REPORT

OF THE

COMPTROLLER AND AUDITOR GENERAL OF INDIA

FOR THE YEAR 1983-84

UNION GOVERNMENT (CIVIL)
REVENUE RECEIPTS
VOLUME II
DIRECT TAXES

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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 this separate volume. The Report is arranged in the following order :—

(i) Chapter I sets out statistical information and reviews on grant of refunds and outstanding audit objections.

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

(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.

VOLUME II

CHAPTER 1

GENERAL

1.01 *Receipts under various Direct Taxes*

The total proceeds from Direct Taxes for the year 1983-84 amounted to Rs. 4498.38* crores out of which a sum of Rs. 1188.21* crores was assigned to the States. The figures for the three years 1981-82, 1982-83 and 1983-84 are given below :—

(In crores of rupees)

		1981-82	1982-83	1983-84
020	Corporation Tax	1969.96	2184.51	2492.73
021	Taxes on Income other than Corporation Tax	1475.50	1569.72	1699.13
023	Hotel Receipts Tax	2.32	0.07	.
024	Interest Tax	.	265.47	177.91
028	Other Taxes on Income and Expenditure	231.67£	.	.
031	Estate Duty	20.31	20.38	26.46
032	Taxes on Wealth	78.12	90.37	93.31
033	Gift-Tax	7.74	7.71	8.84
	GROSS TOTAL	3785.62	4138.23	4498.38
Less share of net proceeds assigned to the States :				
	Income-tax	1016.88	1131.77	1171.64
	Estate Duty	16.50	15.98	16.57
	Hotel Receipts Tax	0.82	.	.
	TOTAL	1034.20	1147.75	1188.21
	Net Receipts	2751.42	2990.48	3310.17

The gross receipts under Direct Taxes during 1983-84 went up by Rs. 360.15 crores when compared with the receipts during

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

£Includes Rs. 231.63 crores on account of receipts under Interest tax. This tax was discontinued with effect from 1 March 1978 but reimposed with effect from 1 July 1980.

1982-83 as against an increase of Rs. 352.61 crores in 1982-83 over those for 1981-82. Receipts under Corporation Tax and Surtax registered an increase of Rs. 308.22 crores while receipts under "Taxes on income other than Corporation Tax" accounted for an increase of Rs. 129.41 crores.

1.02 *Variations between budget estimates and actuals*

(i) The actuals for the year 1983-84 under the Major heads 020—Corporation tax, 021—Taxes on Income, etc., 024—Interest Tax, 031—Estate Duty, 032—Taxes on Wealth and 033—Gift Tax exceeded the budget estimates.

The figures for the years from 1979-80 to 1983-84 under the various heads are given below :—

Year	Budget estimates	Actuals	Variation	Percentage of variation
1	2	3	4	5
			(In crores of rupees)	
020—Corporation Tax				
1979-80	1529.50	1391.90	(—)137.60	(—)8.99
1980-81	1515.00	1377.45	(—)137.55	(—)9.08
1981-82	1690.00	1969.96	279.96	16.56
1982-83	2382.00	2184.51	(—)197.49	(—)8.29
1983-84	2362.00	2492.73	130.73	5.54
021—Taxes on Income other than Corporation Tax				
1979-80	1247.10	1340.31	93.21	7.47
1980-81	1426.00	1439.93	13.93	0.98
1981-82	*1440.00	1475.50	31.50	2.18
1982-83	1562.75	1569.72	6.97	0.45
1983-84	1669.60	1699.13	29.53	1.75
024—Interest-Tax				
1982-83	220.00	265.47	45.47	20.67
1983-84	156.00	177.91	21.91	14.04

*Figures have been revised and Confirmed by the Ministry of Finance.

1	2	3	4	5
			(In crores of rupees)	
031—Estate Duty				
1979-80 . . .	12.00	14.05	2.05	17.08
1980-81 . . .	13.00	16.23	3.23	24.85
1981-82 . . .	15.00	20.31	5.31	35.40
1982-83 . . .	17.00	20.38	3.38	19.88
1983-84 . . .	19.00	26.46	7.46	39.26
032—Taxes on Wealth				
1979-80 . . .	60.00	64.47	4.47	7.45
1980-81 . . .	65.00	67.37	2.37	3.65
1981-82 . . .	66.00	78.12	12.12	18.36
1982-83 . . .	80.00	90.37	10.37	12.96
1983-84 . . .	90.00	93.31	3.31	3.67
033—Gift Tax				
1979-80 . . .	5.75	6.83	1.08	18.78
1980-81 . . .	6.25	6.51	0.26	4.16
1981-82 . . .	6.25	7.74	1.49	23.84
1982-83 . . .	6.75	7.71	0.96	14.22
1983-84 . . .	8.50	8.84	0.34	4.00

(ii) The details of variations under the heads subordinate to the major Heads 020 and 021 for the year 1983-84 are given below :—

1	Budget	Actuals	Increase (+)/ shortfall (—)	Percentage of variation
	2	3	4	5
			(In crores of rupees)	
020—Corporation Tax				
(i) Income-tax on companies	2300.00	2412.03	112.03	4.87
(ii) Surtax	54.00	66.48	12.48	23.11
(iii) Receipts awaiting transfer to other minor heads .	..	0.11	0.11	..
(iv) Other receipts . .	8.00	14.11	6.11	76.37
Total	2362.00	2492.73	130.73	5.54

1	2	3	4	5
			(In crores of	rupees)
021—Taxes on income other than Corporation Tax				
(i) Income-tax . . .	1453.30	1522.12	68.82	4.74
(ii) Surcharge . . .	203.30	159.51	(—)43.79	21.54
(iii) Receipts awaiting transfer to other minor heads .	..	1.46	1.46	..
(iv) Other receipts . .	13.00	16.04	3.04	23.38
(v) Deduct share of proceeds assigned to States . .	1140.05	1171.64	31.59	2.77
Total	529.55	527.49	(—) 2.06	0.39

1.03 *Analysis of collections*

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

(i) The break-up of total collections* of Corporation Tax, Surtax and Taxes on income other than Corporation Tax by pre-assessment and post-assessment, during the year 1983-84 as furnished by the Ministry of Finance, is as under :—

	(In crores of	Amount rupees)
1. Deduction at source		1053.70
2. Advance tax		2861.29
3. Self-assessment		275.77
4. Regular assessment		289.16

Besides, the Ministry of Finance have intimated tax collection of Rs. 288.01 crores representing Surcharge, Surtax and Other Receipts and Refunds of Rs. 576.99 crores.

*Figures furnished by the Ministry of Finance are provisional.

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

	Amount (In crores of rupees)
1. Salaries	332.48
2. Interest on securities	214.54
3. Dividends	130.96
4. Interest other than interest on securities	147.24
5. Payment to contractors and sub-contractors	170.98
6. Other items	57.50

(iii) Advance Tax—Tax payable and collected by way of advance tax during the year 1983-84 is as under :—

	Amount (In crores of rupees)
1. Tax payable by way of advance tax as per statements received, self-estimates or revised estimates filed and notices issued	2883.98
2. Tax collected out of (1) above	2495.79
3. Arrears out of (1) above on 31 March 1984	388.19

1.04 *Cost of collection*

(i) The expenditure incurred during the year 1983-84 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 :—

	Gross collection	Expenditure on collection
	(In crores of rupees)	
020—Corporation Tax		
1980-81	1377.45	6.78
1981-82	1969.96	7.64
1982-83	2184.51	9.02
1983-84*	2492.73	10.37
021—Taxes on income, etc.		
1980-81	1439.93	47.50
1981-82	1475.50	53.48
1982-83	1569.72	63.17
1983-84*	1699.13	72.60

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

†Figures furnished by the Ministry of Finance are provisional.

(ii) The expenditure incurred during the year 1983-84 in collecting other direct taxes, i.e., Taxes on Wealth, Gift-tax and Estate Duty together with the corresponding figures for the preceding three years is as under :—

	Gross collections (In crores	Expenditure on collections of rupees)
031—Estate Duty		
1980-81	16.23	1.21
1981-82	20.31	1.36
1982-83	20.38	1.60
1983-84*	9.89	1.84
032—Taxes on Wealth		
1980-81	67.37	4.22
1981-82	78.12	4.75
1982-83	90.37	5.62
1983-84*	93.31	6.45
033—Gift Tax		
1980-81	6.51	0.60
1981-82	7.74	0.68
1982-83	7.71	0.80
1983-84*	8.84	0.92

1.05 *Number of assessees*

(i) Income Tax

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

For the assessment year 1983-84 no income-tax was payable on a total income not exceeding Rs. 15,000 except in the case of specified Hindu undivided family, registered firms, co-operative society, local authority and company where a lower limit is applicable.

*Figures furnished by the Controller General of Accounts are provisional

(a) The total number of assessees in the books of the department was 49,32,094 as on 31st March 1984 as against 47,97,260 as on 31st March 1983. The break-up of the assessees on the said two dates was as under :—

	As on 31 March 1983	As on 31 March 1984
Individuals	36,11,938	36,38,075
Hindu undivided families	2,40,867	2,72,707
Firms	8,00,470	8,54,860
Companies	49,504	52,951
Others	94,481	1,13,501
Total	47,97,260*	49,32,094

(b) The number of trust assessees in the books of the department as on 31st March 1983 and 31st March 1984 included under "others" in sub-para (a) above were as follows :—

	As on 31 March 1983	As on 31 March 1984
(i) Public Charitable trusts	37,535	39,847
(ii) Discretionary trusts	10,076	11,687
Total	47,611*	51,534

*Figures furnished by the Ministry of Finance in January 1984 have been adopted.

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

	Individuals	Hindu undivided families	Firms	Companies	Others	Total
(i) Below taxable limit . . .	9,05,982	75,514	1,19,666	28,180	58,183	11,87,525
(ii) Above taxable limit but upto Rs. 25,000	17,36,551	1,17,891	3,16,538	10,343	26,609	22,07,932
(iii) Rs. 25,001 to Rs. 50,000 . .	7,57,408	53,852	2,41,373	4,132	15,784	10,72,549
(iv) Rs. 50,001 to Rs. 1,00,000 . .	2,06,947	16,539	1,27,649	3,520	9,572	3,64,227
(v) Rs. 1,00,001 to Rs. 5,00,000 .	30,227	8,841	47,709	3,785	3,151	93,713
(vi) Above Rs. 5,00,000 . . .	960	70	1,925	2,991	202	6,148
TOTAL . .	36,38,075	2,72,707	8,54,860	52,951	1,13,501	49,32,094

(ii) Wealth Tax

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

For the assessment year 1983-84 no wealth-tax was payable where the net wealth is less than Rs. 1.50 lakhs.

The number of wealth-tax assessees in the books of the department as on 31st March 1983 and 31st March 1984 were as follows :—

	As on 31 March 1983	As on 31 March 1984
Individuals	3,68,675	3,80,289
Hindu undivided families	54,614	56,832
Others	22	14
Total	4,23,311	4,37,135

(iii) Gift Tax

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

During the assessment year 1983-84 no gift-tax was payable where the value of taxable gifts did not exceed Rs. 5,000.

The number of gift-tax assessment cases for the years 1982-83 and 1983-84 were as follows :—

1982-83	58,103*
1983-84	65,966

(iv) Estate Duty

Under the provisions of the Estate Duty Act, 1953, in the case of every person dying after 15 October 1953, estate duty at rates fixed in accordance with Section 35 of the Act is levied

*Figures furnished by the Ministry of Finance are provisional.

upon the principal value of the estate comprised of all property settled or not settled including agricultural land and which passes on the death.

During the assessment year 1983-84 no estate duty was chargeable where the principal value of the estate passing on death, did not exceed Rs. 1,50,000.

The number of estate duty assessment cases for the years 1982-83 and 1983-84 were as follows :—

1982-83	37,575*
1983-84	35,892

1.06 *Public Sector Undertakings*

	Central Govt. under-takings	State Govt. under-takings
(1) No. of Public undertakings (including nationalised banks) out of the company assessees, assessed to tax during the financial year 1983-84	183	431
(2) Tax paid by these undertakings during the Financial year 1983-84		
	(In crores of rupees)	
(i) Advance tax	1197.73	20.12
(ii) Self-assessment tax	34.28	3.58
(iii) Regular tax paid in 1983-84 out of arrear and current demands	11.45	4.64
(iv) Surtax	33.00	0.78
(v) Interest tax	145.41	0.01
Total	1421.87	29.13

1.07 *Foreign company assessees**

(i) Cases where returns had been filed for the assessment year 1983-84 and assessments completed, as on 31st March 1984 :—

	Number	Amount (In crores of rupees)
(i) No. of foreign companies	79	
(ii) Income returned		12.82
(iii) Income assessed		13.58
(iv) Gross demand		4.65
(v) Demand outstanding out of (iv) above as on 31 March 1984		0.01
(vi) Tax paid upto 31 March 1984 (iv-v)		4.64

*Figures furnished by the Ministry of Finance are provisional.

(ii) Cases where returns had been filed for the assessment year 1983-84 but assessments were pending as on 31st March 1984 :—

	Number	Amount (In crores of rupees)
(i) No. of foreign companies . . .	247	
(ii) Income returned		106.24
(iii) Gross demand, being tax due on income returned		56.27
(iv) Demand outstanding out of (iii) as on 31 March 1984		5.94
(v) Tax paid upto 31 March 1984 (iii-iv) . .		50.34

(iii) Cases where no returns had been filed for the assessment year 1983-84 as on 31st March 1984 :—

No. of foreign companies	307

1.08 *Arrears of assessments*

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

(i) Income-tax including Corporation Tax

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

Financial Year	Number of assessments for disposal	Number of assessments completed				Number of assessments pending at the end of the year
		Out of current	Out of arrears	Total	Percentage	
1979-80 .	57,89,055	18,97,276	15,92,514	34,89,790	60.0	22,99,265
1980-81 .	65,91,180	18,12,511	22,22,702	40,35,213	61.2	25,55,967
1981-82 .	72,08,405	20,05,194	25,42,522	45,47,716	63.0	26,60,689
1982-83 .	70,15,368	20,19,664	24,15,450	44,35,114	63.2	25,80,254
1983-84	68,92,824	23,47,201	24,64,620	48,11,821	69.8	20,81,003

(b) Category-wise break-up of the total number of assessments completed during the years 1982-83 and 1983-84 was as under :—

	1982-83	1983-84
Scrutiny assessments	11,36,817	9,71,654
Summary assessments	32,98,297	38,40,167
Total	44,35,114	48,11,821£

(c) Status-wise break-up of income-tax assessments completed during the years 1982-83 and 1983-84 was as under :—

	1982-83	1983-84
(i) Individuals	33,84,436	36,55,895
(ii) Hindu undivided families	1,94,808	2,42,879
(iii) Firms	7,26,010	7,84,887
(iv) Companies	47,505	51,923
(v) Association of persons etc.	82,355	88,208
Total	44,35,114*	48,23,792£

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

	As on 31 March 1983	As on 31 March 1984
1979-80 and earlier years	48,681	19,445
1980-81	1,17,446	19,369
1981-82	6,71,180	1,62,867
1982-83	17,42,947	5,54,477
1983-84	..	13,25,344
Total	25,80,254*	20,81,502@

(e) Category-wise break-up of pending income tax assessments as on 31st March 1983 and 31st March 1984 was as under :—

	As on 31 March 1983	As on 31 March 1984
Scrutiny assessments	10,86,017	7,54,822
Summary assessments	14,94,237	13,26,181
Total	25,80,254	20,81,003@

*Figures furnished by the Ministry of Finance in January 1985 have been adopted.

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

(f) Status-wise and yearwise break-up of pendency of income-tax assessments in respect of various assessment years as on 31st March 1984 was as under :—

Status	1979-80 and earlier years	1980-81	1981-82	1982-83	1983-84	Total
(a) Company assessments	2416	1618	4474	17,772	35,319	61,599
(b) Non-company assessments	17,029	17,751	1,58,393	5,36,705	12,90,025	20,19,903
Total	19,445	19,369	1,62,867	5,54,477	13,25,344	20,81,502

The number of assessment cases to be finalised as on 31st March 1984 has decreased compared to that at the close of the previous year. The number of assessments pending as on 31st 1984 was 20,81,003 as compared to 25,80,254 as on 31st March 1983 and 26,60,689 as on 31st March 1982. Of the 20,81,003 of pending cases as many as 13,26,181 cases related to summary assessments.

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

(a) The total number of wealth-tax assessments completed during the years 1982-83 and 1983-84 were as under :—

	1982-83	1983-84
Individuals	3,76,240	4,06,671
Hindu undivided families	50,710	53,747
Others	1,558	1,505
Total*	4,28,508*	4,61,923

*Figures furnished by the Ministry of Finance in January 1985 have been adopted.

(b) The number of gift-tax assessments completed during the years 1982-83 and 1983-84 were as follows :—

	1982-83	1983-84
Individuals	72,172	80,177
Hindu undivided families	1571	2,059
Others	387	68
Total	74,130*	82,304

(c) The number of estate duty assessments completed during the years 1982-83 and 1983-84 were as under :—

1982-83	38,483
1983-84	40.165

The break-up of the estate duty assessments completed during the year 1983-84 according to certain slabs of principal value of estate was as under :—

Principal value of property	Number of assessments completed
(1) Exceeding Rs. 20 lakhs	12
(2) Between Rs. 10 lakhs and Rs. 20 lakhs	96
(3) Between Rs. 5 lakhs and Rs. 10 lakhs	645
(4) Between Rs. 1 lakh and 5 lakhs	6752
(5) Between Rs. 50,000 and Rs. 1 lakh	8012
(6) Below Rs. 50,000	24,648
Total	40,165£

(d) Assessment year-wise details of wealth-tax, gift-tax and estate duty assessments pending as on 31st March 1984 were as under :—

	Number of assessments pending		
	Wealth-tax	Gift-tax	Estate-duty
1979-80 and earlier years	11,721	2,709	8,940
1980-81	52,975	4,837	4,061
1981-82	79,007	6,558	5,194
1982-83	1,22,614	10,805	6,574
1983-84	2,26,435	19,184	9,708
Total	4,92,752	43,893@	34,477

*Figures furnished by the Ministry of Finance in January 1984 have been adopted.

£ Figures furnished by the Ministry of Finance are provisional.

@ The discrepancy in the "totals" is under verification by the Ministry of Finance.

(e) The number of assessments completed under the Companies (profits) Surtax Act 1964 during the years 1982-83 and 1983-84 were as under :—

Year	No. of assessments for disposal	No. of assessments completed	No. of assessments pending at the end of the year
1982-83	6407	1991	4416
1983-84	5963	1818	4145

(f) The year-wise details of assessments under Companies (Profits) Surtax Act, 1964, pending as on 31st March 1984 were as under :—

Year	Number of assessments
1982-83 and earlier years	**
1983-84	4191*

(g) The number of assessments completed under the Interest Tax Act, 1974 during the year 1982-83 and 1983-84 were as under :—

Year	No. of assessments for disposal	No. of assessments completed	No. of assessments pending at the end of the year
1982-83	362	70	292
1983-84	395	42	353

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

**Figures awaited from Ministry of Finance.

(h) The year-wise details of assessments under the Interest Tax Act, 1974 pending as on 31st March 1984 were as under :—

Year	No. of assessments
1982-83 and earlier years	*
1983-84	354**

1.09 *Arrears of tax demands*

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

(i) Corporation Tax and Income Tax

(a) The total demand of tax raised and remaining uncollected as on 31 March 1984 was Rs. 1810.03£ crores including Rs. 509.93 crores in respect of which the permissible period of 35 days had not expired as on 31 March and Rs. 15.77 crores claimed to have been paid but remaining to be verified|adjusted, Rs. 358.65 crores stayed|kept in abeyance and Rs. 23.22 crores for which instalments had been granted by the department and the Courts.

(b) Demands of Income-tax (including Corporation Tax) stayed as on 31 March 1984 on account of appeals and revision petitions were as under :—

	(In crores of rupees)
(1) By Courts	58.95
(2) Under Section 245F(2) (applications to Settlement Commission)	22.34
(3) By Tribunal	8.62

*Figures awaited from Ministry of Finance.

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

£ Figures furnished by the Ministry of Finance are provisional.

(4) By income-tax authorities due to :—	
(i) Appeals and revisions	209.18
(ii) Double income-tax claims	3.58
(iii) Restriction on remittances-Section 220(7)	1.92
(iv) Other reasons	54.06
Total	358.65*

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

	Corporation tax	Income-tax	Interest	Penalty	Total
				(In crores of rupees)	
Arrears of 1973-74 and earlier years	16.64	42.07	19.61	16.01	94.33
1974-75 to 1980-81	48.92	148.20	88.92	43.83	329.87
1981-82	28.90	63.22	36.41	13.80	142.33
1982-83	95.46	97.24	83.52	23.84	300.06
1983-84	429.41	265.35	221.90	26.78	943.44
Total	619.33	616.08	450.36	124.26	1810.03*

(d) The following table gives the break-up of the gross arrears of Rs. 1810.03 crores by certain slabs of income.

	Number of assessees	Total arrears of tax (In crores of rupees)
Upto Rs. 1 lakhs in each case	28,84,120	784.81
Over Rs. 1 lakh upto Rs. 5 lakhs in each case	8,015	160.55
Over Rs. 5 lakhs upto Rs. 10 lakhs in each case	1,866	137.15
Over Rs. 10 lakhs upto Rs. 25 lakhs in each case	623	99.50
Over Rs. 25 lakhs in each case	511	628.02
Total	28,95,135	1810.03

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

The following table gives the year-wise arrears of demands outstanding and the number of cases relating thereto under the

*Figures furnished by the Ministry of Finance are provisional.

three other direct taxes i.e., wealth-tax, gift-tax and estate duty as on 31st March 1984 :—

(Amount in lakhs of rupees)

	Wealth-tax		Gift-tax		Estate Duty	
	Number of cases	Amount	Number of cases	Amount	Number of cases	Amount
1979-80 and earlier years	56,596	5,594	17,838	567	8,842	839
1980-81	34,955	2,627	5,893	470	1,965	203
1981-82	42,744	2,318	7,283	177	2,796	373
1982-83	58,093	3,688	10,094	404	3,847	554
1983-84	1,02,329	5,502	21,964	1,103	8,392	1,476
Total .	2,94,697	19,729	63,072	2,721	25,802	3,445

(iii) Where an assessee defaults in making payment of tax, penalty and interest, the Income-tax Officer may issue a certificate to the Tax Recovery Officer for recovery of the demand by attachment and sale of the defaulter's moveable or immovable property, arrest of the defaulter and his detention in prison, appointing a receiver for the management of the defaulter's moveable and immovable property, etc. The tax demands certified to the Tax Recovery Officers and the progress of recovery to end of 1983-84 are given in the following table :—

Year	Demand Certified			Demand recovered during the year	Balance at the end of the year
	At the beginning of the year	During the year	Total		
				(In crores of rupees)	
1979-80 . .	703.96	323.65	1027.61	287.61	740.00
1980-81 . .	752.07	301.70	1053.77	258.58	795.19
1981-82 . .	861.58	400.24	1261.82	273.33	988.49
1982-83* . .	964.96	349.38	1314.34	376.72	937.62
1983-84£ . .	1208.28	3168.16	4376.44	1061.54	3266.91

Note : No. of certificates issued during the year 1983-84 : 8,65,947£

*Figures furnished by the Ministry of Finance in April 1984 have been adopted.

£Figures furnished by the Ministry of Finance are provisional.

1.10 *Appeals, Revision petitions and writs*

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

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

A tax payer can approach the Commissioner of Income-tax to revise an order passed by an Income-tax Officer or by an Appellate Assistant Commissioner within one year from the date of such orders. The Commissioner can also take up for revision an order which in his view is pre-judicial to the interest of revenue.

(i) Particulars of Income-tax appeals and revision petitions pending as on 31st March 1984 were as under :—

	Income-tax appeals with Appellate Assistant Commissioners/ Cs. I.T. (Appeals)	Income-tax revision petitions with Commissioners
Number of appeals/revision petitions pending :—		
(a) Out of appeals/revision petitions instituted during 1983-84.	1,23,209	5,990
(b) Out of appeals/revision petitions instituted in earlier years	1,14,004	8,978
Total	2,37,213	14,968

(ii) Particulars of wealth-tax, gift-tax and estate duty appeals and revision petitions pending as on 31 March 1984 were as under :—

	Appeals with Appellate Asstt. Commissioners/ Cs.I.T. (Appeals)			Revision petitions with Commissioners		
	W.T.	G.T.	E. D.	W.T.	G.T.	E.D.
Number of appeals/ revision petitions pending :—						
(a) Out of appeals/ revision petitions instituted during 1983-84 . .	33,193	1,373	1,959	1,153	53	..
(b) Out of appeals/ revision petitions instituted in earlier years . .	39,013	1,940	3,573	2,550	126	..
Total . .	72,206	3,313	5,532	3,703	179	..

(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 as on 31 March 1983 and 31 March 1984 respectively, with reference to the year of their institution was as under :—

	Appeals pending with Appellate Asstt. Commissioners/ Cs. I.T. (Appeals)		Revision petition pending with Commissioners	
Years of Institutions . .	31 March 1983	31 March 1984	31 March 1983	31 March 1984
1974-75 and earlier years .	1,038	893	296	268
1975-76	1,146	866	131	129
1976-77	2,101	1,617	205	204
1977-78	3,148	1,927	441	390
1978-79	6,113	3,469	675	522
1979-80	14,285	7,987	917	728
1980-81	23,147	12,899	1,765	1,380
1981-82	52,520	24,333	2,849	2,249
1982-83	1,43,123	60,033	4,906	3,108
1983-84	..	1,23,209	..	5,990
Total	2,46,621£	2,37,213*	12,185£	14,968

*The discrepancy in the "totals" is under reconciliation by the Ministry of Finance.

£The figures Furnished by the Ministry of Finance in December 1984 have been adopted.

(iv) Year-wise break-up of wealth-tax, gift-tax and estate duty appeal cases and revision petitions pending with Appellate Assistant Commissioners and Commissioners as on 31st March 1984 with reference to the year of their institution was as under:—

Year of Institution	Appeals pending with Appellate Asstt. Commissioners/Cs.I.T. (Appeals)			Revision petitions pending with Commissioners		
	W.T.	G.T.	E.D.	W.T.	G.T.	E.D.
1974-75 and earlier years	41	3	17	81	..	..
1975-76	138	3	39	30	1	..
1976-77	151	6	97	87	3	..
1977-78	354	20	219	102	3	..
1978-79	1062	69	218	121	3	..
1979-80	5626	289	395	332	20	..
1980-81	5207	394	390	457	17	..
1981-82	10,991	500	815	615	32	..
1982-83	15,443	656	1,383	725	47	..
1983-84	33,193	1373	1,959	1,153	53	..
TOTAL	72,206	3,313	5,532	3,703	179	..

(v) The following table gives details of appeals references disposed of during the years 1981-82, 1982-83 and 1983-84:—

	1981-82	1982-83	1983-84
(a) (1) Number of appeals filed before Appellate Assistant Commissioners/Cs.I.T. (Appeals)	2,31,574	2,34,804*	2,48,729
(2) Number of appeals disposed of by AACs/Cs. I. T. (Appeals) . . .	2,37,567	2,61,341*	2,60,206
(b) Number of appeals filed before Income-tax Appellate Tribunals :			
(1) by the assessee . .	24,850	25,088	28,544
(2) by the department . .	21,577	24,935	27,849
(c) Number of assessee's appeals decided by the Tribunal in favour of the assessees fully out of (b) (1) above . .	10,560	8,610	10,483
(d) Number of departmental appeals decided by the Tribunals in favour of the department fully out of (b)(2) above	4,491	3,208	4,511

*Figures furnished by the Ministry of Finance are provisional.

(e) Number of references filed to the High Courts :			
(1) by the assessees . .	1,890	1,992	1,595
(2) by the department . .	4,146	5,240	4,542
(f) Number of references in the High Courts disposed of in favour of the			
(1) assessees . . .	202	143	231
(2) department . . .	490	474	977
(g) Number of appeals filed to the Supreme Court			
(1) by the assessees . .	68	9	19
(2) by the department . .	219	25	31
(h) Number of appeals disposed of by the Supreme Court in favour of the			
(1) Assessees . . .	4	1	15
(2) department . . .	12	..	1

(vi) Writ petitions pending:—

	In Supreme Court	In High Courts	Total
1	2	3	4
(a) Number of writ petitions pending as on 31-3-1984 . .	335	4116	4451
(b) Out of (a) above :			
(i) Pending for over 5 years .	27	250	277
(ii) Pending for 3 to 5 years .	66	607	673
(iii) Pending for 1 to 3 years .	173	1668	1841
(iv) Pending up to 1 year	69	1591	1660

1.11 *Completion of Reopened and set aside assessment* £

(1) Income-tax

(a) Disposal of cases of assessments cancelled under section 146 of Income-tax Act.

Year	No. of assessments for disposal	No. of assessments completed	No. of assessments pending at the end of the year
1982-83 .	19,047	9,846	9,201
1983-84* .	20,496	11,801	8,705

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

£The figures supplied by the Ministry of Finance are provisional.

(b) Year-wise details* of cases of assessments cancelled under section 146 of Income-tax Act, 1961 (or under the corresponding provisions of the old Act) and which are pending finalisation on 31-3-1984.

Year	No. of cases
1974-75 and earlier years	513
1975-76	661
1976-77	405
1977-78	421
1978-79	713
1979-80	1157
1980-81	2313
1981-82	2169
1982-83	1072
1983-84	866
Total	10,290*

(c) Disposal of cases of assessment cancelled under section 263 of Income-tax Act.

Year	No. of assessments for disposal	No. of assessments completed	No. of assessments pending at the end of the year
1982-83*	1223	607	636
1983-84*	1639	721	916*

(d) Yearwise details of cases of assessments cancelled under section 263 of the Income-tax Act, 1961 (or under corresponding provisions of the old Act) and which are pending finalisation on 31-3-1984.

Year	No. of cases
1974-75 and earlier years	73
1975-76	33
1976-77	52
1977-78	75
1978-79	164
1979-80	223
1980-81	259
1981-82	131
1982-83	109
1983-84	126
Total£	1,247*

(e) Disposal of cases of assessment cancelled|set aside by AAC|CIT(A) under section 251 of Income-tax Act or by ITAT under section 254 of Income-tax Act.

Year	No. of assessments for disposal	No. of assessments completed	No. of assessments pending at the end of the year
1982-83*	10,404	4,767	5,787
1983-84*	11,365	5,416	5,991

*The discrepancy in the figures is under reconciliation by the Ministry of Finance.
£The discrepancy in "totals" is under reconciliation by the Ministry of Finane.

(f) Year-wise details* of cases of assessment set aside by the Appellate Assistant Commissioner|CIT (Appeals) under section 251 of the Income-tax Act, 1961 (or under the corresponding provisions of the old Act) by the Appellate Tribunal under Section 254 of the Income-tax Act, 1961 (or under the corresponding provisions of the old Act) where fresh assessments have not been completed as on 31-3-1984.

Assessment year	Set aside A.A.Cs/CIT (A) No. of cases	Set aside by Appellate Tribunal No. of cases
1974-75 and earlier years	727	124
1975-76	465	116
1976-77	420	74
1977-78	526	77
1978-79	733	92
1979-80	2037	80
1980-81	1022	66
1981-82	655	43
1982-83	514	24
1983-84	789	52
Total	6,888	748

(ii) Wealth-tax and Gift-tax

(a) Disposal of cases of assessment cancelled under Section 25 of Wealth-tax Act, 1957 and under Section 24(2) of the Gift-tax Act, 1958.

Year	No. of assessments for disposal		No. of assessments completed		No. of assessments pending at the end of the year	
	WT	GT	WT	GT	WT	GT
1982-83*	1145	8	112	12	1038	173
1983-84*	1368	14	208	11	1174	6

(b) The year-wise details* of assessments cancelled under section 25 of the Wealth-tax Act, 1957 and under Section 24(2) of the Gift-tax Act, 1958 which were pending finalisation as on 31st March 1984 were as follows:

Assessment year	No. of cases	
	WT	GT
1974-75 & earlier years	437	.
1975-76	234	.
1976-77	256	.
1977-78	71	1
1978-79	61	.
1979-80	30	.
1980-81	18	.
1981-82	17	.
1982-83	18	2
1983-84	54	.
Total£	1166	3

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

(e) Disposal of cases of assessments set aside by the Appellate Assistant Commissioner|Commissioner (Appeals)| Appellate Tribunal under Section 23(5)|24(5) of the Wealth-tax Act, 1957, Section 22(5)|23(5) of the Gift-tax Act, 1958 and Section 62(5)|63(5) of the Estate Duty Act, 1953.

Year	No. of assessments for disposal			No. of assessments completed			No. of assessments pending at the end of the year		
	WT	GT	ED£	WT	GT	ED£	WT	GT	ED£
1982-83* . .	2,689	25		852	13		1834	24	
1983-84* . .	3,768	83		1218	24		2532	67	

(d) The year-wise details* of assessments set aside by the Appellate Assistant Commissioner|Commissioner (Appeals)| Appellate Tribunal under Section 23(5)|24(5) of the Wealth-tax, 1957, Section 22(5)|23(5) of the Gift-tax Act, 1958 and section 62(5)|63(5) of the Estate Duty Act, 1953, where fresh assessments had not been completed as on 31 March 1984 were as under:—.

Assessment years	Set aside by AACs/ Commissioners (Appeals) Number of cases			Set aside by Appellate Tribunal Number of cases		
	WT	GT	ED	WT	GT	ED
1974-75 & earlier years . .	1149	25	9	136	2	2
1975-76	338	4	2	45	.	.
1976-77	354	7	1	34	.	.
1977-78	359	4	2	22	.	1
1978-79	314	5	1	16	6	1
1979-80	198	3	2	6	.	1
1980-81	149	6	4	2	1	..
1981-82	98	1	10	.	1	2
1982-83	64	1	9	.	.	1
1983-84	172	2	37	12	.	3
TOTAL . . .	3,195	58	77	273	10	11

1.12 *Reliefs and Refunds*

Where the amount of tax paid exceeds the amount of tax payable the assessee is entitled to a refund of the excess. If the refund is not granted by the department within three months from the end of the month in which the claim is made, simple interest at the prescribed rate becomes payable to the assessee on the amount of such refund (vide Section 237 read with Section 243 of the Income-tax Act).

*The discrepancy in the figures is under reconciliation by the Ministry of Finance
£ Figures awaited from Ministry of Finance.

(i) (a) The particulars of cases of refunds for which claims were made, the claims settled and the balance outstanding during 1983-84.

Financial year	Opening Balance	Claims received during the year	Total	No. of refunds made	Balance outstanding
1979-80 . .	10,843	1,25,927	1,36,770	1,21,501	15,269
1980-81 . .	15,269	1,33,691	1,48,960	1,31,584	17,376£
1981-82 . .	17,506£	1,91,587	2,09,093	1,93,660	15,433
1982-83 . .	15,433	1,34,306	1,49,739	1,22,680	27,059£
1983-84 . .	16,543£	1,50,697	1,67,240	1,37,095	29,146£

(b) Year-wise analysis of the balance claims as on 31 March 1984.

Financial year in which application was made	No. of case pending
1980-81 and earlier years	20
1981-82	60
1982-83	3,202
1983-84 . .	25,864
TOTAL	29,146

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

The particulars of assessment pending revision, revisions actually made and the no. of cases of assessment outstanding as on 31 March 1984.

Financial year	Opening balance	Assessment for revision during the year	Total	No. of assessments revised out of col. 4	Number of assessments which resulted in refunds as a result of revision out of col. 5	Assessments pending revision
1	2	3	4	5	6	7
1979-80	6,528	1,13,926	1,20,454	1,11,132	50,891	9,322£
1980-81	9,240£	1,04,447	1,13,687	1,06,771	50,104	6,916£
1981-82	6,961£	1,04,114	1,11,075	1,05,296	20,700	5,779
1982-83	5,779	91,631	97,410	90,387	33,963	7,023£
1983-84	7,554	78,257	85,811	77,600	29,178	7,888£

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

(b) Year-wise analysis£ of balance cases as on 31 March 1984.

Financial year	No. of cases pending
1980-81 and earlier years	439
1981-82	429
1982-83	3,362
1983-84	3,742
TOTAL	7,972

(iii) Grant of Refunds

The Central Board of Direct Taxes issued instructions in July 1980 regarding preparation of refund vouchers|advice notes, watching their encashment and their accountal, for compliance by field officers. These instructions have been issued primarily to prevent issue and encashment of fradulent refund vouchers.

The procedures applicable in respect of issue of refund vouchers are as under :

For refunds upto Rs. 999 :

The refund vouchers will consist of three foils. The first foil will remain in the Refund Voucher Book as office copy. The second and third foils, will be sent to the assessee for presenting to the bank, indicated therein, for encashment. After payment, the bank will send the third foil along with a Bank Refunds scroll to the designated officer, who in turn will forward it to the concerned Income-tax Officer. The second foil along with another copy of scroll will be sent to the Zonal Accounts Officer.

For refund of Rs. 1,000 and above :

Here the refund vouchers will consist of only two foils of which the first foil will remain in the refund voucher book and the second foil will be issued to the assessee for presenting it to the bank for encashment. An advice note bearing the same number as that of the Refund Voucher is prepared, signed and simultaneously issued to the bank on which the Refund Voucher is drawn. The first foil of the Advice Note will remain in the book and the second and third foils are sent to the bank. The bank on

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

presentation of the refund voucher would tally the amount with that noted in the Advice Note before honouring it. After making the payment, at the end of the day, the Bank will forward the third for along with a scroll to the designated officer who will forward it to the concerned Income-tax Officer. The paid refund voucher, the second foil of the Advice Note along with another copy of the scroll are sent to the Zonal Accounts Officer concerned.

The observance of these instructions and the disposal of Refund claims by the field offices were generally reviewed in Audit in 1983-84 by test check of departmental records for the years 1980-81 to 1982-83. The results of the review are indicated below :

(a) *Writing of Refund Vouchers*

It is laid down that after the refund voucher is written up by a Clerk or a Tax Assistant, it will be checked by a Supervisor or a Head Clerk before the same is put up to the Income-tax Officer for final check and signature. The person who writes the refund vouchers and the one who checks the same, will have to put their signatures (with names in brackets) on the office copies of the refund vouchers and advice notes.

This procedure is not being observed in most of the Income-tax Wards, as will be evident from the following table :

Sr. No.	Commissioners Charges	No. of wards test checked	No. of wards not complying with Board's instructions
1.	Bombay	180	150
2.	Calcutta	58	54
3.	Madhya Pradesh	13	9
4.	Rajasthan	24	23
5.	Kerala	18	18
6.	Gujarat	56	21
7.	Haryana	9	9
8.	Himachal Pradesh	5	5
9.	Delhi	37	37
10.	Karnataka	12	12

In 24 wards relating to five Commissioners' charges in Punjab the names of writer and checker were indicated only on 293 refund vouchers out of 13,291 refund vouchers issued during 1982-83. In Andhra Pradesh, in 53 wards the names of writer and checker were indicated only on 4,715 refund vouchers out of 24,206 vouchers issued during 1982-83.

(b) *Tallying of Paid Vouchers with office copies*

In order to help in detecting the encashment of bogus Refunds, specific checks are laid down. In case of refunds upto Rs. 999, on receipt of the third foil of the refund voucher, the Clerk or the Tax Assistant concerned will tally the amount paid with the office copy (first foil) of the refund voucher and also write the date of encashment in the space provided in the office copy. In regard to refunds of Rs. 1,000 and above, the Income-tax Officer himself on receipt of the third foil of the Advice Note has to tally the amount paid with the office copy of the refund voucher and also write out the date of encashment in the space provided in the office copy.

Omission to verify and tally the amount of refund already made with that shown in the office copy and the omission to indicate the date of encashment of the refund in the office copy, were noticed extensively. The following table summarises the results of test check by Audit :

Sr. No.	Commissioners Charge	No. of wards test checked	No. of wards where tallying of paid vouchers with office copy was not done
1.	Bombay	180	149
2.	Calcutta	58	54
3.	Madhya Pradesh	13	11
4.	Bihar	6	6
5.	Rajasthan	24	22
6.	Gujarat	56	32
7.	Punjab	24	24
8.	Haryana	9	8
9.	Himachal Pradesh	5	5
10.	Delhi	37	37
11.	Karnataka	12	12

In Andhra Pradesh, in 53 wards selected for check the paid vouchers were not tallied with the office copy of the refund vouchers in 14,788 cases of refund of Rs. 282.56 lakhs out of 24,206 cases of refunds for Rs. 496.40 lakhs authorised during 1982-83.

In Kerala, in 18 wards, selected for check the paid vouchers were not tallied with the office copy of refund vouchers in 3,905 cases of refund of Rs. 143.21 lakhs out of 5,091 cases of refunds for Rs. 205.11 lakhs authorised during 1982-83.

(c) *Quarterly verification of receipt of paid vouchers*

As a further check for detecting encashment of bogus refunds, the Income-tax Officer is required to make a quarterly verification from the office copies of the refund vouchers as well as the relevant entries in the Demand and Collection Register to find out the cases where the paid foils of refund voucher have not been received upto six months from the date of issue of refund voucher. In such cases, the Income-tax Officer will have to consult the records of the Central Treasury Units etc. and if necessary approach the concerned bank to ascertain the position about the encashment of the relevant refund vouchers to ensure that there has been no fradulent payment.

Again extensive failure to conduct such quarterly verification was noticed as will be evident from the results of test check tabulated below :

Sr. No.	Commissioners Charge	No. of wards test checked	No. of wards where quarterly verification was not done
1.	Bombay	180	127
2.	Calcutta	58	58
3.	Assam	9	9
4.	Madhya Pradesh	13	13
5.	Bihar	6	6
6.	Rajasthan	24	24
7.	Gujarat	56	12
8.	Punjab	24	22
9.	Haryana	9	9
10.	Andhra Pradesh	53	47
11.	Himachal Pradesh	5	5
		12	12
		12	12

It may be mentioned that as per records of the wards test checked in respect of 12,587 refund vouchers for amount of Rs. 259.97 lakhs issued during 1980-81 to 1982-83 in 5 units (as per details below) paid vouchers were not available on record. As such it cannot be said that they have been encashed. The linking of refund vouchers issued with relevant paid vouchers is a very important check to detect fraudulent refund vouchers.

Units	No. of wards test checked	Number	Refunds vouchers for which paid vouchers are not available (Amount in lakhs of rupees)
Calcutta	58	1129	105.72
Rajasthan	24	676	20.58
Gujarat	27	1315	13.04
Punjab	24	4757	49.01
Andhra Pradesh	53	4710	71.62
		12,587	259.97

In an Income-tax Ward in Tamil Nadu three refund voucher forms and corresponding advice notes were removed from respective refund orders/advice books and refund orders totalling to Rs. 1,26,278 were issued under the signature of a 'fictitious' Income-tax Officer, using stolen seal of one of the Income-tax Officers, favouring a 'fictitious' assessee. The refunds were encashed in December 1981. The Government suffered a loss of Rs. 1,26,278.

The fraud came to the notice of the Department on 22nd January 1982. A case was registered with Central Bureau of Investigation who finalised their report on 31st December 1983, recommending regular departmental action for major penalty against a staff officer of the Reserve Bank of India and an Assistant in the concerned Income-tax Ward and for minor penalty against the Income-tax Officer of the concerned ward. Further action is pending (September 1984).

(d) *Maintenance of Daily Tally Register (Refunds)*

On receipt of distribution Memo along with copies of refund advices from the District Collection Unit/Local Treasury Unit (in places where more than one Income-tax Officer functions) the Income-tax Officer should record the particulars of the Memo

and advice notes and the amount involved in them in a register called Daily Tally Register (Refunds) and segregate the refunds according to income-tax, wealth-tax and gift-tax. After noting the refunds in the respective Daily Refund Register, and the Demand and Collection Register, the Income-tax Officer has to indicate total number of refund advices and the amount thereof in respect of each tax as entered in the Daily Collection Register, in the Daily Tally Register and ensure that action had been taken on all refund advices received in his office.

This important register was not maintained in 125 wards out of 180 in 20 Commissioners' charges in Bombay, in 48 out of 58 wards in 15 Commissioners' charges in Calcutta, in 8 wards in Assam, in 11 wards out of 13 in Madhya Pradesh, in 6 wards in Bihar, in 17 out of 24 wards in 2 Commissioners' charges in Rajasthan, in 40 wards out of 56 relating to 6 Commissioners' charges in Gujarat, in 17 wards out of 24 in 5 Commissioners' charges in Punjab, in 9 wards in Haryana, in 37 wards out of 53 in Andhra Pradesh, in 5 wards of Himachal Pradesh, 32 wards out of 37 in Delhi and 11 wards out of 12 wards in Karnataka.

(c) *Maintenance of Register of Refund Applications*

(1) In order to ensure prompt disposal of refund applications, a Register of Refund Application in the prescribed form is required to be maintained in each office. The Income-tax Officer should personally review this register periodically.

It was noticed in Audit that in 9 wards in Assam, 13 wards in Madhya Pradesh, 6 wards in Bihar, 5 wards in Rajasthan, 31 wards in Gujarat, 15 wards in Punjab, 9 wards in Haryana, 5 wards in Himachal Pradesh, 12 wards in Orissa, 57 wards in Calcutta and 12 wards in Karnataka, the control Register was not maintained. In the absence of these it was not possible to ascertain the number of pending refund claims and their age.

(2) The number of refund applications pending on 31 March of the five years 1980 to 1984, as per the figures furnished by the Ministry are—

March ending	No. of applications
1980	15,269
1981	17,376
1982	15,433
1983	27,059
1984	25,146

In the absence of the prescribed register in many income-tax wards, the veracity of figures cannot be verified.

(f) *Delay in authorisation of Refunds due*

Where the refund is delayed beyond three months, Government have to pay interest at 12 per cent per annum (15 per cent per annum from 1st October 1984) on the amount of refund due from the day following the expiry of 3 months to the day on which the refund is granted.

A review of refund vouchers issued during the three years 1980-81 to 1982-83 in selected wards of certain charges disclosed refunds amounting to Rs. 284.59 lakhs (4,133 refunds vouchers) had been authorised after delays ranging from six months to more than three years. The details are as under :

Refund authorised after delay of—

Charges	6 months to 1 year		1 year to 3 years		More than 3 years	
	(Amount in lakhs of Rupees)					
	Items	Amount	Items	Amount	Items	Amount
1. Bombay	2657	139.39	185	15.89	45	1.79
2. Calcutta	483	108.30	351	9.76	57	1.63
3. Others	187	1.71	157	5.97	11	0.15
Total .	3327	249.40	693	31.62	113	3.57

Such interest paid, on account of delay in authorising refunds during the five year period 1979-80 to 1983-84 is as below**

Year	Amount (Rupees in lakhs)
1979-80	103.18
1980-81	239.18
1981-82	254.99
1982-83	289.27
1983-84	564.78

CONCLUSION :

(1) Instructions of the Central Board of Direct Taxes also require that the Inspecting Assistant Commissioners should in the course of periodical inspections check that the system of issuing refunds and the various checks prescribed are being strictly adhered to. The Test Check in audit had, however, shown that the procedure evolved by the Central Board of Direct Taxes in July 1980 to safeguard against bogus or fradulent refunds etc. remains largely to be implemented by the field formations.

(2) There is no control whatsoever in regard to timely and expeditious disposal of refund claims as is evident from non-maintenance of Register of Refund application and heavy interest payments on belated refund authorisations.

This review was sent to the Ministry of Finance in October 1984; their reply is awaited. (November 1984).

1.13 Interest*

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

The particulars of interest levied and interest paid by Government under different provisions of the Act during the year 1983-84 are given below :—

1	No. of assessments 2	Amount (In crores of rupees) 3
(a) The total amount of interest levied under various provisions of the Income-tax Act . . .	9,49,751	323.00
(b) Of the amount of interest levied, the amount :		
(1) Completely waived by the department .	16,739	13.39
(2) Reduced by the department . . .	1,53,900	122.31
(3) Collected by the department . . .	3,11,006	38.91
(c) The total amount of interest paid :		
(1) On advance tax paid in excess of assessed tax	1,29,575	19.47
(2) On delayed refunds	1,743	0.33
(3) Where no claim is needed for refund . .	7,923	7.47

1.14 Cases Settled by Settlement Commission

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

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

*Figures furnished by the Ministry of Finance are provisional.

(i) Income-tax

Financial year	No. of cases for disposal	No. of cases disposed of	Percentage	Pending cases
1979-80	1,189	210	17.66	979
1980-81	1,276	294	23.04	982
1981-82	1,231	159	12.91	1,072
1982-83	1,430	186	13.00	1,244
1983-84	1,799	224	12.45	1 575

(ii) Wealth-tax

Financial year	No. of cases for disposal	No. of cases disposed of	percentage	Pending cases
1979-80	489	61	12.47	428
1980-81	497	69	13.88	428
1981-82	506	86	16.99	420
1982-83	551	47	8.52	504
1983-84	702	92	13.1	610

1.15 Penalties and prosecutions*

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

(i) Income Tax

A. Penalties

(a) No. of penalty orders passed under section 271(1)(c) during 1983-84		36,120
(b) Concealed income involved in (a) above	Rs.	15.64 Crores
(c) Total amount of penalty levied in (a) above :		
(i) No. of orders		16,526
(ii) Amount	Rs.	9.10 Crores

*Figures furnished by the Ministry of Finance are provisional.

(d) Total amount of penalty collected in (c) above :

(i) No. of orders			1,602
(ii) Amount	Rs.	0.68	Crores
(e) No. of penalty orders passed under other sections of the Act during 1983-84			6,39,391
(f) Income involved in (e) above	Rs.	101.79	Crores
(g) Total amount of penalty levied in (e) above :			
(i) No. of orders			2,18,647
(ii) Amount	Rs.	19.59	Crores
(h) Total amount of penalty collected in (g) above :			
(i) No. of orders			43,294
(ii) Amount	Rs.	3.92	Crores

B. Prosecutions

(a) No. of prosecutions pending before the courts on 1-4-1983	3,194
(b) No. of prosecution complaints filed during 1983-84 under Sections 276C, 276CC, 276D, 277 and 278	1,541
(c) No. of prosecutions decided during 1983-84	92
(d) No. of convictions obtained in (c) above.	38
(e) No. of cases which were compounded before launching prosecutions	67
(f) Composition money levied in such cases (e) above	Rs. 6.15 lakhs

(ii) Wealth-tax and Gift-tax

A. Penalties

	Wealth-tax	Gift-tax
(a) No. of penalty orders passed under section 18(1)(c)/17(1)(c) during 1983-84	6,827	360

(b) Amount of concealed net wealth/value of gift involved in (a) above (in lakhs of rupees)	1275.88	7.80
(c) Total amount of penalty levied in (a) above :		
(i) No. of orders . .	1579	55
(ii) Amount (in lakhs of rupees)	375.00	11.23
(d) Total amount of penalty colected in (c) above :		
(i) No. of orders	149	3
(ii) Amount (in lakhs of rupees)	1.66	..
(e) No. of penalty orders passed under other sections during 1983-84	57,352	4,725
(f) Amount of net wealth/value of gift involved in (e) above (in lakhs of rupees)	4679.04	69.85
(g) Total amount of penalty levied in (e) above :		
(i) No. of orders	15,465	985
(ii) Amount (in lakhs of rupees)	379.66	4.84
(h) Total amount of penalty collected in (g) above :		
(i) No. of orders . .	2251	260
(ii) Amount (in lakhs of rupees)	13.27	1.15

B. Prosecutions

(a) No. of prosecutions pending before the courts on 1-4-1983	269
(b) No. of prosecution complaints filed during 1983-84 under Sections 35A, 35B, 35C, 35D and 35F	151
(c) No. of prosecutions decided during 1983-84 . .	..
(d) No. of convictions obtained in (c) above . . .	.
(e) No. of cases which were compounded before launching prosecutions	..
(f) Composition money levied in such cases (e) above (in lakhs of rupees)	

1.16 *Searches and Seizures**

Sections 132, 132A and 132B of the Income-tax Act, 1961 provide for search and seizure operations. A search has to be authorised by a Director of Inspection, Commissioner of Income-tax or a specified Dy-Director of Inspection or Inspecting Assistant Commissioner. Where any money, bullion, jewellery or other valuable article or thing is seized, the Income-tax Officer has, after necessary investigations, to make an order with the approval of the I.A.C. within 90 days of the seizure, estimating the undisclosed income in a summary manner on the basis of the material available with him and calculating the amount of tax on the income so estimated, specifying the amount that will be required to satisfy any existing liability and retain in his custody such assets as are, in his opinion sufficient to satisfy the aggregate of the tax demands and forthwith release the remaining portion, if any, of the assets to the person from whose custody they were seized. The books of account and other documents cannot be retained by the authorised officer for more than 180 days from the date of seizure unless the Commissioner approves of the retention for a longer period.

Searches and Seizures

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

	No. of assessees	No. of assessments
1981-82	1683	4,434
1982-83	3,070	5,692
1983-84	1,951	3,536
(b) No. of search cases in which assessments were awaiting completion at the beginning of the year 1983-84:		
(1) No. of assessees	5107	
(2) No. of assessments	10,495	
(c) No. of search cases in which assessments were completed during the year 1983-84:		
(1) No. of assessees	2,194	
(2) No. of assessments	4,165	
(d) (A) No. of search cases in which assessments are awaiting to be completed at the end of the year 1983-84:		
(1) No. of assessees	4,570	
(2) No. of assessments	9,193	

*The figures furnished by the Ministry of Finance are provisional.

(B) Number out of (A) above, which are pending for more than 2 years after the date of search :	
(1) No. of assessees	1,439
(2) No. of assessments	2,970
(e) Total concealed income assessed in cases referred to in item (c) above :	
(1) No. of cases	1,044
(2) Amount	Rs. 32.83 Crores
(f) Penalty levied for concealment of income in search cases during the year (irrespective of whether assessments are completed in this year or earlier)	
(1) No. of cases	167
(2) Amount	Rs. 9.89 Crores
(g) No. of search cases in respect of which prosecution was launched in the Court during the year 1983-84 (irrespective of whether assessments are completed in this year or earlier) :	243
(h) No. of convictions obtained during the year 1983-84	23
(i) No. of cases where no concealment or tax evasion found on completion of assessments	1150
(j) Total amount of cash, jewellery, bullion and other assets seized during the year 1983-84 (approximate value) :	
(1) Cash	Rs. 6.63 crores
(2) Bullion and jewellery	Rs. 9.81 crores
(3) Others	Rs. 11.55 Crores
TOTAL	Rs. 27.99 Crores
(k) No. of search cases in respect of which summary assessment orders under section 132(5) of the Income-tax Act were passed during the year 1983-84	525
(l) Amount of undisclosed income determined in the orders under section 132(5) referred to in item (k) above	Rs. 89.83 Crores
(m) (1) Value of assets retained as a result of orders passed under section 132(5) referred to in item (k) above	Rs. 17.18 Crores

(2) Value of assets returned as a result of orders passed under section 132(5) referred to in item (k) above	Rs. 13.29 Crores
(n) Amount of cash, jewellery, bullion and other assets held on 31-3-1984 irrespective of the year of search :	
(1) Cash	Rs. 10.55 Crores
(2) Bullion and jewellery	Rs. 19.04 Crores
(3) Others	Rs. 15.15 Crores
TOTAL	Rs. 44.74 Crores
(o) The break up of the amount at Cash, Jewellery, bullion and other assets held on 31-3-1984	
(i) Over 5 years	Rs. 4.21 Crores
(ii) Between 3 to 5 years	Rs. 8.65 Crores
(iii) Below 3 years	Rs. 31.88 Crores
Total	Rs. 44.74 Crores
(p) Arrangements made for the safe custody of the assets still held and for their physical verification	Cash is deposited in the personal Deposit Account of the Commissioners of Income-tax in the Reserve Bank of India. Other valuables are kept either in well guarded strong rooms in the office building or in the treasuries or in Bank vaults, etc.

(ii) The Central Board of Direct Taxes have issued instructions in August 1965 that money seized should be credited to Personal Deposit Account of the jurisdictional commissioner in a Government Treasury with utmost expedition. Reiterating these instructions in November 1974 the Board stated that where it is desired to preserve the identity of the seized currency notes from the point of prosecution, the Commissioner may after consultation with the Prosecuting Counsel retain the currency in original form and record reasons for doing so. The packages containing the currency notes should then be kept in safe custody of a bank|treasury.

Finding delays ranging from 2 to 3 years in remitting cash running into lakhs of rupees seized in course of search, the Public Accounts Committee recommended in their 79th Report (6th Lok Sabha) (1977-78), that a firm time limit should be laid down in the Income-tax Rules 1962. The Central Board of Direct Taxes, however, once again reiterated their earlier instructions for expeditious remittance of cash seized to Govern-

ment account in January 1978|August 1978. The Board proposed to watch strict observance of their instructions through monthly reports from the Commissioners.

As on 31st March 1983, the cash that remained to be taken to Government account in 84 cases of seizure was Rs. 90.09 lakhs as shown below :

Year of seizure	No. of cases	Amount (Rs. in lakhs)
1978-79	5	4.58
1979-80	10	5.46
1980-81	6	2.45
1981-82	12	17.58
1982-83	51	60.02
	84	90.09*

(iii) A search was conducted by the Income-tax Department in July 1956 in the business premises of a registered firm. The department issued notices to the assessee firm in March 1965 and July 1966 i.e. after about 10 years from the date of search to file its returns of income for the assessment years 1950-51, 1951-52, 1952-53 and 1956-57. In response to the notices, the assessee filed the returns of income for the assessment years 1950-51 to 1952-53 only in April 1970 and did not file any return for the assessment year 1956-57. The Income-tax Officer made *exparte* assessments in March 1971 for the assessment years 1950-51 to 1952-53 and in December 1968 for the assessment year 1956-57 on a total income of Rs. 1,55,94,855, Rs. 1,43,35,373, Rs. 57,86,816 and Rs. 12,51,286 respectively. The said *exparte* assessments were reopened in July 1973 for the assessment years 1950-51 to 1952-53 under the orders of the Appellate Assistant Commissioner, and for the assessment year 1956-57 in October 1970 by the Income-tax Officer himself.

The department made fresh assessments, again, *exparte* in December 1982, after about nine years, with the income as originally assessed. These assessments were again cancelled and reopened by the department in January 1983. Fresh assessments are yet to be made (August 1984).

On the inordinate delay in finalising the assessments being pointed out in audit in November 1983, the department pleaded

*Figures furnished by the Ministry of Finance.

helplessness attributing the delay to frequent transfer of jurisdiction of the case, frequent changes in assessing officers and non-cooperation by the assessee. Considerable revenues of the exchequer are in jeopardy.

The paragraph was forwardel to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

1.17 *Acquisition of Immovable Properties*

1.17.01 Chapter XXA of the Income-tax Act, 1961, introduced with effect from 15 November 1972, empowers the Central Government to acquire an immovable property, where such property is transferred by sale or exchange and the true consideration for such transfer is concealed with the object of evading tax. The scope of these provisions has been extended through the Income-tax (Amendment) Act, 1981 with effect from 1 July 1982, to cover :

(a) transfers of flats or premises owned through the medium of co-operative societies and companies;

(b) agreements of sale followed by part performance viz. by actual physical possession of the property by the *defacto* buyer, and

(c) long term leases i.e. leases for a period of 12 years or more.

1.17.02 Acquisition proceedings under these provisions can be initiated where an immovable property of fair market value exceeding Rs. 25,000 (Rs. 1 lakh with effect from 1 June 1984) is transferred for an apparent monetary consideration, which is less than the fair market value by more than 15 per cent of the apparent monetary consideration. The compensation payable on acquisition is the amount of the monetary consideration shown in the transfer document plus 15 per cent of such amount.

1.17.03* Particulars of cases where notices of acquisition issued, acquisition made, etc. are given in the table below :—

	1981-82	1982-83	1983-84
1. Total Number of commissioners charges	21	21	21
2. No. of cases where notices of acquisition issued.	6,678	11,120	12,853
3. No. of cases where notices were withdrawn	2,476	3,003	3,507
4. No. of cases where acquisition made pursuant to the notice	15	5	25
5. In respect of properties at 4			
(a) The value determined in respect of property acquired	33,99,300	12,30,400	50,34,463
(b) Whether the amount was actually paid	..	.	..
(c) Whether the acquisition was appealed against	2	2	6
(d) Expenditure incurred in the maintenance of property wherever acquired	..	..	..
(e) If the property is not resold whether rental income is received and accounted for	..	..	..

*Figures furnished by the Ministry of Finance are provisional.

1.18 Functioning of Valuation Cells

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

(i) No. of Valuation Units/Districts;

Year	No. of Units	No. of Districts
1981-82	80	11
1982-83	80	11
1983-84	80	11

	Income-tax	Wealth-tax	Gift-tax	Estate-duty
(ii) No. of cases referred :				
1981-82	14,982	17,539	107	496
1982-83	11,619	15,815	129	599
1983-84	13,138	15,585	166	633
(iii) No. of cases decided :				
1981-82	12,626	12,671	67	260
1982-83	9,864	11,444	101	424
1983-84	10,849	10,580	100	417
(iv) No. of cases pending :				
1981-82	2,356	4,868	40	236
1982-83	1,755	4,369	28	175
1983-84	2,289	5,005	66	216

1.19 Revenue demands written off by the department

(i) Income-tax

A demand of RS. 769.14 lakhs in 35,631 cases was written off by the department during the year 1983-84, of this, a sum of Rs. 466.01 lakhs relate to 8,532 company assessees and Rs. 303.13 lakns to 27,099 non-company assessees. Income-tax demands written off by the department during the year 1983-84 are given below categorywise:

(Amount in lakhs of rupees)

	Companies		Non-companies		Total	
	No.	Amount	No.	Amount	No.	Amount
1 2	3	4	5	6	7	8
I. (a) Assessees having died leaving behind no assets or have become insolvent	2	51.34	961	78.42	963	129.76
(b) Companies which have gone into liquidation and are defunct	8,442	262.00	5,512	24.76	13,954	286.76
TOTAL	8,444	313.34	6,473	103.18	14,917	416.52
II. Assessees being untraceable	52	5.21	7,063	110.89	7,115	116.10
III. Assessees having left India	..	..	177	8.13	177	8.13
IV. Other reasons :						
(a) Assessees having no attachable assets	2	4.31	1,110	34.02	1,112	38.33
(b) Amount being petty, etc.	..	..	10,451	32.74	10,451	32.74
(c) Amount written off as a result of scaling down of demands	..	..	1,820	10.48	1,820	10.48
TOTAL	2	4.31	13,381	77.24	13,383	81.55
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	34	143.15	5	3.69	39	164.84
GRAND TOTAL	8,532	466.01	27,099	303.13	35,631	679.14

(ii) Wealth tax, Gift tax and Estate Duty demands written off by the department during the year 1983-84 are given below category-wise :—

(Amount in lakhs of rupees)

	Wealth tax		Gift tax		Estate Duty	
	No.	Amount	No.	Amount	No.	Amount
I. (a) Assessees having died leaving behind no assets or become insolvent . . .	17	0.87	10	0.96	..	..
(b) Companies which have gone into liquidation and are defunct	..	..	..	..	..	..
TOTAL	17	0.87	10	0.96	..	..
II. Assessees being untraceable	..	..	57	0.51	..	..
III. Assessees having left India	..	..	..	..	..	..
IV. Other reasons :						
(a) Assessees who are alive but have no attachable assets	..	..	..	..	..	..
(b) Amount being petty, etc.	15	0.07	92	0.07	82	0.04
(c) Amount written off as a result of scaling down of demands	..	..	..	..	..	..
TOATL	15	0.07	92	0.07	82	0.04
V. Amount written off on grounds of equity or as a matter of international courtesy or where the time, labour and expenses involved in legal remedies for realisation are considered disproportionate to the amount of recovery	..	..	..	..	..	..
GRAND TOTAL	32	0.94	159	1.54	82	0.04

1.20 Compulsory Deposit Scheme (Income-tax Payers) Act, 1974*

In the interest of national economic development, the Compulsory Deposit Scheme (Income-tax Payers) Act, 1974 was brought into force with effect from 17th July, 1974. The Act requires deposits at the prescribed rates to be made compulsorily by all income-tax payers who are individuals, Hindu undivided families or trustees of private discretionary trusts, in cases where the aggregate of their non-agricultural and agricultural income, if any, exceeds Rs. 15,000 in a year. The compulsory deposit is repayable in five annual instalments with interest.

(a) The particulars of amounts deposited, refunds made and the balance for the five years ending 1983-84 are as below :-

(Rs. in lakhs)

Financial Year	Opening Balance	Deposits made during the year	Total	Refunds made	Balance
1979-80 . .	441.93	154.71	596.64	98.58	498.06
1980-81 . .	496.85	168.60	665.45	110.14	555.31
1981-82 . .	591.39	146.39	737.78	124.95	612.83
1982-83 . .	609.44	197.37	806.81	131.05	675.76
1983-84 . .	674.82	227.55	902.37	150.65	751.72

(b) The interest paid and the expenditure incurred on administering the Scheme during the five year period are shown below :

(Rs. in lakhs)

Financial Year	Interest	Other expenditure incurred in collection
1	2	3
1979-80	0.69	—
1980-81	0.71	—
1981-82	0.92	—
1982-83	1.02	—
1983-84	1.03	—

*The figures furnished by the Ministry of Finance are provisional.

(c) (i) Amounts due as deposits at the end of each of the five years ending 1983-84 is indicated below (cumulative) ;

Financial Year	No. of cases	Amount (Rs. in lakhs)
1	2	3
1979-80	14,815	613.30
1980-81	17,096	1082.25
1981-82	20,503	1301.23
1982-83	24,358	1360.73
1983-84	31,746	1720.08

(ii) The break up of arrears as on 31 March 1984, year-wise, is as follows ;

Financial Year	No. of cases	Amount (Rs. in lakhs)
1	2	3
1974-75	368	21.96
1975-76	511	12.38
1976-77	1,055	65.30
1977-78	1,359	59.01
1978-79	2,091	288.20
1979-80	2,878	142.18
1980-81	3,785	481.59
1981-82	4,717	226.26
1982-83	5,602	71.54
1983-84	9,380	351.66
TOTAL	31,746	1720.08

1.21 Outstanding Audit Objections

As on 31 March 1984, 1,19,462 audit objections involving revenue of Rs. 287.93 crores (approximately), raised by the internal audit of the department and by the statutory audit, are pending without settlement. Of these, 10,920 cases (only major cases) of the internal audit accounted for Rs. 97.31 crores. The remaining 1,08,542 were statutory audit objections involving Rs. 190.62 crores.

