being liable to pay any interest for non-payment thereof. This was pointed out in audit in December 1979.

While accepting the objection the Ministry of Finance have stated that the surtax assessment in question has been completed on 9-1-1980 and that the amount of additional demand raised/revised in appeal and collected is Rs. 1,60,051.

2.28 *Omission/delay in revising surtax assessments*

Pursuant to the recommendations of the Public Accounts Committee contained in paragraph 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 the income-tax proceedings and

finalised within a month of the completion of the relevant 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 income-tax assessments were disputed in appeal.

(i) The taxable income of an assessee-company for the assessment year 1974-75 was determined as Rs. 35,42,351 in June 1978. As the chargeable profits, Rs. 12,62,660, exceeded the statutory deduction of Rs. 2 lakhs, the company was assessable to surtax on the net chargeable profits of Rs. 8,33,016. However, the assessee did not furnish any return of chargeable profits, nor did the assessing officer initiate necessary proceedings to levy surtax. The Register of Pending Action maintained by the assessing officer also did not show any pendency in this respect. The chargeable profits of the company, therefore, escaped assessment to surtax which would amount to Rs. 2,39,000.

The Ministry of Finance have accepted the objection in principle.

(ii) In another case, the taxable income of an assessee-company for the assessment year 1973-74 was determined at Rs. 35,43,460 in the revised assessment finalised on 22nd January, 1979. As the chargeable profits of Rs. 18,21,672 exceeded the statutory deduction of 10 per cent of the capital, the company was assessable to surtax on the net chargeable profits of Rs. 4,67,800. However, neither the assessee filed the return of chargeable profits, nor did the assessing officer initiate necessary proceedings for levy of surtax. The net chargeable profits of Rs. 4,67,800, therefore, escaped taxation with consequent non-levy of surtax of Rs. 1,19,170.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been made and that the amount of additional tax raised and collected is Rs. 1,19,170.

(iii) In a third case, it was noticed in audit in December 1979 that even though the income-tax assessments of an assessee-

company, for the assessment years 1973-74, 1974-75 and 1975-76 had been completed on 7-6-1977, 26-4-1978 and 23-9-1978 respectively, the surtax assessments initiated on 3-10-1978 for all the three years, had not been finalised (till audit) resulting in demands of Rs. 82,600, Rs. 1,62,400 and Rs. 4,43,000 not being raised for 11, 5 and 15 months respectively.

While accepting the objection the Ministry of Finance have stated that the surtax assessments for all the three years have been completed in September 1980, raising a demand of Rs. 4,14,858.

(iv) The provisional assessment of surtax of a company for the assessment year 1975-76 was made in February 1976 levying a tax of Rs. 6,35,863. The income-tax assessment for the year was completed in September 1978 with taxable income of Rs. 1,34,39,660 and tax payable thereon as Rs. 77,60,578. Ten per cent of the capital being Rs. 27,25,846, surtax of Rs. 9,72,282 was leviable on the chargeable profits of Rs. 29,41,801. It was noticed in audit that the surtax assessment was not revised on the basis of the income-tax assessment. Omission to revise the surtax assessment resulted in short levy of surtax of Rs. 3,36,419.

The Ministry of Finance have accepted the objection in principle.

(v) In another case of an assessee-company, the income-tax assessments for the assessment years 1971-72 to 1974-75 were completed in 1978 on the basis of which the chargeable profits of the company exceeded the statutory deduction by an aggregate sum of Rs. 5,99,170, during these four years. However, the assessee did not furnish any return of chargeable profits nor did the assessing officer initiate necessary proceedings to levy the surtax. The chargeable profits of the company, therefore, escaped assessment leading to undercharge of surtax of Rs. 1,72,077 in the four assessment years.

The Ministry of Finance have accepted the objection in principle.

(vi) In the case of an assessee-company provisional surtax assessments for the assessment years 1975-76 and 1976-77 were made by the department in October 1976 and December 1976 wherein surtax demands of Rs. 3,33,425 and Rs. 6,85,927 respectively were raised. Regular income-tax assessments for the said assessment years were completed in March 1978 and January 1979 repectively on the basis of which surtax of Rs. 4,51,990 and Rs. 7,40,485 respectively would be leviable. No action was, however, taken by the department to revise the provisional surtax assessments or to make regular surtax assessments as required under the Board's instructions. The omission in this regard led to short levy of surtax of Rs. 1,73,123 in the assessment years 1975-76 and 1976-77.

The Ministry of Finance have accepted the objection in principle.

(vii) The provisional surtax assessment of a company for the assessment year 1975-76 was completed in February 1976 levying surtax of Rs. 4,91,321. The income-tax assessment for the year was completed in September 1978 with total income of Rs. 2,79,26,820 and tax levied thereon was Rs. 1,61,27,739. In the provisional assessment for surtax, no adjustment on account of dividends paid out of the general reserve was made in computing the capital. Further, as a result of certain adjustments in the income-tax assessment there was an increase in the chargeable profits for the year. As the surtax assessment of the year was not finalised on the completion of the income-tax assessment, there was a short levy of surtax of Rs. 1,17,327, the surtax on final assessment being leviable at Rs. 6,08,648.

The Ministry of Finance have accepted the objection in principle.

(viii) The income-tax assessment of an assessee-company for the assessment year 1975-76 was finalised in September 1978 assessing the income at Rs. 29,62,800. However, the surtax

assessment proceedings were not initiated simultaneously though the surtax return had been filed on 3rd July, 1975. In January 1979 only a provisional assessment of surtax was made on the basis of the return filed by the assessee, without taking into consideration the income as already assessed. There was a mistake in calculation of tax in provisional assessment which resulted in undercharge of surtax by Rs. 58,530. Further, as only provisional assessment was made in January 1979 on the basis of the return filed by the assessee without considering the higher amount of income assessed in the income-tax proceedings, there would be delay in raising and collection of additional surtax of Rs. 94,272 till the regular assessment is finalised.

The Ministry of Finance have accepted the objection ; the amount of additional tax raised is Rs. 58,530.

(ix) In the case of a company, the regular assessment under the Income-tax Act, 1961 for the assessment year 1973-74 was made in August 1974 on a total income of Rs. 1,51,42,738. The income-tax assessment was revised in December 1974 reducing the income to Rs. 1,51,28,243 and again in March 1976, further reducing the income to Rs. 1,49,41,037. In July 1976, however, the income-tax assessment was revised for the third time enhancing the assessed income to Rs. 1,56,51,810 on account of certain income from technical services, erroneously claimed and treated as exempt in the earlier assessments, being brought to tax. As against four income-tax assessments, only two surtax assessments for the corresponding periods were made in November 1974 and June 1975 with reference to the total incomes of Rs. 1,51,42,738 determined in August 1974 and Rs. 1,51,28,243 determined in December 1974. As per the last surtax assessment made in June 1975, a demand of Rs. 7,63,252 was raised. However, this assessment was not revised thereafter, particularly when the income-tax assessment underwent the third revision in July 1976 when the income was enhanced to Rs. 1,56,51,810. Had a surtax assessment been made on that basis, the surtax due would have been determined as Rs. 8,29,616. Non-revision of the surtax assessment resulted in under-assessment of surtax of Rs. 66,064 in the assessment year 1973-74.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been revised and that the amount of additional demand raised and collected is Rs. 66,064.

2.29 *Short levy of surtax due to incorrect application of rates*

Under the provisions of the Companies (Profits) Surtax Act, 1964, as amended with effect from 1-4-1975, surtax is chargeable at 25 per cent of so much of the excess of chargeable profits over the statutory deduction, as does not exceed 5 per cent of the amount of capital and at 40 per cent of the balance amount, if any.

The chargeable profits of an assessee-company for the assessment year 1975-76 were determined by the department in January 1979 as Rs. 11,27,435 on which surtax of Rs. 2,91,333 was levied. It was noticed in audit that the department had erroneously adopted the rate of 30 per cent of the chargeable profits in excess of 5 per cent of the capital, as against the correct rate of 40 per cent.

When the mistake involving short levy of surtax of Rs. 84,185 was pointed out in audit in July 1979, the department did not dispute the short levy but contended that they were aware of the mistake, the assessee itself having brought it to their notice in February 1979. It was claimed that the rectificatory action was not taken in view of the possibility of the surtax assessment requiring further revision as a result of appellate decision awaited in respect of the relevant income-tax order. The contention of the department was not valid. According to the executive instructions issued in September 1968, apparent errors in completed assessments coming to the notice of the department should be rectified within 3 months. These instructions were not observed in the instant case. The possibility of revision of the income-tax assessment order on a later date as a result of appellate orders should not stand in the way of rectifying the error in the surtax order pointed out by the assessee itself. Another plea of the department was that the relevant files were with other authorities

and hence the rectification could not be carried out before audit detected the error. This plea was also not found to be valid, as in fact, a revision of the income-tax assessment order was made in June 1979 to give effect to an appellate decision.

The Ministry of Finance have accepted the objection.

CHAPTER 3

INCOME TAX

3.01 Income-tax collected from persons other than companies is booked under the Major Head "021-Taxes on income other than Corporation Tax". Under Article 270 of the Constitution, 85 per cent of the net proceeds of this tax, except in so far as these are attributable to Union emoluments, Union Territories and Union Surcharges, is assigned to the States in accordance with the recommendations of the Seventh Finance Commission.

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

3.03 *Avoidable mistakes in computation of tax*

(i) The total income of an assessee-firm for the assessment year 1973-74 was computed in August 1978 at Rs. 5,65,853 after setting off unabsorbed depreciation and development rebate of earlier years including unabsorbed depreciation of Rs. 6,97,219 for the assessment year 1970-71 as determined in March 1977. It was, however, noticed that the assessment for the assessment year 1970-71 had been revised in July 1978 wherein unabsorbed depreciation had been reduced to Rs. 3,72,911. As in the assessment for the assessment year 1973-74 completed in August 1978 the department set off a sum of Rs. 6,97,219 as against the correct amount of Rs. 3,72,911, there was excess set off of unabsorbed depreciation by Rs. 3,24,308 in the assessment year 1973-74 resulting in under-assessment of income by the same amount with consequent tax undercharge of Rs. 1,22,353 including penal interest for late submission of return and short payment of advance tax on estimate.

The Ministry of Finance have accepted the objection in principle.

(ii) An assessee remitted a sum of Rs. 65,186 on 28-2-1977, being self-assessment tax relating to the assessment year 1975-76 for which the credit was correctly given for that year. But in computing the net demand for the assessment year 1976-77 the credit of the same amount was given again resulting in double adjustment of the same credit. This resulted in a short demand of Rs. 78,226 including interest for the assessment year 1976-77.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been revised and an additional demand of Rs. 78,226 raised.

(iii) While assessing the income of an assessee-firm for the assessment years 1973-74 to 1975-76 the Income-tax Officer held that the entire income of the firm was to be treated as the income of a Hindu undivided family which was one of the partners of the firm having 40 per cent share. Accordingly, the entire income was included in the income-tax assessments of the Hindu undivided family for the respective years. However, while working out the tax payable by the family in respect of the income assessed for the assessment year 1974-75, the income of the firm included in the assessee's income was considered for determining the rate of tax but no tax was levied on that income. This resulted in undercharge of tax of Rs. 1,45,713 apart from interest charges amounting to Rs. 90,742.

The Ministry of Finance have accepted the objection in principle.

or set apart and the period, not exceeding ten years, for which it is to be accumulated or set apart, and the money so accumulated or set apart is invested in specified securities within the time prescribed. The Act further provides that, if the accumulated income is not utilised for the purpose for which it was accumulated within the notified period, not exceeding ten years, the entire accumulated income shall be deemed to be the income of the trust of the previous year immediately following the expiry of the notified period. These provisions apply also to societies and companies formed without a profit motive, for charitable purposes.

(i) An assessee-company claiming to be a charitable institution gave notice on 30-3-1966 of its intention to accumulate for a period of ten years from the previous year relevant to the assessment year 1966-67 its income from property held under trust for the purpose of construction of a building and to carry out other welfare activities. The limitation period of ten years expired on 31-3-1975. It was noticed that the accumulated income of Rs. 2,56,894 had not been spent for the specified purpose of construction of building before that date. As such, the entire accumulated income of Rs. 2,56,894 should have been taxed in the assessment year 1976-77. Instead, the department taxed only the income of Rs. 23,000 pertaining to the first year i.e. asessment year 1966-67, in the assesment year 1976-77. This resulted in under-assessment of income by Rs. 2,33,894 and a short levy of tax of Rs. 1,35,070.

The Ministry of Finance have accepted the objection.

(ii) The Act further provides that voluntary contributions received by a trust created wholly for charitable purposes shall be deemed to be income except where such contributions are made with a specific direction that they shall form part of the corpus of the trust or institution.

A charitable institution received a sum of Rs. 1,33,447 as voluntary contribution with the direction that it be spent for the construtions of a girls hostel, assembly hall, library etc. There was no specific direction from the donors that the said sums

shall form part of the corpus of the institution. As the income was not also applied for charitable purposes but was accumulated, it was taxable under the law. The department, however, exempted the same, treating the income as forming part of the corpus. The erroneous exemption resulted in under-assessment of income by Rs. 1,33,447 for the assessment year 1976-77 with consequent short levy of tax of Rs. 79,313.

Final reply of the Ministry of Finance is awaitd (December 1980).

3.05 *Incorrect status adopted in assessments*

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 every person. The term "Person" for this purpose includes an "association of persons". An association of persons is assesable as such in respct of any income earned by it without any allocation for assessment in the hands of its members unless otherwise specified in the Act.

(i) An assessee was assessed in the status of an association of persons for the purposes of income-tax for the assessment year 1973-74. The income of the association of persons included a sum of Rs. 21,14,920 on account of capital gains derived from the sale of certain immovable properties. This sum was not taxed in the hands of the assessee but was allocated for assessment in the hands of its co-owners. This resulted in under-assessment of income from capital gains to the extent of Rs. 13,71,450 in the hands of the association of persons for the assessment year 1973-74 (after allowing for statutory deductions) leading to a short levy of tax of Rs. 12,96,890.

The paragraph was sent to the Ministry of Finance in August 1980; their reply is awaited (December 1980).

(ii) An assessee, having separate individual income, invested the amount of a gift received by him in his individual capacity in a firm and returned the income of Rs. 82,870 therefrom

for the assesment year 1974-75 in the status of a Hindu undivided family of which he was a member. The department accepted the separate status for that income and assessed the same accordingly.

The separate status claimed and accepted for the income was, however, not correct as the gift was to the individual and income arising therefrom could not be treated as that of the Hindu undivided family; it was includible in the other individual income of the assessee for the purpose of taxation. The adoption of incorrect status for the income arising from the investment of the gift resulted in short levy of tax and interest of Rs. 50,569.

The Ministry of Finance have accepted the objection.

3.06 *Incorrect computation of salary income*

According to the provisions of the Income-tax Act, 1961, any salary paid or due or allowed in the previous year, is taxed in the assessment year, relevant to the previous year in which it was paid or was due, or was allowed by the employers. The expression 'salary' for the purpose includes commission also.

A company, instead of paying a sum of Rs. 45,000 in cash as commission to one of its employees in each of the two assessment years 1974-75 and 1975-76, took two deferred annuity policies for like amounts on the life of the assessee employee. The total amount of Rs. 90,000 applied for the purchase of deferred annuities was not treated as income from salary and charged to tax in the assessment years 1974-75 and 1975-76, resulting in total under-assessment of salary income of Rs. 90,000 with consequent short levy of tax of Rs. 76,050.

