REPORT
OF THE
COMPTROLLER
AND
AUDITOR GENERAL
OF INDIA

FOR THE YEAR

1978-79

UNION GOVERNMENT (CIVIL)

REVENUE RECEIPTS

VOLUME II

DIRECT TAXES

ERRATA

Page	Para	Line	*For*	*Read*
3	1(c)8	10th from bottom	on	or
11	5(ii)A	11th to 13th from top	Amounts under Verification	
17	7(a)(vi)	2nd from bottom	13,02,685	13,02,785
		last line	19,25,464	19,25,564
18	7(a)(viii)	2nd from bottom	21,595&39,191	21,695&39,291
		last line	13,02,685&19,25,464	13,02,785& 19,25,564
22	7(d)	2nd from top	year 1977-78 and	years 1976-77 to
25	9(a)	17th from bottom	undertaking	undertakings
27	9(b)(ii)(5)	Ist from top	2,128	2,728
	10	22nd from top	in come	income
29	11	Ist from top	197879	1978-79
		4th from top	7,61	7.61
		6th from top	income wealth	income/wealth
	12	16th from bottom	1,723,97	1,723.97
			96.315	96,315
31	13 (I)(b)	15th from bottom	provision	provisions
		11th and 13th from bottom	prosectution	prosecutions
32	13(II)	7th from top	3,269	32,69
			118	1,18
		13th, 15th and 18th from top	prosections	prosecutions
		20th from top	fo, avove	of, above
33	14(2)	13th from top	Valutation	valuation
		3rd & 4th from bottom	cummulative	cumulative
34	14(4)	6th from top	determined	determined
		2nd & 3rd from bottom	cummulative	cumulative
		7th from bottom	1976-77 earlier year	1976-77 and earlier years
36	15(1)	9th from top	etx.	etc.
53	24(1)	4th from top	machinry	machinery
55	24(ii)	13th from top	exports	experts
104	52	Last line	campany	company

Page	Para	Line	*For*	*Read*
112	54	Ist line from top	Mistakes in assessment of firms partners	Mistakes in assessment of firms and partners.
114	56(i)	4th from bottom	the karta..... High.	about Rs. 78,500 escaped assessment with
118	59.3	10th from top	beside	besides
123	59.8 (iv)	17th from top	retified	ratified
	59.8 (v)	Last line	cerain	certain
	59.8(v)	Last line	incorrecly	incorrectly
128	59.11(i)	4th from bottom	discretionery	discretionary
132	62	4th from top	insert the word 'were' in between the words 'etc'. and 'continued'.	
138	65(ii)(b)	15th from top	for	from
150	74(i)	10th from top	paragraps	paragraphs
152	74(ii)(c)	5th from top	radios	ratios
172	90	10th from top	Comptroller and Auditor General	Comptroller and Auditor General's.
172	90	19th from top	Comprtoller	Comptroller

Report
of the
Comptroller
and
Auditor General
of India

For the year

1978-79

Union Government (Civil)

Revenue Receipts

Volume II

Direct Taxes

TABLE OF CONTENTS

PREFATORY REMARKS

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

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

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

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

(*iv*) Chapter IV relates to Wealth-tax, Gift-tax and Estate Duty.

(*v*) Chapter V covers points relating to other receipts.

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

Volume II

CHAPTER I

GENERAL

1. *Receipts under various Direct Taxes*

The total proceeds from Direct Taxes for the year 1978-79 amounted to Rs. 2527.73* crores out of which a sum of Rs. 717.33 crores was assigned to the States. The figures for the three years 1976-77, 1977-78 and 1978-79 are given below :—

(In crores of rupees)

	1976-77	1977-78	1978-79
020 Corporation Tax	984.23	1220.77	1251.47
021 Taxes on Income other than Corporation Tax	1194.40	1002.02	1177.39
028 Other Taxes on Income and Expenditure	71.27	115.84	24.53
031 Estate Duty	11.73	12.30	13.08
032 Taxes on Wealth	60.44	48.46	55.41
033 Gift Tax	5.67	5.55	5.85
Gross Total	2327.74	2404.94	2527.73
Less share of net proceeds assigned to the States			
Income-tax	652.24	675.44	706.62
Estate Duty	9.52	9.38	10.71
TOTAL	661.76	684.82	717.33
Net receipts	1665.98	1720.12	1810.40

The gross receipts under Direct Taxes during 1978-79 went up by Rs. 122.79 crores when compared with the receipts during 1977-78 as against an increase of Rs. 77.20 crores in 1977-78 over those for 1976-77. Receipts under Corporation tax accounted for an increase of Rs. 30.70 crores and taxes on income other than Corporation tax Rs. 175.37 crores.

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

*(a) The break-up of total collections of Corporation tax and Taxes on income other than Corporation tax, during 1978-79 as furnished by the Ministry of Finance, is as under :—

Pre-assessment and post-assessment collection of tax during 1978-79 :—

	(In crores of rupees)
(i) Deduction at source	528.48
(ii) Advance tax (net)	1538.47
(iii) Self assessment	240.73
(iv) Regular assessment	246.74
	2554.42

Besides, the Ministry of Finance has intimated tax collection of Rs. 152.43 crores representing Surtax, Surcharge on 020—CT, other receipts and receipts awaiting transfer to other minor heads and refunds of Rs. 278.56 crores.

*(b) The details of deductions at source under broad categories are as under :—

	(In crores of rupees)
(i) Dividends distributed by companies	68.51
(ii) Salaries	207.98
(iii) Payments to contractors	59.43
(iv) Winnings from Lotteries and Crossword Puzzles	3.04

(c) Deduction of tax at source by companies on dividends distributed*:—

(1)	(i) No. of company assessees as on 1-4-1978	42,084
	(ii) No. of company assessees as on 1-4-1979	41,532
	(a) No. of foreign company assessees as on 1-4-1978 [included in (i) above]	1,028
	(b) No. of foreign company assessees as on 1-4-1979 [included in (ii) above]	1,238
(2)	No. of foreign companies which had made the prescribed arrangements for declaration and payment of dividends within India :—	
	As on 1-4-1978	3
	As on 1-4-1979	29

*Figures furnished by the Min. of Finance are provisional.

(3) No. of companies which have distributed dividends during 1978-79 and amount of dividend :—

	Number	Amount of dividend (in thousands of rupees)
(*a*) Indian companies	3,772	1,82,50,85
(*b*) Foreign companies	2	35,79

(4) No. of companies out of (3) from whom the statement prescribed in Rule 37(2) was received:—

(*a*) Indian companies	3,740
(*b*) Foreign companies	2

(5) No. of companies and amount of deduction of tax shown in the statement in (4) above :—

	No. of companies	Amount (in thousands of rupees)
(*a*) Indian companies	3,738	39,43,20
(*b*) Foreign companies	2	8,95

(6) No. of companies out of (4) in which the tax deducted was remitted to banks within a week :—

(*a*) Indian companies	3,623
(*b*) Foreign companies	2

(7) Amount involved in (6) above :—

(*a*) Indian companies	38,68,02
(*b*) Foreign companies	8,95

(8) No. of companies out of (4) which remitted the tax deducted, after one week of date of deduction on receipt of challan :—

(*a*) Indian companies	115
(*b*) Foreign companies	—

(9) No. of companies out of (4) above from whom the returns prescribed in Section 286 were not received, when the dividends paid to a company exceeded Re. 1 and to any other share holder Rs. 5,000 :—

(*a*) Indian companies	—
(*b*) Foreign companies	—

(10) No. of companies out of (3) above which have (a) not deducted tax at source and (b) not furnished the statement prescribed in Rule 37(2) :—

	Tax not deducted at source	State-ment not furnished under Rule 37(2)
(*a*) Indian companies	34	32
(*b*) Foreign companies	—	—

(d) Advance Tax.—Demand and Collection.* Demand raised (*i.e.*, notices issued) and collected by way of advance tax during 1978-79 :—

	Number of cases	Amount (in crores of rupees)
(*i*) Demand raised	Not furnished	1628.56
(*ii*) Demand collected out of (i)	-do-	1535.42
(*iii*) Arrears under advance tax as on 31st March, 1979	-do-	93.14

(e) Figures of interest levied under the various provisions of the Income-tax Act, 1961 are given below :—

	(In (crores of rupees)*
(*i*) The total amount of interest levied under the various provisions of the Income-tax Act during the year 1978-79	136.07
(*ii*) Of the amount of interest levied, the amount	
(*a*) Completely waived by the Department . . .	12.70
(*b*) Reduced by the Department	22.76

2. *Variations between Budget estimates and actuals*

(i) The actuals for the year 1978-79 under the Major heads '021—Taxes on Income etc.'; '031—Estate Duty', '032—Taxes on Wealth' and '033—Gift-tax' exceeded the Budget estimates.

*Figures furnished by the Ministry of Finance.

The figures for the years from 1974-75 to 1978-79 under the various heads are given below :—

Year	Budget estimates	Actuals	Variation	Percentage of variation
			(in crores of rupees)	
(1)	(2)	(3)	(4)	(5)
020—Corporation Tax				
1974-75	661.00	709.48	48.48	7.33
1975-76	780.50	861.70	81.20	10.40
1976-77	1025.00	984.23	(—)40.77	(—)3.98
1977-78	1298.20	1220.77**	(—)77.43	(—)5.96
1978-79	1441.90	1251.47**	(—)190.43	(—)13.20
021—Taxes on Income etc.*				
1974-75	709.00	878.25	169.25	23.87
1975-76	791.00	1214.36	423.36	53.52
1976-77	957.00	1194.40	237.40	24.81
1977-78	1038.20	1002.02**	(—)36.18	(—)3.48
1978-79	1134.80	1177.39**	42.59	3.75
031—Estate Duty*				
1974-75	9.00	10.94	1.94	21.55
1975-76	9.25	11.65	2.40	25.95
1976-77	8.75	11.73	2.98	4.06
1977-78	10.75	12.30**	1.55	14.42
1978-79	11.00	13.08**	2.08	18.91
032—Taxes on wealth				
1974-75	40.00	39.23	(—)0.77	(—)1.92
1975-76	43.00	53.73	10.73	24.95
1976-77	52.00	60.44	8.44	16.23
1977-78	54.90	48.46**	(—)6.44	(—)11.73
1978-79	55.00	55.41**	0.41	0.75
033—Gift-tax				
1974-75	4.00	5.06	1.06	26.50
1975-76	4.50	5.11	0.61	13.55
1976-77	4.75	5.67	0.92	19.37
1977-78	5.50	5.55**	0.05	0.91
1978-79	5.75	5.85**	0.10	0.18

*Gross figures have been taken.

**Figures furnished by the Controller General of Accounts are provisiona

(ii) The details of variations under the heads subordinate to the Major heads 020 and 021 for the year 1978-79 are given below :—

	Budget	Actuals	Increase(+) Short fall(—)	Percentage of variation
		(In crores of rupees)		
020—Corporation Tax				
(*i*) Income-tax on companies	1379.90	1153.13	(—)226.77	(—)16.43
(*ii*) Surtax	55.00	47.84	(—)7.16	(—)13.02
(*iii*) Surcharge	..	44.71	44.71	—
(*iv*) Other receipts*	7.00	5.79	(—)1.21	(—)17.29
	1441.90	1251.47**	(—)190.43	(—)13.20
021—Taxes on Income other than Corporation Tax				
(*i*) Income-tax	991.75	1012.42	20.67	2.08
(*ii*) Surcharge	127.00	115.92	(—)11.08	(—)8.72
(*iii*) Receipts awaiting transfer to other minor-heads	..	36.03	36.03	..
(*iv*) Other receipts	16.05	13.02	(—)3.03	(—)18.88
Deduct share of Proceeds assigned to States	735.95	706.62	29.33	3.98
	398.85	470.77**	71.92	18.03

*Budget provision under "other receipts" has been shown as against "Miscellaneous receipts".