(i) Internal Audit

Internal Audit was introduced in the department in June 1954. Initially the scope was limited to checking the arithmetical accuracy of computation of income and determination of tax. However, after the introduction of the statutory audit in 1960, the scope of internal audit was widened and is now coextensive with that of statutory audit. There are 150 internal audit parties (including 40 special parties) sanctioned as on 31st March 1984 Out of these 142 internal audit parties are actually working. The work of the internal audit is supervised by Income-tax Officers (Internal Audit) and by Inspecting Assistant Commissioners (Audit) under the over-all charge of Commissioner of Income-tax. The Central Board of Direct Taxes have laid down that mistakes pointed out in internal audit should be rectified within three months from the date of intimation to the assessing officer. The assessing officers have to ensure that the rectifications are effected before action becomes time-barred.

As per the monthly Reports drawn up by the Directorate of Inspection (Income-tax and Audit) of the Department, the number of major objections (with tax effect Rs. 10,000 and above under income-tax and Rs. 1,000 and above under other direct taxes) disposed of and pending during the five year period 1979-80 to 1983-84 are as follows :

Financial Year	No. of cases for disposal (Amount in Crores)	No disposed of	Per centage	Pending cases
1	2	3	4	5
1979-80	15,261	4,487	9.40	10,774
	118.69	20.60	17.35	98.09
1980-81	16,114	3,894	24.16	12,220
	131.19	21.50	16.38	109.09
1981-82	18,036	5,039	27.94	12,997
	141.86	23.56	16.61	118.30
1982-83	17,218	5,516	32.03	11,702
	143.85	49.16	34.19	94.69
1983-84	16,335	5,415	33.15	10,920
	133.74	36.43	27.24	97.31

Though there is a slight increase in the percentage of cases disposed of during 1983-84 when compared to the earlier year, there is a fall in total number of cases disposed of. The decrease in revenue effect of cases disposed of from Rs. 49.16 crores in 1982-83 to Rs. 36.43 crores in 1983-84 and the increase in the revenue effect of the pending cases from Rs. 94.69 crores in 1982-83 to Rs. 97.31 crores in 1983-84 indicate that cases involving larger tax effect were not given priority.

No year-wise analysis of the age of the pending items is being undertaken by the Central Board of Direct Taxes to enable them to watch that old items are cleared expeditiously. According to the information furnished by the Central Board of Direct Taxes, in respect of eleven charges (two consolidated charges of Delhi and Karnataka and nine other charges of Commissioners of Income-tax) 1142 items involving revenue of Rs. 11.07 crores were outstanding for more than one year for settlement. Similar information in respect of other charges is awaited (November 1984).

(ii) Statutory Audit

(a) As on 31 March 1984, 1,08,542 objections involving a revenue of Rs. 190.62 crores, are outstanding without final action. The years-wise particulars of the pendency are as follows :—

Amount
(Rupees in Crores)

	Income-tax		Wealth-tax		Gift-tax		Estate Duty		Total	
	Items	Amount	Items	Amount	Items	Amount	Items	Amount	Items	Amount
Upto 1978-79 and earlier Years	37,620	52.54	5,205	4.80	1,513	1.96	612	8.00	44,950	67.30
1979-80	11,878	20.15	3,228	3.57	673	1.65	261	0.28	16,040	25.65
1980-81	11,587	21.41	2,456	2.26	480	2.12	330	0.20	14,853	25.99
1981-82	12,488	29.07	2,298	3.11	507	0.89	361	0.95	15,654	34.02
1982-83	13,991	32.70	2,303	3.29	479	1.30	272	0.37	17,045	37.66
TOTAL	87,564	155.87	15,490	17.03	3,652	7.92	1,836	9.80	1,80,542	190.62

(b) In the following charges the income-tax involved in the outstanding objections exceeded Rs. 1 crore :

Sr. No.	Charge	Items	Tax amount involved (Rs. in Crores)
1.	Bombay	5,471	35.46
2.	Tamil Nadu	8,224	28.89
3.	West Bengal	2,268	18.22
4.	Gujarat	4,684	6.12
5.	Madhya Pradesh	3,189	5.94
6.	Andhra Pradesh	7,778	5.11
7.	Karnataka	1,274	4.04
8.	Delhi	2,939	4.01
9.	Assam	1,244	3.92
10.	Kerala	1,300	3.13
11.	Bihar	4,160	2.94
12.	Orissa	618	2.49
13.	Uttar Pradesh	2,000	2.27
14.	Jammu and Kashmir	554	1.18

(c) In the following charges, the wealth-tax involved in the outstanding objections exceeded Rs. 20 lakhs :

Sr. No.	Charge	Items	Tax amount involved (Rupees in lakhs)
1.	Tamil Nadu	1,865	271.42
2.	Andhra Pradesh	806	226.43
3.	Madhya Pradesh	831	214.55
4.	Gujarat	179	91.48
5.	Bombay	469	94.70
6.	West Bengal	224	58.96
7.	Assam	433	50.11
8.	Karnataka	819	49.47
9.	Delhi	433	46.93
10.	Rajasthan	597	45.14
11.	Orissa	77	27.33

(d) In the following charges, the gift-tax involved in the outstanding objections exceeded Rs. 10 lakhs.

Sr. No.	Charge	Items	Tax amount involved (Rupees in lakhs)
1.	Gujarat	61	276.00
2.	Bombay	175	263.04
3.	Tamil Nadu	331	48.43
4.	West Bengal	39	14.46

(e) In the following charges, the estate duty involved in the outstanding objections exceeded Rs. 10 lakhs :

Sr. No.	Charge	Items	Duty amount involved (Rupees in lakhs)
1.	Andhra Pradesh	71	707.13
2.	Madhya Pradesh	153	73.92
3.	West Bengal	371	72.07
4.	Tamil Nadu	170	25.82
5.	Bombay	156	16.29
6.	Kerala	52	11.50

The Central Board of Direct Taxes have laid down in April 1970 that the Department should furnish replies to the audit objections within 45 days of receipt of the audit objections. In February 1975 the Board introduced a system of selective control in relation to audit objections. The Commissioner is responsible for ensuring remedial action within a month of the receipt of the Local Audit Report in cases where the tax involved is Rs. 25,000 or more in Income-tax and Rs. 5,000 or more in other Direct Taxes. The Range Inspecting Assistant Commissioners are responsible for remedial action in respect of objections involving revenue between Rs. 10,000 and Rs. 25,000 in Income-tax and Rs. 1,000 and Rs. 5,000 in respect of other Direct Taxes.

With a view to having an effective control over the pursuance and settlement of objections raised by the statutory audit and to ensure rectification/revision before objections become barred by time, the Central Board of Direct Taxes had, in pursuance of the recommendation by Public Accounts Committee

46th Report, Third Lok Sabha 1965-66) issued instructions in February 1966 prescribing maintenance of a Register in the Commissioners offices. In May 1977, the Central Board of Direct Taxes instructed that two registers (one for major and one for minor objections) should be maintained by each Income-tax Officer. The Board's instructions required the Internal Audit of the Department to verify periodically and ensure that the prescribed registers are maintained properly. A test check by Audit in 194 wards during May-July 1984 disclosed that the registers had not been maintained in 48 wards and that the registers maintained in 47 wards were defective.

It is apparent that the control system is inadequate and the pace of settlement of audit objections unsatisfactory in view of the fact that 44,950 items involving revenue of Rs. 67.30 crores relate to 1978-79 and earlier years. The Action plan target of the department for 1984-85 included 100 per cent disposals of all arrear major audit objections (both internal and statutory) and the clearance of objections raised during 1984-85 (upto December 1984) by 31 March 1985.

This review was sent to the Ministry of Finance in October 1984; their reply is awaited (November 1984).

1.22 Results of test audit in general

During the period from 1 April 1983 to 31 March 1984 in the test audit of the documents of Income tax offices etc. 23,675 cases of under-assessment involving a total revenue effect of Rs. 6732.46 lakhs were noticed. Besides these, various defects in following the prescribed procedure also came to the notice of Audit. The test audit of assessment records covered assessments made by Income-tax Officers, Wealth-tax Officers, Gift-tax Officers, Assistant Controllers of Estate duty and also the Inspecting Assistant Commissioners (Assessment).

The Public Accounts Committee in para 12.7 of their 186th Report (5th Lok Sabha; 1975-76) found that "———reason for the repetitive mistakes in big cases resulting in huge loss of revenue, is that assessment work is largely left in the hands of comparatively inexperienced Income-tax Officers" and expres-ed the hope that if Assistant Commissioners of Income-tax are given assessment powers to assess directly certain cases, the standard of performance will improve and the possibility of mistakes reduced. Pursuant to these recommendations, the in-stitution of Inspecting Assistant Commissioners (Assessment)

was created in October 1978 with a view to utilising the experience gained by senior officers amongst other things on making assessments in bigger and complicated cases. At the commencement of financial year 1982-83, 108 posts of Inspecting Assistant Commissioners were sanctioned for assessment work. The test audit of assessment records, however, revealed that inspite of posting senior officers of the rank of Inspecting Assistant Commissioners for assessment work errors in the application of law, mistakes due to negligence or carelessness etc. continued to occur in the assessments. A number of such cases have been mentioned in this report.

Corporation Tax and Income-tax

During the period under report test audit of the documents of the Income-tax Offices revealed total under-assessment of tax of Rs. 6254.01 lakhs in 19,388 cases.

Of the total 19,388 cases of under-assessment, short levy of tax of Rs. 5563.12 lakhs was noticed in 2546 cases alone. The remaining 16,842 cases accounted for under-assessment of tax of Rs. 690.89 lakhs.

The under assessment of tax of Rs. 6254.01 lakhs is due to mistakes categorised broadly under the following heads :—

	No. of cases	(Amount in lakhs of rupees)
1	2	3
1. Avoidable mistakes in computation of tax	1,597	461.09
2. Failure to observe the provisions of the Finance Acts.	327	64.92
3. Incorrect status adopted in assessments	386	279.72
4. Incorrect computation of salary income	476	31.97
5. Incorrect computation of income from house property	769	138.93
6. Incorrect computation of business income	3,562	1358.68
7. Irregularities in allowing depreciation and development rebate	1,309	372.08
8. Irregular computation of capital gains	254	205.29
9. Mistakes in assessment of firms and partners	599	82.56
10. Omission to include income of spouse/minor child, etc.	154	13.79
11. Income escaping assessment	1,662	984.73
12. Irregular set off of losses	252	115.67
13. Mistakes in assessments while giving effect to appellate orders	130	179.56

1	2	3
14. Irregular exemptions and excess reliefs given	1,645	494.64
15. Excess or irregular refunds	582	75.33
16. Non-levy/incorrect levy of interest for delay in submission of returns, delay in payment of tax etc.	1,940	179.47
17. Avoidable or incorrect payment of interest by Government	497	126.78
18. Omission/short levy of penalty	950	88.63
19. Other topics of interest/miscellaneous	2,137	752.28
20. Under assessment of Surtax/Super Profits Tax	160	247.89
TOTAL	19,388	6254.01

(ii) Wealth-tax

During test audit of assessments made under the Wealth-tax Act, 1957 short levey of Rs. 243.93 lakhs was noticed in 3206 cases.

The under-assessment of tax of Rs. 243.93 lakhs was due to mistakes categorised broadly under the following heads :—

1	No. of cases 2	Amount (in lakhs of rupees) 3
1. Wealth escaping assessment	628	48.82
2. Incorrect valuation of asset	724	71.39
3. Mistakes in computation of net wealth	511	23.11
4. Incorrect status adopted in assessments	130	23.25
5. Irregular/excessive allowances and exemptions	423	13.83
6. Mistakes in calculation of tax	322	17.16
7. Non-levy or incorrect leavy of additional wealth-tax	57	11.12
8. Non-levy or incorrect levy of penalty and non-levy of interest	185	19.36
9. Miscellaneous	226	15.89
TOTAL	3,206	243.93

(iii) Gift tax

During the test audit of gift-tax assessments it was noticed that in 613 cases there was short levy of tax of Rs. 107.02 lakhs.

(iv) Estate duty

In the test audit of estate duty assessments it was noticed that in 468 cases there was short levy of estate duty of Rs. 127.50 lakhs.

CHAPTER 2

CORPORATION TAX

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

Year	Amount
	In crores of rupees
1979-80	1391.90
1980-81	1377.45
1981-82	1969.96
1982-83	2184.51
1983-84	2492.73

*2.02 According to the Department of Company Affairs, Ministry of Law, Justice and Company Affairs, there was 96,471 companies as on 31 March 1984. These included 326 foreign companies and 1,599 associations "not for profit" registered as companies limited by guarantee and 282 companies with unlimited liability. The remaining 94,264 companies comprised 971 Government companies and 93,293 non-Government companies with paid up capitals of Rs. 16414.9 crores and Rs. 5513.6 crores respectively. Among non-Government Companies, over 86 per cent (80,768) were private limited companies with a paid up capital of Rs. 1454.9 crores.

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

As on 31st March	Number
1980	42,581
1981	44,125
1982	46,355
1983	48,597
1984	52,951

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

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

Year	No. of assessments		Amount of demand	
	Completed during the year	Pending at the close of the year	Collected during the year	in arrears at the close of the year
			(In crores of Rupees)	
1979-80	38,033	43,886	1391.90	190.34
1980-81	44,937	52,250	1377.45	290.95
1981-82	47,238	55,861	1969.96	311.74
1982-83	47,505	57,638	2184.51	442.07
1983-84	51,923	61,599	2492.73	619.33

2.05 Some instances of mistakes noticed in the assessments of companies under the Income-tax Act and the Surtax Act, 1964 are given in the following paragraphs.

2.06 *Avoidable mistakes in the computation of income-tax*

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

The Public Accounts Committee in paragraph 5.21 of their 186th Report (5th Lok Sabha), in paragraphs 5.11, 6.13 and 6.14 of their 196th Report (5th Lok Sabha) and in paragraphs 5.24 and 5.25 of their 51st Report (7th Lok Sabha) expressed concern over under-assessment of tax on account of mistakes due to carelessness or negligence, which could have been avoided had the assessing officers and their staff been a little more vigilant.

The Central Board of Direct Taxes in their instructions issued in December 1968, May 1969, October 1970, October 1972, August 1973, January 1974 and the Directorate of Inspection (Income-tax) in their circular issued in July 1981 emphasised the need for ensuring arithmetical accuracy in the computation of income and tax, carry forward of figures etc. Inspite of these repeated instructions such mistakes continue to occur.

The under-assessment of tax due to avoidable mistakes in the computation of income or tax noticed in the test audit of assessment records from the year 1979-80 onwards are given below :

Year	Number of items	Amount of tax under assessed (In lakhs of Rupees)
1979-80	2,304	74.95
1980-81	1,288	65.33
1981-82	1,133	71.92
1982-83	1,548	127.04
1983-84	1,533	458.94

A few illustrative cases noticed in audit are given in the following paragraphs.

(i) In the assessment of a nationalised bank for the assessment year 1980-81 (assessment made in March 1983 by Inspecting Assistant Commissioner (Assessment), the assessing officer disallowed losses and bad and doubtful debts written off by the assessee amounting to Rs. 5,73,85,795 for the reasons that the assessee had written off the amount at a stage when the various law suits were in progress, that in many cases the debts were written off as bad on hypothetical considerations and that the assessee had not proved that the debts had become conclusively bad. However, in the actual computation of income, the amount was not added back. The mistake resulted in under-assessment of income by Rs. 5,73,85,795 involving a short levy of tax of Rs. 3,39,29,350.

The Ministry of Finance have accepted the mistake (July 1984).

(ii) While computing the business income of a State Electricity Board for the assessment year 1977-78 in July 1980, the Income-tax Officer allowed a sum of Rs. 1,63 62,392 towards interest on Government loan although the same was already charged in the profit and loss account of the year. The incorrect allowance resulted in double deduction of interest amounting to Rs. 1,63,62,392 involving potential tax effect of Rs. 94,49,280.

The Ministry of Finance have accepted the mistake (September 1984).

(iii) The assessment of a public limited company for the assessment year 1979-80 was originally made in June 1982. The assessment was revised in September 1982 to rectify certain errors in the original assessment and in the carry-forward of investment allowance etc. In the revised assessment, the income was arrived at Rs. 16,50,671 before considering the allowance of Rs. 1,13,12,455 towards depreciation. The assessing officer had instead of adjusting the depreciation of Rs. 1,13,12,454 against the income of Rs. 16,50,671 and carry forward the balance for set-off in future years, carried forward the entire amount as unabsorbed depreciation. The income of Rs. 16,50,671 was also not taxed in the assessment year 1979-80. This led to excess carry-forward of unabsorbed depreciation of Rs. 16,50,671 involving a potential tax effect of Rs. 9,30,567 for the assessment year 1983-84 (in which the assessee had positive income after set off of the carried forward losses etc.).

The Ministry of Finance have accepted the mistake (September 1984).

(iv) A public sector company in its income-tax assessment for the assessment year 1979-80, completed in September 1982, claimed a deduction of Rs. 24,04,201 towards bad debt. On the department allowing only a sum of Rs. 7,13,156 towards bad debt the assessee preferred an appeal, which was allowed by the appellate authority. While giving effect to the appellate order in February 1983, the department allowed the entire amount of Rs. 24,04,201 as deduction ignoring the fact that deduction of Rs. 7,13,156 was already allowed in the original order. The mistake resulted in short-computation of income by Rs. 7,13,156 involving a short-levy of tax of Rs. 4,11,846.

The Ministry of Finance have accepted the mistake (November 1984).

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

During the previous year relevant to the assessment year 1977-78, an assessee company debited a sum of Rs. 9,61,003 in its profit and loss account on account of provision for gratuity

liability upto December 1975. This liability was allowed by the Inspecting Assistant Commissioner (Assessment) in the assessment made in March 1978. The gratuity liability of Rs. 21,11,795 which also included the sum of Rs. 9,61,003, debited by the assessee company in its profit and loss account for the previous year relevant to the assessment year 1976-77 was fully allowed by the assessing officer in computing the assessee's income for that year. Since the gratuity liability of Rs. 9,61,003 was already allowed in the assessment year 1976-77 its allowance again in the assessment year 1977-78 resulted in double allowance leading to under-assessment of income of Rs. 3,84,400 with consequent short-levy of tax of Rs. 2,82,534.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(vi) In the original assessment of a company for the assessment year 1972-73 the assessee's claim for a deduction of Rs. 3,60,778 on account of gratuity liability determined on actuarial valuation was disallowed. While completing the assessment for the assessment year 1976-77 in March 1980, the Income-tax Officer allowed a gratuity liability of Rs. 9,62,592 which included the liability of Rs. 3,60,778 relating to the assessment year 1972-73 which was disallowed earlier. On appeal by the assessee against the assessment orders for the assessment year 1972-73 the Commissioner of Income-tax (Appeals) allowed the liability of Rs. 3,60,778 and the assessment for the assessment year 1972-73 was revised in July 1980 to give effect to the appellate order and the liability was allowed. However, the department did not correspondingly rectify the assessment for 1976-77 to withdraw the allowance of Rs. 3,60,778 allowed therein resulting in double allowance of the same liability once in assessment for 1972-73 and again in 1976-77. This led to under-assessment of income by Rs. 3,60,778 in the assessment year 1976-77 with consequent under charge of tax of Rs. 2,27,291.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(vii) In computing the business income of a company, the department had been following the practice of first disallowing the provisions made in the accounts for staff gratuity and pension and then allowing the actual payments made on gratuity and pension during the relevant previous years.

The assessment for the assessment year 1979-80 of a company was made in September 1982 and revised in February 1983 by the Income-tax Officer disallowing a total sum of Rs. 2,15,000 towards provision for staff gratuity (Rs. 1,65,000) and pension (Rs. 50,000) and allowing deduction of Rs. 1,81,945 only being the actual amount paid out of the two provisions, in accordance with the practice followed in earlier assessments. The company had, however, actually made a provision of Rs. 4,70,000 for staff gratuity and the disallowance on account of provision for staff gratuity should have, therefore, been made for Rs. 4,70,000 instead of Rs. 1,65,000 only. The short disallowance of Rs. 3,05,000 led to under-assessment of business income by the same amount with consequent undercharge of tax of Rs. 1,76,138 in the assessment year 1979-80.

The Ministry of Finance have accepted the mistake (November 1984).

(viii) The Income-tax Act, 1961 provides for a deduction of amount equal to twenty per cent of income from the total business income of an assessee, derived from a business carried on printing and publication of books.

The business income of a Government company engaged in the business of printing and publication of text books was determined in March 1983 by the Inspecting Assistant Commissioner (Assessment) at Rs. 89,33,688 for the assessment year 1980-81. A sum of Rs. 3,45,558 being income from sources other than printing and publication of books, was deducted therefrom and a relief of Rs. 17,17,626 at 20 per cent of balance income of Rs. 85,88,130 was allowed. The balance of Rs. 68,70,504 was determined as the taxable income derived from printing and publication of books. While determining the total taxable income of the assessee company, the assessing officer did not add the other income of Rs. 3,45,558 to the total income as a result of which income was under-assessed by Rs. 3,45,558 involving short-levy of tax of Rs. 2,34,185 including surtax for the assessment year 1980-81.

The Ministry of Finance have accepted the mistake (October 1984).

(ix) In the case of a company, the assessment for the assessment year 1979-80 made in September 1981 arrived at a loss of Rs. 12,87,075. The total amount of depreciation allowance

admissible as per the details kept in the schedule appended to the assessment order correctly worked out to Rs. 10,75,924 only as against Rs. 13,75,924 which was allowed in the assessment order. This mistake resulted in excess allowance of depreciation of Rs. 3,00,000 with consequent excess carry forward of depreciation for that assessment year with a potential tax effect of Rs. 1,73,250.

The Ministry of Finance have accepted the mistake (September 1984).

The assessment was checked by the Internal Audit Party of the department, but the mistake was not detected.

(x) During the previous year relevant to the assessment year 1979--80, a widely held company paid a sum of Rs. 3,00,101 to a Labour Welfare Fund and claimed it as business expenditure. While completing (July 1982) the assessment, the assessing officer treated it as donation and allowed appropriate tax relief on the sum paid but overlooked to add back the sum of Rs. 3,00,101, in the income computation. This resulted in under-assessment of business income of Rs. 3,00,101 and a short levy of tax of Rs. 1,64,642.

The Ministry of Finance have accepted the mistake (August 1984).

(xi) The income-tax assessment of a company in which the public are substantially interested, for the assessment year 1979-80 was completed in August 1982 on a taxable income of Rs. 45,64,840. While computing the tax payable by the company, the assessing officer incorrectly computed the surcharge payable as Rs. 12,553 instead of the correct amount of 1,25,533. The omission resulted in under-charge of tax of Rs. 1,63,785 including interest leviable for belated filing of the return of income and for short-fall in payment of advance tax.

The Ministry of Finance have accepted the mistake (November 1984).

(xii) In the case of a public company, as a result of revision of the assessment for the assessment year 1975-76 in February 1981 to give effect to appellate orders, a sum of Rs. 1,35,385 was refunded. The assessment under went further rectification in September 1982 and again in the last week of March 1983 according to which the assessee became liable to pay a tax of Rs. 3,69,606. While calculating the demand, the Income-tax

Officer did not take into account the income-tax refund of Rs. 1,35,385 already made to the assessee in February 1981. The omission resulted in short-levy of tax of Rs. 1,35,385.

The Ministry of Finance have accepted the mistake (December 1984).

(xiii) In the assessment of a company made in November 1982 for the assessment year 1982-83 depreciation of Rs. 2,09,504 charged to the account was added back to the loss of Rs. 1,17,882 shown in the profit and loss account resulting in income of Rs. 91,622. Out of the admissible depreciation of Rs. 2,09,504 for the year, a sum of Rs. 91,622 was set off against the income mentioned above. Thus, the balance depreciation required to be carried forward as unabsorbed was only Rs. 1,17,882. Instead, the Income-tax Officer carried forward the amount of Rs. 91,622 as business loss and also unabsorbed depreciation allowance of Rs. 2,09,504. This mistake resulted in excess carry forward of Rs. 1,83,244 (business loss of Rs. 91,622 and the already absorbed depreciation allowance of Rs. 91,622) with a potential tax effect of Rs. 1,03,304.

The Ministry of Finance have accepted the mistake (August 1984).

The Internal Audit Party of the department has checked the assessment; but did not notice the mistake.

(xiv) Any sum credited to reserve account in the profit and loss appropriation account, as distinct from the actual business expenditure shall not be admissible deduction for the purpose of computation of business income.

In computing the business income of a company for the assessment year 1980-81, the assessing officer started from the loss as shown in the profit and loss appropriation account. A sum of Rs. 1,72,630 which represented a credit given to Investment allowance Reserve Account, by debit to profit and loss appropriation account was, however, not added back as an inadmissible item while framing the assessment in February 1983. The mistake resulted in excess computation and carry forward of business loss of Rs.1,72,630 with consequent potential tax effect of Rs.1,02,067.

The Ministry of Finance have accepted the mistake (August 1984).

(xv) While computing income, the assessing officer usually

proceeds from the net profit as the starting point and adds back the amount of inadmissible expenditure actually charged in the profit and loss account for considering their admissibility under the provisions of the Income-tax Act, 1961. Similarly in the case of loss, where the Income-tax Officer proceeds with the net loss, he deducts therefrom the amounts of inadmissible expenditure. The amount of expenses admissible under the Act are thereafter allowed as deduction.

In computing the total income of a company for the assessment year 1979-80 (assessment completed in September 1982), the Income-tax Officer started from the net loss as shown in the profit and loss account to which depreciation of Rs. 49,267 already charged to the account was erroneously added instead of being deducted therefrom. The amount of depreciation as admissible under the Act was also allowed separately. The mistake resulted in under-assessment of total income by Rs. 98,534 with consequent tax undercharge of Rs. 94,818 including interest for failure to file the estimate of advance tax.

The Ministry of Finance have accepted the mistake (November 1984).

(xvi) Out of the advance tax of Rs. 4,77,500 paid by an assessee for the assessment year 1977-78, a sum of Rs. 94,404 was refunded consequent on the provisional assessment made in July 1977. In the regular assessment made in June 1980, the amount of tax already paid was taken correctly as Rs. 3,83,096. However, during re-assessment made in January 1983, credit for the entire amount of advance tax of Rs. 4,77,500 was allowed instead of Rs. 3,83,096 overlooking the refund of Rs. 94,404 already made. This resulted in short levy of tax of Rs. 94,404.

The Ministry of Finance have accepted the mistake (August 1984).

(xvii) In computing the total income of an assessee in July 1982 for the assessment year 1979-80, the assessing officer started from net loss of Rs. 6,89,492 as shown in the profit and loss account and determined a net business loss of Rs. 4,27,992. As the net income for the year was a minus figure, depreciation allowable amounting to Rs. 37,497 was carried forward as unabsorbed depreciation. However, the Income-tax Officer did not initially deduct depreciation amounting to Rs. 2,96,801 and investment allowance reserve of Rs. 3,22,684 debited to the

profit and loss account by the assessee as depreciation and investment allowance were allowed separately. The omission led to determination of net loss in respect of the company instead of a positive income of Rs. 1,53,996 resulting in undercharge of tax of Rs. 88,935.

The Ministry of Finance have accepted the mistake (June 1984).

(xviii) In the case of a private limited company in another commissioners' charge, the original assessment for the assessment year 1979-80 was completed by the Inspecting Assistant Commissioner (Assessment) in March 1980. This assessment was set aside by the Commissioner of Income-tax (Appeals) in August 1980. In the fresh assessment done in March 1983, the assessing officer allowed depreciation amounting to Rs. 81,34,973 stating that the allowance was according to the original assessment. In the original assessment order the assessee was, however, allowed depreciation of Rs. 80,14,705 only as claimed by him and the appellate order did not make any reference to the quantum of depreciation allowance. The omission to adopt the correct amount of depreciation in the revised assessment led to excess allowance of depreciation by Rs. 1,20,268 involving short-levy of tax of Rs. 75,768.

The Ministry of Finance have accepted the mistake (November 1984).

(xix) In the case of a banking company for the assessment year 1980-81, the assessing officer disallowed capital expenditure amounting to Rs. 85,000 while computing the income for the assessment year 1980-81 in March 1983. However, the amount was not added back. This resulted in under-assessment of income by Rs. 85,000 leading to undercharge of tax of Rs. 50,255.

The Ministry of Finance have accepted the mistake (November 1984).

(xx) In the case of an assessee company, while computing the income in September 1982 for the assessment year 1979-80, the Income-tax Officer proceeded to compute the income taking the "Adjusted statement of income" of the assessee enclosed to the return of income, as the starting point. In the statement the assessee had shown the income as Rs. 1,91,099. After making an addition of Rs. 5,72,419 on various counts, the Income-tax Officer allowed, among other things, deductions towards donations to charitable purposes and relief to newly established

undertakings in backward areas to the extent of Rs. 1,251 and Rs. 1,45,253 respectively. The amount of Rs. 1,91,099 shown by the assessee in the adjusted statement of income was arrived at by the assessee after deducting the sums of Rs. 1,251 and Rs. 93,228 towards donations and relief on account of new undertaking in backward area respectively. The deductions of these amounts again amounted to double deductions leading to under-assessment of income by Rs. 94,479 with a consequent undercharge of tax of Rs. 80,467.

The Ministry of Finance have accepted the mistake (October 1984).

(xxi) The assessment of an industrial company in which the public are not substantially interested, for the assessment year 1981-82 was completed in March 1982 on a taxable income of Rs. 1,81,307. In computing this income, the assessing officer had added the amount of depreciation, donation etc. amounting to Rs. 1,00,142 already charged to the account, to the net profit of Rs. 2,87,739 as per the profit and loss account. However, the total was erroneously arrived at as Rs. 2,97,881 instead of the correct amount of Rs. 3,87,881. This incorrect computation resulted in under-assessment of taxable income of Rs. 90,000 involving a short-levy of tax of Rs. 73,736 including interest paid on excess advance tax refunded.

The Ministry of Finance have accepted the mistake (August 1984).

(xxii) In the previous year relevant to the assessment year 1976-77, a private limited company debited a sum of Rs. 23,50,000 towards provision for income-tax in its accounts. While making the assessment in April 1982, the Income-tax Officer in a Central circle where the assessment was done, disallowed the provision but added back a sum of Rs. 22,50,000 only instead of Rs. 23,50,000. The mistake remained unnoticed by the Income-tax Officer while giving effect to appellate orders in December 1982. The omission resulted in under-assessment of income of Rs. 1,00,000 with consequent short-levy of tax of Rs. 64,268.

The Ministry of Finance have accepted the mistake (November 1984).

(xxiii) A tea company was originally assessed in August 1976 for the assessment year 1973-74 on a loss of Rs. 1,07,558

and the same was adjusted against the profits of the assessee for the assessment year 1975-76. The assessment was revised in April 1978 reducing the quantum of loss to Rs. 29,560. However, the assessment for the assessment year 1975-76 was not consequently revised. This omission resulted in under-assessment of taxable income by Rs. 77,998 with consequent short-levy of tax and interest of Rs. 57,615 for the assessment year 1975-76

The Ministry of Finance have accepted the mistake (October 1984).

(xxiv) In the assessment of a public limited company for the assessment year 1978-79 made in April 1981, in the same charge, the depreciation admissible was worked out as Rs. 12,08,11,880 and in the absence of any chargeable income in that year, the amount was allowed to be carried forward to the subsequent years. This amount of unabsorbed depreciation was, however, indicated in the assessment orders for the subsequent years (assessment year 1979-80 made in August 1982 and assessment year 1980-81 made in June 1983) as Rs. 12,09,11,880. This mistake resulted in excess carry forward of depreciation amounting to Rs. 1,00,000 with a potential tax effect of Rs. 57,750.

The Ministry of Finance have accepted the mistake (September 1984).

2.07 *Incorrect application of rate of tax.*

Adoption of incorrect rates of tax is another common mistake. A few illustrative cases are given in the following paragraphs.

(i) Under the provisions of the Finance Acts, as applicable to the assessment years 1978-79, 1979-80 and 1980-81 the income of an industrial company in which public are not substantially interested is charged to tax at the rate of 55 per cent if the income does not exceed Rs. 2 lakhs and at 60 per cent if it exceeds Rs. 2 lakhs.

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

in April 1980 that the term "industrial company" covers a construction company only when it is engaged in the construction of ship. Hence companies engaged mainly or otherwise in the construction of anything other than ships cannot be considered as industrial company and shall be charged to tax at the rate of 65 per cent of the total income.

In the assessment of a private industrial company made in July 1982 for the assessment year 1979-80 tax was levied at the rate of 55 per cent on a total income of Rs. 61.14 lakhs instead of at 60 per cent. The incorrect application of rate resulted in short levy of tax of Rs. 3,24,350 including interest for late filing of return.

The Ministry of Finance have accepted the mistake (June 1984).

(ii) In the assessment completed in May, June and October 1981 of a private company engaged in the business of constructing houses, buildings etc. the department levied tax at the rate of 60 per cent for the assessment years 1978-79, 1979-80 and 1980-81 treating the company as an industrial company. In terms of the judicial decision on the subject the company was to have been treated as non-industrial company and tax was leviable at the rate of 65 per cent. The mistake in the application of rate of tax resulted in short-levy of tax aggregating to Rs. 2,01,332 for the three assessment years.

The Ministry of Finance have accepted at the mistake (December 1984).

(iii) A private limited company, which is not engaged in manufacturing or processing of goods but only in the business of installation and erection of oil extraction plants was treated as industrial company and was charged to tax at the rate of 60 per cent in the assessment years 1979-80 and 1980-81 assessments of which were completed in February and March 1982 respectively. As the assessee was not an industrial company, it was liable to pay tax at the rate of 65 per cent and not at the rate of 60 per cent as charged by the department. Incorrect application of rate resulted in aggregate short-levy of tax of Rs. 61,791 in both the years.

The Ministry of Finance have accepted the mistake (August 1984).

(iv) A non-resident company incorporated in Panama was engaged by an Indian Oil Company for operating the offshore

drilling rigs at Bombay. The tax was paid by the Indian company as the agent of the non-resident foreign company and the tax paid was required to be treated as perquisite and taxed on tax-on-tax basis.

In the assessment of the non-resident foreign company completed in March 1982 by the Inspecting Assistant Commissioner (Assessment) for the assessment year 1980-81, the income arising out of the payments made to the company was computed at Rs. 14,47,768. While arriving at the value of tax perquisite, surcharge was calculated at 5 per cent instead of at 7.5 per cent. This led to short computation of income-tax by way of perquisite by Rs. 25,337.

While determining the tax payable on the total income inclusive of tax perquisite, surcharge was again levied at 5 per cent instead of at 7.5 per cent. The two mistakes led to total short-levy of tax of Rs. 77,500 including interest for non-payment of advance tax.

The Ministry of Finance have accepted the mistake (September 1984).

Incorrect computation of business income

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

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

2.08 *Mistakes in the allowance of ex-gratia or ad hoc payments*

(i) Under the Income-tax Act, 1961 bonus paid to employees covered by the Payment of Bonus Act, 1965 in excess of the limits prescribed therein or any ex-gratia payment in addition to the bonus paid under that Act is not an admissible expenditure. The Central Board of Direct Taxes issued instructions in December 1980 clarifying that such additional payment cannot be treated as any other expenditure incurred wholly and exclusively for the purpose of business and resort cannot, therefore, be had to any other provision of the Income-tax Act to claim deduction in excess of what is admissible under the Bonus Act.

During the previous year relevant to the assessment year 1978-79, a jute company made payment of bonus of Rs. 9,46,261 calculated at 8.33 per cent of the salary of its employees. The company also made *ad hoc* payment of bonus of Rs. 1,69,591 to its employees during the year. Although in the draft assessment order for the assessment year 1978-79, the Income-tax Officer allowed only the bonus of Rs. 9,46,261 as admissible expenditure and disallowed the *ad hoc* payment of Rs. 1,69,591, the Inspecting Assistant Commissioner directed the Income-tax Officer to allow the *ad hoc* payment also as business expenditure. In the assessment made in September 1982, the *ad hoc* payment of bonus was accordingly allowed as business expenditure.

As the *ad hoc* payment of bonus was over and above the statutory liability for bonus, the *ad hoc* payment was not allowable. The omission to disallow the claim resulted in excess computation of carry forward of business loss of Rs. 1,69,591 to the next assessment year.

The Ministry of Finance have accepted the mistake (August 1984).

(ii) During the previous year relevant to the assessment year 1979-80, a private limited company made an ex-gratia payment of Rs. 1,53,298 to its employees in addition to the bonus admissible under the Bonus Act. The ex-gratia payment over and above the statutory liability for bonus, was not allowable in computing the income. However, while completing the assessment for the assessment year 1979-80 in September 1982, the ex-gratia payment claimed as deduction by the assessee was not disallowed. The omission resulted in short computation of income by Rs. 1,53,298 with consequent excess carry-forward of unabsorbed investment allowance to the same extent.

The Ministry of Finance have accepted the mistake (October 1984).

(iii) Under the Income-tax Act, 1961, in respect of establishments to which the provisions of payment of Bonus Act, 1965 do not apply, the expenditure on bonus is allowable as a deduction on the basis of reasonableness with reference to service conditions of the employees, the profits of the establishment and the general practice in similar businesses. The Bonus Act, 1965 ceased to apply to the employees of a banking company with effect from the accounting year 1974 onwards. The Reserve Bank of India, in their communications in October 1975 and December 1975 to the commercial banks, however, directed that the eligible

employees of the bank be paid Rs. 750 per head as ex-gratia payment in lieu of bonus for the year 1974 and that the Central Board of Direct Taxes had indicated that this ex-gratia payment would qualify for deduction subject to the fulfilment of the conditions stipulated in the Act.

In the assessment of a public sector banking company for the assessment year 1976-77, completed in July 1980, the expenditure of Rs. 44,64,208 claimed by the assessee as deduction towards ex gratia payment made to its employees in lieu of bonus for the year 1974, was allowed in full. The amount payable to its employees eligible for such deduction as per the directive of the Reserve Bank of India taking into account the wage levels, the financial circumstances and other relevant factors as required by the Central Government (which was available to the income-tax officer while finalising the assessment) was only Rs. 22,52,530. The excess deduction of Rs. 22,11,678 resulted in short levy of tax of Rs. 12,77,244.

The Ministry of Finance have contended (January 1985) that the payment was made before the issue of guidelines by the Reserve Bank of India, but it satisfied the requirement of the law and if the assessee chose to later recover the amount paid, the recovered amount would be brought to tax under the law.

The reply need reconsideration as the correct computation of income under the provisions of the income-tax Act, 1961 need not wait for the determination of the excess payment by some other agency, especially when the quantum of liability became crystallised and was known to the income-tax officer at the time of assessment.

2.09 *Incorrect allowance of gratuity liability*

Under the Income-tax Act, 1961, no deduction shall be allowed in respect of any provision made by an assessee for the payment of gratuity to his employees on their retirement or on termination of their employment. However, a provision made by the assessee for payment by way of any contribution towards an approved gratuity fund is admissible as a deduction. Further income chargeable to tax under the provisions of the Act, is computed in accordance with the method of accounting regularly employed by the assessee.

(i) In the previous year relevant to the assessment year 1976-77, a company in which public are substantially interested created an approved gratuity fund. The assessee company paid a total sum of Rs. 6,04,500 being the gratuity liability for the period upto 31 March 1972 arrived at by actuarial valuation in the previous year relevant to the assessment year 1977-78 to the gratuity fund and claimed it as deduction in the above assessment year. This was allowed by the assessing officer while completing the assessment for the assessment year 1977-78 in July 1980. As the assessee was following mercantile system of accounting and as the gratuity fund was approved in December 1975, the liability to pay the initial contribution towards gratuity arose in the previous year relevant to the assessment year 1976-77 and not in the assessment year 1977-78. Consequently the deduction allowed for the assessment year 1977-78 was not in order which resulted in undercharge of tax of Rs. 4,51,632 including surtax of Rs. 1,02,245.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(ii) In the previous year relevant to the assessment year 1976-77 a company in which public are substantially interested created an approved gratuity fund. The assessee company paid a total sum of Rs. 4,10,454 being the gratuity liability for the period upto 31st March 1972 arrived at by actuarial valuation in the previous years relevant to the assessment years 1977-78, 1979-80 and 1980-81 to the gratuity fund and claimed it as deductions in the above assessment years. While completing the assessment for the assessment years in March 1980, December 1981 and March 1982 respectively, the assessing officer allowed the above claim of Rs. 4,10,454. The allowance of Rs. 4,10,454 was not in order as the assessee was following the mercantile system of account and as such the liability to pay the initial contribution towards gratuity arose in the previous year relevant to the assessment year 1976-77 in which the fund was created and not in the assessment years 1977-78, 1979-80 and 1980-81. The incorrect allowance resulted in under-assessment of income aggregating to Rs. 4,10,454 with consequent short-levy of tax of Rs. 241,619 for the three years (including withdrawal of interest of Rs. 6,688 allowed on the excess advance tax paid by the assessee for the assessment year 1979-80).

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

2.10 *Incorrect computation of income of financial corporations*

The Central Board of Direct Taxes issued instructions in August 1968 that the expenditure incurred by way of discount on issue of bonds by State Financial Corporations from time to time as part of their business is allowable as business expenditure in the asessment of corporations. In other words, the expenditure on account of discount is allowed in the assessment year in which the bonds are repaid. However, in January 1973, the Board clarified that "as soon as debentures are issued on discount by any financial institution it stands to honour the determined liability. As such, the discount becomes an ascertained liability in the year of issue itself". The Board further stated that the loss representing the amount on account of discount granted should, therefore, be allowed as a deduction in the year of issue.

The Madras High Court held in November 1979 (124 ITR 454), in the case of a financial corporation, that discount allowed at the time of issue of debentures did not constitute expenditure.

The judiciary held that before there could be any expenditure, there has to be some payment out and as there is no such payment in the case of issue of bonds at a discount the amount of discount granted could not be treated as expenditure. The Board have accepted the judgment in June 1981. The Board have, however, revised their instructions of January 1973 only in October 1983 more than two years after they accepted the decision of Madras High Court. In the meantime, the assessees were given the deluction in the year of issue of Bonds as per the instructions of 1973. The inordinate delay in reviewing the judicial decision withdrawing the January 1973 instructions, had resulted in loss of revenue to the ex-chequer. A few instances are given below :

(i)(a) A State Financial Corporation debited sums of Rs. 1,26,495 and Rs. 63,249 towards discounts on the issue of 6½ per cent Bonds 1989 and 6¾ per cent Bonds 1990 in the profit and loss account of the periods relevant to the assessment years 1979-80 and 1980-81 and claimed deduction of these amounts as expenditure on discount. In the assessments made in September 1982 and August 1982, the Income-tax Officer allowed the expenditure as claimed by the Corporation for these two assessment years 1979-80 and 1981-82.

The discount did not constitute allowable expenditure as held judicially and also accepted by the Board. The incorrect

deduction resulted in net under-assessment of total income of Rs. 1,35,530 with consequent undercharge of tax of Rs. 1,00,284 (including penal interest under section 215 of Rs. 21,393 in the assessment year 1979-80).

The Ministry of Finance have accepted the mistake but pleaded that as the instructions of 1973 were beneficial to assessees, the Income-tax Officer would not be competent to withdraw the deduction allowed (July 1984).

(b) A State industrial development corporation assessed in a different Commissioner's charge debited a sum of Rs. 1,12,000 towards discount on the issue of debentures bounds, in each of the previous years relevant to the assessment years 1979-80 and 1980-81 and claimed deduction of the discounts as expenditure. In the assessment made in March 1983, the Income-tax Officer allowed the expenditure as claimed by the corporation for these two assessment years. As the discount allowed on these debenture bonds does not constitute expenditure as held judicially, the allowance was not in order. The incorrect deduction resulted in net under-assessment of total income of Rs. 1,69,000 involving short-levy of tax of Rs. 99,044 for the assessment years 1979-80 and 1980-81.

The paragraph was forwarded to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(c) An assessee debited sums of Rs. 1,56,000 and Rs. 1,89,750 towards discount on the issue of 6 per cent and 6-1|4 per cent 10 years Bond at 99 per cent redeemable at par, in the profit and loss account of the periods relevant to the assessment years 1978-79 and 1980-81 respectively, and claimed deduction of these amounts as expenditure on discount. In the assessments made in March 1981 and February 1983, the Income-tax Officer allowed the expenditure as claimed by the assessee for the two years. As the mere grant of discount on these bonds did not constitute 'expenditure' as held judicially and also accepted by the Board, the allowance was not in order. The incorrect deduction resulted in excess carry forward of loss of Rs. 3,45,750 for the assessment years 1978-79 and 1980-81.

The Ministry of Finance have accepted the mistake (August 1984).

(ii) Under the provisions of Income-tax Act, 1961, as it stood for the assessment years 1975-76 to 1977-78, approved financial corporations or joint financial corporations established

under the State Financial Corporation Act, 1951 engaged in providing long term finance for industrial or agricultural development in India are entitled to a special deduction in the computation of their taxable profits of the amounts transferred by them out of such profits to a Special Reserve Account, upto an amount not exceeding 40 per cent of their total income as computed before making any deduction under Chapter VI-A of the Act. In the case of other financial corporations, the special deduction is allowed upto an amount not exceeding 25 per cent of the total income as so computed in cases where the paid up share capital of the corporation does not exceed Rs. 3 crores and 10 per cent where the paid up share capital exceeds Rs. 3 crores. By an amendment to the Act by Finance (No. 2) Act, 1977, limit of Rs. 3 crores or over was removed and all such approved financial corporations became entitled to a deduction in respect of amounts transferred to the special reserve account upto 25 per cent of the total income. By another amendment to the Act by Finance Act, 1979, the ceiling limit of the deductible amount in the case of all approved financial corporations was raised from 25 per cent to 40 per cent.

The Central Board of Direct Taxes in their instructions issued in November 1969 and August 1979 clarified that the amount of deduction allowable on this account is to be calculated by applying the specified percentage to the total income arrived at after the deduction is made.

(a) An industrial investment corporation was allowed (September 1980) a deduction of Rs. 58,30,000 for the assessment year 1977-78 to the extent the amount was actually carried to the special reserve account. In appeal, the Commissioner (Appeals) deleted (January 1981) the addition of Rs. 1,22,05,120 being interest on loans considered doubtful of recovery included in the total income assessed and the same was given effect to in February 1981 by the assessing officer and the total income was recomputed as Rs. 43,70,470. However, the special deduction of Rs. 58,30,000 allowed earlier in the original assessment was not correspondingly reduced. Omission to do so resulted in under-assessment of income of Rs. 16,67,300 and a consequential undercharge of tax of Rs. 9,62,866.

The Ministry of Finance have accepted the mistake (October 1984).

(b) The assessment of a financial corporation for the assessment year 1972-73 finalised in February 1975, determining the income at Rs. 11,75,908 was revised in May 1975 to allow deduction of Rs. 2,93,206 towards the amount transferred to special reserve and the revised total income was assessed at Rs. 8,82,702. While revising the assessment order again in October 1980, to allow certain deductions amounting to Rs. 9,67,071 as per the appellate orders, the deduction in question, was allowed from the net income of Rs. 8,82,702, determining loss of Rs. 84,369. The correct computation under the law requires that the relief of Rs. 9,67,071 as per appellate orders should first be deducted from the income of Rs. 11,75,908 and therefrom relief for the special reserve created allowed. The omission led to non-assessment of income of Rs. 1,67,070 in the assessment year 1972-73 resulting in short-levy of tax of Rs. 94,185 and excess carry forward of loss of Rs. 84,369 for adjustment against future years income.

The Ministry of Finance have accepted the mistake (August 1984).

(c) Public Companies formed and registered in India with the main object of carrying on the business of providing long term finance for the construction or purchase of residential houses in India, provided the company is for the time being approved by the Central Government, are also entitled to the special deduction from the assessment year 1980-81.

A Housing Development Corporation engaged in providing long-term loans for purchase or construction of houses was allowed a special deduction of Rs. 4 lakhs under the above provisions in the assessment made in March 1983 for assessment year 1980-81. The deduction was calculated by the Income-tax Officer on the basis of total income of Rs. 10,42,806 before reducing therefrom the special deduction due. The total income after making such a reduction worked out to Rs. 7,44,862. Accordingly the special deduction worked out to Rs. 2,97,944 only as against Rs. 4 lakhs allowed by the department. The excess allowance of Rs. 1,02,056 resulted in undercharge of tax of Rs. 61,656.

The Ministry of Finance have accepted the mistake (December 1984).

(d) In September 1982 the taxable income of a financial corporation for the assessment year 1979-80 was determined at Rs. 30,42,690. This income had been arrived at after allowing deduction of Rs. 4 lakhs towards amount transferred

to the special reserve and Rs. 1,09,238 towards other deductions admissible. The assessment for the assessment year 1979-80 was revised in October 1982 to allow set off of losses relating to the assessment years 1977-78 and 1978-79 wherein the entire income was adjusted towards the losses and the unadjusted balance was allowed to be carried-over to the subsequent period. However, for allowing the set off, the net income of Rs. 30,42,690 as determined earlier was considered as against the gross total income i.e. Rs. 35,51,926 before allowing other deduction towards special reserves. The incorrect allowance of set-off resulted in excess carry forward of unadjusted loss by Rs. 5,09,236, involving potential tax effect of Rs. 2,94,084.

The Ministry of Finance have accepted the mistake (August 1984).

(e) An industrial development corporation (approved by the Central Government) was assessed in September 1980 for the assessment year 1977-78 by the Income-tax Officer and the aforesaid special deductions was allowed at 10 per cent of the total income treating the corporation as not one established under the State Financial Corporation Act, 1951 and having a paid-up capital exceeding Rs. 3 crores. On appeal the Commissioner (Appeals) in his order of January 1981 decided that the assessee was a financial corporation established under the State Financial Corporation Act, 1951 and, therefore, the assessee was entitled to the special deduction at 40 per cent of the total income. Accepting the orders of Commissioner (Appeals) the department rectified the assessment in March 1981 allowing a deduction of Rs. 12,38,484 calculated at 40 per cent of Rs. 30,96,210 being the total income before allowing the special deduction therefrom.

Similarly in the assessment made in March 1981 for the assessment year 1978-79 treating the corporation as having been established under the State Financial Corporation Act, 1951 the department allowed a deduction of the total income of Rs. 42,50,741 limited to Rs. 17,00,000 being the actual credit to the special reserve account (as against Rs. 17,00,296) before allowing the special deduction.

In their orders of January 1979, for the assessment years 1975-76 and 1976-77 the Income-tax Appellate Tribunal had, however, held that the assessee corporation was not a financial corporation established under the State Financial Corporation Act, 1951. These orders were not, however, brought to the

notice of the Commissioner (Appeals) before the appeal for the assessment year 1977-78 was finalised by him in January 1981. The assessee had also admitted in April 1984 before the Income-tax Officer, that it was a financial institution created under the Industrial Development Bank of India Act, 1964 as notified by the Central Government in June 1976. As the corporation was one not established under the State Financial Corporation Act, 1951, the assessee corporation was entitled to a reduction of 10 per cent of total income for the assessment year 1977-78 and 25 per cent for the assessment year 1978-79 as against deduction of 40 per cent of total income allowed by the Income-tax Officer. The method adopted for determining the amount of deduction was also not in accordance with the instructions of the Board. The percentage deduction is to be applied on the total income as reduced by the special deduction and not before allowing the deduction. These mistakes resulted in under-assessment of income of Rs. 9,57,010 and Rs. 8,49,852 for the assessment years 1977-78 and 1978-79 respectively involving short-levy of tax of Rs. 10,43,464 for the two assessment years.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

2.11 *Incorrect allowance of provisions*

Under the Income-tax Act, 1961 any expenditure laid out or expended wholly and exclusively for the purpose of business of an assessee is admissible as a deduction provided the expenditure is not in the nature of capital expenditure or personal expenses of the assessee. A provision made in the accounts for an accrual or known liability is an admissible deduction, while other provisions made do not qualify for deduction.

(i) A Central Government public sector undertaking made 'provision for redundancy' in the accounts of the previous years relevant to the assessment years 1978-79 and 1979-80 of Rs. 82,06,992 and Rs. 1,12,67,523 respectively, representing 3 per cent of the closing stock of raw materials components, stores and spares. The provision was intended to cover the risk of loss arising out of change in the design etc. of the product by the customer after the stores and other materials were procured by the corporation.

While computing the business income of the assessee in April and September 1982 for the assessment years 1978-79 and 1979-80 respectively, the Income-tax Officer allowed the

provision of Rs. 82,06,992 and Rs. 1,12,67,523 in the respective assessments.

During the previous years relevant to these assessment years redundant materials actually charged off in the accounts, however amounted to Rs. 1,61,136 and Rs. 71,76,989 only and the balance amount provided in the accounts represented only apprehended loss and not an ascertained liability incurred during these assessment years. The company was, therefore, entitled to a deduction equal to the value of the redundant stock actually charged off and not to the entire provision made for redundancy. The incorrect allowance resulted in excess deduction of Rs. 80,45,856 and Rs. 40,90,534 leading to under-assessment of income involving short-levy of tax of Rs. 70,08,764 for the two assessment years.

The paragraph was forwarded to the Ministry of Finance in October 1984; their reply is awaited (November 1984).

(ii) A company debited an amount of Rs. 1.32,866 in its accounts for the year 1979-80 on account of 'Bonus set on' and the same was allowed by the department in the assessment completed in March 1983 for the assessment year 1980-81. As the amount of 'Bonus set on' was not an expenditure for the year but merely a provision for future payments of bonus, the same was to have been disallowed by the department. The omission resulted in under-assessment of income of Rs. 1,32,866 and short-levy of tax of Rs. 85,701.

The Ministry of Finance have accepted the mistake (June 1984).

2.12 *Incorrect allowance of bad debts*

Under the provisions of the Income-tax Act, 1961, the amount of any bad debt or part thereof which is established to have become bad in the previous year is allowable as a deduction in computing income chargeable to income-tax under the head 'profits and gains of business or profession'.

(i) In the accounts of the previous year relevant to assessment year 1980-81, a company had written off a sum of Rs. 2,99,310 being debt due to it from another company by debiting the amount in its accounts. The debtor company was a running concern and according to its directors' report it would show better results in the years to come. Therefore, it cannot be said that the debt had been established to have become bad and hence the allowance of the claim as a bad debt by the department, was not in order. The incorrect

allowance of bad debt resulted in excess carry forward of loss of Rs. 2,99,310 with a notional undercharge of tax of Rs. 1,76,967 when the loss is set off against positive income in the subsequent years.

The paragraph was forwarded to the Ministry of Finance in May 1984; their reply is awaited (November 1984).

(ii) In the case of another assessee, a deduction of Rs. 1,50,000 towards 'provision for doubtful debts' which had been disallowed by the department in the past was allowed as deduction while computing its business income in May 1981 for the assessment year 1978-79. There was, however, no evidence on record to show that any debt had been established to have become bad in the previous year relating to assessment year 1978-79. This incorrect allowance resulted in under-assessment of income by Rs. 1,50,000 and short-levy of tax of Rs. 86,625.

The Ministry of Finance have accepted the mistake (August 1984).

(iii) The debt which is written off as bad must be one which has arisen on account of business dealings of the assessee and not any other loss.

In the previous year relevant to the assessment year 1979-80, an assessee company claimed deduction on account of bad debt amounting to Rs. 4,85,660 due from its holding company. This amount was advanced by the assessee company to its holding company for constructing two floors on a building. The advance was not in the course of business dealings. The assessee company was also not engaged in the business of money lending. However, in the assessment completed in September 1982 the Income-tax Officer allowed, on the instruction of Inspecting Assistant Commissioner, bad debt of Rs. 4,85,660 as claimed by the assessee company. Since the loss incurred was not connected with the business carried on by the assessee, the amount in question was not allowable as a bad debt. The incorrect allowance resulted in under-assessment of business income by Rs. 4,85,660 and short-levy of tax of Rs. 3,31,462.

The paragraph was forwarded to the Ministry of Finance in May 1984; their reply is awaited (November 1984).

2.13 *Incorrect grant of agricultural development allowance*

Under the provisions of the Income-tax Act, 1961 where any company which is engaged in the manufacture of any article or thing, which is made from any product of agriculture has incurred after the 29th day of February 1968, whether directly or through an association or body which has been approved for this purpose by a prescribed authority, any expenditure on the provision of any goods, services or facilities specified in the Act, to a person who is a cultivator,grower or producer of such product in India, the company shall be allowed a deduction of a sum equal to one and one-fifth times the amount of such expenditure incurred during the previous year.

(i) In the previous year relevant to assessment years 1979-80 to 1981-82, a company engaged in the manufacture of sugar incurred a total expenditure of Rs. 10,36,133 by way of payment made to Cane Development Council and in the assessments made between July 1980 and March 1983, the department allowed a total weighted deduction of Rs. 12,43,420. The Cane Development Council had not been approved by the prescribed authority under the provisions of the Income-tax Act. The nature of expenditure incurred by the association, so as to ensure that the expenditure was for the specified purposes, was not also ascertained from the assessee and kept on record. In the absence of a compliance with the provisions of the law, the assessee was not entitled to the grant of agricultural development allowance which resulted in short-levy of tax of Rs. 3,16,668 for the assessment year 1979-80 together with an aggregate excess carry forward of loss of Rs. 6,95,075 for the September 1984; their reply is awaited (November 1984).

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(ii) In the assessments completed in September 1982 and March 1983 of a company for the assessment years 1979-80 and 1980-81 agricultural development allowance of Rs. 1,65,318 equal to one-fifth of expenditure of Rs. 8,26,593 incurred during the two relevant previous years was allowed as a deduction. This expenditure was incurred through the Zonal Development Council and a Cane Marketing Union which were not approved for the purpose by the prescribed authority and also included an expenditure of Rs. 1,71,288 on repairs to roads and bridges on which no deduction was admissible. The deduction allowed is, therefore, not in order. The incorrect allowance of deduction resulted in under-assessment of income by Rs. 1,65,318 and consequent undercharge of tax of Rs. 1,05,447.

The Ministry of Finance have accepted the mistake (December 1984).

2.14 *Omission to disallow interest paid on deposits.*

Under the Income-tax Act, 1961, where the assessee being a company other than a banking or financial company, incurs any expenditure by way of interest in respect of any deposit received by it, 15 per cent of such expenditure shall not be allowed as deduction in the computation of business income. The term deposit' has been explained to mean any deposit of money with and includes any money borrowed by a company except those specifically excluded in the Act.

A private company paid interest amounting to Rs. 1,17,467 in the previous year relevant to the assessment year 1982-83 on the deposits received by it from the Directors and their relatives. In the assessment made in Octoer 1982, the interest was allowed in full by the Inspecting Assistant Commissioner (Assessment) holding that the deposits were made voluntarily by the Directors and their relatives and they did not represent borrowals by the company from the public for augmenting its capital etc. However, according to law, 15 per cent of the expenditure by way of interest in respect of any deposit received by a company has to be disallowed. The excess allowance of interest resulted in excess carry forward of loss involving potential tax effect of Rs. 66,220.

The Ministry of Finance have accepted the mistake (September 1984).

2.15 *Omission to disallow excessive remuneration to Directors.*

Under the Income-tax Act, 1961, any expenditure incurred by a company which results directly or indirectly in the provision of any remuneration benefit or amenity to a director is not allowable as deduction from the business income to the extent such expenditure is in excess of Rs. 72,000 during a previous year comprising of more than eleven months.

During the previous years relevant to the assessment years 1979-80 and 1980-81 a company paid sums of Rs. 6,08,842 and Rs. 3,65,564 respectively by way of remuneration and commission to its two governing directors. In the assessments completed in May 1981 and May 1982 and revised in March 1983

for the assessment years 1979-80 and 1980-81, the remuneration and commission of Rs. 6,08,842 and Rs. 3,65,564 was allowed as deductions in full by Income-tax Officer instead of restricting the expenditure to Rs. 1,44,000 as prescribed in the Act, for the two directors in each year. This having not been done, there was under-assessment of income by an aggregate sum of Rs. 6,86,406 with consequent undercharge of tax of Rs. 5,36,017 including surtax of Rs. 1,00,258 in the two assessment years.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

2.16 *Incorrect allowance of interest.*

The Income-tax Act, 1961 specifically prvides for deduction of the amount of interest paid in respect of capital borrowed for the purposes of the business or profession. Recurring subscriptions paid periodically by share holders or subscribers in Mutual Benefit Societies in fulfilment of prescribed conditions shall be deemed to be capital borrowed.

The Articles of Association of a Mutual Benefit Society, assessed in the status of a company, permitted its members, besides subscribing to the shares, to make deposits of money with the Society or take Recurring Deposits with the Society. The Articles of Association further provided that out of the profits arrived at every year after deduction of remuneration of Directors, bonus to staff etc. 20 per cent of the balance shall be carried to a reserve fund, 2 per cent to the charity reserve, 3 per cent to the Dividend equalisation Fund and not exceeding 30 per cent for payment of dividend to the members. Out of the remaining amount a suitable sum may be utilised for grant of additional interest to the holders of Recurring Deposits by way of bonus in proportion to the paid up Recurring Deposits standing to their credit.

In its profit and loss accounts for the previous years relevant to the assessment years 1976-77 to 1979-80 the mutual benefit society carrying on banking activities for the benefit of its members, debited a total amount of Rs. 18,41,370 towards interest paid to the members on the recurring deposits made by them with the society. In the profit and loss appropriation accounts for the same years, total amount of Rs. 4,47,578 described as "proposed additional interest on recurring deposits" was also debited. In determining the business income of the society for the assessment years 1976-77 to 1979-80, completed during

the period December 1976 to November 1979, the department allowed the regular interest of Rs. 18.41,370 as well as the "additional intrest" of Rs. 4,47,578.

The assessee had debited a sum of Rs. 4,47,578 in the profit and loss appropriation accounts on account of payment of "additional interest". This payment represented additional interest of Recurring Deposit holders and the expenditure being appropriation of the profits of the society, after the profits had reached the Society, was not an allowable deduction. As a result of the incorrect deduction of the amount of Rs. 4,47,578 towards additional interest there was short-levy of tax of Rs. 2,58,477.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

2.17 *Incorrect computation of business income of a shipping company.*

Under the provisions of the Income-tax Act, 1961, in the case of a non-resident assessee engaged in the business of operation of ships a sum equal to 7½ per cent of the amount paid or payable (whether in or out of India) to the non-resident assessee on account of carriage of passengers, goods or live stock etc. shipped at any port in India consititutes its income.

A non-resident company engaged in the business of operation of ships received demurrage charges amounting to Rs. 13,60,794 and Rs. 18,35 966 during the previous years relevant to the assessment years 1980-81 and 1981-82 respectively. As these charges were paid by shippers to the assessee for detention of ships they were includible in the total income on account of carriage of goods. In the assessment done in January 1983 for the assessment years 1980-81 and 1981-82 the Income-tax Officer accepted the gross freight earnings as returned by the assessee company which did not include the demurrage charges received by the assessee company. This omission to add back the demurrage charges to the total income resulted in under-assessment of income aggregating to Rs. 2,39,759 involving short-levy of tax of Rs. 90,209.

The Ministry of Finance have accepted the mistake (January 1985).

2.18 *Excessive allowance of entertainment expenditure.*

Under the Income-tax Act, 1961, entertainment expenditure incurred by a company in the course of its business in

excess of ½ per cent of first Rs. 10 lakhs of profits or gains from business or Rs. 5,000 whichever is higher, is not allowed as business expenditure.

An assessee company was allowed an expenditure of Rs. 21,700, Rs. 45, 200 and Rs. 70,230 on entertainment of customers|foreigners in five star hotels and on gifts to them during the previous years relevant to assessment years 1979-80, 1980-81 and 1981-82 respectively. As this expenditure was in the nature of entertainment it was allowable to the extent of Rs. 5,000 only as prescribed in the Act in each of these assessment years and the excess expenditure amounting to Rs. 16,700, Rs. 40,200 and Rs. 65,230 was to have been disallowed and added to income. The omission led to under-assessment of income of Rs. 1,19,350 for the assessment years 1979-80, 1980-81 and 1981-82 and aggregate short-levy of tax of Rs. 86,663.

The Ministry of Finance have accepted the mistake (July 1984).

2.19 *Mistake in the assessment of a charitable trust*

Under the provisions of the Income-tax Act, 1961 the income from property held under trust wholly for charitable purposes, is exempt to the extent to which the income is applied for such purposes in India. The income of the trust could, however, be accumulated or set apart for future application provided the trust specifies by notice in writing given to the Income-tax Officer, the purpose for which the income is being accumulated or set apart and the period not exceeding ten years for which it is accumulated or set apart and invest the money so accumulated or set apart and invest the money so accumulated or set apart in specified securities, *viz.*, government securities or government approved securities (prior to 1 April 1971) within the time prescribed.

The assessments of a trade association (registered as a public limited company under the Companies Act 1956) for the assessment years 1969-70 and 1970-71 were revised to give effect to Appellate Assistant Commissioner's orders in October 1978 determining the income at Rs. 25,130 and Rs. 88,240 respectively. On further appeal by the assessee the Appellate Tribunal held that the association was a charitable association, the purpose being promotion of the interests of the engineering industry. As a result, the assessments were revised determining the income as 'nil' though the assessee had

accumulated the entire income during the previous years relevant to the assessment years 1969-70 and 1970-71, the notice in writing to the Income-tax Officer regarding accumulation was in fact given only in January 1975 for accumulation from the assessment year 1974-75 specifying the purpose of accumulation. Besides, the assessee had not invested the accumulated income in Government securities but the accumulations were deposited only in a bank. Accordingly, the assessee was liable to pay tax on the accumulated income. The omission to do so resulted in the non-levy of tax of Rs. 61,360.

The Ministry of Finance have accepted the mistake (December 1985).

2.20 *Mistake in the grant of export markets . development allowance.*

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

(i)(a) A public sector corporation claimed weighted deduction at the rate of one and one-half times of the expenditure of Rs. 65,48,518 incurred in connection with business of export of goods outside India during the previous year relevant to the assessment year 1979-80 and was allowed by the Income-tax Officer. The assessee company was entitled to a claim of weighted deduction at the rate of one and one-third times only since the higher weighted deduction was admissible upto the assessment year 1978-79 only. The allowance of higher rate of deduction for the assessment years 1979-80 resulted in under-assessment of income of Rs. 10,91,420 with a short-levy of income-tax of Rs. 6,30,295.