The Ministry of Finance have stated that the case involves a controversial legal issue which is not yet settled by the Supreme Court.

3.07 *Incorrect computation of business income*

(i) Under the provisions of the Income-tax Act, 1961, any expenditure, not being in the nature of capital expenditure or personal expenses of the assessee, laid out or expended wholly and exclusively for the purpose of the business or profession is allowable as a deduction in computing the income of the assessee from business or profession. It has been judicially held that if an assessee carries on several distinct businesses, the profits of each business must be computed separately and allowances must be confined to the appropriate business.

In the case of an assessee, having two sources of income *viz.* (i) income from insurance commission and (ii) income/loss from chit fund business, the loss amounting to Rs. 1,25,529 shown in the return was allowed to be set off against the income from insurance commission. The profit and loss account relating to the chit fund business, however, disclosed that the excess of income over expenditure was to the tune of Rs. 1,25,529. Failure to treat this amount as profit instead of loss, resulted in a total under-assessment of tax of Rs. 1,41,688 inclusive of interest under sections 139(8) and 217(1) of the Income-tax Act, 1961 for the assessment year 1975-76.

The Ministry of Finance have stated that in order to ascertain the correct position thorough scrutiny of accounts by the Income-tax Officer is necessary and that the assessment has been set aside for making a fresh assessment after proper scrutiny of the accounts.

(ii) The Act further provides that income chargeable under the head "Profits and gains of business or profession" shall be computed in accordance with the method of accounting regularly employed by the assessee.

An assessee-firm engaged in contract works maintained accounts on mercantile basis. During the previous year relevant to the assessment year 1977-78, the firm received a sum of

Rs. 17,29,392 for execution of works after deduction of Rs. 2,16,791 from the bills towards security deposit. This net amount of Rs. 17,29,392 was accounted for as receipt in the trading and profit and loss accounts, instead of the gross amount of Rs. 19,46,183 as per the method of accounting adopted by the assessee. This resulted in short accountal of receipts by Rs. 2,16,791. Similarly, in the previous year relevant to the assessment year 1978-79, security deposit of Rs. 1,19,018 withheld from bills was not accounted for in the profit and loss accounts.

Omission to include the amounts withheld as security deposits in the total income resulted in under-assessment of income by Rs. 3,35,809 and short levy of tax of Rs. 90,174 in the two assessment years, 1977-78 and 1978-79, in the hands of the firm alone.

The Ministry of Finance have stated that the assessment has been set aside and that the Income-tax Officer has been asked to examine the matter.

(iii) Under the provisions of the Income-tax Act, 1961, any payment of interest, salary, bonus, commission or remuneration made by a firm to any partner of the firm is not an allowable deduction in computing the income of the firm under the head "Profits and gains of business or profession". It has been judicially held that the expression 'commission' has no technical meaning but both in legal and commercial acceptance of the term, it has definite signification and is understood to be an allowance for service or labour in discharging certain duties such as those of an agent, factor, broker or any other person who manages the affairs or undertakes to do some work or renders some service to another. Mostly it is a percentage on price or value or upon the quantum of work involved in a transaction. It can be for a variety of services and is of the nature of recompense or reward for such services.

An individual as sole proprietor of a business concern, entered into an agreement in May 1969 to act as sole selling agent

on commission of a registered firm in which he was a partner. Later, in February, 1972, on a fresh agreement with the firm, the partner became entitled to receive service charges on sales of a product at different slabs varying with the quantum of sales and commission on sales of three other products of the firm. As the service charges paid by the firm to the partner were of the nature of commission, they were required to be disallowed in computing the business income of the firm. In the assessments for the years 1976-77 to 1978-79, allowance of commission and service charges amounting to Rs. 4,68,212 in the computation of business income of the firm resulted in undercharge of tax of Rs. 1,25,677.

The Ministry of Finance have accepted the objection.

(iv) The Act further provides that the amount of any debt, which is established to have become a bad debt in the previous year, may be allowed as a deduction in computing the business income.

It was noticed that in the accounts of an assessee-firm for the previous year relevant to the assessment year 1975-76, a sum of Rs. 2,86,549 was shown as written off on account of bad debts. In the assessment completed on 12-9-1978 the assessing officer came to the finding that the claim for the deduction of Rs. 2,86,549 was not allowable. In actual computation, however, the deduction was not disallowed and added back to the total income. Omission to do so resulted in under-assessment of income of Rs. 2,86,549 with tax undercharge of Rs. 1,25,583 together with short levy of interest for late submission of return of income and short payment of advance tax on its estimates.

The Ministry of Finance have accepted the objection regarding under-assessment of income of Rs. 2,86,549.

(v) Under the instructions issued by the Central Board of Direct Taxes in December 1974, the cost of acquiring distribution rights of a film may be allowed amortisation on the basis

of collections during the period of exploitation of the film. As the period of exploitation is likely to exceed one year, the assessment for the first year may be framed provisionally by allowing a part of the cost of distribution rights on an estimated basis against the actual receipts in the year under consideration. The final adjustment is made after the exploitation period.

An assessee-firm engaged in distribution of films purchased distribution right of a certain film for Rs. 4,28,549 during the previous year relevant to the assessment year 1976-77. The amount of Rs. 2,52,512 was allowed to be amortised in the assessment year 1976-77. Against the balance amount of Rs. 1,77,047 an amount of Rs. 2,77,047 was allowed to be amortised in the assessment year 1977-78. This resulted in excess allowance of Rupees one lakh and excess computation of loss to this extent in the assessment year 1977-78.

The Ministry of Finance have accepted the objection.

3.08 *Irregularities in allowing depreciation.*

The Income-tax Act, 1961, provides for grant of depreciation on buildings, plant and machinery owned by the assessee and used for the purpose of business in computing the income from business. The Rules prescribed in this regard, provide for specified rates of depreciation for certain items of plant and machinery and a general rate of 10 per cent for the remaining items of plant and machinery, on the actual cost or the written down value of the assets, as the case may be.

During the assessment year 1973-74 an assessee-firm dealing in transport business purchased 20 new trucks at a cost of Rs. 13,85,860. While completing the assessment the department allowed depreciation thereon for an amount of Rs. 2,07,880 only calculated at 15 per cent of the cost instead of at the admissible rate of 30 per cent. The assessment was subsequently revised in May 1976, and a further depreciation of Rs. 2,07,880 as admissible was allowed. A total depreciation of Rs. 4,15,760 having thus been allowed on trucks in the assessment year 1973-74, the correct written down value of the asset to be carried forward to the next assessment year worked out to Rs. 9,70,100. The department, however, while

completing the assessments for the subsequent assessment years allowed depreciation on the basis of the written down value of Rs. 11,77,980 as initially determined after allowing depreciation of Rs. 2,07,880. The adoption of the incorrect written down value resulted in excess allowance of depreciation to the extent of Rs. 81,946 in the assessment years 1974-75 to 1976-77 with consequent tax undercharge of Rs. 68,858 including penal interest for late submission of return and short payment of advance tax on estimate.

The Ministry of Finance have accepted the objection in principle.

3.09 *Irregular exemptions*

(i) Under the provisions of the Income-tax Act, 1961, interest on 12-year National Defence Certificates to the extent to which the amounts of such certificates do not exceed the maximum amount which is permitted to be deposited therein, viz. Rs. 50,000, is not to be included in computing the total income.

In the case of an unrecognised "Pension and Gratuity Fund" assessed in the status of an "association of persons", it was seen in audit that interest on 12-Year National Defence Certificates of the face value of Rs. 39 lakhs was exempted from tax for the assessment years 1971-72, 1972-73 and 1973-74. Omission to tax the interest on the unexmpted portion of the investment of Rs. 38.5 lakhs involving under-assessment of tax of Rs. 6,90,000 for the three years was pointed out by Audit in June 1975.

While accepting the objection the Ministry of Finance have stated that the assessment for the assessment year 1973-74 has been revised raising an additional demand of Rs. 2,32,643. The remedial action for the assessment years 1971-72 and 1972-73 got barred by limitation after receipt of the audit objection.

(ii) Under the provisions of the Income-tax Act, 1961, income-tax liability of the employee discharged by the employer is a perquisite to be treated as salary and it has to be taxed in

the hands of the recipient on "tax on tax" basis. But in the case of technicians who fulfil certain conditions laid down under the Act and whose contracts of service have been approved by the Central Government, the salary received by them to the extent of Rupees four thousands per month and the tax borne by the employer are exempt from tax.

In the case of a foreign technician for the assessment years 1977-78 and 1978-79, it was seen that though his contract of service had not been approved by the Central Government and the salary received by him was also not claimed as exempt from tax, the tax borne by the employer was not taken as perquisite and brought to tax. This resulted in short demand of tax of Rs. 1,14,762 for the above two years.

Final reply of the Ministry of Finance is awaited (December 1980).

3.10 *Irregular computation of capital gains*

Any profits or gains arising from the transfer of a capital asset is chargeable to income-tax under the head "capital gains".

(i) The term "capital asset" includes jewellery including ornaments, silver, utensils etc.

An assessee sold silver articles costing Rs. 3,18,601 for Rs. 6,89,827 in the previous year relevant to the assessment year 1975-76. The sale resulted in a taxable capital gain of Rs. 2,19,736 after allowing for deductions provided in the law. This amount of capital gain was neither returned by the assessee nor assessed to tax by the department. The omission to do so led to non-levy of capital gains tax of Rs. 1.64 lakhs.

The paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

(ii) Under the provisions of the Income-tax Act, 1961, where a capital gain arises from the transfer of a capital asset being land which, in the two years immediately preceding the

date on which the transfer took place, was being used by the assessee or a parent of his for agricultural purposes, and the assessee has, within a period of two years after that date, purchased any other land for being used for agricultural purposes, then the net excess of capital gains over the cost of the new agricultural land alone is chargeable to tax as 'income' of the previous year in which the transfer took place. The Central Board of Direct Taxes while explaining the scope of a similar provision regarding exemption of capital gains on the sale of a house property, had clarified that the concession is applicable only to individuals and not to Hindu undivided families.

In the case of two Hindu undivided families, a portion of the capital gains that arose on the sale of agricultural lands in the assessment year 1974-75, amounting to Rs. 66,041 each was allowed exemption on the ground that they had purchased agricultural land jointly with three other Hindu undivided families within the prescribed time. As the concession was not admissible to Hindu undivided families, there was an under-assessment of income of Rs. 66,041 in each of the two cases and an aggregate short levy of tax of Rs. 1,29,108 for the assessment year 1974-75.

The Ministry of Finance have stated that the very fact that the Board had to issue clarificatory instructions indicates that the matter was not free from doubt. The fact, however, remains that the assessment was not revised by the department for more than 1½ years after the issue of the Board's instructions till the assessment became barred by limitation and resulted in loss of revenue.

3.11 *Mistakes in assessment of firms and partners.*

Under the Income-tax Act, 1961, firms are classified into registered firms and unregistered firms. A registered firm pays only a small amount of tax on its income; the rest of its income is apportioned among the partners and included in their individual assessments. An unregistered firm pays full tax on its total income. Where at the time of completion of the assessments of the partners, the assessment of the firm has not been

completed, the share income from the firm is included in the assessments of the partners on a provisional basis and revised later to include the final share income when the assessment of the firm is completed. For this purpose, the Income-tax Officers are required to maintain "Register of cases of provisional share income" so that these cases are not omitted to be rectified. Instances of default in the revision of the partners' assessments in such cases have been commented upon in paragraph 61(i) of Audit Report 1975-76, paragraph 59 of Audit Report 1976-77, paragraph 53(b)(ii) of Audit Report 1977-78 and paragraph 54 of Audit Report 1978-79.

Pursuant to the paragraphs featured in the Audit Reports in the past, the Public Accounts Committee have from time to time expressed concern at the delay in the revision of provisional assessments of partners' share incomes after completion of the firms' assessments and have taken a serious note of the failure to keep a proper watch over such cases. Their recommendations/observations are contained in paragraph 65 of their 21st Report (Third Lok Sabha), paragraph 45 of their 28th Report (Third Lok Sabha), paragraph 2.224 of their 51st Report (Fifth Lok Sabha), and Chapter VIII of their 186th Report (Fifth Lok Sabha). The Central Board of Direct Taxes also issued instructions in the matter in March 1973.

(i) The assessments of a registered firm for the years 1973-74 and 1974-75 were re-opened under Section 147 of the Income-tax Act, 1961, and the re-assessments were finalised on 18-11-1977. However, the assessments in the case of 3 partners of the firm assessed by the same Income-tax Officer were not rectified to include the revised share of income from the firm till October 1979. No note of the pending action had also been kept either in the assessment records of the partners or in the register prescribed by the Board in 1973 for this purpose. This resulted in short levy of tax to the extent of Rs. 40,256 in the hands of these three partners for the assessment years 1973-74 and 1974-75.

(ii) In another case, the assessment of an individual for the assessment year 1968-69 originally completed in March 1972 at Rs. 1,22,460 was set aside in appeal. Fresh assessment was made in March 1976 and finally revised in August 1978 for giving effect to appellate orders. Total income as finally computed in August 1978, amounted to Rs. 85,000 which included his provisional share income of Rs. 16,705 from a firm.

However, the firm's assessment case was not consulted in finalising his assessment in August 1978 nor was a record of the fact that the share income from the firm had been adopted on provisional basis kept in the prescribed register to watch subsequent revision after consulting the firm's completed assessment.

The firm's original assessment for 1968-69 completed in March 1972 had been set aside in March 1975 in appeal and fresh assessment had been finalised in March 1978, according to which the assessee's share income amounted to Rs. 93,694.

Omission to include final share of income from the firm in the assessments of the assessee resulted in undercharge of tax of Rs. 61,661.

(iii) In the case of another registered firm, the share incomes of its four partners were assessed on provisional basis for the assessment years 1972-73 and 1973-74 subject to revision on the completion of assessment of the firm. The assessment of the firm for the assessment year 1972-73 was completed/rectified in March 1975/January 1976 while that for the year 1973-74 was completed in March 1976 but the assessments of the partners on the basis of final share incomes were not revised even after a period of 13 to 25 months from the completion of revised assessments of the firm. It was also noticed that no note for such a revision had been kept by the Income-tax Officer. This resulted in short demand of tax of Rs. 86,823.

(iv) In 40 other cases spread over assessment years 1970-71 to 1974-75, the assessments were completed by taking provisional share incomes from the firms subject to rectification. Though the assessments of the firms had been finalised later, no action was taken to rectify the partners' assessments by adopting their determined shares, even after the lapse of a period of 13 to 48 months of the completion of assessments of the firms. This resulted in under-assessment of tax of Rs. 1,59,619.

The total undrecharge of tax was Rs. 3,48,359.

The Ministry of Finance have accepted the objection in 9 cases ; their reply is awaited in the remaining 39 cases (December 1980).

3.12 *Omission to include income of spouse/minor children*

(i) Under the provisions of the Income-tax Act, 1961, in computing the total income of an individual, there shall be included all such income as arises directly or indirectly to the spouse/minor child of such individual from the membership of the spouse/minor child in a firm carrying on a business in which such individual is a partner. Further, it has been judicially held that even where an individual represents a joint family, the partnership is not between the family and the other partners but between the individual personally and the other partners. In such cases, the Karta may be accountable to the family for the income received but the partnership is exclusively one between the contracting members. It follows that even in such cases the clubbing provisions of the Act are attracted.