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

3. *Cost of collection*

The expenditure incurred during the year 1978-79 in collecting Corporation tax and Taxes on Income other than Corporation Tax, together with the corresponding figures for the preceding three years is as under :—

(In crores of rupees)

	Gross collection	Expenditure on Collections
020—Corporation Tax		
1975-76	861.70	4.85
1976-77	984.23	4.91
1977-78	1220.77	5.18
1978-79*	1251.47	5.68
021—Taxes on Income- etc.		
1975-76	1214.36	33.96
1976-77	1194.40	34.38
1977-78	1002.02	36.28
1978-79*	1177.39	47.59

**4. *Total number of Assessees*

(i) The total number of assessees (including companies) in the books of the Department as on 31st March, 1979 was 39,69,965. As compared to the previous year ending 31st March, 1978 there was an increase of 14,721 assessees. The number of assessees status-wise as on 31st March, 1978 and 31st March, 1979 was as under :—

	As on 31st March, 1978	As on 31st March, 1979
Individuals	30,37,778	30,52,482
Hindu undivided families	2,02,349	2,11,036
Firms	6,20,499	6,11,088
Companies	42,084	41,532
Others	52,534	53,827
TOTAL	39,55,244	39,69,965

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

**Information supplied by Min. of Finance

(vi) The number of estate duty assessments completed during 1978-79 was as follows :—

Principal value of property	Number of assessments completed
(*i*) Exceeding Rs. 20 lakhs	10
(*ii*) Between Rs. 10 lakhs and Rs. 20 lakhs	48
(*iii*) Between Rs. 5 lakhs and Rs. 10 lakhs	453
(*iv*) Between Rs. 1 lakh and 5 lakhs	6,653
(*v*) Between Rs. 50,000 and Rs. 1 lakh	7,180
TOTAL	14,344

5. *Information in respect of Foreign Companies*

(i) Information in respect of foreign companies, including companies which have declared their Indian income on the basis of apportionment of their global income, is given below :—

A. Cases where returns have been filed and assessments completed as on 31-3-1379:—

	Number	Amount (In crores of rupees)*
(*i*) No. of foreign companies	412	
(*ii*) Income returned		83
(*iii*) Income assessed		91
(*iv*) Gross demand		38
(*v*) Demand outstanding out of (iv) as on 31-3-1979		06
(*vi*) Tax paid upto 31-3-1979 [(iv)-(v)]		32

B. Cases where returns have been filed but assessments were pending as on 31-3-1979:—

	Number	Amount (In crores of rupees)
(*i*) No. of foreign companies	482	
(*ii*) Income returned		73
(*iii*) Gross demand being tax due on income returned		44
(*iv*) Demand outstanding out of (iii) as on 31-3-1979		02
(*v*) Tax paid upto 31-3-1979 [(iii)—(iv)]		42

C. Cases where no returns have been filed as on 31-3-1979:—
Number of foreign companies 345

*Information supplied by Ministry of Finance.

(ii) Information in respect of only those foreign companies which have declared their Indian income on the basis of apportionment of their global income is as under :—

A. Cases where returns have been filed and assessments completed as on 31-3-1979 :—

	Number	Amount (in crores of rupees)
(*i*) Number of foreign companies . . .	81	
(*ii*) Global Income shown		21
(*iii*) Income returned		17
(*iv*) Income assessed		08
(*v*) Gross demand		12
(*vi*) Demand outstanding out of (v) as on 31-3-1979		—
(*vii*) Tax paid upto 31-3-1979 [(v)-(vi)] . . .		12

B. Cases where returns have been filed but assessments were pending as on 31-3-1979 :—

	Number	Amount (In crores of rupees)
(*i*) Number of foreign companies . . .	68	
(*ii*) Global Income shown		84
(*iii*) Income returned		29
(*iv*) Gross demand being tax due on Income returned		19
(*v*) Demand outstanding out of (iv) as on 31-3-1979		—
(*vi*) Tax paid upto 31-3-1979		19

C. Cases where no returns have been filed as on 31-3-1979 :—
No. of foreign companies 12

*6. *Arrears of tax demands*

(a) *Corporation Tax and Income-tax*

(i) The total demand of tax raised and remaining uncollected as on 31st March, 1979 was Rs. 734.87 crores. This did not include Rs. 175.77 crores, the collection of which had not fallen due on that date but included Rs. 7.40 crores claimed to have been paid but pending verification/adjustment, Rs. 154.73 crores stayed/kept in abeyance and Rs. 17.84 crores for which instalments had been granted.

*Information supplied by Min. of Finance.

(ii) The figures of Corporation tax, Income-tax, interest and penalty comprised in the gross arrears of Rs. 910.64 crores and the years to which they relate are shown below :—

	Corporation tax	Income tax	Interest	Penalty	Total (in crores of rupees)*
Arrears of 1968-69 and earlier years .	16.30	44.64	8.28	7.75	76.97
1969-70 to 1975-76 .	28.85	131.54	52.40	36.69	249.48
1976-77 . .	12.93	47.18	22.60	14.30	97.01
1977-78 . .	28.59	70.44	42.28	19.59	160.90
1978-79 . .	81.37	143.81	74.86	26.24	326.28
TOTAL .	168.04	437.61	200.42	104.57	910.64

(iii) The table below shows the number of assessees from whom gross arrears of *Rs. 910.64 crores are due :—

Arrear demands	Number of assessees	Total arrears of tax (in crores of rupees)*
Upto Rs. 1 lakh in each case	33,55,934	458.11
Over Rs. 1 lakh upto Rs. 5 lakhs in each case . .	5,753	111.94
Over Rs. 5 lakhs upto Rs. 10 lakhs in each case .	833	55.48
Over Rs. 10 lakhs upto Rs. 25 lakhs in each case .	479	74.28
Over Rs. 25 lakhs in each case	291	210.83
TOTAL	33,63,290	910.64

*Figure furnished by the Ministry of Finance is provisional.

(iv) Tax demand certified to Tax Recovery Officers and State Government Officers for recovery and its year-wise particulars to the end of 1978-79 are as under :—

	Demand certified		Total	Demand recovered	Balance
	At the beginning of the year	During the year			
				(In crores of rupees)	
1969-70 . .	359.52	183.55	543.07	116.45	426.62
1970-71 . .	425.25	181.36	606.61	145.37	461.24
1971-72 . .	483.53	208.79	692.32	167.52	524.80
1972-73 . .	530.57	264.98	795.55	189.06	606.49
1973-74 . .	598.15	192.62	790.77	161.93	628.84
1974-75 . .	616.07	188.16	804.23	176.29	627.94
1975-76 . .	616.35	333.92	950.27	290.56	659.71
1976-77 . .	678.72	330.30	1009.02	370.67	638.35
1977-78 . .	638.00	258.00	896.00	244.00	652.00
1978-79*	655.00	309.00	964.00	267.00	697.00

NOTE:— In 6,41,924 cases, recovery certificates were issued during the year 1978-79.

(v) Demands of Income-tax (including Corporation-tax) stayed as on 31st March, 1979 on account of appeals and revision petitions were as under :—

	(In crores of rupees)*
(*a*) By courts	18.82
(*b*) Under Section 243F(2) (applications to Settlement Commission).	7.17
(*c*) By Tribunal	4.32
(*d*) By Income-tax authorities due to :—	
(*i*) Appeals and revisions	83.56
(*ii*) D.I.T. Claims	6.81
(*iii*) Restriction on remittances—Section 220(7) . .	0.75
(*iv*) Other reasons	33.30
TOTAL	154.73

*Figures furnished by Min. of Finance are provisional.

(vi) Arrears of Sur-tax demands outstanding as on 31st March, 1979 were as follows :—

Relating to demands raised in	Amount outstanding (In thousands of rupees)*
1969-70 and earlier years	57,61
1970-71	96
1971-72	3,87
1972-73	7,86
1973-74	6,94
1974-75	17,54.8
1975-76	18,20
1976-77	32,64
1977-78	3,72,04
1978-79	5,74,65.9
TOTAL	10,92,32.7

(vii) The following table shows the position of arrears of Annuity Deposits for the last three years :—

	As on 31st March 1977	As on 31st March 1978	As on 31st March 1979
		(In lakhs of rupees)*	
(*i*) Arrears out of Advance Annuity Deposits	..	..	..
(*ii*) Arrears out of self and provisional Annuity Deposits	0.02	..	..
(*iii*) Arrears out of Regular Annuity Deposits	1284.02	1075.11	864.59
TOTAL	1284.04	1075.11	864.59

*Information supplied by Min. of Finance.

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

(i) The following table shows the year-wise arrears of demands outstanding and the number of cases relating thereto under the three other direct taxes *i.e.*, wealth-tax, gift-tax and estate duty as on 31st March, 1979 :—

(In crores of rupees)

	Wealth-tax		Gift-tax		Estate Duty	
	Number of cases	Amount Rs.	Number of cases	Amount Rs.	Number of cases	Amount Rs.
1974-75 and earlier years.	38944	8.95	11494	2.11	4086	5.33
1975-76	16598	5.48	4449	0.48	1148	1.72
1976-77	22484	7.70	5654	0.67	2003	1.83
1977-78	38109	13.80	10256	1.58	3507	2.94
1978-79	113071	148.15	23935	12.88	8049	5.29
TOTAL	229206	184.08	55788	17.72	18793	17.11

(ii) Demands of tax/duty stayed on appeals and revision petitions for Wealth-tax, Gift-tax and Estate Duty, as on 31st March, 1979 were as under :—

(In lakhs of rupees)

	Wealth-tax	Gift-tax	Estate Duty
(*a*) By Courts	65.40	4.70	49.29
(*b*) By Wealth-tax/Gift-tax/Estate Duty authorities :			
(*i*) Pending disposal of appeals etc. (including amounts under protective assessments) . . .	538.73	79.15	215.49
(*ii*) Pending disposal of settlement petitions	84.32	2.94	11.18
(*iii*) For other reasons . . .	82.55	46.41	207.38

7. **Arrears of assessments*

(a) *Income-tax including Corporation tax*

(i) The number of assessment cases to be finalised as on 31st March, 1979 has increased as compared to that at the close of the previous year. The number of assessments pending as

*Information supplied by Min. of Finance.

on 31st March, 1979 was 19.26 lakhs as compared to 15.38 lakhs as on 31st March, 1978 and 17.42 lakhs as on 31st March, 1977. Of the 19.26 lakhs of pending cases as many as 10.52 lakh cases related to small income and summary assessments.

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

		Number of assessments completed				
Financial year	Number of assessments for disposal	Out of current	Out of arrears	Total	Percentage	Number of assessments pending at the end of the year
1974-75	55,18,327	24,23,575	14,17,271	38,40,846	69.6	16,77,481
1975-76	57,34,327	25,08,108	14,99,536	40,07,644	69.9	17,26,683
1976-77	56,90,717	24,88,743	14,60,136	39,48,879	69.4	17,41,838
1977-78	55,81,355	25,72,678	14,71,135	40,43,813	72.5	15,37,542
1978-79	52,35,891	21,07,544	12,02,783	33,10,327	63.2	19,25,564

(iii) Category-wise break-up of the total number of assessments completed during the years 1977-78 and 1978-79 is as under :—

	1977-78	1978-79
(*a*) Business cases having income over Rs. 25,000	2,75,248	2,33,472
(*b*) Business cases having income over Rs. 15,000 but not exceeding Rs. 25,000 . . .	1,50,733	1,37,511
(*c*) Business cases having income over Rs. 7,500 but not exceeding over Rs. 15,000 . . .	2,19,303	2,01,362
(*d*) All other cases (including refund cases) except those mentioned in categories (e) and (f) .	3,49,871	2,79,929
(*e*) Small income scheme cases, Government salary and non-Government salary cases below Rs. 18,000	60,731	45,888
(*f*) Summary assessments	29,87,927	24,12,165
TOTAL	40,43,813	33,10,327

(iv) Status-wise break-up of income-tax assessments completed during the years 1977-78 and 1978-79 is as under :—

	1977-78	1978-79
(*i*) Individuals	31,85,228	25,49,938
(*ii*) Hindu Undivided Families	1,94,186	1,77,732
(*iii*) Firms	5,84,815	5,08,196
(*iv*) Companies	41,533	35,982
(*v*) Association of persons	38,051	38,479
TOTAL	40,43,813	33,10,327

(v) The position of assessments completed under Summary Assessment Scheme is as under :—

1. Total number of assessments completed under Section 143(1) of the Act.	24,12,165
2. Assessments made under Section 143(2)(a) of the Act. (where an assessment having been made under Section 143(1) and assessee makes within one month an application objecting to the assessment).	1,804
3. Assessments made under Section 143(2)(b) that is where the Income-tax Officer considers it necessary to verify the correctness of the return by requiring the presence of the assessee	1,107

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

	As on 31st March 1977	As on 31st March 1978	As on 31st March 1979
1974-75 and earlier years	91,770	37,426	24,828
1975-76	4,07,231	37,797	19,233
1976-77	12,42,837	3,84,814	61,185
1977-78	—	10,77,505	5,17,533
1978-79	—	—	13,02,685
TOTAL	17,41,838	15,37,542	19,25,464

(vii) Category-wise break-up of pending income-tax assessments as on 31st March, 1978 and 31st March, 1979 is as under :—

	As on 31st March, 1978	As on 31st March, 1979
(*a*) Business cases having income over Rs. 25,000 .	1,64,340	1,86,943
(*b*) Business cases having income over Rs. 15,000 but not exceeding Rs. 25,000	1,59,232	1,72,335
(*c*) Business cases having income over Rs. 7,500 but not exceeding Rs. 15,000	2,07,908	2,17,097
(*d*) All other cases (including refund cases) except those mentioned in categories (e) and (f) below .	2,93,088	2,97,258
(*e*) Small income scheme cases, Government salary cases and non-Government salary cases below Rs. 18,000	50,567	35,900
(*f*) Summary assessments	6,62,407	10,16,031
TOTAL	15,37,542	19,25,564

(viii) Status-wise and year-wise break-up of pendency of income-tax assessments as on 31st March, 1979 is as under :—

Status	1974-75 and earlier years	1975-76	1976-77	1977-78	1978-79	Total
Individuals .	15,766	13,285	43,630	3,44,702	9,56,799	13,74,182
Hindu undivided families .	1,813	1,413	3,841	33,548	79,319	1,19,934
Companies .	2,687	938	2,551	12,573	21,814	40,563
Firms .	3,761	3,061	9,802	1,11,812	2,23,158	3,51,594
Association of persons .	801	536	1,361	14,898	21,595	39,191
TOTAL .	24,828	19,233	61,185	5,17,533	13,02,685	19,25,464

(ix) Re-opened assessments and set aside assessments which are pending.