The Ministry of Finance have accepted the mistake (September 1984).

(b) In the assessment made in September 1982 for the assessment year 1979-80, the Inspecting Assistant Commissioner (Assessment) allowed a weighted deduction of Rs. 7,75,505 on the total expenditure of Rs. 15,51,011 on export promotion incurred after 31 March 1978 by a widely held domestic company calculating the deduction at one half instead of the correct allowance of Rs. 5,17,003 calculated at 1/3 of the qualifying expenditure. The mistake resulted in excess allowance of Rs. 2,58,502 leading to under-assessment of business income by the same amount involving undercharge of tax of Rs. 2,63,134 including penal interest of Rs. 70,163 for late filing of returns and non-furnishing of estimates and short-levy of surtax of Rs. 43,687 in the assessment year 1979-80.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(c) In the case of a company in which public were substantially interested, such deduction on expenditure incurred on development of export market was given by the department at one and one-half times of the expenditure of Rs. 5,28,356 in the assessment year 1980-81 (assessment made in February 1983 by Inspecting Assistant Commissioner (Assessment) as against one and one third times only of the expenditure incurred. This mistake resulted in excess allowance of Rs. 88,059 and consequent short-levy of tax of Rs. 52,064.

The Ministry of Finance have accepted the mistake (July 1984).

(ii) **Under the Income-tax Act, 1961** prior to its amendment by Finance Act (No. 2) 1980, with effect from 1 April 1981, expenditure incurred in India in connection with distribution, supply or provision of goods and expenditure incurred by the assessee on items like carriage, freight and insurance of goods whether in India or outside do not qualify for weighted deduction.

(a) In the assessment of a company for the assessment years 1978-79 to 1980-81 (assessments made in January, March and November 1980 respectively) export markets development allowance aggregating to Rs. 6,07,247 was allowed on expenditure of Rs. 13,61,665 incurred by the assessee on shipping including port charges, marine and transit insurance etc. As these expenses did not qualify for weighted deduction having been

specifically excluded in the Act, the incorrect allowance resulted in under-assessment of income totalling to Rs. 6,07,247 with consequent undercharge of tax of Rs. 2,44,351 for the three assessment years 1978-79 to 1980-81 and excess carry forward of loss of Rs. 1,76,089 in the assessment year 1981-82. This also resulted in excess payment of interest of Rs. 14,396 on advance tax paid in excess by the company for the assessment years 1978-79 to 1980-81.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(b) During the previous years relevant to the assessment years 1978-79 to 1980-81, two domestic companies incurred expenditure of Rs. 29,83,042 and Rs. 62,19,274 on blending of tea and special packing according to the requirements of the foreign buyer. These services were rendered in India in the factories of the assessees and the expenditure thereupon was also incurred in India. In the assessments completed between May 1981 and May 1982 for the assessment years 1978-79 to 1980-81, the Income-tax Officer allowed a weighted deduction of Rs. 9,94,347 and Rs. 20,73,091 respectively. Since the services were rendered in India and the expenditure was incurred in India, the assessee-companies were not entitled to deduction on account of export markets development allowance.

The incorrect allowance resulted in under-assessment of income by Rs. 9,94,347 involving short-levy of tax of Rs. 7,61,602 for the assessment years 1979-80 and 1980-81 in the case of one company; in the case of other company, there was under-assessment of income of Rs. 20,73,091 for the assessment years 1978-79 to 1980-81 and excess carry-forward of business loss by the same amount.

The Ministry of Finance have accepted the mistake (December 1984).

(c) In the assessment for the assessment year 1980-81 made by an Income-tax Officer in a central circle in April 1982, an assessee company claimed and was allowed weighted deduction in respect of commission of Rs. 4,09,982 paid by the company for export business. The commission consisted of Rs. 73,590 paid out of India and the balance of Rs. 3,36,392 paid to the agents in India. Since the commission of Rs. 3,36,392 was paid in India, the weighted deduction thereon was not admissible. The

mistake resulted in incorrect allowance of deduction of Rs. 1,12,130 with consequent short-levy of tax of Rs. 72,324.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(iii) The expenditure incurred upto 31 March 1978 on distribution, supply or provision outside India of goods, services or facilities being dealt with by an assessee is entitled for weighted deduction.

In the assessment of a company for the assessment year 1981-82 made in March 1982 weighted deduction amounting to Rs. 1,55,640 equal to one third of the expenditure of Rs. 4,66,937 incurred on development of export market was allowed by the Department. This expenditure included a sum of Rs. 3,18,057 spent on distribution and supply of goods and services outside India which did not qualify for deduction as it was incurred after 1 April 1978. The incorrect allowance of deduction resulted in under-assessment of income by Rs. 1,06,019 (being one-third of Rs. 3,18,057) and short-levy of tax of Rs. 62,684 in the assessment year 1981-82.

The Ministry of Finance have accepted the mistake (November 1984).

(iv) Under an amendment to the Income tax Act, 1961 by the Finance Act, 1978, any expenditure incurred after 31 March 1978 on advertisement or publicity outside India in respect of the goods|services or facilities dealt in or provided by the tax-payer in the course of his business did not qualify for the weighted deduction. This amendment was in force during the assessment year 1979-80

A company incurred expenditure of Rs. 3,53,973 outside India on exhibitions and fairs during the previous year commencing from 1 April 1978 relevant to the assessment year 1979-80. As this expenditure constituted expenditure on advertisement and publicity and was incurred after 31 March 1978, no weighted deduction was admissible on this expenditure. Omission to disallow this in the assessment for the assessment year 1979-80 completed in September 1982 resulted in under-assessment of income of Rs. 1,17,991 with consequent short-levy of tax of Rs. 68,410.

The Ministry of Finance have accepted the mistake (November 1984).

2.21 *Omission to disallow excessive expenditure on advertisement, publicity, sales promotion etc.*

Under the provisions of the Income-tax Act, 1961 as operative during the period 1 April 1979 to 31 March 1981 where the aggregate expenditure on advertisement, publicity and sales promotion in India does not exceed 1|4 per cent of the turn over or gross receipts of the business or profession, 10 per cent of the adjusted expenditure, where such aggregate expenditure exceeds 1|4 per cent but does not exceed 1|2 per cent of the turn over, 12-1|2 per cent of the adjusted expenditure and where such aggregate expenditure exceeds 1|2 per cent of the turn over, 15 per cent of the adjusted expenditure has to be disallowed, excepting in cases where the aggregate amount of such expenditure did not exceed Rs. 40,000. In the absence of a statutory definition of the term 'sales promotion' any expenditure for effecting sales such as a sales organisation, commission paid to salesmen, commission paid to sales agents and whatever expenses which were in connection with sales would constitute expenditure on sales promotion. The Act had specifically laid down that any expenditure incurred by an assessee on, advertisement in any small newspaper or in any newspaper for recruitment of personnel or any notice required to be published under any law in any newspaper the maintenance of any office or payment of salary to employees for the purpose of advertisement, publicity or sales promotion, holding of or participation in sales conference, trade fairs, convention or exhibition and participation of journals, catalogues or price lists had to be excluded from the purview of advertisement publicity and sales promotion expenses. In other words in view of the fact that the law itself lays down what is to be excluded, all the expenses other than those mentioned above had to be treated as constituting expenditure on advertisement, publicity and sales promotion.

The expression 'adjusted expenditure' means the aggregate of expenditure incurred on advertisement, publicity and sales promotion in India, as reduced by expenditure not allowable as business expenditure in the computation of business income of the assessee and further reduced by expenditure specifically excluded in the Act.

(i) Six companies assessed in five different Commissioners' charges debited a sum of Rs. 1,42,60,830 in their profit and loss accounts for the period relevant to the assessment years 1979-80 and 1980-81 and the expenditure was allowed while computing income. The turn over of the companies ranged between Rs. 11

crores and Rs. 54 crores. As the expenditure on advertisement, publicity and sales promotion exceeded the prescribed percentage of the turn over of the respective companies, the excess expenditure was required to be disallowed by the assessing officers of the computation of business income. In the assessment made between February 1982 and March 1983 for the assessment years 1979-80 and 1980-81 the Income-tax Officers did not disallow the excess expenditure on this account. The omission resulted in under-assessment of income of Rs. 18,56,765 involving undercharge of tax of Rs. 8,88,114 in the case of five companies and excess carry-forward of loss of Rs. 6,06,460 with a potential tax effect of Rs. 3,50,231 in the case of the sixth company.

The Ministry of Finance have accepted the mistake in respect of four cases. Replies in respect of the other two cases, reported to the Ministry of Finance in September 1984 are awaited (November 1984).

The internal audit party of the department checked the assessment of one company, but did not detect the mistake.

(ii) Fifteen other companies assessed in four different Commissioners' charges incurred expenditure of Rs. 2,84,12,902 on commission on sales, expenditure on foreign tour in connection with sales promotion, brokerage and discount on sales, export brokerage, turn over bonus in order to promote sales, overriding commission to distributors etc. The turn over of these companies ranged between Rs. 13.28 lakhs and Rs. 70.07 crores. As the expenditure was in respect of sales promotion and also exceeded the prescribed percentage of the turn over of the respective companies, the excess expenditure was required to be disallowed by the assessing officers in computing the business income of the companies. In the assessments made between September 1981 and March 1983 for the assessment years 1979-80 and 1980-81, the Inspecting Assistant Commissioner (Assessment) (in the case of two companies) and by Income-tax Officer (in the other companies) did not disallow the excess expenditure on this account. The omission resulted in under-assessment of income of Rs. 40,80,113 involving undercharge of tax of Rs. 27,19,192.

These cases were reported to the Ministry of Finance in July, August and September 1984; their replies are awaited (November 1984).

2.22 *Other computation mistakes*

(i) Under the Income-tax Act, 1961 any expenditure laid out or expended wholly and exclusively for the purpose of business is allowable as deduction in computing the business income of an assessee, provided the expenditure is not in the nature of capital expenditure or personal expenses. The deduction of admissible expenditure from business income is, therefore, allowed only if the business existed during the accounting year relevant to the assessment year and if the business had been closed and discontinued in a year previous to the commencement of the accounting year, no deduction in respect of such discontinued business is allowable.

A non resident company was engaged in executing several projects in India on contract basis of which reclamation of Salt Lake near Calcutta was one. All the projects except Salt Lake Reclamation Project were completed by 1971. The contract for Salt Lake Reclamation Project was entered into the February 1961. The project was started in May 1962 and it was terminated by the State Government in November 1970 (relevant to assessment year 1971-72). It was claimed by the assessee that the last filing work at Salt Lake Reclamation Project was done in August 1970 (assessment year 1971-72) and after the termination of the contract in November 1970, physical operation of the project ceased and the entire activities of the assessee during the previous years relevant to asesment years 1972-73 to 1978-79 consisted of disposal of assets and scraps and awaiting compensation payment. Accordingly during this period it was not engaged in any business activity but was incurring expenses. A compensation of Rs. 30,00,000 was paid to the assessee during 1971 for premature termination of contract. By mutual agreement of August 1976 a further compensation of Rs. 1,45,00,000 was paid by the State Government to the assessee in 1976 and 1977

As per the directions of the appellate authority the assessment of the income from reclamation of salt lake project of the company was reframed on the basis of the consolidated final accounts for the assessment years 1963-64 to 1978-79, were made in a single sheet of paper. The assessments were and accordingly made on completed contract basis in May 1979, computing a total loss of Rs. 2,03,33,069 (business loss of Rs. 30,25,733 unabsorbed depreciation Rs. 1,73,03,202 and unabsorbed development rebate Rs. 4,134). A refund of tax of Rs. 24,01,189 was determined in the assessment, of which Rs. 20,69,009 was refunded in March 1982.

The assessments for the assessment years 1979-80 and 1980-81 were completed in February 1982 and in November 1982 respectively computing total income at 'nil' after setting off unabsorbed depreciation of Rs. 12,95,260 and Rs. 6,30,168 out of carried forward unabsorbed depreciation of Rs. 1,73,03,202 at the end of assessment year 1978-79 as per the consolidated assessment in May 1979.

Audit has following observations to make on the above assessments.

(1) The assessee's contention that it had completed the contracted work in March 1977 (assessment year 1978-79) was accepted by the Income-tax Officer who accordingly treated the expenditure of Rs. 3,25,51,334 debited by the assessee to the profit and loss account relating to the previous years relevant to the assessment years 1972-73 to 1978-79 as expenditure incurred for business during these years.

The Income-tax Officer erred in coming to this conclusion for the following reasons :

(i) The State Government had terminated the contract with the assessee in November 1970 (relevant to assessment year 1971-72) and paid compensation for premature termination of contract;

(ii) The assessee had claimed in December 1978 that the last filing work at Salt Lake Reclamation Project was done in August 1970 (assessment year 1971-72) and no work was done thereafter as a result of failure of State Government to give new terrains where the work could be done; and

(iii) After the termination of the contract in November 1970, the physical operation of the project ceased and the entire activities of the assessee during the previous years relevant to assessment years 1972-73 to 1978-79 consisted of disposal of assets and scraps and awaiting compensation payments. During this period it was not engaged in any business activity.

As such the business activity of the assessee ceased from the previous year relevant to the assessment year 1971-82 Accordingly, expenditure incurred thereafter cannot be considered as expenditure in connection with the business activity of the assessee.

(2) It has been judicially held that the assessee could not be said to be engaged in business merely because it was engaged in realising its assets, earning interest or profits in selling stores and spares or awaiting payment of compensation. Expenditure incurred for closing down the business is also not allowable nor any depreciation during the post closure period since the business was not in existence.

In view of the statutory provisions and judicial pronouncements in the matter and the fact that the business activity of the assessee ceased from the previous year relevant to the assessment year 1971-72, the entire expenditure incurred by the assessee during the previous years relevant to the assessment years 1972-73 to 1978-79, subsequent to closure of the business should have been treated as not incurred for the purpose of the business and disallowed in the consolidated assessment made in May 1979. However, the Income-tax Officer out of a total expenditure of Rs. 3,25,51,334 disallowed expenditure totalling Rs. 26,67,793 only. Further an incorrect deduction of Rs. 15,51,652 on sales of assets during assessment years 1972-73 to 1978-79, after closure of the business was allowed by the Income-tax Officer, which is not admissible under the statute.

If the above mistakes are taken into account, the assessee would become assessable for a positive income of Rs. 1,11,02,124 in place of loss of Rs. 2,03,33,069 as computed by the Income-tax Officer. On a rough estimate the undercharge of tax on this income is Rs. 72,16,380.

(3) (i) In the assessment order of May 1979 the Income-tax Officer determined the unabsorbed depreciation at Rs. 1,73,03,202 and this was allowed to be set off against the income for the assessment years 1979-80 and 1980-81. As a result the positive income for assessment year 1979-80 and 1980-81, was determined as 'nil' figure by setting off unabsorbed depreciation of Rs. 12,95,260 and Rs. 6,30,168 respectively. In view of the facts mentioned above there can be no carry forward of any unabsorbed depreciation. As a result there was a total under-assessment of income of Rs. 19,25,428 with tax effect of Rs. 14,26,217.

Thus, the total undercharge of tax amounted to Rs. 86,42,597 (Rs. 72,16,380 plus Rs. 14,26,217).

The paragraph was sent to the Ministry of Finance in October 1984; **their reply is awaited (November 1984).**

(ii) A company engaged in the manufacture of sugar was assessed in July 1982 for the assessment year 1980-81 on a loss of Rs. 1.04 crores. For the sugar season corresponding to the assessment year 1980-81 the price of the levy sugar was fixed by the Central Government in September 1979 at Rs. 157.87 per quintal. Not satisfied with the price fixed by the Government, the assessee company filed a writ petition in the Bombay High Court. The High Court by its interim order of January 1980 fixed the price of sugar at Rs. 212.58 per quintal as against the price of Rs. 157.87 per quintal fixed by the Government. The closing stock of sugar as on 30 September 1979 was valued by the assessee company at Rs. 9,74,31,261 taking the price at Rs. 212.58 per quintal of sugar. However, the Inspecting Assistant Commissioner (Assessment) Range, while computing the business income of the assessee company for the assessment year 1980-81 worked out the value of closing stock at Rs. 8,86,33,649 and deducted Rs. 87,97,612 from the value of stock. Since the High Court had fixed the price at Rs. 212.58 per quintal of sugar by its orders of January 1980 and that being the realised and realisable value and also correctly adopted by the assessee company in its accounts, the deduction of Rs. 87,97,612 adopting a lower price by the assessing officer was not in order.

The incorrect deduction led to excess carry forward of loss by Rs. 87,97,612 involving a potential tax effect of Rs. 56,74,458.

The Ministry of Finance have accepted the mistake (January 1985).

(iii) In computing the business income of a scheduled bank, the interest tax payable by the bank under the provisions of Interest-tax Act, 1974 for any assessment year shall be deductible from the business income of the bank for that assessment year.

(a) A scheduled bank was originally assessed in September 1980 for the assessment year 1977-78 and interest-tax liability of Rs. 1,18,83,121 was allowed by the Income-tax Officer in a central circle. The interest-tax assessment of the bank was modified in April 1982 reducing the interest-tax liability to Rs. 1,17,02,212. Consequently, the income-tax assessment of the bank also required to be revised to withdraw the excess liability in the original income-tax assessment of the bank was rectified in May 1982 to give effect to the orders of Commissioner (Appeals) and the interest-tax liability was adopted as

Rs. 1,18,83,121. The omission to revise the income-tax assessment of the bank for the assessment year 1977-78 resulted in under-assessment of income by Rs. 1,80,909.

For the assessment year 1978-79, the interest-tax liability amounting to Rs. 1,35,68,578 was allowed in the revised income-tax assessment of the bank made in July 1982. The interest-tax assessment was modified in April 1982 reducing the liability to Rs. 1,32,20,250. No revision of the income-tax assessment consequent upon the revision of interest-tax liability was made. The omission resulted in under-assessment of income of Rs. 3,48,328.

The total under-assessment of income for the two years was Rs. 5,29,237 resulting in total short-levy of tax of Rs. 3,05,533.

The Ministry of Finance have accepted the mistake (September 1984).

(b) In the original assessments for the assessment years 1975-76 to 1978-79 made between March 1978 and November 1979 of a banking company under the Interest-tax Act, 1974, the Income-tax Officer levied interest-tax at 7 per cent on the additional amount collected by the bank from its customers towards interest-tax payments along with the interest due from them. The income-tax assessments of the bank for the assessment years 1975-76 to 1978-79 were also completed allowing the full interest-tax. The Appellate Tribunal, however, held in November 1979 that in respect of the interest-tax assessments for the assessment years 1975-76 and 1976-77 the provisions of the Interest-tax Act, did not contemplate levy of tax on 'interest on interest' and deleted the addition. For the assessment years 1977-78 to 1978-79 also the levy of interest-tax on the additional amount collected was deleted by the Commissioner (Appeals). The interest-tax assessments for the assessment years 1975-76 to 1978-79 were accordingly revised (April 1981) by the Income-tax Officer to give effect to the appellate orders and an aggregate refund of Rs. 2,22,890 was made. However, the amount of interest-tax liability reduced in the revised interest-tax assessments for the assessment years 1975-76 to 1978-79 was not correspondingly disallowed in the income-tax assessments. The omission to add back the amount of Rs. 2,22,890 in the income-tax assessment resulted in total short-levy of Rs. 1,38,255 for the four assessment years.

The Ministry of Finance have accepted the mistake (January 1985).

(iv) Under the Income-tax Act, 1961, any sum paid on account of any rate or tax levied on the profits or gains of any business or profession shall not be deducted in computing the income chargeable under the head 'profits and gains of business or profession'. It has been judicially held that the term 'tax' cannot be understood to mean only income-tax. The tax sought to be imposed on a company by the Companies (Profits) Surtax Act is essentially of the same character as income-tax or excess profits tax and the disallowance of tax is applicable to surtax also.

In the assessment of a company in which the public were substantially interested for the assessment year 1979-80 completed in September 1982 and revised in October 1982, a deduction of Rs. 2,00,000 towards surtax expenditure was allowed by the department as claimed by the assessee. A surtax is not an allowable deduction in computing the business income, the department should have disallowed the surtax liability. The omission to do so resulted in under-assessment of income of Rs.2,00,000 involving short-levy of income-tax of Rs. 1,36,650 (including surtax of Rs. 21,150).

The paragraph was sent to the Ministry of Finance in June 1984; their reply is awaited (November 1984).

(v) The income-tax assessment of a corporation engaged in construction activity for the assessment year 1979-80 was finalised in September 1982. An expenditure of Rs. 2,53,107 on account of hire charges of machinery hired during the previous years relevant to earlier assessment years was debited to the profit and loss acconut of the previous year relevant to the assessment year 1979-80. As the assessee maintained its accounts on mercantile system the expenditure of Rs. 2,53,107 was not allowable for the assessment year 1979-80. The omission to add back the inadmissible expenditure resulted in the excess carry forward of loss of the company by Rs. 2,53,107 for the assessment year 1979-80.

The Ministry of Finance have accepted the mistake (August 1984).

(vi) Any revaluation of stock of an assessee on account of following a method of valuation of stock different from that followed regularly in income-tax assessment is required to be revalued on the basis of the method regularly followed in earlier assessment and the differences between the book value and the

revised value to be determined. In case the net effect of such difference results in increase of income, it is to be added to the book result. If it results in reduction of income, it is deducted therefrom.

In the assessment of an assessee company for the assessment year 1980-81 completed in March 1983, the assessing officer revalued both the opening and the closing balance of stock of the relevant previous year and determined the undervaluation of opening and closing stock at Rs. 17,860 and Rs. 1,26,524 respectively. As the under valuation of closing stock was more than that of opening balance, the net result would be an increase in the taxable income, which was required to be added back to the book result instead of deducting it therefrom. The omission to do so resulted in under-assessment of income of the assessment year 1980-81 by Rs. 2,17,328 involving a potential tax effect of Rs. 1,28,495.

The Ministry of Finance have accepted the mistake (August 1984).

(vii) During the previous year relevant to the assessment year 1981-82 a private limited company debited a sum of Rs. 5,68,556 in its accounts on account of maintenance carried out in respect of a building constructed by it and was allowed as deduction by the department in computing the business income of the assessee in June 1982. These charges were, however, recoverable from the individual members occuping the building and thus not being the assessees liability was not an admissible business expenditure. The incorrect allowance of deduction resulted in excess carry forward of loss of Rs. 5,68,556 involving notional tax effect of Rs. 3,97,278 for set off against future years, income.

The Ministry of Finance have accepted the mistake (December 1984).

(viii) A tea company credited a sum of Rs. 1,72,000 in the profit and loss account relevant to the assessment year 1976-77 on account of "contingency provision written back". While computing the income in March 1978, the Income-tax Officer did not take into account the credit, stating that contingency provision made in the earlier years was disallowed in the respective assessments and hence there was no need to treat the

credit of Rs. 1,72,000 as income. In the earlier years' assessments, however, no such disallowance was in fact made by the Income-tax Officer. The incorrect exclusion of Rs. 1,72,000 resulted in short-levy of tax of Rs. 50,568.

The paragraph was sent to the Ministry of Finance in September 1984; thier reply is awaited (November 1984).

(ix) Expenditure incurred by an assessee after the commencement of his business, in connection with the extension of his industrial undertaking or in connection with the setting up a new industrial unit, constitute preliminary expenses and are not allowable as deduction in income computation as the expenditure was not incurred wholly and exclusively for the purposes of the existing business. The Income-tax Act, 1961, however, provides that such preliminary expenditure can be amortised and claimed as deduction of an amount equal to one-tenth of such expenditure for each of the ten successive previous years beginning with the previous year in which the extension of the industrial undertaking is completed or the new industrial unit commences production or operation. The type of expenditure constituting the preliminary expenses specified in the Act inter-alia includes expenditure in connection with issue of shares, expenditure on market survey etc.

On amalgamation of a private non-resident company and a resident company in which the public were not substantially interested, a new company (assessee) was incorporated in June 1977. In the previous year relevant to the assessment year 1979-80, the assessee debited the profit and loss account with expenditure of Rs. 2,91,400 incurred in connection with public issue of shares, solicitors fees relating to amalgamation and expenditure on market research etc. and claimed it as expenditure in the computation of income. The Inspecting Assistant Commissioner (Assessment) while making the assessment in November 1981, allowed the claim in full. As the expenditure constituted preliminary expenses before setting up business and such expenditure is allowable in ten equal instalments under the amortisation provisions of the law, only a sum of Rs. 29,140 was allowable as deduction for the assessment year 1979-80. The excess relief of Rs. 2,62,260 led to short-levy of tax of Rs. 1,73,484 including interest for late filing of the return.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(x) While computing income under the mercantile system of accounting a provision made for any accrued or known liability is allowable as deduction whereas an amount appropriated to a reserve is not. The Income-tax Act, however, specifically provides that (i) any provision for bad and doubtful debts made by a scheduled bank in relation to advances made by its rural branches and (ii) any special reserve created by a financial corporation engaged in providing long-term finance for industrial or agricultural development or by a public company having its objects of providing long-term finance for construction or purchase of house properties in India for residential purposes are allowed as deduction in the computation of income. Reserves in all other cases and provisions made, not for accrued or known liability, are disallowable.

The question whether reserves|provisions made by an assessee under statutory compulsions can be allowed as deduction while computing taxable income of an assessee had been dealt with by the Supreme Court and High Courts in a number of cases. In the case of M|s. Pune Electric Supply Company (April 1955), the Supreme Court held that the amount taken to the consumers benefit reserve under the Electricity (Supply) Act, 1948 was allowable as a deduction, as the amount was reserved to be returned to the consumers and it did not form part of assessee's real profits. As regards deduction for 'reserve for contingencies' under the same Electricity (Supply) Act, 1948, the High Courts had taken different views. The Kerala (December 1972), Bombay (July 1973) and Patna (July 1978) High Courts had held that the amount taken to the reserve was allowable as a deduction while computing income from business, whereas the Madras (December 1976), and Calcutta (March 1981 and June 1983) High Courts had taken the view that the amounts credited to the reserve was not admissible as a deduction while computing income. The Calcutta High Court in its decision of June 1983 exhaustively dealt with all the earlier case-laws and lent support to the departmental view that the reserve was not to be allowed as a deduction. According to the High Court, if a sum is set apart by an assessee under compulsion of law for meeting unknown business needs of the company, a diversion of income at source by an over-riding title does not take place. In such cases, according to the High Court, the assessee has title to the fund, exercises dominion over the fund and regulates its use. In the opinion of the High Court, it cannot be said that the amount that has been appropriated to the fund does not form part of the real income of the assessee.

The Madras High Court, in a case arising under the Co-operative Societies Act ruled that merely because the statute contemplated creation of a particular fund and its utilisation in a particular manner, it did not mean that there was any diversion by over-riding title as such. The High Court came to the conclusion that the contribution by way of fixed percentage of net profits to the Education Fund, for subsequent remittance to the Co-operative union was done after the profits were earned and had reached the assessee and hence was not admissible as a deduction while computing income. This decision of the High Court was also in favour of the Revenue.

In spite of conflicting views of various High Courts on the subject of allowability as a deduction while computing income, of amounts appropriated to reserves|provisions under a statute, the department have not issued any instructions for the guidance of the assessing officers to regulate the deduction so as to ensure uniformity in assessment.

(a) Two companies engaged in the business of manufacture of sugar, made a provision of Rs. 5,37,834 during the previous years relevant to the assessment years 1976-77 to 1979-80 towards contribution to Molasses Fund and debited the same in the profit and loss appropriation account of the respective years. The provision was made in terms of the U.P. Molasses Control Act, 1964 and was intended for creation of a fund out of sales proceeds of molasses for utilisation for provision and maintenance of adequate storage facilities of molasses. In the assessments (assessed in Calcutta charge) completed between June 1978 and March 1982 for the assessment years 1976-77 to 1979-80, this provision was allowed by the Income-tax Officer as business expenditure. The provisions made by the company were only appropriation of income and were not allowable as deduction. The incorrect deduction allowed resulted in excess carry forward of loss of Rs. 50,846 for the assessment year 1978-79 in the case of one company and short-levy of tax of Rs. 2,81,235 for the assessment years 1977-78 to 1979-80 in the case of both the companies.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(b) In the case of another sugar manufacturing company assessed in a different commissioner's charge (in Maharashtra) in the assessments completed in September and November 1981 for the assessment years 1977-78 and 1978-79, the assessee

company was allowed deduction of Rs. 37,978 and Rs. 40,734 on account of provision for Molasses storage fund made in terms of U. P. Molasses Control Act, 1964. The provisions made for the creation of the fund amounted to appropriation of profits already earned and was required to be added back to the profits in the computation of business income. The incorrect deduction allowed resulted in under-assessment of income by Rs. 78,712 involving short-levy of tax of Rs. 45,456 in both the assessment years.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(c) In the assessment of a public limited company, for the assessment year 1980-81 completed in February 1983, an amount of Rs. 1,76,807 debited in the accounts towards transfer to 'storage reserve' out of sale of molasses and claimed as deduction by the assessee, had been allowed by the Income-tax Officer, even though deduction for a similar reserve of Rs. 44,485 claimed for the previous assessment year 1979-80 had been disallowed. The erroneous allowance of deduction for the reserve of Rs. 1,76,807 for the assessment year 1980-81 resulted in excess carry forward of loss of like amount, involving a potential tax effect of Rs. 99,675 for the assessment year 1983-84 in which the assessee had positive income after set off of carried forward losses of earlier years.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(xi) Under the provisions of the Income-tax Act, 1961 where any depreciable asset is sold, the difference between the sale price and the written down value is chargeable to tax as income in the year in which the surplus arises.

A non-resident company engaged in the execution of several projects in India on contract basis, sold its earth-moving machinery for Rs. 16,00,000 in the previous year relevant to the assessment year 1979-80 and the "Dredger Dream" for Rs. 11,01,000 in the previous year relevant to the assessment year 1980-81. In the depreciation schedule filed by the assessee with the return for the assessment year 1978-79 the written down value of these assets were shown as Rs. 3,50,632 and Rs.2,55,791 respectively. In the assessments for the assessment years 1979-80 and 1980-81 made in February 1982 and November 1982 respectively, while computing the profits on

the sale of these assets, the written down values of the assets were taken at Rs. 6,27,551 and Rs. 4,58,223 respectively instead of the correct written down value of Rs. 3,50,632 and Rs. 2,55,791 as given in the depreciation schedule. The incorrect adoption of the written down values of assets led to short computation of income by Rs. 4,79,851 in the assessment years 1979-80 and 1980-81 involving short-levy of tax of Rs. 3,55,866.

The Ministry of Finance accepted the mistake (December 1984).

Irregularities in allowing depreciation development rebate and investment allowance.

2.23 *Mistakes in the allowance of depreciation*

Under the Income-tax Act, 1961, in computing the business income of an assessee a deduction on account of depreciation is admissible at the prescribed rates on plant, machinery or other assets provided it is owned by the assessee and used for the purpose of his business during the relevant previous year.

Depreciation on buildings and plant and machinery is calculated on their written down value according to the rates prescribed in the Income-tax Rules, 1962. Special rates of depreciation ranging from 15 per cent to 100 per cent are prescribed for certain specified items of machinery and plant. A general rate of 10 per cent (15 per cent from the assessment year 1984-85) is prescribed in respect of machinery and plant for which no special rate has been prescribed.

(i) In the case of a private limited company, while completing the assessment in September 1981, for the assessment year 1980-81, the Inspecting Assistant Commissioner (Assessment) allowed depreciation on factory building and machinery of Rs. 5,36,030. The assessee company had taken the factory building on lease from another company and did not also acquire the machinery in question during the previous year relevant to the assessment year. As the assets were thus not owned by the assessee, the depreciation allowed by the assessing officer was not in order and resulted in total under-assessment of income by Rs. 5,36,030 involving short-levy of tax of Rs. 3,45,740.

The Ministry of Finance have accepted the mistake (August 1984).

(ii) It has been judicially held that the expression "used for the purpose of the business" means that the assets must be used by the owner for the purposes of carrying on the business and earning profits therefrom. If the assets have not at all been used for any part of the accounting year, no depreciation allowance can be claimed.

In the Auditor's as well as the Director's report of a company for the previous years relevant to the assessment years 1977-78 to 1980-81 it was stated that the entire plant and equipment of one of its collieries was submerged under water since December 1975 and the plant and machinery remained wholly unused throughout the period. For the assessment years 1977-78 to 1980-81 the Income tax officer had however allowed a total depreciation of Rs. 85,26,311 on the said plant and machinery. The incorrect allowance of depreciation resulted in excess carry forward of depreciation of Rs. 85,26,311 for set-off against the income of subsequent years.

The paragraph was forwarded to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(iii) With a view to encouraging the use of renewable energy devices, depreciation at the rate of 30 per cent was allowed with effect from 1 April 1981 on any special devices including electric generators and pumps running on wind energy.

In the case of any new machinery or plant which has been installed after the 31 March 1980 but before 1 April 1985, the Act further provides for allowing additional depreciation of a sum equal to one half of the normal depreciation admissible in respect of the previous year in which such machinery or plant is installed.

A company engaged in the manufacture of iron and steel products claimed depreciation on electric generator at the rate of 30 per cent on its actual cost and additional depreciation at 50 per cent thereof for the assessment year 1981-82 on the ground that the electric generator was exclusively used for renewal energy. While finalising the assessment on 31 March 1982 the Income-tax Officer allowed depreciation on electric generator as claimed by the assessee.

There was however nothing on record to show that the generator was being run on wind energy to be eligible for depreciation at 30 per cent. In view of this, depreciation was admissible at

the general rate of 10 per cent only. The resultant excess allowance of additional depreciation led to an excess allowance of depreciation of Rs. 8,79,975. The total excess allowance of depreciation of Rs. 8,82,717 (including a minor mistake) resulted in undercharge of tax of Rs. 4,57,774 including interest of Rs. 55,260.

The Ministry of Finance have accepted the mistake (September 1984).

The Internal Audit Party of the department checked the assessment, but failed to detect the mistake.

(iv) In the assessment made in August 1982 of a public limited company for the assessment year 1982-83 depreciation at 30 per cent and additional depreciation at 15 per cent were allowed on its machinery 'crusher Plan' costing Rs. 28,63,456 instead of at 15 per cent and 7½ per cent respectively. The mistake led to excess allowance of depreciation to the extent of Rs. 6,44,277 with consequent short-levy of tax of Rs. 3,63,211.

The Ministry of Finance have accepted the mistake (September 1984).

(v) In the case of an assessee company engaged in the manufacture of Radio-frequency connectors and printed circuited edge connectors for the assessment years 1978-79 and 1979-80 (made in March 1981) depreciation on toolings was incorrectly granted at the rate of 30 per cent as against 15 per cent correctly admissible. The mistake resulted in grant of excess depreciation of Rs. 1,04,240 and 97,219 in the assessment years 1978-79 and 1979-80 respectively leading to short-levy of tax of Rs. 1,16,341.

The Ministry of Finance have accepted the mistake (December 1984).

(vi) In the previous year relevant to the assessment year 1981-82, a company purchased two shovels costing Rs. 23,51,828 for the purpose of its business and claimed depreciation allowance thereon at the general rate of 10 per cent. Through a revised return in February 1982, the assessee claimed depreciation allowance at 30 per cent on shovels, and the claim was allowed by the assessing officer in the assessment made in October 1982 for the assessment year 1981-82. No special rate of depreciation is prescribed for shovels and, therefore, depreciation is admissible at the general rate of 10 per cent only. The incorrect allowance of depreciation at 30 per cent resulted in the excess deduction of Rs. 7,05,548 involving short-levy of tax of Rs. 4,55,080.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

(vii) Depreciation at the rate of twenty per cent is admissible in respect of machinery used in the manufacture of electronic goods or components.

A company in which the public were not substantially interested claimed for the assessment year 1982-83 depreciation allowance of Rs. 1,70,777 at 30 per cent on moulds used in the manufacture of electronic goods. While completing the assessment in August 1982 the assessing officer allowed the claim. However, in the revised assessment for the assessment year 1981-82 made in July 1983, depreciation was allowed on the moulds at 20 per cent only based on a clarification issued (March 1983) by the Inspecting Assistant Commissioner of Income-tax (Audit).

The omission to revise the assessment for the assessment year 1982-83 led to excess allowance of Rs. 1,05,752 by way of depreciation with consequent short levy of tax of Rs. 66,006.

The Ministry of Finance have accepted the mistake (October 1984).

(viii) (a) Depreciation was admissible at a higher rate of 15 per cent in respect of machinery and plant coming into contact with corrosive chemicals.

A company manufacturing synthetic yarn furnished along with the return of income for the assessment year 1980-81, details of plant and machinery coming into contact with corrosive chemicals and claimed depreciation at the rate of 15 per cent. In the assessment made in March 1983, the assessing officer, however, allowed depreciation at the higher rate of 15 per cent on the entire plant and machinery instead of restricting it to those machinery coming into contact with corrosive chemicals and allowing depreciation on other plant and machinery at the rate of 10 per cent. The adoption of the incorrect rate of depreciation resulted in excess allowance of depreciation of Rs. 22,76,050 (including extra shift allowance) with under-assessment of income to the same extent with consequent under-charge of tax of Rs. 16,89,960 (including short levy of interest for short payment of advance tax).

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

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

In the assessments made between September 1979 and June 1982 of a company running sugar mills, for the assessment years 1976-77, 1977-78 and 1979-80 to 1980-81 depreciation at the rate of 15 per cent instead of at the rate of 10 per cent and extra shift allowance at full rate of the normal depreciation allowance was allowed on the plant and machinery as claimed by the assessee. The mistake resulted in excess carry forward of depreciation of Rs. 22,57,548 for the assessment year 1981-82.

The Ministry of Finance have reported in October 1984 that there was no mistake in grant of depreciation at 15 per cent since the processing of sugar cane involves use of acids at all stages and the machinery comes in contact with corrosive elements.

When a similar mistake in respect of another Sugar Mill was pointed out in the Audit Report of the Comptroller & Auditor General for the year 1982-83 the Ministry of Finance had however accepted the mistake in December 1983.

The reply of the Ministry of Finance would require reconsideration (November 1984).

(ix) (a) Under the provisions of the Income-tax Act, 1961, expenditure of a capital nature incurred by an assessee on scientific research during the relevant previous year is deductible in computing the taxable income for that assessment year. In such a case the assessee will not be entitled to depreciation in respect of the capital expenditure on scientific research represented by any asset either in the same or in any other previous year.

While computing in income of a company in April 1982, for the assessment year 1978-79 depreciation of Rs. 9,53,945 was allowed on assets valued at Rs. 93,46,284 acquired for scientific research during the earlier year(s) though the entire expenditure incurred on the assets was allowed as deduction in the earlier assessments. The incorrect allowance of depreciation resulted in under-assessment of income of Rs. 9,53,945 with a consequent under-charge of tax of Rs. 5,50,902.

The Ministry of Finance have accepted the mistake (October 1984).

(b) While completing (April 1978) the income-tax assessment of a company in which the public are substantially interested, for the assessment year 1975-76, the assessing officer disallowed the claim of the assessee for capital expenditure on scientific research of a sum of Rs. 16,90,376 including the value of land of Rs. 1,269 and instead, allowed depreciation of Rs. 3,91,450 on the machinery valued at Rs. 16,89,107. The Commissioner of Income-tax (Appeals) allowed (May 1979) the appeal of the assessee for the deduction of Rs. 16,90,376 and it was given effect to in July 1979 by the Income-tax Officer. However, the depreciation of Rs. 3,91,450 already allowed in the assessment year 1975-76 was not withdrawn. Besides, depreciation of Rs. 5,08,649 on the written down value of the machinery was also erroneously allowed in the assessments for the assessment years 1976-77 and 1977-78 completed in July 1979 and December 1979. The department had initiated (July 1981) rectificatory proceedings and issued a notice to the assessee for rectification of assessment for the assessment year 1975-76 but no follow-up action had been taken till the date of Audit (July 1983). No action was initiated for the assessment years 1976-77 and 1977-78. The omission to withdraw the depreciation allowance of Rs. 9,00,099 incorrectly allowed resulted in total short-levy of tax of Rs. 6,14,876 including surtax of Rs. 95,073.

The Ministry of Finance have accepted the mistake (January 1985).

(x) In computing the business income, the Income-tax Act, 1961 provides for grant of depreciation at the prescribed rates on the actual cost or the written down value of the assets, as the case may be, owned by the assessee and used for the purpose of business. The Act, further provides that the term 'actual cost' for the purpose of allowance of depreciation means the actual cost of the assets to the assessee reduced by that portion of the cost, if any, as has been met directly or indirectly by any other person or authority. The Central Board of Direct Taxes clarified in March 1976 that the subsidy received under "10 per cent central outright grant of subsidy scheme, 1971" for establishing industrial units in selected backward areas constitute capital receipts in the hands of the recipient and as such this amount would have to be reduced from the cost of the assets, for the purpose of allowing depreciation on such assets.

(a) In the previous year relevant to the assessment year 1977-78, an assessee company received a subsidy of Rs. 8,22,525 under the above scheme. The original cost of the asset (Plant

and Machinery) installed in the said previous year, was, therefore, required to be reduced to arrive at the actual cost for the purpose of allowing depreciation. The omission resulted in excess allowance of depreciation of Rs. 4,01,364 in the assessment years 1977-78 to 1979-80 with consequent under-charge of tax aggregating to Rs. 3,29,240.

The Ministry of Finance have accepted the mistake (September 1984).

(b) The assessments of a public limited company engaged in the manufacture of watches, machine tools etc. for the assessment years 1977-78 and 1978-79 were completed by the Income-tax Officer in February 1980 and April 1981 respectively. The assessee company received a subsidy of Rs. 10,00,000 under "Central Outright grant of subsidy scheme, 1971" during the previous year relevant to the assessment year 1977-78 from the Central Government for acquisition of machinery and other assets in respect of the watch factory at Srinagar. The assessee had also received subsidy of Rs. 17,12,370 under the same scheme earlier to the assessment year 1977-78. The actual cost of assets for purpose of allowance of depreciation has to be arrived at after reducing the total amount of subsidy of Rs. 27,12,370 received by the assessee company from the actual cost of assets. While completing the assessments, the actual cost of the assests was not however reduced; instead depreciation was calculated on their full value. The omission resulted in excess deduction of depreciation of Rs. 5,15,370 for the assessment years 1977-78 and 1978-79 leading to short-levy of tax of Rs. 2,97,601.

The Ministry of Finance have accepted the mistake in principle (December 1984).

(c) In the case of a company, a subsidy of Rs. 13,33,332 was received from the Central Government in two instalments during the previous years relevant to the assessment years 1976-77 and 1978-79 towards the cost of the assets in its Mechanical Compost Plant which was commissioned in the assessment year 1979-80. Accordingly in computing depreciation and investment allowance on the said assets in the assessment year 1979-80, the above subsidy of Rs. 13,33,332, received by the assessee, was required to be deducted from the cost of the assets. The omission resulted in excess allowance of depreciation and investment allowance for an aggregate sum of Rs. 4,66,666 leading to underassessment of total income by the same amount in the assessment year 1979-80. As, however, the total income for this

year was reduced to nil after adjusting a portion of the unabsorbed loss of earlier assessment years, the underassessment led to excess carry forward of unabsorbed depreciation and investment allowance of Rs. 4,66,666.

The Ministry of Finance have accepted the mistake (July 1984).

(d) In the case of a coal mining company, a part of the cost of construction of buildings for housing its employees and water supply installations under Coal Mines Welfare Organisation was met by a Central Government subsidy amounting to Rs. 1,19,12,310 and Rs. 9,50,913 respectively in the previous year relevant to the assessment year 1980-81. The subsidies received by the assessee were not however, deducted to arrive at the actual cost of the assets. The omission resulted in excess allowance of depreciation of an aggregate amount of Rs. 7,38,253 with consequent excess carry forward of loss by the same amount for the assessment year 1980-81.

The Ministry of Finance have accepted the mistake (August 1984).

(e) A company in which public are substantially interested purchased and installed a 1500 K.W. Turbo Alternator set for Rs. 19,24,605 during the previous year relevant to the assessment year 1977-78. The company had received a subsidy of Rs. 4,65,335 from Uttar Pradesh State Financial Corporation to meet a portion of the cost of the machinery. As such the cost of the machinery for computation of depreciation worked out to Rs. 14,59,270 only after reducing the subsidy received from the initial cost. However, in the assessment made in July 1980 and July 1981 the Income-tax Officer allowed depreciation, initial depreciation and extra shift allowance on the entire cost of Rs. 19,24,605 for the assessment years 1977-78, 1978-79 and 1979-80.

The mistake resulted in excess allowance of total depreciation of Rs. 2,19,017 for the three assessment years and led to excess carry forward of unabsorbed depreciation aggregating to Rs. 2,19,017 involving a notional tax effect of Rs. 1,03,484.

The Ministry of Finance have accepted the mistake (January 1985).

(xi) In the draft assessment order for the assessment year 1978-79 of a private limited company, the Income-tax officer in a central circle proposed to the Inspecting Assistant Commissioner that the depreciation on "Roads, Bridges and Jetties" as claimed by the assessee to the extent of Rs. 1,30,918 should be disallowed. In his direction, the Inspecting Assistant Commissioner however, allowed depreciation on these assets to the extent of Rs. 65,459. While completing the assessment in August 1981, the Income-tax Officer, not only wrongly allowed the depreciation of Rs. 1,30,918 as claimed by the assessee, but also allowed the relief of Rs. 65,459 as directed by the Inspecting Assistant Commissioner. In appeal, the Commissioner of Income-tax (Appeal) allowed a further relief of Rs. 65,459 on "Roads, Bridges and Jetties". This relief was also allowed by the Income-tax Officer in September 1982. Thus, depreciation of Rs. 1,30,918 was allowed twice by the Income-tax Officer. This had resulted in short computation of Income of Rs. 1,30,918 with a consequent short levy of tax of Rs. 82,477 for the assessment year 1978-79.

The Ministry of Finance have accepted the mistake. (August 1984).

(xii) While making the assessment of a company for the assessment year 1978-79 in January 1983, the Income-tax Officer allowed depreciation of Rs. 1,63,37,183 as claimed by the assessee company. The correct amount of depreciation admissible, however, worked out to Rs. 1,47,21,006 on the basis of the written down value, determined at the time of completion of assessment for the assessment year 1977-78 in September 1981. The mistake occurred as the Income tax officer overlooked the fact that the assessee filed the return for the assessment year 1978-79 in March 1981(i. e. earlier to the completion of assessment for the assessment year 1977-78). The excess allowance of depreciation amounted to Rs. 16,16,177 leading to short levy of tax of Rs. 12,06,476 including Surtax.

The case was seen by the Special Audit Party of the Department but the mistake remained unnoticed.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(xiii) The Income tax Act, 1961 provides for deduction on account of depreciation on plant and machinery owned and used

by the assessee for the purpose of his business during the relevant previous year, development rebate in respect of new plant and machinery and tax relief in respect of a newly established Industrial Undertaking. Actual cost of the machinery or its written down value for subsequent years forms the basis for calculation of these allowances. Any change effected in the original cost subsequently will necessitate revision of the allowance already allowed.

In the case of a company, liability on account of custom duty of Rs. 4,55,621 allowed in the previous year relevant to the assessment year 1969-70 was taken into account for allowing depreciation, development rebate and tax holiday relief in respect of a newly established industrial undertaking of the company for the assessment years 1969-70 to 1974-75. The customs duty was not paid and on the duty liability ceasing to exist, the same was written back in the company's account for the previous year relevant to the assessment year 1975-76. The write back resulted in reduction of cost of the assets by Rs. 4,55,621 requiring downward revision of tax reliefs already allowed in the years 1969-70 to 1974-75. The revision not having been done there was excess allowance of depreciation, development rebate and tax holiday relief in respect of newly established undertaking aggregating Rs. 3,58,851 with consequent short levy of tax of Rs. 2,03,104.

While accepting the mistakes for the assessment years 1971-72 to 1974-75 the Ministry of Finance have stated (January 1985) that action for assessment years 1969-70 and 1970-71 (involving revenue of Rs. 32,613) has become time barred.

2.24 *Incorrect allowance of extra shift depreciation*

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

In September 1970, the Board issued instructions in modification of their instructions of December 1967 stating that where a concern has worked double shift or triple shift, extra shift allowance may be allowed in respect of the entire plant and machinery used by the concern without making any attempt to determine the number of days on which each machine had actually worked double or triple shift during the relevant previous year. These instructions ran counter to the instructions of September 1966 issued at the instance of audit and as such grant of extra shift allowance for the concern as a whole without reference to each machinery, is not in accordance with the law. The Board was accordingly requested in July 1971 to re-examine the question. The Board, however, repeated the instructions in their circular of March 1973. On a reference seeking their advice, the Ministry of Law opined in February 1978 that if in any particular year any particular machine or plant was not at all used even for a day, the normal depreciation allowance was not admissible and as a corollary thereto extra shift depreciation would not be admissible and suggested that the Board's instruction of September 1970 should be modified. It followed from the Law Ministry's advice that depreciation both normal and extra shift should be calculated not for the entire concern but with reference to the various items of machinery and plant.

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

The point came before different High Courts on a number of occasions. The Madras High Court held in September 1981 that the Income-tax Officer has to apply his mind and examine whether the machinery owned by the assessee has been used by him in extra shift. As long as the particular machine has worked extra shift, it would be eligible for extra shift allowance on the number of days it has worked. Earlier the Calcutta and Allahabad High Courts had also held in 1968, 1972, 1974 and 1980 that the extra shift allowance has to be calculated in proportion to the number of days the plant and machinery had actually worked and not an amount equal to the full amount of normal depreciation. In fact these two High Courts had held even prior to the issue of Board's instruction of September 1970 that the extra shift allowance should be allowed proportionately for the actual number of days the machinery had worked. In all these cases, the department presented its case and succeeded in obtaining the Court's verdict that the extra shift allowance is to be allowed only for the number of days the plant and machinery has worked double or triple shift. There is no judicial decision for the opposite view taken in the Board's instruction of September 1970.

The non-maintainability in law of Board's instructions of September 1970 was again referred to the Board in May 1984 for issuing revised instructions which would be in conformity with the Act and judicial pronouncements. The Board have however not revised their instructions of September 1970 so far (November 1984).

A few cases where the extra shift allowance was incorrectly allowed were reported in the Report of the Comptroller and Auditor General of India for the year 1982-83. A few more such cases are given below.

(i) Two public limited companies claimed extra shift depreciation allowance of Rs. 1,14,591 and Rs. 65,324 for the assessment year 1979-80 for having worked triple shift. The assessing Officers while completing their assessments in April 1982 and September 1982 respectively, allowed the claim in full. Most of the items of machinery and plant of one of the companies had been purchased during the last quarter of the relevant previous year and in respect of the other, they had been installed during the second quarter of the relevant previous year. As the machinery and plant purchased|installed during

the course of the relevant previous year had not worked on all the days on which the concern had worked triple shift, the extra shift depreciation allowance should have been proportionately reduced. The omission resulted in total excess allowance of extra shift allowance of Rs. 1,38,761 and short-levy of tax of Rs. 1,03,585 (including surtax of Rs. 16,467 in respect of one of the companies).

The paragraph was sent to the Ministry of Finance in August 1984 ; their reply is awaited (November 1984).

(ii) In the assessment made in December 1982 of a company assessed in another commissioner's charge for the assessment year 1980-81 extra shift allowance equal to normal depreciation for working of three shifts, amounting to Rs. 1,40,278 was allowed on machinery which was purchased between August 1979 and December 1979 of the previous year ending 31 December 1979 of the company. As the machinery did not work on all the days the concern had worked triple shift during the previous year, the extra shift allowance should have been restricted proportionate to the amount worked out on the basis of the actual number of days the machinery had worked extra shifts. On this basis, extra shift allowance admissible worked out to Rs. 13,478 only as against Rs. 1,40,278 allowed by the department. The mistake resulted in excess grant of extra shift allowance by Rs. 1,26,800 leading to short levy of tax of Rs. 74,970.

The paragraph was sent to the Ministry of Finance in September 1984 ; their reply is awaited (November 1984).

2.25 *Other cases of extra shift depreciation allowance*

(i) Under the Income-tax Rules, 1962 extra shift depreciation allowance shall be allowed upto a maximum of one half of normal depreciation allowance where the concern had worked double shift and upto the maximum of amount equal to the normal allowance where the concern had worked triple shift.

According to a certificate furnished by the Factory Manager, a company had actually worked only double shift during the assessment years 1979-80 to 1981-82. In the assessments for these assessment years made between November 1981 and February 1983, extra-shift allowance on plant and machinery

for double-shift working was incorrectly granted at 100 per cent of normal depreciation instead of at the admissible rate of 50 per cent. This resulted in grant of excess extra shift depreciation allowance of Rs. 2,06,842 with consequent undercharge of tax of Rs. 1,09,155 in the three assessment years together with excess carry forward of loss of Rs. 18,515 in the assessment year 1979-80.

The Ministry of Finance have accepted the mistake (November 1984).

The assessment was checked by the Internal Audit Party of the department which did not detect the mistake.

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

(a) A private limited company claimed extra shift allowance amounting to Rs. 2,54,632 on dies, electrical installation and air-conditioner in the assessment year 1976-77 which was allowed by the department in the assessment made in September 1980. Extra shift allowance is not admissible in respect of these items of machinery as they have been specifically excepted by the stipulation of the letters 'NESA' in the depreciation schedule. The erroneous allowance of extra shift allowance resulted in excess computation of loss by Rs. 2,54,632. Further, the company was allowed initial depreciation of Rs. 64,136 on machinery twice resulting in a further excess allowance of Rs. 64,136. The total excess allowance of Rs. 3,18,258 resulted in excess computation of loss to the same extent involving potential tax effect of Rs. 2,00,817.

The Ministry of Finance have accepted the mistake (December 1984).

(b) In Computing the business Income of a private limited company engaged in production of sugar for the previous year relevant to the assessment years 1973-74 to 1975-76, the assessee's claim for extra shift allowance of Rs. 1,60,858 on certain items of electrical machinery was accepted by the department. However no extra shift allowance was admissible for such machinery since these machines have been specifically excepted by stipulation of letters 'NESA' in the depreciation Schedule. The incorrect allowance of Rs. 1,60,858 resulted in short levy of tax of Rs. 1,01,339.

The Ministry of Finance have accepted the mistake (December 1984).

(c) For the assessment years 1978-79 and 1979-80 (assessments completed in April 1982 and September 1982) a company was allowed extra shift depreciation amounting to Rs. 3,88,202 and Rs. 1,77,477 respectively on the plant and machinery categorised by the assessee company under communication equipments and "industrial furniture". In the absence of specific mention of communication equipments as such in the depreciatoin schedule, for purposes of application of rate of depreciation, the communication equipment would fall either under "office machinery" or "wireless appliances" both of which have been specifically excepted by the inscription of the words NESA against them. The "industrial furniture" would come under "Furniture and fittings" and also not being plant and machinery, no extra shift allowance on these assets are admissible. The incorrect allowance of extra shift depreciation on these items resulted in under-assessment of income by Rs. 3,88,202 and Rs. 1,77,477 for the assessment year 1978-79 and 1979-80 respectively, leading to under charge of tax aggregating to Rs. 3,26,678 for the two assessment years.

The paragraph was sent to the Ministry of Finance in August 1984 ; their reply is awaited (November 1984).

(iii) Under the Income-tax Rules 1962 no extra shift allowance resulted in excess computation of depreciation and Machinery and wiring and fittings of electric light and fan installation falling under 'Electrical Machinery'.

In the assessment of a public sector undertaking for the assessment year 1979-80 (completed in January 1982) extra shift depreciation allowance amounting to Rs. 1,54,154 claimed on electrical installations and electrical equipment falling under the category of 'Electrical Machinery' was allowed. The incorrect allowance resulted in excess computation of depreciation and consequent excess carry forward of loss to the extent of Rs. 1,24,154 for adjustment against future years' income.

The Ministry of Finance have accepted the mistake (August 1984).

(iv) Under the Income-tax Rules 1962 no extra shift allowance is admissible on furniture and fittings.

While completing the assessment in February 1983 of a public company for the assessment year 1980-81, the Income-tax Officer incorrectly allowed extra shift allowance of

Rs. 1,64,705 on the furniture and fittings of the company. This irregular allowance led to short computation of income to the extent of Rs. 1,64,705 involving a short levy of income-tax of Rs. 1,14,212 including surtax for the assessment year 1980-81.

The Ministry of Finance have accepted the incorrect grant of extra shift allowance (November 1984). Report regarding rectification of surtax assessment is awaited (December 1984).

2.26 *Incorrect grant of investment allowance*

As per the provisions of the Income-tax Act, 1961, in respect of machinery owned by the assessee and used for purpose of business carried on by him, a deduction shall be allowed in the previous year of installation or in the previous year of first usage, of a sum by way of investment allowance, equal to twenty-five per cent of the actual cost of the machinery to the assessee. The Act further provides that the machinery used in an industrial undertaking other than a small scale undertaking and eligible for the investment allowance shall be for the purpose of manufacturing any article or thing not specified in the list in the Eleventh Schedule.

(i) In the assessment made in February 1982, of a private limited company for the assessment years 1979-80 and 1980-81, investment allowance of Rs. 2,28,890 and Rs. 8,16,086 was allowed by the Inspecting Assistant Commissioner (Assessment) in addition to the claim made by the assessee on machinery installed during the previous year relevant to the two assessment years. The machines were however used in the manufacture of items listed in the Eleventh Schedule to the Act such as refrigerators, cupboards, spring doors, fire resisting cabinets etc. and, therefore, the allowance was not admissible. The incorrect allowance resulted in under-assessment of income of Rs. 9,91,907 for the two assessment years leading to a short levy of tax of Rs. 6,37,008.

The Ministry of Finance have accepted the mistake (July 1984).

(ii) In the case of two companies assessed in another Commissioner's charge, investment allowance of Rs. 1,69,315, Rs. 90,597 and Rs. 1,30,588 was allowed for the assessment years 1978-79 to 1980-81 in the assessments completed by Inspecting Assistant Commissioner (Assessment) in September 1982 &

March 1983 on the machinery utilised in the manufacture of sanitary and stoneware pipes. The articles "Tablewares and Sanitarywares" stood included in the Eleventh Schedule at item No. 16 upto 31 March 1982. The item was deleted from the Eleventh schedule only from 1 April 1982. Hence, the assessees were not entitled to the investment allowance up to the assessment year 1981-82. The incorrect grant of investment allowance for the assessment years 1978-79 to 1980-81 resulted in short-levy of tax aggregating to Rs. 2,32,030.

The paragraph was sent to the Ministry of Finance in June 1984; their reply is awaited (November 1984).

(iii) If the machinery cannot be used in the year in which it is installed, the Act permits the deduction on account of investment allowance being allowed in the immediately succeeding year in which it is first put to use but not later on.

In the case of a company, machinery costing Rs. 43,06,983 was installed upto the previous year relevant to the assessment year, 1977-78 but it was put to use for the first time in the previous year relevant to the assessment year 1979-80. As the machinery was not put to use in the assessment year 1978-79 being the immediately succeeding the year, it did not qualify for the grant of investment allowance.

The grant of investment allowance in the assessment year 1979-80 resulted in excess carry forward of unabsorbed investment allowance of Rs. 10,76,746.

The Ministry of Finance have accepted the mistake (August, 1984).

(iv) In the Income-tax assessment of a company for the assessment year 1978-79 completed in April 1981, a deduction of Rs. 1,83,570 towards investment allowance was allowed on an amount of Rs. 7,34,282. This amount did not represent the cost of any new plant and machinery installed by the assessee during the relevant previous year, but only the amount of bank guarantee and commission charges in respect of machinery purchased on deferred payment basis and installed much earlier. This amount was disallowed while assessing the income on the ground that it was a capital expenditure. Though the expenditure was treated as capital expenditure increasing thereby the cost of plant and machinery, investment allowance was not admissible thereon in the assessment year 1978-79 as the

concerned plant and machinery were neither installed nor brought to use for the first time during the relevant previous year. The incorrect grant of investment allowance on capitalised expenditure resulted in under assessment of income of Rs. 1,83,570 with consequent short levy of tax of Rs. 1,06,012.

The Ministry of Finance have accepted the mistake (August 1984).

(v) No deduction on account of investment allowance is allowable on any machinery or plant acquired and used by the assessee in the business if whole of the actual cost of it is allowed as a deduction in computing business income in any previous year whether by way of depreciation or otherwise.

While computing the business income of a company for the assessment year 1978-79 (assessment made in April 1982) the assessing officer granted investment allowance of Rs. 23,05,707 at 25 per cent of Rs. 92,22,829 being the cost of the plant and machinery which were installed by the assessee for conducting scientific research. The entire cost of the plant and machinery was allowed as deduction as they were intended for scientific research. Since the whole of the actual cost of machinery had been allowed as deduction in the computation of business income, the assessee was not entitled to investment allowance. The incorrect grant of investment allowance resulted in under assessment of income of Rs. 23,05,707 with consequent under charge of tax of Rs. 13,,31,544.

The Ministry of Finance have accepted the mistake (November 1984).

The assessment was checked by the Internal Audit Party of the department; but the mistake escaped its notice.

(vi) The new machinery has been explained in the Act to include machinery or plant which before its installation by the assessee was used outside India by any other person, or the machinery was not used previous to its installations by the assessees in India or such machinery was imported into India from abroad or no deduction of depreciation in respect of such machinery has been allowed or allowable under the Act in computing the total income of any person.

An iron and steel manufacturing company was assessed in February 1983 for the assessment year 1978-79 and a sum of

Rs. 77,27,885 was allowed to be carried forward towards unabsorbed investment allowance. In the previous year relevant to the assessment year 1978-79, the assessee company reconditioned its old E.D.T. Cranes in the Malting shop and Rolling Mills at a cost of Rs. 1,99,34,005 and Rs. 25,13,831 respectively and claimed investment allowance at the rate of 25 per cent thereof for Rs. 49,83,501 and Rs. 6,28,458 respectively and the claim was allowed by the Income-tax Officer. The reconditioned machinery was not a new machinery but only an old machinery used by the assessee company. Neither the machinery was used outside India, before it was put to use in India nor was it imported from abroad. Therefore, the grant of investment allowance to an old reconditioned machinery was not in order. This resulted in excess carry forward of investment allowance of Rs. 56,11,959.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(vii) The Income-tax Act further provides that where the gross total income of an assessee includes any profit and gains derived from an industrial undertaking located in a backward area, a deduction of 25 per cent of such profits and gains shall be allowed in computing the total income of the assessee provided it has begun or begins to manufacture or produce articles after 31 December 1970 in any backward area.

Accordingly the investment allowance and the deduction on account of setting up an industrial undertaking in a backward area are admissible to the industrial undertaking engaged in manufacture or production of articles only and not to other kinds of activities to which the plant and machinery is put to use by the assessee.

A company was assessed in April 1982 for the assessment year 1979-80 on a total income of Rs. 1,54,984. The assessee was allowed for the assessment year 1979-80 investment allowance of Rs. 89,719 and deduction of Rs. 17,453 on setting up a new cold storage plant in a backward area. As the cold storage plant was not used for the purpose of manufacture or production of articles but for preserving articles stored therein where no manufacture or production takes place, it was not eligible for the said allowance and deduction. The allowance and deduction of Rs. 1,07,172 allowed to the assessee company was not in order which resulted in total short levy of tax of Rs. 1,51,240

including interest for late filing of returns and failure to furnish estimate of advance tax payable by the company.

The Ministry of Finance have accepted the mistake (December 1984).

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

(a) The income-tax assessment of a company for the assessment years 1979-80 and 1980-81 were completed by the Inspecting Assistant Commissioner (Assessment) in November 1981 and December 1982 computing total loss of Rs. 52,36,240 and Rs. 45,74,430 respectively. The assessee company was granted investment allowance of Rs. 1,71,250 and Rs. 74,505 for these assessment years on plant and machinery. The company was not allowed any depreciation on machinery in either of the two assessment years on the ground that the plant and machinery owned by it had been purchased out of the grants received from the Government of India and the actual cost of their acquisition to the assessee was "nil". Since the actual cost of the machinery to the assessee was "nil" it was not entitled for investment allowance also and consequently the grant of investment allowance aggregating to Rs. 2,45,755 for these two assessment years was not in order. The incorrect allowance led to excess carry forward of loss to the extent of Rs. 2,45,755.

The Ministry of Finance have accepted the mistake for the assessment year 1979-80 (September 1984). For the assessment year 1980-81 they have stated that necessary disallowance of investment allowance will be made on completion of further enquiries. Further report is awaited (November 1984).

(b) In the assessment of a company for the year 1979-80 completed in September 1982, investment allowance was allowed on the value of the new plant and machinery installed by the company during the previous year relevant to the assessment year. The assessee, had during the relevant previous year received a capital subsidy of Rs. 14,07,200 from the Government of a Union Territory in respect of these plant and machinery.

The cost of the plant and machinery to the assessee was correctly reduced by the Income-tax Officer, by the amount of subsidy to work out the depreciation admissible. However, the investment allowance was allowed on the unreduced value of new plant and machinery instead of on the "actual cost" to the assessee. The mistake resulted in excess allowance of investment allowance by Rs. 3,51,800 with the consequent excess carry forward of investment allowance of Rs. 3,51,800 for the assessment year 1979-80 involving potential tax effect of Rs. 2,21,634.

The Ministry of Finance have accepted the mistake (November 1984).

(ix) Under the provisions of the Income-tax Act, 1961, if a machinery on which investment allowance is granted is sold at any time before the expiry of eight years from the end of the previous year in which it was installed the investment allowance originally granted has to be withdrawn.

A company, installed a machinery during the previous year relevant to assessment year 1979-80 on which investment allowance of Rs. 1,77,200 was granted by the department during that year. The machinery was sold during the previous year relevant to assessment year 1981-82. It was noticed at the time of checking the assessment records of the company for the assessment year 1981-82 (assessment completed in October 1982) that the assessment for assessment year 1979-80 was not revised withdrawing the investment allowance originally granted. Omission to do so resulted in under assessment of income of Rs. 1,77, 000 and short-levy of tax of Rs. 1,02,333.