In 4 cases in 2 Commissioners' charges spread over the assessment years 1975-76 to 1978-79, such incomes of spouse/minor children were not included in the total incomes of the assessees concerned resulting in undercharge of tax of Rs. 1,06,829.

(ii) The Act further provides that if both the husband and the wife are partners in a firm, the share incomes from the firm of the spouses and of their minor children should be included

in the income of that spouse whose total income excluding such share income is greater.

In 8 cases in 4 Commissioners' charges spread over the assessment years 1973-74 to 1978-79, such incomes of spouse/ minors were not included in the total income of the other spouse whose total income excluding such share income was greater. This resulted in undercharge of tax of Rs. 1,26,251.

(iii) The Act as amended from 1st April, 1976, further provides that the income arising to a minor child of an individual from the admission of the minor to the benefit of partnership is to be included in computing the income of that individual even if such individual is not a partner in the firm.

In 22 cases in 10 Commissioners' charges spread over the assessment years 1973-74 to 1978-79, such incomes of minor children were not included in the total incomes of the assessees concerned. The omission to do so resulted in tax undercharge of Rs. 5,20,140.

(iv) Further, according to an amendment made from 1st April, 1976, in computing the total income of an individual, income arising directly or indirectly to the spouse of such individual by way of salary, commission, fees or other form of remuneration whether in cash or in kind from a concern in which the individual has substantial interest, is to be included in his total income.

In one case in one Commissioner's charge, such income was not so included in the total income of the assessee concerned for the assessment years 1976-77 to 1978-79 resulting in tax undercharge of Rs. 29,280.

The paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

3.13 *Income escaping assessment due to lack of correlation with records of other direct taxes*

The need for a proper co-ordination among the assessment records pertaining to direct taxes to ensure an overall improvement in the administration of these taxes has been frequently emphasized 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 61st Report (Sixth Lok Sabha) of the Public Accounts Committee. Though such cases of lack of correlation have continuously been pointed out in the previous Audit Reports and the Central Board of Direct Taxes have also issued instructions on 15-5-1970, 10-1-1973, 8-5-1973, 24-8-1973, 15-11-1973 and 11-4-1979 for carrying out such correlation, instances of undercharge of tax resulting from omission to utilise information already available in the assessment records of other direct taxes continue to be noticed. A few instances are given below :

(i) Two brothers, representing their respective Hindu undivided families, had equal rights in ten grounds of vacant lands in a city. This was admitted by them for their wealth-tax assessments upto and inclusive of the assessment year 1972-73. But for the assessment year 1973-74, they did not offer the asset for taxation for wealth-tax nor did they indicate any reason therefor. While finalising the wealth-tax assessment for that year, (March 1979), the department did not correlate the returns with those for the earlier year and, consequently failed to notice the omission. When this was pointed out in audit (June 1979), the department stated that, according to one of the assessees, the vacant lands had been sold in February 1970 itself and that, if the lands were found to be non-agricultural, levy of capital gains tax on the transaction would be considered. However, on examination, it was noticed that the assessees had obtained the necessary statutory certificate from the department before the sale deed was registered, and the income-tax assessment records for the assessment year 1971-72 thus contained information regarding the sale of the lands in question. It was further

noticed that the assessees and another brother of theirs (with equal rights) had sold the lands in February 1970 for a total consideration of Rs. 3.75 lakhs. As the lands were non-agricultural (being building plots), the department should have levied capital gains tax on the income of all the three brothers in the assessment year 1971-72. Omission to do so in the case of the two brothers (information whether the third brother was assessed to capital gains tax on this transaction was not readily available) resulted in undercharge of tax of Rs. 70,246.

The Ministry of Finance have accepted the objection.

(ii) A Hindu undivided family filed income-tax return showing income of Rs. 9,085 and was assessed on that amount for the assessment year 1975-76. However, on correlating the case with the wealth-tax records, it was noticed that capital gain in respect of a house sold for Rs. 61,000 had escaped assessment. On the basis of the approved valuer's report, estimating the value of the house on 31-3-1969 at Rs. 21,000 and stating that it was constructed about 60 years ago, the value of the house could be taken at Rs. 10,000 on 1-1-1954 for working out the capital gain. On that basis, capital gain escaping assessment amounted to Rs. 34,500 leading to short levy of tax of Rs. 16,815 and interest (for late filing of return) of Rs. 5,669. In addition, penalties leviable for late filing of return and for concealing particulars of income, amounted to Rs. 8,656 and Rs. 16,815, respectively. The total undercharge of tax, interest and penalties leviable worked out to Rs. 47,954.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been re-opened.

(iii) From the wealth-tax returns of an assessee it was noticed that the increase in wealth in successive years was shown on the basis of income during the relevant years. While the income assessed for income-tax purposes for the year 1974-75 tallied with the figure of income shown in the return of wealth, in subsequent two years (1975-76 and 1976-77), the income so

assessed was far less than the accretion of wealth on the basis of income shown in the wealth-tax returns of the corresponding periods. Lack of correlation of assessment records of direct taxes resulted in under-assessment of income by Rs. 95,850 in two years. The consequential short levy of tax amounted to Rs. 50,722 and the penalty leviable for filing incorrect particulars of income amounted to Rs. 66,170.

While accepting the objection the Ministry of Finance have stated that the assessments in question have been revised and that the amount of additional tax raised, after taking into account additions made by the Income-tax Officer for house-hold expenses, is Rs. 1,08,861.

3.14 *Non-levy/incorrect levy of interest*

(i) Under the provisions of the Income-tax Act, 1961, where the return for an assessment year is furnished after the specified date, the assessee is liable to pay interest at prescribed rates from the day immediately following the specified date to the date of furnishing of the return on the amount of the tax payable on the total income as determined on regular assessment, as reduced by the advance tax, if any, paid, and any tax deducted at source. The Act further provides that where as a result of rectification the amount of tax on which interest was payable has been reduced, the interest shall also be reduced accordingly.

(a) A registered firm filed its return of income for the assessment year 1973-74 in November 1975 i.e. after the expiry of 27 months from the due date i.e. August 1973, of filing the return of income permissible under the Act. In arriving at the amount of interest payable by the assessee as per revised assessment order made in January 1978, the original assessment being made in January 1977, the department calculated the period of delay as 19 months instead of 27 months resulting in short levy of interest of Rs. 21,355.

(b) Similarly, for the assessment year 1975-76 the return of income was filed by the assessee in May 1977 i.e. after the expiry of 20 months from the due date i.e. August 1975, for filing the return of income. Although penal interest for delayed filing of return was charged in the original asessment completed in July, 1978, the department omitted to charge penal interest of Rs. 40,580 while revising the assessment in December 1978.

The above mistakes led to total non/short levy of interest of Rs. 61,935 in the two assessment years.

While accepting the objection the Ministry of Finance have stated that the assessments in question have been rectified and that the amount of additional tax raised and collected is Rs. 61,935.

(ii) The Act further provides that where the tax payable on current income is likely to exceed the amount of advance tax demanded by more than 33⅓ per cent, the assessee is required to file an estimate of his income and pay the amount of advance tax according to such estimate on or before the due dates prescribed for payment of advance tax instalments. Where, on making the regular assessment, the Income-tax Officer finds that such an assessee has not sent the estimate of his current income, simple interest at the rate of 12 per cent per annum is leviable from the 1st day of April next following the financial year in which the advance tax was payable upto the date of the regular assessment upon the amount by which the advance tax paid fell short of the assessed tax.

For the assessment year 1976-77 two individual assessees were served with notices of demand to pay advance tax of Rs. 26,240 and Rs. 63,000 respectively. The tax payable on their returned income worked out to Rs. 1,56,882 in both the cases. As the excess tax liability was more than 33⅓ per cent of the advance tax demanded, the assessees were required under the law to submit estimates for the higher tax and pay advance

tax accordingly. Failure to do so rendered the assessees liable to charge of interest of Rs. 1,09,362 which was not levied by the department.

The Ministry of Finance have accepted the objection.

(iii) Where an assessee fails to pay the amount otherwise than by way of advance tax, specified in any notice of demand within thirty-five days of the service of the notice, he shall be liable to pay interest at the prescribed rates commencing after the end of the period of thirty-five days to the date on which such payment is made. Further, under the Income-tax Rules, 1962, interest chargeable has to be calculated at the end of each financial year and fresh demand raised.

Two individual assessees were served with notices of demand on 3rd August, 1966 to pay tax of Rs. 6,53,296 and Rs. 6,26,145 respectively in respect of the assessment year 1960-61. The tax demands were ultimately reduced to Rs. 3,04,126 and Rs. 3,08,042 respectively and payments thereof were made in different instalments between March 1972 and March 1973. As the assessees failed to complete payment of the demands within the stipulated period, a total amount of Rs. 2,94,086 was payable by them as interest calculated at prescribed rates for the period of default from September 1966 to March 1973. No action was, however, taken by the department to realise the same.

The Ministry of Finance have accepted the objection.

3.15 *Avoidable or incorrect payment of interest by Government*

(i) Under the Income-tax Act, 1961, where the advance tax paid by an assessee during a financial year exceeds the amount of tax determined on regular assessment, the Government is liable to pay interest at the prescribed rate on the amount of advance tax paid in excess for the period from the 1st April next following the financial year to the date of regular assessment, provided the advance tax is paid according to the notice of demand issued by the department or in accordance with the estimate filed by

the assessee, as the case may be. Further, advance tax paid by an assessee beyond the last date for payment of advance tax shall not qualify for payment as confirmed by the Central Board of Direct Taxes in their instruction issued in October 1975.

In the assessment of a charitable trust for the assessment year 1974-75, the total income was finally determined at nil and the entire payment of Rs. 1,00,574 made by the assessee earlier in March 1974 was refunded. Interest of Rs. 56,280 was also paid to the assessee on the aforesaid sum of Rs. 1,00,574 treating it as payment of advance tax. As, however, the aforesaid sum of Rs. 1,00,574 was deposited by the assessee only on 29th March, 1974 which was beyond the last date for payment of advance tax *i.e.* 15th December, 1973 in the instant case, this could not be considered as payment of advance tax for allowing the interest. It was also noticed that in regard to the said payment made by the assessee, the assessee was neither served with a notice of demand from the department nor was any estimate of advance tax payable furnished by him. The payment of interest of Rs. 56,280 by the department was, therefore, irregular.

The Ministry of Finance have supported the action of the assessing officer on the strength of a judicial decision which is opposed to the existing instruction of the Board and also to another judicial decision.

(ii) Under the provisions of the Income-tax Act, 1961, where as a result of any order passed in appeal or other proceeding under the Act, refund of any amount becomes due to the assessee and if the Income-tax Officer does not grant the refund within a period of 3 months from the end of the month in which such order is passed, the Central Government shall pay to the assessee simple interest at 12 per cent per annum on the amount of the refund due from the date immediately following the expiry of the period of 3 months aforesaid to the date on which the refund is granted. Instructions were also issued by the Central Board of Direct Taxes in July 1962 to the effect that the Income-tax Officer shall dispose of the refund cases within a fortnight of the receipt of appellate orders.

An individual assessee went in appeal against the assessments completed by the Income-tax Officer for eleven assessment years, 1959-60 and 1961-62 to 1970-71. The appellate authority passed orders thereon in January 1974 and February 1975. On the basis of those orders a refund of Rs. 1,48,670 became due to the assessee. This refund was allowed by the department only in September 1978. As a result of delay of about four years in giving effect to the aforesaid appellate orders, the assessee had also to be paid interest of Rs. 81,758.

The Ministry of Finance have accepted the objection.

3.16 *Non-levy of penalties*

(i) Compulsory Deposit Scheme (Income-tax Payers), 1974.

Under the Compulsory Deposit Scheme (Income-tax Payers) Act, 1974, where the current income of an individual or Hindu undivided family, for the assessment year 1975-76, exceeds fifteen thousand rupees, the assessee is required to make a compulsory deposit at specified rates and by specified dates. If the assessee fails to make the deposit or the deposit made by him falls short of the requisite amount, he is liable to pay penalty at 25 per cent of the amount of compulsory deposit not paid or short paid.

Mention about non-levy of penalty in cases of default in this regard was made in paragraph 64 of Audit Report 1976-77. Pursuant to audit objections, the Directorate of Inspection (Income-tax also issued necessary instructions *vide* DI(IT) Circular No. 78 dated 22nd March, 1979. The irregularities in this respect have, however, persisted.

During the course of audit of income-tax wards in one Commissioner's charge it was noticed that 230 assessees had failed to make compulsory deposits amounting to Rs. 3,75,683 during the assessment years 1976-77 to 1978-79. The amount of penalty leviable under the above provisions of the scheme

works out to Rs. 93,911. No action had been taken by the department to raise demands for the unpaid compulsory deposits and to levy penalties in these cases.

The paragraph was sent to the Ministry of Finance in July 1980; their reply is awaited (December 1980).

(ii) *Failure to furnish returns of interest*

Under the provisions of the Income-tax Act, 1961, a person responsible for paying any interest not being interest on securities exceeding Rs. 1,000 is required to furnish to the Income-tax Officer on or before the 15th day of June of the assessment year a return in the prescribed form indicating the names and addresses of all persons to whom such interest was paid. For failure to furnish the return, penalty upto Rs. 10 per day is leviable for the period of default.

During the audit of Income-tax wards in one Commissioner's charge it was noticed that this provision had not been complied with in 100 cases involving 77 assessees for the assessment years 1975-76 to 1978-79 but no action had been taken by the department against the defaulting persons. The amount of penalty that could be imposed under the law would work out to a maximum of Rs. 4,19,160.

The paragraph was sent to the Ministry of Finance in July 1980; their reply is awaited (December 1980).

Other topics of interest

3.17 *Loss of revenue due to loss of return filed by an assessee*

Under the provisions of the Income-tax Act, 1961, as it stood upto the assessment year 1967-68, all assessments should be completed within the time limit of four years from the end of the assessment year in which the income was first assessable.

In the case of an individual assessee, the assessing officer having found that no return had been filed for the assessment

year 1967-68, issued a notice to her for furnishing the same. In response, the assessee filed a return in June 1976 showing income of Rs. 2,47,970 but claimed that the return had already been filed by her in January 1968 and that the department having failed to frame an assessment for this assessment year within the prescribed time limit of four years, the case was already time barred. The assessing officer without examining these facts made an assessment in January 1977 on a total income of Rs. 2,80,860 with a tax demand of Rs. 1,92,108. The assessee went in appeal against the assessment. In course of the appeal proceedings she produced a receipt granted by the department in January 1968 in acknowledgement of the return and also a copy of the challan for Rs. 1,33,157 in support of payment of tax on self-assessment made in February 1968 on the basis of the returned income. The Appellate Assistant Commissioner set aside the assessment in November 1977 with a direction to verify factual accuracy of the appellant's observations. The assessment proceedings were ultimately dropped in February 1978, with the approval of the Commissioner, as being bad in law and the tax demand of Rs. 1,92,108 raised against the assessee was vacated. The loss of the return filed by the assessee and the department's failure to frame an assessment within the time limit prescribed under the Act led to a net loss of revenue of Rs. 58,951 after considering credit of Rs. 1,33,157 deposited by the assessee towards payment of tax on self-assessment.

The Ministry of Finance have accepted the objection.