(1) Year-wise details of assessments cancelled under Section 146 of the Income-tax Act, 1961 (or under the corresponding provisions of the old Act) and which are pending finalisation on 31st March, 1979 are as follows :—

Assessment year	Number of assess-ments
1970-71 and earlier years	2,164
1971-72	289
1972-73	399
1973-74	661
1974-75	1,255
1975-76	2,055
1976-77	2,509
1977-78	1,248
1978-79	1,452
TOTAL	12,032

(2) Year-wise details of assessments cancelled under Section 263 of the Income-tax Act, 1961 (or under the corresponding provisions of the old Act) which are pending finalisation on 31st March, 1979 are as follows :—

Assessment year	Number of assess-ments
1970-71 and earlier years	349
1971-72	33
1972-73	56
1973-74	87
1974-75	92
1975-76	76
1976-77	76
1977-78	88
1978-79	81
TOTAL	938

(3) Year-wise details of assessments set aside by the Appellate Assistant Commissioners under Section 251 of the Income-tax Act, 1961 (or under the corresponding provisions of the old Act) or by the Appellate Tribunals 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 31st March, 1979 :—

Set aside by Appellate Assistant Commissioners		Set aside by Appellate Tribunals	
Assessment year	Number of cases	Assessment year	Number of cases
1970-71 and earlier years	3039	1970-71 and earlier years	554
1971-72	379	1971-72	65
1972-73	517	1972-73	119
1973-74	723	1973-74	133
1974-75	1040	1974-75	140
1975-76	1038	1975-76	116
1976-77	861	1976-77	117
1977-78	627	1977-78	124
1978-79	779	1978-79	104
TOTAL	9,003		1,472

(b) *Pendency of Super Profits Tax and Surtax assessments*

The position of pendency as on 31st March, 1979 is given below :—

(Amount in thousands of rupees)

	Super Profits tax	Surtax
(*i*) Total number of cases for disposal during 1978-79	12	5,204
(*ii*) Number of cases disposed of provisionally	..	760
(*iii*) Number of cases disposed of finally	1	988
(*iv*) Amount of demand raised on provisional assessments	..	41,32,14.9
(*v*) Amount of demand collected on provisional assessments	..	38,72,97.1
(*vi*) Amount of demand raised on final assessments	28,21	25,94,08.4
(*vii*) Amount of demand collected on final assessments	29,76	25,07,38.1
(*viii*) Number of cases pending as on 31st March 1979	11	4,216
(*ix*) Approximate amount of tax involved in (viii)	194	34,80,21.7

Year-wise details of assessments under Companies (Profits) Surtax Act, 1964, pending as on 31st March, 1979 are as under :—

	Number of assessments
1969-70 and earlier years	48
1970-71	20
1971-72	35
1972-73	69
1973-74	107
1974-75	226
1975-76	441
1976-77	831
1977-78	1176
1978-79	1238
TOTAL	4191

(c) Year-wise details of Wealth-tax, Gift-tax and Estate Duty assessments pending on 31st March, 1979 are given below. The approximate amount of tax/duty involved therein has not been furnished by the Ministry of Finance :—

	Number of assessment pending		
	Wealth-tax	Gift-tax	Estate duty
1974-75 and earlier years	9,942	2,581	4,509
1975-76	35,936	2,520	3,220
1976-77	46,147	2,966	4,932
1977-78	63,478	3,896	6,117
1978-79	1,76,058	9,844	9,024
TOTAL	3,31,561	21,807	27,802

(d) *Incentive Scheme for outstanding performance in assessment work.*

As a result of Public Accounts Committee's recommendation to improve the performance of assessment work and in order to encourage the Income-tax Officers to give their best, an Incentive Scheme for quality work in assessment has been introduced from 1st April, 1976. The Scheme contemplates 20 cash awards, 8 of Rs. 2,000 each and 12 of Rs. 1,000 each to be given annually to the Assessing Officers whose assessments are rated to be the best of the year.

The information regarding the number of beneficiaries and the amount disbursed is 'nil' for the year 1977-78 and 1978-79.

8. *Appeals and Revision petitions**

(i) (a) Particulars in respect of Income-tax appeals pending on 31st March, 1979 are as under :—

	Income-tax appeals with Appellate Assistant Commissioners Cs.I.T. (Appeal)	Income-tax revision petitions with Commissioners
Number of appeals/revision petitions . . .	2,23,012	9,462
(*a*) Out of appeals/revision petitions instituted during 1978-79	1,41,141	5,672
(*b*) Out of appeals/revision petitions instituted in earlier years	81,871	3,790

(b) Particulars in respect of Wealth-tax, Gift-tax and Estate Duty appeals and Revision petitions pending on 31st March, 1979 are as under :—

	Appeals with Asstt. Appellate Commissioners CsIT (Appeals)			Revision petitions with Commissioners of Income-tax		
	W.T.	G.T.	E.D.	W.T.	G.T.	E.D.
(*i*) No. of appeals/ revision petition pending . .	47,142	2,843	5,316	1,826	119	..
(*ii*) Out of appeals/ revision petitions instituted during 1978-79 . .	31,033	1,885	2,648	944	83	..
ii) Out of appeals/ revision petitions instituted in earlier years . .	16,109	958	2,668	882	36	..

*Information supplied by Ministry of Finance.

(ii) (a) Year-wise break-up of Income-tax appeal cases and revision petitions pending with Appellate Assistant Commissioners and Commissioners of Income-tax (Appeals), and C.I.T's for the periods ending 31st March, 1978 and 31st March, 1979 respectively with reference to the year of institution is as under :—

Years of institution	Appeals pending with Appellate Assistant Commissioners/Cs.I.T. (Appeal)		Revision petitions pending with Commissioners of Income-tax*	
	31st March 1978	31st March 1979	31st March 1978	31st March 1979
1970-71 and earlier years	183	155	112	89
1971-72	195	187	119	84
1972-73	689	563	124	89
1973-74	999	793	179	124
1974-75	2,755	1,846	275	177
1975-76	12,461	5,341	481	258
1976-77	44,265	19,521	1,500	689
1977-78	1,22,884	53,465	6,403	2,280
1978-79	..	1,41,141	..	5,672
TOTAL	1,84,431	2,23,012	9,193	9,462

(b) Year-wise break-up of Wealth-tax, Gift-tax and Estate Duty appeal cases and revision petitions pending with Appellate Assistant Commissioners and Commissioners of Income-tax for the period ending 31st March, 1979, with reference to the year of institution, is as under :—

Years of institution	Appeals pending with Appellate Asstt. Commissioners*			Revision petitions pending with Commissioners of Income-tax*		
	W.T.	G.T.	E.D.	W.T.	G.T.	E.D.
1970-71 and earlier years	16	..	4	47	..	..
1971-72	36	..	17	16	..	..
1972-73	31	1	14	24	..	..
1973-74	78	6	14	53	..	..
1974-75	203	15	34	57	1	..
1975-76	1,121	78	243	81	4	..
1976-77	3,931	185	725	178	7	..
1977-78	10,693	673	1,617	426	24	..
1978-79	31,033	1,885	2,648	944	83	..
TOTAL	47,142	2,843	5,316	1,826	119	..

*Information supplied by Min. of Finance.

(iii) The following table gives details of appeals/references disposed of during 1976-77, 1977-78 and 1978-79 :—

	1976-77	1977-78	1978-79
(*i*) (*a*) No. of appeals filed before Appellate Assistant Commissioners	2,13,612	1,87,173	2,18,589
(*b*) No. of appeals disposed of during 1978-79 by AAC's .	1,69,347	64,289	1,63,510
(*ii*) No. of appeals filed before Income-tax Appellate Tribunals during 1978-79			
(*a*) by the assessees . . .	31,067	30,429	25,080
(*b*) by the department . .	17,532	16,981	17,089
(*iii*) No. of assessees appeals decided by the Tribunals in favour of the assessees out of (*ii*)(*a*) above .	12,995	11,560	12,996
(*iv*) No. of departmental appeals decided by the Tribunals in favour of the department out of (*ii*)(*b*) above	4,468	3,396	3,389
(*v*) No. of references filed to the High Courts			
(*a*) by the assessees . . .	1,868	1,569	1,645
(*b*) by the department . .	3,705	3,925	4,517
(*vi*) No. of references in the High Courts disposed of in favour of the			
(*a*) assessees partly or wholly .	635	99	260
(*b*) department partly or wholly .	113	293	616
(*vii*) No. of appeals filed to the Supreme Court			
(*a*) by the assessees . . .	36	26	36
(*b*) by the department . .	115	146	65
(*viii*) No. of appeals disposed of by the Supreme Court in favour of the			
(*a*) assessees partly or wholly .	..	..	28
(*b*) department partly or wholly .	11	2	8

9. *Reliefs and Refunds**

(a) *Reliefs*

The Income-tax Act contains several provisions in Chapter VI-A, affording reliefs to tax-payers either for the purpose of providing an incentive for saving or development or for the purpose of relieving hardship arising from certain types of obligatory expenditure. The Ministry of Finance was requested to furnish information regarding the number of cases where these tax benefits were actually availed of by the assessees and the following table gives the information, as furnished by them for the year 1977-78 :—

	No. of assess-ments	Amount of relief allowed
	(In thousands	of rupees)
(*i*) Relief on account of expenditure on medical treatment of handicapped dependants . .	515	1,30
(*ii*) Relief in respect of payments for securing retirement benefits	70	62
(*iii*) Relief in respect of incomes earned by Indian teachers, research workers working in foreign universities and educational institutions .	46	1,02
(*iv*) Relief for newly established industrial undertaking or ships or hotels	408	2,47,45
(*v*) Relief for expenditure incurred on education abroad of children of foreigners . . .	156	54
(*vi*) Relief for industrial undertakings which provide employment for displaced persons .	164	11,47

(b) *Refunds*

(i) Refunds under Section 237 :—

1. No. of applications pending on 1-4-1978	5,660
2. No. of refund applications received during the year 1978-79 .	1,21,287
3. No. and amount of refunds made during 1978-79 :	
(*a*) Out of (1) above	
(*i*) Number	5,584
(*ii*) Amount (in thousands of rupees)	41,77
(*b*) Out of (2) above	
(*i*) Number	1,10,520
(*ii*) Amount (in thousands of rupees)	11,33,41

*Information furnished by Min. of Finance.

4. No. of refund cases in which interest was paid under Section 243, the amount of such interest, and the amount of refund, on which such interest was paid during 1978-79 :

(*a*) Out of (1) above

(*i*) Number . . . .

(*ii*) Amount of refund (in thousands of rupees) . . ..

(*iii*) Amount of interest paid . . . .