While not accepting the mistake, the Ministry of Finance have stated (July 1984) that the Income-tax Officer was aware of the need to withdraw the investment allowance and that he had made necessary note in the assessment order finalised for the year 1981-82.

No such note was found to have been made in the assessment order for the year 1981-82 while conducting the audit of the assessment records. Even assuming but not conceding that the department had noticed the mistake in October 1982 no action was taken by the department to withdraw the incorrect investment allowance till the omission was pointed out in Audit in October 1983.

(x) No deduction of investment allowance shall be allowed in respect of plant and machinery installed in office premises or any office appliances.

In the assessment made in March 1983 for the assessment year 1980-81 of a company engaged in the manufacture and sale of steel furniture, deduction of Rs. 1,11,521 by way of investment allowance was allowed on the cost of plant and machinery including computers installed in the office and brought into use by the company. As the steel furniture manufactured by the assessee is one of the items listed in the Eleventh Schedule to the Act and the computers having been installed in office premises the assessee company is not entitled to investment allowance.

The incorrect allowance resulted in under assessment of income by Rs. 1,11,521 for the assessment year 1980-81 with consequent under charge of tax of Rs. 71,931.

The Ministry of Finance have accepted the mistake (December 1984).

2.27 *Incorrect grant of development rebate*

Under the provisions of Income-tax Act, 1961 development rebate is allowable at the prescribed rates in respect of new machinery installed before 1 June 1974. The development rebate was abolished w.e.f. 1 June 1974.

(i) Development rebate at higher rate was admissible on machinery or plant installed for the purpose of business of construction, manufacture or production of any one or more of articles or things specified in the Fifth Schedule to the Act.

For the assessment years 1974-75 and 1975-76, a company having three manufacturing units claimed development rebate at the higher rate of 25 per cent on plant and machinery installed in one of the units and at the rate of 15 per cent in respect of the other two units. The Income-tax Officer disallowed the claim for the development rebate at the higher rate and allowed it only at 15 per cent. Pursuant to an appellate order of January 1979, directing allowance of the rebate at the higher rate, the assessments were revised in February 1979, wherein the Income-tax Officer allowed development rebate at the higher rate for all the three units instead of for only one unit claimed by the assessee.

The mistake resulted in excess allowance of development rebate of Rs. 1,87,158 in the two years leading to under-assessment of income by the same amount involving undercharge of tax of Rs. 1,08,083 in the assessment year 1975-76.

The Ministry of Finance have accepted the mistake (September 1984).

(ii) If the total income assessable before deduction of the development rebate was less than the full amount of the admissible amount, the rebate allowable should be only such amount as to reduce the total income to 'nil' and the unabsorbed rebate should be carried forward for adjustment in the next assessment year, the carry forward being restricted to eight years.

In the case of an assessee company, the original assessment for the assessment year 1977-78 completed in November 1980 was rectified in October 1981 and again in February 1983 computing revised total income at Rs. 3,92,514 after carrying out the necessary adjustment on account of unabsorbed development rebate and the net tax payable was determined at Rs. 1,06,281.

While computing the total income a sum of Rs. 2,83,324 towards unabsorbed development rebate for the assessment years 1969-70 to 1975-76 was however given set off twice. The mistake resulted in under-assessment of total income by Rs. 2,83,324 with tax undercharge of Rs. 1,78,494.

The Ministry of Finance have accepted the mistake (July 1984).

(iii) The Income-tax Act, 1961 provides that if any machinery or plant on which development rebate was allowed in any assessment year is sold or otherwise transferred before the expiry of eight years from the end of the previous year in which it was installed, the development rebate so granted is to be withdrawn.

(a) During the previous year relevant to the assessment year 1974-75, a widely-held company purchased (August 1973) a diesel generator set at a cost of Rs. 5,93,812 and in the assessment completed (March 1977) the assessing officer allowed development rebate of Rs. 1,48,453 thereon. The generator was sold by the company in September 1974 relevant to the assessment year 1976-77. As the asset was sold within the period of eight years, the development rebate of Rs. 1,48,453

originally allowed on the asset would have to be withdrawn. The omission resulted in under-assessment of income of Rs. 1,48,453 involving short levy of tax of Rs. 1,00,730 including surtax of Rs. 14,995 for the assessment year 1974-75.

The Ministry of Finance have accepted the mistake (September 1984).

(b) An assessee company installed machinery valued at Rs. 5,80,688 during the previous years relevant to the assessment years 1974-75 to 1976-77, and a total development rebate amounting to Rs. 1,45,171 was allowed by the department during these assessment years. The company sold the plant and machinery during the previous year relevant to the assessment year 1980-81. Although the machinery was sold within the period of eight years from the date of installation, the development rebate amounting to Rs. 1,45,171, allowed in the assessment years 1974-75 to 1976-77 was not withdrawn. The omission resulted in under-assessment of income of Rs. 1,45,171 for the assessment years 1974-75 to 1976-77 leading to aggregate short-levy of tax of Rs. 91,456.

The Ministry of Finance have accepted the mistake (July 1984).

(c) In the case of a company, machinery on which development rebate of Rs. 1,53,160 was allowed in the assessment years 1973-74, 1974-75 and 1975-76 was sold during the previous year relevant to assessment year 1980-81. Though the machinery was sold before the expiry of the prescribed period, the development rebate granted was not withdrawn resulting in under-assessment of income of Rs. 1,53,160 and aggregate short-levy of tax of Rs. 88,450 in the three assessment years.

The Ministry of Finance have accepted the mistake (July 1984).

2.28 *Omission to levy capital gains tax*

Under the provisions of the Income tax Act, 1961 any profits or gains arising from transfer of a capital asset are chargeable to tax under the head 'Capital gains'. Capital gains shall be computed by deducting the cost of acquisition of the capital asset and the cost of any improvement thereto from the value of consideration received. For the purpose of computation of capital gains, the term 'transfer' has been defined in the Act to include sale, exchange or relinquishment of an asset or extinguishment of any rights therein.

(i) During the previous year relevant to the assessment year 1979-80 a public sector undertaking sold 9,331 acres of land for a consideration of Rs. 4,03,775 and credited the same to the land account. The original cost of the land in question was Rs. 29,083 as exhibited in the accounts of the assessee. As the sale proceeds of the land exceeded the actual cost thereof, the gain of Rs. 3,74,692 constituted capital gains and was liable to tax. Neither the assessee returned the capital gains nor the same was brought to tax by the department in the assessment made in September 1982 for the assessment year 1979-80. The omission resulted in under-assessment of income of Rs. 3,74,692 involving short-levy of tax of Rs. 1,87,346.

The Ministry of Finance have stated (November 1984) that the levy of capital gains tax is being considered in reassessment proceedings.

(ii) Under the provisions of the Income-tax Act, 1961 where the total income of a private limited company includes any income chargeable under the head long-term capital gains relating to land and buildings, the tax payable by the company shall be the aggregate of the income-tax on the long term capital gain calculated at the rate of 50 per cent and income-tax leviable on other income at the normal rates.

In the assessment of a private limited company for the assessment year 1982-83, the Inspecting Assistant Commissioner (Assessment) computed its income at Rs. 65,58,312 in October 1982 including capital gain of Rs. 1,38,462. The actual capital gain was Rs. 2,76,925. While computing the total income, the Inspecting Assistant Commissioner (Assessment) erroneously allowed a deduction of Rs. 1,38,462 being 50 per cent of the long-term capital gain from the total, and added the balance long term capital gain of Rs. 1,38,463 to the other income and levied tax of Rs. 40,33,361. The omission to levy tax at the rate of 50 per cent on the entire long-term capital gains and at the prevailing rate on the other income and to aggregate the tax liability resulted in short-levy of tax of Rs. 53,837.

The Ministry of Finance have accepted the mistake (December 1984).

2.29 *Income escaping assessment*

As per the provisions of the Income-tax Act, 1961, the total income of any previous year of a person who is a resident includes all income (from whatever source derived) which is received or is deemed to have been received in India in the

previous year. In the case of an assessee who is following the mercantile system of accounting, all income accrued though not actually received during the previous year relevant to the assessment year has to be included in that assessment year only and not in any other assessment year.

(i) A shipping company was entitled to receive ocean freight amounting to Rs. 36.67 lakhs in respect of voyages of its ships to and from Mozambique performed during the accounting year ending 30 June 1975 relevant to the assessment year 1977-78. As there was a military Coup in Mozambique and the foreigners living there were required to leave the country, no information was available regarding the freight receivable and, therefore, the credit for Rs. 36.67 lakhs was not taken into account by the company in its accounts for the previous year relevant to the assessment year 1977-78. It was clarified in a note forming part of the balance sheet of the company that the credit for the amount had not been taken into account as the recoverability thereof was on diverse considerations not free from doubt. However, a settlement was reached during the subsequent year ending 30 June 1977 and the company received a sum of Rs. 21.50 lakhs as against its dues of Rs. 36.67 lakhs. This amount was included by the company in the accounts of the subsequent year ending 30 June 1977 relevant to the assessment year 1978-79.

In the assessment of the company for the assessment year 1977-78 done in September 1980, the department did not bring the amount of Rs. 36.67 lakhs to tax. As the company was following the mercantile system of accounting, the gross amount of Rs. 36.67 lakhs was taxable on accrual basis in the assessment year 1977-78 and the excess amount of Rs. 15.17 lakhs subjected to tax, could be rectified later. The amount of Rs. 21.50 lakhs was, however, included in the income of the company for the assessment year 1978-79. The taxable income of the company for the assessment year 1978-79 was determined as 'nil' after adjusting development rebate due to it. Omission to include the amount in the assessment year 1977-78 in which year there was positive income resulted in short-levy of tax amounting to at least Rs. 12,41,900.

The Ministry of Finance have accepted the mistake (August 1984).

(ii) (a) The income-tax assessments of a public limited company for the assessment years 1979-80, 1980-81 were finalised in

October 1981 and for the assessment year 1981-82 in December 1981, assessing the income at Rs. 1,66,400, Rs. 2,08,653 and Rs. 76,220 respectively. The assessee, who maintained the accounts on mercantile system had not included in the returns of income, interest amounting to Rs. 2,09,730 that had accrued on loans of Rs. 8.05 lakhs during the relevant previous years on the ground that recovery of principal and interest had become stagnant in those cases for some years and the assessee had approached the courts of law for recovery of the dues. Accepting the assessee's contention the assessments were finalised by the Income-tax Officer without including the interest accrued as above in the assessed income. The loans were not actually written off as bad debts by the assessee in the accounts. On the other hand the Director's report indicated that the said loans were good and fully recoverable. In fact a part of the amount was recovered after 31 March 1981.

The omission to include the interest accrued on the loans resulted in under-assessment of income of Rs. 2,09,730 for the assessment years 1979-80 to 1981-82 with consequent undercharge of tax aggregating to Rs. 1,31,420.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(b) An assessee company following mercantile system of accounting received interest amounting to Rs. 3,82,666 during the previous year relevant to the assessment year 1977-78 out of which a sum of Rs. 2,97,021 related to previous year relevant to the assessment year 1976-77. The entire interest income of Rs. 3,82,666 was, however, assessed in the assessment year 1977-78 (assessment made in July 1979) on receipt basis. The Income-tax Appellate Tribunal in its order of August 1982 held that interest amounting to Rs. 2,97,021 relatable to previous year relevant to the assessment year 1976-77 was not assessable in the assessment year 1977-78, since the assessee was following mercantile system of accounting. While giving effect to the Income-tax Appellate Tribunal's orders in October 1982, the assessment for the assessment year 1977-78 was revised excluding the sum of Rs. 2,97,021 from the total income. Simultaneously, the assessment for the assessment year 1976-77 was not, however, revised to include the income of Rs. 2,97,021. Omission to do so resulted in escapement of income of Rs. 2,97,021 with consequent excess carry forward of loss by the same amount.

The Ministry of Finance have accepted the mistake (January 1985).

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

In the case of an assessee company, during the previous year relevant to the assessment year 1980-81, certain creditors of the assessee company had agreed for the write-off of interest of Rs. 11,22,613 due to them and the assessee company had also written back this amount in its accounts relevant to that assessment year. This amount was already charged to accounts in the earlier years and was allowed as deduction by the department. However, in the assessment for the assessment year 1980-81 completed in November 1982, the amount remitted was not treated as income of that year by the Income-tax Officer and added back to the total income. The omission resulted in under-assessment of income of Rs. 11,22,613 leading to short-levy of tax of Rs. 7,24,085.

The paragraph was sent to the Ministry of Finance in July 1984; their reply is awaited (November 1984).

(b) In the profit and loss appropriation accounts for the previous year relevant to the assessment year 1979-80, a company credited a sum of Rs. 8,58,383 being write-back of excess liability provided for in the earlier years as it was no longer required. As the liability had already been allowed in earlier assessments the sum of Rs. 8,58,383 was required to be treated as income and charged to tax in the assessment year 1979-80. In the assessment concluded in March 1982 for the assessment year 1979-80, the assessing officer did not include the write-back of the liability as income of that year. The omission led to escapement of income of Rs. 8,58,383 leading to excess carry forward of loss by the same amount for the assessment year 1979-80 involving a potential tax effect of Rs. 5,85,844.

The Ministry of Finance have accepted the mistake (June 1984).

(c) In the case of an assessee company interest of Rs. 6,26,591 due to Maharashtra State Finance Corporation Limited on a loan granted by them to the assessee during the previous years relevant to the assessment year prior to 1979-80 was written-off by the Corporation on 31 March 1979. As the liability for the interest ceased, the amount of interest of Rs. 6,26,591 was required to be written back and included as income in the assessment year 1979-80 whose previous year ended on 31 March 1979. Omission to do so resulted in determination of loss of the company in excess by Rs. 6,26,591 involving potential tax effect of Rs. 3,94,752 which was carried forward for set off against positive income in future years.

The Ministry of Finance have stated in December 1984 that the full and final payment of the loan was made in April 1979 and hence the interest waived was assessable for the assessment year 1980-81 and not for the assessment year 1979-80. The Financial Corporation who advanced the loan, however, averred that the Board passed a resolution on 15 March 1979 and the settlement took place on 31 March 1979 relevant to the assessment year 1979-80. Hence the interest waived is correctly chargeable to tax in the assessment year 1979-80.

(d) The Income-tax Act as it stood prior to its amendment by Finance Act, 1983 provided for export markets development allowance to resident assessee engaged in export of goods. Widely-held domestic companies were entitled to a deduction on account of this allowance from the business income at one and one half times the qualifying expenditure incurred during the period from 1 March 1973 to 31 March 1978.

In the accounts of the previous year relevant to the assessment year 1980-81, an assessee had written back a sum of Rs. 12,35,000 on account of commission paid on exports which was allowed as deduction in the earlier years as normal liability. While allowing the commission on exports, the company had also been allowed 55 per cent of this amount as weighted deduction towards export market development allowance in the respective years. In the assessment made in February 1983 for the assessment year 1980-81 although the deduction of Rs. 12,35,000 was brought to tax, 50 per cent thereof allowed as weighted deduction, was not brought to tax. The omission resulted in under-assessment of income by Rs. 6,17,500 leading to a short-levy of tax of Rs. 3,65,096.

The Ministry of Finance have accepted the mistake (June 1984).

(e) A sum of Rs. 4,37,944 representing excess sales service charges was recovered by a company in which the public are substantially interested during the previous year relevant to the assessment year 1979-80 from their sole selling agents. The sales service charges had earlier been allowed as a deduction in the assessments relating to the assessment years 1976-77 to 1978-79. While completing the assessment for the assessment year 1979-80 in September 1982 the department did not include the excess sales service charges of Rs. 4,37,944 on the plea that the assessee company had offered to return the amount in the respective assessment years. The assessee company had not, however, actually offered the amount in the assessment for the earlier years till June 1983. Under the provisions of the Act, the amount of Rs. 4,37,944 was to have been brought to tax as profits in the assessment year 1979-80 relevant to the previous year in which the service charges were recovered. The omission resulted in escapement of income of Rs. 4,37,944 involving short-levy of tax of Rs. 2,99,167 including surtax.

While accepting the mistake, the Ministry of Finance have stated that the assessment is being revised (September 1984).

(f) In the previous year relevant to the assessment year 1977-78 an amount of Rs. 1,90,372 representing excess provision and sundry credit balances were written back by the assessee company. The amount of write back representing cessation of liability constituted income for the assessment year 1977-78. While completing the assessment in August 1981 for the assessment year 1977-78 the assessing officer did not add back this amount to the income of the company. Omission to do so resulted in under-assessment of income of Rs. 1,90,372 with consequent short-levy of tax of Rs. 1,00,939.

The Ministry of Finance have accepted the mistake in principle (January 1985).

(g) The assessment of a company for the assessment years 1978-79 and 1979-80 were completed in October 1979 and December 1981 computing losses of Rs. 38,946 and Rs. 74,521 respectively. In the profit and loss appropriation accounts for the previous years relevant to these assessment years, the company had written back sums of Rs. 8,31,607 and Rs. 16,797 respectively being provision and liability provided previously, now no longer required. As these liabilities were allowed as deduction in full in the earlier assessment years, these should have been treated as income and charged to tax in the assessment years 1978-79

and 1979-80 respectively. The omission resulted in under-assessment of income aggregating to Rs. 8,48,404 with consequent excess carry forward of loss to the same extent in the two assessment years.

While accepting the omission, for the assessment year 1979-80, the Ministry of Finance have stated (January 1985) that for the assessment year 1978-79 involving income of Rs. 8,31,607 action has become time barred.

(h) In the assessment of a private limited company for the assessment year 1974-75, the Income-tax Officer allowed (July 1981) under appellate orders, deduction for a sum of Rs. 3,43,678 towards provisions for gratuity as claimed by assessee. Out of the above provision of Rs. 3,43,678 the assessee had written back and credited a sum of Rs. 2,56,849 as excess provision in its accounts for the year ended 31 March 1978 (relevant to the assessment year 1978-79). However, this sum of Rs. 2,56,849 was not brought to tax as income in the assessment year 1978-79. The omission resulted in excess carry forward of loss of Rs. 2,56,849 involving tax of Rs. 82,612 for the assessment year 1979-80. The tax effect in assessment year 1980-81 is awaited.

The Ministry of Finance have accepted the mistake (December 1984).

(iv) (a) Under the Income-tax Act, 1961, where any business is discontinued in any year, any sum received after the discontinuance shall be deemed to be the income of the recipient and charged to tax accordingly in the year of receipt, if such sum would have been included in the total income of the person who carried on the business had such sum been received before such discontinuance.

An assessee company maintaining accounts on mercantile system, did not include in its income returned for assessment year 1982-83 a sum of Rs. 8,13,308 being interest payable by Government on excess advance tax paid for the assessment year 1981-82. The regular assessment for the assessment year 1981-82 was completed on 27 February 1982 and a copy of assessment order indicating inter-alia the refund of Rs. 8,13,308 was issued to the assessee company on 6 March 1982 which fell in the accounting year relevant to the assessment year 1982-83. In the assessment made in September 1983 for the assessment year 1982-83 the Inspecting Assistant Commissioner (Assessment) did not include the amount of interest in the income assessed. Omission to do so resulted in escapement of income of Rs. 8,13,308 from tax leading to short-levy of tax of Rs. 4,58,498.

The Ministry of Finance maintained (December 1984) that the interest refunded on 7 April 1982 was taxable in the

assessment year 1983-84. This is not tenable as the assessee company maintained the accounts in mercantile system, and accordingly the income accrued was taxable only in assessment year 1982-83.

(b) An assessee received from the Income-tax department interest amounting to Rs. 6,31,127 on excess advance tax paid by it during the previous year relevant to assessment year 1982-83. However, while finalising the assessment on 31 March 1983 for the assessment year 1982-83, the Inspecting Assistant Commissioner (Assessment) did not treat the interest paid as income and did not include the same in the taxable income of the company. This resulted in the income of Rs. 6,31,127 escaping assessment involving short-levy of tax of Rs. 3,88,143.

The Ministry of Finance have accepted the omission and have reported that remedial action is being taken (August 1984).

(c) During the previous year relevant to the assessment year 1977-78, a company received a sum of Rs. 2,62,340 as interest from the Income-tax department in respect of the assessment year 1973-74. Neither the assessee had returned the income for the assessment year 1977-78 nor the Income-tax Officer assessed it to tax while completing the assessment for the assessment year 1977-78 in February 1980. The omission resulted in escapement of income of Rs. 2,62,340 from tax involving short-levy of tax of Rs. 1,51,501.

While accepting the omission, the Ministry of Finance have reported that the assessment has been revised raising additional demand of Rs. 1,51,501 (September 1984).

(d) On the nationalisation of coal mines under the Coal Mines (Nationalisation) Act, 1973, a private limited coal-mining company closed its business with effect from 1 May 1973. In February 1976, the company received a sum of Rs. 26,204 on account of interest on excess payment of advance tax for the assessment year 1973-74. The company also received another sum of Rs. 1,62,803 in July 1981 on account of interest for delay in the grant of refund of Rs. 1,82,935 ordered by the Income-tax Appellate Tribunal in September 1973. These sums received by the company after the discontinuance of business in May 1973, were liable to charge of income-tax. Neither the company filed any return for the assessment years 1977-78 and 1982-83 nor the department initiated action to bring these receipts to tax. Thus, income of Rs. 1,89,007 escaped tax amounting to Rs 1 26,220.

The paragraph was sent to the Ministry of Finance in July 1984; their reply is awaited (November 1984).

(v) Under the Income-tax Act, 1961, interest on any security of the Central or State Government and debentures or other securities for money issued by or on behalf of a local authority or a company or a corporation established by a Central, State or Provincial Act shall be chargeable to income-tax under the head 'interest on securities' in the assessment year relevant to the previous year in which the interest becomes due.

In the case of banking company, Income-tax Officer completed the assessments for the assessment years 1976-77 and 1977-78 in August 1979 and January 1980 respectively. While computing the income under the head 'interest on securities' for the assessment year 1976-77, the Income-tax Officer excluded income of Rs. 13,13,812 as relating to the assessment years 1972-73 to 1974-75. Similarly, while computing income for the assessment year 1977-78, income of Rs. 6,09,613 was excluded as it pertained to the assessment year 1976-77. However, no action was taken by the Income-tax Officer to revise the assessments for the assessment years 1972-73 to 1974-75 and 1976-77 to bring to charge the income of Rs. 13,13,812 and Rs. 6,09,613 respectively to tax. The omission resulted in income of Rs. 19,23,425 escaping assessment involving short-levy of tax of Rs. 6,68,415.

The Ministry of Finance have accepted the mistake (October 1984).

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

(vi) During the previous year relevant to the assessment year 1981-82 a company engaged in the business of construction and sale of building was holding eight office premises the cost price of which was Rs. 15,03,025. The assessee company paid a compensation of Rs. 8,43,151 to its original members who had surrendered their rights in the premises booked by them in the building. The total cost of the eight premises together with the compensation paid was Rs. 23,46,176. These premises were resold by the assessee company to other parties at a price amounting to Rs. 27,99,480. Consequently the net profit of Rs. 4,53,304 on sale of the premises was required to be brought to tax while completing the assessment in June 1982 for the assessment year 1981-82. Neither the assessee returned the profit nor did the Inspecting Assistant Commissioner (Assessment) bring the same to tax. The omission resulted in excess carry-forward of loss of Rs. 4,53,304 with potential tax effect of Rs. 3,16,745.

The Ministry of Finance have accepted the mistake (December 1984).

(vii) A company in which the public are substantially interested was assessed to tax in June 1982 for the assessment year 1981-82 on a total income of Rs. 40,633. The assessment was revised in September 1983 reducing the total income to Rs. 34,630 and a tax demand of Rs. 16,753 was raised.

The assessee's main business of coal-mining was nationalised with effect from 1 May 1972 under the Coal Mines (Nationalisation) Act, 1972 and the total compensation amounting to Rs. 9,77,500 receivable by the assessee was adjusted in the accounts ending 31 December 1976. The assessee had also received a sum of Rs. 4,18,356 towards interest from the Commissioner of Payments under the above Act during the accounting year ending 31 December 1980 relevant to the assessment year 1981-82. Neither the assessee returned the interest income for the assessment year 1981-82 nor the department considered the receipt while computing the income of this year. The omission resulted in the income of Rs. 4,18,356 escaping assessment with consequent short levy of tax of Rs. 2,86,219 including interest for short payment of advance tax.

The Ministry of Finance have accepted the mistake (October 1984).

(viii) A company debited Rs. 23,56,004 on account of interest payable on loan taken from the head office in the profit and loss account of its branch office for the previous years relevant to the assessment years 1981-82 and 1982-83. In the profit and loss accounts of the head office for the corresponding period, credit on account of the above interest was, however, taken to the extent of Rs. 20,55,306 only. The non-inclusion of interest of Rs. 3,00,698 in the head office accounts resulted in escapement of income of Rs. 3,00,698 leading to under-charge of tax of Rs. 1,97,231 including short-levy of interest of Rs. 4,074 for late filing of returns for the two assessment years.

The paragraph was sent to the Ministry of Finance in July 1984; their reply is awaited (November 1984).

(ix) The original assessment of a company in which public were substantially interested was made in March 1971 for the assessment year 1970-71 after disallowing the company's claim for accrued gratuity liability amounting to Rs. 35,61,198 for the period ending December 1969. As a result of orders of August

1976 of the Income-tax Appellate Tribunal directing that the gratuity liability should be allowed on the basis of actuarial valuation, the assessment for the assessment year 1970-71 was re-opened in November 1976 and a deduction of Rs. 17,15,913 only towards accrued gratuity liability upto December 1969 was allowed therein. The assessee went in appeal to the Income-tax Appellate Tribunal claiming for a deduction of Rs. 31,64,259 towards this liability calculated on actuarial basis. The Income-tax Appellate Tribunal in its orders of March 1979 allowed the appeal and the assessment for the assessment year 1970-71 was accordingly revised again in June 1979 and the gratuity liability of Rs. 31,64,259 was allowed by the Income-tax Officer.

In the meanwhile in the assessments made between March 1978 and March 1979 for the assessment years 1974-75 to 1976-77 the company was allowed deductions of Rs. 4,91,694 on account of acutual payment of gratuity relating to the period upto December 1969. These payments were made by the company over and above the provision for gratuity liability of Rs. 17,15,913 allowed for the same period in the revised assessment made in November 1976.

However, consequent upon allowing deduction of Rs. 31,64,259 in June 1979 on account of full accrued gratuity liability upto December 1969, the deduction of Rs. 4,91,694 in the assessments for the assessment years 1974-75 to 1976-77 was to have been correspondingly withdrawn which was not done. The omission resulted in the income of Rs. 4,91,694 escaping assessment for three years involving short-levy of Rs. 1,59,525 for the assessment years 1974-75 and 1975-76 and excess carry forward of loss of Rs. 2,17,432 for the assessment year 1976-77.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

(x) A company engaged in the business of supply of power was entitled to receive a dividend of Rs. 6,60,000 for the year ending 31 March 1977 from its wholly owned subsidiary company. The dividend of Rs. 6,60,000 was credited to the assessee company in the accounts for the year ending 31 March 1977 relevant to the assessment year 1977-78. The subsidiary company was amalgamated with the assessee company from the close of its business on 31 March 1977. It was claimed by the assessee company that the subsidiary company from which the dividend was receivable, no longer existed on its amalgamation, was not

in a position to hold the general body meeting to declare the dividend and as such the dividend income of Rs. 6,60,000 did not accrue to it. It was contended by the assessee company that for the purpose of inclusion of dividend income in the total income of the assessee, the dividend was to be declared by the company and in the absence of the declaration, the dividend although credited shall not be deemed to be income of the assessee. Accepting the contention of the assessee, the assessment for the assessment year 1977-78 was completed excluding the dividend income of Rs. 6,60,000. The dividend income was not considered in the subsequent assessment years also.

The scheme of amalgamation sanctioned by the High Court in their order of February 1977 provided that all properties, rights and powers and all the liabilities of the amalgamated company stood transferred to and vested in the assessee company from the close of business on 31 March 1977. The High Court issued further orders in May 1977 to the effect that the dividend of Rs. 6,60,000 in question was receivable by the assessee from the amalgamated company in respect of the year ended 31 March 1977. Further the amalgamated company provided for the dividend liability of Rs. 6,60,000 in its accounts for the year ended 31 March 1977 in pursuance of the High Court's orders of May 1977. In the light of High Court orders of May 1977, the dividend income became chargeable in the hands of the assessee in the assessment year 1978-79. In the assessment completed in September 1981 and revised in November 1982, the Income-tax Officer, however, did not include the dividend income of Rs. 6,60,000 in the total income of the assessee company. This resulted in under-assessment of income involving short levy of tax of Rs. 1,56,508 including interest for late filing of returns.

While accepting the mistake, the Ministry of Finance have reported that the assessment had been rectified and additional demand of Rs. 1,55,508 raised (October 1984).

(xi) An assessee company engaged in repair work of barges received, as certified in the certificates of tax deduction at source enclosed to the return of income, contract receipts of Rs. 12,94,771 and Rs. 8,42,287 in the previous years relevant to the assessment years 1978-79 and 1979-80 respectively against which the amounts accounted for by the assessee and taxed by the Income-tax Officer were only Rs. 11,02,959 and Rs. 7,00,784 respectively. These mistakes resulted in under-assessment of income of

Rs. 1,91,812 and Rs. 1,41,003 for the two assessment years respectively involving undercharge of tax of Rs. 1,30,911 for the assessment year 1978-79 and incorrect carry forward of loss of Rs. 1,41,503 for the assessment year 1979-80 involving potential tax effect of Rs. 96,576.

The Ministry of Finance have accepted the mistake (November 1984).

(xii) During the previous year relevant to the assessment year 1980-81, a non-resident shipping company received a sum of Rs. 87,066 representing interest on account of surplus shipping earnings kept on short-term deposits with banks. The interest income of the company was assessable to tax under the head "Income from other sources". Neither the assessee returned the interest income of Rs. 87,066 nor did the department bring the same to tax in the assessment made in January 1983. Although the assessment was rectified twice thereafter, in February and March 1983, the income escaped assessment. The omission resulted in under-assessment of income of Rs. 87,066 involving short-levy of tax of Rs. 67,483 including interest for belated filing of returns.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

2.30 *Incorrect set off of losses*

Under the Income-tax Act, 1961, when for any assessment year, the loss under the head 'profits and gains of business or profession' cannot be set off against any other income in the relevant year, such loss shall be carried forward to the following assessment year and shall be set off against the profits and gains of business or profession of that year and if there is no positive income in that year also it can be carried forward to the subsequent year for set off and so on for eight assessment years immediately succeeding the assessment year for which the loss was first computed.

(i) In the assessment made in September 1982 in the case of a company for the assessment year 1979-80, the business loss of Rs. 10,05,342 relating to earlier assessment years 1975-76 and 1976-77 was set off against its business income.

As a result of the revision of the assessment for the assessment year 1975-76 in September 1979 to give effect to the orders of August 1979 of the Commissioner of Income-tax (Appeals),

the loss was determined by the Income-tax Officer at Rs. 3,78,368. Similarly for the assessment year 1976-77, the assessment was revised in February 1980 to give effect to the orders of January 1980 of Commissioner of Income-tax (Appeals) and the loss was determined by the Income-tax Officer at Rs. 4,50,495. Therefore, the total loss requiring set off for the two assessment years was only Rs. 8,28,863. However, while completing the assessment in September 1982 for the assessment year 1979-80, the revisions made in September 1979 and February 1980 in respect of the assessment years 1975-76 and 1976-77 were overlooked by the Income-tax Officer and the loss of Rs. 10,05,342 originally computed was adjusted. This resulted in excess set off of loss with an underassessment of income of Rs. 1,76,479 involving short-levy of tax of Rs. 71,743.

The Ministry of Finance have accepted the mistake (January 1985).

(ii) The income of a private company for the assessment year 1980-81 was determined as Rs. 10,36,644 in March 1983 and the income was fully set off against the carried forward business loss of Rs. 10,32,762 for the assessment years 1977-78 to 1979-80 and unabsorbed depreciation of Rs. 3,882 for the assessment year 1977-78. The unabsorbed depreciation amounting to Rs. 60,696 for the assessment year 1977-78 to 1979-80 was allowed to be carried forward to the subsequent assessment years.

The assessment of the company for the assessment year 1977-78 was originally made in March 1980 at a loss of Rs. 2,68,028 and was carried forward for set off in the subsequent assessment years. The assessment of the company for the assessment year 1978-79 was completed in November 1981 and the unabsorbed business loss of Rs. 2,68,028 relating to the assessment year 1977-78 was adjusted against the total income of Rs. 91,510 for that year and the net loss of Rs. 1,76,518 was carried forward. The assessment for the assessment year 1978-79 was revised (June 1982) to give effect to the orders of the Commissioner of Income-tax (Appeals) allowing deduction of Rs. 4,68,923 and the revised net loss and unabsorbed depreciation for the assessment year 1978-79 to be carried forward was arrived at as Rs. 6,45,441. Subsequently, the assessment for the assessment year 1977-78 was revised in July 1982 to give effect to the reduction of Rs. 1,53,677 allowed by the Appellate Tribunal in its orders of April 1982 and the total loss for the

assessment year 1977-78 was arrived at as Rs. 4,21,705 (including unabsorbed depreciation of Rs. 28,370) and the same was allowed to be carried forward. Consequent upon this revision, the assessment for the assessment year 1978-79 was not, however, revised. The omission to do so resulted in the carry forward of business loss of Rs. 2,68,028 twice over. The set off of loss for the assessment years 1977-78 to 1979-80 against the income determined for the assessment year 1980-81 led to double adjustment of the loss of Rs. 2,68,028 in the assessment year 1980-81. This resulted in short-levy of tax of Rs. 1,28,532 and incorrect carry forward of unabsorbed depreciation of Rs. 60,696.

The Ministry of Finance have accepted the mistake (October 1984).

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

(iii) When depreciation allowance cannot be allowed in full in any assessment year for want of sufficient income assessed in that year, the balance of depreciation remaining unabsorbed can be carried forward and added to the amount of depreciation for the following years.

In the case of an assessee company, the unabsorbed depreciation relating to the assessment years 1976-77 and 1977-78 was computed at Rs. 68,69,560 and Rs. 43,08,566 respectively to be carried forward and set off against the profits of the subsequent assessment years. Out of the total unabsorbed depreciation of Rs. 1,11,78,126, a sum of Rs. 54,67,266 was set off in the assessment year 1978-79 leaving a balance of Rs. 57,10,860 to be set off in the assessment year 1979-80. However, while computing the income for the assessment year 1979-80 in May 1983 a sum of Rs. 64,21,058 on account of unabsorbed depreciation was set off against the income of the year instead of the correct amount of Rs. 57,10,860. The mistake resulted in excess set off of unabsorbed depreciation by Rs. 7,10,198 with consequent under-assessment of income to the same extent and undercharge of tax of Rs. 7,02,234.

The Ministry of Finance have accepted the mistake (December 1984).

(iv) The Income-tax Act, 1961 provides that where in respect of any assessment year the net result of computation under the head "capital gains" is a loss from long-term capital

assets such loss shall be carried forward to the following assessment years and set off against capital gains relating to long-term capital assets for these assessment years. Such loss cannot be adjusted against any other head of income.

A private company deriving its income from contract business and purchase and sale of jute goods was assessed in September 1979 for the assessment year 1976-77 on a loss of Rs. 1,05,68,076. The assessee held 2,54,641 shares valued at Rs. 20,83,703 of a colliery company which was a subsidiary to the assessee. In November 1975 relevant to the assessment year 1976-77, the company sold these shares for Rs. 8,78,512 and incurred a loss of Rs. 12,05,191 and debited the entire loss in the profit and loss account of the previous year relevant to the assessment year 1976-77. These shares were held as investment by the company and not as its stock-in-trade, and accordingly the loss incurred on their sales was to be treated as long-term capital loss. However, in the assessment for the assessment year 1976-77, this loss was allowed by the Income-tax officer as a business loss. The mistake in treating the capital loss as business loss resulted in under-assessment of income by Rs. 12,05,091 resulting in excess carry forward of loss to the same extent.

The Ministry of Finance have accepted the mistake (August 1984).

(v) Under the Income-tax Act, 1961 when for any assessment year, the loss under the head 'capital gains' relating to assets other than short-term capital assets cannot be set off against any other long-term capital gains, such loss shall be carried forward and set off only against the long-term capital gains of the following four assessment years.

The assessment of a company in which public are substantially interested for the assessment year 1973-74 was revised and the total income including the capital gains of Rs. 5,34,782 as recomputed was determined (April 1982) as Rs. 93,76,940 in a central circle. The long-term capital losses of Rs. 3,55,002 relating to the assessment year 1969-70 and Rs. 1,48,121 relating to assessment year 1971-72 were set off against the aforesaid capital gains of Rs. 5,34,782. The assessment for assessment year 1971-72 in which the capital loss of Rs. 1,48,121 originally determined was subsequently revised in April 1982 and instead of capital loss, a capital gain of Rs. 43,360 was computed. The capital gain of Rs. 43,360 was adjusted against the carried forward capital loss of Rs. 4,920 relating to assess-

ment year 1967-68 and capital loss of Rs. 38,440 (out of Rs. 3,55,002) relating to assessment year 1969-70. Consequent on the revision of the assessment for 1971-72 in April 1982, there was no long-term capital loss to be carried forward from the assessment year 1971-72 and the balance of long-term capital loss pertaining to assessment year 1969-70 to be carried forward and set off was only Rs. 3,16,562. However, the assessment for the year 1973-74 made in April 1982 was not revised subsequently to withdraw the excessive set off of long-term capital loss of Rs. 1,86,561 (Rs. 38,440 for assessment year 1969-70 and Rs. 1,48,121 for the assessment year 1971-72). The omission resulted in short-levy of income-tax of Rs. 83,952 in the assessment year 1973-74.

The Ministry of Finance have accepted the mistake (October 1984).

The internal audit party of the department has checked the assessment but did not detect the mistake.

(vi) Under the Income-tax Act, 1961 any loss computed in respect of a speculation business carried on by the assessee can be set off only against profits and gains of another speculation business. It has also been provided in the Act that where any part of the business of a company (other than an investment, banking or a financial company) consists in the purchase and sale of shares of other companies, such company shall be deemed to be carrying on a speculation business to the extent to which the business consists of purchase and sales of shares.

The assessment of a company deriving its income mainly from management and consultancy services was done in a central circle in July 1982 for the assessment year 1980-81, computing the income of the company at Rs. 1,41,540 after set off of loss of Rs. 4,12,092 on short-term capital assets. The loss arose on sale of shares of another company belonging to the same group in September 1979 for a consideration of Rs. 2,14,959. The shares were initially purchased by the assessee during the period from June 1978 to March 1979 for Rs. 6,27,051.

Since the assessee company was not an investment, banking or financial company but one engaged in management and consultancy services, that part of the business in the previous year relevant to the assessment year 1980-81 consisting of the purchase and sale of shares of other companies, should be deemed

to be a speculation business and the loss incurred therefrom as a speculation loss, which under the law cannot be set off against the income under any other source. The speculation loss has to be carried forward for set off against speculation profit in future years. The incorrect set-off resulted in under assessment of business income by Rs. 4,12,090 involving short-levy of tax of Rs. 2,43,649.

The Ministry of Finance have accepted the mistake (January 1985).

2.31 *Mistakes in assessments while giving effect to appellate orders.*

The Income-tax Act, 1961, provides for deduction of capital expenditure incurred on scientific research in computing the business income of an assessee. The Act further provides that where expenditure on scientific research is represented wholly or partly by an asset no deduction is allowable by way of depreciation allowance on the cost of the asset in the same or any other previous year. The appellate authorities had been taking the view that deduction on account of depreciation on these assets would not be available only in relation to the year in which the capital expenditure was allowed and where the asset was continued to be used for purpose of scientific research, in subsequent years, the assessee would be entitled to depreciation on the capital assets in subsequent years. The Act was amended by the Finance (No. 2) Act, 1980 retrospectively with effect from 1 April 1962 to make it clear that no depreciation would be admissible on capital assets on scientific expenditure whether in the year in which the capital expenditure on the assets was allowed or in any other previous year.

(i) (a) In the assessment of a company made in February 1984 for the assessment year 1974-75 a sum of Rs. 29,75,204 was allowed as depreciation on capital assets used for scientific research in the engineering research centre of the company on the basis of Appellate Tribunal's order of March 1980. As the full cost of the assets used for scientific research had already been allowed as a deduction, no further deduction by way of depreciation was admissible in the light of amendment to the Act. The Income-tax Officer was to approach the Tribunal to rectify their order as a mistake apparent from record to enable him to disallow the depreciation already allowed. The omission resulted in incorrect allowance of depreciation leading to under-assess-

ment of income by Rs. 29,75,204 and short-levy of tax of Rs. 17,18,178.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(b) A company was originally assessed in September 1979 for the assessment year 1976-77 disallowing depreciation of Rs. 1,79,457 on assets used for scientific research, the cost of which was fully allowed as a deduction. On appeal the Commissioner of Income-tax (Appeals) in his order of January 1980 allowed depreciation amounting to Rs. 1,79,457 on these assets. The assessment for the assessment year 1976-77 was revised in March 1980 to give effect to the orders of Commissioner (Appeals). On appeal by the department, the Appellate Tribunal in its order of August 1982 allowed the appeal and reversed the orders of the Commissioner (Appeals) in view of the retrospective amendment to the Act. Although the assessment for the assessment year 1976-77 was revised again in December 1982 to give effect to the orders of the Appellate Tribunal, the depreciation of Rs. 1,79,457 wrongly allowed in the revised assessment made in March 1980 was not withdrawn. The omission resulted in under-assessment of income of Rs. 1,79,457 involving short-levy of tax of Rs. 1,03,638.

The Ministry of Finance have accepted the mistake (September 1984).

(ii) The original assessment of a company was completed in May 1978 for the assessment year 1974-75 by the Income-tax Officer disallowing an expenditure of Rs. 1,50,000 incurred by the company for filing fees paid to the Registrar of Companies for raising the authorised share capital, holding the expenditure as capital. On appeal the Commissioner (Appeals) in his order of January 1979 held the expenditure as revenue expenditure and the assessment for the assessment year 1974-75 was revised in March 1979 allowing a deduction of Rs. 1,50,000. On appeal to the Appellate Tribunal both by the department and the assessee company on several grounds including the allowance of the above expenditure by the Commissioner (Appeals) the Appellate Tribunal in its order of May 1980, holding that the expenditure of Rs. 1,50,000 incurred to raise the capital of the company is a capital expenditure, reversed the orders of the Commissioner (Appeals). Though the assessment was revised in February 1981 to give effect to the orders of the Appellate Tribunal and further revised in April 1981 and July 1981 to rectify some other mis-

takes, the deduction of Rs. 1,50,000 allowed in March 1979 was not withdrawn by the Income-tax Officer. The omission resulted in under-assessment of income by Rs. 1,50,000 involving short-levy of tax and surtax of Rs. 1,05,638 including surtax of Rs. 19,013.

The Ministry of Finance have accepted the mistake (December 1984).

(iii) In the assessment of a company for the assessment year 1975-76 (made in August 1978), the Income-tax Officer allowed the tax holiday relief in respect of the new industrial undertaking of the company after deducting the long-term borrowings and debts from total value of assets, as laid down in the Income-tax Rules, 1962. On an appeal preferred by the assessee, the Commissioner (Appeals) allowed in September 1979 more relief treating the long-term borrowings also as capital employed as was then held by some of the High Courts. The assessment was accordingly revised in November 1979 affording more relief. As a result of further appeal preferred by the department, the Appellate Tribunal directed in April 1982, that the relief should be recomputed as envisaged in the retrospective amendment of the law from 1 April 1972.

Accordingly, the Commissioner (Appeals), also directed in December 1982 that the capital already computed by the assessing officer, in his assessment order, was correct in view of the retrospective amendment of the law. However, the revision made in November 1979 was not cancelled restoring the original assessment made by the Income-tax Officer in August 1978. The omission led to excess allowance of relief of Rs. 42,13,502 in the assessment year 1975-76, with consequent short-levy of tax of Rs. 28,78,348 (including surtax) in the assessment year 1976-77 when the relief allowed was adjusted.

The Ministry of Finance have accepted the mistake (September 1984).

(iv) Under the provisions of the Income-tax Act, 1961 prior to its amendment by the Finance Act, 1980 with effect from the assessment year 1981-82 where the gross total income of an assessee includes any profits and gains derived from a newly established industrial undertaking which went into production before 1 April 1981, the assessee is entitled to tax re-

lief in respect of such profits and gains upto 6 per cent per annum (7½ per cent from 1 April 1976) of capital employed in the undertaking in the assessment year in which it begins to manufacture or produce articles and also in each of the four succeeding assessment years. Where the profits and gains derived from the industrial undertaking fall short of the relevant amount of capital employed or where there are no profits and gains, the whole or balance of deficiency can be carried forward for adjustment upto the seventh assessment year, reckoned from the end of the initial assessment year.

In the regular assessment of a company for the assessment year 1974-75 finalised in July 1977, an amount of Rs. 17,78,792 being unabsorbed tax holiday relief due in respect of a new industrial undertaking of the company for the assessment years 1967-68 to 1971-72 was set off against the profits. As a result of orders of Commissioner (Appeals), the tax holiday relief was enhanced by Rs. 55,885 for the assessment year 1971-72. However, the amount of carried forward relief for set-off against future profits was reduced by Rs. 5,21,915 for the assessment year 1971-72 under the orders of September 1979 of the Appellate Tribunal, which ordered determination of the income of the unit afresh for the assessment year 1971-72. The Appellate Tribunal's orders were given effect to in January 1980. Consequently the relief originally allowed in the assessment year 1974-75 in July 1977 was required to be withdrawn, which was not done by the assessing officer. The omission led to under-assessment of income of Rs. 4,66,030 (Rs. 5,21,915 minus Rs. 55,885) involving short-levy of tax Rs. 2,66,820.

The Ministry of Finance have accepted the mistake (August 1984).

(v) In the income-tax assessment of a private company for the assessment years 1976-77 and 1977-78 finalised in September 1978 and December 1979 respectively, the assessing officer quantified the tax holiday relief admissible in respect of profits or gains derived from a new industrial unit owned by the assessee at Rs. 9,732 and Rs. 2,490 respectively. For want of profit, the relief was allowed to be carried over for adjustment in subsequent assessment year. On appeal by the assessee against both the assessments, the Commissioner (Appeals) held (June 1980) that the quantum of relief is to

be determined on the gross value of the capital employed in the undertaking without reducing therefrom the liabilities owned by the assessee. The appellate orders were given effect to in March 1980 revising the relief admissible to Rs. 1,17,924 and Rs. 1,27,308 respectively. Consequent on the retrospsctive amendment of the relevant provision of tax holiday relief in the Income-tax Act, 1961 with effect from 1 April 1972, the Appellate Tribunal on an appeal by the department set aside (June 1981) the orders of the Commissioner (Appeals) and directed the assessing officer to determine the relief afresh. The orders of the Tribunal had not, however, been given effect to till the date of audit (June 1983). Meanwhile, the relief in respect of the profits and gains of the units as revised in terms of the orders of the Commissioner (Appeals). was carried forward and set off was allowed against the income for the assessment year 1980-81 completed in Septemebr 1982. As against the total relief of Rs. 12,222 admissible in respect of both the assessment years, deduction of Rs. 2,45,232 was, therefore, allowed in the assessment year 1980-81. The incorrect grant of relief resulted in under-assessment of income by Rs. 2,33,010 involving undercharge of tax of Rs. 1,51,505.

The Ministry of Finance have accepted the mistake (August 1984).

Incorrect exemptions and excess reliefs

2.32 *Incorrect deductions in respect of inter-corporate dividends.*

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

The Calcutta (February 1978) and Gujarat (November 1981) High Courts have held that in the case of assessee carrying on business as dealers-in-shares, the shares constitute their stock-in-trade and consequently the dividend income is in

the nature of business income and the entire expenses relating thereto could be allowed in the computation of business income without allocating specifically to the dividend income.

Finding that there are no guidelines available with the assessing officers to determine who are dealers in shares, the Public Accounts Committee in para 67 of their 206th Report (Seventh Lok Sabha 1983-84) recommended that "the Central Board of Direct Taxes should issue necessary guidelines to the field formations on the tests to be applied to determine who are dealers-in-shares. They should also issue instructions to lower formations to take special care to scrutinise the balance sheets and profit and loss accounts of such assessee companies as claiming to be dealers-in-shares".

(i) (a) The assessments of a closely-held company for the assessment years 1974-75, 1975-76 and 1976-77 were revised (February 1980—May 1980) wherein the deduction on account of inter-corporate dividends amounting to Rs. 24,41,729 was allowed by the department computing the same with reference to the gross dividend income instead of Rs. 19,13,910 with reference to the net dividend income. In accordance with retrospective amendment of the Act from 1 April 1968, the assessee company was entitled to a deduction of Rs. 19,13,910 only. The excess deduction resulted in under-assessment of income of Rs. 5,27,819 for the three years with consequent short-levy of tax of Rs. 3,60,237.

The Ministry of Finance have accepted the mistake in principle (November 1984).

(b) While completing the assessment of two banking companies for the assessment years 1974-75 and 1975-76 originally assessed between September 1977 and August 1978 and subsequently revised in January 1981 and November 1981 deductions on account of inter-corporate dividends were allowed to the extent of Rs. 5,61,059 on the gross amount of dividends. In view of the retrospective amendment made to the Income-tax Act, 1961, through the Finance Act, 1980 the deduction is allowable only on the net amount of dividends. The mistake resulted in short-levy of tax of Rs. 3,24,012.

The paragraph was forwarded to the Ministry of Finance in Septemebr 1984; their reply is awaited (November 1984).

(c) Form 1 April 1977 the specified deduction on account of inter-corporate dividends is not admissible to a non-resident company. Instead where the total income of a foreign company includes any income by way of dividends, the income-tax shall be payable at the rate of 25 per cent.

In the case of a non-resident company for the assessment year 1976-77 completed in March 1980, the deduction on account of inter-corporate dividends was allowed on the gross dividend income as per law as it stood at that time. Consequent on the amendment of law in 1980 with retrospective effect from 1 April 1968 the deduction was required to be allowed on the net dividend income which was not done although the assessment was revised in March 1983 on some other grounds. This resulted in excess allowance of deduction of Rs. 21,85,520 with consequent tax undercharge of Rs. 1,60,612.

Further, in the assessment year 1979-80 (revised assessment completed in March 1983) a deduction of Rs. 2,82,480 on account of inter-corporate dividends was allowed to the same non-resident company overlooking the amendment to the law with effect from 1 April 1977. This led to under-assessment of income of Rs. 2,82,480 with tax undercharge of Rs. 70,620.

The two mistakes led to undercharge of tax of Rs. 2,31,232 in the two assessment years.

The paragarph was sent to the Ministry of Finance in June 1984; their reply is awaited (November 1984).

2.33 *Incorrect deduction of fees received from foreign enterprise*

Under the Chapter VI-A of the Income-tax Act, 1961, where the gross total income of an Indian company includes income by way of royalty, fees or any similar payment received by the company from a foreign enterprise in consideration for technical services rendered outside India to the foreign enterprise under an agreement approved by the Board of Direct Taxes and such income is received in convertible foreign exchange in India, a deduction of the whole of such income shall be allowed in computing the income of the company. Chapter VI-A of the Act provides for certain deductions to be made from the gross total income to arrive at net chargeable income to tax. The overriding condition is that the total deduction should not exceed the gross total income of the assessee. Gross total income has been defined as the total income computed in accordance with

the provisions of the Act before making deduction under Chapter-VIA. Where set-off of unabsorbed loss of earlier years, being an anterior stage results in reducing the total income to 'nil' or loss, no deduction under Chapter VI-A is admissible. No provision exists in the Act to carry forward the unabsorbed income received by a company from a foreign enterprise for deduction from the gross total income of future years.

For the assessment years 1977-78, 1978-79 and 1979-80 an assessee company claimed deduction of Rs. 5,61,882, Rs. 2,34,192 and Rs. 8,01,599 respectively on account of fees received from a foreign enterprise for the technical services rendered by the company. In the assessments made in March 1981, August 1981 and September 1982 for the assessment years 1977-78 to 1979-80 respectively, the Income-tax Officer allowed the deduction as claimed by the assessee company. The gross total income of the assessee company, not being sufficient to adjust the fees received from foreign enterprise in full, the Income-tax Officer allowed the company to carry forward the unabsorbed deduction of Rs. 42,178, Rs. 1,84,427 and Rs. 5,55,892 in the assessment years 1977-78 to 1979-80 respectively. In the assessment for the assessment year 1980-81 made in March 1983, the Income-tax Officer set off the unabsorbed fees of the earlier years against the positive income of Rs. 1,86,167 and allowed to carry forward the balance unabsorbed fees amounting to Rs. 5,96,330. As the Act stipulates that the deduction of fees received from foreign enterprise should not exceed the gross total income of the respective assessment years of the company and no carry forward of the unabsorbed deduction is admissible, the carry forward of the unabsorbed fees of Rs. 7,82,497 for deduction from future years gross total income was not in order. The mistake resulted in under-assessment of income of Rs. 1,86,167 involving short-levy of tax of Rs. 1,30,085 and excess carry forward of loss of Rs. 5,96,330 in the assessment year 1980-81.

The Ministry of Finance have accepted the mistake (December 1984).

2.34 *Incorrect allowance of relief in respect of newly established business undertaking.*

Under the provisions of Income-tax Act, 1961, prior to its amendment by the Finance Act, 1980 with effect from the assessment year 1981-82 where the gross total income of an

assessee included any profits and gains derived from a newly established undertaking which went into production before 1 April 1981, the assessee became entitled to tax relief in respect of such profits and gains upto 6 per cent per annum (7-1|2 per cent from 1 April 1976) of capital employed in the undertaking in the assessment year in which it began to manufacture or produce articles and also in each of the four succeeding assessment years.

Where, however, such profits and gains fall short of the relevant amount of capital employed during the previous year the amount of such short fall or deficiency was to be carried forward and set off against future profits upto the seventh assessment year reckoned from the end of the initial assessment year.

The method of computing capital employed in the industrial undertaking was laid down in Income-tax Rules, 1962 according to which the capital employed would be the value of assets on the first day of the computation period of the undertaking, as reduced by moneys and debts owed by the assessee on that day. Accordingly the capital employed was calculated on the basis of owned capital and reserves only exclusive of borrowed capital. By an amendment through the Finance Act, 1980 to the Act, the provisions of the Rules were incorporated in the Act itself retrospectively from 1 April 1972.

(i) In the assessment of a private limited company for the assessment year 1978-79 completed in March 1979 and modified in April 1981, the department allowed relief in respect of its newly established undertaking at Rs. 3,44,588 as claimed by the company. Neither the claim by the assessee was supported with necessary details nor the assessing officer, at the time of allowing the relief, called for the details and verified the correctness of claim.

At the instance of audit in August 1981, the Income-tax Officer called for the details. The correct relief admissible as per the law was found to be only Rs. 1,47,960. The excess relief on withdrawal resulted in additional demand of tax of Rs. 1,23,865.

The excess relief allowed was not also noticed in the internal audit.

The Ministry of Finance have accepted the mistake (September 1984).

(ii) (a) While computing the capital employed in the new industrial undertaking of a company in the assessment for the assessment year 1979-80 completed in September 1982, a sum of Rs. 1,85,44,000 being the balance of unsecured loan due to the Central Government had not been deducted to arrive at the net capital employed and the tax holiday relief as claimed by the assessee was allowed by the Income-tax Officer. The omission to deduct the borrowings resulted in excess computation of capital by Rs. 1,85,44,000 and excess allowance of tax holiday relief of Rs. 11,12,640 with consequent undercharge of tax of Rs. 6,42,549 in the assessment year 1979-80.

The Ministry of Finance have accepted the mistake (August 1984).

(b) In the assessment of a manufacturing company for the assessment year 1974-75 revised in September 1982 the Income-tax Officer allowed a set off of Rs. 12,74,396 on account of carry forward deficiency of tax holiday relief granted to an industrial undertaking of the assessee. The tax holiday relief in respect of the industrial undertaking for the assessment year 1973-74 was calculated by the assessing officer on the basis of gross assets only without taking into account the liabilities relating to the new unit. The new industrial undertaking was entitled to a tax holiday relief of Rs. 5,98,359 only worked out on the basis of value of assets on the first day of computation period as reduced by the debts owed by the unit. The mistake in not taking into account the debts owed by the unit resulted in excess computation of capital employed leading to excess carry forward of loss of Rs. 6,76,837, for the assessment year 1974-75 with a tax effect of Rs. 4,25,903.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(iii) A company was entitled for tax holiday relief of Rs. 1,25,160 and Rs. 2,66,808 for the assessment years 1975-76 and 1976-77 respectively on its newly established industrial undertaking. As the new unit suffered loss, the tax holiday relief for these two years was allowed to be carried forward for adjustment in the subsequent years. The deficiency was adjusted in full in the assessment made in September 1982 for the assessment year 1979-80.

The assessment for the assessment year 1977-78 which was originally made in June 1980 was revised in May 1983 to give

effect to certain orders of August 1982 of the Income-tax Appellate Tribunal and while revising the asessment the tax holiday relief of Rs. 3,91,968 carried forward from the assessment years 1975-76 and 1976-77 was again adjusted. However, no action to withdraw the adjustment of the relief already made in September 1982 in the assessment for assessment year 1979-80 was taken. The omission resulted in double allowance of the tax holiday relief leading to under-assessment of income by Rs. 3,91,968 involving short-levy of tax of Rs. 2,14,477 for the assessment year 1979-80.

The Ministry of Finance have accepted the mistake (November 1984).

(iv) The assessment of a company in which public were substantially interested for the assessment year 1978-79 was completed in September 1982 in which the capital employed was computed, taking the written down value as returned by the assessee in the revised return filed for that year in March 1981. The written down value had, however, undergone revision for the assessment year 1977-78 completed in September 1981 after filing of the return for the assessment year 1978-79 in March 1981 and had been reduced by Rs. 42,72,865 due to allowance of further depreciation during the course of the assessment. Adoption of the value of plant and machinery at a higher amount, without taking into account their revised written down value led to excess computation of capital and consequently to excess tax holiday relief of Rs. 2,56,372 involving undercharge of tax (including surtax) of Rs. 1,91,382.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

(v) In the assessment of a private company made in September 1982 for the assessment year 1979-80, the assessing officer allowed in full the tax holiday relief amounting to Rs. 7,78,050 in respect of a new unit although the profit from the unit was Rs. 5,22,000 only. Since the profit of the new unit fell short of relief, it was required to be restricted to the available profit only. Failure to do so resulted in excess allowance of relief to the extent of Rs. 2,56,050 leading to short-levy of tax of Rs. 1,47,868.

The Ministry of Finance have accepted the mistake (July 1984).

(vi) A company in which public are not substantially interested commenced production in the previous year relevant to the assessment year 1969-70 and the relief in respect of newly established industrial undertaking for the assessment years 1970-71 and 1971-72 was determined as Rs. 88,548 and Rs. 45,865 respectively. The relief was allowed to be carried forward for set off against future profits for want of sufficient profits and gains in the respective assessment years. Under the provisions of the Act, the relief could be carried forward and set off against the profits only upto the assessment year 1976-77, being the seventh assessment year from the end of the initial assessment year 1969-70. In the assessments for the assessment years 1977-78 and 1978-79 completed in March 1983, the relief was, however, incorrectly brought forward and set off against the profits and gains of these years to the extent of Rs. 1,34,413. The incorrect set off resulted in total short-levy of tax of Rs. 84,679 for the two assessment years.

The Ministry of Finance have accepted the mistake (August 1984).

(vii) The provisions of tax holiday relief was amended by the Finance Act, 1979 under which an industrial undertaking which manufactured or produced any articles specified in the Eleventh Schedule to the Act was not entitled to tax holiday benefit with effect from 1 April 1979.

An assessee company claimed a deduction of Rs. 1,58,285 for the assessment year 1980-81 in respect of the unit manufacturing utensils in its packing division which was allowed by the assessing officer in the assessment made in December 1982. As the manufacture of utensils was an item listed in the Eleventh Schedule to the Act, it was not eligible for the tax holiday relief. The incorrect relief granted by the department resulted in under-assessment of income by Rs. 1,58,285 with consequent undercharge of tax of Rs. 93,584.

While not accepting the mistake, the Ministry of Finance stated (December 1984) that industries manufacturing items prescribed in the Eleventh Schedule are precluded from claiming tax holiday benefit, if the manufacturing has commenced after 1 April 1979. Since the assessee company had commenced manufacturing in 1978, the assessee was not barred from getting the benefit. The reply of the Ministry is contrary to the provisions

of Law which had withdrawn the tax holiday concessions in respect of industrial undertakings which had been manufacturing or producing articles listed in the Eleventh Schedule with effect from 1 April 1979.

(viii) In the case of a company, the tax holiday relief allowable for the assessment years 1981-82 and 1982-83 completed in October 1982 was computed at Rs. 7,98,717 and Rs. 8,14,366 respectively and carried forward for set off against profits of future years. While computing the relief for these two assessment years, secured loans totalling to Rs. 70,42,167 and Rs. 85,66,902 respectively were not, however, deducted from the value of the assets. This resulted in excess relief by Rs. 5,28,165 for the assessment year 1981-82 and Rs. 6,42,517 for the assessment year 1982-83 leading to excess carry forward of Rs. 11,70,682 for adjustment against future years income.

The Ministry of Finance have accepted the mistake (December 1984).

(ix) While computing the gross total income as defined in the Act the unabsorbed business loss, depreciation or development rebate should first be set off against the profit and gain. The tax holiday relief is to be set off against the balance profits, if any.

A hydraulic unit, a new industrial undertaking of an assessee company, went into production in the assessment year 1972-73. The new unit did not derive any profit upto the assessment year 1975-76 and the tax holiday relief in respect of the new unit for the assessment years 1972-73 to 1975-76 amounting to Rs. 9,56,927 was carried forward for set off against the profits for the assessment year 1976-77. In the assessment completed in July 1980 for the assessment year 1976-77, the carry forward loss to the extent of Rs. 5,20,897 was set off against the profit of Rs. 5,20,897 of the unit as computed by the assessee. For the assessment year 1975-76 the assessee company was allowed to carry forward unabsorbed development rebate of Rs. 5,27,487 which included development rebate of Rs. 1,88,528 relating to the new unit of the assessee company. In addition, the assessee was entitled to a development rebate of Rs. 26,347 for the assessment year 1976-77 for the new unit. The unabsorbed and current development rebate was required to be set off first against the profit of the new unit before adjusting the carried forward

relief. Instead the entire profit was adjusted against the carry forward deficiency of tax holiday relief. The adjustment led to under-assessment of income by Rs. 2,14,875 for the assessment year 1976-77.

In the case of the same unit, in the assessment completed in May 1981 for the assessment year 1977-78, the Income-tax Officer set off the unabsorbed tax holiday relief amounting to Rs. 8,64,349 for the assessment years 1974-75 to 1976-77 against the profit as computed by the assessee company at Rs. 5,94,888 of the unit. The company was allowed investment allowance of Rs. 6,87,670 for the assessment year 1977-78 in respect of the new unit, which was required to be deducted first from the profits derived by the unit before adjusting the carry forward relief. The omission to first adjust the investment allowance which itself was more than the profits, and incorrect adjustment of carry forward relief when no profit was available for such adjustment resulted in under-assessment of income by Rs. 8,64,349 for the assessment year 1977-78.

The total under-assessment of income for the two assessment years was Rs. 10,79,224 involving short-levy of tax of Rs. 6,11,352.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(x) The Rules stipulate that in case of depreciable assets, the written down value as at the beginning of the previous year should be taken into account while computing capital employed.

In the assessment made in February 1983 of a company for the assessment year 1979-80, while determining the capital employed in the new industrial undertaking, the Inspecting Assistant Commissioner (Assessment) Special Range, valued the depreciable assets at Rs. 7,93,19,187 as claimed by the assessee company instead of adopting the written down value of the assets at Rs. 7,03,36,502 as per Income-tax Rules. This resulted in excess computation of capital of Rs. 89,82,685 leading to excess allowance of relief of Rs. 6,73,701 for the assessment year 1979-80. As the new unit did not derive any profit, it led to excess carry forward of unabsorbed relief of a like amount.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(xi) Under the provisions of the Finance Acts, an 'industrial company' is subject to lower rates of tax as compared to a non-industrial company. The Finance Act defines an 'industrial company', as a company which is mainly engaged in the business of generation or distribution of electricity or any other form of power or in the construction of ships or in the manufacture or processing in goods or in mining. The provisions of the Income-tax Act offer a tax holiday relief to new industrial undertakings. Under the Income-tax Act, the relief ensures to the profits and gains derived by an assessee from a new industrial undertaking which begins to manufacture or produce articles.

A company engaged in purchase, re-drying and exporting of tobacco to foreign companies claimed the tax holiday relief in respect of the three re-drying units, newly set-up, during the previous years relevant to the assessment years 1974-75 to 1976-77. In the original assessments made in June 1974 and June 1975, the relief was disallowed by the department on the ground that the assessee was not engaged in the manufacture or production of articles as envisaged in the Act.

The assessee, *inter-alia*, preferred appeals that it should be treated as an 'industrial company' entitling it to concessional rates of tax under the Finance Act and to benefit of tax holiday relief under the Income-tax Act, as it had set up new units. The Appellate Tribunal in its orders of June 1980 and November 1980 for the three assessment years admitted the claim of the assessee for the status of an 'industrial company' under the provisions of the concerned Finance Acts. As regards the contention of the assessee for affording the tax holiday relief, the Appellate Tribunal directed the Income-tax Officer to consider the claim and allow it if the mandate of the section is satisfied. In the light of the Appellate Tribunal's findings, the assessee's entitlement to tax holiday relief under the Income-tax Act needed consideration afresh by the Income-tax Officer.

Instead of examining the claim *de novo*, the Income-tax Officer merely allowed the claim in the re-assessments made for the three years in June/December 1981 stating that it was done as per orders of the Tribunal. As the tax holiday relief is not admissible under the Income-tax Act units engaged in processing of goods, the assessee was not entitled to the tax holiday relief. The incorrect relief of Rs. 8,52,215 resulted in short-levy of tax of Rs. 5,81,626.

The Ministry of Finance have accepted the mistake (January 1985).