3.18 *Inordinate delay in completing set aside/re-opened assessments*

The original assessments of a firm for the assessment years 1943-44, 1944-45, 1945-46 and 1946-47, completed on 25th March, 1948, 21st April, 1949, 12th February, 1949 and 12th February, 1949 respectively, in the status of registered firm (non-resident) for the first year and of unregistered firm (non-resident) for the next three years, were set aside by the

Income-tax Appellate Tribunal in March 1953 with directions to make fresh assessments according to law after bringing on record necessary facts to decide the issue about the status of the firm. The set aside assessments for the four years were completed, ex-parte, by the assessing officer on 2nd March, 1976, *i.e.* after 23 years, adopting the same status as in the original assessments and raising a total demand of Rs. 8,05,077. The ex-parte assessments were later cancelled and assessments re-opened on the basis of the assessee's application filed on 29th March, 1976, pleading that no appearance could be made on 28th February, 1976, the date fixed for the hearing, as it was a State Government holiday on account of "Mahashivratri" and was also a Bank holiday. The re-opened assessments had not been finalised till March 1980.

The Ministry of Finance have accepted the objection.

3.19 *Adoption of incorrect rates for conversion of foreign currency*

Under the provisions of the Income-tax Act, 1961, any income which accrues or arises to an assessee outside India or any income which accrues or arises to an assessee in foreign currency but is deemed to accrue or arise in India is assessable to tax in India. The Income-tax Rules, 1962, framed under the Act, prescribe that the rate of exchange for the calculation of the value in rupees shall be the telegraphic transfer buying rate of the State Bank of India on the specific dates. Under the executive instructions issued by the Central Board of Direct Taxes in September 1978, such rates will be communicated by the Central Board of Direct Taxes and are to be adopted for the purpose of conversion of foreign currency.

For the assessment year 1978-79 in the assessment cases of 20 non-resident assessees, the correct rates of conversion as intimated by the Board were not adopted. This resulted in

under-assessment of income of Rs. 80,074 with short levy of tax of Rs. 58,607.

The paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

3.20 *Delay in collection of revenue due to non-issue of advance tax notice*

Under the provisions of the Income-tax Act, 1961, before amendment with effect from 1st June, 1978, in the case of an assessee who had been previously assessed to income-tax by way of regular assessment, the assessing officer was required to issue a notice requiring him to pay advance tax determined in accordance with the provisions of the Act. If any assessee who is required to pay advance tax, estimates that tax payable on his current income will be greater than the advance tax determined by 33⅓ per cent, he has to file his own estimate of current income and pay advance tax accordingly. When such an estimate is not filed, he has to pay penal interest at 12 per cent per annum from the 1st of April next following the financial year in which the advance tax was payable till the date of regular assessment.

In the case of an individual assessee who was previously assessed to income-tax, no notice for payment of advance tax was issued by the department in respect of the assessment year 1975-76. The failure to issue advance tax notice resulted in the collection of revenue to the extent of Rs. 7.6 lakhs being deferred for 3½ years without levy of interest thereon.

The Ministry of Finance have accepted the objection in principle.

CHAPTER 4

OTHER DIRECT TAXES

A. Wealth-tax

4.01 The actual receipts under wealth-tax in the financial years 1975-76 to 1979-80 compared with the budget estimates in these years, thus :—

Year	Budget estimates	Actuals
	(In crores of rupees)	
1975-76	43	53.73
1976-77	52	60.44
1977-78	54.90	48.46
1978-79	55	55.41
1979-80	60	64.47 (Prov.)

4.02 The arrears of demand and cases pending assessment as at the end of the assessment years 1976-77 to 1979-80 are given below. The arrears of demand exceed three times the yearly realisation of tax.

Year	No. of cases pending assessments	Arrears of demand
	(Rupees	in crores)
1976-77	2,88,949	52.75
1977-78	3,14,224	56.41
1978-79	3,31,561	184.08
1979-80	4,32,988	180.54

4.03 The Taxation Laws (Amendment) Act, 1975 introduced a provision in the Wealth-tax Act, 1957, laying down a time-limit for completion of assessments/re-assessments in cases of wealth-tax. Before this provision, effective from 1-1-1976, there was no time-limit prescribed for the completion of these assess-

ments. According to this amendment, no assessment for the assessment years upto 1974-75 could be made after the expiry of four years from 1-4-1975 *i.e.* after 31-3-1979. It was noticed in audit that the completion of pending assessments was not phased over a period of 3 years available but was made in the closing months of the assessment year 1978-79. A bulk of these pending assessments were made in March 1979 to save them from time-bar. This Audit Report mentions a large number of cases of mistakes/omissions resulting from rush in completion of such pending assessments near the end of the period of limitation.

4.04 During the test audit of assessments made under the Wealth-tax Act, 1957, conducted during the period from 1st April, 1979 to 31st March, 1980, the following types of mistakes resulting in under-assessment of tax were noticed :—

(i) Wealth escaping assessment.

(ii) Incorrect valuation of assets.

(iii) Incorrect computation of net wealth.

(iv) Incorrect allowance of exemptions.

(v) Incorrect application of rates.

(vi) Non-levy of additional wealth-tax.

(vii) Non-levy of penalty and interest.

(viii) Undue delay in action resulting in loss of revenue.

A few important cases illustrating the above types of mistakes are given in the following paragraphs.

4.05 *Wealth escaping assessment due to lack of correlation with records of other direct taxes*

The Public Accounts Committee have been emphasising the need for proper co-ordination among the assessment records pertaining to different direct taxes (paragraph 4.12 of the Committee's 186th Report) (Fifth Lok Sabha). In their 50th Report

(Paragraph 2.9) and 103rd Report (paragraph 1.12) (Fifth Lok Sabha), the Committee also laid particular stress on a critical examination of income-tax cases with a view to finding out cases of evasion of wealth-tax. Though such cases of lack of correlation have been pointed out repeatedly in the Audit Reports and the Central Board of Direct Taxes have also issued instructions on 10-1-1973, 15-11-1973 and 11-4-1979, instances of undercharge of tax resulting from omission to utilise information available in the assessment records of the assessee under various direct taxes for levy of wealth-tax continue to be noticed.

In paragraph 2.9 of their 50th Report (Fifth Lok Sabha), the Public Accounts Committee recommended that the income-tax returns of all the assessees having business income of over Rs. 15,000 should be reviewed to see whether all those having taxable wealth were submitting returns. This review conducted by the Board upto the assessment year 1973-74 revealed an escapement of wealth-tax of Rs. 44 lakhs in 1,16,599 and 15,064 cases of individuals and Hindu undivided families respectively. As cases of escapement of wealth-tax continue to be reported by Audit, the Board have again ordered in June, 1980 a similar review upto the assessment year 1979-80 of income-tax cases of 'individuals' and 'Hindu undivided families' having business income above Rs. 15,000. Results of this review are awaited (December 1980).

(i) While computing the net wealth for the assessment years 1973-74 to 1978-79 of two assessees, deductions of Rs. 2,53,541 for the assessment years 1973-74 to 1978-79 in one case and Rs. 1,49,741 for the assessment years 1976-77 to 1978-79 in the other case were allowed from their net wealth as their liabilities for capital gains tax. However, the corresponding additions made on account of capital gains in their income-tax assessments had already been deleted by the appellate authorities. Consequently capital gain tax was not payable and the liabilities did not exist when the wealth-tax assessments were actually completed. The irregular allowance of these liabilities, thus, resulted in a total short levy of tax of Rs. 95,393 in the two cases.

The Ministry of Finance have accepted the audit objection in principle.

(ii) During the previous year relevant to the assessment year 1969-70, the wife of the *karta* of a Hindu undivided family, comprising the *karta* and the wife only, died. This brought an end to the Hindu undivided family from 9th August 1968, the date of her death, since a single individual cannot form a Hindu undivided family. This position was recognised in the income-tax assessment of the assessee where the income derived from 9th August 1968 to the end of the previous year was included in the income-tax assessment of the *karta* in his status as 'individual'. Similarly, the entire assets of the 'Hindu undivided family' became the individual property of the *karta,* who also held separate properties liable to wealth-tax. Consequently, the entire wealth comprising the value of the property of the defunct family and of his separate property as on 21st October 1968 *i.e.* the relevant valuation date, was required to be assessed together to wealth-tax for the assessment year 1969-70. However, an amount of Rs. 34,27,180, being the value of the net wealth of the Hindu undivided family as on the 9th August, 1968, was not included in computing the net wealth of the individual and was separately taxed on 16-3-1979 (time-bar operating on 31-3-1979) in the status of 'Hindu undivided family'. The omission to make one assessment on aggregation, as was done in the income-tax assessment, resulted in under-assessment of wealth of Rs. 34,27,180 in the case of the individual with consequent undercharge of tax of Rs. 97,084. This wealth-tax assessment for 1969-70 was not revised even when subsequently for the assessment year 1970-71, the individual made only one wealth-tax return both for his own property and the property of the family coming to him as the sole owner.

The Ministry of Finance have accepted the audit objection in principle.

(iii) A Hindu undivided family claimed exemption in respect of agricultural land returned at Rs. 25,000 for the assessment years 1973-74 and 1974-75 which was allowed by the department.

On correlation with the income-tax assessment records as well as a letter filed by the assessee family in respect of the wealth-tax assessment for the assessment year 1977-78 (before the assessments for the years 1973-74 and 1974-75 were finalised on 19-2-1979, time-bar operating on 31-3-1979), it was noticed in audit that part of the land was situated within the municipal limits of a town and had been constructed upon. The value of the land so constructed upon, calculated on the basis of a departmental Valuer's report, was Rs. 3,52,674 and Rs. 5,37,408 for the assessment years 1973-74 and 1974-75 respectively. The land thus being non-agricultural was not exempt from tax. The omission to correlate these assessments with the income-tax records led to short levy of wealth-tax of Rs. 23,806 and of additional wealth-tax of Rs. 14,671 in these two assessment years.

The audit paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

4.06 *Incorrect valuation of properties*

The Wealth-tax Act, 1957 provides that the value of an asset shall be estimated to be the price which it would fetch if sold in the open market on the valuation date.

With a view to checking leakage of tax by undervaluation of assets, a departmental Valuation Cell was set up in 1969 for valuation in cases referred to it by the assessing officers. Apart from cases where a reference is considered necessary by the assessing officer in the interest of revenue, categories of cases of properties required to be referred to the Valuation Cell for valuation were prescribed by the Board in their executive instructions of December 1971 and a number of subsequent instructions. In 1972, the various direct tax enactments were amended through the Taxation Laws (Amendment) Act, 1972 to provide a statutory basis for reference of the question of valuation to the Valuation Cell. According to the rules framed under the amended Acts, in the case of wealth-tax, a reference shall be made to the Valuation Officer, if, in a case supported by the certificate of a

registered valuer, the assessing officer is of the opinion that the returned value is less than the fair market value and, in any other case, the assessing officer considers that the fair market value exceeds the returned value by more than 33⅓ per cent or Rs. 50,000, whichever is less. Under this amendment, valuation done by the departmental Valuation Officer was made binding on the Wealth-tax Officer.

In paragraph 14 of the Audit Report, 1974-75, test cases where reference for valuation to the Valuation Cell was required to be made under instructions of the Board and provisions of the Act, but was not made, were mentioned. Pursuant to this paragraph, the Public Accounts Committee, in paragraphs 2.41 and 3.96 of their 7th Report (Sixth Lok Sabha) desired the Board to take serious note of the omissions and to issue suitable instructions to the assessing officers for reference of cases to the Cell for valuation. Consequently, the Central Board of Direct Taxes have again issued numerous instructions, the latest being on 27-4-1979, directing that there should be no omission to make such references.

Cases of non-reference of valuation of house properties to the departmental Valuation Cell continue to be noticed. A few costly omissions noticed in test audit are given below :—

(i) The wealth-tax assessments and re-assessments of an individual for the assessment years 1974-75 to 1976-77 were completed in January and March 1977 and October 1977 in which the value of a house property was adopted as Rs. 7,44,400, as returned by the assessee on the basis of certificate of an approved valuer. The income-tax assessment records of the assessee revealed that the entire property was rented out and was fetching a gross annual rent of Rs. 1,94,825. Its net annual value was of Rs. 1,18,784, Rs. 1,23,543 and Rs. 1,20,247 for the assessment years 1974-75 to 1976-77 respectively. This case was not referred to the Valuation Cell for valuation as required in the Board's instruction of December, 1971, although the value of the property was more than Rs. 5 lakhs and the value returned by the assessee was also less than 8 times the net rental value. In the wealth-tax assessments of the same assessee for the assessment

years 1974-75 and 1975-76 additional wealth-tax on the value of urban assets owned by him was also not levied.

On these mistakes being pointed out by Audit in September 1976 and August 1977, the department accepted them and referred the case to the departmental Valuation Cell which determined the value of the house property as Rs. 11,36,000, Rs. 11,27,000 and Rs. 14,18,000 respectively for the assessment years 1974-75 to 1976-77. Thereupon, the department revised the assessments on 8-6-1978, adopting the valuation determined by the Valuation Officer and raised an additional demand of Rs. 72,286 for the assessment years 1974-75 and 1975-76. Report about the assessment year 1976-77 is awaited (December 1980).

The audit paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

(ii) In determining the value of certain immovable properties owned jointly by three individuals, the Wealth-tax Officer estimated the same at Rs. 14.25 lakhs for the assessment year 1966-67. Though, under the standing instructions of the Board, issued on 21st December, 1957, this value was to be revised at normal intervals of three years, the same value was adopted in the assessments upto the assessment year 1973-74 in the case of two assessees and upto the assessment year 1972-73 in the case of the third. Further, under instructions of the Board, issued in December 1971, these properties were required to be referred to the Valuation Cell for valuation. Reference was, however, not made. The valuation of these properties was referred to the departmental Valuation Cell only in January 1977, as directed by the Inspecting Assistant Commissioner and the Valuation Cell valued the said properties at Rs. 17.69 lakhs, Rs. 20.60 lakhs and Rs. 24.58 lakhs as on the 1st day of April, 1965, 1968 and 1972 respectively. Failure to determine the correct value in time, therefore, resulted in a total under-valuation of property by Rs. 38,38,492 with consequent short levy of wealth-tax and loss of revenue of Rs. 67,679 for the assessment years 1966-67 to 1973-74 in the three cases.

The audit paragraph was sent to the Ministry of Finance in August 1980; their final reply is awaited (December 1980).

(iii) In the case of an assessee, the value of agricultural lands owned by him was determined at Rs. 95,832 in the assessments for the assessment years 1970-71 to 1975-76. It was, however, noticed that the Valuation Officer of the department had, in another case, valued similar lands in the same neighbourhood and if those rates were applied in the instant case, the value of the assessees's lands would work out to Rs. 2,91,015 as against the returned value of Rs. 95,832. In view of this, reference to Valuation Cell for valuation was required in this case which was not made. Failure to refer the valuation of lands to the departmental Valuation Officer or to adopt the known values led to under-assessment of wealth of Rs. 1,95,183 in each of the six assessment years. Further, in the assessment year 1975-76, exemption of Rs. 68,000 was also allowed in excess in respect of agricultural lands and certain financial assets over and above the maximum admissible limit of Rs. 1.50 lakhs prescribed by the Act. These mistakes together resulted in short levy of wealth-tax of Rs. 32,386.

The Ministry of Finance have accepted the audit objection.

4.07 In the following cases, noticed in test audit, the Wealth-tax Officer omitted to base valuation of properties on the valuation report of the Valuation Officer, though such valuation was binding on him under the Wealth-tax Act, 1957.