(*b*) Out of (2) above

(*i*) Number 878

(*ii*) Amount of refunds (in thousands of rupees) . . 7,78

(*iii*) Amount of interest paid (in thousands of rupees) . 77

5. No. and amount of refunds made during 1978-79 on which no interest was paid :

(*i*) Number 1,15,226

(*ii*) Amount (in thousands of rupees) 11,67,40

6. No. of refund applications pending as on 31-3-1979 . . 10,843

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

(*i*) Refund applications for less than a year . . . 10,767

(*ii*) Between 1 year and 2 years 75

(*iii*) For 2 years and more 1

(ii) Appeal/Revision etc. effects and Refunds under Section 240 and payment of interest under Section 244 :—

1. No. of assessments which were pending revision on account of appellate/revision etc. orders 7,526

2. No. of assessments which arose for similar revision in 1978-79 1,07,351

3. No. of assessments which were revised during 1978-79 :

(*i*) Out of those pending as on 1-4-78 7,242

(*ii*) Out of those that arose during 1-4-78 to 31-3-1979 . 1,01,124

4. No. of assessments which resulted in refunds as a result of revision and total amount of refund given :

	Number	Amount of refund
		(In thousands of rupees)
(*i*) Under item 3(*i*) above	4,607	1,43,64
(*ii*) Under item 3(*ii*) above	48,675	40,18,09

5. No. of assessments n which interest became payable under Section 244 and amount of interest :

(*i*) Under item 4(*i*) above 153 1,78

(*ii*) Under item 4(*ii*) above	1,375	2,128
6. No. of assessments pending revision on 1-4-1979:		
(*i*) Out of (1) above	284	
(*ii*) Out of (2) above	6,227	
7. Break-up of assessments mentioned at (6) above :		
(*i*) Pending for less than 1 year . . .	6,227	
(*ii*) Pending for more than 1year and less than 2 years	284	
(*iii*) Pending for more than 2 years . . .	—	

10. *Searches and Seizures**

	1976-77	1977-78	1978-79
(*i*) Total number of searches and seizure operations conducted .	3,571	617	1345
		(In lakhs of rupees)	
(*ii*) Total amount each of money, bullion and jewellery or other valuable articles or things seized :			
Cash	352	101	220
Jewellery and bullion . .	1,031	119	261
Other assets	661	133	100
TOTAL	2,044	353	581
(*iii*) Amount of concealed in come estimated u/s 132(5) in (*i*) above	**	**	1062
(*iv*) Total amount each of money, bullion and jewellery or other valuable articles or things released by 31-3-1977/31-3-1978/31-3-1979 :			
Cash	56	23	32
Jewellery and bullion . .	391	31	45
Other assets	163	11	9
TOTAL	610	65	86
(*v*) Total amount of money, bullion and jewellery or other valuable articles or things held as on 31-3-1977/31-3-1978/31-3-1979 irrespective of the year of search :			
Cash	588	410	477
Bullion and jewellery . .	1,795	1,004	983
Other assets	854	640	469
TOTAL	3,237	2,054	1,929
(*vi*) The earliest date from which any of these assets is still retained .			4/6/1965

*Information furnished by Min. of Finance.

**Information awaited from the Ministry of Finance.

(*vii*) The arrangements made for the safe custody of assets still held and for their physical verification	Cash is deposited in the Personal Deposit Accounts of the Commissioners of Income-tax in the Reserve Bank of India. Other valuables are kept either in well-guarded strong-rooms in the office building or in the treasuries or in Bank vaults etc.
(*viii*) No. of assessments involved in Search and Seizure operations pending as on 1-4-1978 . .	4424
(*ix*) No. of assessments proceedings started during 1978-79 . .	2583
(*x*) No. of assessments completed out of (*viii*) above during 1978-79 .	2081
(*xi*) No. of assessments completed out of (*ix*) above during 1978-79 .	826
(*xii*) Balance out of (*viii*) pending as on 31-3-1979	2343
(*xiii*) Balance out of (*ix*) pending as on 31-3-1979	1757
(*xiv*) No. of prosecutions in Search and Seizure cases launched during the year irrespective of the date of search	24
(*xv*) No. of convictions obtained during the year:	
(*a*) Out of prosecutions launched in earlier years	13
(*b*) Out of prosecutions launched during theyear . . .	..

11. *Cases settled by Settlement Commission*

	1976-77	1977-78	1978-79
1. No. of cases disposed of by the Commission :			
Income-tax	12*	83*	113**
Wealth-tax	2	13	68
2. No. of assessment years involved	42	313	I.T.630 W.T.480
3. Amount of income in dispute which is the subject matter of applications (Rs. in crores)		9.90*	I.T.9.61** W.T 37.06

* Rs. 9.90 crores for 77 cases out of 95 cases. The balance 12 cases were not capable of quantification as intimated by Ministry of Finance.

** No. of cases involving quantified dispute is 99 out of total disposal of 113 Income-tax cases and 61 out of total disposal of 68 W.T. cases The balance involved issues not capable of quantification.

4. Out of (3) above, the amount offered for settlement	1976-77 and 1977-78		197879
	Rs. (in crores) 4.62	I.T.	Rs. 2.05
		W.T.	Rs. 7,61
5. Out of (3) above, the actual income wealth determined by the Commission	Rs. (in crores) 7.70	I.T.	Rs. 4.55
		W.T.	Rs. 26.61
6. Tax on (5) above	Not available		Not available
7. Penalty and Interest:	No. of cases	Amount	No of cases	Amount
(*a*) Penalties under section 271(1)(c) of the IT Act, 1961	3	2,45,226	I.T.1	5,000
			W.T.2,	38,163
(*b*) Other penalties	1	Amount not	I.T.1	27,753
			W.T.3	37,812
(*c*) Interest levied	10	quantified	I.T.16	16,25,534
			W.T.—	—
8. Recovery of tax, penalty and Interest			Not available	
9. Balance of Tax outstanding			Not available	

12. *Revenue demands written off by the Department**

(a) A demand of Rs. 2155 lakhs in 96,641 cases was written off by the Department during the year 1978-79. Of this, a sum of Rs. 431.04 lakhs relates to 326 company assessees and Rs. 1,723,97 lakhs to 96,315 non-company assessees.

	Companies		Non companies		Total	
	No.	Amount Rs.	No.	Amount Rs.	No.	Amount Rs.
1 2	3	4	5	6	7	8
I. (*a*) Assessees having died leaving be hind no assets or gone into liquidation or become insolvent:	92	74,88,902	999	6,38,31,923	1091	7,13,20,825

*Figure furnished by the Min. of Finance.

(*b*) Companies which are defunct though not gone into liquidation	104	97,38,447			104	97,38,447
TOTAL	196	1,72,27,349	999	6,38,31,923	1195	8,10,59,272
II. Assessees being untraceable	41	24,59,302	45,887	3,14,23,099	45,928	3,38,82,401
III. Assessees having left India	2	21,12,659	12,089	2,33,56,254	12,091	2,54,68,913
IV. For other reasons :						
(*i*) Assessees who are alive but have no attachable assets	17	1,87,60,530	3989	3,65,46,885	4006	5,53,07,415
(*ii*) Amount being petty etc.	63	1,69,107	32,619	73,79,438	32,682	75,48,545
(*iii*) Amount written off as a result of settlement (cases of scaling down of demand)	2	20,00,000	408	12,62,000	410	32,62,000
(*iv*) Demands rendered unenforceable by subsequent developments such as duplicate demands wrongly made demands being protective etc.	1	3,25,000	243	84,35,190	244	87,60,190
TOTAL	83	2,12,54,637	37,259	5,36,23,513	37,342	7,48,78,150

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 realisalion are considered disproportionate to the amount for recovery	4	49,600	81	1,62,449	85	2,12,049
GRAND TOTAL	326	4,31,03,547	96,315	17,23,97,238	96,641	21,55,00,785

13. *Penalties for Concealment and Prosecution*

I. (a) *Income-tax*

(*i*) No. of orders of penalty under Section 28(1)(c)/271(1)(c) passed during 1978-79	28,776
(*ii*) Concealed income involved in (i) above .	Rs. 14.96 crores
(*iii*) Total amount of penalty levied in (i) above	Rs. 11.96 crores

(b) *Position of prosecution cases under the provision* of the Income tax Act

(*i*) No. of prosectution pending before the courts on 1-4-78	533
(*ii*) No. of prosections complaints filed during 1978-79 under section 276(c) (substituted w.e.f. 1-10-75), 276CC, 276-D, 277 and 278	62
(*iii*) No. of prosecutions decided during 1978-79	38
(*iv*) No. of convictions obtained in (iii) above	13
(*v*) No. of cases which were compounded before launching prosecutions . . .	7
(*vi*) Composition money levied in such cases [(v) above] (Amount in thousands) .	1,21

(II) *Wealth-tax and Gift-tax*

	Wealth tax (In thousands of Rs.)	Gift tax
(*a*) (*i*) No. of orders of penalty under Section 18(1)(c)/17(1)(c) passed during 1978-79 .	3,269	118
(*ii*) Amount of concealed net Wealth/Value of gift involved in (i) above. . .	3,86,50	12
(*iii*) Total amount of penalty levied in (i) above	2,56,90	12
(*b*) Position of prosecution cases under the provisions of Wealth/Gift tax Act		
(*i*) No. of prosections pending before the courts on 1-4-1978	105	—
(*ii*) No. of prosections complaints filed during 1978-79, under Section 35A, 35B, 35C, 35D and 35F	—	—
(*iii*) No. of prosectitions decided during 1978-79	—	—
(*iv*) No.fo convictions obtained in (iii) avove .	—	—
(*v*) No. of cases which were compounded before launching prosecutions . .	—	—
(*vi*) Composition money levied in such cases [(v) above]	—	—

(III) Penalities which could not be imposed due to time bar under Section 275 of the Act.

Year	No. of cases	Amount Rs.
1976-77	Nil	Nil
1977-78	1	157
1978-79	Nil	Nil

14. *Results of functioning of the Valuation Cells*

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

(1) No. of Valuation Units/Districts :

Year	No. of valuation Units	No. of valuation Districts functioning
1976-77	80	10
1977-78	80	10
1978-79	80	10

(2) No. of Cases referred to the Valutation Cells excluding cases brought forward from previous year :—

	Income-tax	Wealth-tax	Gift-tax	Estate duty
1976-77 and earlier years .	**4,143	41,239@	316@	1,327@
1977-78	1,571	16,755	137	585
1978-79	1,525	19,193	162	296

(3) Total amount of Valuation declared by the assessees :

(In lakhs of Rs.)

	Income-tax	Wealth-tax	Gift-tax	Estate Duty
1976-77 and earlier years .	9422.35	58667.02	294.38	2396.68
1977-78	4310.01	21762.01	140.56	745.06
1978-79	2997.06	38924.70	683.69	356.04

*Information given by the Min. of Finance.

**These figures are commulative for the years 1974-75 to 1976-77.

@These figures are cummulative for the years 1972-73 to 1976-77.

NOTE:—The figures shown against 1977-78 and 1978-79 rela'e to the particular year only (i.e. no. brought forward from previous year).

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

(In lakhs of rupees)

Year	Income-tax			Wealth-tax			Gift-tax			Estate Duty		
	No. of Cases	Value returned	Value determined	No. of cases	Value returned	Value determined	No. of cases	Value returned	Value determined	No. of cases	Value returned	Value determined
1976-77	3875*	7251.47*	9536.06*	33,345	53,090.63	108,089.85	245	290.98	604.52	1113	2576.40	5949.09
earlier year				@	@	@	@	@	@	@	@	@
1977-78	1516	3648.52	4605.94	15340	22,481.36	47,902.78	129	114.87	259.36	635	752.85	1616.59
1978-79	1620	2997.06	4825.49	26152	38,924.70	1,09,733.96	252	683.69	1056.05	321	356.04	821.77

*These figures are cummulative for the years 1974-75 to 1976-77.

@These figures are cummulative for the years 1972-73 to 1976-77.

NOTE:—The figures shown against 1977-78 & 1978-79 relate to particular year only. (no brought forward from previous year)

15. *Results of test audit in general*

(i) *Corporation tax and Income-tax*

During the period from 1st April, 1978 to 31st March, 1979, test audit of the documents of the income-tax offices revealed total under-assessment of tax of Rs. 2190.14 lakhs in 28,304 cases. Besides these, various defects in following the prescribed procedures also came to the notice of Audit.

Of the total 28,304 cases of under-assessment, short levy of tax of Rs. 1810.34 lakhs was noticed in 1,901 cases alone. The remaining 26,403 cases accounted for under-assessment of tax of Rs. 379.80 lakhs.

The under-assessment of tax of Rs. 2190.14 lakhs is due to mistakes categorised broadly under the following heads :—

(1)	No. of items (2)	Amount (In lakhs of rupees) (3)
1. Avoidable mistakes in computation of tax .	2,779	64.67
2. Failure to observe the provisions of the Finance Acts	511	23.13
3. Incorrect status adopted in assessments . .	365	29.71
4. Incorrect computation of salary income . .	801	40.53
5. Incorrect computation of income from house property	1213	33.54
6. Incorrect computation of dividend income. .	56	2.45
7. Incorrect computation of business income . .	3530	193.67
8. Irregularities in allowing depreciation and development rebate	1529	148.70
9. Irregularities in connection with export incentives	11	0.21
10. Irregular exemptions and excess reliefs given .	2172	453.57
11. Irregular computation of capital gains . . .	329	120.28
12. Mistakes in assessment of firms and partners .	692	117.29
13. Omission to include income of spouse/minor child etc.	228	18.35

14. Income escaping assessment	1963	195.05
15. Irregular set off of losses	133	25.82
16. Under-assessment due to adoption of incorrect procedure	..	..
17. Mistakes in assessments while giving effect to appellate orders	92	11.47
18. Excess or irregular refunds	1207	21.96
19. Non-levy/incorrectlevy of interest for delay in submission of returns, delay in payment of tax etx.	3073	172.96
20. Avoidable or incorrect payment of interest by Government	62	24.15
21. Omission/short levy of penalty	81	33.51
22. Other topics of interest/miscellaneous	7386	398.95
23. Under-assessment of Surtax/Super Tax	91	60.17
TOTAL	28,304	2190.14

(ii) *Wealth-tax*

During test audit of assessments made under the Wealth-tax Act, 1957, short levy of tax of Rs. 205.58 lakhs was noticed in 4,520 cases.