(xii) Under the provisions of the Income-tax Act, 1961 where the gross total income of an assessee includes any profits and gains derived from ships brought into use after 31 March 1976, the assessee becomes entitled to tax relief in respect of such profits and gains, upto 7½ per cent of the capital employed in the ships in the assessment year in which the ship is first brought into use and also in each of the following four assessment years. According to the Income-tax Rules, the capital employed in a ship shall be for the first year of relief the net cost of acquisition and for other years, the written down value as on the first day of the relevant previous year.

In the assessment of a public sector company doing dredging in sea, the capital employed for the purpose of computing the relief for the assessment year 1980-81 finalised in January 1983 was computed taking the written-down value of the assets as on 31 March 1980 (Rs. 27,70,22,153) instead of their written down value (Rs. 27,34,39,107) as on 1 April 1979. This resulted in excess computation of the relief by Rs. 2,68,728 and a short demand of tax of Rs. 1,58,986.

The Ministry of Finance have accepted the mistake in principle (December 1984).

(xiii) Under the Income-tax Act, 1961 where the gross total income of an assessee includes any profits and gains derived from an industrial undertaking which had begun to manufacture or produce articles after 31 December 1970 in any backward area, the assessee is entitled to a deduction from such profits or gains for an amount equal to 20 per cent thereof in computing its total income.

In the assessment of a company for the assessment years 1978-79 to 1980-81 made between May 1981 and December 1982, the Income-tax Officer allowed deduction of Rs. 6,61,492 for setting up a new industrial undertaking in a backward area. The profit of the new unit not being readily ascertainable, the Income-tax Officer calculated the total income of the entire business and arrived at the profit of the new unit on a *pro-rata* basis with reference to the total income determined for each of the assessment years. While calculating the total income of the entire business for these assessment years, the department did not take into account the business loss and unabsorbed investment allowance and certain other adjustments of the entire business in earlier years. Accordingly the assessee was entitled to a deduction on this account for a sum of Rs. 4,78,690 only. The

omission led to excess allowance of deductions to the new unit by Rs. 1,82,082 for the assessment years 1978-79 to 1980-81 with consequent undercharge of tax of Rs. 1,06,078.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

2.35 *Excess or irregular refunds*

Under the Income-tax Act, 1961 where a return has been furnished by an assessee and the assessee claims that the tax paid by him by way of tax deducted at source and advance payment of tax exceeds the tax payable on the basis of the return and the Income-tax Officer is of the opinion that the regular assessment is not likely to be made within six months from the date of filing the return; he shall make a provisional assessment after making adjustment to the income declared in the return to the extent laid down in the Act, and refund the tax paid in excess. Under the Act, the tax paid on self assessment shall be deemed to have been paid towards regular assessment and, therefore, for determining the refund of tax due on provisional assessment, the tax paid on self assessment is not required to be considered.

(i) An assessee company paid advance tax of Rs. 5,38,313 for the assessment year 1980-81 and filed the return of income for that assessment year in June 1980 declaring taxable income of Rs. 11,97,860. The assessee also paid self-assessment tax of Rs. 1,68,661 in June 1980. Subsequently the assessee filed a revised return in January, 1981 for the same assessment year showing a reduced taxable income of Rs. 8,23,600. On the basis of the assessee's claim for refund as per the revised return, the Income-tax Officer made a provisional assessment in January 1981 and refunded a tax of Rs. 2,21,281 including the tax of Rs. 1,68,661 paid on self-assessment as per the original return while a refund of tax of Rs. 52,620 being the advance tax paid only was due. The irregular refund made resulted in excess refund of tax of Rs. 1,68,661.

The Ministry of Finance have accepted the mistake (December 1984).

(ii) The Act further provides that while making a provisional assessment, the assessing officer shall make necessary adjustment for giving deductions for unabsorbed investment allowance and tax holiday benefits (available to new industrial undertakings) of earlier years. These deductions should be computed with reference to the assessments made by the department in the earlier years and not on the basis of the returns filed by an assessee.

In the case of private company while making provisional assessment in October 1982 for the assessment year 1981-82, the assessing officer allowed set off of unabsorbed investment allowance and tax holiday benefit for earlier years at Rs. 3,41,112 as claimed in the returns instead of allowing a sum of Rs. 1,04,756 on the basis of the allowance and relief computed in the assessments of the relevant earlier assessment years. This excess allowance resulted in excess grant of deduction to the extent of Rs. 2,36,356 leading to excess refund of tax of Rs. 1,52,448 at the time of making the provisional assessment.

The Ministry of Finance have accepted the mistake (December 1984).

(iii) In the assessment of a company for the assessment year 1980-81 completed in March 1981, the income of the company was computed at Rs. 21,52,930 and the tax payable at Rs. 12,72,919. Interest aggregating Rs. 57,863 was also levied for late filing of the return and short-fall in the payment of advance tax. The assessee company had paid advance tax of Rs. 8,27,750 during the relevant previous year and after adjusting this amount towards total demand of Rs. 13,30,782 the balance demand of Rs. 5,03,032 was set off against the refund due to it for the assessment year 1978-79. In May 1981, the Inspecting Assistant Commissioner of Income-tax waived the interest aggregating Rs. 57,863 levied towards late filing of the return and short-fall in the payment of advance tax. The amount of refund of Rs. 57,863 thus arising was adjusted in March 1982 towards the demand due from the assessee for the assessment year 1979-80.

The assessment for assessment year 1980-81 was further revised in February 1983 to give effect to certain deductions allowed in appeal in the order of January 1983 of the Commissioner of Income-tax (Appeals), and the revision resulted in the computation of income at a loss of Rs. 1,00,433. As no tax was payable, the entire demand of Rs. 1,3,30,782 was refunded to the company in February 1983 overlooking the fact that Rs. 57,863 included therein had already been refunded by adjustment in March 1982. Thus, the refund due to the assessee on the rectification made in February 1983 was only Rs. 12,72,919 as against Rs. 13,30,782 actually made. This erroneous double refund resulted in excess refund of interest to the extent of Rs. 57,863.

The Ministry of Finance have accepted the mistake (August 1984).

NON-LEVY OR INCORRECT LEVY OF INTEREST

2.36 *Delay in filing the return*

Under the Income-tax Act, 1961, where the return for an assessment year is furnished after the specified due date, the assessee shall be liable to pay simple interest at twelve per cent per annum from the day immediately following the specified date to the date of furnishing of the return on the amount of tax payable on the total income as determined on regular assessment, as reduced by the advance tax, if any, paid and tax deducted at source. The Income-tax Rules, 1962 provide that the period for which such interest is to be calculated shall be rounded off to a whole month(s) and for this purpose any fraction of month shall be ignored. The Central Board of Direct Taxes on advice by the Ministry of Law clarified in December 1974 that for this purpose the actual date of filing the return should be included in computing the period for which interest is leviable.

(i) The revised total income of a non-resident company for the assessment year 1975-76 was computed in June 1981 by the Inspecting Assistant Commissioner (Assessment) of a Foreign Company Range at Rs. 2,83,57,132 and a net tax demand of Rs. 47,28,548 was raised. The assessee company had filed its return of income on 30 September 1975 while the due date for filing the return was 30 June 1975. For the delay in filing the return the assessee was liable to pay interest amounting to Rs. 1,41,855 for a period of three months. The Inspecting Assistant Commissioner (Assessment) however. levied interest of Rs. 94,570 calculated for a period of two months only instead of for three months. The mistake resulted in short-levy of interest of Rs. 47,285.

The Ministry of Finance have accepted the mistake (November 1984).

The Special Audit Party has checked the assessment but did not raise this point.

(ii) During the previous year relevant to the assessment year 1981-82, an assessee company paid advance tax totalling to Rs. 2,00,000 in four equal instalments in July, September, December 1980 and March 1981. However no statement of advance tax payable was filed by the company as required under

the provisions of the Income-tax Act and the omission attracted levy of penal interest of Rs. 55,011. In the assessment completed in April 1982, for the assessment year 1981-82, no penal interest was levied by the Income-tax Officer. The omission led to non-levy of penal interest of Rs. 55,011.

The paragraph was forwarded to the Ministry of Finance in July 1984 ; their reply is awaited (November 1984).

2.37 *Non-payment|Short payment of Advance-tax*

Under the Income-tax Act 1961, where an assessee company has paid advance tax for any financial year and the advance tax paid falls short of eighty three and one third per cent of the tax determined on regular assessment, interest at twelve per cent per annum is payable by the assessee on the amount by which the advance tax paid falls short of the assessed tax from the first day of next financial year to the date of regular assessment.

(i) During the financial year relevant to the assessment year 1981-82, an industrial company in which public are substantially interested paid a sum of Rs. 1,31,59,267 as advance tax. On completion of regular assessment in February 1983, for the assessment year 1981-82 on a taxable income of Rs. 2,79,64,380 the Inspecting Assistant Commissioner (Assessment) levied tax of Rs. 1,65,33,940. As the advance tax paid fell short of eighty three and one third per cent of the assessed tax, the company was liable to pay interest amounting to Rs. 6,62,066 on account of short-payment of advance tax. The interest was, however, not levied by the department.

The Ministry of Finance have stated in September 1984 that (i) even though interest was not charged, "the intention of Inspecting Assistant Commissioner was to reduce or waive the interest", as he is empowered to reduce or waive the interest under the Income-tax Rules; and (ii)in view of the nature of additions made to the closing stock in the assessment, the interest leviable may not be exigible.

The levy of interest is mandatory and takes no cognisance, of the intentions of the assessing officer. The levy is not also dependent upon the additions made in the Income Computation.

(ii) In the case of a company, the aggregate advance tax paid for the assessment year 1975-76 on the basis of its revised estimate filed on 13 December 1974 was Rs. 1,45,000. As such each instalment of advance tax payable by it in June and September 1974 worked out to Rs. 48,33,333. However, the company had paid Rs. 35 lakhs and Rs. 20 lakhs only towards the first two instalments on 18 June 1974 and 14 September 1974 respectively on the basis of its original estimate of a lower figure of Rs. 1,04,52,750 filed on 14 June 1974. As the advance tax payable was originally under-estimated by the company, the deficiency in the payment of first two instalments attracted interest of Rs. 1,15,611 under the Act. The department did not levy the interest.

The Ministry of Finance have accepted the mistake (August 1984).

2.38 *Delay in Payment of tax demand*

Under the Income-tax Act, 1961, any demand for tax should be paid by an assessee within thirty five days of service of the notice of demand and failure to do so would attract simple interest at twelve per cent per annum from the date of default. In November 1974, the Central Board of Direct Taxes issued instructions that the interest for belated payment of tax should be calculated and charged within a week of the date of payment of the tax demands.

Under the executive instructions issued by the Central Board of Direct Taxes in April 1982, in cases where the original assessments are subsequently revised, interest is required to be calculated with reference to the date of the service of original demand notice on the tax finally determined irrespective of the fact that during the intervening period there was no tax payable by the assessee under any operative order.

(i) (a) In the case of an assessee company, the original assessments for the years 1975-76 and 1976-77 were completed in July 1979 and August 1979 respectively. These assessments were subseqently rectified in August 1981 and September 1981 respectively and demands of Rs. 2,58,534 and Rs. 4,20,789 were raised. These demands were paid in August 1983. As these payments were delayed beyond the period of thirty five days from the date of original demand notice, interest thereon

was leviable. The omission resulted in non-levy of interest of Rs. 1,99,553 for the two assessment years 1975-76 and 1976-77.

The Ministry of Finance have reported (November 1984) that the additional demand amounting to Rs. 1,99,553 has been raised. Report regarding collection is awaited (December 1984).

(b) For the assessment years 1978-79 and 1979-80 completed in May 1981 and September 1982 respectively, a company was served with notices of demand on 1 June 1981 and 21 September 1982 to pay taxes of Rs. 39,14,088 and Rs. 46,52,469 for the two assessment years. The demands were, however, paid by the assessee on 31 October 1981 and 20 January 1983. Since the demands were not paid within the prescribed period, the assessee was liable to pay interest amounting to Rs. 2,05,935. The interest was, not, however, levied by the department.

The Ministry of Finance have accepted the Omission (July 1984).

(ii) Where an assessee has presented an appeal, the Income-tax Officer may treat the assessee, as not being in default in the payment of tax, in respect of the amount in dispute in appeal even though the time for payment has expired as long as such appeal remains undisposed of. Consequently the amount of tax which is not being disputed is required to be paid by the assessee within the prescribed time.

The original assessment of a company for the assessment year 1979-80 was completed in September 1982 on a total income of Rs. 9,70,18,420 after disallowing certain claims made by the assessee and a tax demand of Rs. 4,26,19,097 was raised. The assessee went in appeal against this assessment order and the assessment was revised under the orders of Commissioner of Income-tax (Appeals) in March 1983 reducing the total income to Rs. 3,49,55,550 and net tax demand of Rs. 36,80,997 was raised by the department. The assessment was again revised in May 1983 further reducing the income of Rs. 3,42,70,230 raising a demand of Rs. 32,85,222. This demand was paid by the assessee on 25 May 1983.

Before the appeal was decided by the Commissioner of Income-tax (Appeal), the department informed the assessee company in November 1982 and February 1983 that pending decision of the Commissioner of Income-tax (Appeal) in the

appeal made by the company, the undisputed demand should be paid by the company immediately. Although there was no dispute over the demand of Rs. 32,85,222 which stood included in the demand raised in September 1982, the amount was paid in May 1983 only.

Since the demand was not paid within the prescribed time, the assessee was liable to pay interest of Rs. 1,97,112. The interest was, however, not levied by the department.

The Ministry of Finance have accepted the omission (July 1984).

(iii) For the assessment year 1979-80 assessment of which was completed in September 1982, a company was served with a notice of demand on 18 September 1982 to pay tax of Rs. 23,42,158. The demand was reduced to Rs. 20,91,319 as a result of a rectification made on 26 February 1983 and the final demand was paid in instalments after the due date. Since the demand was not paid within the prescribed period, the assessee was liable to pay interest amounting to Rs. 1,23,013. The interest was, however, not levied by the department.

The Ministry of Finance have accepted the omission (July 1984).

(iv) In the case of a non-resident company the demand notices for payment of taxes for the assessment years 1975-76 to 1980-81 [assessments were completed by Inspecting Assistant Commissioner (Assessment) between January 1977 and December 1980] were served on the assessee on various dates from March 1977 to December 1980. The tax demands should have been paid by the assessee company before the respective specified due dates. The tax was, however, collected in instalments. For the belated payments, the interest of Rs. 93,145 for the assessment years 1975-76 to 1980-81 was leviable within a week of the final payment of tax demands. No demands for interest were made by the department, though the omission was pointed out by the Special Audit Party of the department in December 1980 in respect of assessment years 1975-76 to 1977-78.

The Ministry of Finance have accepted the mistake (September 1984).

(v) In the case of an assessee company for the assessment year 1977-78, the original demand of Rs. 15,48,516 raised on 29 August 1981 was subsequently revised to Rs. 5,96,036 on 3 August 1982 and was paid on 27 September 1982. However, interest of Rs. 65,560 for the belated payment of tax was not levied for the period from 2 October 1981 (i.e. 35 days after 29 August 1981) to 27 September 1982.

The Ministry of Finance have accepted the mistake (September 1984).

2.39 *Omission to deduct tax at source*

Under the Income-tax Act, 1961, any person not being an individual or a Hindu undivided family who is responsible for paying to a resident any income by way of interest other than income chargeable under the head "interest on securities" shall, at the time of credit of such income to the account of the payee or at the time of payment thereof in cash or by issue of cheque whichever is earlier, deduct income-tax thereon at the rate of 10 per cent as it was applicable for the assessment years 1977-78 to 1979-80 and deposit the same to the credit of Government. Failure to deduct tax at source renders the assessee liable to pay interest at 12 per cent per annum on the amount of such tax.

A private company made a total payment of interest of Rs. 4,49,743 to a resident assessee during the previous years relevant to the assessment years 1977-78 to 1979-80. The company was required to deduct tax at source of Rs. 94,445 calculated at 10 per cent of the payment made from time to time and credit the same to Government. No tax was however deducted by the company at source at the time of making payment and consequently the company was liable to pay interest for this omission.

In the assessments completed in March and May 1981 for the assessment years 1977-78 to 1979-80 no interest was however levied on the failure of the company to deduct tax at source. Omission to do so resulted in non-levy of interest of Rs. 56,343. The aggregate sum recoverable from the assessee was Rs. 1,50,788 (Rs. 94,445 tax plus 56,343 interest).

The Ministry of Finance have accepted the mistake relating to non-levy of interest (January 1985). Reply regarding recovery of the tax not-deducted at source (Rs. 94,445) in awaited.

2.40 *Avoidable or Incorrect payment of interest by Government*

Under the Income-tax Act, 1961, where the advance tax paid by an assessee exceeds the amount of tax payable as determined on regular assessment, the Government is liable to pay interest on the amount of advance tax paid in excess for the period from 1 April of the assessment year to the date of regular assessment. The Board issued instructions in April 1966 directing the Income-tax officers to complete regular assessments as soon as possible after receipt of the return.

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

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

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

Despite the controls prescribed by the Board, the omission to make provisional assessments continue to occur involving

avoidable payment of substantial amounts of interest by Government apart from the delay caused in refunding the amounts due to the assessees under the law.

(i) Four companies in three different Commissioners' charge filed their return of income for the assessment years 1978-79, 1979-80 and 1980-81 between October 1978 and September 1980, three of them returning a loss of Rs. 3,14,13,581 and the fourth an income of Rs. 18,56,810. The companies had paid advance tax and tax deducted at source amounting to Rs. 1,79,80,930 in respect of these assessment years. As refunds were *prima facie* due to the four assessee companies, provisional assessments were required to be made in pursuance of the provisions in the Act and executive instructions issued by the Board. No provisional assessments were however made to refund the tax paid in excess by the companies. The regular assessments of the four companies were made by the Income-tax officers between August 1981 and March 1983 and a sum of Rs. 58,32,355 was refunded to the assessees on account of tax paid in excess along with interest thereon. The omission to make provisional assessments resulted in delay ranging over 28 months to 35 months in the assessees getting refunds and also necessitated payment of interest of Rs. 20,47,276 by the Government which could have been avoided, if the statutory provisions were complied with by the assessing officers.

In three cases, involving payment of interest of Rs. 7,21,792 the Ministry of Finance have contended that the payment of interest is as per law. Steps taken to make the system of framing provisional assessments more effective as contemplated in the law have not however, been indicated by the Ministry.

Reply in respect of the remaining case, sent to the Ministry of Finance in June 1984 is awaited (November 1984).

(ii) Four other companies assessed in three commissioners charges in Bombay city filed their returns of income for the assessment years 1977-78 to 1980-81 between July 1977 and January 1981. As refunds were *prima facie* due to these companies, provisional assessments were required to be made to determine and refund the tax paid in excess. Except in the case of one company, no action was taken by the assessing

officers to make the provisional assessments to refund the taxes paid in excess by the assessee companies. Even in that one case, the provisional assessment was made by the Income-tax Officer after a period of two years whereas it was to have been made within six months from the date of receipt of return. The regular assessments in respect of these cases were completed between August 1980 and March 1983 and taxes amounting to Rs. 52,83,038 paid in excess were refunded to them alongwith interest of Rs. 18,03,137. Had provisional assessments been made within the prescribed time limit of six months, payment of interest amounting to Rs. 12,68,147 could have been avoided.

The Ministry of Finance have accepted the mistake in principle (January 1985).

(iii) Two banking companies assessed in two other Commissioners' charges filed their returns of incomes for the assessment years 1974-75 and 1979-80 in October 1974 and October 1979, respectively returning a total income of Rs. 2,92,52,740. The advance tax and tax deducted at source amounting to Rs. 3,36,68,550 was paid by the two banks for these two assessment years. Since the advance tax paid by the banks exceeded the tax payable on the basis of the returns, refund of excess paid tax was *prima facie* due to them and the department was required to make the provisional assessment before April 1975 and April 1980 respectively to refund the tax. The provisional assessments were however made only in April 1977 and November 1980 after a delay of 13 and 30 months respectively. The regular assessments of the two banking companies were made in April 1978 and September 1982 and a refund of tax of Rs. 2,20,43,189 including interest amounting to Rs. 15,95,153 was made. Had the provisional assessments been done within the prescribed period of six months and the tax paid in excess refunded payment of interest by Government amounting to Rs. 7,20,109 could have been avoided.

The Ministry of Finance accepted the omission in both the cases (September and Dember 1984).

(iv) The Central Board of Direct Taxes have issued instructions in April 1976 that, if the regular assessment needs rectification on account of a mistake apparent from the records,

the interest payable by Government can be altered either on the assessee's application, or by the Income-tax Officer, on his own motion with reference to the tax payable, as per the rectified order.

In the draft assessment order for the assessment year 1977-78 of a company, forwarded for approval of the Inspecting Assistant Commissioner under the provisions of the Act, the assessing officer treated certain expenses relating to replacement of machinery as capital expenditure. Even before the draft order had become final, the Income-tax Officer finalised the regular assessment of the company for the next assessment year viz., 1978-79, in April 1981 allowing depreciation of Rs. 80,12,157 on the capitalised expenditure and granted refund of tax of Rs. 1,01,04,772 paid in excess, with interest thereon, amounting to Rs. 36,37,392.

The Inspecting Assistant Commissioner, however, did not approve the Income-tax Officer's proposal for the assessment year 1977-78 treating the expenditure as capital and allowed the entire cost of replacement of machinery as revenue expenditure and accordingly the assessment for the assessment year 1977-78, was finalised in August 1981. As a consequence, the regular assessment for the assessment year 1978-79 was rectified in December 1981, withdrawing the depreciation of Rs. 80,12,157. Though demand of Rs. 46,27,022 for the assessment year 1978-79 was raised on the basis of the rectification order, the amount of interest of Rs. 36,37,372 paid earlier was not modified on the basis of the rectification order. The omission resulted in excess payment of interest of Rs. 16,65,727.

The Ministry of Finance have accepted the mistake (August 1984).

(v) It was judicially held in October 1983 that an assessee is entitled to interest on the excess amount of advance tax determined only by first order of regular assessment and not on any subsequent revision of assessment based on an appellate order.

The Act has been amended by Taxation Law's amendment Act, 1984 providing for increasing or reducing the interest payable by government as a result of appellate orders only from assessment year 1985-86.

In the case of an assessee company for the assessment year 1976-77 the regular assessment was made in July 1980 raising

a demand of Rs. 27,046. The assessment was rectified in December 1981, raising a demand of Rs. 78,596. No refund of advance tax paid by the company arose in these assessments owing to creation of additional demand of tax and consequently no interest on excess advance tax paid arose. The assessment was revised in November 1982 to give effect to an appellate order, as a result of which tax of Rs. 1,66,706 was refunded to the company. In addition to refund of tax, the department paid interest of Rs. 1,28,849 also on the advance tax paid in excess by the assessee. The payment of interest on excess advance tax paid based on a revised assessment and not on the regular assessment, was not in order. This resulted in incorrect payment of interest of Rs. 1,28,849.

The Ministry of Finance have accepted the mistake (November 1984).

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

In the case of a private limited company, assessed in a central circle provisional assessment for the assessment year 1969-70 was made in June 1970 and refund of Rs. 79,397 was found due to the company. It was ordered by the Assessing Officer on the same day that the refund should be adjusted against the advance tax due from the assessee for the assessment year 1970-71. However, the refund could not be adjusted against the advance tax payable for the subsequent year, since the due date for payment of the last instalment of advance tax had already expired on 15 December 1969. The refund thus remained to be made.

The regular assessment for the assessment year 1969-70 was made in February 1972 and at that time, the non-adjustment of the refund of Rs. 79,397 against the advance tax for

the assessment year 1970-71 and the need for refund were not also noticed. The refund of the amount was, however, made to the company only in September 1982 after a delay of over 12 years. The inordinate delay in making the refund necessitated payment of interest of Rs. 1,08,367 by Government on a refund of Rs. 79,397.

The Ministry of Finance have accepted the omission (September 1984).

(vii) An assessee company became entitled to a total refund of Rs. 4,57,104 in respect of the assessment years 1965-66 and 1966-67 as a result of appellate orders passed in October 1973 and April 1974. Due to frequent changes of the assessing officers and failure to keep a watch over the pendency, the refund was actually made in April 1981 and consequently the department had to pay interest of Rs. 3,76,189 for the delay of more than seven years in granting the refund. Had timely action been taken by the assessing officer to refund the excess tax paid, payment of interest of Rs. 3,76,189 could have been avoided.

In the assessment for the assessment year 1967-68 completed in July 1972 in respect of the same company, interest of Rs. 39,381 was payable on the excess advance tax paid by the company. The amount of interest of Rs. 39,381 was paid only in April 1981 after a delay of more than nine years and for the delay, the assessing officer allowed interest of Rs. 42,766 for the period from March 1972 to March 1981. There is no provision under the Act for payment of interest owing to delay in making payment of interest on advance tax paid in excess and the payment of Rs. 42,766 on this account was not in order.

The Ministry of Finance have accepted the mistake (December 1984).

(viii) Under the Income-tax Act, 1961, where an assessee becomes entitled to refund of any amount paid after 31 March 1975 as a result of any orders passed in appeal or other proceedings under the Act, the Central Government shall pay interest at 12 per cent per annum on the amount so refundable from the date, the disputed demand was paid to the date on which the refund is granted. No interest will, however, be payable for a period of one month from the date of the order passed in appeal or other proceedings. The Central Board of

Direct Taxes issued instructions in January 1977 to the effect that appellate orders involving refunds should be given effect to with extraordinary promptness ensuring that in any case they are given effect to within a month of the date of the order.

The income-tax assessments of a company in which public are substantially interested for the assessment years 1970-71 to 1973-74 were revised in November 1982 to give effect to appellate orders of January 1980|February 1980 passed in favour of the assessee company. According to the Board's instructions of January 1977, the orders were to have been given effect to in February 1980|March 1980 to refund the excess tax paid by the company. However, the appellate orders were given effect to and refund of Rs. 13,09,837 made only in November 1982 after a delay of two years and seven months. Delay in refund had also led to avoidable payment of interest of Rs. 2,64,957 by Government.

The Ministry of Finance have accepted the mistake.

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

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

(i) Consequent upon certain appellate orders passed in March 1980 by the Commissioner (Appeals) an assessee company became entitled to a refund of Rs. 26,67,319 in respect of the assessment year 1976-77. The refund which was to have been granted by April 1980 was actually paid to the assessee in September 1981 together with interest of Rs. 3,34,773. Similarly for the assessment year 1975-76, Commissioner (Appeals) passed orders granting refund of Rs. 19,91,474 in February 1980. However, the refund was granted to the assessee in September 1981 alongwith interest of Rs. 2,48,066. Head the department granted the refunds by April 1980 and March 1980 respectively in respect of the two years, payment of interest amounting to Rs. 5,82,839 could have been avoided.

The Ministry of Finance have accepted the mistake (December 1984).

(ii) Under the Income-tax Act, 1961, if the advance-tax paid during any financial year exceeds the amount of tax determined on regular assessment, the Central Government shall pay simple interest on such advance-tax paid at twelve per cent per annum from the 1st day of April next following the said financial year to the date of regular assessment provided that in respect of any amount refunded on provisional assessment no interest shall be paid for the period after the date of such provisional assessment. Also the interest payable on the refunded amount, upto the date of provisional assessment is payable only on completion of regular assessment and not before. The central Board of Direct Taxes, however, issued instructions in August 1969 that interest due on the advance tax paid in excess, to the assessee shall be allowed along with the refund made on completion of provisional assessment. The Kerala High Court held in July 1979 that the Board's circular of August 1969 cannot be treated as authority for the proposition that interest is payable on the amount of refund ordered at the provisional assessment stage. The court further held that interest on such amount could be and should be paid on regular assessment. The Ministry also confirmed to Audit (July 1980) that interest is payable only on completion of regular assessment and not at the time when a provisional assessment is completed.

The question came up before the Public Accounts Committee and as reported in para 1.25 of 100th Report (7th Lok Sabha) of the Public Accounts Committee, the Ministry of Finance admitted that the withdrawal of Board's instructions of August 1969 allowing the payment of interest at the stage of provisional assessment, is under consideration in view of the Kerala High Court decision. On a reference made, the Ministry of Law advised in December 1981, that the law should be suitably amended to clarify the position. In para 1.36 of their 100th Report, the Public Accounts Committee recommended that a clarificatory amendment to Sec. 214 might be brought forward at an early date.

However, the instructions of August 1969 have not been withdrawn so far, despite the Board's assurances before the Public Accounts Committee. As a result instances continue to occur where interest is paid on the completion of provisional

assessment and such payments are justified by the assessing officers stating that the Board circular of August 1969 still held the field.

In the case of two private limited companies provisional assessments were made in September 1980 and November 1981 in respect of the assessment year 1980-81 on the admitted total income of Rs. 46,71,550 and Rs. 8,00,010 respectively. The assessee companies were allowed refunds of Rs. 8,19,206 and Rs. 3,06,950 out of the advance tax paid. In addition, payment of Rs. 1,02,593 was also made towards interest though payment of such interest was to be made only after completion of regular assessments. The regular assessments were made only in September 1983 and March 1983 determining the total income at Rs. 56,82,430 and Rs. 9,45,070 respectively raising a tax demand of Rs. 36,65,167 and Rs 6,09,570 in respect of the two companies respectively. As such the total interest of Rs. 1,02,593 paid earlier (on the excess tax paid) at the time of making provisional assessments instead of on completion of regular assessment was not in order and resulted in un-intended benefit to the assessee companies.

In regard to the first case, the Ministry of Finance have stated in December 1984, that the amendment to Sec. 214-(IA) effective from 1 April 1985, has settled the issue. The amendment has however, no releveince to the issue. The executive instruction of the Board of August 1969, which derived no authority from the statute continue to be in force. The Ministry's reply in the other case in awaited (January 1985).

2.42 *Non-levy of interest/penalty*

The Income-tax Act, 1961 provides that a company 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 was actually paid. The Company is also liable in such a case, to pay such penalty as the Income-tax Officer may direct, but not exceeding the amount of tax in arrears.

On a reference made by the Ministry of Finance, the Law Ministry opined in March 1984 that under the Bidi and Cigar workers (Conditions of Employment) Act 1966, the expression 'contractor' includes an agent or munshi and hence the provisions in the Income tax Act relating to tax deduction at source by contractors|sub-contractors would apply in respect of payments made to agent or munshi.

Four companies engaged in the business of manufacture of bidies employed munshis as labour contractors who in turn employed labourers for manufacture and binding of bidies. During the previous years relevant to the assessment years 1978-79 to 1980-81 the four companies credited the accounts of the munshis and also paid them in cash a total amount of Rs. 3,64,59,071. Under the aforesaid provisions of the Income-tax Act, the companies were required to deduct tax of Rs. 7,29,181 from the payments made to the munshis and credit the tax to Government Account. Omission to recover the tax at source would attract levy of interest and penalty.

In the assessments for the assessment years 1978-79 to 1980-81 completed by the Income-tax Officer between May 1980 and September 1982, the tax of Rs. 7,29,181 was not deducted at source by the companies at the time of making payment to the munshis. The companies were therefore liable to pay interest and penalty of Rs. 3,81,219 besides tax of Rs. 7,29,181. No action was however taken to levy and recover the demand of Rs. 11,10,400.

The Ministry of Finance have accepted the mistake (December 1984).

2.43 *Short levy of penalty.*

Under the Income-tax Act, 1961, if the assessing officer, in the course of any proceeding is satisfied that any person has concealed the particulars of his income or furnished inaccurate particulars of such income, he may direct that such person shall pay by way of penalty not exceeding twice the amount of tax sought to be evaded.

A company concealed its income amounting to Rs. 2,66,615 in the previous year relevant to the assessment year 1979-80. Having satisfied that the company has concealed the income, the Income-tax Officer levied penalty at twice the amount of tax sought to be evaded, amounting to Rs. 2,51,950 by his order of November 1982. The tax leviable was however wrongly calculated a the rate of 45 per cent instead of 55 per cent on the

income of Rs. 2,66,615 and consequently as against penalty of Rs. 3,07,938 leviable on the tax of Rs. 1,53,969 a sum of Rs. 2,51,950 was levied leading to short-levy of penalty of Rs. 55,988.

The Ministry of Finance have accepted the mistake (July 1984).

2.44 *Non-levy of additional income-tax*

Under the provisions of the Income-tax Act, 1961 where the profits and gains of any previous year distributed as dividends within the twelve months immediately following the expiry of the previous year by a company, not being one in which the public are substantially interested or a hundred per cent subsidiary of any such company, are less than the statutory percentage of the distributable income of that previous year, the company is liable to pay additional income-tax at the rates given below on the distributable income as reduced by the amounts and dividends actually distributed if any :

(i) Investment company	50 per cent
(ii) Trading company	37 per cent
(iii) Any other company	25 per cent

By an amendment by Finance (No. 2) Act, 1977 to the Income-tax Act, 1961, from 1 April 1978 an Indian company whose business consists mainly in the construction of ships or in the manufacture or processing of goods or in mining or in the generation or distribution of electricity or any other form of power is not required to pay additional income-tax.

A private limited company engaged in the business of construction of buildings and houses had distributable income of Rs. 5,35,457 and Rs. 3,40,087 for the assessment years 1979-80 and 1980-81 respectively. Since the assessee company was not in the business of construction of ships or in the manufacture or processing of goods, it was required to distribute dividend of Rs. 3,21,274 and Rs. 2,04,052 calculated at the prescribed percentage of 60 of the distributable income in respect of these two assessment years. The assessee company had however distributed a dividend of Rs. 1,89,405 only for each year and in the assessments completed in June and October 1981 for the assessment years 1979-80 and 1980-81, the Income-tax Officer had accepted the same. Since the dividend distributed by the assessee company was less than the statutory percentage, the company was liable to pay additional income-tax at the rate of 25 per cent on the distributable income as reduced by Rs. 1,89,405 for each year

on account of dividend actually distributed. The omission resulted in non-levy of additional income-tax of Rs. 1,24,183 for the two assessment years 1979-80 and 1980-81.

The paragraph was forwarded to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

ANOTHER TOPIC OF INTEREST

2.45 *Non issue of recovery certificate for arrears of tax and omission to raise demand for interest for delay in payment of tax*

Under the provisions of the Income-tax Act, 1961, where an assessee is in default in making a payment of tax the Income-tax Officer may forward to the Tax Recovery Officer a certificate specifying the amount of arrears due from the assessee. The rules made under the act require that at the time of issuing a certificate the Income-tax Officer should calculate the interest payable on the arrears of tax from the day following the due date to the date of issue of the certificate and include such interest in the certificate issued. It is also provided that the recovery certificate should be issued well in time and care should be taken that the demand does not become barred by time and that when any demand is revised, the requisite particulars should be entered in the plus and minus memorandum and a note thereof kept in the remarks column of the Register of Demand and Collections against the original entry.

The assessment of a private company for the assessment year 1975-76 was completed by the Income-tax Officer in November 1977 and a notice of demand for Rs. 2,82,593 was served on 24 November 1977. The demand was reduced to Rs. 2,45,001 in the revision order of August 1978, out of which a demand of Rs. 15,966 was paid in January 1979. The assessment was revised again in March 1982 and an additional demand of Rs. 29,979 was raised. As the assessee was in arrears of tax, a tax recovery certificate was issued on 31 March 1983.

The certificate was however issued only for the additional demand of Rs. 29,979 raised in March 1982 together with the interest thereon and no recovery certificate was issued for the balance of Rs. 2,29,035 which was outstanding as on 31 March, 1983 as necessary entry was not made in the plus and minus memorandum in the register of demand and collections to indicate the correct revised demand. The interest due thereon for

the delay in payment of tax and recoverable as arrears of tax worked out to Rs. 1,64,498 upto the end of November 1983. The omission to follow the correct procedure resulted in non-recovery of tax and interest there on aggregating to Rs. 3,89,533.

The paragraph was forwarded to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

SURTAX

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

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

During the period under review, under-assessment of super profits tax/surtax of Rs. 394.09 lakhs was noticed in 181 cases. A few illustrative cases are given in the following paragraphs.

2.46 *Incorrect Computation of capital*

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 15 per cent 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. It further lays down that 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 purpose of computation of capital. Where no specific provision is made for payment of dividends and the proposed dividends are to be paid out of general reserve, the general reserve is to be reduced by such proposed dividends. Again as per Rules laid down for capital computation, where a part of the income, profits and gains of a company is not includible in its total income as computed under the Income-tax Act, the captial base is to be reduced proportionately.

(i) In computing the capital of an assessee company in which public are substantially interested for the purpose of levy of surtax for the assessment years 1976-77, the company had made no provision for declaration of dividends for the year ending 31 March 1975 even though the directors had proposed payment of dividends to the extent of Rs. 54,00,000. This was paid during the year ended 31 March 1976 by appropriating the amount from the general reserve. While completing the surtax assessment for the assessment year 1976-77 in March 1983, the assessing officer incorrectly adopted the amount so proposed for dividends (Rs. 54,00,000) included in the general reserve, for the purpose of computation of capital and statutory deduction. This resulted in excess computation of capital and consequent excess allowance of statutory deduction by Rs. 5,40,000 leading to undercharge of surtax of Rs. 2,56,500.

The Ministry of Finance have accepted the mistake (November 1984).

The assessment was checked by the internal audit party of the department; but the mistake was not detected by it.

(ii) The surtax assessment of a public limited company for the assessment year 1977-78 was completed by the Income-tax Officer in March 1983 on chargeable profit of Rs. 1,61,84,123. In the computation of capital, the entire balance of general reserve amounting to Rs. 3,38,35,002 had been included by the Income-tax Officer. A note appended to the balance sheet of the company as on 31 March 1971 indicated that dividend for the year 1975-76 amounting to Rs. 17,01,661 was paid out of the year's profits transferred to the general reserve. As the dividend liability stood included in the general reserve, the amount of Rs. 17,01,661 was to be reduced from the general reserve for the purpose of capital computation.

For the assessment year 1977-78, the net agricultural income of the assessee company amounted to Rs. 73,000 and the agricultural income being exempt from income-tax, the corresponding capital employed for agricultural income was also to be excluded in the capital computation for the purpose of surtax. The proportionate amount of capital employed for agricultural income for the assessment year 1977-78 worked out to Rs. 3,18,000 and this was required to be excluded in the computation of capital of the company.

As a result of these mistakes, the capital of the company was determined in excess by Rs. 20,19,661 involving short-levy of tax of Rs. 1,36,327 for the assessment year 1977-78.

The Ministry of Finance have accepted the mistake (November 1984).

(iii) The surtax assessment of a company was made in January 1983 for the assessment year 1973-74 on net chargeable profits of Rs. 19,04,145. While computing the chargeable profits of the company, although the assessing officer excluded the income by way of management compensation amounting to Rs. 11,53,797 from its total income, the amount of Rs. 6,66,317 on account of income-tax payable thereon was not deducted from the total income-tax payable by the company. Similarly a sum of Rs. 6,72,940 on account of income-tax on dividend income of Rs. 11,93,686 was deducted from the income-tax payable by the company as against the correct amount of tax of Rs. 6,89,353 owing to the mistake in the application of rate of surcharge. These two mistakes resulted in excess deduction of income-tax of Rs. 6,82,730.

In addition, the assessing officer added a sum of Rs. 19,00,000 on account of Dividend Equivalisation Reserve to the paid up capital in the capital computation of the company. The sum of Rs. 19,00,000 however included, a provision of Rs. 14,00,000 for the payment of dividend for the year 1971 which was also paid. Consequently an amount of Rs. 5,00, 000 only was to have been regarded as reserve for calculating the capital base. This led to incorrect computation of capital by Rs. 14,00,000 resulting in the under statement of chargeable profits by Rs. 8,22,730 involving short levy of surtax by Rs. 2,50,319.

The Ministry of Finance have accepted the mistake (October 1984).

(iv) The Central Board of Direct Taxes clarified in November 1974 that "debenture sinking fund" and "debenture redemption reserve" are only provisions and not reserve and as such, they are not to be included in computing the capital.

In computing the capital of an assessee company in August and October 1982 in respect of assessment years 1973-74, 1975-76 and 1976-77 the debenture redemption reserve of Rs. 31,68,743, Rs. 37,68,743 and Rs. 40,68,743 respectively were taken into account in computation of capital. The item being a provision and not a reserve, was not includible in computation of capital. The mistake resulted in excess-computation

of capital with consequent under-charge of surtax amounting to Rs. 2,75,157 for the assessment years 1973-74, 1975-76 and 1976-77.

While accepting the mistake for the assessment year 1975-76 and 1976-77, the Ministry of Finance have stated (January 1985) that action for the assessment year 1973-74 (involving revenue of Rs. 79,219) has become time barred.

(v) Under the Companies (Profits) Surtax Rules, 1964 for computing the capital of a company for the purpose of levy of surtax, the paid-up share capital of the company as on the first day of the previous year relevant to the assessment year is taken into account. The Surtax Act also lays down that any premium received in cash by the company on the issue of its shares standing to the credit of the share premium account is also regarded as forming part of its paid-up share capital.

In the surtax assessments of a company for the assessment years 1971-72 and 1972-73 made in February 1978, a sum of Rs. 1,90,76,428 representing share premium not received in cash but created by accounts adjustment was included in the capital base as on the first day of the relevant previous years. The mistake resulted in excess computation of capital by Rs. 1,90,76,428 leading to under-assessment of chargeable profits by Rs. 19,07,643 for each of the assessment year 1971-72 and 1972-73 involving total under-charge of surtax of Rs. 10,96,895 for both the assessment years.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

2.47 *Mistakes in the Computation of Chargeable Profits*

Under the Companies (Profits) Surtax Act, 1964, surtax is leviable on the amount by which the chargeable profits of a company exceeds the statutory deduction, which is an amount equal to ten per cent (fifteen per cent from April 1977) of the capital of the company or rupees two lakhs, whichever is greater. It is also stipulated that in cases where the relevant previous year is longer or shorter than a period of twelve months, the aforesaid ten per cent (fifteen per cent from April 1977) of capital or rupees two lakhs, as the case may be, should be increased or decreased proportionately.

(i) While finalising the surtax assessment of a company in March 1983 for the assessment year 1976-77 the assessing

officer assessed the statutory deduction at Rs. 7,32,34,075 being ten per cent of the capital computed at Rs. 73,23,40,749 and allowed deduction in determining the taxable profit. The records however, disclosed that the previous year relevant to the assessment year 1976-77 comprised of a period of nine months only (1 April 1975 to 31 December 1975) and hence the statutory deduction should have been reduced proportionately. Omission to do so, resulted in under-assessment of net chargeable profits by Rs. 1,83,08,519 with consequent under-charge of surtax of Rs. 43,52,835.

The Ministry of Finance have accepted the mistake (August 1984).

(ii) The total income assessed as reduced by income tax payable on the said income is the basis for computation of chargeable profits of a company for the purpose of levy of surtax. Income tax payable means the gross tax as reduced by any relief, rebate or deduction allowable under the Income tax Act or the relevant annual Finance Act.

A sum of Rs. 11,99,000 having been deposited by an assessed company under the Companies Deposits (Surcharge on Income-tax) Scheme 1976, the Surcharge payable by the company was less to the same extent. Hence the Income-tax to be deducted for computation of chargeable profits in the assessment year 1977-78 (surtax) would have to be reduced by Rs. 11,99,000. The omission led to under-statement of net chargeable profits by Rs. 11,99,000 with consequent short-levy of Surtax of Rs. 4,79,600 in the assessment year 1977-78.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(iii) In computing the chargeable profits of a public company for the assessment year 1977-78 completed in December 1982 for the purpose of levy of surtax a sum of Rs. 4,27,997 being the income-tax payable on donation and dividends was added to the Income-tax of Rs. 10,14,56,222 instead of subtracting the same from income-tax. Consequently income-tax liability of Rs. 10,18,84,219 was deducted from the total income instead of deducting the correct amount of income-tax of Rs. 10,10,28,225. The mistake resulted in short-computation of chargeable profits by Rs. 8,55,994 with consequent short-levy of surtax of Rs. 2,13,999.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(iv) In the surtax assessment of a company in which public were substantially interested made in September 1983 for the assessment year 1980-81, the department reduced the net chargeable profits by Rs. 2,96,126 being income-tax calculated on the amount of export markets development allowance of Rs. 5,12,733 allowed in the income-tax assessment. As the sum of Rs. 5,12,733 did not suffer any tax, the assessee company was not entitled to reduce the chargeable income by a sum of Rs. 2,96,126. The mistake resulted in under-assessment of net chargeable profits by Rs. 2,96,126 with consequent under-charge of surtax of Rs. 1,18,450 in the assessment year 1980-81.

The Ministry of Finance have accepted the mistake (September 1984).

(v) In the surtax assessment completed in February 1983 of a company for the assessment year 1977-78, the Income-tax Officer allowed a deduction of Rs. 61,55,705 on account of income-tax payable by the company in arriving at the chargeable profits. The said sum comprised of Rs. 58,62,575 on account of income-tax and Rs. 2,93,130 on account of surcharge thereon. In the income-tax assessment for the assessment year 1977-78, surcharge on income-tax was not levied in view of deposit of Rs. 15,00,000 (which was much more than Rs. 2,93,130 being the surcharge payable by the company) made by the assessee under the Companies Deposits (Surcharge on income-tax) Scheme 1976. As surcharge on income-tax was not payable by the company, the deduction to be allowed on account of income-tax payable should have been Rs. 58,62,575 only and not Rs. 61,55,705. The mistake resulted in under assessment of net chargeable profit by Rs. 2,93,130 with consequent short levy of surtax of Rs. 73,283 in the assessment year 1977-78.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

2.48 *Omission to make surtax assessments*

Under the Companies (Profits) Surtax Act, 1964, there is no statutory time limit for completion of surtax assessments. Pursuant to the recommendations of the Public Accounts Committee in para 6.7 of their 128th Report (Fifth Lok Sabha) the Central Board of Direct Taxes issued instructions in October

1974 that surtax assessment proceedings should be initiated along with the income-tax assessments. The Board further laid down that the surtax assessments should not be kept pending on the ground that the additions made in the income-tax assessment were disputed in appeal and the time lag between the date of completion of income-tax assessments and surtax assessments should not ordinarily, exceed a month unless there are special reasons justifying the delay.

The Public Acconuts Committee noticing the persistent delay or omission in completing the surtax assessments in spite of their earlier recommendation and Board's instructions pursuant thereto reiterated in paragraph 3.3 to 3.10 of their 85th Report (Seventh Lok Sabha) that a statutory time limit for completion of surtax assessments under the Surtax Act should be prescribed. The need for a statutory time limit for completion of surtax assessment was again stressed by the Public Accounts Committee in para 1.13 of their 193rd Report (7th Lok Sabha).

(i) In the case of nine companies assessed in seven Commissioners' charges, for the assessment years 1975-76 to 1980-81, although the income-tax assessments had been completed, the surtax assessments had not been made, the delay ranging from 7 months to 33 months (as on the date of audit). The omission resulted in non-levy of surtax of Rs. 36,10,356.

The Ministry of Finance have accepted the omission in seven cases. In one case, while not accepting the omission, the Ministry of Finance have stated (December 1984) that assessment proceedings will have to wait till orders for the succcession of the business of the assessee are passed. Reply in the remaining one case is awaited (December 1984).

(ii) In the case of six companies assessed in five different commissioners' charges for the assessment years 1975-76 to 1980-81, although provisional surtax assessment was made between March 1978 and April 1981, the final surtax assessments had not been made. The omission to do so resulted in short levy of surtax of Rs. 27,82,841 for the above assessment years.

The Ministry of Finance have accepted the omission in respect of five companies. Reply for the remaining case sent to the Ministry in September 1984 is awaited (December 1984).

2.49 *Incorrect grant of credit for payment of tax in the absence of Challans etc.*

An assessee company was assessed to surtax in June 1982 for the assessment year 1979-80 on a net chargeable profit of Rs. 61,63,348, and surtax payable thereon was determined at Rs. 22,57,936. A net demand of Rs. 26,405 was raised after giving a credit for Rs. 22,31,531 being the surtax paid by the assessee on provisional assessment made in November 1979. After adjusting refund of income-tax of Rs. 3,29,546 due to the assessment year 1979-80 against the demand of Rs. 22,31,531 a net demand of Rs. 19,01,985 was raised on completion of the provisional assessment of surtax in November 1979. On verification of credits, it was found that challans in support of payment of tax of Rs. 14,00,726 were only available in the assessment records of the assessee. No supporting challan in respect of the balance amount of Rs. 5,01,259 could be produced by the department. This resulted in incorrect grant of credit of Rs. 5,01,259 leading to under-charge of surtax by the same amount (Rs. 5,01,259) in the assessment year 1979-80.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

CHAPTER 3

INCOME-TAX

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

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

3.03 *Avoidable mistakes in the computation of tax*

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

A few cases are given in the following paragraphs :

(i) While computing income, the Income-tax Officer usually proceeds from the net profit shown in the profit and loss account as the starting point. He adds back the amount of inadmissible expenditure charged to the account.

In computing the income of a registered firm for the assessment year 1975-76 in July 1979, the assessing officer, instead of adding back certain inadmissible expenditure aggregating Rs. 4,04,003 to the net income, actually deducted the amount therefrom leading to excess carry forward of loss of Rs. 8,08,006 as unabsorbed development rebate. This excess carry forward resulted in short levy of tax of Rs. 4,71,208 in the hands of the firm and its partners in the assessment year 1976-77.

The Ministry of Finance have accepted the mistake (December, 1984).

(ii) In the income-tax return filed by an individual for the assessment year 1982-83, an income of Rs. 80,817 was returned, *inter alia* as income from own business chargeable to tax. However, while completing the regular assessment in December 1982, the assessing officer treated the income of Rs. 80,817 as loss of Rs. 80,817. The mistake resulted in excess computation and carry forward of loss of Rs. 1,51,469.

The Ministry of Finance have accepted the mistake (September 1984).

(iii) Under the provisions of the Income-tax Act, 1961, in computing the business income of an assessee a deduction is allowed by way of investment allowance at twenty-five per cent of the actual cost of the new machinery or plant installed and used for the purpose of business carried on by the assessee. Further, 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 holiday 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 in each of the following four immediately succeeding assessment years. Where the total income of an assessee (without making any deductions allowable as above) is 'nil' then the unabsorbed investment allowance|tax holiday relief is to be carried forward to the next assessment year for being set off against the assessable income for that year.

The assessments of a registered firm for the assessment years 1978-79 to 1980-81 were completed in January 1981 and November 1982 determining losses of Rs. 1,07,480, Rs. 1,33,790 and Rs. 1,88,790 respectively. The losses determined were allocated among the eight partners of the firm and were set off against the income under other heads of income in their individual assessments. The losses for the three assessment years had, however, been determined after adjusting investment allowance aggregating to Rs. 81.696 and allowing tax relief of Rs. 74.641 for new industrial undertakings. As the firm had no positive income to absorb the investment allowance or tax holiday relief in the respective years, the same should not have been included in business loss and allocated to the partners but carried forward in the firms' assessments for adjustment in subsequent years.

The mistake resulted in short-levy of tax aggregating to Rs. 85,555 in respect of the eight partners of the firm.

The Ministry of Finance have aceepted the mistake for the assessment year 1978-79 (November 1984). As regards the assessment years 1979-80 and 1980-81, a reply is awaited.

(iv) In the case of a firm, the assessment for the assessment year 1980-81 was completed in March 1983 treating it as an unregistered firm, as the assessee did not furnish the declaration in the prescribed form for continuation of registration. However, while levying tax, the rates of tax applicable to registered firm were incorrectly adopted. The incorrect adoption of rates resulted in short-levy of tax of Rs. 78,240.

The Ministry of Finance have accepted the mistake (September 1984).

(v) The claim of an assessee that it was a religious and charitable trust for the assessment years 1979-80 and 1980-81 (assessment completed in February 1983) was rejected by the assessing officer and hence tax was leviable on its income at the rate laid down in the Income-tax Act. However, the assessing officer levied tax on the income at the normal rates applicable to association of persons laid down in the Finance Acts. This resulted in short levy of tax of Rs. 65,440.

The Ministry of Finance have accepted the mistake (December 1984).

(vi) The original assessment of an individual assessee in respect of the assessment year 1964-65 which was completed in March 1969, was set aside (June 1971) by the Appellate Assistant Commissioner. While revising the assessment (September 1981), the Income-tax Officer did not include an income of Rs. 51,566 which had been originally assessed under 'other sources' and was not deleted by the Appellate Assistant Commissioner. This resulted in an under-assessment of income by Rs. 51,566 and consequential short-levy of tax of Rs. 43,842.

The Ministry of Finance have accepted the mistake (October 1984).

3.04 *Incorrect status adopted in assessments*

(i) Under the provisions of Income-tax Act, 1961, winnings from lotteries are subject to income-tax under the head "income from other sources". In the Report of the Comptroller and Auditor General for the year 1981-82, two cases of short levy of tax of Rs. 1,14,885 due to omission to make a single assessment

in the status of association of persons when a number of pe.sons had joined in a common purpose with the object of producing income from lotteries, were mentioned. The Ministry of Finance had stated in reply (December 1982) that the issue was not free from doubt and it could not be said with certainty whether the income in such a case would be assessed in the status of an individual or as association of persons|body of individuals.

A group of eight individuals assessed in a ward jointly won the first prize in a lottery conducted by a State Government and received a sum of Rs. 2,34,375 each as the share of the prize money in June 1981. They offered the amount as income in their individual assessments for the assessment year 1982-83 and the assessments were completed accordingly by the assessing officer between May 1982 and August 1982. As the eight individuals had joined in a common purpose with the object of producing income, the entire income was assessable in the status of the 'association of persons|body of individuals' instead of as individuals. This omission resulted in short-levy of tax of Rs. 3,25,379.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

(ii) 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 incidence of income-tax differs, according to the residential status of the tax-payer. An individual is treated as resident in a previous year if during that year he has resided in India for a total period of 182 days in all or more. For and upto the assessment year 1982-83 a person, maintaining a dwelling place in India for a period or periods amounting in all to 182 days or more and who has been in India for 30 days or more in that year is also treated as a resident. In order to become an "ordinarily resident", an individual should have been resident in nine out of ten preceding previous years and also been in India for a period or periods amounting in all 730 days or more during the seven years preceding that previous year, failing which he shall be treated as not ordinarily resident. For persons who are resident and ordinarily resident all incomes whether arising in India or outside India, are chargeable to tax.

Two assessees, husband and wife, who were employees of a church in United States of America, receiving salary in U.S. Dollars, were assessed as resident and ordinarily resident from

the assessment year 1969-70 onwards. In the assessment years 1979-80 and 1980-81, the assessments of which were completed in September 1981, their status was taken as not ordinarily resident and subjected to tax accordingly. The assessees left India on 5 December 1979 and returned on 8 December 1980. Thus, during the financial year 1979-80, the assessees were in India for more than 182 days and were, therefore, 'resident' during the assessment year 1980-81. Their income earned in and outside India was taxable as they served in India and had a dwelling house in India. Similarly, in the assessment year 1981-82, the assessees were to be treated as 'resident' as they had a dwelling house and also stayed in India for more than 30 days.

The amounts received outside India in the assessment years 1980-81 and 1981-82 amounting to U.S. $ 3046.50 and $ 6216 respectively by each of these assessees had, however, escaped assessment. Aggregate short-levy of tax on this account worked out to Rs. 50,341 for the two assessment years.

The Ministry of Finance have accepted the mistake (June 1984).

3.05 *Incorrect computation of 'salary' income*

(i) Under the provisions of the Income-tax Act, 1961, income received by an employee from an employer is chargeable under the head 'salary'. Salary includes profits in lieu of salary received from the employer. The Act also provides for standard deduction in respect of expenditure incidental to the employment of an assessee.

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

In para 3.05(i) (a) of the report of Comptroller & Auditor General of India for the year 1982-83 (Revenue Receipts, Volume II), cases of under assessment of salary income of employed medical practitioners, due to misclassification of part of the income as income from profession, instead of salary, were reported.

Similar cases of under-assessments noticed are given below :—

(a) An assessee employed as radiologist in a hospital received his remuneration in two parts, first part comprising fixed monthly

salary and the other being share of hospital profits. The assessee worked under the supervision and control of the hospital authorities. During the assessment years 1980-81 and 1981-82, the amount received as share of profit was assessed by the department as income from profession after allowing deduction for the expenses claimed whereas his fixed monthly salary income was charged to tax under the head 'salary'. As there was an apparent employer-employee relationship, the entire income arising from the employment in the hospital was assessable under the head 'salary' after allowing the standard deduction admissible under the Act. The incorrect classification of part of the income as income from profession, resulted in under-assessment of income of Rs. 1,14,801 and short-levy of tax of Rs. 55,053, for the assessment years 1980-81 and 1981-82.

(b) Three assessees employed in a hospital as medical officers, similarly received their remuneration in two parts viz., a monthly fixed salary and a share of hospital income, as per terms of the employment during the assessment years 1978-79 and 1979-80. Instead of the entire income being assessed as salary income, the share of hospital income was assessed as professional income after allowing deductions for expenses claimed.

This resulted in incorrect computation of salary income of Rs. 1,01,013 and short-levy of tax of Rs. 29,541.

The two cases were referred to the Ministry of Finance in April 1984; their reply is awaited (November 1984).

(c) In the case of another assessee an employee of a hospital, a standard deduction of Rs. 1,950 was allowed on a salary income of Rs. 7,800 in the assessment year 1980-81 completed in May 1982. The assessee had also received a sum of Rs. 1,40,724 as "profit in lieu of or in addition to salary" from the laboratory department of the hospital for indoor/outdoor visits and other works on which a further deduction of Rs. 69,356 was allowed towards expenses. As the whole income arising from the hospital, the assessee being only an employee of the hospital, was assessable under the head 'salary', no deduction for expenses other than the standard deduction was admissible in the computation of salary income.

The incorrect deductions, thus allowed resulted in under-assessment of income of Rs. 69,356 and consequent short-levy of tax of Rs. 49,935.

The paragraph was sent to the Ministry of Finance in July 1984; their reply is awaited (November 1984).

(ii) The Income-tax Rules, 1962 provide that the rate of exchange for the conversion of the value in rupee of any income accruing to an assessee in foreign currency shall be the telegraphic transfer buying rate adopted by the State Bank of India on the 'specified dates', when the income in question accrues or arises or is deemed to accrue or arise. In the case of salaried persons, the 'specified date' will be the last day of the month immediately preceding the month in which the salary is due.

Two assessees, husband and wife, who are employees of a church in United States of America, received their salary in U.S. Dollars. The salary certificates in both the cases were enclosed to the returns. The U.S. Dollars received were converted into Indian rupees at the rate of Rs. 7.50 per U.S. Dollar and taxable income was worked out accordingly every year.

In these cases, the amounts paid by the employer during the year were certified. In the absence of monthly particulars, adopting the prescribed rate of exchange on monthly average salary it was found in audit in April 1983 that income of Rs. 88,128 was under assessed in the two cases for the assessment years 1979-80 to 1982-83 leading to short levy of tax of Rs. 35,570.

The Ministry of Finance have accepted the mistake (June 1984).

3.06 *Incorrect computation of business income*

(i) Under the Income-tax Act, 1961, while computing the income of an assessee under the head 'business', the maximum allowable deduction on account of payment of salary to an employee during a year is Rs. 60,000 only. The term 'salary' has been defined to include wages, annuity or pension, gratuity, fees and commission or profits in lieu thereof.

During the previous years relevant to the four assessment years from 1977-78 to 1980-81, a registered firm paid sums of Rs. 94,625, Rs. 1,05,875, Rs. 95,696 and Rs. 1,19,693 respectively by way of salary and commission to its General Manager. While computing business income of the firm for the respective assessment years the deduction thereof was not restricted to the prescribed limit, resulting in under-assessment of business income by an aggregate sum of Rs. 1,75,889 for the four assessment years. The short-levy of tax was Rs. 1,41,011 including other minor mistakes in computation.

The Ministry of Finance have accepted the mistake (October 1984).

(ii) With effect from the assessment year 1972-73, any compensation or other payments due to or received by any person, for or in connection with the vesting in the Government, or in any corporation owned or controlled by the Government under any law for the time being in force, of the management of any property or business, shall be chargeable to income-tax under the head "profits and gains of business or profession".

Management of collieries run by a firm was taken over by the Government in January 1973 followed by nationalisation in May 1973. As a result, the firm had no business activities while payments of compensation were made to the partners of the firm directly in accordance with the respective profit-sharing ratios. An individual (a partner) had during the previous year relevant to the assessment year 1979-80 received a sum of Rs. 5,08,875 towards management compensation, profit for the managed period and interest receipts, which though, includible in the total income were not assessed to tax while completing the assessment in October 1982. This resulted in under assessment of income by Rs. 5,08,875 with consequent short-levy of tax of Rs. 3,45,658. The assessments of the firm and other partners were also required to be revised in the light of the observations made in audit.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

(iii) 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 purposes of the business or profession shall be allowed in computing the income chargeable under the head "profits and gains of business or profession".

An assessee's main business consisted of supplying stores, provisions, food stuffs etc., required on board of ships. On board, the materials were examined for their quality and weight. At this time, it was customary to give cash gifts to prevent unnecessary rejection of goods on flimsy grounds. The expenditure was not vouched. In the assessments of the firm for the assessment years 1978-79 to 1981-82 (assessments completed in September 1981), out of total expenditure of Rs. 2,66,186 the department considered 80 per cent of such expenditure as allowable wholly for the purpose of business and 20 per cent as entertainment expenditure resulting in disallowance of a sum of Rs. 32,136. In

the absence of any proof of payment considering the balance of Rs. 2,34,050 as admissible expenses was not in order. This resulted in short-levy of tax of Rs. 1,80,305 in the hands of the firm and its partners for the four assessment years.

The Ministry of Finance (January 1985) justified the assessment relying on a Madras High Court decision of 1980. Howeve., subsequently in 1982, it has been held by the Bombay High Court in another case that if the assessee failed to prove the payments made with names and addresses of the recipients, the payments were not deductible.

(iv) Under the Income-tax Act, 1961 where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee, and subsequently during any previous year the assessee has obtained, whether in cash or in any other manner whatsoever, any amount in respect of such loss or expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained by him or the value of benefit accuring to him, is deemed to be profits and gains of business or profession chargeable to income-tax as the income of that previous year. It has been judicially held in March 1980 that the amount received by the assessee as refund of sales-tax in its character as a trader constituted trading receipt and was includible in computing the total income (128 ITR 43).

An assessee-firm deriving income from purchase and sale of agricultural implements had made provision for payment of sales tax amounting to Rs. 2,29,434 by debit to the profit and loss accounts for the accounting years relevant to the assessment years 1975-76 to 1978-79. The liability was allowed as deduction in the assessments for these years. As the assessee's contention, that no sales-tax was payable on agricultural implements, was ultimately accepted by the State Government, the provision toward sales tax was written back by the assessee in the previous year relevant to the assessment year 1982-83. While making assessment for the assessment year 1982-83 in January 1983 the amount of Rs. 2,29,434 was incorrectly excluded by the Income-tax Officer from the computation of income. This resulted in short-levy of tax of Rs. 1,35,410.

The Ministry of Finance have stated (December 1984) that on cessation of liability to sales tax, sum of Rs. 92,113 was brought to tax in the assessment year 1978-79 and the balance of Rs. 1,40,848 which accrued during the assessment year 1980-81 remained to be taxed.

(v) Under the provisions of the Income-tax Act, income chargeable under the head 'profits and gains of business' shall be computed in accordance with the method of accounting regularly employed by the assessee. Any expenditure laid out or expended wholly and exclusively for the purposes of business is allowed as deduction in computing the business income provided it is an ascertained liability.

(a) In the Income-tax assessments of a registered firm, provision made in its accounts for payment of sales tax was being regularly disallowed upto the assessment year 1976-77 on the ground that no sales tax was payable on the finished steel products as the raw materials had already suffered tax as steel materials. Similar provisions made in the accounts for the assessment years 1979-80 and 1980-81 were also disallowed. As the provision was not an ascertained liability, the amounts of Rs. 1,03,194 and Rs. 2,65,257 claimed on this account for the assessment years 1977-78 and 1978-79 should also have been similarly disallowed. This was not done and the erroneous deduction resulted in underassessment of income of Rs. 3,68,451 leading to total short-levy of tax of Rs. 2,61,094 for the two assessment years in the hands of the firm and its partners.

The Ministry of Finance have accepted the mistake (December 1984).

(b) The assessment of a co-operative society for the assessment year 1980-81 was completed in October 1982 on a taxable income of Rs. 6,36,540 after allowing deduction on account of reserves for damaged stock, provisions for bonus and gratuity aggregating to Rs. 2,62,344, as claimed by the assessee. In the assessments for the earlier years, similar provisions and reserves were added back and the actual payments made during the relevant years were only allowed. Accordingly, the expenditure allowable on the basis of actual payments made under the aforesaid three categories for the assessment year 1980-81 worked out to Rs. 36,868 as against Rs. 2,62,344 allowed in the assessment. The incorrect allowance resulted in underassessment of income by Rs. 2,25,476 leading to short-levy of tax of Rs. 1,08,230.

The Ministry of Finance have accepted the mistake (December 1984) except that part relating to provision for damaged goods for which a final reply is due.

(c) In the case of a registered firm, the original assessment for the assessment year 1965-66, completed in February 1970,

was set aside by Appellate Assistant Commissioner for examination of the position of fresh introduction of hundi loans, amounting to Rs. 11.52 lakhs during the period 1957 to 1964. The department determined the hundi loans as bogus and this was agreed to by the assessee. A fresh assessment was completed in October 1982.

However, on a sum of Rs. 7,99,500 shown as outstanding balance of hundi loans as on 31 December 1964, interest amounting to Rs. 80,606 claimed by the assessee was not disallowed while completing the assessment for the assessment year 1965-66 in October 1982. As the loan itself was held to be bogus, the interest on the same was also not allowable. The mistake resulted in underassessment of total income by Rs. 80,606 with consequent undercharge of tax of Rs. 51,195 in the hands of the firm and its three partners.

The Ministry of Finance have accepted the mistake (November 1984).

(d) A registered firm engaged in the business of tea production incurred expenditure on replantation and replacement of tea bushes to the extent of Rs. 1,04,879 and Rs. 1,66,898 in the previous years relevant to the assessment years 1977-78 and 1978-79 respectively. Besides, the assessee firm incurred further expenditure on extension of tea garden to the extent of Rs. 22,639 during the previous year relevant to the assessment year 1977-78 and on land and plantation to the extent of Rs. 11,313 during the previous year relevant to the assessment year 1978-79.