(i) The wealth-tax returns of an individual for the assessment years 1970-71 to 1974-75 included a piece of land admeasuring 3,751 sq. yds. within the well-developed part of a big city. This land was claimed to be agricultural and its value was returned at Rs. 3 lakhs for the assessment years 1970-71 to 1972-73 and at Rs. 3.30 lakhs for the assessment years 1973-74 and 1974-75, as certified by an approved valuer. The assessment records showed that, as early as August, 1974, the Wealth-tax Officer had considered the land to be non-agricultural for these assessment years and on the 2nd August, 1974 referred

its valuation to the departmental Valuation Officer. The Valuation Officer in his report of 23rd May, 1975 had valued the land at different values ranging from Rs. 4,87,630 for the assessment year 1970-71 to Rs. 8,32,730 for the assessment year 1974-75. This report of the Valuation Officer was made after spot inspection by him and he had observed in it that it was uncultivated land, was fenced around and was situated in well-developed old residential area in the city. The assessments of these five assessment years were, however, finalised on the 30th December, 1978 *i.e.* more than three and half years after this valuation report, incorrectly treating the land as agricultural and accepting the value of the land as returned and as certified by an approved valuer as Rs. 3 lakhs and Rs. 3.30 lakhs. In these assessment orders, no mention was made of the fact that the valuation of the land had been referred to the Valuation Officer and his report had also been received. Failure to consider the valuation report of the departmental Valuation Officer, which was binding on the Wealth-tax Officer, in wealth-tax assessments for the assessment years 1970-71 to 1974-75 (done together on 30th December, 1978 as against time-bar operating on 31st March, 1979) resulted in total under-assessment of wealth of Rs. 24.80 lakhs with consequent undercharge of tax of Rs. 87,527.

The audit objection has been accepted by the Ministry of Finance.

(ii) A house property in a metropolitan city shared equally by four individual assessees was valued at Rs. 31,87,500 and Rs. 21,33,600 (its value fell as a number of flats in the building had been sold) for the assessment years 1972-73 and 1974-75 respectively by the departmental Valuer. While completing the wealth-tax assessments in the case of one co-owner in January 1978, the department considered his 1/4th share in the value of the property on the basis of the said valuation. In the wealth-tax assessments of the other three co-owners for the same assessment years 1972-73 to 1974-75, completed in September 1974 and February 1975, the value of the house property had

been adopted at a much lower figure. These assessments also needed revision for adoption of the higher value as per the departmental Valuer's report subsequently received. This was not done. The omission resulted in an under-assessment of wealth of Rs. 31,86,621, in the aggregate, leading to a total undercharge of wealth-tax of Rs. 82,578, including non-levy of additional wealth-tax.

Further, according to the Board's instructions of June, 1970, the Wealth-tax Officer was also required to re-open, in June 1978, when departmental valuation report was received, the earlier assessments (for the assessment years 1970-71 and 1971-72 which were not then time-barred) in all these four cases for consideration of the correct value of the property. This was also not done. Re-opening of the assessments for the assessment years 1970-71 and 1971-72 is now time-barred.

The Ministry of Finance have accepted the audit objection and stated (December 1980) that the matter is being examined whether remedial action can be taken now as escaped wealth.

(iii) An individual owned a house property in a metropolitan city. She added another multi-storeyed building in the same premises in 1964-67. The departmental Valuation Cell, in their report of January, 1972, determined the value of the entire property, as on 31st March 1968, at Rs. 29,61,000 which included the value of the new construction at Rs. 18,83,500. In the wealth-tax assessment, completed on 28th March, 1979 (as against the end of limitation period on 31st March, 1979) for the assessment year 1968-69 (valuation date 6th April, 1968), the value of the said property was, however, erroneously taken at Rs. 22,32,026 including the value of the new construction at Rs. 11,54,526 only. Thus, the value determined by the departmental Valuation Cell for the assessment year 1968-69 was omitted to be adopted in this assessment. The resulting undervaluation of the property by Rs. 7,28,974 led to under-charge of tax of Rs. 44,494, including additional wealth-tax.

The Ministry of Finance have accepted the audit objection and stated (December 1980) that remedial action is being taken.

(iv) In the wealth-tax assessments of an individual for the assessment years 1972-73 to 1975-76, finalised during July 1976, the value of the immovable property owned by the assessee was assessed at Rs. 21,200, as returned. The assessment records showed that valuation of this property had been referred to the departmental Valuation Officer, who, in his report dated 30th October, 1976, had valued the property at Rs. 4,79,000 for the assessment year 1972-73 which would hold good for the assessment years 1973-74 and 1974-75 and, in the absence of evidence for the rise in its value, also for the assessment year 1975-76. Even when the higher valuation determined by the Valuation Officer was reported to the assessing officer in October 1976, no action was taken by him to re-open these assessments till the date of audit in September 1979. Failure thus to act on the report of the Valuation Officer resulted in aggregate under-assessment of wealth of Rs. 18,31,200 with consequent under-charge of tax of Rs. 40,799 for the assessment years 1972-73 to 1975-76. As the assessment records of the assessee had not been made available during earlier audits, audit objection could not be issued earlier.

4.08 *Other cases of incorrect valuation*

(i) The income-tax records of an assessee for the assessment years 1966-67 to 1974-75 disclosed that she had purchased 1,14,605 sq. ft. of land in a posh locality in Bangalore in May 1960 for a consideration of Rs. 1,05,000 and that she had sold portions of the land totalling 27,605 sq. ft. between the years 1965-66 and 1974-75. With reference to these details, the area of land held by the assessee on the valuation date relevant to the assessment year 1966-67 would be 1,06,108 sq. ft. and would thereafter progressively reduce on successive valuation dates bringing it on the valuation date relevant to the assessment year 1974-75, to 87,000 sq. ft. In the wealth-tax assessments of the

assessee for the assessment years 1966-67 to 1974-75, which were made together on 16th March, 1979 (time-bar operating on 31st March, 1979), the area of land held by the assessee on the respective valuation dates was uniformly taken at 50,000 sq. ft. only and its value was adopted as Rs. 5,56,600 for the assessment years 1971-72 to 1974-75 and for the earlier assessment years, a reduction of 10 per cent in value for each assessment year was made. Thus, for all the assessment years the correct area of land which was workable from the income-tax records was omitted to be adopted for valuation, resulting in under-assessment of wealth aggregating Rs. 36,29,107 for nine years from 1966-67 and a total short levy of tax of Rs. 86,706.

The Ministry of Finance have accepted the audit objection in principle.

(ii) An individual owned an immovable property in an urban area consisting of a building, outhouse, *pegi*-house and land admeasuring 5,831 sq. yds. In the wealth-tax assessments of the assessee for the assessment year 1962-63, the Wealth-tax Officer assessed the value of the property at Rs. 1,04,600 which was finally reduced by the Appellate Tribunal on an appeal by the assessee to Rs. 95,100. He returned the same value of Rs. 95,100, determined by the Tribunal for the assessment year 1962-63, in his wealth-tax returns for the assessment years 1971-72 to 1977-78. The wealth-tax assessments of all these assessment years were finalised during February 1979 (as against the end of the limitation period on 31st March, 1979 for the assessment years upto 1974-75), accepting the value of the property at Rs. 95,100 as returned by the assessee. Even though during the intervening period ranging from 10 to 15 years there was steep increase in the value of urban property, the returned and the assessed value remained the same as Rs. 95,100. It was observed that open land situated in the locality where the assessee's property was situated was sold at rates more than Rs. 9 per sq. ft. during the previous year relevant to assessment year 1972-73. Computing the value of the land owned by the assessee at Rs. 9 per sq. ft. and taking the value of buildings

even at Rs. 51,600 as returned by the assessee for the assessment year 1962-63, the market value of the property for the assessment years 1971-72 to 1977-78 was not less than Rs. 5,23,920, as against the value of Rs. 95,100 adopted in the assessments. This under-valuation resulted in under-assessment of net wealth by Rs. 4,28,820 for each of the assessment years 1971-72 to 1977-78 with consequent aggregate undercharge of wealth-tax of Rs. 49,860.

The Ministry of Finance have accepted the audit objection in principle.

4.09 *Incorrect valuation of jewellery*

The value of jewellery and silver articles, owned by an individual, was assessed at Rs. 4,00,000 and Rs. 1,00,000 for the assessment years 1972-73 and 1973-74 and at Rs. 4,25,000 and Rs. 1,20,000 for the subsequent assessment year 1974-75. However, as the rates of gold and silver which were Rs. 202.75 per 10 grms. and Rs. 534.50 per kg. on 31-3-1972 had risen to Rs. 506 per 10 grms. and Rs. 1260 per kg. respectively on 31-3-1974, the value of jewellery and silver articles on the relevant valuation dates 31-3-1973 and 31-3-1974 would be Rs. 5,50,000 and Rs. 1,16,000 and Rs. 9,98,000 and Rs. 2,35,700 respectively. The undervaluation of jewellery and silver articles resulted in total under-assessment of wealth of Rs. 8,54,700 with consequent short levy of tax of Rs. 63,040 in the assessment years 1973-74 and 1974-75.

The Ministry of Finance have accepted the audit objection in principle.

4.10 *Mistakes in computation of net wealth*

(i) In the case of three individuals belonging to the same family group, the wealth-tax assessments of two of them for all the assessment years 1967-68 to 1974-75 and that of the third for the assessment years 1964-65 to 1975-76 were all completed

only on 8th March 1979 and 28th March 1979 (as against the end of the limitation period on 31st March, 1979). In these assessments, the share interest in a firm included in the net wealth of two of them for the assessment years 1968-69 to 1975-76 was computed in terms of the provisions of Section 7(2) of the Wealth-tax Act, 1957 read with the relevant rules framed under the Act on the basis of the net assets of the firm as reflected in its connected balance-sheets, after deducting all losses and liabilities shown therein. In addition, a deduction on account of loss of share capital in the said firm, as claimed by the assessees, was incorrectly allowed in computing their share interest in it for inclusion in their net wealth in all these assessments. This led to total under-assessment of wealth by Rs. 16,35,680, Rs. 14,64,299 and Rs. 23,73,755 respectively. Further, the value of one-third interest of each of them in a house property was adopted in the wealth-tax assessments of two of them for the assessment years 1967-68 to 1974-75 and in those of the third for the assessment years 1964-65 to 1975-76 at Rs. 1,26,667, as returned. The value of this property as determined by the Appellate Assistant Commissioner in June 1970 for the assessment years 1964-65 to 1966-67 was Rs. 1,66,666. Thus, their share interest was undervalued, even by reference to earlier assessments, to the extent of Rs. 39,999 in each of the above assessments. Further still, the standing instructions of the Board relating to revision of valuation of a house property at normal intervals of three years and reference of its valuation to the Valuation Cell were not complied with. This apart, each of the above assessees gifted a sum of Rs. 40,000 to an individual during the previous year relevant to the assessment year 1967-68. While the department did not accept the gift as valid and included the amount in the net wealth of two of them for the assessment year 1967-68, the same was not so treated in the case of the third assessee.

These omissions resulted in under-assessment of wealth aggregating Rs. 66,33,706 with consequent undercharge of total tax of Rs. 1,04,106 in the three cases for the assessment years 1964-65 to 1975-76.

The Ministry of Finance have accepted these mistakes and stated (December 1980) that remedial action is being taken.

(ii) The wealth-tax assessments of an individual for the assessment years 1962-63 to 1974-75 were done together on 20th September, 1978 (in the last assessment year of the limitation period). A scrutiny of these assessments by audit in July 1979 indicated failure to include the value of jewellery, certain non-agricultural urban lands, compensation receivable on acquisition of certain other lands by Government and undervaluation of lands and buildings. Further, additional wealth-tax in respect of urban assets was leviable since their value exceeded the exemption limit for the assessment years 1965-66 to 1972-73. Additional wealth-tax was, however, not levied. These mistakes together resulted in under-assessment of wealth-tax of Rs. 70,470 for all these assessment years.

The audit paragraph was sent to the Ministry of Finance in September 1980 ; their reply is awaited (December 1980).

4.11 *Incorrect allowance of exemptions.*

(i) Under the provisions of the Wealth-tax Act, 1957, as amended by the Finance Act, 1979, the value of one building or a group of buildings owned by a cultivator or receiver of rent or revenue out of agricultural land is exempt from wealth-tax with effect from the assessment year 1971-72 onwards provided the building/buildings concerned is (are) in the immediate vicinity of the land and is required by the assessee by reason of his connection with the land as a dwelling house, storehouse or outhouse.

In the wealth-tax assessments of a Hindu undivided family for the assessment years 1973-74 and 1974-75, exemption was allowed under these provisions in respect of a farmhouse valued at Rs. 3,22,500 and Rs. 8,99,050 for these assessment years. Since the net wealth, as arrived at on 30-3-1979 (*i.e.* on the day before the time-bar operating on 31-3-1979) did not exceed Rs. 2 lakhs, no wealth-tax was levied. The income-tax/wealth-tax

assessment records of the family and its members disclosed that its members owned 23 acres and 38 *guntas* of agricultural land till 30th March, 1970. On that day, 23 acres of land were partially partitioned by them, leaving a small piece of 38 *guntas* with the family. In the wealth-tax assessment of two members of the family for the assessment years 1970-71 onwards, they had claimed the land to be agricultural. The Wealth-tax Officer, however, on the basis of the report of the departmental Valuation Officer, to whom a reference for valuation had been made, determined the lands to be non-agricultural and disallowed the claim for exemption admissible for agricultural lands. Considering the fact that the assessee owned land measuring even less than an acre and its nature was also non-agricultural, no exemption was allowable in respect of the 'farmhouse'. The irregular exemption, so allowed, resulted in under-assessment of wealth of Rs. 3,22,500 and Rs. 8,99,050 for the assessment years 1973-74 and 1974-75 with consequent undercharge of wealth-tax (including additional wealth-tax) of Rs. 57,398. Further, though the assessee had filed the wealth-tax returns for the assessment years 1970-71 onwards claiming similar exemption, no assessment orders for the assessment years 1970-71 to 1972-73 were recorded. In their absence it could not be ascertained in audit whether the exemption had been similarly allowed in these years also. These cases otherwise became time-barred on 31st March, 1979.

In the same case, the value of a building returned and assessed for the assessment year 1973-74 was Rs. 3,22,500 as certified by an approved valuer on 18th October, 1968. The value of the same building was adopted as Rs. 8,99,050 for the assessment year 1974-75, on the basis of another certificate of an approved valuer of 12th July, 1974. Having regard to the large difference in value and also the fact that earlier valuation had been made many years back in October, 1968, the assessing officer was not only to adopt correct value for the property for the assessment year 1973-74 but also was required, under Board's instructions of June, 1970, to re-open as many past assessments as possible in or about July, 1974 to consider the correct value of the property. This was not done.

Under another standing instruction of the Board, properties were to be revalued at normal intervals of three years. These instructions were also not complied with.

All these assessments/re-assessments upto the assessment years 1974-75 were barred by limitation on 31st March 1979.

The Ministry of Finance have accepted the objections.

(ii) Under the Wealth-tax Act, 1957, valuable trees on agricultural lands became chargeable to wealth-tax along with the value of agricultural land with effect from 1970-71. Such trees, not situated in a plantation, have been exempted from tax with effect from the assessment year 1976-77 by an amendment of the Act introduced by the Finance Act, 1975. Consequently, valuable trees (other than crops growing on them) in plantations continue to be liable to tax with effect from 1st April 1970.