The under-assessment of tax of Rs. 205.58 lakhs was due to mistakes categorised broadly under the following heads :—

	No. of items	Amount (in lakhs of rupees)
1. Wealth escaping assessment	558	46.48
2. Incorrect valuation of assests	577	22.86
3. Mistakes in computation of net wealth	903	17.89
4. Irregular/Excessive allowances and exemptions	801	18.40
5. Mistakes in calculation of tax	658	15.98
6. Non-levy or incorrect levy of additional wealth-tax	67	17.44
7. Non-levy or incorrect levy of penalty and non-levy of interest	298	16.86
8. Incorrect status adopted in assessments	100	21.41
9. Mistakes in refunds	15	0.10
10. Miscellaneous	543	28.16
TOTAL	4520	205.58

(iii) *Gift-tax*

During the test audit of gift-tax assessments it was noticed that in 1,159 cases there was short levy of tax of Rs. 151.83 lakhs.

(iv) *Estate Duty*

In the test audit of estate duty assessments it was noticed that in 493 cases there was short levy of estate duty of Rs. 29.89 lakhs.

CHAPTER II

CORPORATION TAX

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

Year	Amount (in crores of rupees)
1974-75	709.48
1975-76	861.70
1976-77	984.23
1977-78	1220.77
1978-79	1251.47

The number of companies on the books of the Department for the last five years has been as follows :—

As on 31st March	Number
1975	35,911
1976	40,055
1977	40,237
1978	42,084
1979	41,532

17. As on 31st March, 1979 there were 52,885 companies. These included 358 foreign companies and 1,414 associations not for profit registered as companies limited by guarantee and 62 companies with unlimited liability. The remaining 51,051 companies comprised 782 Government companies and 50,269 non-Government companies with paid-up capitals of Rs. 8,315 crores and Rs. 3,563 crores respectively. Among non-Government companies over 84 per cent were private limited companies*.

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

18. The arrears outstanding under Corporation tax during the last five years, together with the number of assessments pending at the end of each year have been as follows :—

Year	No. of assessments		Amount of demands	
	Completed during the year	Pending at the close of the year	Collected during the year	In arrears at the close of the year
			(In crores of rupees)	
1974-75	36,574	28,438	709.48	179.63
1975-76	40,327	31,613	861.70	192.11
1976-77	41,878	34,008	984.23	146.38
1977-78	41,533	34,864	1220.77	185.96
1978-79	35,982	40,563	1251.47	168.04

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

20. *Avoidable mistakes in computation of tax*

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

In spite of the remedial action taken by the department, the mistakes still continue to occur. As already pointed out in paragraph 15(i) of Chapter I, 2,779 cases of avoidable mistakes involving short levy of tax of Rs. 64.67 lakhs were noticed in test audit during the year 1978-79 under Corporation tax and Income-tax. Some of the important mistakes relating to Corporation tax are given below :—

(i) The income-tax assessment of a company for the assessment year 1974-75 was revised in December 1977 computing the total income at Rs. 2,94,827

which included business loss of Rs. 67,737. The assessment was revised again in March 1978 when the business income was determined at Rs. 1,28,951 as against the loss of Rs. 67,737 and the total income was computed at Rs. 4,91,515. While levying tax, however, the total income was incorrectly taken as Rs. 4,23,778 after deducting business loss of Rs. 67,737. The erroneous deduction of Rs. 67,737 resulted in undercharge of income to that extent with consequent short levy of tax of Rs. 46,236.

The Ministry of Finance have accepted the objection.

(ii) In the assessment of a company for the assessment year 1973-74 completed in August 1976, the department disallowed a sum of Rs. 3,05,149 debited to accounts, being provision for retiring gratuities on the ground that the fund was not approved and simultaneously allowed a sum of Rs. 54,416 being the amount of gratuity actually paid during the year. Subsequently on production of a copy of the order of the Commissioner of Income-tax approving the fund, the department rectified the assessment in December 1976, to allow the provision of Rs. 3,05,149 disallowed earlier but failed to deduct therefrom the sum of Rs. 54,416, allowed already in August 1976. The omission led to excess allowance of gratuity of Rs. 54,416 and under-assessment of income by identical amount with consequent tax undercharge of Rs. 31,425.

The Ministry of Finance have accepted the objection.

21. *Failure to observe the provisions of the Finance Acts*

(i) The scrutiny of assessment of a closely-held company for the assessment year 1977-78 disclosed that the total income

of the company amounting to Rs. 16,94,055 was charged to tax at 55 per cent instead of at 60 per cent provided in the Finance Act, 1977. Further, while computing the total income, the assessing officer allowed a sum of Rs. 43,907 as expenditure on scientific research without adding back a sum of Rs. 58,307 already debited to the profit and loss account on the same account. These mistakes resulted in tax undercharge of Rs. 1,25,669.

The Ministry of Finance have accepted the objection.

(ii) According to the provisions of the Finance Act, 1975, the rate of tax applicable to an industrial company in which public are not substantially interested is 55 per cent on so much of its total income as does not exceed rupees two lakhs and 60 per cent on the balance, if any.

In the assessment of a company for the assessment year 1975-76 completed in November 1978, the department levied a tax of Rs. 7,86,782 applying the flat rate of 55 per cent on the total income determined at Rs. 13,62,392 although the assessee was an industrial company in which the public were not substantially interested. As the correct amount of tax leviable in terms of the provisions of the Finance Act, 1975, was Rs. 8,47,807, the application of incorrect rate led to an under-charge of tax of Rs. 61,025.

The Ministry of Finance have accepted the objection.

22. *Incorrect computation of income from house property*

The Income-tax Act, 1961 specifically provides for the deductions allowable in the computation of income from house property. Any payment to the previous lease-holders to vacate their right to hold the property on lease is not, however, so specified and is not deductible in computing income from house property of an assessee.

A private limited company on its formation acquired a house property from the persons who formed the company. The company paid during each of the previous years relevant to the assessment years from 1973-74 to 1975-76 a sum of Rs. 72,000 to the previous lease holders for vacating their right to hold the property on lease and the payments so made were allowed as deductions in the computation of property income. The incorrect allowance led to undercharge of tax of Rs. 1,14,223 in the assessment years 1973-74 to 1975-76.

The paragraph was sent to the Ministry of Finance in October 1979; they have stated in January 1980 that the objection is under consideration.

23. *Incorrect computation of business income*

(i) Under the provisions of the Income-tax Act, 1961, any expenditure laid out or expended wholly and exclusively for the purposes of business or profession is an allowable deduction in the computation of business income provided the expenditure is not in the nature of capital expenditure. The assessment for each year is made for a self-contained accounting period and in computing the income derived by an assessee during that accounting period, only the expenditure incurred or a liability provided for in respect of that year is an allowable deduction.

(a) In the case of a foreign company, the consolidated statements of earnings appearing in its Annual Reports for the previous years relevant to the assessment years 1972-73 to 1974-75 disclosed provision for investment in affiliated and subsidiary companies and capital tax on preference shares. In computing the business loss of the company for the assessment years 1972-73 to 1974-75 on the basis of its world income, the above provisions and the tax which were not incurred for the purpose of business were incorrectly allowed in the assessments. The incorrect allowance led to excess computation

and excess carry forward of business loss to the extent of Rs. 3,16,976 in respect of the three assessment years.

The Ministry of Finance have accepted the objection.

(b) In the case of a company, expenditure of Rs. 1,15,576 incurred in the assessment year 1976-77 for payment of commission to the Central Bank of India for standing guarantee on behalf of the company for the purchase of certain assets on deferred payment basis, was allowed as revenue expenditure instead of treating the same as capital expenditure. This resulted in under-assessment of income of Rs. 1,15,576 and short levy of tax of Rs. 66,745.

The Ministry of Finance have accepted the objection.

(ii) Further, if no specific liability has arisen during the year and the liability is only a contingent one, no deduction is permissible for such liability even under the mercantile system. Where an employer sets apart sums for leave salary payable to employees for leave unavailed, the liability for actual payment arises only when the employees take leave or are discharged or after being refused leave, quit the employment. It was judicially held in 1966 and again in 1970 that as the liability arises only on the happening of any of the said contingencies, the liability for leave salary is only a contingent one and not an ascertained or accrued liability.

(a) In the assessments of a company for the assessment years 1968-69 to 1971-72, the assessments of which were completed in December 1972 and March 1973, provision made by the assessee for payment of holiday wages amounting to Rs. 1,18,47,373 was allowed as deduction. The actual expenditure during the four years on account of holiday wages amounted

to Rs. 1,11,26,244 only. It was pointed out in audit in October 1974 that deduction was admissible only for a sum of Rs. 1,11,26,244 and the incorrect deduction allowed for Rs. 1,18,47,373 led to under-assessment of income of Rs. 7,21,129 involving a tax undercharge of Rs. 3,96,620.

The Ministry of Finance have stated that the Income-tax Officer cannot be held to have acted wrongly in allowing the provision made in the accounts as a deduction. For this they have relied upon a decision of the Supreme Court which has actually no application to the present case. In fact, the Board had itself issued instructions agreeing to the Audit view long after the said judgment.

(b) A company created a trust for providing certain benefits to its employees such as education of their children, payment of pension etc. and transferred to it a sum of Rs. 4,20,000 for the purpose. The department allowed the assessee's claim treating it as business expenditure in the assessment year 1976-77. As the assessee-company had merely provided for future possible expenditure in its accounts, the deduction was irregular during the relevant previous year. This resulted in under-assessment of income of Rs. 4,20,000 and consequent short levy of tax of Rs. 2,42,550 for the assessment year 1976-77.

The Ministry of Finance have accepted the objection.

(iii) It has been judicially held that expenditure incurred in connection with proceedings regarding breach of law would not be an admissible deduction, even if incurred for the purposes of the business.

The accounts of an assessee-company for the previous year relevant to the assessment year 1976-77 included a debit of Rs. 1,17,014 on account of "Sales tax and penalty", which was

allowed in full by the department while computing the income of the company for the assessment year 1976-77. It was, however, seen that the above sum included an amount of Rs. 1,08,767 being penalty in the form of interest for delayed payment of sales tax which was not allowable. The irregular deduction resulted in under-assessment of income by Rs. 1,08,767 with tax undercharge of Rs. 68,523.

The Ministry of Finance have accepted the objection.

(iv) Under the provisions of the Income-tax Act, 1961, the total income of any previous year of a person who is resident includes all income, from whatever source derived, which accrues or arises or is deemed to accrue or arise to him in India during such year. An assessee who is following the mercantile system of accounting should accordingly take credit in his accounts for income actually received as well as income accruing or deemed to accrue to him.

An assessee-company advanced huge sums of money to certain companies. Interest amounts of Rs. 8.87 lakhs and Rs. 17.51 lakhs accruing on the advances during the previous years relevant to the assessment years 1973-74 and 1974-75 were, however, exhibited by the assessee in his balance sheet under "interest suspense account" instead of being credited to the profit and loss accounts of the respective years. As a result, there was an under-statement of income of Rs. 26.38 lakhs and consequent short levy of tax of Rs. 15,23,445.

The Ministry of Finance have accepted the objection.

(v) Under the provisions of the Income-tax Act, 1961, deduction is not normally admissible to an assessee in computation of business income in respect of any provision made for payment of gratuity to his employees. However, in respect of assessment years 1973-74 to 1975-76 provision for gratuity made in the relevant previous years could be allowed, if the assessee satisfied certain conditions prescribed in the Act. One of the

conditions is that the provision for gratuity should have been made on the basis of an actuarial valuation of the ascertainable liability.

In its accounts for the year ended 31st December, 1973, a public company made a provision of Rs. 15,00,066 towards gratuity liability to its employees for past years. In the assessment order for the assessment year 1974-75 (passed in July 1976) the provision was allowed by the department as a deduction from business income.

During local audit conducted in January 1978, it was noticed that the quantum of gratuity liability was determined only by the auditors of the company and that there was no evidence on record to show that the liability was based on actuarial valuation. It was pointed out to the department that, since the statutory requirement regarding determination of the liability on an actuarial basis had not been satisfied, the deduction was inadmissible and the allowance of the same resulted in underassessment of business income by Rs. 15,00,066 involving a short levy of tax of Rs. 8,66,290.

The Ministry of Finance have accepted the objection.

(vi) The Income-tax Act, 1961, further provides that any contribution made towards an approved gratuity fund created by an assessee for the exclusive benefit of his employees under an irrevocable trust is allowable as a deduction in computing his income from business to the extent the amount of such provision does not exceed an amount calculated at the rate of eight and one-third per cent of the salary of each employee entitled to the payment of such gratuity for each year of his service.

In the case of an assessee-company, the total gratuity provision amounting to Rs. 3,62,171 made in the assessment years 1974-75 and 1975-76 was allowed in full in those years as a deduction instead of limiting the same to the aforesaid prescribed limit of eight and one-third per cent of the salary of each employee for

the two years. The gratuity provision allowed in excess resulted in under-assessment of income of Rs. 68,637 and an aggregate short levy of tax of Rs. 43,241.