The four items of expenditure amounting to Rs. 3,05,729 incurred by the assessee were of a capital nature but the department allowed them as revenue expenditure in computing the taxable income in the relevant assessment years. This resulted in underassessment of income by Rs. 1,22,290 being 40 per cent of Rs. 3,05,729 during the two assessment years with consequent short-levy of tax aggregating Rs. 50,442 including interest leviable for non-compliance of the provisions of the Act in the hands of the firm. The tax effect in the hands of the partners has to be ascertained.

The Ministry of Finance have accepted the mistake (September 1984).

(e) The assessment of a Co-operative Sugar Mill for the assessment year 1979-80 was completed in February 1982 at a

loss of Rs. 32,55,530. During the previous year relevant to the assessment year, the assessee had received subsidy of Rs. 22 lakhs as compensation for loss incurred on the running of the mill during that year. Instead of treating the subsidy as income of the assessee, the assessing officer treated it as capital receipt and excluded it while computing the taxable income. This resulted in under-assessment of income leading to excess carry forward of loss by Rs. 22 lakhs. Further, due to incorrect adoption of the written-down value of plant and machinery, depreciation was allowed in excess by Rs. 1,55,431 and similar amount was allowed to be carried forward for set off against income of future years.

The Ministry of Finance have accepted the mistake for failure to tax the Government subsidy. Reply in respect of adoption of incorrect written down value is awaited (October 1984).

(vi) Under the Income-tax Act, 1961, agricultural income is exempt from tax but the same is to be taken into account for determining the rates of tax applicable to total income of a particular year under the provisions of a Finance Act. Income from the sale of tea grown and manufactured by an assessee is treated as arising partly from business and partly from agriculture. The Income-tax Rules, 1962 prescribe that only forty per cent of such income derived from the sale of tea grown and manufactured by a seller in India should be deemed to be income liable to Income-tax and the balance is agricultural income within the meaning of the Act. No further expenses, if any, incurred by the assessee would be admissible as deduction.

An assessee individual was engaged solely in cultivation and sale of green tea leaves. Such income, being agricultural in nature, was exempt from tax. While completing the assessment for the assessment years 1981-82 and 1982-83 in December 1981 and November 1982 respectively, the department while excluding the income, however, allowed 40 per cent of the garden expenses amounting to Rs. 43,664 and Rs. 1,75,016 respectively for the two assessment years as deduction while computing the other income. The deduction was not admissible as the entire income from growing of tea and sale of tea leaves was exempted from tax. The incorrect deduction led to aggregate short levy of tax of Rs. 1,29,149.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

(vii) Under the provisions of the Income-tax Act, 1961, as operative during the period April 1979 to March 1981, where the aggregate expenditure on advertisement, publicity and sales promotion in India exceeds half a per cent of the turn-over, 15 per cent of the adjusted expenditure thereof has to be disallowed. This provision which applied to all categories of tax payers carrying on business or profession was not applicable to cases where the aggregate amount of such expenditure does not exceed Rs. 40,000. The expression "adjusted expenditure" meant the aggregate expenditure incurred on publicity, advertisement and sales promotion as reduced by the expenditure not allowable as business expenditure under the general head and further reduced by expenditure specifically stated in the Act as admissible.

The gross-turn-over of an assessee firm for the previous year relevant to the assessment year 1979-80 (assessment completed in January 1982) amounted to Rs. 138.57 lakhs and the expenditure on account of sales promotion as claimed by the assessee amounted to Rs. 5,36,147. As the expenditure exceeded the limit of half a per cent of total turn-over i.e. Rs. 69,286, fifteen per cent of Rs. 5,36,147 i.e., Rs. 80,422 had to be disallowed.

The omission to disallow resulted in short-computation of income of Rs. 80,422 involving short levy of tax of Rs. 55,982 in the hands of the firms and its partners.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

3.07 *Incorrect allowance for contribution to scientific research*

Under the provisions of the Income-tax Act, any sum paid to a scientific research association, university, college or other institution to be used for scientific research is allowed as deduction in the computation of business income of an assessee provided that such association, university, college or institution is approved by the prescribed authority, viz., the Secretary, Department of Science & Technology (Government of India). On approval by the prescribed authority, the Ministry of Finance, Department of Revenue issues a notification conveying the approval of the prescribed authority for the purposes of the provisions of the Income-tax Act laying down *inter alia* the period for which the approval could be effective, maintenance of separate accounts, rendition of annual accounts to the prescribed authority and to

the Commissioner of Income-tax concerned. The Income-tax Act also provides for a weighted deduction in respect of contribution paid to such a research institution if the contribution is used for scientific research under a programme approved by the prescribed authority, viz., the Secretary, Department of Science and Technology. The weighted deduction is equal to one and one-third times the sums so paid.

In the previous years relevant to the assessment years 1979-80 and 1980-81 a Hindu undivided family contributed a sum of Rs. 12,63,386 towards research fees to a private limited company of which the 'karta' of a Hindu undivided family was the Managing Director. The Department of Science & Technology (Government of India) recognized the private company in July 1978 as a research and development laboratory for the purposes and facilities provided in the import policy (1978-79) for import of goods required for research and development. While according approval, it was made clear that the recognition was not meant for tax exemptions concessions, development rebate etc., under the Income-tax Act for which the private company should take up the matter separately with the tax authorities. While completing the assessments for the two assessment years in March 1982|March 1983, the department allowed a deduction of Rs. 16,84,515 accepting the claim of the assessee for weighted deduction on the contribution made. The assessee was not entitled for the entire deduction of Rs. 16,84,515 (which included weighted deduction) for the following reasons :

(1) The approval given by the Department of Science and Technology in July 1978 was intended only for the import of goods required for research and development.

(2) The private limited company was not approved as a scientific research association by the prescribed authority for the purposes of the provisions of the Income-tax Act relating to scientific research.

(3) The Ministry of Finance (Department of Revenue) had not issued any notification conveying the approval of the prescribed authority.

(4) A specific programme of scientific research was not also got approved by the prescribed authority.

The incorrect deduction allowed resulted in underassessment of income by Rs. 16,84,515 leading to short levy of tax

of Rs. 10.76 lakhs. While accepting the mistake relating to weighted deduction, the Ministry of Finance have stated (November 1984) that the fact that the private company which received the contribution was not recognised as a scientific research association was noticed by the department and remedial action is underway.

3.08 *Mistakes in grant of export markets development allowance*

Under the Income-tax Act, 1961, domestic companies and resident non-corporate assessees engaged in the business of export of goods outside India or of providing services or facilities outside India were entitled upto March 1983 to export markets development allowance equal to the actual amount of qualifying expenditure plus an extra amount of one-third thereof as weighted deduction.

(i) Assortment charge paid to sort out, cut and polish diamonds, before getting the goods ready for export, being in the nature of commission is only a trading activity in India and as such does not qualify for the weighted deduction.

In the case of two assessee registered firms, weighted deduction was allowed on assortment charges during the assessment years 1973-74, 1977-78, 1978-79 and 1979-80 for the first firm and during the assesment year 1978-79 for the second firm. The incorrect allowance resulted in aggregate underassessment of income of Rs. 4,01,815 involving short levy of tax of Rs. 2,99,892 in the hands of the two firms and their partners.

The Ministry of Finance have accepted the mistake (August 1984).

(ii) From 1 April 1978 the weighted deduction would be admissible subject to the conditions that the assessee was either a small scale exporter or a holder of an Export House Certificate; or was engaged in the business of provision of technical know-how or rendering of services in connection with that business, to persons outside India.

In the case of an assessee, weighted deduction of Rs. 2,12,275 was allowed, in the assessment year 1979-80 on expenditure incurred on development of export market, even though none of the above mentioned conditions was fulfilled. The mistake resulted in underassessment of income by Rs. 2,12,275 and short-levy of tax of Rs. 1,46,474.

The Ministry of Finance have accepted the mistake (August 1984).

3.09 *Mistakes in valuation of closing stock*

In order to determine the profits from business, an assessee who maintains accounts on mercantile basis, may choose to value the closing stock of his business every year, at cost price or market price whichever is lower. It has been judicially held in September 1980 that the privilege of valuing closing stock in a consistent manner would be available only to a continuing business and that it cannot be adopted where a business comes to an end, when stock on hand should be valued at the market price in order to determine the true profits of the business on the date of closure of business (102 ITR 622).

The Ministry of Law also had confirmed this position in August 1982 and March 1984. The Central Board of Direct Taxes have not, however, issued any instructions in this regard for the guidance of assessing officers.

(i) A proprietary business in tyres, tubes and other automobile parts of a Hindu undivided family was taken over with effect from the 1 April 1981 by a firm in which the members of the Hindu undivided family became partners along with a stranger. The assessment records of the Hindu undivided family for the assessment year 1981-82 (assessment completed in December 1982) revealed that the closing stock held by the proprietary business as on 31 March 1981 had been valued at cost price instead of at the market price for computing the business income of Hindu undivided family. With the taking over of the business by the firm from April 1981, the business of the Hindu undivided family came to a close, as such the closing stock held at the time of closure of its business required valuation at the market price to ascertain the true profits of the business run by it upto that date. The omission resulted in under-computation of income by Rs. 4,81,278 for the assessment year 1981-82 with consequential short levy of tax of Rs. 3,17,207.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

(ii) In the previous year relevant to the assessment year 1980-81, a registered firm was dissolved due to the death of one of its partners. The remaining partners formed a new partnership taking in some more partners and took over the business as a going concern and continued it. The accounts of the

old firm were closed upto the date of dissolution by valuing the closing stock of textiles at cost price of Rs. 12,35,543. While completing the assessment in March 1983 to the best of his judgment, the assessing officer accepted the value of the closing stock instead of adopting the market price to determine the true profits of the business on the date of dissolution. The omission to do so resulted in under assessment of income by Rs. 1,53,207 (based on the gross profit ratio of 12.4 per cent in the absence of full details) with consequent total short-levy of tax of Rs. 98,564 in the hands of the firm and its partners.

The Ministry of Finance have accepted the mistake (January 1985).

(iii) Two partnership firms valued their closing stocks, every year, at cost price (which was less than the market price). One of these firms was dissolved on 31 October 1979 and the other on 5 October 1980. Their business was taken over by the existing partners who commenced their own separate proprietary business. In the assessment of one firm for the year 1980-81 finalised in October 1981 and that of the other firm for the year 1982-83 finalised in February 1983, the business income was determined adopting the value of closing stock at cost price as Rs. 5,57,755 and Rs. 12,26,360 as on 31 October 1979 and 5 October 1980 respectively instead of at the market value of the closing stock which worked out to Rs. 6,13,530 and Rs. 13,09,660 (based on the gross profits returned by them).

The omission resulted in underassessment of income of the concerns by Rs. 1,39,075 with consequent short-levy of tax of Rs. 94,621 in the hands of the firms and its partners.

The Ministry of Finance have accepted the mistake (January 1985).

3.10 *Incorrect allowance of depreciation*

(i) The Income-tax Act, 1961, provides for grant of depreciation allowance on buildings, plant and machinery owned by an assessee and used for the purpose of business, in computing the income from business. The Rules prescribed in this regard provide for specific rates of depreciation ranging from 15 per cent to 100 per cent for certain items of plant and machinery and a general rate of 10 per cent (15 per cent from the assessment year 1984-85) in respect of plant and machinery for which no special rate has been prescribed.

(a) According to the depreciation schedule in the Income-tax Rules, depreciation is admissible on "building contractors machinery" at the rate of 15 per cent of its actual cost. Depreciation at the rate of 30 per cent is admissible on "earthmoving machinery employed in heavy construction work such as dams, tunnels, canal etc.".

An assessee firm undertaking contract works and engaged in the construction of dry docks claimed for the assessment years 1977-78 to 1979-80 depreciation on pile driving equipment used for construction of dry docks at 30 per cent, classifying the item as "earth moving machinery". The internal audit party of the department had raised an objection for the earlier assessment years that only a rate of 15 per cent would be admissible, treating the item as 'building contractors machinery'. The Commissioner of Income-tax decided in his note of September 1980 that the rate of depreciation admissible would be 30 per cent as claimed by the assessee. The assessments were accordingly completed between March 1981 and April 1982 allowing the higher rate. The decision of the Commissioner of Income-tax was based on the observations of the Chief Engineer (Valuation Cell) that there are basic similarities between the functions of a pile driving equipment and earth moving machinery in that both types of equipments deal with earth viz., work to be done in the earth or ground.

The report of the Chief Engineer cited by the Commissioner of Income-tax specifically mentions that 'a pile driving equipment is an equipment for driving piles into the ground in order to transfer heavy building loads to the subsoil at suitable depth' while the term earth moving machinery is generally applied to equipments which are used for excavating and/or transporting earth like bulldozers, scrappers, excavators, dumpers, shovels etc. Admittedly, the two equipments are different and are used for different purposes. As such the pile-driving equipments are not classifiable as 'earth moving machinery' entitling higher rate of depreciation. The incorrect grant of depreciation at the rate of 30 per cent instead of 15 per cent resulted in excess allowance of depreciation of Rs. 35,96,951 leading to short levy of tax of Rs. 27,34,910 for the three assessment years 1977-78 to 1979-80.

The Ministry of Finance have accepted the mistake (December 1984).

(b) In respect of rigs used in mineral oil concerns only the special rate of depreciation of 30 per cent is applicable which

implies that the general rate of 10 per cent would be applicable in respect of rigs used by all other concerns.

Two registered firms engaged in the busines of drilling bore-wells for tapping drinking water claimed in the revised returns filed for the assessment years 1980-81 and 1981-82, depreciation in respect of rigs and compressors at 30 per cent. While completing the assessments in November 1982, the assessing officer allowed the claim of the assessee. As the rigs were used only in drilling borewells and not in mineral oil concerns, the correct rate of depreciation allowable was 10 per cent and not 30 per cent. The mistake resulted in excess allowance of depreciation to the extent of Rs. 7,88,984 and a total short levy of tax of Rs. 2,06,960 in the hands of the firms and its partners for the two assessment years.

The Ministry of Finance have accepted the mistake (November 1984).

(c) Similarly in another case of a registered firm engaged in the business of sinking bore-wells for water, for the assessment years 1978-79 to 1980-81, depreciation allowance on rigs and compressors was incorrectly allowed at the rate of 30 per cent applicable to mineral oil concerns, instead of at the general rate of 10 per cent. The mistake resulted in aggregate short-levy of tax of Rs. 85,797 in the hands of the firm and its two partners.

The Ministry of Finance have accepted the mistake (September 1984).

(d) A registered firm did not claim depreciation on new machinery valued at Rs. 9,02,876 on the ground that the machinery had not been put to use during the previous year relevant to the assessment year 1977-78. However, while finalising the assessment in December 1979 the assessing officer, allowed depreciation at 10 per cent on this machinery. The mistake was also not noticed by him when the assessment was revised in September 1981 to give effect to an appellate order. The incorrect allowance of Rs. 90,287 led to short-computation of business income to the extent of Rs. 72,230 involving a short-levy of tax of Rs. 52,587 in the hands of the firm and its partners.

The Ministry of Finance have accepted the mistake (September 1984).

(e) With effect from 1 April 1981, depreciation at special rate of thirty per cent of written down value is allowable on

certain renewable energy devices which *inter alia* include "any special devices including electric generators and pumps running on wind energy".

In computing total income of an assessee firm, depreciation on generator running on diesel was allowed at the higher rate of thirty per cent and additional depreciation and extra shift allowance was calculated accordingly. Since the generator running on diesel was not a renewable energy device, depreciation thereof was allowable at the general rate of ten per cent only. Owing to erroneous application of rates, depreciation including additional and extra depreciation was allowed in excess by Rs. 89,073 leading to undercharge of tax of Rs. 46,833 in the hands of firm and its three out of four partners. The assessment records of the fourth partner were not produced to audit.

The Ministry of Finance have accepted the mistake (December 1984).

(ii) Under the Income-tax Act, 1961, depreciation is allowed at the prescribed rates on the actual cost or the written down value of the assets as the case may be. In determining the written down value of assets for purposes of allowance of depreciation for any assessment year both normal depreciation and extra shift allowance allowed are required to be taken into account.

(a) In the case of a co-operative sugar factory, although extra shift allowance of Rs. 5,80,606 and Rs. 5,56,348 was allowed on the plant and machinery used by it for the assessment years 1978-79 and 1979-80 respectively, it was not taken into account in determining the written down value of the assets in the succeeding assessment years 1979-80 and 1980-81, assessments of which were completed in February 1983. The mistake resulted in overstatement of the written down value of the assets and consequent excess allowance of depreciation and extra shift allowance of an aggregate sum of Rs. 2,78,795 thereby leading to excess carry forward of depreciation allowance by Rs. 2,78,795 for the assessment year 1980-81.

The Ministry of Finance have accepted the mistake (September 1984).

(b) In the case of another co-operative sugar factory, extra shift allowance, similarly allowed on the plant and machinery used in business, for the assessment years 1977-78, 1978-79 and 1979-80 was not deducted in determining the written down value of the assets for the succeeding assessment years viz.,

1978-79, 1979-80 and 1980-81, assessments for which were completed in September 1981, March 1982 and March 1983 respectively. The assessment for assessment year 1979-80 done on best judgment basis had been subsequently cancelled and reopened; no fresh assessment had been made. Thus, depreciation for the two assessment years 1978-79 and 1980-81 allowed on un.educed amount of written down value resulted in excess allowance of depreciation of Rs. 2,82,918 and Rs. 12,22,332 respectively leading to total excess carry forward of loss of Rs. 15,05,250.

The Ministry of Finance have accepted the mistake (November 1984).

(iii) Under the Income-tax Rules, 1962, depreciation on motor buses, motor lorries and motor taxis is admissible at 40 per cent if used in the business of running them on hire; otherwise the admissible rate is at 30 per cent.

An assessee firm engaged in quarrying and sale of stones deployed their vehicles on hire for short durations of casual nature in the previous year relevant to the assessment year 1981-82. The assessee was allowed depreciation at the higher rate of forty per cent in the assessment completed in March 1982. As the assessee was not engaged in the business of plying vehicles on hire and as the vehicles were primarily used for the assesseee's business of quarrying and sale of stones. The assessee was entitled to depreciation at the lower rate of 30 per cent only. The incorrect allowance of depreciation resulted in underassessment of income by Rs. 94,756 with a short-levy of tax of Rs. 48,204 including a minor mistake in granting depreciation on firm's car used for non-business purposes, in the hands of the firm and its partners.

A similar mistake in two other cases for the assessment years 1981-82 and 1982-83 had resulted in short levy of tax of Rs. 60,664.

The Ministry of Finance have accepted the mistakes (October and November 1984).

(iv) In addition to the normal depreciation allowance, the Income-tax Rules 1962 provide that in respect of machinery or plant, an extra shift depreciation allowance upto a maximum of one half of the normal allowance is allowed where a concern

claims and establishes that it has worked double shift and upto a maximum of the normal allowance where it claims and establishes that it has worked triple shift. In this connection the preamble to para 2.24 may also be referred to.

In the case of a registered firm extra shift allowance of Rs. 1,13,453 was allowed by the assessing officer for the assessment year 1980-81 in the assessment completed in June 1982. Though the assessee firm had installed new machinery in the second quarter of the previous year and also on the last day of the previous year, it had claimed extra shift allowance for the full year. As the machinery had not worked for the entire period, the extra shift allowance should have been restricted in proportion to the number of days, the machinery had actually worked in extra shifts. This was not done. This resulted in excess allowance of depreciation amounting to Rs. 91,271 leading to short levy of tax of Rs. 73,080 in the hands of the firm and its partners.

The Ministry of Finance have stated in reply (December 1984) that the assessment was in accordance with their instructions of March 1973, which, however, is contrary to judicial pronouncements in the matter. It may be added that on a similar case falling in the same jurisdiction reported in the Comptroller and Auditor General's Report (Volume II). Direct Taxes for the year 1982-83, the Ministry accepted the mistake (December 1982) in view of the judicial decision of September 1981.

3.11 *Incorrect grant of investment allowance*

Under the provisions of the Income-tax Act, 1961 as applicable for the assessment year 1977-78, while computing the business income of an assessee, a deduction is allowed by way of investment allowance at twenty-five per cent of the actual cost of machinery or plant installed in any industrial undertaking after 31 March 1976 for the purposes of business of construction, manufacture or production, of any one or more of the articles or things specified in the list in Ninth Schedule to the Act.

(i) In the assessment of a co-operative society engaged in the production of sugar and wine, for the assessment year 1977-78, completed in January 1981, a deduction by way of investment allowance was allowed for a sum of Rs. 1,14,741 calculated at the prescribed rate on the cost of new plant and machinery brought to use in its distillery unit during the relevant previous year. Since the product of distillery unit of the

society was not covered by any of the items specified in the Ninth Scheduled of the Act, investment allowance of Rs. 1,14,741 was not admissible to the society.

Further in respect of the sugar unit, investment allowance amounting to Rs. 4,70,893 allowed on the cost of new plant and machinery of Rs. 18,83,573 was also not admissible as the plant and machinery was installed prior to 1 April 1976. However initial depreciation amounting to Rs. 3,76,714 at twenty per cent of the cost of said plant and machinery could be allowed. Thus, the investment allowance amounting to Rs. 94,179 (4,70,893 minus 3,76,714) was incorrectly allowed in respect of sugar unit.

The investment allowance of Rs. 2,08,920 incorrectly allowed in both the units resulted in short levy of tax of Rs. 91,925.

The assessment was checked by the internal audit of the department but the mistakes escaped their notice.

The Ministry of Finance have accepted the mistake (January 1985).

(ii) The deduction towards investment allowance is admissible in the year of installation of the plant and machinery or if they were put to use in the immediately succeeding year, in the year in which they were put to use. However, the actual deduction on this account in any assessment year is to be allowed only to the extent sufficient to reduce the total income to nil and the balance, if any, is carried forward to the subsequent assessment year for adjustment. Further, investment allowance can be allowed only if the assessee furnishes the prescribed particulars in respect of the plant and machinery installed and put to use and debits an amount equal to 75 per cent of the investment allowable to the profit and loss account of the previous year in which the deduction is allowed and credits it to a reserve account called "Investment Allowance Reserve Account". While there is no obligation to create the reserve in the year of installation of plant and machinery or in the subsequent year when they are put to use, in case the assessee has incurred loss during the relevant previous year, the reserve is to be created in the year in which there is positive income and to the extent of income, in case the profit is not adequate to absorb the full amount of reserve to be created.

The Income-tax assessment of a registered firm for the assessment year 1981-82 was finalised in March 1983 assessing the net income at Rs. 1,38,611 after allowing deduction of Rs. 2,08,026 towards investment allowance which included investment allowance of Rs. 1,76,340 in respect of plant and machinery installed and put to use during the earlier assessment years 1978-79 to 1980-81 (though certain plant and machinery were installed during the previous year relevant to assessment year 1977-78, they were put to use during the subsequent year). The assessment records disclosed that the assessee had not furnished the prescribed particulars in respect of the plant and machinery during the respective assessment years, and claimed investment allowance thereon. Though the returned and assessed income of the assessment years 1978-79 to 1980-81 was positive, the assessee had not created the investment allowance reserve by debiting 75 per cent of the admissible investment allowance to the profit and loss account or in the absence of sufficient profit, to the extent of available profit. There was also no evidence to show that the claim for investment allowance was admitted by the Income-tax Officer. It was only in the accounts of the previous year relevant to the assessment year 1981-82 that the assessee created the necessary reserve for all the earlier years and claimed the investment allowance which was allowed by the assessing officer. This was not in order because, such a claim could have been made and admitted under the provisions of the Act only in the year of installation of plant and machinery or in the subsequent year if they were first put to use during that year. The incorrect procedure adopted by the assessee and allowed by the assessing officer resulted in excess allowance of investment allowance of Rs. 1,76,340 with consequent under charge of tax of Rs. 77,591 in the hands of the firm and its partners including interest on excess advance tax paid.

The Ministry of Finance have accepted the mistake (November 1984).

(iii) An assessee is entitled to investment allowance on the actual cost of a ship or plant and machinery owned by him and wholly used for the purposes of his business. The ship must be a new one acquired after 31 March 1976 and the assessee must have been engaged in the business of operation of ships. If it is plant and machinery, it should be new and installed after 31 March 1976 in an industrial undertaking. No claim for investment allowance is admissible for replacement of old plant and machinery by a new one in a ship.

While assessing the income of a registered firm engaged in running steamer services, for the assessment year 1981-82 (assessment completed in December 1982), investment allowance of Rs. 74,171 was allowed on four numbers of new gear boxes fitted into the steamers. As investment allowance is admissible on acquisition of new ships|steamer and as the assessee was also not engaged in any industrial undertaking, the replacement of old gear boxes with the new ones did not entitle the firm to any investment allowance. The incorrect grant of investment allowance of Rs. 74,171 resulted in under assessment of income of the same amount with under charge of tax of Rs. 54,206, in the hands of the firm and its partners.

The Ministry of Finance have accepted the mistake (January 1985).

(iv) The Act provides for withdrawal of relief already allowed if the assets are sold or otherwise transferred to any person at any time before the expiry of eight years from the end of the previous year in which the assets were acquired or installed. The right to investment allowance is lost even if the transfer of an asset results from a business re-organisation or expansion e.g., when a sole proprietary firm is formed into a partnership.

In the assessment of an individual carrying on a proprietary business, the department had allowed investment allowance of Rs. 40,930 and Rs. 75,413 for the assessment years 1978-79 and 1979-80 respectively. During the previous year relevant to the assessment year 1980-81, the individual converted his proprietary business into a partnership with another person. As the conversion amounted to a "transfer" under the Act and as the transfer had taken place within a period of eight years from the end of the previous year in which the asset was acquired, the investment allowance of Rs. 1,16,343 allowed for the two assessment years was required to be withdrawn. The omission to withdraw the allowance resulted in short-levy of tax aggregating Rs. 68,350.

The Ministry of Finance have accepted the mistake (August 1984).

3.12 *Omission to levy capital gains tax*

Under the provisions of the Income-tax Act, 1961, any profits or gain arising from the transfer of a capital asset are chargeable to income-tax the head 'capital gains'.

(i) It has been judicially held, in April 1981 as also reiterated by Central Board of Direct Taxes in June 1982, that, when a person brings his assets into a firm in which he is a partner, as his capital contribution, it amounts to a transfer of capital assets as the person losses his exclusive right over the said assets which became the property of the firm, his sole title in respect of the assets being limited to his share in money representing the value of the property of the firm as a whole.

(a) Six persons (one HUF and five individuals belonging to a family) transferred the equity shares in companies held by them to a firm in which they became partners, in the previous year relevant to the assessment year 1980-81, at market value. The cost of acquisition of the assets as per books was Rs. 4,05,438 and the consideration for which they were transferred to the firm was Rs. 11,26,866. While completing the assessment in September 1980, the department did not bring the resultant capital gains of Rs. 7,21,428 to tax thereby leading to short-levy of tax of Rs. 4,39,035.

While accepting the omission to levy capital gains tax in three cases, the Ministry of Finance have contended (January 1985) that the other three persons were dealers in shares.

(b) An assessee entered into partnership and transferred in July 1976, his 6,240 equity shares at a value of Rs. 9,04,480 for which he was given credit in the capital account. The cost of acquisition of the shares in the hands of the assessee was only Rs. 5,12,400. Though the transfer of the shares to the firm as share capital is transfer within the meaning of the Act and attracted levy of capital gains tax, no tax was levied by the department at the time of assessment for the assessment year 1977-78 completed in June 1979. The omission led to underassessment of income by Rs. 2,72,622 and consequent short-levy of tax by Rs. 2,08,718 including interest for short payment of advance tax.

The paragraph was sent to the Ministry of Finance in August 1984 ; their reply is awaited (November 1984).

(c) The Income-tax return of a partnership firm for the assessment year 1980-81 indicated that the firm was formed with effect from 26 August 1979 with two partners who transferred their ancestral land valued at Rs. 12,000 as on 7 April 1964, as capital contribution to the firm carrying on the business of construction and sale of flats etc. The land was valued at Rs. 4,00,000 and the capital accounts of the assessees were

credited with Rs. 2,00,000 each. Taking the value of the capital asset at Rs. 6,000 each as on 1 January 1964, the income by way of capital gains of Rs. 1,41,750 arising to each of the partners was not brought to tax in the assessment year 1980-81 leading to non-levy of tax aggregating Rs. 1,78,470.

The Ministry of Finance have accepted the mistake (September 1984).

(d) Three individuals transferred their immovable property consisting of salt pans to a firm in which they became partners along with another individual, in the previous year relevant to the assessment year 1978-79 assessed between May 1979 and December 1980 and credited a sum of Rs. 2.75 lakhs towards their capital contribution. The cost of acquisition of the salt pans admeasuring 225.48 acres was Rs. 1.02.859 as on 1 January 1964. The transfer involved a capital gain of Rs. 1,72,141 which was not subjected to tax. The omission resulted in under assessment of income by Rs. 1,17,855 and consequent non-levy of tax of Rs. 67,508 in the hands of the three individuals.

The Ministry of Finance have accepted the mistake (January 1985).

(e) An assessee introduced during the previous year relevant to the assessment year 1978-79, 50 per cent of his share in a salt pan, as his capital contribution in a registered firm at a value of Rs. 2,40,000 against the book value of Rs. 97,644. The income by way of capital gains of Rs. 1,42,356, was not brought to assessment, resulting in non-levy of tax of Rs. 69,760.

The Ministry of Finance have accepted the mistake (July 1984).

(ii) Capital gains are computed by deducting from the full value of the consideration received, the cost of the acquisition of the capital asset and the cost of any improvement thereto. Where the capital asset became the property of an assessee or the previous owner in case where the assessee got the property by succession or by inheritance, from a date prior to 1 January 1954 the cost of acquisition is deemed to be the cost for which the previous owner of the property acquired it or at the option of the assessee, at its fair market value as on 1 January 1954. From the assessment year 1978-79, however, in respect of an asset in possession of an assessee from a date prior to 1 January 1964, the cost of acquisition could be taken as its fair market value as on that date.

(a) Two sisters inherited a property, a film theatre in 1975 after the death of their three brothers. The income arising from the asset was being assessed in the hands of the two sisters upto the assessment year 1979-80 in the status of 'body of individuals' and the share of each was included in the individual assessments along with other income. During the previous year relevant to the assessment year 1980-81, the two sisters entered into a partnerhip with two major sons of one of the sisters and all the four constituted a firm. The two sisters brought into the firm, the film theatre, machinery and equipment etc., as their capital in the new firm and Rs. 12,24,000 was credited to their capital accounts towards the capital contribution. While making the assessment of the firm in March 1983, the Income-tax Officer did not consider levy of tax on the capital gains arising from the transfer of the film theatre and other assets owned by the two sisters to the firm. The asset viz., the film theatre came into existence prior to 1964 and for purposes of arriving at capital gains the value of the asset as on 1 January 1964 had to be substituted. In the absence of records establishing the value of the asset as on 1 January 1964 if the values of the asset is taken as Rs. 3,06,000, i.e., 25 per cent of the value credited in the books of the firm in the previous year relevant to the assessment year 1980-81, the capital gains chargeable to tax would be Rs. 9,18,000. In consequence, capital gains tax of about Rs. 4,83,005 in the hands of the two sisters escaped levy. The exact amount of short levy has to be arrived at after determining the fair market value as on 1 January 1964.

The Ministry of Finance have accepted the mistake (December 1984).

(b) Two assessees having ownership in equal proportions of a land with a building transferred the two portions of it viz., 2400 sq. metres and 772 sq. metres during the previous years relevant to the assessment years 1976-77 (assessed in December 1980) and 1979-80 (assessed in March 1981) respectively to a firm in which they were partners, in consideration of which they were given credit of Rs. 3 lakhs and Rs. 1.50 lakhs respectively in their capital accounts in the years of transfer. The capital gain arising out of the transfer worked out to Rs. 4,99,500 for the assessment year 1976-77 (Rs. 6,00,000 minus assumed value as on 1 January 1954 at Rs. 1,00,500) and Rs. 2,08,904 for the assessment year 1979-80 (Rs. 3,00,000 minus Rs. 91,096 the cost of acquisition adopted based on the sale rate of a portion of the same asset sold

in 1974, in the absence of information of fair market value as on 1 January 1964) which was not subjected to tax. The omission resulted in aggregate short-levy of tax of Rs. 3,03,437.

The Ministry of Finance have accepted the mistake (October 1984).

(c) The Income-tax law allows certain reductions while computing taxable long-term capital gains arising in a year. If there be any short-term capital loss in the same year, the short-term capital loss should be set off against the long-term capital gains and the further deductions admissible are to be calculated on the net long-term capital gains.

In the assessment of an individual for the assessment year 1982-83 (completed in December 1982) capital gain arising out of a sale of house property was determined as Rs. 5,31,110. As the property was acquired before 1 January 1964, the assessee had the option to adopt the fair market value as on 1 January 1964 as the cost of acquisition and accordingly showed a sum of Rs. 4,80,960 as cost of acquisition in the income-tax return. The assessee arrived at the figure of cost of acquisition on the basis of a departmental valuation report drawn up to show the value as on 31 March 1967. Eighty per cent of such value was taken by the assessee as the fair market value on 1 January 1964. However, in the wealth-tax assessment for the assessment year 1964-65 (the valuation date being 14 April 1964), the value assessed and accepted by the assessee was only Rs. 1,31,220 for the property. Hence, the fair market value of the property as on 1 January 1964 cannot exceed the sum of Rs. 1,31,220.

The incorrect adoption of the fair market value of the property as on 1 January 1964 together with the omission to set off a short-term capital loss against the long-term capital gain on the sale of property, accounted for underassessment of income of Rs. 2,78,320 leading to short-levy of tax of Rs. 1,83,691.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(d) An assessee individual sold land and buildings during the previous year relevant to the assessment year 1976-77 at Rs. 1,75,000 which had been acquired in November 1968 for a consideration of Rs. 13,000. While working out the capital

gains in the assessment for the assessment year 1976-77 completed in January 1983, however, the Income-tax Officer adopted the cost of acquisition of the assets at the value certified by the Chief Engineer, P.W.D., based on the rates of 1973 (viz. Rs. 1,42,846) as returned by the assessee instead of Rs. 13,000. The mistake led to underassessment of income by Rs. 85,596 involving short levy of tax of Rs. 61,765.

The Ministry of Finance have accepted the mistake (January 1985).

(iii) With effect from the assessment year 1978-79 onwards, the Income-tax Act, 1961, provides for exemption from income-tax, the capital gains arising from the transfer of any long-term capital asset, if the full value of the consideration received or accruing as a result of the transfer is invested or deposited by the assessee in specified assets within a period of six months after the date of the transfer.

(a) Where, however, the long term capital gain accrues|or arises after 28 February 1979 but before 1 March 1983, the benefit of exemption shall be available only if the net consideration is invested in 7 year National Rural Development Bonds carrying interest at 7-1|2 per cent per annum. In case a part of the consideration only is so invested or deposited, a proportionate part of the capital gains shall be so exempted. These provisions were extended from the assessment year 1978-79, through Finance Act, 1978 to cover cases, where enhanced compensation was awarded by a court|tribunal in respect of assets acquired compulsorily under any law and accordingly the department was empowered to issue a revised order within the specified time limit to bring to charge in the year of the transfer, the quantum of compensation which does not enjoy exemption.

In the assessment records for the assessment year 1980-81 completed in February 1982 it was observed that an assessee had claimed that the capital gains arising on account of additional compensation of Rs. 4,64,900 received in July 1979 in respect of lands acquired by Municipal Authorities in 1974 was exempt from tax on the ground that an amount of Rs. 4,30,000 was invested in the 7-year National Rural Development Bonds within the time allowed. This position was accepted by the department and accordingly the amount was not brought to tax. The assessment to be amended to bring the additional compensation received in July 1979 to tax was, however, for the assess-

ment year 1975-76, the original capital gains having been brought to tax in that year. It was noticed in Audit that the original compensation in regard to the same assets had been received in July 1974 and April 1977 and as such the enhanced compensation of Rs. 4,64,900 received by the assessee in July 1979 was exigible to tax in the assessment year 1975-76. The provisions in the Act, relating to exemption of capital gains (including additional compensation), when invested in specified securities, took effect only from the assessment year 1978-79; as such the grant of exemption in respect of enhanced compensation was not in order. This incorrect grant of exemption resulted in short-demand of tax of Rs. 2,46,918.

The Ministry of Finance have accepted the mistake (September 1984).

(b) In respect of fixed deposits made after 27 April 1978, the assessee should furnish alongwith the deposit, a declaration to the bank that he would not take any loan or advance on the security of the deposit and to the Income-tax Officer alongwith the return a copy of the declaration attested by the bank.

During the period relevant to the assessment year 1979-80, an assessee became a partner in a partnership firm and introduced a plot of land valued at Rs. 1,80,000 in August 1978 as his capital contribution. The land was purchased by the assessee at a cost of Rs. 7,000 in February 1960. The assessee made a capital gain of Rs. 1,73,000 and claimed exemption thereto on the basis of investment of Rs. 1,55,000 in fixed deposits and Rs. 25,000 in Unit Trust of India in February 1979. The Income-tax Officer allowed the exemption in the assessment made in September 1979. The exemption allowed was not admissible for the following reasons.

(1) The assessee did not secure any consideration for the transfer so as to enable him to invest the proceeds thereof in the prescribed securities. He merely contributed his capital in kind. Investment of other funds belonging to the assessee would not entitle him to the tax relief.

(2) Further, the said investment was made after the expiry of six months from the date of transfer. The assessee did not produce a copy of declaration attested by the bank as stipulated in the Act.

The incorrect exemption resulted in short levy of tax of Rs. 69,097.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

3.13 *Mistakes in computation of trust income.*

(i) Under the provisions of the Income-tax Act, 1961, where the individual shares of the persons on whose behalf or for whose behalf such income is receivable by a trust, are indeterminate or unknown, tax is chargeable on such income in the hands of the trust at the maximum marginal rate.

(a) A lady created two trusts by two deeds of settlement in November 1975. As per terms of these trust deeds, the income was notionally divided into two parts called trust fund No. 1 and trust fund No. 2. The trust deeds in both the cases further provided that the amount credited to each of the two funds was to be retained by the trustees jointly for the benefit of the three beneficiaries mentioned in each of the deeds. Besides, on the date of distribution of the corpus i.e., 31 December 2000 or such earlier date as may be decided by the trustees, the corpus of the trust fund is to be distributed amongst the beneficiaries and their wives and children at the absolute discretion of the trustees.

The assessments of these trusts for the assessment years 1979-80 to 1981-82 in one case and for the assessment year 1979-80 in the other case were completed between October 1980 and November 1982 in the same ward (assessment completed in a summary manner except for the assessment year 1981-82) indicating the distribution of taxable income as shares of fund No. 1 and fund No. 2 as beneficiaries without levying any tax on the trusts. The trust fund No. 1 and No. 2 were, however, charged to tax at the normal rates applicable to association of persons. As the beneficiaries of the two trusts were the persons whose names appeared in the trust deed and not the two trust funds and as the shares of the beneficiaries were indeterminate, the trusts should have been treated as discretionary and tax levied at maximum marginal rate in the hands of the two trusts. The omission led to aggregate short-levy of tax of Rs. 1,60,897 for the three assessment years after giving credit to the tax in the hands of the two trust funds.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

(b) In respect of the assessment year 1980-81 (assessment completed in March 1983) an assessee trust was assessed on income of Rs. 1,54,790. In the assessment order, the trust was shown as 'specified' and the shares were stated to be 'determinate'. Accordingly no tax was payable by the trust as the income of the trust was divided amongst the beneficiaries as per the trust deed. As per the trust deed, however, the trustees can, in their absolute discretion, decide the share of each of the beneficiaries in the entire income of the trust fund different from the shares stipulated between the beneficiaries. This power of the trustees included power to exclude anyone or more beneficiary or to give the entire income or only a part thereof to anyone of the beneficiaries. Since the trust deed empowered the trustees to vary the distribution of the income to the beneficiaries, the trust should be treated as a discretionary trust and assessed accordingly at the higher marginal rate of 72 per cent as applicable to the assessment year 1980-81. The omission led to short levy of tax of Rs. 1,54,439 in the hands of the trust, after adjusting the tax already levied in the hands of the beneficiaries.

The Ministry of Finance have accepted the mistake (September 1984).

(c) From the assessment year 1980-81, a private discretionary trust in which the shares of the beneficiaries are indeterminate or unknown, is liable to tax at the maximum marginal rate of income-tax including surcharge, as applicable to the highest slab of income in the case of an association of persons as specified in the Finance Act of the relevant year.

In the case of a family trust created by a deed in April 1981, the shares of beneficiaries in the trust were not specified and as such, the trust was chargeable to tax at the maximum marginal rate of 66 per cent for the assessment year 1982-83. The assessment was, however, made in January 1983 treating the trust as not assessable and the income of Rs. 61,600 of the trust was apportioned in equal shares of Rs. 12,320 among the five beneficiaries. The omission to assess the trust itself on its income of Rs. 61,600 for the assessment year 1982-83 led to short-levy of tax of Rs. 40,656.

The Ministry of Finance have accepted the mistake (October 1984).

(ii) Under the provisions of the Income-tax Act, 1961, income derived from property held under trust wholly for charitable or religious purposes is exempt from tax to the extent to which such income is applied for such purposes in India. The various deductions admissible while computing income from business are not admissible while computing surplus income of a charitable trust.

In computing the taxable surplus of an assessee trust in respect of the assessment year 1978-79 (in November 1981) depreciation of Rs. 38,501 relating to the immovable property of the trust was allowed as deduction which was not admissible in the case of trust deriving income from property. The mistake resulted in underassessment of taxable income by Rs. 38,501 and consequent short-levy of tax by Rs. 32,867 including interest for late filing of return.

The Ministry of Finance have accepted the mistake (August 1984).

(iii) Any income of an assessee by way of dividends attributable to profits and gains from new industrial undertakings, or ship or hotel business in certain specified cases is deductible from the gross total income. The charitable trusts, the income of which is chargeable to tax are not entitled to this exemption.

In computing the taxable surplus of a charitable trust for the assessment year 1979-80 in August 1981, deduction of such income to the extent of Rs. 77,928 was allowed by the department. The incorrect deduction on this account resulted in under-assessment of income of Rs. 77,928 and short levy of tax of Rs. 31,120.

The paragraph was sent to the Ministry of Finance in April 1984; their reply is awaited (November 1984).

3.14 *Mistakes in assessments of firm and partners*

Under the provisions of the Income-tax Act, where at the time of completion of the assessment of a partner of a firm, the assessment of the firm has not been completed and the final share income of the partner is not known, the assessment of the partner may be completed by taking his share income from the firm on a provisional basis. In such cases, the assessments of the partners are to be revised subsequently to include the final share income, when the assessment of the firm is completed. For this purpose the Income-tax Officers are required, under instructions (February 1959) of the Central Board of Direct

Taxes, and reiterated in March 1973 to maintain a 'register of cases of provisional share income', so that timely action may be taken to revise the partners' assessments. The instructions of the Board issued in July 1976 provide that the cases of partners of a firm should, as far as possible, be assessed in the same ward|circle where the firm is assessed as to reduce the rectification work to the minimum.

(a) A registered firm with its three partners and another registered firm with one of its partners were assessed in the same ward. The assessments of the four persons for the assessment years 1979-80 to 1981-82 were completed between March 1980 and January 1982 adopting their share income from the firm provisionally as the firms assessments had not been completed by then. The assessments of the first firm for the three assessment years and of the second firm for two assessment years 1980-81 and 1981-82 were subsequently completed in January 1982 and May 1982. In the provisional share income register maintained by the department, no entries were made indicating the adoption of provisional share income for certain assessment years, and for the other assessment years though it was indicated in the register as having been revised, actually the assessments were not revised at all. The omission to revise the assessments involved an aggregate short levy of tax of Rs. 2,00,582.

The Ministry of Finance have accepted the mistake (November 1984).

(b) For the assessment years 1977-78 and 1979-80 the assessments of an individual having 40 per cent share income in a registered firm, were finalised in December 1979, and October 1980 adopting share income from the firm at Rs. 1,09,665 and Rs. 97,539 respectively, as returned by the assessee. The correct share income from the firm for these years as per the firm's assessments finalised in July 1980 and in August 1982 was Rs. 1,58,337 for the assessment year 1977-78 and Rs. 2,06,930 for the assessment year 1979-80. However, the assessments of the partner for both the years were not revised resulting in under-assessment of income of Rs. 48,672 and Rs. 1,09,391 with aggregate short levy of tax of Rs. 1,07,601 for the two assessment years.

The Ministry of Finance have accepted the mistake (August 1984).

(c) In the case of an individual who was a partner in two firms (one of them assessed in the same ward), the Income-tax Officer completed the assessments for the assessment years 1978-79 and 1979-80 in August 1980 and June 1981 respectively, adopting the share income from the firms provisionally. In the case of the firm assessed in the same ward, the assessments for the assessment years 1978-79 and 1979-80 had been completed in March 1981 and March 1982 respectively and the correct share income of the individual had been determined as Rs. 35,313 and Rs. 1,24,438 respectively against the provisional share income of Rs. 34,275 and Rs. 36,263 respectively assessed earlier. In the case of the other firm, particulars of the correct share income of the individual for the assessment year 1978-79, (showing the correct share income as Rs. 6,354 against the provisional share income of Rs. 4,001 adopted), had been received by the Income-tax Officer and was on record. The assessing authorities, did not watch the revision of the assessments through the register of cases of provisional share income and revise the assessments. The omission resulted in an aggregate under charge of income-tax of Rs. 55,907.

The Ministry of Finance have accepted the mistake (November, 1984.

(d) The Income-tax assessment of a partner in two registered firms for the assessment year 1977-78 was completed in March 1980, provisionally adopting her share income from one of the firms as Rs. 54,800. Though the assessee herself on finalisation of the assessment of the said firm intimated to the Income-tax Officer in February 1981 that her share income from the firm concerned should be Rs. 1,34,443, no action was taken to revise the assessment. The omission resulted in short-levy of tax of Rs. 52,151.

The Ministry of Finance have accepted the mistake (October 1984).

(e) In the case of two individuals, assessed in the same ward, provisional share incomes were adopted in the assessments for the assessment years 1977-78 and 1978-79 completed between February 1980 and February 1981. The assessments of the firm in which the assessees were partners for these two years were completed in July 1981 and September 1981 in a different ward. The assessments of the individuals were not, however, revised adopting the correct share income. In the prescribed register

entry was made in respect of one individual only for the assessment year 1978-79. The omission to adopt the correct share income involved an aggregate short levy of tax of Rs. 96,190.

The Ministry of Finance have accepted the omission (November 1984.

3.15 *Mistakes in assessment of firms*

The excise rules of a state, under which licences were issued for sale of liquor, prohibited the transfer of the licence by the licencee|licencees (in cases they were held jointly) to any other person or include|exclude any partner, other than those endorsed in the licence, except with the prior permission of the licensing authority. It has been judicially held in October 1978 by the Punjab and Haryana High Court that the partnerships formed in violation of the rules are not legal and such partnerships are not entitled to registration under the Income-tax Act. Departmental instructions were also issued to the same effect, in June 1981. If partnership firms are constituted in violation of extent rules, they are to be assessed to tax as unregistered firms. In another decision pronounced by the Andhra Pradesh High Court in April 1983, it has, however, been held that merely because prior permission of State licensing authority had not been obtained, it cannot be an illegal partnership and contract between the partners being valid. the firm is entitled to registration under the Act. The department has, however, moved special leave appeal in this case to the Supreme Court (March 1984) against this decision.

(a) In four income-tax wards, the department incorrectly granted registration to twenty one partnership firms engaged in arrack trade though the licences were issued to some of the partners in their individual capacity. The transfer and formation of firms without prior permission of the licence issuing authority, rendered the firms ineligible for registration and eventually resulted in short demand of tax of Rs. 5,15,370 for the assessment years 1979-80 to 1982-83.

The paragraph was sent to the Ministry of Finance in August/ September 1984; their reply is awaited (November 1984).

(b) After securing the liquor licences, five assessees in another ward joined hands with other persons and formed partnership firms without permission of the licence issuing authority. Since it was in violation of the State Excise Act and Rules, the

firms were not eligible for registration. The incorrect grant of registration for the assessment years 1979-80 and 1981-82 re-resulted in short levy of tax of Rs. 1,68,453.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

3.16 *Omission to include income of spouse/minor child etc.*

(i) Under the provision of the Income-tax Act, 1961 where a person and his wife both are partners in the same firm, the income from the firm of both the persons should be clubbed together and assessed in the hands of that spouse whose income (excluding that from the firm) is higher. In this connection, the Central Board of Direct Taxes have also issued clarificatory instructions in August 1975 that clubbing provisions would apply even where a karta of a Hindu undivided family and his wife are partners in the same firm.

(a) An individual in his capacity as "karta" of his Hindu undivided family, became, in the previous year relevant to the assessment year 1977-78, a partner in a firm, in which his wife was also a partner. As the quantum of the husband's income was higher than that of the wife, the income of the wife from the firm was to be clubbed with the individual income of the husband for purposes of levy of tax in his hands. This was, however, not done and as a result, tax aggregating Rs. 71,870 was short levied in the assessment years 1977-78 to 1982-83.

The Ministry of Finance have accepted the mistake (September 1984).

(b) In computing the income of an individual for the assessment years 1978-79 to 1981-82, share income of his wife from a registered firm of which both husband and wife were partners was clubbed with his income in spite of the fact that the income of wife was higher. This erroneous clubbing of share income of wife with that of her husband led to undercharge of tax of Rs. 67,451.

The Ministry of Finance have accepted the mistake (January 1985).

(ii) Under the provisions of the Income-tax Act, 1961, income arising from assets transferred by an individual directly or indirectly to his son's wife and his son's minor children, on or after 1 June 1973, otherwise than for adequate consideration,

has to be included in the income of the transferor and subjected to tax. It has been judicially held (May 1978) that the words "directly or indirectly" would cover cases of transfer through the medium of trusts also.

An individual and his wife jointly created a trust in January 1981 by settling Rs. 10,000 each for the benefit of their son, son's wife and son's seven minor children. The trust carried on business. Under the trust deed, 90 per cent of the income arising to the trust was to go to the benefit of the son's wife and son's minor children in specified proportions, the balance 10 per cent going to the son. For the assessment years 1981-82 and 1982-83 the department, instead of including 90 per cent of the income arising to the trust from the business carried on by it in the respective total incomes of the grand-parents, assessed the shares allocated to the beneficiaries to tax as their individual incomes. This resulted in a short-demand of tax of Rs. 1,37,131 in the hands of the grand-parents for the assessment years 1981-82 and 1982-83.

The Ministry of Finance have accepted the mistake (October 1984).

3.17 *Income escaping assessment*

(i) Under the provisions of the Income-tax Act, 1961, any advance or loan made by a closely-held company to a share-holder who has a substantial interest in it, is deemed to be dividend in the hands of the share-holder, to the extent to which the company possesses accumulated profits.

A closely-held private company advanced to an individual who had a substantial interest in it, sums amounting to Rs. 5,61,313 and Rs. 3,07,084 during the assessment years 1979-80 and 1980-81 respectively. As the company had accumulated profits which were more than the amounts advanced to the share-holder, the advances of Rs. 5,61,313 and Rs. 3,07,084 should have been treated as deemed dividends and subjected to tax in the hands of the share-holder. The omission to do so resulted in short-levy of tax of Rs. 6,08,406 in the assessment years 1979-80 and 1980-81.

While accepting the escapment of income, the Ministry of Finance have stated (November 1984) that time for remedial action for the assessment year 1979-80 had already expired and that for the assessment year 1980-81, the action was being taken. Had timely action been taken, when the omission was pointed

out in audit (August 1983) the loss of revenue of Rs. 3,87,385 for the assessment year 1979-80 could have been avoided.

(ii) Under the provisions of the Income tax Act 1961, the total income in any previous year of a person who is a non-resident includes all income from whatever source received or deemed to be received in India in such a year by or on behalf of such a person.

Two assessees were assessed in a ward as non-residents for the assessment year 1979-80 excluding their foreign dividend income of Rs. 1,29,474 and Rs. 1,27,533 in the computation of total income chargeable to tax in India. The assessees had authorised the Chartered Bank of Hongkong to receive the foreign income on their behalf at Hongkong and remit the same to India for credit in their account. During the period from 1 April 1978 to 31 March 1979, their accounts with the Bombay branch of Chartered Bank were credited with total sum of Rs. 1,29,474 and Rs. 1,27,533 representing the foreign dividends paid to them by foreign companies at Hongkong.

The Chartered Bank of Hongkong acted merely as an agent in collecting their dividends at Hongkong and passing them on to India for credit to their accounts in India. The income was, therefore, taxable as it is deemed to be received in India on behalf of the assessees. The incorrect exclusion of the dividend income from total income resulted in short levy of tax of Rs.2,35,435 including interest leviable for failure to comply with the provisions of the Act regarding payment of advance tax.

The paragraph was sent to the Ministry of Finance in July 1984; their reply is awaited (November 1984).

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

(a) In the case of an assessee individual, the assessment for the assessment year 1980-81 was made on a total income of Rs. 2,74,723 in December 1982. The assessed income did not include (i) his share income from a firm and (ii) income from a brandy shop, to the extent of Rs. 35,831 and Rs. 1,85,000 respectively. The income from these two sources for the assessment year 1980-81 was, however, returned as income by another firm in which the assessee was a partner. While finalising the

assessment of this firm for the assessment year 1980-81 in December 1982 the Income-tax Officer held that the income referred to above belonged to the assessee partner in his individual capacity and not to the firm returning the income and accordingly excluded it in the computation of the business income of the firm. However, the assessment of the individual which was finalised five days earlier was not amended. Accordingly the income from these two sources amounting to Rs. 2,20,831 remained unassessed in the hands of the assessee, even at the time of audit in January 1984. The undercharge of tax on this account worked out to Rs. 1,58,999.

The Ministry of Finance have accepted the omission (December 1984).

(b) In the case of a co-operative society other than a consumer co-operative society, engaged in activities not specified under the provisions of the Act, total income beyond Rs. 20,000 as attributable to such activities, is liable to income-tax .

An assessee co-operative society, set up in 1973 was engaged in various activities for the benefit of its members and beneficiaries. It derived income from bidding fishing rights and interest from deposits in District Co-operative Bank. This income had not been subjected to tax for the assessment year 1978-79. Neither the assessee filed any return of income nor did the department call for any return. The omission resulted in non-levy of tax Rs. 57,286.

The paragraph was forwarded to the Ministry of Finance in May 1984; their reply is awaited (November 1984).

(iv) Capital gains arising from the transfer of a capital asset is deemed to be the income of the previous year in which the transfer takes place and taxed accordingly.

(a) It has been judicially held in 1972 that where interest is awarded on enhanced compensation as a result of compulsory acquisition of any asset, the liability to pay such interest would arise when the compensation due to the assessee had not been paid in each of the relevant years from the date of dispossession. The method of accounting being mercantile, accrual of interest would have to be spread over the years between the date of acquisition and the date of actual payment and the amount of interest income would be taxed in a particular assessment year which accrued in that year.

The lands of an assessee had been acquired by the Government in the year 1953-54. As per the award of May 1973 of the Land Acquisition Officer, the assessee received the compensation amount of Rs. 5,44,917 in March 1975. The Land Acquisition Officer in his orders of July 1976, directed payment of interest at 4 per cent on the amount of compensation from 1 March 1954 (the date of acquiring the lands) to 7 March 1975 (the date of payment of compensation). The interest amount of Rs. 3,69,151 accrued to the assessee but the same was not brought to tax in any year. The omission resulted in the under assessment of interest income of Rs. 1,17,120 for the years from 1970-71 to 1975-76 involving short levy of tax Rs. 1,07,786. Rectification for the assessment years 1954-55 to 1969-70 had become time-barred.

The Ministry of Finance have accepted the mistake (January 1985).

(b) The wealth-tax assessment records of an assessee individual for the assessment year 1979-80 revealed that in the relevant previous year the assessee had sold his two properties for consideration of Rs. 1,60,000 and Rs. 1,80,000. Taking into account, the cost of acquisition including cost of additions to the properties at Rs. 96,837 and Rs. 1,03,787 respectively, the aggregate long term capital gains arising to the assessee worked out to Rs. 1,39,376.

Neither any return of income had been filed for the assessment year 1979-80, nor did the department initiate assessment proceedings against the assessee. Income of Rs. 1,39,380 involving tax of Rs. 45,618 thus escaped assessment.

The Ministry of Finance have accepted the mistake (September 1984).

(v) The Income-tax Act, 1961, provides that where any Central Act enacts that the income-tax shall be charged for any assessment year at any rate or rates, income-tax at the rates so specified is to be charged in respect of the total income of the previous year of every person. The term 'person' as defined in the Act includes, *inter alia* 'body of individuals'. The scope of the term 'body of individuals' as judicially interpreted includes a combination of individuals who have a unity of interest but who are not actuated by a common design, and one or more of whose members produce or help to produce income for the benefit of all.

An individual, who was a partner in a registered firm having one third share, died intestate in December 1977. The partnership deed provided that, in the event of death of any of the partners, one heir of the deceased partner, as unanimously decided by all the heirs, can be admitted as a partner in the firm. Accordingly, the widow of the deceased on behalf of herself, three minor sons and a major son entered into agreement in January 1978 and the widow was authorised to become the partner of the firm representing all the heirs. The agreement also stated that the share of interest in the firm belonged to all the members and that the widow must pay to the other members one fifth of the share of profits and retain only one-fifth share for herself. In accordance with this agreement, the widow of the deceased was taken as a partner of the firm in the partnership deed executed in January 1978 and became entitled to one third share of profit of the firm. During the previous years relevant to the assessment years 1979-80 to 1981-82 finalised between February 1980 and November 1981, the widow received Rs. 67,907, Rs. 94,105 and Rs. 1,14,904 respectively as the share of profit allocated to her while finalising the firm's assessment. The widow had distributed the income received from the firm amongst the heirs and returned only one fifth of the share of income in her income-tax returns. The income-tax assessments were also finalised accordingly as it was decided that each member was to be taxed in respect of his share of income separately. Since the heirs of the deceased had executed an agreement authorising one of them viz., the widow of the deceased, to enter into partnership on behalf of all of them, they would constitute a 'body of individuals' and the entire share of income from the registered firm was taxable in the hands of the 'body of individuals'. Omission to do so resulted in non-assessment of income in the hands of 'body of individuals' for the assessment years 1979-80 to 1981-82 and consequential short levy of tax aggregating Rs. 90,347 (Appr.).

On this being pointed out in audit (August 1982) the department contended (March 1983) that one fifth share of income was correctly taxed in the hands of each heir, in view of the decision of Supreme Court in a case in March 1960 and the judgment of the Gujarat High Court in a case in November 1975. It was brought to the notice of the department (September 1983) that these judgments pertained to cases where there was partition of Hindu undivided family and the question decided was about taxation of income after such a partition and the facts did not fit in with the particulars of the case under audit objec-

tion in which an agreement was entered into in January 1978 by all the surviving members authorising one to become a partner in the firm.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(vi) An assessee firm, executing civil works contracts followed the method of offering to tax the value of gross bills received during the previous year. The recoveries made from the bills towards security deposits were taken as 'assets' in the balance sheet. When the security deposit was released by the contracting agency on fulfilment of the contract, it was shown as reduction of the 'asset' in the balance sheet.

In the assessment year 1981-82 (assessment completed in October 1982), the firm received Rs. 1,23,763 towards release of security deposit recovered from the bills in the earlier years. Instead of exhibiting this amount as reduction of the relevant asset in the balance sheet in which it already stood included, the assessee deducted the same from the gross bills of Rs. 7,19,998 of the assessment year 1981-82 and exhibited the balance of Rs. 5,96,235 in the profit and loss account. This resulted in short computation of income by Rs. 1,23,763 and consequent short levy of tax of Rs. 60,545 in the hands of the firm and its partners.

The paragraph was sent to the Ministry of Finance in July 1984; their reply is awaited (November 1984).

(vii) The income-tax assessment of a cooperative society engaged in purchase and sale of goods for the assessment year 1978-79 was finalised in February 1981 determining the income at a loss of Rs. 4,50,000. A comparison of the balances appearing in the balance sheet at the close of the relevant previous year (30 June 1977) with those appearing in the earlier year (30 June 1976) disclosed an increase in the balances of the reserve to an extent of Rs. 1,51,568. As these increases could not be linked with any of the items of expenditure debited to the profit and loss account and also no details were on record showing the sources from which the balances under the reserves increased, the factual position was brought to the notice of the department to ascertain whether the increase in the reserve represented undisclosed income of the assessee. After investigation, the department reported that the increase was on account of capital gain on sale of shares credited to the reserve fund. Further as per the details, collected by the department, the society had sold

the shares for a consideration of Rs. 1,58,378 against purchase price of Rs. 19,000 only, thereby deriving capital gain of Rs. 1,39,378. According to the department, the net capital gain (after assessing deduction) of Rs. 80,628 would reduce the loss assessed earlier. It was brought to the notice of the department that under the relevant provisions of the Act, the full capital gain amounting to Rs. 1,39,378 was to be adjusted against the loss assessed earlier thereby reducing the loss carried forward to the same extent. The potential tax effect amounted to Rs. 59,509.

The Ministry of Finance have accepted the mistake (December 1984).

(viii) Under the Income-tax Act, 1961, 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. The income computed for assessment of tax should also include amounts due though not actually received during that year. The Central Board of Direct Taxes had in their instruments of November 1974 directed that proper liasion should be maintained with sales-tax authorities so that various matters arising from proceedings under the Sales-tax Act, which have a bearing on the income-tax assessments, are taken due note of by the income-tax authorities in the relevant assessment proceedings.

(a) Sales tax authorities raided the premises of a registered firm in November 1975 and detected unaccounted sales worth several lakhs of rupees. While framing the sales-tax assessment for assessment year 1975-76 (relevant to income tax assessment year 1976-77) the turnover of the assessee was enhanced by Rs. 4,00,000 by the sales tax department in March 1980. However, this enhanced turnover was reduced to Rs. 2,00,000 by the sales-tax appellate authority in May 1980. The income-tax department framed the assessment for the assessment year 1976-77 in November 1977 in which taxable income was determined at Rs. 48,170. Owing to lack of liasion with the sales-tax department no action was taken by the income-tax department to reopen the assessment as a result of sales-tax proceedings against the assessee, till the facts were brought to the notice of the assessing officer by Audit in July 1984.

Addition of sales of Rs. 2,00,000 in the trading account will correspondingly increase the profit of the firm resulting in under charge of tax of Rs. 47,508 in the hands of the firm against which penalty for concealment of income is also leviable. Short

levy of tax in the hands of the partners as a result of the revision of the assessment of the firm is yet to be ascertained.

The Ministry of Finance have accepted the omission (December 1984).

(b) In respect of assessment of an unregistered firm engaged in liquor business, accounts rendered by the assessee for the previous year (ending on 31 March 1979) relevant to the assessment year 1979-80, were rejected by department and gross sales for the year were estimated at Rs. 13,00,000. By applying a net profit rate of 8 per cent of sales, total income for the assessment year 1979-80 was determined at Rs. 1,04,000 in February 1983.

A correlation with sales-tax records indicated that the assessee, for the purposes of sales-tax assessment had returned sales of Rs. 18,00,000 for the same period. Total sales for the income-tax assessment were consequently under stated by Rs. 5,00,000 leading to short computation of income by Rs. 40,000. This resulted in short levy of tax of Rs. 40,296 including interest for default in payment of advance tax.

The Ministry of Finance have accepted the mistake (October 1984).

3.18 *Irregular set off of losses*

Under the Income-tax Act, 1961, losses relating to long term capital assets arising under the head 'capital gains' which cannot be adjusted in the assessment of the same assessment year are to be carried forward to the follwing assessment years for set-off against the income under the same head. The loss can be carried forward for four assessment years immediately succeeding the assessment year for which the loss was first computed.

In the case of a Hindu undivided family the assessment for the assessment year 1980-81 was completed in May 1981 allowing set-off of unadjusted loss under the head 'capital gains' of the assessment year 1976-77 amounting to Rs. 1,44,924 against the income of the relevant previous year under the same head. Subsequently the assessment of the assessment year 1976-77 was revised in September 1982 in order to give effect to the directions of the Income-tax Appellate Tribunal, which *inter alia* had the effect of reducing the loss under the head 'capital gains' by Rs. 1,19,597. However, the assessment for the assessment year 1980-81 was not rectified accordingly modifying the amount of loss which had been allowed set off earlier. The mistake

resulted in under-assessment of income by Rs. 71,758 with consequent under charge of tax of Rs. 51,665.

The Ministry of Finance have accepted the mistake (August 1984).

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

Under the provisions of the Income-tax Act, 1961, as amended retrospectively with effect 1 April 1972 by the Finance Act 1980 where the gross total income of an assessee included profits and gains derived from a newly established industrial undertaking which went into production before 1 April 1981 the assessee becomes entitled to tax relief in respect of such profits and gains upto six per cent 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 succeeding assessment years. For the purpose of arriving at the value of capital employed, the aggregate of the moneys borrowed or debts owed by the assessee should be deducted from the gross value of the assets.

While finalising the income-tax assessment of a registered firm for the assessment year 1980-81 in February 1983, the assessee was allowed deduction of Rs. 2,36,842 on account of the relief in respect of a new industrial undertaking owned by the assessee on the capital computed at Rs. 39,47,369 after deducting the current liabilities and provisions amounting to Rs. 8,29,308 from the total asset valued at Rs. 47,76,677. The additional liability of Rs. 14,32,000 outstanding towards secured and unsecured loans and advances was not, however, taken into account while computing the capital employed and this resulted in excess computation of the capital employed and under assessment of income by Rs. 85,920 with consequent under charge of tax of Rs. 53,531 in the hands of the firm and its partners.

The Ministry of Finance have accepted the mistake (November 1984).

3.20 *Non levy or incorrect levy of interest.*

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 the prescribed rates from the day immediately following the specified date to the date of furnishing the return on the amount of

tax payable on the total income as determined on regular assessment as reduced by the advance tax, if any paid, and any tax deducted at source.

The Income-tax assessments for the assessment years 1972-73 to 1976-77 in respect of an individual were completed in March 1983 *ex parte*. As no returns of income had been filed, penal interest was levied by the department. However, while calculating the period for which interest was chargeable, the period was taken short by 11 months in respect of each assessment. The mistake resulted in short levy of interest aggregating Rs. 78,845.