However, in the case of an individual, exemption on account of tea plants in certain tea plantations valuing Rs. 4,85,813, Rs. 4,85,813 and Rs. 5,12,702 was incorrectly allowed for the assessment years 1970-71 to 1972-73. Besides, an inadmissible exemption was allowed in this case for 'labour quarters' situated in the plantations. The allowance of these exemptions led to under-assessment of tax of Rs. 43,638.

The Ministry of Finance have accepted the mistake in principle.

4.12 *Application of incorrect rates*

The Schedules to the Income-tax Act, 1961 and to the Wealth-tax Act, 1957, as amended by the Finance Act, 1973, prescribed a higher rate of tax (income-tax as well as wealth-tax) for every Hindu undivided family having at least one member with assessable income and/or net wealth, with effect from the assessment year 1974-75. Omissions to levy tax at higher rates in cases of such specified Hindu undivided families have been

pointed out in the Audit Reports 1975-76, 1976-77, 1977-78 and 1978-79.

In paragraph 61.3 of the Audit Report, 1977-78, it was pointed out that in January 1979 the Board ordered a review by the department generally of income-tax and wealth-tax cases from the assessment years 1974-75 onwards with a view to locating cases of under-assessment of tax due to incorrect application of rates of tax in cases of specified Hindu undivided families. Under-assessment of income-tax of Rs. 9.29 lakhs in 1041 cases and of wealth tax of Rs. 3.93 lakhs in 132 cases, noticed in an incomplete review upto March 1979 was also pointed out. Results of a complete review are awaited (December 1980).

In the meanwhile, such mistakes continued to be noticed in the course of test audit in the period from April 1979 to March 1980. In fifteen cases of specified Hindu undivided families in eight Commissioners' charges, where such mistakes were pointed out in audit, there was under-assessment of wealth-tax of Rs. 2,36,219 in the assessment years 1974-75 to 1978-79.

The Ministry of Finance have accepted the audit objection in all these cases. Additional demands for wealth-tax raised in these accepted cases is of Rs. 2,31,455.

4.13 *Non-levy/short levy of additional wealth-tax*

Under the Wealth-tax Act, 1957, before its amendment by the Finance Act, 1976, where the net wealth of an individual or a Hindu undivided family included buildings or lands (other than business premises used throughout the previous year for the purpose of his or its business or profession) or any rights therein, situated in an urban area, additional wealth-tax was leviable on the value of such urban assets above the prescribed limit.

While considering paragraph 71 of the Audit Report 1970-71, in which undercharge of additional wealth-tax of Rs. 1.36 lakhs in 67 cases was pointed out, the Public Accounts Committee in paragraph 2.60 of their 88th Report (Fifth Lok Sabha), desired

a review of wealth-tax cases. Accordingly, the Board conducted a review between 1972 and 1975 in which omission to levy additional wealth-tax amounting to Rs. 3.25 lakhs was detected in 105 cases. However, as cases of non-levy/short levy of additional wealth-tax continued to be noticed and reported in the subsequent Audit Reports, that review did not appear to be complete.

The Central Board of Direct Taxes was, therefore, requested in October 1979 to consider having a complete review conducted. Accordingly, in February, 1980 the Board ordered a fresh review. Results of this review are awaited (December 1980).

Some of the cases where such omissions have been noticed further are given below :—

(i) The net wealth of an individual for each of the assessment years 1968-69 to 1975-76, computed in these assessments (all completed in May 1978 in the last assessment year of the limitation period), included urban immovable properties valued at Rs. 25,26,000 on which additional wealth-tax was leviable. The department, however, did not levy such tax. The omission resulted in a net non-levy of wealth-tax of Rs. 2,66,028 for all the above years. Further, though the assessee had not paid self-assessment tax, no penalty for non-payment of self-assessment tax was levied.

The Ministry of Finance have accepted these omissions.

(ii) The net wealth of an individual for the assessment years 1969-70 to 1976-77, assessed on 30th December 1978 (as against the end of the time-limit on 31st March 1979), included, *inter alia*, urban immovable assets valued at Rs. 7,68,700, Rs. 7,68,700, Rs. 8,70,200, Rs. 8,70,200, Rs. 10,59,800, Rs. 11,92,300, Rs. 11,92,300 and Rs. 10,98,000 respectively on which additional wealth-tax was leviable to the extent of Rs. 1,78,362, in the aggregate. The department, however, did not levy any such tax. This resulted in non-levy of additional wealth-tax of Rs. 1,78,362 for the assessment years 1969-70 to 1976-77.

In the same case, no penalty for non-payment of self-assessment tax was levied for the assessment years 1969-70 and 1972-73 to 1976-77. Further, the detriment to revenue from undue postponement of payment of self-assessment tax could have been avoided, if the assessing officer had made provisional assessments on the basis of returned wealth. This was not done for the assessment years 1972-73 to 1974-75 and 1976-77.

The Ministry of Finance have accepted these omissions and stated that demand for additional tax of Rs. 1,87,736 has been raised.

(iii) The value of urban properties, included in the net wealth of an individual assessed on 31st October 1977 for the assessment years 1965-66 to 1974-75 and on 31st January 1978 for the assessment years 1975-76 and 1976-77, exceeded the exemption limit of Rs. 7,00,000 up to the assessment year 1970-71 and Rs. 5,00,000 for the assessment years 1971-72 to 1976-77. Consequently, additional wealth-tax was leviable. No additional wealth-tax was, however, levied. This omission resulted in non-levy of additional wealth-tax of Rs. 1,68,708 in all the assessment years from 1965-66 to 1976-77.

The Ministry of Finance have accepted the audit objection and stated that remedial action has been commenced.

(iv) The net wealth of a specified Hindu undivided family for the assessment years 1968-69 to 1974-75, as determined in these assessments done on 26th March 1979 (as against the end of the limitation period on 31st March 1979,) included urban immovable properties valued more than the prescribed limits on which additional wealth-tax was leviable. The department, however, did not levy the tax. The omission resulted in a total short levy of additional wealth-tax of Rs. 1,56,949. Penalty for non-payment of tax on self-assessment was also not levied for the assessment year 1974-75

The Ministry of Finance have stated (December 1980) that audit objection will be kept in view while giving effect to the appellate orders.

(v) The net wealth of an individual included urban immovable assets valued at Rs. 10,08,780, Rs. 7,69,755 (returned value Rs. 12,25,086), Rs. 7,69,755 (returned value Rs. 12,21,808), Rs. 9,95,643, Rs. 9,95,643, Rs. 9,95,643, Rs. 8,93,162 and Rs. 8,93,162 for the respective assessment years from 1967-68 to 1974-75 on which additional wealth-tax was leviable. The department, however, did not levy this tax in any of these assessments, all done on 23rd November 1977. This omission resulted in an aggregate short levy of additional wealth-tax of Rs. 96,287.

The Ministry of Finance have accepted the audit objection and stated (November 1980) that additional tax demand has been raised.

(vi) In 26 other cases in 22 Commissioners' charges, additional wealth-tax of Rs. 12,16,118 was similarly omitted to be levied for various assessment years between 1965-66 and 1976-77. The tax not levied in each of these cases was above Rs. 20,000.

The Ministry of Finance have accepted the omission in all the cases; in 19 accepted cases, demand for additional tax raised is of Rs. 8,25,263.

4.14 *Non-levy of additional wealth-tax in respect of urban assets owned by partnership firms and specified types of companies*

The Schedule to the Wealth-tax Act, 1957, as applicable to the assessment years 1971-72 to 1976-77, provided that proportionate value of urban assets owned by firms and specified types of companies, computed in the prescribed manner, would be liable to additional wealth-tax. This was the case, if this proportionate value, together with the value of urban assets owned by an individual or a Hindu undivided family, being a partner or a shareholder, exceeded the prescribed limit.

(i) The net wealth of two assessees for the assessment years 1971-72 to 1974-75 comprised urban immovable properties valuing Rs. 18,07,000, Rs. 18,95,200, Rs. 17,02,750 and

Rs. 18,80,750, including the value of urban land and building owned by a Land and Development Corporation, a partnership firm in which the two assessees were equal partners. Therefore, additional wealth-tax of Rs. 1,58,096, Rs. 1,67,996, Rs. 1,43,040 and Rs. 1,66,116 respectively was leviable on the value of such urban assets. It was, however, seen to have been omitted to be levied by the department. The omission resulted in a total non-levy of additional wealth-tax of Rs. 6,35,248 for the assessment years 1971-72 to 1974-75.

The Ministry of Finance have stated that the results of the appeals taken by the department before the Tribunal for the inclusion of the value of land belonging to the firm are awaited (December 1980).

(ii) In the case of an individual, the Wealth-tax Officer omitted to levy additional wealth-tax on urban immovable properties owned by him and also on the proportionate value of urban land comprising the assets of a partnership firm, in which he was a partner. The value of these properties so liable to tax was Rs. 6,13,450, Rs. 6,53,800, Rs. 7,84,064 and Rs. 6,10,614 for the assessment years 1973-74 to 1976-77 respectively. This omission led to non-levy of additional wealth-tax of Rs. 35,335, in the aggregate.

The Ministry of Finance have accepted the omission and stated that additional demand for tax of Rs. 35,335 has been raised.

(iii) In five cases, two relating to individuals and three to Hindu undivided families, where their net wealth included the value of the assessees' interest, as partners of certain partnership firms, in the value of their urban assets, additional wealth-tax in respect of urban assets valued at Rs. 65,44,100, in the aggregate, for the assessment years 1973-74 and 1974-75, was omitted to be levied. The omission resulted in non-levy of additional wealth-tax aggregating Rs. 78,320 in all these cases for the two assessment years.

The Ministry of Finance have accepted that additional wealth-tax shall be levied in respect of the urban assets of the firms not used by them as their business premises.

(iv) The net wealth of an assessee for the assessment years 1971-72 to 1974-75 included *inter alia* urban assets owned by him valuing at Rs. 4,73,523. As the value of the urban assets was less than Rs. 5 lakhs, no additional wealth-tax was levied while completing the assessments for these assessment years on 21st January 1979 (as against the end of the limitation period on 31st March 1979). It was, however, noticed in audit (July 1979) that the assessee was holding 7,360 shares, out of a total issue of 16,170 shares, in a private company on the valuation dates relevant to the aforesaid assessment years and that this private company also owned an urban asset valued at Rs. 9,36,700. The part of the value of these shares which was to be deemed as value of 'urban assets' for levy of additional wealth-tax worked out to Rs. 4,26,000. This value was omitted to be considered for purposes of determining the levy of additional wealth-tax. This omission resulted in non-levy of total additional wealth-tax of Rs. 79,900 for the assessment years 1971-72 to 1974-75.

The Ministry of Finance have accepted the audit objection in principle and stated (December 1980) that additional wealth-tax shall be levied on the proportionate value of urban assets of the company not used as its business premises.

4.15 *Non-levy of penalty*

The Wealth-tax Act, 1957 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. In their executive instructions issued in July 1969, the Central Board of Direct Taxes directed that where the Wealth-tax Officer has decided not to levy penalty, having regard to the circumstances of the case, a note should be recorded in the order-sheet giving detailed reasons for not invoking these penalty provisions. Failures to levy penalty even without any recorded reasons continue to be noticed with the result that these provisions for levy of penalty

made in the Act as a deterrent against undue delay in filing of returns fail to serve the intended purpose. Instances of such failure were pointed out in paragraph 97(ii) of the Audit Report, 1975-76 and paragraph 81 of the Audit Report, 1976-77. Some of the important cases of omissions to levy penalty are given below :—

(i) In the case of an assessee, where delay in filing the returns was 53 months and 43 months for the assessment years 1968-69 and 1969-70 respectively, proceedings for levy of penalty for delayed filing were initiated but the assessments themselves were later on set aside by the Appellate Tribunal for being done again. While redoing the assessments under the Tribunal's directions, assessing officer omitted to initiate the penalty proceedings. Reasons for not initiating the penalty proceedings were also not recorded. The minimum penalty leviable in this case was Rs. 4,24,390.

The Ministry of Finance have accepted the omission on the part of the Wealth-tax Officer to record reasons for not initiating the penalty proceedings.

(ii) In the case of an assessee, a Hindu undivided family, which failed to furnish the returns of net wealth for the assessment years 1970-71 to 1976-77 within the time allowed by the Act (delay ranging from 25 months to 101 months), a minimum penalty of Rs. 4,12,735 was leviable but no penalty proceedings were initiated nor were there any recorded reasons for not invoking the penalty proceedings.

The audit paragraph was sent to the Ministry of Finance in September 1980 ; their reply is awaited (December 1980).

(iii) A Hindu undivided family filed its wealth-tax returns for the assessment years, 1966-67 to 1972-73 on 28th August 1973. No penalty proceedings were initiated while doing these assessments on 24th March 1979 (as against the limitation period expiring on 31st March 1979) nor was there any note recorded by the Wealth-tax Officer on the order-sheet for not invoking the

penalty provisions. Thus, there was no indication from the assessment records that the assessing authority had decided against the levy of penalty for late filing of these returns. The minimum penalty leviable was Rs. 1,46,417 for these assessment years.

The Ministry of Finance have accepted the audit objection in principle.

4.16 *Non-levy of interest*

Under the Wealth-tax Act, 1957, an assessee is deemed to be in default if the amount specified in the notice of demand is not paid within 35 days of its service and, for the period of default, the assessee is liable to pay simple interest at 12 per cent per annum.

A notice of demand imposing penalties of Rs. 25,570 and Rs. 30,234 respectively for the assessment years 1964-65 and 1965-66 was issued on 12th August 1974 in the case of an individual for delay in filing his wealth-tax returns without reasonable cause. The amount of Rs. 55,804 was due for payment on or before 17th September 1974. The assessee did not pay this amount before the due date but paid Rs. 25,247 for the assessment year 1964-65 and Rs. 2,181 for the assessment year 1965-66 in February, 1979 only. It was noticed in audit (May 1979) that the assessing officer had not levied interest of Rs. 28,946 up to January 1979 for delay in payment of the demand in arrears.

The Ministry of Finance have accepted the default on the part of the assessing officer for not levying interest in the period from February 1979 to May 1979.

4.17 *Undue delay in action causing loss of revenue*

(i) The Wealth-tax Act, 1957, as amended with effect from the 1st April, 1971, provides that the order imposing a penalty should be passed within two years from the end of the financial year in which the proceedings in the course of which action for imposition of penalty has been initiated, failing which the proceedings are barred by limitation.

An individual submitted his wealth-tax returns for the assessment years 1961-62 to 1965-66 long after the due dates specified in the Act. The minimum penalty leviable for late submission of returns for the assessment years 1961-62 to 1965-66 amounted to Rs. 61,458, in the aggregate. Though, in the course of completing the assessments in September, 1974, the department initiated penalty proceedings for delayed submission of returns, no orders imposing penalty were passed within the period of limitation expiring on 31st March, 1977. The minimum penalty leviable in this case was of Rs. 61,458.

The audit paragraph was sent to the Ministry of Finance in September 1980; their final reply is awaited (December 1980).

Three other assessees submitted their wealth-tax returns for the assessment year 1967-68 after the expiry of more than 44 months from the due date specified in the Act. The minimum penalty leviable in these cases for delayed submission of returns amounted to Rs. 1,46,755, in the aggregate. In the course of the assessments completed in March 1971 on the net wealth of Rs. 5,62,040, Rs. 5,69,020 and Rs. 4,20,184 respectively, the department initiated penalty proceedings for delayed submission of returns but issued notices to the assessees only in November 1973 i.e. after the end of the limitation period on 31st March 1973. The delay in the issue of notices resulted in the proceedings getting time-barred. The minimum penalty involved in these time-barred cases was of Rs. 1,46,755.