The Ministry of Finance have accepted the objection.

(vii) Under the provisions of the Payment of Bonus Act, 1965, a minimum bonus is to be paid at the rate of 4 per cent of wages and salaries subject to fulfilment of other conditions. Schedules to the Act prescribe the manner in which the available surplus of an establishment is to be determined for the purpose of computation of bonus. The available surplus does not include *ex-gratia* payments.

An assessee-company had made a provision of Rs. 4.50 lakhs towards bonus in its accounts for the financial year 1973-74 which was the previous year relevant to the assessment year 1974-75. However, while finalising the assessment for the assessment year 1974-75, the assessing officer allowed a further deduction of Rs. 2.50 lakhs (in addition to Rs. 4.50 lakhs) on assessee's representation that the actual liability would be more due to agreement with the employees for payment of bonus at higher rates. The actual payment of bonus for the financial year 1973-74 was made during the financial year 1974-75 and as no provision had been made for additional bonus in its accounts, the amount of Rs. 1,94,808 paid on this account was included in the profit and loss account of the later year against "Salaries, Wages and Bonus". As the claim for deduction of additional liability for bonus was admitted in the assessment year 1974-75 itself, the actual payment made in the subsequent year was required to be disallowed in the assessment year 1975-76. Omission to do so resulted in under-assessment of income of Rs. 1,94,808 for the assessment year 1975-76 with consequent undercharge of tax of Rs. 1,12,499. Further, since the actual payment against the additional allowance of Rs. 2.50 lakhs amounted to Rs. 1,94,808 only, excessive allowance of Rs. 55,192 should have also been withdrawn from the assessment year 1974-75. Failure to do so resulted in under-assessment of

income by Rs. 55,192 and short levy of tax of Rs. 31,873 for the assessment year 1974-75.

The total undercharge of tax for the two assessment years, 1974-75 and 1975-76, was Rs. 1,44,372.

The Ministry of Finance have accepted the objection.

(viii) Under the provisions of the Income-tax Act, 1961, the maximum deduction allowable in each year on account of payment to a director, or to a person who has a substantial interest in the company, is an amount calculated at the rate of Rs. 6,000 for each month or part thereof comprised in that period. Further, expenditure which results directly or indirectly in the provision to an employee of any benefit or amenity or perquisite, whether or not convertible into money, should not be allowed as deduction from the business income of the employer to the extent such expenditure or allowance exceeds one-fifth of salary or an amount calculated at the rate of one thousand rupees for each month or part thereof comprised in the period of employment of the employee during the previous year, whichever is less.

(a) During the previous years relevant to the assessment years 1976-77 and 1977-78 a company incurred a total expenditure of Rs. 2,55,333 by way of providing perquisites to its Manager and Chief Accountant. The department while computing the business income for the respective assessment years allowed the expenditure in full without restricting it to the admissible limit of Rs. 33,600 calculated at one-fifth of salary or at the rate of Rs. 1,000 per month comprised in the period of employment. The mistake resulted in under-assessment of income by Rs. 2,21,733 with consequent tax undercharge of Rs. 92,911 for the assessment years 1976-77 to 1978-79, a portion of loss computed for the assessment years 1976-77 and 1977-78 having been set off in the assessment year 1978-79.

While accepting the objection the Ministry of Finance have stated that the assessments in question have been revised and an additional demand of Rs. 92,911 raised.

(b) During the previous years relevant to the assessment years 1972-73, 1973-74, 1975-76 and 1976-77, a company paid a total remuneration of Rs. 3,98,342 to two foreign technicians employed as Technical Directors of the company. While computing the business income of the company for the respective assessment years, the department, however, did not restrict the deduction in respect of such payment to the maximum limit of Rs. 2,64,000 for the four years. The mistake resulted in excess allowance of deduction of Rs. 1,34,342 with consequent total tax undercharge of Rs. 77,599 in the assessment years 1974-75 to 1976-77, the total income for the assessment years 1972-73 and 1973-74 being losses.

The paragraph was sent to the Ministry of Finance in August 1979; they have stated in December 1979 that the objection is under consideration.

(c) During the previous years relevant to the assessment years 1973-74 and 1974-75 an assessee tea company paid secretarial remuneration of £ 21,378 and £ 23,463 equivalent to Rs. 4,05,461 and Rs. 4,45,098 respectively to a firm in which two directors of the assessee-company were also partners. The two directors were also beneficially interested in the company. The payment of secretarial remuneration to such a firm, therefore, resulted in the provision of indirect benefit to the two directors of the assessee-company by virtue of their being the partners of the recipient firm. Accordingly, in the computation of business income of the assessee-company for the respective assessment years, the deduction on account of such expenditure should have been restricted to the allowable limit of Rs. 1,44,000 for two directors. This having not been done, there was under-assessment of net taxable income by an aggregate sum of Rs. 2,25,023 being 40 per cent of gross under-assessment of income of Rs. 5,62,559 with resultant tax undercharge of Rs. 1,93,833 including interest for delay in submission of return and short payment of advance tax on estimate in the assessment years 1973-74 and 1974-75.

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

(ix) Under the Income-tax Act, 1961, where an assessee has been allowed a deduction in his assessment on account of any trading liability and subsequently he obtains some benefit in respect of such trading liability either by way of remission or cessation thereof, the value of benefit accruing to him is chargeable to tax in the year in which the liability is liquidated.

In the case of a company, provision for gratuity amounting to Rs. 21,94,410 debited in the accounts for the year relevant to the assessment year 1974-75 was allowed as a deduction. In the next year relevant to the assessment year 1975-76 the assessment of which was completed in October 1978, the sum of Rs. 21,94,410, which represented the total amount of provision so far made, was written back by credit to profit and loss appropriation account. The Director's Report revealed that the assessee had decided not to maintain any gratuity fund but to make payment in future on cash basis. The assessing officer, however, did not add back the amount of Rs. 21,94,410 already allowed. The omission to do so resulted in under-assessment of income by an identical amount with consequent tax undercharge of Rs. 12,67,271 for the assessment year 1975-76.

Besides, the allowance of gratuity provision of Rs. 21,94,410 in the assessment year 1974-75 itself was not in order inasmuch as the assessee failed to fulfil the requisite condition to deposit the entire amount of provision to the gratuity fund within 31st March, 1977. The assessee's letter of July 1977 revealed that it had paid to the gratuity fund within the stipulated date a sum of Rs. 10,68,090 only instead of the entire amount of the provision.

The paragraph was sent to the Ministry of Finance in September 1979; they have stated in January 1980 that the objection is under consideration.

(x) It has been judicially held that collections made by an assessee towards sales tax constitute trading receipt and are to be included in business income.

In the previous years relevant to the assessment years 1974-75 and 1975-76, a public limited company collected Rs. 1,89,543 towards additional sales tax and Rs. 1,64,665 towards surcharge on sales tax from its customers. According to the Sales Tax Law of the State, additional sales tax should be borne by the dealer himself. Realising that the collection from the customers was illegal, the assessee retained the amount of Rs. 1,89,543 (without paying it to the State Government) for eventual refund to the customers. The sum of Rs. 1,64,665 collected towards surcharge on sales tax was first remitted by the assessee to the State Government which subsequently refunded the amount to the assessee as the company was found not liable to pay the surcharge. The assessee credited both the amounts in its books in a separate account and did not offer them as business income, on the ground that the amounts were eventually to be refunded to the customers. This claim was accepted by the department in the assessment for the assessment years 1974-75 and 1975-76 (revised in January 1977 and July 1977).

The amounts constituted trading receipts of the assessee and should have been included in the total income of the relevant years and the incorrect exclusion resulted in under-assessment of income by Rs. 3,54,208 involving short levy of income-tax of Rs. 2,04,555.

The Ministry of Finance have accepted the objection.

(xi) Under the provisions of the Income-tax Act, 1961, the profits or gains arising from the transfer of a capital asset shall be deemed to be the income of the previous year in which the transfer took place.

In the case of a company, capital gain of Rs. 2,58,138 from the sale of immovable property was set off against the capital loss of Rs. 2,93,000 from the sale of 80,000 shares in another

company. The printed accounts of the company for the year ended 29-2-1976, however, disclosed that out of 80,000 shares shown as sold, the transfer of 50,000 shares was effected only after the end of the accounting year ended 29-2-1976. The loss on account of the sale of 50,000 shares was, therefore, not allowable in the assessment year 1976-77. The incorrect allowance of loss resulted in under-assessment of income of Rs. 1,65,140 with tax undercharge of Rs. 74,300 (Approx.).

The Ministry of Finance have accepted the objection.

(xii) An assessee paid Rs. 75,00,000 for the purchase, in March 1971, of 30 acres of forest land (Rs. 19,87,500) and the trees (valued at Rs. 55,12,500) standing thereon. The assessee also paid total registration fee of Rs. 7,50,000 on the purchase deed. In May 1971, the forest land was acquired by Government without payment of any compensation. The loss suffered by the assessee on the acquisition of land itself (excluding the trees) was treated as short-term capital loss and adjusted against his other income. However, while calculating the quantum of loss, the total registration fee of Rs. 7,50,000 was added to the cost of land (Rs. 19,87,500) though the proportionate fee of Rs. 1,98,750 only as related to the cost of the land was allocable. The amount of short-term capital loss, therefore, was inflated by Rs. 5,51,320. As this loss was adjusted against other income of the assessee, the total income was under-assessed by Rs. 5,51,320 resulting in short levy of tax to the extent of Rs. 3,10,510.

The paragraph was sent to the Ministry of Finance in October 1979; they have stated in January 1980 that the objection is under consideration.

Incorrect allowance of depreciation, development rebate and investment allowance.

24. *Depreciation*

(i) The Income-tax Act, 1961 provides for grant of depreciation on buildings, plant and machinery owned by the

assessee and used for the purpose of business in computing the income from business if the prescribed particulars have been furnished by the assessee in respect of such buildings, plant and machinry. The Rules prescribed in this regard, provide for specified rates of depreciation for certain items of plants and machinery and a general rate of 10 per cent for the remaining items of plant and machinery, on the actual cost or the written down value of the assets, as the case may be. The Rules also provide for the allowance of additional depreciation for extra shift working of plant and machinery based on the number of days they have worked double or triple shift.

(a) In the case of a non-resident shipping company depreciation on trailors and cargo containers was allowed at the rate of 30 per cent of the written down value against 5 per cent of the actual cost as admissible under the Rules. In the absence of the details of the actual cost of the assets in the assessment records depreciation allowance at 5 per cent of the written down value of the assets worked out at Rs. 3,05,892 and on that basis the excess allowance of depreciation in the assessment for 1971-72 amounted to Rs. 15,29,460.

Further, in the assessment for the assessment year 1972-73, the assessee claimed depreciation allowance of Rs. 10,25,868 in respect of certain assets for which the assessee did not furnish any details. The department also did not maintain any depreciation chart. In the absence of details no depreciation was allowable on these assets. However, on the basis of the written down value of the assets as furnished in the assessment for the assessment year 1971-72, depreciation of Rs. 3,29,924 was allowable in the assessment year 1972-73. As the department allowed depreciation of Rs. 10,25,868, depreciation of Rs. 6,95,944 was allowed in excess in the assessment for the assessment year 1972-73.

The total undercharge of tax on account of the two mistakes in the assessment years 1971-72 and 1972-73 amounted to Rs. 4,23,228.

The paragraph was sent to the Ministry of Finance in October 1979; they have stated in January 1980 that the objection is under consideration.

(b) In the case of another assessee-company, while computing the income for the assessment year 1970-71, depreciation on 'Pay Loader' was allowed at 30 per cent against the general rate of 10 per cent applicable in this case. The application of incorrect rate of depreciation resulted in under-assessment of income by Rs. 4,49,854 with tax effect of Rs. 2,47,420.

In the case of the same assessee-company, while computing the income, deduction by way of development rebate on barges was allowed at the rate of 40 per cent in the assessment year 1970-71 against the admissible rate of 20 per cent. Incorrect application of the rates resulted in under-assessment of income of Rs. 2,62,211 leading to short levy of tax of Rs. 1,44,215.

There was thus total tax undercharge of Rs. 3,91,635 for the assessment year 1970-71.

The paragraph was sent to the Ministry of Finance in August 1979; they have stated in December 1979 that the objection regarding depreciation allowance is under consideration; their final reply in respect of the objection regarding development rebate is awaited (February 1980).

(c) The Act further provides that the term "actual cost" for this purpose means 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.