The Ministry of Finance have accepted the mistake (January 1985).

3.21 *Mistakes in assessments under summary assessment scheme.*

The problem of mounting arrears of assessment had been engaging the attention of the Government from time to time. With the increase in the volume of work, vis-a-vis the available man-power, the department adopted a selective approach in the completion of assessments while at the same time, building an atmosphere of mutual trust. The Taxation Laws (Amendment) Act, 1970 which came into effect from 1 April 1971 gave statutory recognition to the scheme of completing assessments in a summary manner upto the prescribed range of income.

The main objects of this scheme, *inter alia* are :

(i) reduction of mounting arrears of work ;

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

(iii) to dovetail the work load to match the available man-power resources of the department for achieving more efficiency and effective output by the department ;

(iv) deployment of the man-power so saved on higher income cases to achieve better results ; and

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

Under this scheme, the Income-tax Officer may without requiring the presence of the assessee or the production of any

evidence in support of the return, make an assessment of the total income on the basis of the return itself. In their instructions of May 1980, February 1981 and May 1983, the Central Board of Direct Taxes have framed guidelines for the operation of the scheme. Some of the assessment cases made summarily are selected at random by the department for detailed scrutiny.

Mistakes noticed in audit in some cases where assessments were completed in a summary manner are detailed in succeeding paragraphs.

(i) Under the Income-tax Act, 1961, any profits and gains arising from the transfer of a capital asset are chargeable to income-tax under the head capital gains for the purpose of computation of capital gains. The term "transfer" has been defined in the Act to include sale, exchange or relinquishment of an asset or extinguishment of any right therein.

An assessee individual had for the assessment years 1977-78 and 1978-79 returned total income of Rs. 9,860 for each year under the head "other sources". The Income-tax Officer accepted the returned income and completed the assessments in a summary manner in March 1979 and March 1981 for the two years. According to the wealth-tax records, the assessee owned four land sites bearing No. 26,27,36 and 45 (value indicated as Rs. 13,410 for each site) in the assessment year 1976-77. During the previous year relevant to the assessment years 1977-78 and 1978-79 the assessee had sold the sites No. 36 and 26 respectively but the sale particulars had neither been returned in the income-tax returns nor any capital gains arising out of the sales offered to tax by the assessee. Based on the orders of the Appellate Assistant Commissioner (September 1983) relating to the wealth-tax assessments for the assessment years 1977-78 and 1978-79, the sale value of the two sites could, however, be adopted at Rs. 1,57,000 and Rs. 1,00,000 respectively. Deducting therefrom, the value shown by the assessee for the sites at Rs. 13,410 each in the wealth-tax returns, the capital gains arising to the assessee would work out to Rs. 1,43,590 and Rs. 86,590 for the two assessment years. The omission to bring the income to tax, led to a short-levy of tax of Rs. 78,692.

The Ministry of Finance have accepted the mistake (October 1984).

(ii) Under the provisions of the Income-tax Act, 1961, all income accruing or arising or deemed to accrue or arise to an

assessee in India in a previous year relevant to the assessment year is includible in the total income of the assessee.

An assessee filed his return for the assessment year 1978-79 in April 1980, showing income of Rs. 93,827 from his own business, basides share income of Rs. 6,292 from a firm in which he was a partner, and accordingly paid advance tax of Rs. 20,000. The Income-tax Officer, however, made a summary assessment only on the correct share income at Rs. 6,600 from the firm and refunded the entire advance tax of Rs. 20,000 together with interest of Rs. 5,400 thereon. The omission to assess the income of Rs. 93,827 from assessee's own business resulted in short-levy of tax of Rs. 62,455 including interest for belated filing of return and short fall of payment of advance tax as also the interest of Rs. 5,400 incorrectly allowed on advance tax.

The Ministry of Finance have accepted the mistake (October 1984).

(iii) Under the Income-tax Act, 1961, dividends paid by newly established undertaking out of the profits and gains exempt from tax, are entitled to a deduction from the total income of the recipient assessee for the relevant assessment year. The extent of deduction to be allowed is indicated by the Principal Officer of the concerned company on the dividend warrants themselves.

In the assessments of two assessees for the assessment year 1981-82, completed in August 1982 in a summary manner, the department allowed deduction from the total income of dividends aggregating Rs. 85,225 received from a company even though the dividend warrants did not bear the prescribed certificate for allowing exemption. The incorrect deduction resulted in short-demand of tax of Rs. 46,618.

In reply, the Ministry of Finance have stated (December 1984) that the assessment was made in a summary manner and remedial action is being taken.

(iv) Under the Income-tax Act, the capital gains arising from the transfer of a capital asset is not taxed in case the consideration for such transfer does not exceed Rs. 25,000 and the aggregate of the fair market value of all the capital assets, the income from which is assessed under income from 'house property' owned by the assessee immediately before the transfer, does not exceed Rs. 50,000.

A Hindu undivided family filed a return of income for the assessment year 1982-83 showing a taxable income of Rs. 23,750. In the return, the capital gains arising out of the sale of a house for Rs. 19,875 was claimed as exempt under the Act. In respect of sale of another property for Rs. 90,000, capital gain was not returned as according to the assessee it was the 'stridhan' of his wife. The Income-tax assessment for the assessment year 1982-83 was completed in March 1983 under the summary assessment scheme on the taxable income of Rs. 23,750 as returned.

In the Income-tax|wealth-tax assessments for the assessment year 1970-71 and later years, the claim of the assessee that one of the properties belonged to his wife was negatived by the department and the property was treated as that of the assessee. The capital gain arising out of the sale of the second property was accordingly chargeable to tax. Besides, as the value of the two properties sold exceeded Rs. 50,000 the exemption of capital gains allowed in relation to the first property was not also in order.

The omission resulted in non-assessment of capital gains of Rs. 95,875 with consequent non-levy of tax of Rs. 35,829.

The Ministry of Finance have accepted the mistake (December 1984).

(v) Under the provisions of the Income-tax Act, 1961, unabsorbed business loss of an assessee for an assessment year can be carried forward and set off against the profits and gains from business for eight subsequent assessment years provided that the assessee continues to carry on the business to which the loss pertains in the year in which the set off is claimed. Further, if the assessee is a partner in a registered firm, the loss sustained by the firm is to be allocated among the partners and it is the partners who can claim set off during subsequent assessment year subject to the conditions specified earlier.

In the income-tax assessment of an individual for the assessment year 1980-81 finalised in April 1981 in a summary manner, the income of the relevant previous year was assessed at an amount of Rs. 82,084 which was fully set-off against the business loss of earlier years amounting to Rs. 1,03,323 and the net income was assessed at 'nil'. The unabsorbed loss of Rs. 21,239 was allowed to be carried forward for subsequent assessment year. The assessment records disclosed that the business loss

carried forward from earlier years pertained to the assessee's share of loss from two registered firms in which he was a partner. However, the assessee ceased to be a partner in these two firms during the previous year relevant to the assessment year 1980-81 and hence, it cannot be said that he had carried on the business in which the loss was incurred during the said previous year. Therefore, the set off of loss of the earlier years to the extent of Rs. 82,084 was not in order, and the mistake resulted in under-assessment of income of Rs. 78,031 (after allowing deductions admissible under the Act) with consequent non-levy of income-tax of Rs. 32,539.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

(vi) Under the provisions of the Income-tax Act, 1961, the entire income of a co-operative society from specified activities is exempt from income-tax. For a co-operative society engaged in other activities either independently or in addition to those specified, a deduction from such income relatable to other activities is admissible to the extent of Rs. 20,000.

(a) The income of a co-operative society for the assessment years 1978-79 to 1980-81 included income from purchase and sale of agriculture implements, which is exempt from tax. In the returns filed, the assessee deducted the gross income from the specified activity from the total income and arrived at the taxable income for all the three years. Accepting the returned income, the Income-tax Officer completed the assessments in a summary manner, in December 1980. The taxable income should have been arived at after excluding the net income and not the gross income from the said activity as returned by the assessee. In the absence of details regarding the actual expenditure incurred, if the proportionate amount of expenditure attributable to the activity was considered for arriving at the net income from the said activity, for purposes of exclusion from gross total income, the excess relief allowed to the assessee would work out to Rs. 3,07,500 leading to short levy of tax of Rs. 1,43,015 for all the three assessment years.

In reply, the Ministry of Finance have stated (January 1985) that the assessments, made in a summary manner, had been set aside.

(b) In the case of a co-operative society engaged in trading of consumer goods as well as business of banking, the assessing officer computed the income chargeable to tax at Rs. 13,880 and Rs. 7,200 for the assessment years 1980-81 and 1981-82 respectively and completed the assessments in a summary manner in October 1982, as income relating to trading in consumer goods. The annual reports of the society for the relevant previous years ending 30 June 1979 and 30 June 1980, however, revealed that after setting off expenses towards the trading activity, the society had earned income from consumer goods alone, to the extent of Rs. 86,899 and Rs. 1,13,756 for the two years. After allowing a deduction of Rs. 40,000 as admissible the income chargeable to tax would work out to Rs. 46,899 and Rs. 73,756 as against Rs. 13,880 and Rs. 7,200 respectively. This led to short-levy of tax aggregating Rs. 51,444.

In reply, the Ministry of Finance have stated (January 1985) that the assessments were made in a summary manner and remedial action has been initiated.

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

Under the Income-tax Act, 1961, where any person enters into a contract with any other person for carrying out any work or supply of goods or services in connection therewith, the value of which exceeds Rs. 50,000 he shall within one month of entering into contract furnish to the Income-tax Officer, particulars of the contract in the prescribed form. In the event of failure to furnish such particulars, the Commissioner of Income-tax may impose a fine not exceeding Rs. 50 for each day of default subject to a maximum of 25 per cent of the value of the contract.

An assessee firm had entered into a sub-contract worth Rs. 38,74,369 with a contractor in June 1976 for construction of two additional stores. The assessee was to file the details of contract, to the Income-tax Officer within one month of execution of contract. The assessee had not, however, filed the statutory return and the maximum fine leviable consequently would work out to Rs. 9,68,592 which was not levied by the department.

The Ministry of Finance have admitted (December 1984) that there was failure on the part of the assessee to comply with the provisions of law.

OTHER TOPICS OF INTEREST

3.23 *Non-levy of tax on capital gains on transfer of assets*

The Inocme-tax Act, 1961, contains a provision for the computation of capital gains arising on transfer of a capital asset with reference to its market value as on the date of its transfer, ignoring the amount of consideration shown by the assessee, if the following two conditions are satisfied :—

(1) The transfer is to a person who is directly or indirectly connected with the assessee ; and

(2) The Income-tax Officer has reason to believe that the transfer was effected with the object of avoidance or reduction of the liability of the assessee to tax on capital gains.

This provision has a limited operation and does not apply to other cases, where tax liability on capital gains on transfer of capital assets between parties not connected with each other is sought to be avoided or reduced by an under-statement of the consideration paid for the transfer of the asset.

With a view to countering evasion of tax on capital gains through the device of under-statement of the full value of the consideration received or receivable on the transfer of a capital asset, the law was amended with effect from 1 April 1964, re-numbering the existing section as sub-section (1) and adding a new provision as sub-section (2). The new provision enables the Income-tax Officer to compute the amount of capital gains arising on the transfer of capital asset with reference to its fair market value as on the date of its transfer, if in his opinion, such fair market value exceeds the full value of the consideration for it as declared by the assessee by 15 per cent of the value so declared. The fair market value of a capital asset is deemed to be the price that a capital asset would ordinarily fetch on sale in the open market on the relevant date.

According to the Department of Revenue, the only condition for attracting the applicability of the new provision is that the fair market value of the capital asset transferred by the assessee as on the date of transfer, exceeded the full value of the consideration declared by the assessee in respect of the transfer by an amount not less than 15 per cent of the value so declared. Once, the Income-tax Officer is satisfied that this condition exists, he can proceed to invoke the provision and compute the capital

gains adopting the fair market value as the full value of the consideration. Further, proving or establishing the fact of understatement of consideration, before invoking the section, is not contemplated. This stand of the Department was, however, held to be untenable by the Supreme Court in a case in September 1981. The Supreme Court decided that the new provision can be invoked only where the consideration for the transfer of a capital asset has been under stated by the assessee, or in other words, the consideration actually received by the assessee is more than what is declared or disclosed by him, and the burden of proving such understatement or concealment is on the revenue. According to the judgment, this burden may be discharged by the revenue by establishing facts and circumstances from which a reasonable inference can be drawn that the assessee has not correctly declared or disclosed the consideration received by him and there is an understatement or concealment of the consideration in respect of the transfer. As a result of the onus of establishing the understatement or concealment of sale consideration having been placed on the Department by the Supreme Court, the provision has become practically inoperable thereby defeating the original intention of countering tax evasion on capital gains through this provision. The impact of the Supreme Court judgment on the application of the law has not, however, been reviewed by Government thereafter and action taken to modify or amend the law to achieve the legislative intention. Instructions for the guidance of the assessing officers explaining the implications of the Supreme Court judgment and the precautions to be taken in the application of the law have not also been issued so far (November 1984).

Two cases which have come to notice of audit in this regard are cited below:

(a) An assessee sold a part of one of his properties during the assessment year 1979-80 for a consideration of Rs. 8 lakhs which was accepted by the Income-tax Officer in the assessment completed in February 1980. The site of the property measuring 9 grounds and 552 sq. ft. and with a built up area of 16,627 sq. ft. was located in one of the most important commercial localities in a metropolitan city. Considering the location, area as also the fact that the Departmental Valuation Officer himself had estimated the value per ground in respect of another property, in the same area at nearly Rs. 1,26,000 during this period, the value of the plot itself even at a conservative rate of Rs. 1 lakh per ground would work out to Rs. 9,23,000. Adding thereto, the

cost of construction of Rs. 5,98,572 (at 1969 rates) the total value of the property would be Rs. 15,21,572 as against Rs. 8,00,000 returned by the assessee and accepted by the department for the assessment. The omission to adopt the fair market value as on the date of transfer resulted in under assessment of capital gains of at least Rs. 7,21,572 involving a short levy of tax of Rs. 3,96,800.

On this under-assessment being pointed out during the course of audit, the department stated (February 1984) that in view of the Supreme Court's decision the point raised was infructuous.

(b) An assessee had three-fourth share in a house property which was sold by him during the previous year relevant to the assessment year 1976-77 to a private limited company for a total consideration of Rs. 4,95,000. This property was valued by the District Valuation Officer at Rs. 7,49,000 as on 31 March 1975 for purposes of wealth-tax and the same value was adopted in the wealth-tax assessment of the assessee for the assessment year 1975-76. As the company which acquired the property and the assessee were connected, the omission to take the fair market value of the capital asset on the date of transfer as the full value of the consideration for the transfer resulted in escapement of capital gains of Rs. 1,41,938 involving short-levy of tax of Rs. 92,981.

On this omission being pointed out in audit in July 1981, the department justified it by quoting the Supreme Court judgment.

The paragraph was sent to the Ministry of Finance in September 1984 ; their reply is awaited (November 1984).

3.24 *Payment of additional foreign allowance in lieu of Income-tax under executive instructions*

A person who is not resident in India is not taxed on the income which arises outside India. So government servants who are posted abroad and become technically non-residents, after some time, are not liable to tax on the salaries drawn by them abroad. With a view to subject such salaries, paid out of public revenues of India (exclusive of all allowances and perquisites granted to meet the cost of having to stay abroad) to tax, irrespective, of the period of the government employees' stay abroad, the income-tax Act, 1922 was amended through Finance Act 1959, with effect from 1 April 1959 providing that such salary income shall be deemed to accrue or arise in the taxable

territories and become chargeable to tax. Simultaneously, the allowances or perquisites paid or allowed to a citizen of India by the Government for rendering service outside India were exempted from levy of tax. These provisions in the Income-tax Act 1922 were in *toto* carried into the Income-tax Act, 1961, which is now in force. The legislative intention is that salary-part of remuneration of government servants posted abroad, is liable to tax.

Government of India, Ministry of External Affairs through executive instructions of April 1959 (revised from time to time) authorised payment of "additional foreign allowance" to all government servants posted abroad as relief in lieu of income tax payable on salaries which were exempt from tax before April 1959. The additional foreign allowance is in no way related to the normal foreign allowance granted for cost of living etc. in a foreign station. However, this allowance is not subject to tax. Initially the additional foreign allowance, varied according to the salary slab and had no relationship with actual tax liability. In December 1981, the Ministry revised the quantum of additional foreign allowance equating it to the amount of tax actually paid. The *modus operandi* of the arrangement is that, without deducting tax at source from salary at the time of payment every month as contemplated in the law, the tax liability is calculated just before the close of the financial year and a book adjustment made debiting the service head and crediting revenue.

As a result of the payment of additional foreign allowance since April 1959, the salary income of government servants posted abroad, has, in effect become totally free of income-tax though the specific decision of the Legislature was to tax the salary-portion of the emoluments. The propriety of nullifying the statutory provisions through executive instructions would seem questionable.

The paragraph was sent to the Ministry of Finance in October 1984 ; their reply is awaited (November 1984).

CHAPTER 4

OTHER DIRECT TAXES

A—WEALTH TAX

4.01 In the financial years 1979-80 to 1983-84 wealth-tax receipts *vis-a-vis* the budget estimates were as given below :—

Year	Budget Estimates	Actuals
	(In crores of rupees)	
1979-80	60.00	64.47
1980-81	65.00	67.37
1981-82	66.00	78.12
1982-83	80.00	90.37
1983-84	90.00	93.31*

4.02 Particulars of cases finalised, pending assessment and arrears of demand are given below :—

Year	Number of assessments completed during the year	Number of cases pending assessment at the end of	Arrears of demand pending collection at the end of (In crores of rupees)
1979-80	3,25,718	4,32,988	180.54
1980-81	3,50,583	4,99,903	217.11
1981-82	3,97,211	5,67,381	208.92
1982-83	4,27,483**	5,41,594**	182.29**
1983-84	4,61,923	4,92,752	197.29

4.03 During the test audit of assessments made under the Wealth-tax Act, 1957, conducted during the period 1 April 1983 to 31 March 1984, the following types of mistakes were noticed :

(i) Wealth escaping assessment.
(ii) Incorrect valuation of assets.
(iii) Incorrect computation of net wealth.

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*Provisional

**Figures furnished by Ministry of Finance in March/April 1984 have been adopted.

(iv) Incorrect exemptions and deductions.

(v) Mistakes in application of rates of tax, calculation of tax, etc.

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

(vii) Non-levy|short-levy of penalty.

(viii) Miscellaneous.

A few important cases illustrating these mistakes are given in the following paragraphs.

4.04 *Wealth escaping assessment*

(i) Under the Wealth-tax Act, 1957, the net wealth of an assessee means the aggregate value of all assets, wherever located, belonging to the assessee, as reduced by the aggregate value of all admissible debts owed by him on the valuation date. Further, the Act also provides for the levy of penalty, *inter alia,* if an assessee has, without reasonable cause, failed to furnish the wealth-tax return within the prescribed time or concealed the particulars of any assets or furnished inaccurate particulars of any assets or debts.

(a) A person, in the status of individual filed income-tax returns (October 1980 and revised returns in March 1981) for the assessment years 1978-79 and 1979-80. Income returned consisted of income from contract business and income from house property. During the course of assessment proceedings, the assessing officer found (December 1982) that the house property consisted of ten houses in urban area and belonged to the Hindu undivided family of which the above person was a coparcener. The Hindu undivided family had not filed any wealth-tax return in respect of these properties. Accordingly, the assessing officer issued notices to the Hindu undivided family under the Act for filing returns of net wealth for the assessment years 1980-81 and 1981-82. However, the assessments for earlier years from 1975-76 to 1979-80 should have simultaneously been opened as the Hindu undivided family had owned these ten houses in years prior to 1980-81 and in December 1982 it was possible to open assessments for the assessment year 1975-76 and onwards. The assessing officer had not recorded any reasons as to why the assessments for the years prior to 1980-81 were left out.

The above omission resulted in escapement of wealth of Rs. 50,00,000, with consequent short levy of tax (including additional wealth-tax on urban immovable properties for the

assessment years 1975-76 and 1976-77) of Rs. 1,05,570, for the assessment years 1975-76 to 1979-80. In addition, penalty for delay in filing the returns amounting to Rs. 4,32,200 was also leviable, which was not levied.

The paragraph was sent to the Ministry of Finance in July 1984 ; their reply is awaited (November 1984).

(b) A Hindu undivided family filed wealth-tax returns, for the assessment years 1977-78 to 1980-81 in October 1980. Wealth returned consisted of immovable properties valued at Rs. 2.95 lakhs, as on 31 March 1974, by a registered valuer in June 1974.

As the value of the property returned by the assessee was considered to be on lower side, the Wealth-tax Officer referred the matter to the departmental valuer who valued the property (January 1982) at Rs. 12.85 lakhs, Rs. 14.04 lakhs, Rs. 15.23 lakhs and Rs. 16.76 lakhs as on 31 March 1977, 31 March 1978, 31 March 1979 and 31 March 1980 respectively.

As the assessee opted for the value of the property as on 1 April 1971, in respect of self-occupied portion, the Wealth-tax Officer again referred the matter to the valuation cell for valuing the property. The revised valuation so desired by the Wealth-tax Officer was not received and the assessment, for assessment year 1977-78, was completed, in March 1982, adopting the value of the property at Rs. 12.85 lakhs on the basis of Departmental Valuation Officer's report of January 1982, received on 2 February 1982, subject to rectification of assessment on receipt of revised valuation report. In appeal, in August 1982, the Appellate Assistant Commissioner directed that the assessment should be made afresh after taking the value in respect of self-occupied portion. Similarly, the assessment, for the assessment year 1978-79, was completed, in March 1983, adopting the value of the property at Rs. 14.04 lakhs, subject to rectification on receipt of revised valuation report.

From the assessment records and the pendency register for the year 1982-83 it was observed that the assessee did not file the wealth-tax returns up to the assessment year 1976-77. The department also did not call for the returns as per pendency register. The returns for the assessment years 1973-74 to 1976-77 could have been called for by 31 March 1982, because by that time (2 February 1982) it was known through the above valuation report that the market value of the property as on 31 March 1977, for the assessment year 1977-78, was Rs. 12,85,000.

The departmental valuation report showed that on an average the annual appreciation in the value of the properties was ten per cent. After considering the concession available in respect of the self-occupied portion of the house for the assessment year 1976-77 and taking the value of the properties less by 10 per cent each year as compared to the value of Rs. 12,85,000 for the assessment year 1977-78, the amount of net wealth that escaped assessment was Rs. 7 lakhs, Rs. 8 lakhs, Rs. 9 lakhs and Rs. 9 lakhs, for the assessment years 1973-74 to 1976-77, respectively. Consequent short levy of tax (including additional wealth-tax on urban immovable properties) worked out to Rs. 1,51,895. Out of this, revenue of Rs. 52,275, for the assessment years 1973-74 and 1974-75, was lost as the rectificatory action was time-barred. Further, penalty provisions for non-filing of the returns were also attracted.

The Ministry of Finance have accepted the mistake in principle (November 1984).

(c) In computing the net wealth of two assessees in Match 1982 for the assessment year 1977-78, one-fifth shares in the amounts of Rs. 25 lakhs and Rs. 51,500 due from a Sugar Mill and an estate of an erstwhile Hindu undivided family, respectively, in respect of each of the assessees, were not included in their net wealth. However, one-fifth shares mentioned above were not included in respect of each of the assessee in the assessment year 1978-79 on the grounds that the court Receiver had filed a suit for recovery of Rs. 25 lakhs from the Mill and the Mill was solvent and hence it could not be said that the debt had become bad. Regarding the sum of Rs. 51,500 there was no evidence on the file to indicate that the estate was not capable of meeting the liability. These omissions resulted in under-assessment of wealth of Rs. 10,20,600, with consequent short levy of wealth-tax of Rs. 34,510.

The Ministry of Finance have accepted the mistakes (September 1984).

(ii) An amount of Rs. 11,05,000 advanced by a Hindu undivided family to a debtor for which a decree was issued by a Court in its favour, was included in its total wealth for the assessment years 1969-70 to 1972-73. The inclusion was confirmed by the Commissioner of Income-tax (Appeals), rejecting the contention of the assessee that the debt was not includible because of the debtor's appeal to the Supreme Court against the decree granted by the lower Court. The debt was not one of the assets

which were divided during two partial partitions that took place in March 1971 and July 1971. The debt was, therefore, includible in the total wealth of the assessee Hindu undivided family for the assessment years subsequent to 1972-73 also. But it was not so included resulting in short levy of wealth-tax of Rs. 3,99,800 for the assessment years 1973-74 to 1978-79, of which Rs. 2,43,900 relating to the assessment years 1973-74 to 1975-76 cannot be recovered as claims are time-barred.

The paragraph was sent to the Ministry of Finance in July 1984 ; their reply is awaited (November 1984).

(iii) An assessee (specified Hindu undivided family) applied in June 1976, August 1976 and September 1976 for extension of time for filing his wealth-tax return, for the assessment year 1976-77. The application dated September 1976 was rejected by the department. A notice was served on the assessee in February 1977 requiring him to file the return. However, neither the assessee had filed the return nor the department had taken further action to finalise the assessment.

The assessee's net wealth for the earlier assessment year 1975-76 was computed at Rs. 19,45,200 and tax including additional wealth-tax of Rs. 1,24,887 was levied. Based on that year's computation, the wealth escaping assessment for the assessment year 1976-77 was Rs. 19,45,200 with consequent short-levy of wealth-tax (including additional wealth-tax) of Rs. 1,24,887. Penalty provisions for non-filing of the return were also attracted.

The Ministry of Finance have accepted the mistake (October 1984).

(iv) The Central Board of Direct Taxes issued instructions (November 1973 and April 1979) emphasising the need for proper co-ordination amongst assessment records pertaining to different direct taxes with a view to prevent cases of evasion of tax.

(a) An individual, succeeded to the estate of his father (died in October 1976) as per deceased's 'will' of March 1975. The net wealth of the individual for the assessment years 1977-78 and 1978-79 was assessed in February 1982 and January 1983, at Rs. 15,11,593 and Rs. 13,96,940, respectively, after allowing, *inter alia*, a deduction of Rs. 15,36,997 towards estate duty liability for both the assessment years.

A correlation of the assessment records of the deceased in respect of the wealth-tax and estate duty revealed that certain assets (house property, deposits, amounts loaned out, share in Hindu undivided family, etc.) of the deceased bequeathed to the assessee under the 'will' were not included in the net wealth of the assessee for the above two assessment years. Taking into account the above assets, the correct net wealth of the assessee worked out to Rs. 25,31,773 and Rs. 20,03,376, for the two assessment years 1977-78 and 1978-79, respectively. The failure to correlate the different direct taxes returns resulted in short-levy of tax of Rs. 52,930.

The paragraph was sent to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

(b) Income-tax assessment records of an individual for the assessment year 1974-75, revealed that the assessee possessed 'Jagir Bonds' worth Rs. 1,85,750 with maturity dates in July and December 1971, agricultural land measuring 40 Bighas, a residential house under self-occupation and other immovable properties with rental income of Rs. 4,310 in the years 1972-73 to 1974-75 and Rs. 9,158 in the year 1975-76. This information available with the department was not made use of by the assessing officer and consequently the values of the above assets were not considered for wealth-tax assessments of the assessee, for the assessment years 1972-73 to 1977-78. This resulted in non-levy of tax of Rs. 34,100.

The Ministry of Finance have accepted the mistake (October 1984).

(v) The value of an estate was determined (March 1983) by the Departmental Valuation Officer at Rs. 89.41 lakhs as on 31 December 1977 (valuation date) against its book value of Rs. 29.14 lakhs returned by eight assessees who owned it, for the assessment year 1978-79. In the case of four assessees, who had one-eighth share each in the said property, an addition of Rs. 7.53 lakhs in each case was made by the department at the time of completing the wealth-tax assessment in March 1983, towards the increase in the valuations. Similar additions were not, however, made in the case of three other assessees who had also one-eighth share each in the said property and whose assessments for the assessment year 1978-79 were also completed in March 1983 in the same ward (the assessment of the eighth person not having been completed). The omission in the three cases resulted

in under-assessment of wealth of Rs. 7.53 lakhs in each case, with consequent short-levy of tax in the aggregate of Rs. 50,385.

The Ministry of Finance have accepted the mistake (November 1984).

(vi) Five individuals, jointly owned agricultural lands measuring 148 acres in fixed shares from a period prior to April 1970. This asset was not disclosed by any of the five individuals in their returns of net wealth, for the assessment years 1970-71 to 1972-73. However, only one individual disclosed part of the land, *viz.*, 55 acres in her return of net wealth for the assessment year 1973-74 and the remaining part (93 acres) in her return for the assessment year 1975-76.

While completing the wealth-tax assessment of the above individual in March 1979, for the assessment year 1973-74, the Wealth-tax Officer determined the value of 55 acres of land at Rs. 5,000 per acre as no valuation of these lands was given by the assessee. The total value worked out on this basis was Rs. 2,75,000, out of which an exemption of Rs. 1,50,000 was allowed. The Wealth-tax Officer also completed the wealth-tax assessment of the same individual, for the assessment year 1975-76, in February 1980, and determined the value of 55 acres of land at Rs. 7,000 per acre and Rs. 5,000 per acre for the remaining 93 acres, total value of these lands was thus worked out at Rs. 8,50,000.

The Wealth-tax Officer also noticed the co-ownership of five individuals in the value of lands and allocated the value of Rs. 8,50,000 of lands amongst the five individuals as per their personal law which was taken into account for purposes of wealth-tax assessments in respect of each of the five individuals, for the assessment year 1975-76. However, no action was taken by him to re-open the assessments for the earlier assessment years 1970-71 to 1974-75 of these individuals, though the land was assessable to wealth-tax for these assessment years also. Taking the value of 148 acres of land at Rs. 5,000 per acre as determined by the Wealth-tax Officer, for the assessment year 1973-74, the total value of lands worked out to Rs. 7,40,000, which escaped assessment in each of the assessment years 1970-71 to 1974-75, with consequent short-levy of tax of Rs. 48,329.

The Ministry of Finance have accepted the mistake (December 1984).

(vii) Jewellery valued at Rs. 5.26 lakhs in the immediately preceding years was not included in the wealth-tax assessments of an assessee, for the assessment years 1969-70 and 1970-71, in spite of the orders of December, 1972 of the Commissioner of Wealth-tax. His orders were sustained also in appeal. The omission led to wealth escaping assessment to the tune of Rs. 10.52 lakhs. No action to rectify the assessment and realise the additional demand is possible now due to time-bar and the omission thus led to loss of revenue of Rs. 30,642 for the assessment years 1969-70 and 1970-71.

The Ministry of Finance have accepted the mistake (September 1984).

4.05 *Incorrect valuation of assets*

A. *Immovable properties*

(i) Six assessees were co-owners of five house properties. The report of the Departmental Valuation Officer valuing these properties as on the valuation dates relevant to the assessment years 1976-77, 1977-78 and 1978-79, was received by the Wealth-tax Officer in July 1980. The value so determined was higher than that determined by the Appellate Tribunal in December 1980, for the assessment years 1973-74 and 1974-75. In the assessments, for the assessment years 1976-77, 1977-78 and 1978-79, made after July 1980, the Wealth-tax Officer took the lower value of these assets as approved by the Appellate Authority for the earlier years ignoring the higher value for the subsequent years as determined by the departmental valuer, although the valuer's report was binding on the Assessing Officer. This resulted in under-valuation of net wealth in the cases of five assessees, with consequent short-levy of tax of Rs. 65,080.

The Ministry of Finance have accepted the mistake (January 1985).

(ii) The net wealth of an assessee included two self-occupied properties. The value of the first property was determined (August 1979) by the Valuation Officer at Rs. 4.08 lakhs, Rs. 4.60 lakhs and Rs. 5.28 lakhs as on 31 March, 1973, 31 March, 1974 and 31 March, 1975, for each of the respective assessment years 1973-74 to 1975-76. The value of the second property in which the assessee had only one-fourth share, was determined (July 1979) by the Valuation Officer at Rs. 16.23 lakhs, Rs. 16.91 lakhs and Rs. 15.60 lakhs as on 31 March, 1973,

31 March, 1974 and 31 March, 1975, respectively. While completing reassessments in March 1982 [the original assessments having been set aside in July 1979 by the Commissioner (Appeals)] in the light of an audit objection raised in August 1978, for the assessment years 1973-74 to 1975-76, the Wealth-tax Officer had not taken the value of these properties correctly. The value of the second property was taken at the value determined by the Valuation Officer for the first property for each of the assessment year. Similarly, the value of the first property was taken at Rs. 2.09 lakhs as returned by the assessee for each of the assessment year instead of the higher value determined by the Valuation Officer. No additional wealth-tax was also levied on the value of urban immovable properties. The mistakes resulted in short levy of wealth-tax (including additional wealth-tax) of Rs. 45,151.

The Ministry of Finance have accepted the mistake (September 1984).

(iii) While computing (March 1982) the net wealth in the case of a Hindu undivided family, for the assessment year 1977-78, the Wealth-tax Officer had incorrectly taken the value of a piece of land measuring 18,842 sq. yards at Rs. 1,130 (Rs. 2,82,600 returned by the assessee), instead of the correct value of Rs. 11,30,000 (determined by the Departmental Valuation Officer for the assessment year 1976-77). This resulted in under-assessment of wealth by Rs. 11,28,870 with consequent short-levy of wealth-tax of Rs. 38,175.

The Ministry of Finance have accepted the mistake (August 1984).

(iv) In computing the net wealth of a Hindu undivided family, for the assessment year 1975-76, in February 1980, the Wealth-tax Officer adopted the value of the house property belonging to the assessee at Rs. 1,80,000, as returned by the assessee, instead of Rs. 6,66,500 as determined by the Departmental Valuer, in May 1979, as on the relevant valuation date (Diwali 1974).

Further, the assessee had not filed his wealth-tax return, for the assessment year 1977-78. The department also had not called for this return though the assessee had filed returns of wealth-tax for the earlier and subsequent assessment years. The non-filing of return resulted in escapement of wealth. On the basis of the net wealth assessed, for the assessment year 1976-77, in March 1981, the net wealth that escaped assessment amounted to Rs. 6,47,412.

The cumulative effect of the above two mistakes resulted in under-assessment of wealth of Rs. 11,33,912, with consequent short-levy of tax of Rs. 37,672.

The Ministry of Finance have not accepted the mistake and have stated (December 1984) that the mistake was already in the notice of the department much before it was pointed out by audit. The Ministry's reply was not, however, found factually correct.

B. *Partners' share interest in partnership firms*

(i) Goodwill of a business, as a going concern is a valuable asset. The Partnership Act provides that property of a firm includes also the goodwill of the business. As goodwill is a marketable asset, its value is includible in net wealth for purposes of levy of wealth-tax.

The Wealth-tax Rules, 1957, while laying down the method for determination of the net value of assets of business as a whole, *inter alia,* provides that the value of an asset not disclosed in the balance-sheet shall be taken to be, in the case of goodwill purchased by the assessee for a price, its market value or the price actually paid by him, whichever is less. A residuary provision in the said rule also provides that "in the case of any other asset not disclosed in the balance-sheet of the business, its market value as on the valuation date is to be adopted". If goodwill is not purchased and is not also shown in the balance-sheet, its market value as on the valuation date has to be taken into consideration for arriving at the net value of assets of the business as a whole.

(a) While completing the wealth-tax assessments of three assessees, who were partners in a firm, for the assessment years 1968-69 to 1976-77, on various dates between March 1969 and June 1981, their shares of goodwill in the firm were not included in their net wealth. When the constitution of the firm was changed with the introduction of a new partner with effect from 1 April, 1967, the Gift-tax Officer held in March 1981 that the introduction of a new partner without any capital created a gift by five of the partners by relinquishment and the value of goodwill in the deemed gift, was assessed as Rs. 22,27,545. The shares of goodwill in the hands of these three partners worked out to Rs. 3,71,258, Rs. 3,09,381 and Rs. 3,09,381, respectively, which were includible in their net wealth as well. The omission resulted in total short-levy of tax of Rs. 3,70,197, for all the assessment years 1968-69 to 1976-77.

(b) In the case of 20 assessees in two Commissioners' charges who were partners in five different partnership firms, the value of goodwill was not considered in computing their share interest in the firms. The omission resulted in under-assessment of wealth aggregating Rs. 32,43,824, for assessment years 1973-74 to 1977-78, leading to total under-charge of tax of Rs. 57,577.

The Ministry of Finance have stated (December 1984) that the goodwill on which no price has been paid is not chargeable to wealth-tax under the existing Wealth-tax Rules. The Ministry had, however, intimated in May 1978 that the matter was examined in consultation with the Ministry of Law on whose advice the amendment to Rules was under consideration of the Board. The Rules remain to be amended.

(ii) Under the Wealth-tax Act, 1957, where an assessee is a partner in a firm, the value of his interest in the net assets of the firm is to be included in his net wealth. The Wealth-tax Rules, 1957, provide that where the market value of any asset exceeds its book value by more than 20 per cent, the market value is to be substituted for the book value in such valuation. Further, in 1972, the Wealth-tax Act was amended, providing for reference of the question of valuation to the valuation cell. According to the Rule, 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 33-1/3 per cent or Rs. 50,000. The valuation done by the Departmental Valuation Officer is binding on the Wealth-tax Officer.

(a) The income-tax assessment records of a registered firm as well as of its partners revealed that, out of four partners in a firm, only one partner had submitted his wealth-tax returns, for the assessment years 1975-76 to 1981-82. The other three partners, though assessable to wealth-tax in their individual capacity, in respect of the value of their share interest in the partnership firm (along with the value of other assets owned by them), had neither submitted their wealth-tax returns nor the department issued any notice calling for the returns, for the assessment years 1975-76 to 1982-83.

While working out the partner's (of the partner who filed the return) share interest in the assets of the firm, for the

assessment year 1981-82, in September 1981, the Assessing Officer took the value of the building (came into the possession of the firm in May 1965 and valued at Rs. 3,45,000) which was being used as hotel (lodging business), at its book value of Rs. 2,56,838, as on 31st December, 1980, relevant to the assessment year 1981-82. The market value of the building was, however, neither ascertained nor the case referred to the departmental valuation cell for valuation as prescribed in the Act, despite the steep increase in the value of immovable properties during the period from 1965 to 1980. Income derived from the building by way of lodging charges|rent went up from Rs. 1,00,620 in the assessment year 1975-76 to Rs. 2,34,780 in the assessment year 1981-82. In the light of these factors, even if a moderate rate of appreciation in the value of the immovable property from year to year, viz., 10 per cent is adopted, the total short levy of tax (including the tax on the value of share interest in the firm that escaped assessment in the hands of the other three partners) amounted to Rs. 66,915, for the assessment years 1975-76 to 1982-83.

Besides, penalties for delay in filing the returns and concealment of wealth in the case of three partners is also leviable.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(b) While working out the share interest of seven partners in the wealth of a firm, the value of assets, such as buildings (excluding godown), motor vehicles, shop furniture, machinery owned by the firm, was adopted at their depreciated book value at Rs. 29,03,395 continuously for twenty five years from the assessment years 1957-58 to 1982-83, though it was known to the Assessing Officer that the market value of the assets had gone up by more than 20 per cent in view of the following facts noticed from the Income-tax assessment records of the firm :—

(1) As against the book value of Rs. 7.06 lakhs of godowns as on Diwali 1975, their market value was determined at Rs. 20.21 lakhs by the Departmental Valuer and upheld at Rs. 10 lakhs in appeal by the Appellate Tribunal;

(2) On sale of assets (buildings and motor vehicles) in the previous years relevant to assessment years 1981-82 and 1982-83, profits determined under the provisions of Income-tax Act, 1961, showed rise of market price by 33-1|3 per cent and 100 per cent in the respective assessment years;

(3) on sale of similar assets by another assessee assessed in the same ward, profit determined under the relevant provisions of Income-tax Act, 1961, showed rise of market price by more than 400 per cent. Further, the matter was not referred to the valuation cell for valuation as required under the Board's instructions of December 1971.

If in the wealth-tax assessments of the seven partners (Hindu undivided families), completed in February and March 1983, for the assessment year 1982-83, a modest rise in the value of assets owned by the firm at the rate of 100 per cent in the case of buildings and 50 per cent for other assets is adopted the value of the interest in the firm of all the seven partners was under-assessed by Rs. 16,44,300, with consequent aggregate short levy of tax of Rs. 74,375.

The paragraph was sent to the Ministry of Finance in September 1984, their reply is awaited (November 1984).

(c) Three individuals had substantial interest in a company either directly by themselves or through a partnership firm constituted by them. While submitting the returns of wealth, for the assessment years 1971-72 to 1978-79, the three individuals furnished the details of the break-up value of the shares owned by them in the said company. The Wealth-tax Officer, between September 1974 and February 1983, however, determined the market value of the said shares in the company on the basis of the break-up value at Rs. 131.25, Rs. 168, Rs. 180, Rs. 168, Rs. 189, Rs. 170, Rs. 188 and Rs. 184 per share, for the respective assessment years 1971-72 to 1978-79.

However, in computing the wealth of the firm, the book value of Rs. 100 per share as per its balance-sheet was adopted as market value in respect of the 4350 shares owned by the firm in the above company, for all the assessment years 1971-72 to 1978-79, instead of the market value as determined by the Assessing Officer in the case of the individuals. As a result of the under-valuation of the net wealth in the hands of the firm, the value of share interest of the partners in the said firm was under-stated to the extent of Rs. 23,24,450, with consequent short levy of tax of Rs. 55,540.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(d) Five assessees, for the assessment year 1978-79, returned the values of their interest in a firm (Rs. 9,34,913), in which they were partners, on the basis of their capital as well as current account in the books of the firm as shown in the balance-sheet in the accounting year ending on 31 August, 1977. The same valuation of partner's interest in the firm was adopted by the Assessing Officer and the wealth-tax assessments completed between November 1982 and February 1983 accordingly.

In the case of another assessee who was also a partner in the said firm his interest in the firm for the same assessment year was included in his wealth and was taken on the basis of the valuation report of Departmental Valuation Officer, who valued his interest at Rs. 3,40,171, as against Rs. 1,19,987 returned by him on the basis of share capital|current account in the books of the firm.

The non-adoption of the valuation of partner's interest in the firm made by the Departmental Valuation Officer, in the case of the other five assessees resulted in under-assessment of wealth of Rs. 17,15,626, with consequent short levy of tax of Rs. 38,744.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

C. *Unquoted/quoted equity shares*

(i) An assessee held 1,620 equity shares of Rs. 100 each in a company. While completing the wealth-tax assessment of the assessee, for the assessment year 1978-79, in March 1981, the assessing officer had taken the value of these shares at Rs. 102.94 per share. While checking the assessment, in July 1981, the Internal Audit Party of the department, pointed out that there appeared to be a mistake in the valuation of the shares due to double deduction of the advance tax (Rs. 29,84,568) paid by the company and that the correct value of the share was required to be worked out. It was noticed in audit (June 1983) that the assessments of two other assessees holding shares in the same company, for the same assessment year, had been revised (March 1983) by adopting the value of Rs. 280 per share, determined (February 1983) by the Commissioner of Wealth-tax. However, no revision of assessment in respect of the above assessee had been made adopting the value of Rs. 280 per share till June 1983, when the omission was pointed out in Audit.

Further, the same mistake was noticed for the assessment years 1979-80 and 1980-81, completed in November and December 1981, respectively. Based on audit objection the Wealth-tax Officer issued notices for re-opening the assessments, for the assessment years 1979-80 and 1980-81, in the case of two other assessees mentioned above, but no similar proceedings had been initiated to re-open the assessments of the assessee in question.

The omission resulted in total under-assessment of wealth of Rs. 13,17,060, with consequent short levy of tax of Rs. 50,757, for the assessment years 1978-79 to 1980-81.

The Ministry of Finance have accepted the mistake (December 1984).

(ii) For valuation of unquoted equity shares of investment companies, the Central Board of Direct Taxes in their circular of March 1982, revising their earlier circular dated 31 October 1967, for adoption of the average of break-up value and capitalised value on yield basis, have observed that the yield method on the basis of maintainable profits is the generally applicable method. The valuation of shares of investment companies having a wholly owned subsidiary should be worked out treating the parent investment company and the wholly owned subsidiary as one single company.

In computing the net wealth of an assessee, for the assessment years 1978-79 and 1979-80, in March 1983, the Wealth-tax Officer took the value of 173 unquoted equity shares of an investment company (which had a wholly owned subsidiary company) held by the assessee at Rs. 9,586 and Rs. 10,953 respectively, per share as returned by the asstssee. The value of these shares was determined on the basis of average of the valuation as per 'break-up method' and 'yield method' under Board's instructions of October 1967. However, on the basis of Board's revised instructions of March 1982, the value of each share would work out to Rs. 13,739 and Rs. 14,545, for the assessment years 1978-79 and 1979-80, respectively. The incorrect valuation adopted by the department resulted in total under-assessment of wealth of Rs. 13,39,890, with consequent short levy of tax of Rs. 45,260.

The Ministry of Finance have accepted the mistake (November 1984).

(iii) Under the Wealth-tax Act, 1957, the value of any property shall be estimated to be the price which it would fetch if sold in the open market on the valuation date. In the case of quoted shares, the relevant quotations in the stock-exchange represented the price the shares would fetch if sold in the open market on the valuation date.

In computing the net wealth of four individuals, for the assessment years 1981-82 and 1982-83, the value of 38,840 shares, held by them in four companies, was taken as returned by the assessees instead of adopting the stock-exchange quotations for the shares as market price on the relevant valuation dates. This resulted in under-valuation of shares by Rs. 20,55,400, with consequent short levy of tax of Rs. 55,287.

The Ministry of Finance have accepted the mistakes in all the four cases.

D. *Gold ornaments*

An assessee's wealth included 600 tolas (6,995 grams) of gold ornaments at the rate of Rs. 150 per tola (after deduction of impurities) upto the assessment year 1974-75. For the assessment years 1978-79 to 1981-82 (assessments completed in March 1982), the assessee had returned the same value of Rs. 150 per tola for 600 tolas of gold. The Wealth-tax Officer also completed the assessments in March 1982 accordingly without taking into account the appreciation in the value of gold. The value of 10 grams of gold (after giving allowance at 15 per cent for impurities), on the respective valuation dates relevant to four assessment years 1978-79 to 1981-82, worked out to Rs. 565, Rs. 797, Rs. 1,130 and Rs. 1,445 respectively. Omission to include the appreciation in the market value of gold resulted in under-assessment of wealth of Rs. 23.95 lakhs, with consequent short levy of tax of Rs. 50,750.

The Ministry of Finance have accepted the mistake (August 1984).

E. *Private trusts*

In the case of a private discretionary trust under which the trustees had been given wide discretionary powers for distribution of income and corpus of the trust among various beneficiaries, the Appellate Tribunal held in May 1981, that the valuation of the assets held by the trust for the purpose of wealth-tax on the

basis that the value is equal to the sum of the interests of the life tenant and remainderman determined on actuarial principles is inapplicable. According to the Tribunal, in such cases, the value of the interest of the beneficiaries is to be taken as equal to the value of the entire corpus of the trust including the income held by it on the several valuation dates.

The wealth-tax assessments of many discretionary trusts of a family group under the jurisdiction of an income-tax ward were finalised in accordance with the decision of the Tribunal mentioned above. However, in respect of 18 trusts whose wealth-tax assessments, for the assessment years 1978-79 and 1979-80, were finalised during October and November 1982, the net wealth assessable in the hands of the trusts was determind as the total of life interest and interest of remainderman both estimated on actuarial principles. As these trusts were also discretionary trusts wherein not only the trustees but beneficiaries also had been given discretionary powers regarding distribution of income and corpus of the trusts, the decision of the Tribunal was applicable to these 18 cases also. Omission to do so resulted in aggregate under-assessment of wealth of Rs. 36,09,084, with consequent short levy of wealth-tax of Rs. 54,126, for the assessment years 1978-79 and 1979-80.

The Ministry of Finance have accepted the mistake (December 1984).

4.06 *Incorrect computation of net wealth*

(i) Under the Wealth-tax Act, 1957, where at the time of making the assessment, it is brought to the notice of the Wealth-tax Officer that a partition has taken place among the members of the Hindu undivided family and the Wealth-tax Officer, after inquiry, is satisfied that the joint family property has been partitioned as a whole among the various members or groups of members in definite portions, he shall record an order to that effect and shall make assessment on the net wealth of the family as such. Further, where the Wealth-tax Officer is not so satisfied, he may, by an order declare that such family shall be deemed for the purposes of the Act to continue to be Hindu undivided family liable to be assessed as such. It has been judicially held (October/November 1970) that inspite of the partition in the sense of severance of joint status having taken place amongst the members of the Hindu undivided family, if the Wealth-tax Officer is not satisfied that there has been a partition by metes

and bounds, even though there has been a severance of status, the family shall be deemed for the purposes of the Wealth-tax Act to continue to be a Hindu undivided family.

A co-parcener in a Hindu undivided family, filed a civil suit in a court, in October 1966, claiming partition of family assets. Subsequently, all the three members of the family, filed an application in January 1976, for compromise and the Court passed a consent decree in January 1976, which was made effective from October 1966, permitting partition of all assets of the family excepting some immovable properties.

The regular wealth-tax assessments of the above Hindu undivided family, for the assessment years 1967-68 to 1975-76, were completed in March 1979 and March 1980 on a net wealth ranging between Rs. 10,49,000 and Rs. 22,53,250. In appeal the assessments, for the assessment years 1968-69 to 1975-76, were set aside by the Commissioner of Wealth-tax (Appeals), in April 1980, directing the assessing officer to make the assessments *de novo* taking into account the judgment of the civil court.

In pursuance to the appellate orders, the Wealth-tax Officer, completed the reassessments, for the assessment years 1967-68 to 1975-76, in March 1983, for the assessment year 1967-68 on a net wealth, at Rs. 10,49,000 as originally assessed and at 'nil' amount, for the assessment years 1968-69 to 1975-76, on the basis of the decision of the court. The re-assessments for the assessment years 1968-69 to 1975-76, as 'nil' were not in order as there was no physical partition of the family properties into definite portions amongst the family members during the previous years relevant to the assessment years. Further, in the income-tax assessment of the family, for the assessment year 1976-77, completed in February 1979, the Income-tax Officer recorded his findings that the partition by the court order would be treated as a partial partition and would be effective from 30 March 1976 (assessment year 1976-77). The incorrect status adopted by the department resulted in under-assessment of wealth by Rs. 132.18 lakhs (as assessed in the original assessments) with consequent short levy of tax (including additional wealth-tax) of Rs. 6,28,150, for the assessment years 1968-69 to 1975-76.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(ii) Under the Wealth-tax Act, 1957, in the case of an individual being a member of Hindu undivided family, any property having been the separate property of the individaul has, at

any time after the 31 day of December 1969, been converted by the individual into property belonging to the family through the act of impressing such separate property with the character of property belonging to the family, then, for the purpose of computing the net wealth of the individual the converted property, in so far as attributable to the interest of the individual in the property of the family, shall be deemed to be assets belonging to the individual and not to the family. These provisions shall be applicable for the assessment year 1972-73 and onwards. From 1 April 1976 the entire value of the converted property is includible as the wealth of the transferor.

It was seen from the gift-tax return for the assessment year 1971-72, filed in June 1971, that an assessee had impressed 17,500 shares of a company to a Hindu undivided family in February 1971. The said Hindu undivided family consisted of the assessee and his two brothers. Since the assessee being an individual had converted his separate property into property belonging to Hindu undivided family after 31 December 1969, one third of the converted property was required to be included in the assessee's net wealth for the assessment years 1972-73 to 1975-76, and the full value of the converted property for the assessment year 1976-77 and onwards. The valuation date was 31 March each year.

It was seen from the wealth-tax assessment records of the assessee that the addition on this account was made, in the assessment years 1972-73 to 1974-75, by rectifying the assessments which were cancelled (April 1983) on technical ground by the Commissioner of Income-tax (Appeals). So far as the assessment year 1975-76 is concerned, neither the assessment order was on record nor the miscellaneous folder made available. For the assessment years 1976-77 to 1978-79 the value of the shares (converted property) of Rs. 5,42,500, Rs. 3,10,625 and Rs. 1,66,250, respectively, was not included by the assessee in his wealth-tax returns. The department also apparently lost sight of this aspect and finalised the assessments without including the value of the converted property in the assessee's wealth. This resulted in short levy of tax of Rs. 62,457.

The Ministry of Finance have accepted the mistake (August 1984).

(iii) In the computation of net wealth, the Wealth-tax Act, 1957, does not permit deduction of tax liabilities which are outstanding for more than twelve months as on the valuation date.

In the wealth-tax assessments, an individual assessee was allowed deduction towards tax liabilities of Rs. 2,61,010, Rs. 3,06,089, Rs. 3,79,100, Rs. 78,371 and Rs. 1,20,550 in the assessment years 1977-78 to 1981-82. As the liabilities were outstanding for more than 12 months, no deductions were admissible. The incorrect allowance, together with a mistake in calculation of tax, for the assessment year 1980-81, accounted for aggregate short levy of wealth-tax of Rs. 54,641.

The paragraph was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(iv) In computing (January 1983) the net wealth of an individual for the assessment year 1981-82, the assessing officer had incorrectly taken the value of shares held by the assessee on the valuation date (31-12-1980) at Rs. 5,700 instead of the correct market value of Rs. 5,07,000 returned by the assessee. This omission resulted in under assessment of wealth of Rs. 5,01,300, with consequent under charge of tax of Rs. 20,039.

The Ministry of Finance have accepted the mistake (July 1984).

4.07 *Incorrect exemptions and deductions*

(i) Under the Wealth-tax Act, 1957, one building in the occupation of a Ruler and declared by the Central Government as his official residence under the provisions of the Merged States (Taxation Concession) Order, 1949, or of the Part B States (Taxation Concession) Order, 1950, was exempt from wealth-tax. Consequent on the abolition of privileges of the Rulers under the Abolition of Privileges Act, 1972, the Wealth-tax Act was amended to provide that the exemption would be available only in respect of a building which immediately before 28 December 1971 was declared under the aforesaid provisions as the official residence of a Ruler.

For the assessment years upto and including the assessment year 1975-76, the ex-Ruler of a princely state was being granted exemption from the wealth-tax in respect of a palace declared by the Central Government in May 1954 as his official residence. The State Government acquired this palace in May 1975 for public purposes and the wealth-tax assessment of the ex-Ruler, for the assessment years 1976-77 to 1979-80, were completed, in December 1978—November 1979, without allowing the exemption for the value of the official residence. At the request of the

ex-Ruler, the Central Government notified in August, 1980 another palace valued at Rs. 11,20,000 as his official residence effective from the date of acquisition of the exempted palace by the State Government. In view of this notification, the department rectified (March 1981), the wealth-tax assessments of four assessment years (1976-77 to 1979-80) exempting the value (Rs. 11,20,000) of the newly declared palace from wealth-tax and made a total refund of Rs. 2,34,683.

The exemption granted and the consequent refund allowed was not in order as :—

(1) the notification issued in August 1980 declared the second palace as the ex-Ruler's official residence only with effect from May 1975 and not from a date prior to 28 December 1971, as required under the amended provisions of the Wealth-tax Act.

(2) the second palace belonged to the joint family of the Ruler having been thrown into the family hotchpot before 28 December 1971 and the exemption contemplated under the Wealth-tax Act is in respect of the official residence of the Ruler.

The paragraph was sent to the Ministry of Finance in October 1984; their reply is awaited (November 1984).

(ii) In computing the net wealth of an individual or Hindu undivided family not resident in India or resident but not ordinarily resident during the year ending on the valuation date, the exemption admissible, *inter alia,* includes the value of the assets in India represented by any loans or debts owing to the assessee, in any case, where the interest payable thereon is totally exempt from income-tax. Though this provision has grouped together both 'non-resident' and 'resident but not ordinarily resident', in effect the exemption is admissible to non-resident assessee only as the Income-tax Act provision exempts interest income of non-residents only. This position was changed only with effect from 1 April 1982 onwards after the relevant provisions of the Income-tax Act/ Wealth-tax Act were amended by the Finance Act, 1982.

A person filed wealth-tax returns, for the assessment years 1975-76 to 1977-78, declaring the residential status as 'resident but not ordinarily resident' had, claimed exemption in respect of amounts kept in fixed deposit in Non-Resident (External) Account and did not include their value in the net wealth returned by him. The claim was accepted in the wealth-tax assess-

ments of the assessee, for the assessment years 1975-76 to 1977-78, finalised in May 1980, March 1981 and March 1982, respectively. In the income-tax assessment of the individual for the assessment year 1979-80, the Income-tax Officer brought to tax interest income and had also directed that earlier assessments were to be re-opened for taxing the interest income. As the exemption was not admissible to the assessee, his status being 'resident but not ordinarily resident', there was under-assessment of wealth of Rs. 20,95,253, with consequent short levy of tax of Rs. 81,784.

The Ministry of Finance have accepted the mistake (September 1984).

(iii) Under the Wealth-tax Act, 1957, where an assessee is a partner in a firm, the value of his interest in the net assets of the firm is to be included in his net wealth. As a partnership firm as such is not a chargeable person under the Act it is not entitled to any exemptions under the Act. Also what is included in the partner's assessment is the value of his interest in the firm, and not values of any particular assets so that exemptions related to specified assets such as house property are not available to the partner also even if the firm's property includes such assets. It was held by the Madras High Court (August 1975) that neither the firm nor the partners are entitled to any exemptions in such cases.

The Central Board of Direct Taxes in their circular of July 1974 expressed the view that exemption under the Act could not be granted to a partner if the house belongs to a firm. The Board also stated that the larger issue whether any or some or all of the exemptions listed in the Act are available while computing the net wealth of the firm under the Wealth-tax Rules, 1957, was under consideration. Even after a lapse of over nine years, the Board have not issued any instructions for the guidance of the assessing officers, with the result that the assessing officers have not maintained uniformity in assessment.

In the wealth-tax assessments of thirteen assessees, who were partners in a firm, the department incorrectly allowed exemption in respect of a house owned by the firm, for the assessment years 1977-78 to 1982-83. This resulted in aggregate short levy of wealth-tax of Rs. 49,788.

The Ministry of Finance have accepted the mistake (September 1984).

(iv) Under the Wealth-tax Act, 1957, one house or part of a house belonging to an assessee, is not includible in net wealth, provided, if the value thereof exceeds Rs. 1 lakh, the exemption is available only for Rs. 1 lakh. So far as Rulers of former States are concerned, the Act exempts any one building in the occupation of a Ruler being a building which immediately before the commencement of the Constitution (Twenty-Sixth Amendment) Act, 1971 was his official residence. The general provision applicable to all assessees contemplates exemption even for part of a building, but the specific provision applicable to former Rulers, does not, however, provide for such a contingency.

In a Notification issued in May 1954, the Central Government declared two palaces owned by a former Ruler as the official residences as required under the Merged States (Taxation Concessions) Order, 1949, and Part B States (Taxation Concessions) Order, 1950. As exemption from wealth-tax is, however, available only in respect of one palace, the Central Board of Direct Taxes in their letters dated 5 May and 14 May 1958 indicated the option exercised by the former Ruler for exemption for one palace. The Central Board of Direct Taxes clarified in the letters cited that the palace should be taken to include outhouses, garage, guest house and lands appurtenant thereto situated within the same compound or its immediate vicinity.

In the previous year relevant to the assessment year 1975-76, the former Ruler let out a portion of the palace in respect of which option for wealth-tax exemption was exercised and the income therefrom was given to assessment. The wealth-tax exemption for the building was, however, continued to be allowed to the assessee in the assessments for the assessment years 1975-76 and 1976-77. By letting out the palace the Central Government's declaration of the building as his official residence was rendered void, and, therefore, the exemption allowed for the building from wealth-tax was not in order.

Further, jewellery, gold ornaments and silver articles were valued for the assessment years 1975-76 and 1976-77 as in the assessment year 1974-75, despite steep increase in market value of these precious metals in the later years. Old gold and silver coins were not included in the net wealth by incorrectly treating them as pieces of art collection.

The department revised the assessments (February 1984) including the value of the rented portion of the building for wealth-tax purposes and rectifying other mistakes, raised additional demand of tax of Rs. 36,347.

In the absence of a declaration by the Central Government for the portion of the building in use by the assessee as his official residence in terms of relevant statute, exemption allowed to it was not in order.

The Ministry of Finance have accepted the mistake (December 1984).

(v) Under the Wealth-tax Act, 1957, the value of interest of an assessee in the assets (excluding any land or building or any rights in any land or building) forming part of an industrial undertaking belonging to a firm or an association of persons of which the assessee is a partner or a member, as the case may be, is exempt upto a maximum limit of Rs. 1.5 lakhs. Industrial undertaking for this purpose is defined as an undertaking engaged in the business of generation or distribution of electricity or any other form of power or in the construction of ships or in the manufacture or processing of goods or in mining. The definition is almost similar to the definition of an 'industrial company' appearing in the annual Finance Acts for purposes of concessional levy of income-tax. In a case decided by the Bombay High Court in April 1980 (126 ITR 377), it was held that the definition of industrial company covers only that construction company which is engaged in the construction of ships and by implication excludes a company which is engaged mainly or otherwise in the construction of anything other than ships. In other words, applying the ratio of the decision, if an industrial undertaking is engaged in the construction of buildings, it is not entitled for the aforesaid exemption under the Wealth-tax Act.

In the assessments of a Hindu undivided family, for the assessment years 1973-74 to 1980-81 (assessments completed in January 1978 and March 1981), exemption was given on the value of the interest of the assessee in assets of a firm engaged in construction of buildings. The incorrect exemption resulted in under-assessment of aggregate wealth of Rs.11,76,618, with consequent short levy of wealth tax of Rs 33,147 for all the assessment years.

The Ministry of Finance have accepted the mistake (August 1984).

4.08 *Mistakes in application of rates of tax, calculation of tax, etc.*

(i) Under the Wealth-tax Act, 1957, where shares of beneficiaries in a private trust are indeterminate or unknown, wealth-

tax is levied as if the persons on whose behalf or for whose benefit the assets are held are in individual, at the rates specified in the Schedule to the Act or at the flat rate of one and one-half per cent whichever is more beneficial to revenue.

While completing the assessment of a discretionary trust, for the assessment year 1978-79, in March 1983, the department computed the net wealth of the trust at Rs. 1,95,10,476 and raised a demand of tax of Rs. 2,92,657 by applying the uniform rate of one and one-half per cent instead of the higher rates prescribed in the Schedule to the Act, which was more beneficial to revenue. The tax leviable as per the Schedule to the Act worked out to Rs. 6,34,408. The mistake in the application of tax resulted in under charge of tax of Rs. 3,41,751.

The Ministry of Finance have accepted the mistake (September 1984).

(ii) From the assessment year 1974-75, the Schedule to the Wealth-tax Act, 1957, was amended to provide for a higher rate of tax for every Hindu undivided family (HUF) having at least one member with assessable net wealth exceeding Rs. one lakh upto the assessment year 1979-80 and Rs. one lakh and fifty thousands from the assessment year 1980-81 and subsequent years. Other cases of Hindu undivided family attract tax at lower rates.

In the assessments of four such Hindu undivided families, in four commissioners' charges, the prescribed higher rates were not applied in the wealth-tax assessments for the assessment years 1974-75 to 1978-79 and 1981-82. This resulted in aggregate short levy of tax of Rs. 1,03,013.

The Ministry of Finance have accepted the short levy in all the four cases.

(iii) The Finance Act, 1974, revised upwards the rates of wealth-tax from the assessment year 1975-76, in the case of every Hindu undivided family which has at least one member whose net wealth assessable for the assessment year exceeded Rs. 1,00,000.

The assessments of five such Hindu undivided families were completed in March 1981, for the assessment year 1975-76, on net wealth ranging between Rs. 6,40,510 and Rs. 7,87,230. The assessing officer had, however, applied the lower rates of tax applicable to the assessment year 1974-75 instead of the revised

(higher) rates applicable to the assessment year 1975-76. Further, in the assessment of one of the assessees, the net wealth was short computed by Rs. 1,14,000, due to totalling mistake. These mistakes resulted in short levy of tax of Rs. 36,927.

The paragraph was sent to the Ministry of Finance in August 1984 ; their reply is awaited (November 1984).

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

Under the Wealth-tax Act, 1957, before its amendment by the Finance Act, 1976, where the net wealth of an individual or a Hindu undivided family included buildings or lands (other than business premises) or any rights therein, situated in an urban area additional wealth-tax was leviable on the value of such urban assets exceeding rupees five lakhs.

(i) The net wealth of six individuals and a Hindu undivided family, for the assessment years 1969-70 and 1971-72 to 1976-77, included urban immovable properties valued at Rs. 153.20 lakhs on which additional wealth-tax was not levied/short-levied by the department. This resulted in under-charge of tax of Rs. 2,94,781 in these cases.

The Ministry of Finance have accepted the under-charge of tax in all the seven cases.

(ii) An individual had reversionary interest in respect of an urban immovable property, the life interest thereon being vested with his mother. The wealth-tax assessments of this individual, for the assessment years 1970-71 to 1976-77, were completed, in December 1982 and March 1983, to bring to tax his reversionary interest valued at Rs. 53,70,088 in the urban property. The value of the urban property included in the assessments so made exceeded the prescribed limits and attracted levy of additional wealth-tax. However, the additional wealth-tax was not levied by the department. The omission resulted in under-charge of tax of Rs. 92,496.

The Ministry of Finance have accepted the mistake (November 1984).

(iii) An assessee filed the wealth-tax return, for the assessment year 1976-77, in March 1977 and declared the net wealth of Rs. 77,435. The Wealth-tax Officer finalised (March 1981) the assessment to the best of his judgment and assessed the net wealth at Rs. 16,52,904. The difference between the returned

and assessed net wealth was mainly due to assessment of a plot of land owned by the assessee at Rs. 13,28,000, on the basis of the valuation report of the Departmental Valuation Officer (March 1980) as against the returned value of Rs. 1,41,252.

The assessment records including valuation report disclosed that the net wealth of the assessee, included urban immovable properties valued at Rs. 14,48,848. However, additional wealth-tax was not levied by the department. The tax leviable amounted to Rs. 62,434, including a mistake in the tax already levied.