The Ministry of Finance have accepted the audit objection.

(ii) Any tax, interest, penalty, fine or any other sum payable as a result of any order passed under the Wealth-tax Act, 1957 is required to be served upon the assessee through a notice of demand specifying the sum payable without which the assessee is not liable to pay any such sum.

In five cases, orders of regular assessments levying wealth-tax aggregating Rs. 80,710 for the assessment years 1967-68 to 1974-75 were passed within the period from January to March

1979. The connected notices of demand were, however, not issued or served upon the assessees upto the date of audit in December 1979. The omission to issue the notices of demand resulted in undue postponement of demand of Rs. 38,087.

The Ministry of Finance have accepted the audit objection.

(iii) An approved valuer determined the value of agricultural lands owned by an assessee at Rs. 4,81,652 as on 31st March 1973. This value was adopted in the assessment for the assessment year 1973-74 done in November 1973. The Wealth-tax Officer had adopted the value of these lands as Rs. 1,29,806 for the assessment year 1972-73 in the assessment completed on 3rd July 1973. When the Internal Audit Wing of the Department pointed out in March 1974 the omission to revise the assessment for the assessment years 1972-73 also, for revision of the valuation on the basis of the higher value, the Wealth-tax Officer replied that he had already made a note to this effect in the assessment order for the assessment year 1973-74. Nevertheless, in the re-opened assessment for 1972-73, completed in February 1976, the higher value of land was omitted to be considered, resulting in short levy of tax of Rs. 21,611.

The audit objection has been accepted by the Ministry of Finance.

B-GIFT TAX

4.18 Gift-tax is levied on the aggregate value of all gifts made by a person during the relevant previous year. All transfers of property which are made without adequate consideration in money or money's worth are liable to tax unless specifically exempted by the Gift-tax Act. The term 'property' for the purpose of the Gift-tax Act connotes not only tangible movable and immovable property including agricultural land but also other valuable rights and interests.

4.19 The receipts under gift-tax in the financial years 1975-76 to 1979-80 compared as under with the budget estimates of these years :

Year	Budget estimates	Actuals
	(In crores of rupees)	
1975-76	4.50	5.11
1976-77	4.75	5.67
1977-78	5.50	5.55
1978-79	5.75	5.85
1979-80	5.75	6.83 (Prov.)

4.20 Number of cases pending assessment and the arrears of demand are given below :—

Year	No. of pending assessments	Arrears of demand (In crores) of rupees
1976-77	22,580	5.90
1977-78	22,925	6.97
1978-79	21,807	17.72
1979-80	27,403	15.77

4.21 During the test audit of assessments made under the Gift-tax Act, 1958 conducted during the period from 1st April 1979 to 31st March, 1980, the following types of mistakes were noticed :—

(i) Gifts escaping assessment.

(ii) Incorrect valuation of gifts.

(iii) Incorrect allowance of exemptions.

A few important cases illustrating the above types of mistakes are given in the following paragraphs.

4.22 *Gifts escaping assessment*

Some instances of cases of undercharge of wealth-tax, resulting from omission to carry out correlation between assessments under various direct taxes have been pointed out in paragraph 4.05 of this Audit Report. Similar cases of undercharge of gift-tax are given below :—

(i) In June 1974, a registered firm relinquished its claim for the recovery of loans of Rs. 5,40,862 including interest accrued thereon due from its two debtors. In the income-tax assessment of the firm for the assessment year 1975-76, completed in September 1978, the Income-tax Officer observed that the relinquishment was as a result of a mutual agreement and was an attempt to help the debtors for extra commercial consideration. Consequently, the deduction for claim for bad debts was held to be 'not allowable'. No action was, however, taken by the Department to initiate gift-tax proceedings even though the agreement relinquishing these debts attracted levy of gift-tax. This omission, caused by omission to act on the information available in the assessment records of income-tax, resulted in the escapement of a gift of Rs. 5,40,862 involving non-levy of gift-tax of Rs. 1,17,258 for the assessment year 1975-76.

The Ministry of Finance have accepted the audit objection.

(ii) Upto the assessment year 1968-69, a firm had four partners with one partner sharing profit at 34 per cent and the other three at 22 per cent each. The constitution of the firm was revised in the previous year relevant to the assessment year 1969-70 by bringing in three new partners and admitting six minors to the benefits of partnership. None of the new partners and the minors brought in any capital for investment in the firm. The change in the constitution of the firm resulted in the reduction of the profit-sharing ratio of the three original partners from 34 per cent, 22 per cent and 22 per cent to 11 per cent, 9 per cent and 8 per cent respectively. Thus, these three partners relinquished a part of their right to share in the assets and profits of the firm without any consideration in

money or money's worth. Upon this, the proportionate value of the assets and goodwill of the firm less its existing liabilities so relinquished by the three partners, was chargeable to gift-tax. However, neither gift-tax returns were filed nor did the Gift-tax Officer initiate proceedings for the assessment of these gifts to tax. Though the audit objection was issued in August 1971, no action was taken by the department in this case. Even the required notices under Section 16 of the Gift-tax Act for bringing the escaped gifts to tax were not issued, though it was also brought to the notice of the Commissioner that the action to rectify would be barred after 31st March 1978. The failure of the Department to assess the gifts to tax led to a loss of revenue of Rs. 1,60,830.

The audit paragraph was sent to the Ministry of Finance in August, 1980; their reply is awaited (December 1980).

4.23 *Non-levy of 'deemed' gift-tax*

The Gift-tax Act, 1958 provides that where property is transferred otherwise than for adequate consideration, the amount by which the fair market value of the property on the date of the transfer exceeds the value of consideration received shall be deemed to be a gift made by the transferor and subjected to the levy of gift-tax as a 'deemed gift'.

While issuing instructions on the need for proper co-ordination among assessments under different tax laws in November 1973, the Central Board of Direct Taxes had specifically required Gift-tax Officers to levy gift-tax on 'deemed gift' in cases where they, as Income-tax Officers, noticed and brought to capital gains tax, the excess of fair market value over declared consideration. Nevertheless, failure to bring such 'deemed gifts' to tax continues to be noticed as was pointed out in paragraph 92 of the Audit Report, 1976-77, paragraph 76 of the Audit Report, 1977-78 and paragraph 75 of the Audit Report, 1978-79. A few illustrative cases are again given below :

(i) In the course of audit of an income-tax ward, it was noticed that six assessees had transferred unquoted equity shares

of 4 private limited companies (of their family group) held by them, either by way of sale or by way of capital contribution to the firms in which they were partners, during the previous years relevant to the assessment years 1973-74 and 1974-75. In these cases, credit for these shares to their capital account as partners was not equal to their fair market value on the date of transfer. In their income-tax assessments, it was held that the rates at which the shares of three private limited companies were transferred were far below their market value. As a result the excess of their fair market value, as estimated by the departmental Valuation Officer over the declared consideration was brought to tax under 'capital gains'. However, proceedings were not initiated for levy of gift-tax on 'deemed-gift' involved in these cases. Further, it was noticed that the fair market value of the unquoted equity shares in the fourth company on the basis of its net worth was Rs. 235 per share, as against the rate of Rs. 115 per share at which they were credited to capital accounts of partners. 'Deemed gift' on this account in the case of two out of the six assessees, thus, escaped gift-tax. Further still, in the case of another private limited company, which transferred 9,114 shares of this fourth company during the previous year relevant to assessment year 1975-76, similar 'deemed gift' escaped tax. As a result of all these omissions, deemed gift of Rs. 153.69 lakhs escaped assessment during the years 1973-74 to 1975-76, with consequent non-levy of gift-tax of Rs. 70.89 lakhs.

The audit paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

During the course of local audit of another income-tax ward in January, 1979, it was observed in the case of seven assessees, all belonging to a big industrial family group, that action to levy gift-tax on the excess of fair market value of unquoted equity shares over their declared consideration on transfer during the previous year relevant to the assessment year 1974-75 had not been initiated. This omission occurred even though in their income-tax assessments, capital gains-tax had been levied

on this excess. This resulted in non-levy of gift-tax aggregating Rs. 63.25 lakhs on 'deemed gifts' amounting to Rs. 130.55 lakhs.

The corresponding income-tax cases had been seen by the Internal Audit but the omission was not pointed out by them. The audit paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

(ii) A limited company transferred on 27th August, 1971 two immovable properties for a declared consideration of Rs. 6,86,000 and Rs. 11,00,000 to sons of its directors and their relatives. Though both these properties were required to be referred to the departmental Valuation Officer for valuation under the executive instructions of the Board of December 1971, the declared consideration in this case was accepted without such a reference. On this omission being pointed out by Audit in January 1978, a reference was made to the Valuation Cell which determined the fair market value of the properties as Rs. 11,70,600 and Rs. 16,45,300 respectively. Thus, a 'deemed gift' of Rs. 10,29,900 escaped assesssment on which gift-tax leviable amounted to Rs. 2,66,460.

The Ministry of Finance have accepted the audit objection and stated (October 1980) that remedial action has been commenced.

(iii) It was noticed from the statement of accounts filed with income-tax returns by two individuals in the same ward that during the previous year relevant to the assessment year 1974-75, they transferred on 1st June 1973 one-fourth interest of each of them in certain properties to members of their family group at a declared consideration of Rs. 2,59,227 each. The market value of their interest in the said properties was Rs. 4,86,270 each on the basis of their wealth-tax assessments for the assessment year 1973-74 related to the valuation date 31st March 1973. Although the amount of Rs. 2,27,043 in each case, being the excess of fair market value of the property over

the declared consideration, was a "deemed gift" liable to gift-tax, neither any gift-tax return was filed nor did the Department initiate any gift-tax proceedings. The escapement of gift of Rs. 2,27,043 from assessment, resulting from omission to correlate with income-tax and wealth-tax assessments, led to non-levy of gift-tax of Rs. 37,011 in each case for the assessment year 1974-75. There was, thus, non-levy of tax of Rs. 74,022.

In the case of one of the above assessees, it was further noticed that he retired on 1st June, 1973 from a firm of which he had been a 20 per cent partner by repaying to the firm the debit balance of Rs. 61,787 in his capital account with the firm on the date of retirement. The department while computing his share interest in the firm considered the assets at their book value of Rs. 4,59,859 as on 31st March, 1973 instead of their market value of Rs. 18,88,200 as on that date, determined by the departmental Valuer in February 1976. The value of goodwill of the firm was also not computed and included in the assets of the firm for computation of share interest of the retiring partner. Taking the value of assets of the firm at Rs. 18,88,200 instead of as Rs. 4,59,859 but without goodwill, further non-levy of gift-tax in this case was of Rs. 78,852. The total non-levy of tax in these cases was, thus, of Rs. 1,52,874. The omission was accepted by the Department on being pointed out by Audit in May 1979.

The paragraph was sent to the Ministry of Finance in July, 1980; their reply is awaited (December 1980).

4.24 *Incorrect valuation of unquoted equity shares*

Under Section 6(1) of the Gift-tax Act, 1958, the value of a gifted property has to be estimated to be the price which in the opinion of the Gift-tax Officer it would fetch if sold in the open market. Rule 10(2) of the Gift-tax Rules lays down that the value of unquoted equity shares in a company should be ascertained with reference to the value of the total assets of the company. As the provisions of the Gift tax Act are *pari materia*

with those of the Estate Duty Act, 1953 in regard to the valuation of unquoted equity shares, the instructions issued by the Board under the Estate Duty Act for valuation of such shares are equally applicable to gift-tax cases. Under the Estate Duty Act, the Board had issued instructions in May, 1965 and July, 1965 laying down that the value of unquoted shares should be determined on the basis of the market value of the assets of the compay and not the book value of the said assets.

The provisions of valuation of unquoted equity shares in the Wealth-tax Act, 1957 and rules framed thereunder are different from those in the Gift-tax Act and Estate Duty Act. Even then the Board, in their executive instructions, issued in March 1968, extended the provisions of the Wealth-tax Rules for the valuation of the unquoted equity shares to the estate duty and gift-tax cases. This incorrect extension of these instructions to estate duty cases was commented upon in paragraph 72 of the Audit Report, 1972-73 and pursuant to this paragraph these instructions were withdrawn by the Board in October, 1974 both for estate duty and gift-tax cases. It was then stated that the valuation should be done in accordance with the aforesaid instructions of May, 1965 and July, 1965. It was further clarified in May 1975 that the value of the total assets of a company would also include the value of its goodwill whether or not shown in its balance-sheet.

Instances, however, continue to be noticed where incorrect valuation of unquoted equity shares in companies made in disregard of the aforesaid provisions of the Act and rules and instructions of the Board resulted in undercharge of gift-tax. A few important cases of such undercharge were commented upon in paragraph 82 of the Audit Report, 1975-76, paragraph 94 of the Audit Report, 1976-77, paragraph 77 (ii) of the Audit Report, 1977-78 and paragraph 76 of the Audit Report, 1978-79. A few more costly instances of undervaluation are given below :—

(i) During the previous year relevant to the assessment year 1973-74, two private limited companies transferred 300 and

C. ESTATE DUTY

4.26 The receipts under estate duty in the financial years 1975-76 to 1979-80 compared as under with the budget estimates of these years :—

Year	Budget estimates	Actuals
	(In crores of rupees)	
1975-76	9.25	11.65
1976-77	8.75	11.73
1977-78	10.75	12.30
1978-79	11.00	13.08
1979-80	12.00	14.05 (Prov.)

4.27 The arrears of demand and the number of assessments pending as at the end of various assessment years were as follows :—

Year	No. of assessments pending	Arrears of demand
		(in crores of rupees)
1976-77	27,256	15.56
1977-78	28,287	17.52
1978-79	28,278	17.11
1979-80	34,891	17.23

4.28 During the test audit of assessments made under the Estate Duty Act, 1953, conducted during the period from 1st

April, 1979 to 31st March 1980, the following types of mistakes resulting in under-assessment of duty were noticed :—

(i) Estates escaping assessment.

(ii) Incorrect valuation of assets.

(iii) Incorrect computation of the principal value of estates.

(iv) Non-levy of interest.

(v) Mistakes in giving effect to appellate orders.

A few instances of these mistakes are given in the following paragraphs.

4.29 *Escapement of estates due to lack of correlation*

In paragraphs 4.05 and 4.22 of this Audit Report, escapement of wealth-tax and gift-tax caused by lack of correlation of assessments under various direct tax laws has been pointed out. Similar lack of correlation resulting in escapement of estates from levy of estate duty was also noticed in the following cases :—

(i) In the estate duty assessment made in December 1976 in respect of a deceased person, a sum of Rs. 1,59,825 was allowed to be deducted as his income-tax liability for the assessment years 1962-63 to 1970-71 from the principal value of his estate. The income-tax liability, had, however, been reduced in April 1973 and November 1973 to Rs. 46,716 on giving effect to the decision of the Appellate Tribunal. Thus, the lack of correlation of this assessment with the income-tax assessment records of the deceased person resulted in excess allowance of income-tax liability of Rs. 1,13,109 and consequent under-assessment of his estate by an identical amount with undercharge of duty of Rs. 56,521. On the mistake being pointed out by Audit in

February 1977, rectification of the assessment was made in May 1979, raising an additional demand of duty of Rs. 56,521.

The Ministry of Finance have accepted the audit objection.