In the case of an assessee-company a part of the cost of construction of the Industrial Township for housing its employees was met by subsidies received from a State Government, amounting to Rs. 29,50,575 in the previous years relevant to the assessment years 1968-69 and 1969-70. In computing

depreciation on the housing estates the sum of Rs. 29,50,575 (not incurred by the company) was required to be deducted from the cost of the assets to the assessee. Omission to do so resulted in excess allowance of depreciation of Rs. 10,26,087 in the assessment years 1968-69 to 1974-75 on the inflated actual cost of the assets and corresponding excess carry forward of business loss of Rs. 10,26,087.

The Ministry of Finance have accepted the objection.

(ii) The Income-tax Act, 1961 allows depreciation on depreciable assets only.

An assessee-company incurred an expenditure of Rs. 2,73,87,687 on account of fees for Project Report, Working Drawings and expenses on foreign exports upto the year ended 31-3-1967. The amount was shown in the accounts as a separate item in the schedule of fixed assets. In the accounts for the year ended 31-3-1968 relevant to the assessment year 1968-69 an amount of Rs. 1,33,57,907 out of the said expenses of Rs. 2,73,87,687 was capitalised as a distinct item in the schedule of fixed assets (not allocable to tangible assets) and an amount of Rs. 28,13,081 was allocated to different depreciable fixed assets; the balance being transferred to Deferred Revenue Expenditure. The expenditure of Rs. 1,33,57,907 treated as capital expenditure but not allocable as such to any depreciable item of fixed assets, was not entitled to any depreciation. In computing the business income of the company the department, however, allowed depreciation of Rs. 27,70,782 in the assessment years 1968-69 and 1969-70. The incorrect allowance of depreciation led to excess computation and carry forward of loss to the extent of Rs. 26,70,782 in those two assessment years.

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

(iii) Under the provisions of the Income-tax Act, 1961, the entire capital expenditure incurred on scientific research, during the relevant previous year is to be deducted in computing

the taxable income for the assessment year. Hence, the assessee will not be entitled to depreciation allowance in respect of the capital outlay on scientific research. While assessing the income of the assessee-company for the assessment year 1973-74 depreciation of Rs. 1,04,839 was allowed on capital expenditure incurred for scientific research during the relevant previous year though the entire capital expenditure of Rs. 13,48,098 was separately allowed as deduction. This resulted in under-assessment of income of Rs. 1,04,839 with consequent under-charge of tax of Rs. 66,050.

The Ministry of Finance have accepted the objection.

(iv) The Income-tax Act, 1961, as applicable from the assessment year 1975-76 provides for the grant of initial depreciation at twenty per cent of the cost of the new machinery or plant installed and used for the purposes of business in addition to the normal depreciation admissible at varying rates prescribed in the rules, or at 100 per cent when the actual cost of any machinery or plant does not exceed seven hundred and fifty rupees. However, the aggregate of all the deductions in respect of depreciation made should not, under the Act, exceed the actual cost of the assets in respect of which the depreciation is claimed.

In the case of a company normal depreciation allowance was allowed at the rate of 100 per cent on miscellaneous equipment and electrical installations costing Rs. 750 and less. Besides, initial depreciation at the rate of 20 per cent of the cost of equipment was also allowed. Thus the aggregate depreciation allowance granted exceeded the cost of the equipment by 20 per cent. This resulted in under-assessment of income of Rs. 93,709 with consequent short levy of tax of Rs. 54,118 in the assessment year 1976-77.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been revised raising an additional demand of Rs. 54,118.

(v) Further, the Income-tax Rules, 1962 also provide for additional depreciation for extra shift working of the plant and machinery depending upon the number of days of double and triple shifts. The Central Board of Direct Taxes in their circulars of September 1966 and December 1967 issued necessary instructions in the matter in consultation with Audit.

However, in September 1970, the Central Board of Direct Taxes issued revised instructions that the extra shift allowance could be granted with reference to the number of days the concern worked without making any attempt for determining the number of days for which each machine worked, double or triple shift. These instructions of the Board are not in accordance with the provisions of the Income-tax Act.

Since the Act provides for allowance for normal depreciation in respect of each item of machinery and plant, the Rules framed thereunder should also apply to such machinery and plant. However, extra shift allowance has been allowed even in respect of machinery which has not worked at all during the previous year or in excess of actual number of days it has worked. Such irregularities were pointed out in the past also. Mention in this respect is made to paragraph 26(i) of the Audit Report 1975-76 and 23(v) of the Audit Report 1977-78.

Some of the important irregularities of the type noticed during the course of audit are given below :—

(a) In the assessments of an assessee-company for the assessment years 1972-73 to 1974-75, extra shift depreciation on certain items of machinery for triple shift working was allowed as claimed by the assessee at 150 per cent of the normal depreciation which exceeded the prescribed ceiling limit of 100 per cent of the normal depreciation. The mistake resulted in excess extra shift allowance of Rs. 5,58,425 in the aforesaid three years with consequent tax undercharge of Rs. 3,36,377 in the assessment years 1972-73, 1973-74 and 1975-76, there being loss in the assessment year 1974-75. There

was also consequent short levy of interest of Rs. 7,933 for delay in the submission of returns.

The paragraph was sent to the Ministry of Finance in September 1979; they have stated in December 1979 that the objection is under consideration.

(b) In the case of another assessee-company, deduction on account of triple shift allowance equal to normal depreciation allowance amounting to Rs. 1,77,550 was allowed though the company worked triple shift only for 23 days in the previous year relevant to the assessment year 1974-75. The deduction admissible on this account was for Rs. 17,015 only. Incorrect calculation of triple shift allowance resulted in excess deduction on account of depreciation amounting to Rs. 1,60,535 with notional tax undercharge of Rs. 92,708.

The Ministry of Finance have accepted the objection.

(c) Further, in determining the written down value, both normal depreciation and extra shift allowance, allowed if any, are required to be taken into consideration and not normal depreciation alone.

In the assessment of a company for the assessment years 1975-76 to 1977-78 although extra shift allowance was allowed on plants and machinery, the same was not taken into consideration while determining the written down value of the same. This resulted in incorrect determination of written down value leading to excess allowance of depreciation to the extent of Rs. 1,66,671 for the three assessment years. As the assessments resulted in losses, there was excess carry forward of loss by that amount.

The Ministry of Finance have accepted the objection.

25. *Development rebate*

(i) Under the Income-tax Act, 1961, development rebate on plant and machinery installed after 31st March, 1970 for the purpose of construction, manufacture or production of any

one or more of the articles or things specified in the Fifth Schedule to the Act is allowable at twenty-five per cent of the actual cost of the plant and machinery installed. Plant and machinery installed for the purpose of manufacture of telephone and communication cables which is not specified as such in the Fifth Schedule is, however, entitled to development rebate at fifteen per cent of the actual cost of the plant and machinery installed.

In the case of an assessee-company manufacturing telephone and communication cables, development rebate on the plant and machinery installed by it in the previous years relevant to the assessment years 1971-72 to 1975-76 was allowed at twenty-five per cent instead of fifteen per cent. This resulted in excess allowance of development rebate of Rs. 74,54,072 with under-charge of tax of Rs. 42,98,510 in these five assessments.

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

(ii) Although development rebate was abolished from 1st June, 1974, the Finance Act, 1974, by a special provision has continued the same in certain cases on the condition that the machineries should have been purchased or the contracts for the purchase should have been entered into before 1st December, 1973.

In the assessment of an assessee-company, engaged in the manufacture of calcium carbonate, for the assessment year 1976-77 completed in December 1977 and revised in September 1978, development rebate of Rs. 14,14,142 at the rate of 25 per cent on plants and machineries valued at Rs. 56,57,368 was allowed subject to creation of reserve. The entire amount was carried forward as the assessment resulted in a loss. Since the item "Calcium Carbonate" in the manufacture of which the assessee was engaged, is not covered by the articles specified in the Fifth Schedule, development rebate at the ordinary rate of 15 per cent only was admissible inasmuch as the orders for

procurement of machineries were placed before the prescribed date. The incorrect application of rate resulted in excess allowance of development rebate of Rs. 5,65,737 for the assessment year 1976-77 with consequent excess carry forward of unabsorbed development rebate of identical amount.

The Ministry of Finance have accepted the objection.

(iii) The Act also provides that if any machinery or plant on which development rebate was allowed in any earlier assessment is sold before the expiry of eight years from the end of the previous year in which it was installed, the development rebate so allowed should be deemed to have been wrongly allowed and the total income should be recomputed withdrawing the development rebate originally allowed. The rectification has to be done before the expiry of four years from the end of the previous year in which the sale took place.

In the case of two assessee-companies, development rebate of Rs. 3,90,497 was allowed in respect of certain plant and machinery in the previous year relevant to the assessment year 1968-69 in which they were installed and brought to use. The assessment records disclosed that the entire plant and machinery was either sold or otherwise transferred in the previous year relevant to the assessment year 1974-75. As the sale and transfer took place before the expiry of eight years from the end of the previous year in which the machinery was installed, the development rebate allowed earlier was required to be withdrawn. The omission to do so led to undercharge of tax of Rs. 2,11,178.

The Ministry of Finance have accepted the objection in both the cases.

26. *Investment allowance*

Under the provisions of the Income-tax Act, 1961 as applicable from 1st April, 1976, 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 after the 31st day of March, 1976, for the purpose of business of construction, manufacture or production of any one or more of the articles or things specified in the Ninth Schedule to the Act.

In the assessment of a company engaged in the manufacture of gear boxes, gear couplings, clutches, speed regulatory pulleys and general motors etc. for the assessment year 1977-78, completed in August 1977, a deduction by way of investment allowance was allowed for a total sum of Rs. 6,84,677 calculated at the prescribed rate on the cost of new plant and machinery brought into use in the two business units of the company during the relevant previous year. Since, however, the articles and things manufactured by the company were not covered by any of the items specified in the Act, no investment allowance was admissible to the company. The incorrect allowance led to under-assessment of business income by Rs. 6,84,677 with consequent tax undercharge of Rs. 3,95,400 for the assessment year 1977-78.

The Ministry of Finance have accepted the objection.

27. *Incorrect grant of export incentives*

Under the Income-tax Act, 1961 as applicable with effect from the assessment year 1969-70, a domestic company or a non-corporate tax payer resident in India incurring expenditure after 29th February, 1968 wholly and exclusively on any of the items specified in the Act in connection with the development of export markets is entitled to a weighted deduction from the taxable income at the rate of one and one-third times (one and one-half times in respect of expenditure incurred after 28th February, 1973 in certain cases) the amount of such expenditure incurred by him during the previous year provided that the said expenditure was not incurred on items like carriage, freight and insurance of the goods, whether in India or outside.

(i) In the assessment of an assessee-company for the assessment year 1975-76, weighted deduction of Rs. 2,06,197 equal to one-third of the total expenditure of Rs. 6,18,591 incurred by

the assessee towards the development of export market was allowed by the department. The said total expenditure of Rs. 6,18,591 included expenditure of Rs. 5,50,463 representing port charges paid to Calcutta Port Trust. As the expenditure of Rs. 5,50,463 was incurred in India, weighted deduction to the extent of Rs. 1,83,488 being one-third of Rs. 5,50,463 was not allowable to the assessee. The omission to disallow the same resulted in tax undercharge of Rs. 1,53,714 including interest on excess payment of advance tax.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been revised raising an additional demand of Rs. 1,53,714.

(ii) In the case of another assessee-company, the aforesaid weighted deduction was erroneously allowed on expenditure incurred on air freight as also on certain activities such as refining and melting carried on outside India, though such expenditure was not eligible for weighted deduction. The erroneous allowance resulted in under-assessment of income of Rs. 93,829 leading to short levy of tax of Rs. 54,186 in the assessment year 1976-77.

The Ministry of Finance have accepted the objection.

Irregular exemptions and excess reliefs given

28. *Irregular allowance of relief in respect of newly established undertakings*

(i) Under the provisions of the Income-tax Act, 1961, where the gross income of an assessee includes any profits and gains derived from a newly established industrial undertaking, the assessee becomes entitled to tax relief in respect of such profits and gains upto six per cent per annum of the capital employed in the industrial undertaking in the assessment year in which the undertaking begins to manufacture or produce articles and also in each of the following four assessment years. Under the Rules prescribed for computing capital employed in the unit, the value of the assets and liabilities as on the first day of the computation

period are to be considered instead of considering the average values thereof on the first and the last days of the computation period. Further, where there is unabsorbed depreciation or loss in the newly established industrial undertaking in an earlier year, the depreciation and the loss have to be carried forward and set off against the profits and gains of the unit in subsequent years before determining if any deduction is allowable towards tax-free profits.