The Ministry of Finance have accepted the mistake and have stated (October 1984) that assessment has been rectified.

4.10 *Non-levy/short levy of penalty*

Under the Wealth-tax Act, 1957, penalty is leviable where the assessing officer is satisfied that an assessee has, without reasonable cause, failed to furnish the wealth-tax return within the prescribed time. Upto 31 March 1976, the penalty leviable was a sum, equal to one-half per cent of the net wealth assessed for every month, during which the default continued, as reduced by the amount of initial exemption but subject to a maximum of equal to one hundred per cent of net wealth assessed. The Act was amended with effect from 1 April 1976, to provide that the penalty should be equal to two per cent of the assessed tax for every month during which the default continued. As regards cases where the default took place prior to the amendment and continued after the amendment, the Central Board of Direct Taxes issued instructions (February 1977) that such default being a continuous one, the penalty should be imposed for every month during which the default continued by applying the unamended provisions for the period prior to 1 April 1976 and the amended provisions thereafter. However, in April 1981, the Supreme Court held that —

(a) the default was not continuous but was a single default committed on the last date on which the return had to be filed, and

(b) the penalty should be imposed in accordance with the law in force on the date of default.

In view of the judgment, the aforesaid instructions of February 1977 were withdrawn by the Board in October 1981.

(i) Two individuals did not file their returns (due date 30 June 1975) of net wealth, for the assessment year 1975-76. The assessments were completed (February 1980) by the department *ex-parte* on the net wealth of Rs. 18,20,000 and Rs. 15,70,000 respectively and demands of Rs. 65,000 and Rs. 45,600 were raised. Penalty of Rs. 1,29,152 and Rs. 85,500, respectively, was levied in April 1982 by the department for non-filing the returns of net wealth in these two cases. The penalty was incorrectly computed by the department at one-half per cent of assessed net wealth for the period from the due date of filing of return to 31 March 1976 under the law then in force and at two per cent of the assessed tax from 1 April 1976 to the date of assessment.

But as per the law enunciated by the Supreme Court in April 1981, the penalty leviable in both the cases would work out to Rs. 8,77,250. The omission to rectify the levy of penalty resulted in short levy of penalty of Rs. 6,62,598.

The Ministry of Finance have accepted the mistake (September 1984).

(ii) An individual, filed his returns of net wealth, for the assessment years 1970-71 to 1975-76, on 1 January 1976, i.e., long after the due dates of the relevant assessment years. The period of delay ranged between 5 months and 65 months. While completing the assessments in March 1979 and March 1980, a total penalty of Rs. 9,002 was levied by the Wealth-tax Officer, for the delay in filing of the returns. The penalty levied was incorrectly computed at the rate of 2 per cent of the assessed tax for each month of default instead of at the rate of one-half per cent of the net wealth assessed for each month of default as per provisions of law on the date on which returns had to be filed.

On the basis of the principle laid down by the Supreme Court in its decision of April 1981, the penalty leviable would work out to Rs. 2,51,412 The mistake resulted in short levy of penalty of Rs. 2,42,410.

The paragraph was sent to the Ministry of Finance in July 1984; their reply is awaited (November 1984).

(iii) No order imposing a penalty can be passed after the expiry of 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 are completed.

For the assessment years 1969-70 to 1976-77, an individual filed wealth-tax returns, between February 1972 and July 1979, much later than the respective due dates. The periods of delay ranged between 2 months and 36 months. For the belated filing of the returns, the assessing officer initiated penalty proceedings, for the assessment years 1969-70 to 1975-76, in March 1978 and passed an order, in March 1981, for initiation of penalty proceedings for the assessment year 1976-77. The penalty proceedings were not, however, finalised by March 1980 for the assessment years 1969-70 to 1975-76 and by March 1983 for the assessment year 1976-77 as prescribed under the Act, though the assessee had furnished (February 1979) replies to the penalty notices for the assessment years 1969-70 to 1975-76. Further, the Commissioner of Wealth-tax had also rejected assessee's petition for waiver of penatly, in November 1978, for the assessment years 1969-70 to 1971-72. Consequently, levy of penalty had become time-barred resulting in loss of revenue. The minimum penalty leviable would work out to Rs. 88,823 for the assessment years 1969-70 to 1976-77.

While accepting the omission in principle the Ministry stated (November 1984) that levy of penalty being discretionary it cannot be said that the Wealth-tax Officer would have definitely levied penalty and failure to finalise proceedings resulted in definite revenue loss. The reply of the Ministry is presumptuous.

(iv) The Wealth-tax Act, 1957, provides that where any tax is payable on the basis of any return, after taking into account the amount of tax, if any, already paid, the assessee shall be liable to pay such a tax before furnishing the return and the return shall be accompanied by proof of payment of such tax. If any assessee fails to pay the tax or any part thereof, the assessing authority may impose a penalty calculated at the rate of two per cent of such tax remaining unpaid for every month during which the default continued. The Central Board of Direct Taxes clarified in March 1974 that in cases where penal action is not initiated, the assessing officers should properly record the reasons in the order sheet or append a note to the assessment order giving reasons thereof.

(a) In the case of an assessee whose wealth mainly consisted of shares allocated to him in several trusts, the returns of net wealth, for the assessment years 1978-79 to 1981-82, were filed by the trustees without paying the tax in full on self-assessment.

Penalty for the default working out to Rs. 61,722 for these assessment years was, however, not levied and specific reasons were not also recorded for the omission.

The Ministry of Finance have accepted the mistake (September 1984).

(b) An individual filed his return of wealth of Rs. 32,25,291, for the assessment year 1977-78, in August 1977. The assessee paid self-assessment tax of Rs. 32,790 instead of Rs. 86,635 actually payable by him on the basis of return. The assessing officer initiated penalty proceedings in October 1980. Thereafter further action was not pursued. Orders dropping the penalty proceedings were also not on record. The omission resulted in non-levy of penalty of Rs. 52,641.

The Ministry of Finance have accepted the mistake (November 1984).

4.11 *Miscellaneous.*

(i) *Issue of invalid notice*

In August 1983, mistakes in levy of wealth-tax and additional wealth-tax on an assessee assessed as legal representative of a person (deceased), for the assessment years 1972-73 to 1976-77, were pointed out in audit. On local verification (May 1984) of the reply of the department (March 1984) accepting the mistakes, the following further developments were noticed :—

To assess the wealth of the above person, who died in November 1971, a notice was issued by the department, in February 1979, to his daughter as his legal representative, treating the case as one of wealth escaping assessment, for the assessment years 1972-73 to 1978-79. The assessments for all the above assessment years were completed in February 1983 by the Wealth-tax Officer to the best of his judgment.

On an appeal by the deceased's daughter, the Commissioner (Appeals) quashed, in March 1984, all the assessments on the ground that notice under the relevant provisions of the Wealth-tax Act, 1957, which was not a mere formality, was not issued to the daughter (the deceased's only child) in her individual capacity. The notice issued to her as a legal representative of the deceased was legally incorrect. Under the circumstances the

Commissioner held that the assessments were not valid. The department decided (May 1984) that no further appeal to the Tribunal was necessary.

In the meantime the Wealth-tax Officer on his own volition issued notice in January 1983 to the deceased's daughter in the status of individual, for re-opening the assessments, for the assessment years 1974-75 and onwards. However, no notice was issued for the assessment years 1972-73 and 1973-74 as the assessments for these years were time-barred. The Wealth-tax Officer also deleted the demands of Rs. 75,424 and Rs. 1,67,731 for the assessment years 1972-73 and 1973-74, respectively, from the books of the department.

The issue of invalid notice by the Wealth-tax Officer resulted in loss of revenue by way of wealth of Rs. 2,37,347. Further, it was noticed that the total wealth of the assessee included urban assets on which additional wealth-tax for the assessment year 1972-73 was omitted to be levied. Taking into account the additional wealth-tax of Rs. 84,381 and the wealth-tax actually payable for the assessment year 1972-73, the total loss of revenue worked out to Rs. 3,29,654.

The Ministry of Finance have accepted the mistake (October 1984).

(ii) *Inordinate delay in taking action on appellate order*

The Central Board of Direct Taxes issued instructions in August 1976, and, *inter alia,* reiterated these instructions in February 1977, that all appellate orders of the Income-tax Appellate Tribunal should be given effect to promptly within a fortnight of receipt thereof by the Income-tax Officers.

The wealth-tax assessments of an ex-Ruler of an erstwhile Indian State, for the assessment years 1966-67 to 1971-72, finalised in March 1979, included, *inter alia,* the value of a palace owned by the assessee. In appeal, the Commissioner of Wealth-tax (Appeals), allowed exemption, in July 1979, for the value of the said palace and his order was given effect to in September 1979. The department did not, however, accept the decision of the Commissioner of Wealth-tax (Appeals) and preferred an appeal with the Appellate Tribunal for all the assessment years. The Tribunal restored the order of the Wealth-tax Officer, in December 1980, holding that the

value of the palace was includible in the net wealth of the assessee as on relevant valuation dates. Though the order of the Tribunal was required to be given effect to within a fortnight of the receipt of the order as per executive instructions issued by the Board in February 1977, the relevant assessments had not been revised till December 1982 when the omission was pointed out in audit. The delay in giving effect to the appellate order resulted in postponement of raising of demand of tax of Rs. 2.81 lakhs and recovery thereof.

The Ministry of Finance have accepted the mistake (November 1984).

(iii) *Inordinate delay in remedial action on internal audit objection*

According to the executive instructions issued in 1977, mistakes pointed out by internal audit parties of the department should be rectified by the assessing authorities promptly; the remedial action should be initiated within a month and completed, as far as possible, within three months from the date of receipt of the report of internal audit.

The wealth tax assessments of an individual, for the assessment years 1973-74, 1974-75 and 1975-76, were completed in March 1979. The internal audit party of the department scrutinised these assessments and pointed out in August 1979 that the correct value of immovable properties as determined by the departmental valuer had not been adopted, resulting in short levy of tax of Rs. 93,870. Though a note in this regard was kept in the order sheet in February 1980, no action was taken to revise the assessments till November 1982.

On the inordinate delay in rectifying the mistake being pointed out in audit (November 1982), the Ministry of Finance intimated that the assessments have been rectified and additional demand of Rs. 93,828 raised.

(iv) *Omission to obtain orders of appropriate appellate authority*

By an amendment to the Wealth-tax Act, 1957, made by the Finance (No. 2) Act, 1971, exemption in respect of the value of jewellery in the computation of net wealth hitherto allowed, was withdrawn retrospectively with effect from 1 April 1963.

The wealth-tax assessments of two individuals assessed in the same ward, for the assessment year 1964-65 to 1968-69, were completed in February 1970, including the value of jewellery. On appeal by the assessees, the Appellate Assistant Commissioner allowed in April 1970 exemption in respect of jewellery with reference to a Supreme Court decision (February 1970). These orders were revised by another Appellate Assistant Commissioner in October 1973 in view of the retrospective amendment to the section and the jewellery was held liable to wealth-tax.

The assessees went in appeal to the Commissioner of Income-tax (Appeals) against the orders passed in October 1973 on the ground that the Appellate Assistant Commissioner who had passed the orders to include the value of jewellery had no jurisdiction over the assessees and the orders passed were not valid. The Commissioner of Income-tax upheld (February 1982) the contention of the assessees and allowed again the exemption in respect of jewellery. The assessments were revised in May 1982 and the demands raised and collected by the department, aggregating to Rs. 71,685, were refunded to the assessees.

The jurisdiction of the files were transferred from a city ward to a company ward under the jurisdiction of another Appellate Assistant Commissioner by a notification of the Central Board of Direct Taxes in December 1970 and the appellate jurisdiction over the latter ward was again changed in May 1972. Though the appellate jurisdiction of the assessees had been changed twice, the Wealth-tax Officer had not noticed the change in jurisdiction and consequently not obtained orders of the appropriate appellate authority resulting in his obtaining the orders of the wrong Appellate Assistant Commissioner in October 1973. This led to the decision being negatived by the Commissioner of the Income-tax (Appeals) and loss of revenue of Rs. 71,685.

The Ministry of Finance have accepted the mistake in principle (November 1984).

B—GIFT TAX

4.12 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 also liable to tax unless specially exempted by the Gift-tax Act. The term 'property' for the purpose of the Gift-tax Act connotes not only tangible movable and immovable property including agricultural land but also other valuable rights and interests.

4.13 Receipts under gift-tax in the financial years 1979-80 to 1983-84 compared as under with the budget estimates of these years :—

Year	Budget Estimates	Actuals
	(In crores of rupees)	
1979-80	5.75	6.83
1980-81	6.25	6.51
1981-82	6.25	7.74
1982-83	6.75	7.71
1983-84	8.50	8.84*

4.14 Particulars of cases finalised, pending assessment and arrears of demand are given below :—

Year	Number of assessments completed during the year	Number of case pending assessments at the end of	Arrears of demand pending collection at the end of (In crores of rupees)
1979-80	63,042	27,403	15.77
1980-81	60,562	38,226	29.52
1981-82	68,964	53,100	31.16
1982-83	74,163**	47,741**	21.90**
1983-84	82,204	43,893	27.21

4.15 During the test audit of assessments made under the Gift-tax Act, 1958, conducted during the period from 1 April 1983 to 31 March 1984, following types of mistakes were noticed :

(i) Gifts escaping assessment,

(ii) Non-levy of tax on deemed gifts,

(iii) Incorrect valuation of gifted properties and mistakes in computation of gifts,

*Provisional

**Figures furnished by Ministry of Finance in March/April 1984 have been adopted.

(iv) Omission to aggregate gifts for purpose of calculation of tax.

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

4.16 *Gifts escaping assessment*

(i) Under the Gift-tax Act, 1958, gift means the transfer by one person to another of any existing movable or immovable property made voluntarily and without consideration in money or money's worth.

An assessee in his wealth-tax returns, had not returned the value of three flats in Bombay owned by him from the assessment year 1974-75 and onwards. The value of the three flats as for the assessment year 1973-74 was Rs. 2,93,134. On the non-return of the value of the three flats being taken up in Audit in December 1982 the department stated in April 1983 that the assessee had transferred the three flats to his three sisters and hence, he ceased to be the owner of the properties as on the valuation dates relevant to the assessment year 1974-75 and onwards.

It was seen that a note regarding the transfer of the properties was made by the assessee in his wealth-tax return for the assessment year 1974-75, submitted to the department in October 1974. Further, the assessee had brought to the notice of the department in December 1974 that he had made a gift of the properties but had claimed exemption. The claim of the assessee was not, however, examined by the department.

As the assets were transferred without consideration, the assessee was liable to pay gift-tax. Hence, gift amounting to Rs. 2,93,134 escaped assessment, involving gift-tax of Rs. 53,536, for the assessment year 1974-75.

The Ministry of Finance have accepted the mistake and stated (October 1984) that the rectification has become time barred.

(ii) From the details of interest received on deposits filed by an assessee along with his income-tax return for the assessment year 1977-78, it was seen in audit in June 1982 that the assessee had, among other deposits, made a fixed deposit of Rupees one lakh in the name of his spouse in April 1975 in a bank. Though the amount constituted a valid gift to spouse, it was not included in the other gifts amounting to Rs. 1,68,320, assessed to tax in March 1982, for the assess-

ment year 1976-77. This resulted in non-levy of gift-tax of Rs. 24,111.

The paragraph was sent to the Ministry of Finance in May 1984; their reply is awaited (November 1984).

4.17 *Non-levy of tax on deemed gifts*

Under the gift-tax Act, 1958, where property is transferred otherwise than for adequate consideration, the amount by which the market value of property on the date of transfer exceeds the declared consideration, shall be deemed to be a gift made by the transferor and is chargeable to gift-tax.

(i) The income-tax records of seven individual assessees, for the assessment year 1974-75, showed that they sold in September and November 1973, 24,046 unquoted equity shares of a limited company at the face value of Rs. 12.50 per share. The market value of these shares on the dates of gift (i.e., dates of sale) was not determined with reference to the market value of the total assets of the company including goodwill to find out whether any gift had escaped assessment.

On this being pointed out in audit (September 1978), the department completed the assessment in respect of all the seven assessees in March 1980, creating a demand of tax of Rs. 1,94,857. The assessments in respect of six assessees who filed appeals, were set aside by the Appellate Assistant Commissioner in February 1981 with directions that shares should be got revalued according to the principles laid down by the Supreme Court. Accordingly cases of the six assessees (seventh assessee did not file any appeal) were referred to two Departmental Valuation Officers for determining the market value of shares. One Departmental Valuation Officer determined (November 1983) the market value at Rs. 140 per share in the case of four assessees. The report in respect of two other assessees was awaited. On the basis of the market value of Rs. 140 per share, determined by the departmental valuer, deemed gifts aggregating Rs. 30,65,865, involving gift-tax of Rs. 6,40,024, had escaped assessment in respect of all the seven assessees.

The Ministry of Finance have accepted the mistake (November 1984) in five cases; their reply in the remaining two cases is awaited (November 1984).

(ii) In the income-tax assessment of the estate of a deceased person for the assessment year 1975-76 finalised in September 1978, the assessing officer disallowed the claim of the assessee for short-term capital loss of Rs. 6,53,965, on sale of shares of two private limited companies, holding that it was a

fictitious loss. However, no attempt was made to ascertain the fair market value of the shares transferred to determine the 'deemed gift' involved in the transfer of the shares.

The accounts of one of the companies whose shares were transferred showed that it was an investment company with 1,195 shares of Rs. 1000 each fully paid up holding mainly two assets, i.e., a house property of book value of Rs., 4,83,510 and 5,180 shares of another company at the book value of Rs. 5,95,700. The market value of the house property was determined (October 1977) by the Departmental Valuation Officer at Rs. 15,61,900, as on 1 April 1974 and the market value of 5,180 shares of the company would be Rs.12,17,300, at Rs. 235 per share, as worked out in audit estimating the market value of assets. Hence, considering the market value of the assets held by the company, the market value of the shares of the company would be about Rs. 2,500 per share against which 595 shares were sold at Rs. 393 each by the assessee and consequently, the deemed gift involved in the sale amounted to Rs. 12,53,665. Further, taking into account the loss of Rs. 2,92,800 incurred by the assessee on sale of the shares of the second company which was rejected as fictitious while assessing the income, the total value of deemed gift escaping assessment, for the assessment year 1975-76, was Rs. 15,46,465, with consequent short levy of tax of Rs. 4,77,232.

The Ministry of Finance have accepted the mistake (December 1984).

(iii) In the previous year relevant to the assessment year 1980-81, two individual assessees sold 1,000 and 800 unquoted equity shares in a limited company at their face value of Rs. 100 each. The same shares were, however, valued by the Wealth-tax Officer for purposes of levy of wealth-tax in the two cases for the same assessment year 1980-81 at Rs. 745.22 per share, which showed that their fair market value was much higher than the declared consideration of Rs. 100 per share. The transfer attracted levy of gift-tax on 'deemed gift'. However, neither the assessees filed gift-tax returns nor did the department initiate gift-tax proceedings. In the absence of data in the assessment records to determine the market value of share under the Gift-tax Act, even adopting the value of Rs. 745.22 per share, as determined for wealth-tax purposes, "deemed gift" of Rs. 11,61,400 had escaped assessment in these two cases, the gift-tax leviable was Rs. 2,58,420.,

The Ministry of Finance have accepted the mistake (December 1984).

(iv) According to a declaration (February 1973) an assessee's interest in a partnership firm, valued at Rs. 6 lakhs for wealth-tax purposes, was divided equally between the assessee, her son and her married daughter during the previous year relevant to the assessment year 1973-74. The amount of Rs. 4 lakhs, thus surrendered, constituted deemed gift and attracted levy of gift-tax of Rs. 71,500. The assessee did not, however, file any gift-tax return.

The Ministry of Finance have accepted the mistake (December 1984).

(v) The income-tax assessment records of an assessee disclosed that a piece of land was sold for Rs. 1,50,000, the cost price of which was Rs. 3,87,531. The reasons given by the assessee for the sale at such abnormally low price were not accepted by the Income-tax Officer. After considering the various circumstantial evidence and facts mentioned by the assessee the sale price of the said property was estimated at Rs. 5,00,000 as against Rs. 1,50,000 shown by the assessee and the income-tax assessment for the assessment year was completed (March 1983) accordingly. However, the department had not initiated any proceedings under the Gift-tax Act. The difference between the sale price (Rs. 1,50,000) and the estimated market price (Rs. 5,00,000) constituted deemed gift attracting gift-tax of Rs. 67,750.

The Ministry of Finance have accepted the mistake in principle (August 1984).

(vi) Under the Gift-tax Act, 1958, the value of transactions such as release, discharge, surrender, forfeiture or abandonment of any debt, contract, an actionable claim or of any interest in property, if not bonafide, are deemed gifts. The Central Board of Direct Taxes issued instructions in March 1976 and May 1977 clarifying that when a partnership firm is reconstituted either with the same old partners or on retirement of one of the partners or on admission of new partners or on conversion of a sole proprietorship into a partnership and the profit sharing ratios of the partners are revised, any interest surrendered or relinquished by one or more of such persons (without adequate consideration in money or money's worth) in favour of others would attract levy of gift-tax.

(a) A partnership firm was reconstituted on the death of a partner (September 1979) during the previous year relevant to the assessment year 1980-81. A new partner (major) joined the firm and a minor son of the deceased partner was admitted to

the benefits of the partnership. In this process, one of the existing partners who had 25 per cent share in the firm surrendered 15 per cent of his share of interest in the firm in favour of other partners on reconstitution of the firm, which resulted in realignment of the profit sharing ratios of the partners. The surrender of the interest was without consideration in money or money's worth and it, therefore, constituted deemed gift attracting levy of gift-tax. The department did not, however, initiate any gift-tax proceeding in the matter. Taking into account three years purchase value of the net average profits for the last four assessment years 1976-77 to 1979-80 of the firm, the value of deemed gift that escaped assessment worked out to Rs. 5,37,492, with consequent non-levy of gift-tax of Rs. 1,16,247.

The Ministry of Finance have accepted the mistake in principle (December 1984).

(b) A partnership firm was reconstituted on the death of a partner (Septemebr 1979) during the previous year relevant to the assessment year 1980-81. A minor son of the deceased partner was admitted to the benefits of the partnership. In this process one of the existing partners who had 40 per cent share in the firm surrendered 30 per cent of her share of interest in the firm in favour of other partners on reconstitution of the firm which resulted in realignment of the profit sharing ratios of the partners. The surrender of the interest was without consideration in money or money's worth and it, therefore, constituted deemed gift attracting levy of gift-tax. The department did not, however, initiate any gift-tax proceeding in the matter. Taking into account three years purchase value of the net average profits for the last five years 1975-76 to 1979-80 of the firm, the value of deemed gift that escaped assessment, worked out to Rs. 3,39,400, with consequent non-levy of gift-tax of Rs. 65,100.

The Ministry of Finance have accepted the mistake in principle (December 1984).

(c) A Hindu undivided family had fifty per cent share of interest in a registered firm. On the dissolution of the firm, in July 1979, it received the balance to the credit of its account in the books of the firm. The assessee had, however, foregone share in the goodwill and the share in the difference between the market value and cost price of the closing stock; the value of the assets released without consideration was assessable as deemed gift in the hands of the Hindu undivided family. Though the assessing officer had made a note in the miscellaneous records of the firm for the assessment year 1980-81 in July 1981 on the assessability to gift-tax, no follow-up action was taken till the

date of audit (June 1983). The omission resulted in non-levy of gift-tax of Rs. 29,758, on the deemed gift of Rs. 1,96,285.

The Ministry of Finance have accepted the mistake (November 1984).

4.18 *Incorrect valuation of gifted properties and mistakes in computation of gifts*

(i) In the assessment, for the assessment year 1977-78 of an an assessee, the department did not include the value (Rs. 22,000) of shares (500) transferred, while computing the total taxable gift (Rs. 22,10,790). Further, while calculating the tax, an amount of Rs. 8,48,092 was wrongly deducted as against Rs. 2,88,900 towards gift-tax on the aggregate gift of Rs. 10,81,000 made during the four previous years immediately preceding the previous year relevant to the assessment year 1977-78.

The two mistakes resulted in short levy of gift-tax of Rs. 5,75,692.

The Ministry of Finance have accepted the mistake (November 1984).

(ii) The gift-tax assessment of an individual, for the assessment year 1973-74, re-opened to bring to tax certain gift which had escaped assessment in the original assessment order, was finalised on 31 March 1983. As per assessment order gift of Rs. 2,93,384, on account of the difference between the value of certain unquoted equity shares as assessed by the Gift-tax Officer and the value returned, was to be added in the total value of gifts. However, in actual computation of the total value of gifts, this amount was not included. Consequently, the value of the gifts made during the relevant previous year was under-assessed by Rs. 2,93,384, resulting in short levy of gift-tax of Rs. 2,20,038.

The Ministry of Finance have accepted the mistake (September 1984).

(iii) An individual assessee returned an immovable property at a value of Rs. 1,24,080 in the wealth-tax return (valuation rate 31 December 1976) for the assessment year 1977-78. Within two months from this valuation date the assessee gifted (February 1977) this property to her daughter and the gift was assessed on 24 March 1983, for the assessment year 1978-79, at the returned value of Rs. 1,24,000. The case of valuation of the property for weath-tax levy for the assessment year 1977-78 was referred to the Departmental Valuation Officer and the valuer in his preliminary report of 9 March 1983 (confirmed

later on 20 April 1983) reported the value as Rs. 6,07,000. This value of Rs. 6,07,000 for the property was adopted in the wealth-tax assessment made on 29 March 1983. However, the assessing officer neither adopted the value of the gift as Rs. 6,07,000 on the basis of valuer's report of 9 March 1983 in the original gift-tax (assessment done on 24 March 1983) nor did he revise the gift-tax assessment to rectify under-valuation. The under-valuation of the property resulting from omission to correlate the assessments under various direct tax laws led to under assessment of gift by Rs. 4,83,000 and short levy of gift-tax of Rs. 1,15,250, for the assessment year 1978-79.

The Ministry of Finance have accepted the mistake (October 1984).

(iv) An individual settled 62 grounds and 1909 square feet of urban lands owned by him in August 1981 in favour of various parties and returned the total value of the gifted property as Rs. 41,668 in the gift-tax return filed in April 1982. In the gift-tax assessment, for the assessment year 1982-83, completed in April 1982, the department fixed the total value as Rs. 2,17,000, taking the value per ground as Rs. 3,500 and also deducting therefrom the value of the property (Rs. 37,200) as on 1 January 1964, the cost of improvements (Rs. 31,000) and urban land tax of Rs. 18,554, to arrive at the value of the gift.

According to the various settlement deeds filed with the return, the market value was, however, found to be Rs. 6,375 (approximately) per ground and that the total value of 62 grounds and 1909 square feet of land gifted by the individual at that rate amounted to Rs. 3,99,250 (approximately). Taking into account this market value and deducting therefrom urban land tax of Rs. 18,554 (other two deductions being inadmissible) and allowing basic exemption of Rs. 5,000, the taxable gift under-assessed was Rs. 2,51,050, with consequent undercharge of gift-tax of Rs. 58,358.

The Ministry of Finance have accepted the mistake (September 1984).

(v) The Central Board of Direct Taxes clarified (January 1982) that, where, the break-up value method is adopted to determine the value of unquoted shares, no discount for restrictions regarding alienation, should be given.

(a) An assessee gifted 3,000 unquoted equity shares of a private limited company to his grand daughters in April 1981. The break-up value of each share was computed at Rs. 186, on the basis of balance sheet as on 31 May 1980. The market value was adopted at Rs. 144.15 being 77.5 per cent of Rs. 186. The value of 3,000 shares was thus returned at Rs. 4,32,450, which was accepted by the Gift-tax Officer. The assessment was completed in December 1982 and tax of Rs. 88,363 was levied. The incorrect allowance of discount of 22.5 per cent from the break-up value of each share resulted in under-assessment of tax of Rs. 34,037.

The Ministry of Finance have accepted the mistake (October 1984).

(b) The provisions of Gift-tax Act, 1958, are *pari-materia* with those of Estate Duty Act, 1953, in regard to the valuation of unquoted equity shares. Thus, the instructions issued by the Central Board of Direct Taxes under the Estate Duty Act for valuation of shares, are equally applicable to cases under the Gift-tax Act. Under the Estate Duty Act the Board had issued instructions in May and July 1965 that the value of unquoted equity shares should be determined on the basis of market value and not the book value of assets of the company. The Board reiterated their instructions of May and July 1965 in October 1974 and May 1975.

The provisions relating to the valuation of shares under the Wealth-tax Act, 1957 and the rules made thereunder are not applicable to valuation under the Gift-tax Act.

An assessee gifted 260 equity shares of a private limited company during the previous year relevant to the assessment year 1972-73. The assessee showed the value of the gift as 'nil' in the return filed in December 1976. In the assessment made in December 1978, the Gift-tax Officer valued the shares at Rs. 1,915 each. As a result of an appeal preferred by the assessee to the Commissioner (Appeals), the assessment was revised in December 1980, determining the value of each share as Rs. 1,737 after allowing a deduction of 15 per cent, i.e., Rs. 306 towards non-declaration of dividends, as contemplated under the Wealth-tax Rules, 1957. As the wealth-tax Rules of valuation are not applicable for gift-tax purposes the deduction of 15 per cent resulted in aggregate short levy of tax of Rs. 28,860, including a totalling mistake.

The Ministry of Finance have stated (December 1984) that the audit objection is under examination.

(vi) An individual gifted a portion of his house property to his sons during the previous year relevant to the assessment year 1977-78. While assessing the gifted property in May 1982, the assessing officer determined the taxable gift as Rs. 2,01,500, after deducting from the value (Rs. 4,13,000) of the property fixed by the departmental valuer, a sum of Rs. 68,833, being the value of the portion owned by the assessee's wife. The departmental valuer while fixing (January 1981) the value of the property (Rs. 4,13,000) had, however, already excluded the value (Rs. 68,833) of the portion of the property owned by the assessee's wife in his report. Further, a perusal of the income-tax and wealth-tax records upto the assessment year 1976-77 revealed (September 1983) that the income from the entire property was being assessed to income-tax in the hands of the assessee, the entire value of the property was included in the net wealth of the assessee except for the assessment year 1976-77 and no portion of the property belonged to the wife.

The two mistakes resulted in total under-assessment of gift of Rs. 1,37,666, with consequent short levy of gift-tax of Rs. 34,417.

The Ministry of Finance have accepted the mistake (November 1984).

4.19 *Omission to aggregate gifts for purpose of calculation of tax.*

Under the Gift-tax Act, 1958, as amended by the Taxation Laws (Amendment) Act, 1976, from 1 April, 1976, taxable gifts made by an assessee in a previous year are to be charged to tax after aggregating them with the taxable gifts, if any, made during the preceding four previous years (excluding the gifts made before 1 June 1973) at the rates applicable to the relevant assessment year. From the tax so computed, gift-tax on the taxable gifts of the preceding four previous years reckoned at the same rates will be deducted and the balance would represent the gift-tax payable for the year.

In the gift-tax assessment of an individual, for the assessment year 1977-78, finalised on 30 March 1982, the taxable gift was determined as Rs. 7,66,420, on which gift-tax of Rs. 1,86,426 was levied. While computing the tax payable by the assessee the taxable gifts amounting to Rs. 39,89,181 made by the assessee

during the previous years relevant to the assessment years 1975-76 and 1976-77 were, however, not reckoned for purposes of aggregation of gifts. The omission resulted in short levy of gift-tax of Rs. 3,88,389.

The Ministry of Finance have accepted the mistake (August 1984).

C—ESTATE DUTY

4.20 Receipts under the estate duty in the financial years 1979-80 to 1983-84 compared as under with the Budget Estimates of these years :

Year	Budget Estimates (In crores of rupees)	Actuals
1979-80	12.00	14.05
1980-81	13.00	16.23
1981-82	15.00	21.31
1982-83	17.00	20.38
1983-84	19.00	26.46*

4.21 Particulars of cases finalised, pending assessment and arrears of demand are given below :

Year	Number of assessments completed during the year	No. of cases pending assessment	Arrears of demand pending collection at the end of(in crores of rupees)
1979-80	32,607	34,891	17.23
1980-81	32,428	35,862	27.65
1981-82	35,257	36,581	30.73
1982-83	38,483	35,561**	34.31**
1983-84	40,165*	34,477	34.45

4.22 During the test audit of assessments made under the Estate Duty Act, 1953, conducted during the period from 1 April 1983 to 31 March 1984, the following types of mistakes resulting in under-assessment of duty were noticed :—

(i) Incorrect computation of principal value of estate.

(ii) Estates escaping assessment.

*Provisional.

**Final figures revised by Ministry of Finance.

(iii) Incorrect valuation of assets.

(a) unquoted equity shares, and

(b) immovable properties.

(iv) Incorrect grant of reliefs/deductions.

(v) Non-levy of penalty.

(vi) Miscellaneous.

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

4.23 *Incorrect computation of principal value of estate.*

(i) In the estate-duty assessment of a deceased (died in August 1976), the following mistakes were noticed in the computation of principal value of the estate :

(a) Out of the total number of 9,833 shares owned by the deceased in a private limited company, only 3,000 shares were taken for estate duty assessment. Value of 6,833 shares at Rs. 75.94 per share escaped assessment.

(b) The 3,000 shares reckoned for estate duty purposes were valued at Rs. 43.65 only per share, though in the wealth-tax assessment (valuation date 16 August 1976) the same shares were valued at Rs. 75.94 per share. On this basis the 3,000 shares were under-valued by Rs. 32.29 per share.

The value of the estate short-assessed amounted to Rs. 6,15,768 involving short-levy of duty of Rs. 4,77,021.

The Ministry of Finance have accepted the mistakes (September 1984).

(ii) Under the provisions of the Estate Duty Act, 1953 and the instructions issued by the Central Board of Direct Taxes in October 1974 and May 1975 unquoted equity shares in a private limited company where alienation of shares is restricted should be valued for the purpose of levy of estate duty by reference to the market value of the assets of the company, including the value of its goodwill, as on the date of death. The provisions relating to valuation of shares under the Wealth-tax Rules are not applicable to estate duty assessments.

The Act also provides *inter alia* that where any disposition had been made by the deceased person in favour of a relative, it would be treated as a gift unless the disposition had been made on the part of the deceased for full consideration in money or money's worth paid to him for his own use or benefit and that, if such disposition had been made within two years before death, the gift comprised in the disposition would be deemed to pass for levy of estate duty.

The estate of a person (died in July 1964) comprised *inter alia* 10 unquoted equity shares in a private limited investment company which restricted alienation of its shares. In the estate duty assessment made in December 1978, these shares were incorrectly valued at Rs. 5,260.33 per share under the "break-up" value method under the Wealth-tax Rules, adopting book value of assets of the company. Having regard to rental income from a building owned by the company comprising 95 per cent of the income of the company and capitalizing it under the "income-capitalization" method, the fair market value of the building would work out more than its book value in the balance-sheet of the company by Rs. 72.34 lakhs. On adoption of market value of the building, the market value of these shares would work out to Rs. 27,519.27 per share for levy of estate duty instead of Rs. 5,260.33 per share adopted in the assessment.

The deceased had during his life-time, sold 40 such shares to his daughter-in-law in April 1964, i.e., within two years before his death, at Rs. 2,000 per share. As this disposition to relative was not for full consideration the excess of the value of these 40 shares at Rs. 27,519.27 per share over the declared consideration of Rs. 2,000 per share would be gift which would be deemed to pass and was includible in the principal value of the estate. It was not so included.

The two mistakes led to under-assessment of estate by Rs. 12,43,359 and short levy of duty of Rs. 4,72,863.

The Ministry of Finance have accepted the omission (December 1984).

The case was seen in internal audit but mistakes were not noticed.

(iii) Under the Estate Duty Act, 1953, movable property situated outside India is not included in the property passing on the death of a person, unless the deceased was domiciled in India at the time of his death. Domicile is determined

in accordance with the provisions of Indian Sucession Act, 1925 which *inter alia* provides that domicile of origin prevails until a new domicile is acquired.

In December 1974, the Estate Duty Officer directed the accountable person to adduce proof that the deceased was not of Indian domicile and the property was not situated in India at the time of death. In January 1975 the accountable person filed an affidavit to the effect that the deceased migrated to the U.S.A in the year 1964 to run a business and became a permanent resident thereafter. Accepting the affidavit the Estate Duty Officer excluded an insurance amount of Rs. 7,76,382 from the principal value of the estate. The following facts as per the assessment records, indicated that the exclusion of the asset was not in order :—

(a) as per the will executed in April 1972, the deceased transferred his entire property consisting of both movable and immovable assets to his relative. There was no mention therein of the foreign business.

(b) for the assessment years 1971-72 and 1972-73, the assessee was assessed in the status of resident and for the assessment years 1973-74 and 1974-75 in the status of non-resident.

(c) as per the death certificate, the deceased was residing at the time of death in a hotel in New Delhi.

(d) in the death certificate the deceased was shown as Indian citizen with permanent address in India.

(e) the assessee had also purchased a plot of land, in March 1967, in India and in the conveyance deed of July 1972 the Indian address only was shown.

(f) No assets relating to the business in U.S.A. were returned and assessed for estate duty.

These facts confirmed that the deceased was domiciled in India at the time of his death. The incorrect exclusion of the asset of Rs. 7,76,382 resulted in short levey of estate duty of Rs. 2,14,673.

The para was sent to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(iv) Under the provisions of the Estate Duty Act, 1953 and the instructions issued by the Central Board of Direct Taxes in October 1974 and May 1975 unquoted equity shares in a private limited company are to be valued on the basis of the market value of the assets including goodwill of the company as on the date of death. The provisions relating to the valuation of shares under the Wealth-tax Act, 1957 and rules thereunder are not applicable to the valuation under the Estate Duty Act.

A liability for debt and incumbrance can be allowed from the gross value of dutiable estate only when the debt or incumbrance were incurred or created bonafide for full consideration in money or money's worth wholly for the deceased's own use and benefit and take effect out of his interest.

A deceased lady held 1,370 shares of a private limited company and these were valued by the assessing officer at their face value of Rs. 100 each in the assessment made in February 1983 instead of being valued with reference to market value of the assets of the company. In the absence of particulars of market value of assets and value of goodwill being ascertained and kept on record, even under the break-up value method the value per share worked out to Rs. 230 instead of Rs. 100. The omission to adopt the value of shares as Rs. 230 each resulted in under-assessment of the estate by Rs. 1,78,000. The under-assessment will be more if the market value of assets and goodwill were taken into consideration for valuing the shares.

Further a deduction of Rs. 2,08,480 representing balance amount of debt raised by her to discharge liabilities of her husband who had adopted a son in November 1969 was allowed in the assessment, which was not in order as it was not incurred for the deceased's own use and benefit.

These mistakes resulted in under-assessment of principal value of the estate by Rs. 3,86,580 leading to short levy of estate duty by Rs. 1,17,465 (including the mistake of duty free slab taken incorrectly as Rs. 1,50,000 instead of Rs. 50,000).

The Ministry of Finance have accepted the omission (December 1984).

(v) Under the Estate Duty Act, 1953, estate duty shall be due from the date of death and the Controller may at any time after the receipt of account delivered, proceed to make in a summary manner, a provisional assessment of estate duty payable by the person delivering the account on the basis of account so delivered.

In the case of a person, who died on 1 December 1980, principal value of the estate passing on death was returned at Rs. 13,75,479 and in addition, amounts of Rs. 2,66,658 as lineal descendant's share in the properties of Hindu undivided family and Rs. 1,500 representing a gift made were shown as includible for determining the rate of duty payable. While completing the assessment provisionally in November 1982, the assessing officer did not include the amount of Rs. 2,68,158 (Rs. 2,66,658 plus Rs. 1,500) mentioned above for rate purpose. Owing to incorrect computation of the principal value of the estate, there was short levy of estate duty of Rs. 60,350.

The para was forwarded to the Ministry of Finance in August 1984; their reply is awaited (November 1984).

(vi) A male Hindu who, for the time being is the sole surviving coparcener of a Hindu undivided family governed by the Mitakshara School of Hindu Law, is competent to alienate the common property of the family 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 the alienation. Female members of such a family also cannot call for a partition and do not have a right of share in such common property. On the death of such a sole coparcener, the whole of the common property of the family along with his separate property passes for levy of estate duty, as he has power of disposition over these properties. This well settled position of law was reiterated in Board's circulars of October, 1959 and July, 1976.

(a) In the estate duty assessment in respect of a sole coparcener of a Hindu undivided family who died in April 1977 and who *inter alia* owned properties valuing Rs. 3,89,772, the Assistant Controller of Estate Duty included (assessment made in October 1980) only one-half share of the properties instead of the whole in the estate of the deceased, incorrectly excluding the other half as share belonging to his wife. The principal value of his estate was, thus, computed short-by Rs. 1,94,886, resulting in short levy of estate duty of Rs. 58,410.

The case was checked in Internal Audit; however, the mistake escaped their notice.

The Ministry of Finance have accepted the omission (October 1984).

(b) In another case relating to the same charge a sole coparcener of a Hindu undivided family who died in November 1981, *inter alia* owned agricultural land valuing Rs. 3,22,645. The

Assistant Controller of Estate Duty included (assessment made in February 1983) only one-half share of the above property instead of the whole in the estate of the deceased, incorrectly excluding the other half as share belonging to his wife. The principal value of his estate was, thus, computed short by Rs. 1,61,320 resulting in short-levy of estate duty of Rs. 30,778.

Though the case was checked by the Internal Audit Party the point escaped their notice.

The Ministry of Finance have accepted the omission (October 1984).

(vii) In the estate duty assessment completed in April 1982 of a person, who died in May 1979, two house properties were valued at Rs. 2,55,000 and movables and other assets lying in locker of a bank were valued Rs. 81,260. The aforesaid assets were, however, valued by the Calcutta High Court at Rs. 5,22,200 in the letter of Administration granted in November 1982. The omission to revise the original assessment on the basis of his information resulted in under-valuation of the estate by Rs. 1,85,940 with consequent short-levy of duty of Rs. 45,254.

The para was forwarded to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

(viii) In the case of a person who died in June 1981, provisional assessment of estate duty was completed in March 1983 determining the value of the estate at Rs. 2,69,794. The value so determined comprised Rs. 2,09,484 as individual estate and Rs. 60,310 as lineal descendant's share in the properties of Hindu undivided family, aggregated for rate purpose. The details furnished by the accountable person, however, indicated that the sum of Rs. 60,310 represented the deceased's share in the assets of Hindu undivided family and that the lineal descendant's share amounted to Rs. 3,71,883 beside value of individual estate of Rs. 2,09,484. The principal value of the estate thus amounted to Rs. 6,41,677 as against Rs. 2,69,794 adopted in the assessment. This resulted in short-levy of duty of Rs. 33,172.

The Ministry of Finance have accepted the mistake (October 1984).

(ix) Under the provisions of the Estate Duty Act, 1953, any liability of the estate existing on the date of death is deductible in computing the principal value of the estate.

The assessment to estate duty of a person who died in November 1971, was completed in April 1981 allowing a deduction of Rs. 2,35,955 for outstanding liabilities on account of income-tax and interest thereon for the assessment years 1970-71 and 1972-73. These liabilities were based on the original income-tax assessments completed in March 1976. The liability for the two years had, however, been reduced to Rs. 1,27,924 in September 1979 i.e. nearly 20 months prior to completion of the estate duty assessment in April 1981. Omission to correlate estate duty assessment with the corresponding income-tax assessments and adopt correct income-tax and interest liability in the estate duty assessment led to under assessment of the principal value of the estate by Rs. 1,08,031 and short-levy of estate duty of Rs. 32,409.

The para was forwarded to the Ministry of Finance in July 1984 ; their reply is awaited (November 1984).

(x) Under the Estate Duty Act, 1953, any disposition made by the deceased in favour of a relative without he receiving full consideration therefor in money or money's worth, is treated as gift and property taken under any 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 amounts to gift from which the donor was not entirely excluded.

A person, who died in February 1981, had transferred (November 1977) his self-acquired property (4,700 shares of a company), worth Rs. 2,03,274 to the common hotch pot of Hindu undivided family, consisting of himself, his wife and son. As this was a disposition in favour of relatives and the deceased was not excluded entirely from the enjoyment and benefit of the property even after its transfer, the full value of the transferred property was includible in the estate passing on the death of the deceased. However, the assessing officer, in the assessment made in February 1983 included only one-third (Rs. 67,758) of the value of the transferred property and an equal amount as lintal descendant's share only for rate purpose. The above omission resulted in under-charge of duty of Rs. 24,890.

The Ministry of Finance have accepted the omission (September 1984).

4.24 *Estate escaping assessment*

Under the provisions of the Estate Duty Act, 1953 property which the deceased was competent to dispose of at the time of his death is deemed to pass on his death.

(i) In the case of a person, who died in October 1976, refund of wealth-tax of Rs. 68,630 for the assessment years 1973-74 to 1976-77, was made by the department as per Appellate Tribunal's order dated 8 November 1979. The amount of this refund was, however, not included in the estate duty assessment of the estate made in June 1981 and revised subsequently in October 1983. The omission resulted in short-levy of duty of Rs. 52,348.

The para was forwarded to the Ministry of Finance in August 1984 ; their reply is awaited (November 1984).

(ii) In the wealth-tax assessment for the assessment year 1966-67 of an assessee the value of twelve immovable properties in a metropolitan town was assessed at Rs. 3,82,060, accepting the valuation of the assessee as shown in the relevant return. The assessee died in March 1967. In the estate duty assessment done in September 1982 the Assistant Controller of Estate Duty determined the value of these properties at Rs. 2,21,854. The omission to correlate the estate duty assessment with the wealth-tax assessment, thus, resulted in undervaluation of the estate by Rs. 1,60,206 leading to short-levy of duty of Rs. 42,787.

The case was required to be checked in internal audit ; it has not been so checked.

The Ministry of Finance have accepted the omission (November 1984).

(iii) The estate duty assessment of a person, who died in November 1967, was revised in April 1979, to allow relief of court fee paid for obtaining representation to the estate of the deceased. Audit scrutiny revealed (November 1980) that assets worth Rs. 74,770 shown in the succession certificate were not returned in the estate duty return by the accountable person and were also not included in the principal value of the estate by the assessing authority. This resulted in under-assessment of the principal value of the estate by Rs. 74,770, with consequent short levy of duty of Rs. 29,894.

The Ministry of Finance have accepted the omission (November 1984).

4.25 *Incorrect valuation of assets*

(A) *Unquoted equity shares*

According to the provisions of the Estate Duty Act, 1953 and the instructions issued by the Central Board of Direct Taxes in October 1974 and May 1975 unquoted equity shares in a private limited company where alienation is restricted held by a deceased person should be valued for the purposes of levy of estate duty by reference to the market value of the assets of the company, including goodwill, as on the date of death. The provisions relating to the valuation of shares under the Wealth-tax Act, 1957 and Rules thereunder are not applicable to estate duty assessments.

(i) In the estate duty assessment (completed in February 1979) in respect of the estate of a person, who died in August 1976 the assessing officer incorrectly applied Wealth-tax Rules to value unquoted equity shares held by the deceased in various private limited companies and accordingly valued these shares under the break-up value method on the basis of the book value of assets of the companies after allowing thereunder percentage deduction for non-declaration of dividends. Valuation under Wealth-tax Rules is not applicable to estate duty assessments for which valuation is required to be done on the basis of market value of assets, including goodwill, of the companies. The market value of assets of the companies including goodwill not having been ascertained and placed on the assessment records of the assessee, the exact under-valuation of the shares could not be worked out. Even adopting the valuation under Wealth-tax Rules, ignoring the percentage deduction allowed of Rs. 2,72,032 which is not admissible for levy of estate duty, the value of the shares, as part of the estate, was under-assessed by the same amount leading to short levy of estate duty of Rs. 1.36 lakhs (approx). If the shares were valued on the basis of market value of assets of the company, including goodwill, under the Estate Duty Act, the under-assessment and short levy of tax would be still higher.

The para was forwarded to the Ministry of Finance in July 1984; their reply is awaited (November 1984).

(ii) The estate of a person, who died in February 1981, included 2040 unquoted equity shares in a private limited company (including 590 shares as his interest in Hindu undivided family). The shares were valued by the Assistant Controller in October 1981, while making assessment under the break-up value method on the basis of the book value of assets of the company with percentage deduction for non-declaration of dividends. The valuation made by the Assessing Officer adopting the Wealth-tax Rules was not correct, as the valuation had to be done under the provisions of the Estate Duty Act adopting market value of assets, including goodwill of the company.

The market value of assets of the company, including goodwill not having been ascertained and placed on the assessment records in the case of the assessee, the exact under-valuation of the shares could not be worked out. Even adopting the valuation under the Wealth-tax Rules ignoring the percentage deduction of Rs. 2,62,046 allowed in the case, which is not admissible, the value of the shares was under-assessed by the same amount leading to short-levy of estate duty of Rs. 1,07,462. If the shares were valued on the basis of market value of assets of the company, including goodwill, the under-assessment and short-levy of tax would be still higher.

The Ministry of Finance have accepted the omission (November 1984).

(B) *Immovable properties*

(i) A person, who died in December 1975, owned one third share in an urban house property. The assessing officer referred the valuation of the property to the Departmental Valuation Officer who valued the entire property for Rs. 13,91,797. The value of a deceased's share thereof was thus Rs. 4,63,932. However, while completing the estate duty assessment in June 1982, the assessing officer, relying on an appellate order (October 1977) determined the value of the property on a different basis and the value of deceased's share was taken at Rs. 1,21,165.

It was noticed that the appellate order did not relate to this particular property but to two other properties and, therefore, had no relevance to this property. Further, the valuation made by the Departmental Valuation Officer of this property

was accepted by the department in the wealth-tax assessment for the assessment year 1975-76 (valuation date 31 March 1975). The incorrect valuation of the house property resulted in under-assessment of the value of the estate of Rs. 3,43,767, with consequent under-charge of estate duty of Rs. 1,25,194.

The Ministry of Finance have accepted the omission (December 1984).

(ii) Under the provisions of the Estate Duty Act, the value of a property included in the principal estate is estimated to be the price which it would fetch if sold in the open market.

A person who died in January 1959 was a co-owner of immovable properties, his share being one-third. The immovable properties were valued at 20 times of the net income assessed for income-tax purposes. The income from the properties assessed for the assessment years 1958-59 and 1959-60, was Rs. 89,450 and Rs. 1,13,194 respectively. In the estate duty assessment made in November 1982, the Assistant Controller deducted income-tax demands of Rs. 43,667 and Rs. 63,907 respectively from the said income and determined one-third share of the deceased as the average of the two incomes, which amounted to Rs. 15,845. Thus deceased's share in immovable property included in the estate duty assessment was worked out as Rs. 3,16,900. The assessment contained the following two mistakes :—

(a) While determining the value of the property under yield method, no deduction is admissible for income-tax liability.

(b) As the person died in January 1959, the income assessed in the income-tax assessments for the assessment year 1959-60 would be relevant for consideration.

The value of the immovable properties correctly worked out to Rs. 6,75,480 instead of Rs. 3,16,900. The under-assessment of the estate by Rs. 3,58,580 resulted in short-levy of estate duty of Rs. 90,600 (approx).

The para was forwarded to the Ministry of Finance in September 1984; their reply is awaited (November 1984).

4.26 *Incorrect grant of relief/deductions*

Under the Estate Duty Act, 1953, a liability for debt and incumbrance can be allowed from the gross value of dutiable estate only when the debt or incumbrance is incurred or created bonafide for full consideration in money or money's worth wholly for the deceased's own use and benefit and take effect out of his interest.

(i) From the value of the estate left by a deceased (died in August 1982), deduction of Rs. 2,43,539 was allowed (March 1983) as a debt due. According to the legal representative (January 1983) the deceased had stood guarantor for the loans (to the extent of Rs. 2,43,539) obtained by other persons from scheduled banks and of the principal borrowers had not paid off these respective loans to their banks, the banks had filed civil suits for the recovery of the said loans from the borrowers as well as from the guarantor.

The debts were thus not obtained by the deceased himself in exchange of full consideration in money or money's worth for his own use or benefit and the debts had not taken effect out of his own interest. Further, the cases were sub-judice in the court of law and the chances of recovery of the loans from the principal debtors were still there. This incorrect deduction of debt due resulted in under-charge of duty of Rs. 22,610.

The para was forwarded to the Ministry of Finance in June 1984; their reply is awaited (November 1984).

(ii) In the estate duty account filed in respect of a deceased, who died in February 1969, the accountable person claimed deduction for income-tax liability of Rs. 1,31,714. As against this, the department allowed a deduction of Rs. 5,91,341 in assessment made in March 1979, taking into account the increased demand raised by the Income-tax Officer for the assessment years 1962-63 to 1965-66 on re-assessment (done in February 1979 for the assessment year 1962-63, 1963-64 and 1965-66 and in December 1978 for the assessment year 1964-65) to include certain income escaping assessment. These Income-tax re-assessment proceedings themselves were subsequently set aside in July 1979 by the Commissioner of Income-tax (Appeals). However, the increased income-tax liability of Rs. 4,59,627 allowed in the estate duty assessment was not withdrawn involving short levy of duty of Rs. 1,73,996.

The case was required to be seen in Internal Audit as per the standing instructions of the Board ; it was not so checked.

The Ministry of Finance have accepted the omission (September 1984).

(iii) Under the Estate Duty Act, moneys' deposited with Government in such manner as may be prescribed for the purpose of estate duty together with interest, subject to a ceiling of Rs. 50,000 are exempt from tax.

In the estate duty assessment (completed in May 1982) in respect of a person (died in February 1977), rebate of Rs. 1,68,340 was allowed being the matured value of an insurance policy effect for payment of estate duty, instead of limiting the rebate to the ceiling limit of Rs. 50,000 as prescribed in the Act. A further rebate of Rs. 5,000 on another insurance policy was also allowed, even though no such insurance policy had been effected by the deceased on his life.

The two mistakes resulted in excess allowance of rebate of Rs. 1,23,340 leading to undercharge of duty of Rs. 28,271. The case was required to be seen in internal audit under the standing instructions of the Board ; it was not so checked.

The Ministry of Finance have accepted the mistake and stated (September 1984) that these are being rectified.

4.27 *Non-levy of penalty*

Under the Estate Duty Act, 1953, every person accountable for estate duty shall, within six months of the death of the deceased, deliver to the Controller, an account of all the properties in respect of which duty is payable. The Controller may also extend the period of six months. Further, the Controller shall serve a notice on the accountable person to attend in person or produce any evidence in support of his account. The Act also vests powers with the Controller to levy penalty when any person who has without a reasonable cause, failed to deliver an account of the property of the deceased or has without reasonable cause failed to comply with the notice issued under the Act. The quantum of penalty for non-delivery of account is a sum not exceeding twice the amount of estate duty payable by the accountable person and for failure to comply with the notice, a sum not exceeding twice the amount of estate duty.

if any, which would have been avoided if the principal value shown in the account of such persons had been accepted as correct.

Where penalty is not levied in exercise of discretion, reasons for such non-levy are required to be recorded in the course of assessment proceedings as per instructions of July 1969 of Central Board of Direct Taxes.

In a case, after the death of a person in August 1977, the accountable person delivered the accounts of the deceased's estate in January 1979, though no extension of time to deliver the accounts beyond the initial period of six months after the death, had been granted by the assessing authority. Further, due to lack of response from the accountable person to three notices issued in February 1980, in January 1982 and in February 1982 for production of material or personal appearance for completion of assessment the assessing authority finalised the assessment on best judgement basis. The omission to render account in time and failure to respond to notices attracted levy of penalty under the Act.

For the delay in rendering the account of estate, the Assistant Controller neither initiated any penalty proceedings nor recorded reasons therefor in the assessment proceedings. In regard to failure of the accountable person to respond to notices issued, the Controller initiated penalty proceedings in June 1982 but did not issue any notice till May 1983, when audit pointed out the omission. The maximum penalty leviable was Rs. 10,56,724.

The Ministry of Finance have accepted the omission and stated (September 1984) that the penalty proceedings have been initiated.

4.28 *Miscellaneous*

(i) A person, who died in January 1980, held 2,420 equity shares of Rs. 100 each and 29,000 equity shares of Rs. 10 each in two companies. In the estate duty assessment completed in May 1982, the assessing officer had taken the value of shares of the above two companies at their face values.

In the gift-tax assessment of the deceased completed in May 1981, the value of the same shares was, however, determined

under the break-up method at Rs. 384.41 and Rs. 53.40 each respectively as returned by the assessees; the gifts were made in September|November 1979. The omission to correlate estate duty assessment with the gift-tax assessment, resulted in under-valuation of shares by Rs. 284.41 and Rs. 43.40 each respectively, with consequent under-assessment of the estate by Rs. 19,46,872 and short-levy of Rs. 13,50,000 (approx).

The return was due to be filed on 11 July 1980 but it was actually filed on 26 December 1980. Penalty for delay in filing the return was also leviable but was not levied.

The para was forwarded to the Ministry of Finance in August 1984 ; their reply is awaited (November 1984).

(ii) In the case of a person who died in April 1976, the accountable person claimed that the properties left by the deceased belonged to his (deceased's) Hindu undivided family, but did not produce any evidence in support of the claim inspite of repeated requests therefor by the Assistant Controller of Estate Duty. There was no evidence that the deceased had received any fund or other properties from his ancestors or that the assets purchased or accummulated during his life time were either out of such ancestral properties or thrown by him to the common hotch pot of joint family.

In November 1978, the Assistant Controller sought instructions from the Deputy Controller as to what he should do in the face of such complete lack of evidence, but no instructions were received. As the non co-operation of the accountable person continued in this and all other matters of assessment proceedings, the Assistant Controller made the assessment to the best of his judgment in August 1981, where he accepted the status of the deceased as Hindu undivided family on the sole ground that the income-tax assessment, for the assessment year 1974-75, in the case of the deceased was made in that status. However, the deceased never submitted any income-tax and wealth-tax returns and no assessment was ever made in his case. The assessment for the assessment year 1974-75 mentioned above was in fact made in the case of the accountable person.

Further, according to the Controller himself, there was no evidence to support the claim for the status of Hindu undivided family. The adoptions of incorrect status as Hindu undivided family instead of individual resulted in short-levy of duty of Rs. 1,37,460.

The Ministry of Finance have accepted the omission (January 1985).

D—INTEREST TAX

4.29 Under the Interest-tax Act, interest-tax is levied at the rate of seven per cent for every assessment year commencing on or after 1 April 1975, on the total amount of interest received by scheduled banks on loans and advances made in India. The Finance Act, 1983, has reduced the rate of tax to three and a half per cent from the assessment year 1984-85 and onwards. However, interest on Government securities as also debentures and other securities issued by local authorities, companies and statutory corporations will not be included in the tax base. Interest received on loans and advances made to other scheduled banks will likewise be exempted from the levy. Interest accruing or arising before 1 August 1974 or during the period commencing on the 1 March 1978 and ending with the 30 June 1980 shall not be liable to tax. The levy of interest tax was also extended to the specified all India Industrial Finance Institutions in respect of interest accruing or arising after 30 June 1980.

4.30 Receipts under interest-tax were included under the head "28—Other Taxes on Income and Expenditure" prior to its exhibition separately under the head "024—Interest Tax" with effect from the financial year 1982-83 Receipts under interest-tax in the financial years 1982-83 and 1983-84 compared as under with the budget estimates of these years :—

Year	Budget Estimates	Actuals
	(In crores of rupees)	
1982-83	220.00	265.47*
1983-84	156.00	177.91*

4.31 *Incorrect computation of chargeable interest*

Under the Interest-tax Act, 1974, there shall be allowed from the total amount of interest (other than interest on loans and advances made to scheduled banks) accruing or arising to the assessee in the previous year, a deduction in respect of the

*Provisional

amount of interest which is established to have become a bad debt during the previous year subject to conditions specified. No deduction, other than the deduction specified above, shall be allowed from the total amount of interest accruing or arising to the assessee. Accordingly, the amounts paid to the Reserve Bank of India on rediscounting of bills were not to be allowed as deduction from the gross amount of chargeable interest.

(i) The accounts of a banking company indicated that provision of Rs. 18,90,533, made for income-tax, interest-tax and bad and doubtful debt, had been deducted from the gross interest receipts and only the net amount credited in the profit and loss account.

However, while computing the chargeable interest for the purpose of interest-tax assessment of the assessee, for the assessment year 1978-79, in October 1979 (revised in August 1981), instead of adding the provision of Rs. 18,90,533, the amount was deducted from the net amount credited in the profit and loss account. This omission resulted in short assessment of interest of Rs. 37,81,066, with consequent short levy of interest-tax of Rs. 2,64,675.

The Ministry of Finance have accepted the mistake (July 1984).

(ii) While completing the assessments of an assessee bank in September 1979, the amounts of Rs. 4,49,200 and Rs. 9,89,980, paid on rediscounting of bills with the Reserve Bank of India during the previous years relevant to the assessment years 1975-76 and 1976-77, were allowed as deduction from the gross amount of chargeable interest of an assessee.

Such charges paid to Reserve Bank of India are not deductible as they are primarily incurred by the Bank to increase the liquidity of the assessee to make loans, advances, etc., and discount bills. Further, the interest-tax Act imposes tax on the gross amount of interest received by the bank on loans and advances (other than loans and advances made to the scheduled banks) made in India and no deduction, excepting deduction for the amount of interest which is established to have become a bad debt, is admissible in computing the chargeable interest. The rediscounting charges thus incorrectly allowed as deduction from

chargeable interest led to short levy of tax of Rs. 1,00,358, in the assessment years 1975-76 and 1976-77.

The Ministry of Finance have accepted the mistake (December 1984).

V. Sundaresan.

(V. SUNDARESAN)
Director of Receipt Audit-I

New Delhi.
The 24-4-1985 1985.

Countersigned

T. N. Chaturvedi

(T. N. CHATURVEDI)
Comptroller and Auditor General of India

New Delhi.
The 24-4-1985 1985.

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ERRATA

Page	Para	Line	*For*	*Read*
(ii)	Table of contents	10 from top	81	82
(iii)	Table of contents	22 from top	—	179
(iii)	Table of contents	23 from top	AN OTHER	ANOTHER
11	1.07(ii)(v)	13 from top	50.34	50.34* *The discrepancy in the figures is under reconciliation by the Ministry of Finance
11	1.08	18 from top	in	is
14	1.08(ii)(b)	5 from bottom (Footnote)	1984	1985
17	1.09(i)(d)	10 from bottom	lakhs	lakh
18	1.09(ii)	10 from top	8842	8802
18	1.09(ii)	14 from top	1,02,329	1,02,309
18	1.09(iii)	24 from top	1983-84	1982-83
18	1.09(iii)	6 from bottom	Delete 1983-84 and figures there against and note thereunder.	
18	1.09(iii)	Delete the Second Footnote		
24	1.11(f)	15 from top	2037	1037
25	1.11(c)	1 from top	(e)	(c)
25	1.11(c)	15-16 from top	Wealth-tax 1957	Wealth-tax Act 1957
26	1.12(i)(b)	15 from top	case	cases
28	1.12(iii)	4 from top	far	foil
30	1.12(c)	Add at the bottom		12. Orissa
30	1.12(c)	Add at the bottom		13. Karnataka
32	1.12(e)(2)	3 from bottom	25,146	29,146
33	1.12 (f)	17 from bottom	below**	**Figures have been furnished by the Ministry of Finance.
45	1.19(1)	4 from top	lakns	lakhs
46	1.19(1)	1 from top	164.84	146.84
46	1.19(1)	2 from top	679.14	769.14
46	1.19(ii)	7 from bottom	Toatl	Total
51	1.21(ii)(a)	1 from bottom	1,80,542	1,08,542
56	1.22(ii)	12 from bottom	leavy	levy
59	2.06	13 from top	1533	1597
59	2.06	—do—	458.94	461.09
60	2.06(ii)	7 from top	1,13,12,455	1,13,12,454
62	2.06(viii)	19 from top	carried on printing	carried on of printing
82	2.13(i)	16 from bottom	September 1984; their reply is awaited (November 1984)	assessment years 1980-81 and 1981-82

Page	Para	Line	For	Read
86	2.19	13-14 from bottom	Delete the words "and invest the money so accumulated or set apart"	
92	2.21(i)	5 from top	officers of	officers in
93	2.22(i)	17 from top	the	in
94	2.22(i)	4 from bottom	1971-82	1971-72
95	2.22(i)	11 from bottom	year	years
96	2.22(iii)	15 from bottom	Schedued	Scheduled
104	2.22(xi)	6 from top	4,79,851	4,79,351
118	2.25(iii)	18 from bottom	resulted in excess computation of depreciation	is admissible in respect of stationery plant
120	2.26(iii)	12 from top	he	the
128	2.28(i)	2 from top	9,331	9.331
148	2.31(v)	3 from bottom	year	years
149	2.31(v)	2 from top	owned	owed
156	2.34(vii)	4 from bottom	benefit	benefits
159	2.34(xi)	6 from bottom	Act units	Act to units
160	2.34(xiii)	2 from bottom	ea lier	earlier
162	2.35(iii)	10 from bottom	1,3,30.782	13,30,782
165	2.37(ii)	3 from top	1,45,000	1,45,00,000
168	2.39	1 from bottom	in	is
173	2.40(vi)	19 from bottom	month	months
177	2.41(ii)	19 from bottom	releveince	relevance
177	2.41(ii)	16 from bottom	in	is
181	Surtex	20 from top	Rs. 394.09 lakhs	Rs. 247.89 lakhs
181	Surtax	20 from top	181	160
202	3.07 (second sub-para)	18 from top	exemptions concessions	exemptions/ concessions
209	3.10(ii)(b)	7 from top	un educed	unreduced
209	3.10(iii)	24 from top	stones. The	stones, the
213	3.12	Last line	tax the	tax under the
233	3.17(vii)	18 from top	instruments	instructions
246	4.01	6 from top	B dget	Budget
249	4.04(i)(c)	18 from top	Match	March
249	4.04(i)(c)	23 from top	were not included	were included
257	4.05(B)(ii)(b)	16 from bottom	depeciated	depreciated
260	4.05(C)(ii)	12 from bottom	asstssee	assessee
270	4.08(i)	2 from top	in	an
275	4.11(i)	17 from top	Isue	Issue
279	4.14	20 from top	case	cases
279	4.14	21 from top	complted	completed
285	4.18(iii)	8 from bottom	rate	date
296	4.23(x)	4 from bottom	lintal	lineal

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