(ii) In the estate duty assessment made in March 1977 of a deceased person, who died in November 1969, the value of an urban house property owned by him was accepted as Rs. 20,370 as per the revised account of estate filed by the accountable person. However, in the wealth-tax assessment of the deceased person for the assessment years 1967-68 to 1969-70 and also in the wealth-tax returns filed by his legal heirs after his death, the value of this property had been shown and assessed as Rs. 1,01,892. Even in the deed of partition executed by the deceased person and his brother, available in his assessment records, this property had been valued at Rs. 1,01,892. The incorrect valuation of the property, thus, resulted in under-assessment of the estate by Rs. 81,522 (Rs. 1,01,892 less Rs. 20,370). Further, a deduction of Rs. 39,420 was allowed as tax liability. However, a part of this liability had already been set aside by an appellate authority and correct liability allowable was of Rs. 7,840.

The combined effect of these mistakes caused by omission to correlate this estate duty assessment with income-tax and wealth-tax assessments of the deceased person resulted in under-assessment of his estate by Rs. 1,13,102 with consequent undercharge of duty of Rs. 33,930.

The Ministry of Finance have accepted the audit objection.

(iii) In the estate duty assessment completed in March, 1979 in respect of a deceased person (who died in November 1961), the allowance for his total income-tax and wealth-tax liabilities was made for Rs. 11,13,657, as against the liabilities of Rs. 9,58,786 communicated by the Income-tax Officer concerned to the Assistant Controller of Estate Duty. In the same assessment, the value of a property was taken as Rs. 18,000 instead

of Rs. 22,500 and interest of Rs. 58,780 for the period of extension from 25-5-1962 to 15-2-1966, allowed to the accountable person for filing the account of the estate, was not charged. The combined effect of these omissions resulted in short levy of duty of Rs. 98,623.

The audit paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

4.30 *Incorrect valuation of assets*

The principal value of any property shall be estimated to be the price which, in the opinion of the Controller, it would fetch if sold in the open market at the time of the deceased's death.

(i) Under Section 7 of the Estate Duty Act, 1953, property in which the deceased, or any other person had an interest ceasing on the death of the deceased, shall be deemed to pass on the deceased's death to the extent to which a benefit accrues or arises by the cesser of such interest. Section 40 *ibid* also provides that, if the interest of the deceased extended to the whole of the property, the value of the benefit accruing or arising from the cesser of such interest shall be the principal value of that property.

As per the will left by the mother of a deceased person, he had life-interest for possession and enjoyment of the whole of extensive agricultural properties subject to payment of Rs. 1,000 per annum to each of his five sisters. On his death, the properties were to devolve on his five sisters equally. While completing the estate duty assessment on the death of the deceased, the value of his life-interest in the above properties was fixed as Rs. 80,833 at 1/6th of the gross value of the properties, *viz.* Rs. 4,85,000. As, however, the deceased had right of possession and enjoyment of the entire properties worth Rs. 4,85,000

(yielding an annual income estimated at Rs. 45,540), the value of his life-interest ceasing on his death, was to be calculated under sections 7 and 40(b) of the Estate Duty Act 1953. Valuation so done would be Rs. 4,31,750, *i.e.* extending to the full value of the property. The principal value of estate which, thus, escaped assessment due to the incorrect computation of the interest ceasing on death was Rs. 3,50,917 (Rs. 4,31,750— Rs. 80,833) with a consequent short demand of duty of Rs. 76,946. On the basis of the audit observation issued in June 1979, the department revised the assessment in July 1980, raising an additional demand of duty of Rs. 76,946.

The Ministry of Finance have accepted the audit objection and stated that additional demand for duty of Rs. 76,946 has been raised.

(ii) A deceased person (who died in April 1975) had one-fifth share interest as a partner in a family partnership business having rental income from two big let out house properties in Calcutta. The value of this share interest was computed at Rs. 69,501, taking the book value of these properties at Rs. 1,62,727, as shown in the balance-sheet of the firm. The market value of these properties on 'income-capitalisation' method, by capitalising the net annual average maintainable rent of Rs. 97,130 (after allowing one-third of the annual rents of Rs. 1,45,695 as outgoings) at 12 times, was, however, Rs. 11,65,560. This value of Rs. 11,65,560 of the properties was to be adopted while computing the share interest of the deceased partner, instead of Rs. 1,62,727. The incorrect computation of the share interest of the deceased partner so made led to under-assessment of his estate by Rs. 2,00,566 and consequent undercharge of duty of Rs. 51,241.

The Ministry of Finance have accepted the audit objection in principle.

(iii) In the estate duty assessment, completed in March 1979 in respect of a deceased person (died in November 1963), the

assessing officer took the value of lands measuring 312.24 acres at Rs. 5,60,536 as per valuer's report dated 22-11-1971. The correct area of these lands was, however, 475.54 acres as shown in the account filed by the accountable person in March 1965. The omission to include the value of 163.30 acres of land valuing Rs. 4,32,500 resulted in under-assessment of the estate by Rs. 4,32,500 with consequent undercharge of duty of Rs. 57,382.

The audit paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

4.31 *Incorrect valuation of shares in companies*

(i) Under the provisions of the Estate Duty Act, the principal value of any property shall be estimated to be the price which it would fetch if sold in the open market at the time of the deceased's death.

In the estate duty assessment of an individual, who died on 26th December 1975, the value of 2,500 equity shares in a company was computed at the rate of Rs. 10.50 per share while the shares were quoted in the stock exchange at Rs. 24.50, as on 31st December 1975. The shares were, thus, undervalued by Rs. 35,000. This, along with other minor mistakes, resulted in short computation of the value of his estate by Rs. 38,000 and short levy of duty of Rs. 29,214.

The Ministry of Finance have accepted these mistakes.

(ii) In paragraph 4.24 of this Audit Report, the correct method of valuation of unquoted equity shares of companies for levy of gift-tax has been pointed out. The same method is applicable to valuation of unquoted equity shares for levy of estate duty, as the provisions in this regard in the Estate Duty Act are

similar. The extension of the provisions of a wealth-tax rule in regard to valuation of such shares to estate duty cases was withdrawn in October, 1974.

However, in the case of a deceased person, who died on 25th November, 1976, the assessing officer, while computing in August, 1978 the value of unquoted equity shares in companies, comprised in his estate, incorrectly applied the wealth-tax rule and based the valuation on the book value of the assets of the company and allowed discount for non-declaration of dividends by the company. The valuation of these shares was to be done on the basis of market value of assets of the company, including the value of its goodwill. In the absence of the market value of assets and goodwill of the company having been ascertained and placed on record, the under-assessment of estate duty of Rs. 27,510 resulting from incorrect allowance of discount of Rs. 91,700 alone was pointed out in audit in December 1979.

The Ministry of Finance have stated (December 1980) that the Controller of Estate Duty has been directed to look into the undervaluation.

4.32 *Incorrect computation of the principal value of estates*

(i) Under the provisions of the Estate Duty Act, 1953, property comprised in a gift, whenever made, in which the donor retains some interest or benefit, is deemed to pass on his death as part of his estate and is accordingly liable to estate duty. Blending by a deceased person of his self-acquired property with common property of the Hindu undivided family, of which he was a member, would be a disposition liable to estate duty as it amounted to gift from which the donor was not entirely excluded.

In the case of a person, who expired on 19th September, 1976, the principal value of the estate passing on his death, inclusive of the share of his lineal descendants in the property

of his Hindu undivided family, was assessed at Rs. 8,41,624 on 25th July, 1978. The property of the Hindu undivided family considered in the assessment comprised a house valued at Rs. 4,44,211 which had been the individual property of the deceased person but which, before his death, had been blended by him on 1st April, 1970 with the common property of the family, consisting of self, his three sons and wife. The effect of incorrectly treating the property as belonging to the Hindu undivided family was that his wife's 1/5th share was excluded from the estate and lineal descendants' 3/5th share in it was included in the principal value of his estate only for rate purposes. As the conversion of the self-acquired property into joint family property amounted to disposition in favour of relatives from which the donor was not completely excluded, its total assessable value (Rs. 3,44,211) (after allowing admissible exemption of Rs. one lakh for self-residence) was includible in the value of his estate. Omission to do so resulted in under-computation of the value of his estate and consequent short levy of estate duty of Rs. 57,896.

The Ministry of Finance have stated that the Controller is being requested to take necessary remedial action.

(ii) A male who, for the time being, is the sole surviving coparcener in a Hindu undivided family governed by the Mitakshara School of Hindu Law, is competent to alienate the coparcenary property in the same way and to the same extent as his separate property and the alienation cannot be questioned by the female members of the family or by a son, if any, born to or adopted by him subsequent to alienation. On the death of such a sole coparcener, the whole of his property including the coparcenary property, passes by succession to his heirs and, as such, the whole of his estate is assessable to estate duty. This well-settled position at law was laid down also in the Board's circular instructions issued in October 1959 and reiterated in July 1976.

A deceased *kartha* of a Hindu undivided family was a sole surviving coparcener and the family comprised him and his wife.

On his death on 1st August, 1974, the value of the common property of the family was computed as Rs. 4,53,732 in March 1979 and revised to Rs. 4,44,732 in May 1979. The principal value of the estate on the death of this sole coparcener was incorrectly computed at one-half of this value, *viz.* Rs. 2,22,366 instead of the whole of Rs. 4,44,732, in disregard of instructions of the Board. The incorrect computation of the principal value of the estate so made led to short levy of estate duty of Rs. 42,347.

The Ministry of Finance have accepted the audit objection.

(iii) In computing the principal value of the estate of a deceased person, who died on 1st March, 1975, the value of life insurance policies was taken as Rs. 2,83,920 as per the claim admitted by the Life Insurance Corporation of India. From the gross value of the estate an amount of Rs. 84,052 was deducted as loans raised by the deceased person on these policies. It was pointed out in audit (January 1980) that no deduction for the loans was allowable from the policy moneys since the claim admitted by the Corporation was the net amount payable after adjusting the outstanding loans. The deduction of Rs. 84,052 thus wrongly made resulted in short levy of duty of Rs. 25,135.

The audit paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

(iv) In determining the principal value of the estate of a deceased person at Rs. 3,67,518 in December 1978, an amount of Rs. 63,000 representing a fixed deposit made by him during his life-time was omitted to be included. This omission resulted in short levy of estate duty of Rs.15,753.

The Ministry of Finance have accepted the audit objection.

(v) In another estate duty case, the value of certain properties returned in the estate duty account filed by the accountable person on 30th March, 1978 was omitted to be included in the assessment completed on 20th December, 1978. The omission

resulted in short computation of the principal value of the estate by Rs. 52,400 with consequent short levy of duty of Rs. 13,100.

The Ministry of Finance have accepted the omission.

4.33 *Non-levy of interest*

Under the provisions of the Estate Duty Act, 1953, every person accountable for estate duty is required to file an account of the estate of a deceased person within six months of the date of his death. The Controller of Estate Duty is, however, empowered to extend this time-limit on certain terms *inter alia* including payment of interest at the rate of 6 per cent per annum. Further, estate duty in respect of an immovable property may, at the option of the person accountable, be allowed to be paid in instalments on payment of interest at the rate of 4 per cent per annum or any higher interest yielded by the property.

In the case of a deceased person (date of death : 1st July, 1965), the accountable person applied for extension of time to file the account of the estate and submitted the account on 25th March, 1966. In the assessment completed on 20th January, 1969, interest at the rate of 6 per cent per annum amounting to Rs. 62,022 for the period of extension allowed was levied and collected. In November 1972, however, on an application from the accountable person, this levy of interest was cancelled on the ground that the extension of time granted for filing of account had, in fact, not been communicated to the accountable person and the levy of interest was incorrect. Further, while cancelling the levy of interest on this technical ground, no action to levy penalty for belated filing of account was considered by the department.

In the same case, the principal value of the estate was assessed at Rs. 76,92,724, including immovable properties worth Rs. 76,11,206 and a demand for duty of Rs. 52,81,015 was raised which was payable before 24th February, 1969. In March 1969, the accountable person approached the Department seeking permission to pay part of the undisputed demand of

Rs. 17 lakhs, mainly referable to the immovable properties, in three annual instalments of Rs. 5 lakhs each in March each year with interest at six per cent per annum. The Controller acceded to this request. However, in September, 1972, the accountable person on the plea of difficulties in disposing of the immovable properties, requested the department to waive this levy of interest at the rate of 6 per cent per annum for delayed payment of duty. The department thereupon reduced the interest below even the prescribed minimum rate of 4 per cent per annum and charged interest at the rate of 1.50 per cent per annum amounting to Rs. 1,13,810. The correct amount of interest chargeable was Rs. 5,32,410 at the rate of 6 per cent or Rs. 3,54,940 at 4 per cent per annum, the minimum statutory rate.

The audit paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

4.34 *Mistakes in giving effect to appellate orders*

(i) In the estate duty assessment of a deceased person, who died in August 1967, the value of her interest in two settlements on trust was included in the principal value of her estate. In doing so, the estate duty liability arising on the death of a life-interest holder in one of the trusts was excluded. In January 1972, the Appellate Controller of Estate Duty held that the interest of the deceased in this trust was not includible in her estate. Consequently, the aforesaid estate duty liability was not referable to an asset includible in the estate of the deceased person and was not allowable as deduction. However, while giving effect to these appellate orders in June 1972, this estate duty liability was omitted to be disallowed. This omission led to under-assessment of the estate by Rs. 2,53,144 and short levy of estate duty of Rs. 1,26,572.

The Ministry of Finance have accepted the audit objection and stated that additional demand for duty of Rs. 1,28,958 has been raised.

(ii) While giving effect to certain appellate orders in the case of a deceased person, who died on 26th January, 1973, an annuity deposit was included in the principal value of his estate less by Rs. 27,462, the lineal descendants' share of Rs. 40,191 was omitted to be added for rate purposes and interest was not levied on delayed payment of demands of duty. These omissions resulted in short levy of duty of Rs. 45,504. On being pointed out in audit in March 1980, the department accepted these omissions in principle.

The audit paragraph was sent to the Ministry of Finance in September 1980; their reply is awaited (December 1980).

D—INTEREST-TAX

4.35 Under the provisions of the Interest-tax Act, 1974, the amount of interest, which accrues or arises to an assessee before the 1st day of August 1974, shall not be taken into account in computing the chargeable interest of the previous year. Accordingly, the chargeable interest of an assessee (a State Co-operative Bank) for the previous year from 1st July, 1974 to 30th June, 1975, relevant to the assessment year 1976-77, was to be computed after excluding the interest accrued or arisen for the month of July 1974. This was not done. Further, while computing the chargeable interest for the period from August 1974 to June 1975, the assessing officer calculated the gross chargeable interest (excluding the interest on Government securities exempt under the Act) for 11 months on proportionate basis with reference to the amounts received during the year as shown in the profit and loss account. In doing so, the deductions otherwise admissible towards duplication of interest, interest on call deposits and interest received from banks, were allowed for the whole year without restricting these deductions proportionately to 11 months. These mistakes resulted in an under-assessment of chargeable interest of Rs. 18,37,410 and of interest-tax of Rs. 1,28,619.

The Ministry of Finance have accepted the audit objection and stated (December 1980) that the assessment has been set aside for being done afresh.

NEW DELHI
The 21.2., 1981.

(R. S. GUPTA)
Director of Receipt Audit.

Countersigned

NEW DELHI
The 21-2, 1981.

(GIAN PRAKASH)
Comptroller and Auditor General of India.

MGIPF—413NAL/79—50,000—4-12-79.