(a) In the assessments of a company for the previous years relevant to the assessment years 1976-77 to 1978-79, the relief in respect of its new industrial undertaking was computed at Rs. 2,17,372, Rs. 2,17,372 and Rs. 4,44,770 respectively on the capital calculated on the average values of the assets and liabilities of the unit. The relief to the extent of Rs. 4,10,449 and Rs. 75,453 for the three assessments was allowed alongwith unabsorbed depreciation and loss of earlier years in the assessment years 1977-78 and 1978-79 respectively. Further, amounts of Rs. 3,45,449 and Rs. 3,69,317 representing unabsorbed depreciation, loss and reliefs were allowed to be carried forward in the assessment years 1977-78 and 1978-79 respectively. On the basis of the capital computable as per rule on the values of the assets and liabilities as on the first day of the relevant computation periods, no relief was allowable for the assessment years 1976-77 and 1977-78 and a sum of Rs. 69,224 was allowable for the assessment year 1978-79. Further, there being unabsorbed depreciation and loss in the new industrial unit, no relief could be allowed in the assessment year 1977-78. As a result of incorrect computation of capital and relief there had been undercharge of tax of Rs. 2,56,344 in the assessment years 1977-78 and 1978-79 in addition to excess carry forward of depreciation, loss and relief of Rs. 3,45,449 and Rs. 3,69,317 respectively.

The paragraph was sent to the Ministry of Finance in September 1979; they have stated in December 1979 that the objection is under consideration.

(b) During the previous year relevant to the assessment year 1971-72 a company started a new industrial undertaking and tax holiday relief amounting to Rs. 2,78,44,420 calculated at six per cent of the capital employed in the undertaking was allowed in the assessment year 1971-72 which was carried forward to subsequent years due to inadequacy of profits. In the computation of capital employed, the value of fixed assets was taken as Rs. 49,95,72,210. In the course of assessment proceedings for the assessment years 1972-73 and 1974-75 the assessing officer found that during the relevant accounting years, the assessee had reduced the value of certain plant and machinery for a total amount of Rs. 45,70,195 on the ground that the amount capitalised in the accounting year relevant to the assessment years 1971-72 was either not payable or was forgone. The assessment for the assessment year 1971-72 was revised in March 1976 withdrawing the depreciation and development rebate allowed on the sum of Rs. 45,70,195. The value of fixed assets included in the capital computation for purposes of tax holiday relief was, however, not reduced by the said sum of Rs. 45,70,195. This led to excess computation of capital by an identical amount with consequent excess allowance and carry forward of relief to the extent of Rs. 2,74,212 for the assessment year 1971-72.

The paragraph was sent to the Ministry of Finance in July 1979; they have stated in December 1979 that the objection is under consideration.

(c) While claiming the relief for the assessment years 1975-76 and 1976-77, an assessee-company took into account the value of assets and liabilities of the new undertaking as on the last day of the accounting period instead of the first day. The department accepted the claim of the company which resulted in excess allowance of deduction of Rs. 1,67,041 for the two years from taxable profits and gains. Since the new undertaking worked at a loss, the assessee-company was allowed to carry forward the deficiency for future adjustment when the undertaking made profits.

The Ministry of Finance have stated in February 1980 that the action of the Income-tax Officer in computing the capital on the last day of the accounting year is in conformity with a decision of the Calcutta High Court striking down Rule 19A. The fact, however, remains that Rule 19A still remains on the Statute book and the Calcutta High Court decision is not binding on this case.

(ii) The Income-tax Rules, 1962 further provide that borrowed money and debt due by an assessee are deductible from the value of assets in the computation of capital for this purpose.

In computing the capital employed in the new industrial undertaking of an assessee-company for the purpose of allowing deduction on account of profits and gains derived from the new undertaking in respect of the assessment years 1974-75 to 1976-77, the department did not deduct from the value of assets, proportionate amount of borrowed moneys employed in the new undertaking and the entire liability incurred on the imported plant and machinery installed in the new unit. The omission resulted in excess computation of capital leading to excess allowance of relief of Rs. 1,56,692 with tax undercharge of Rs. 90,488 in the three assessment years.

The paragraph was sent to the Ministry of Finance in September 1979; they have stated in January 1980 that the objection is under consideration.

29. *Irregular exemptions given*

(i) The Income-tax Act, 1961 provides that financial corporations engaged in providing long-term finance for industrial or agricultural development in India are entitled to a deduction, in the computation of their taxable profits, of the amount transferred by them out of such profits to a special reserve account, upto a specified percentage of their total income as computed before making any deduction under Chapter VI A of the Act. The Board issued instructions in November, 1969 to the effect that this deduction is to be calculated by applying the specified percentage to the total income arrived at after the deduction.

Subsequently, the Board issued a clarification to the Department of Banking in November, 1973 to the effect that the percentage should be applied to the total income computed before making the said deduction. The clarification being contrary to law was not accepted in Audit and the matter was taken up with the Board in December, 1975. In January, 1977 the Board stated that the viewpoint expressed by Audit was acceptable to them. Necessary instructions in this respect were, however, issued only in August, 1979. In the meantime, the assessing officers continued to act upon the Board's clarification of November, 1973. This accounted for a number of costly mistakes.

(a) In the case of a financial corporation it was observed that this deduction was worked out and refund of tax granted by the department for the assessment years 1961-62, 1964-65 to 1966-67 and 1968-69 to 1973-74 at the prescribed percentage of the income of the corporation, before deducting this allowance, on the basis of the Commissioner of Income-tax's order on a revision petition filed by the corporation in December, 1974, resulting in short computation of income by Rs. 6,47,681 for all the assessment years with consequent excess refund of tax of Rs. 3,60,466.

The Ministry of Finance have stated that the very fact that the Board had to issue instructions on this point, three times shows that the matter was not so obvious or clear.

(b) In another case, an assessee-financial corporation filed the income-tax return for the assessment year 1977-78 on 30th July, 1977 returning an income of Rs. 88,32,430. Provisional assessment was completed on the 10th August, 1977 on the basis of the returned income and excess of advance tax amounting to Rs. 1,98,040 was adjusted against the demand outstanding for earlier period. While computing the income, the assessee had deducted 40 per cent of the total income arrived at before allowing deduction under Section 36(1)(viii) of the Income-tax Act, 1961 towards the deduction admissible under the Act in respect of transfer to special reserve whereas the

deduction should have been allowed at 40 per cent of the income arrived at after allowing such deduction. Had this mistake been considered in the provisional assessment, no refund would have become due to the assessee. This resulted in irregular refund of Rs. 1,98,040.

The Ministry of Finance have stated that only obvious items could be disallowed at the time of provisional assessment. In Audit's view, the law is quite clear on the subject.

(c) In still another case, while assessing the income of a State textile corporation declared as an approved financial corporation for the purpose of Section 36(1)(viii) of the Act, deduction was allowed at 25 per cent instead of at the effective rate of 20 per cent of the income arrived at before allowing the said deduction. This resulted in under-assessment of income of Rs. 80,702 and Rs. 77,556 for the assessment years 1974-75 and 1975-76 respectively with consequent undercharge of tax of Rs. 46,606 and Rs. 44,786 for the respective years.

The Ministry of Finance have stated that the assessment in question will require revision.

(ii) With a view to encouraging Indian companies to export their technical 'know-how' and skill abroad and to augment the foreign exchange resources, the Income-tax Act, 1961, provides for certain tax incentives. The incentive, as applicable to the assessment years 1969-70 to 1974-75 consists of deduction of the entire income by way of royalty, commission, fees etc. received by an assessee for having exported technical know-how and skill, while computing taxable income. To become eligible for the concession, the following conditions, among others, have to be fulfilled :

(a) the income derived is in consideration for the use outside India of any patent, invention, model, design, secret formula or process or in consideration of technical services rendered,

(b) an agreement for the purpose entered into by the assessee with a foreign enterprise is approved by the Government/Central Board of Direct Taxes and

(c) the income in convertible foreign exchange is actually brought into India.

An assessee engaged in manufacture of gramophones and records entered into Matrix Exchange agreement with three enterprises in U.K. and the agreements secured the approval of Government in 1964/1965. Under the agreements, the assessee agreed to supply "a matrix or a copy of any local recording" to enable the foreign enterprises to manufacture records therefrom for sale outside India. The agreements were got approved by the Government to obviate any possible delay affecting the export business. During the previous years relevant to the assessment years 1969-70 to 1974-75, the assessee derived income of Rs. 15,24,117 and the Income-tax Officer deducted the entire income from total income. It was pointed out in audit in 1976 that the relief allowed by way of deduction was not in order for the following reasons :

(a) The assessee did not export any technical know-how or skill.

(b) The agreements were not approved by the Government or the Central Board of Direct Taxes specifically for the purpose of availing the relief.

(c) There was no evidence in the assessment records that the assessee brought the income into India in convertible foreign exchange.

The undercharge of tax due to incorrect relief amounted to Rs. 8,65,523.

The paragraph was sent to the Ministry of Finance in October 1979; they have stated in January 1980 that the objection is under consideration.

30. *Irregular computation of capital gains*

Under the Income-tax Act, 1961, the profits and gains arising from the transfer of a capital asset are chargeable to capital gains tax, but capital gains arising on the transfer of assets by a holding company to its subsidiary and *vice versa* are exempt from the levy if the holding company owns all the shares of the subsidiary company. The principle behind the exemption is that, in such cases, though there is an apparent transfer of assets, there is in reality no change of ownership of the assets as the subsidiary itself is fully owned by the holding company.

In paragraph 33 of the Audit Report on Revenue Receipts for the year 1975-76, mention was made of a case wherein a holding company floated a fully-owned subsidiary to avoid payment of capital gains tax on sale of certain properties. Details of a case where an existing subsidiary was used for avoidance of capital gains tax are furnished below.

A closely held company (H), engaged in purchase and sale of motor cars and spare parts, held in January 1975, 64 per cent of the shares in a subsidiary company (S), manufacturing automobile parts. Of the remaining 36 per cent of the shares in the subsidiary company, 30 per cent was held by the directors of company (H) and the remaining 6 per cent by a private company (U) controlled by the same management. In January 1975, the holding company acquired the balance 36 per cent shares [from its directors and company (U)] and became full-owner of the subsidiary S. On 10th April 1975, company (H) sold 8,000 equity shares of another company (A) of the same group to its subsidiary for a total consideration of Rs. 7.20 lakhs, *i.e.* at Rs. 90 per share, and returned for the assessment year 1976-77, capital gains of Rs. 3,12,361 from the transaction. But the capital gains were claimed as exempt from tax on the ground that the transfer made by the assessee-company (H) was only to its own fully-owned subsidiary. The claim was accepted (January 1977) by the department.

It was noticed (December 1977) that the assessee-company (H) sold the subsidiary itself to company (U) on 12th April,

1975 *i.e.* a mere two days after the aforesaid transfer of shares. Thus the sale of 8,000 shares on 10th April, 1975, though ostensibly made to the subsidiary was, in effect, to company (U) and assessee (H) routed the sale through company (S) only to avoid capital gains tax on the transfer.

The subsidiary company itself avoided capital gains tax payable in respect of another transaction with the holding company, the details of which are given below.

On 10th April, 1975, when all its shares were held by the holding company, the subsidiary company sold to company (H) 3,466 unquoted equity shares in another company (C), for a total consideration of Rs. 9.57 lakhs (at Rs. 276 per share). In the assessment of company (S) for the previous year ended 31st August, 1975, relevant to the assessment year 1976-77, the long-term capital gains of Rs. 6.10 lakhs arising from the sale was claimed as exempt from capital gains tax on the ground that, on the date of sale, the whole of the share capital of (S) was held by the purchaser (H). The department completed the assessment (July 1976) accepting the claim.

As already stated, company (S) was taken over by another closely held company (U) two days after sale, *i.e.* on 12th April, 1975 and the transfer of the 3,466 equity shares was in substance from company (U) to company (H).

The Ministry of Finance have stated that as on the date of sale of shares, the condition of exemption *viz.* transfers being between a holding company and its wholly owned subsidiary was fulfilled. The fact, however, remains that in substance the transactions were arranged only to avoid payment of taxes and a review of the provisions of law is called for.

31. *Income escaping assessment*

(i) According to the provisions of the Income-tax Act, 1961, any distribution by a company to its shareholders on the reduction of its capital, to the extent to which the company possesses

accumulated profits, is to be treated as dividend and taxed in the hands of the shareholders.

Two private limited companies of the same family group, having total paid-up share capital of Rs. 14 lakhs (one with 140 shares of Rs. 5,000 each and another with 700 shares of Rs. 1,000 each) and also having a reserve totalling Rs. 56.80 lakhs (Rs. 26.25 lakhs and Rs. 30.56 lakhs) amalgamated with a private limited company having a paid-up share capital of Rs. 900 only (9 shares of Rs. 100 each) from 1st April, 1968. Under the scheme of amalgamation, the existing shareholders were issued shares worth Rs. 64.72 lakhs (64,720 shares of Rs. 100 each) in lieu of their total paid-up share capital of Rs. 14.01 lakhs. The amalgamated company paid during the course of the previous year relevant to the assessment year 1972-73 a sum of Rs. 32.36 lakhs to its shareholders by way of repayment of 50 per cent of its subscribed capital at the rate of Rs. 50 per share. It was also certified by the company that out of the sum of Rs. 50 repaid, Rs. 48.38 represented the return of capital and Rs. 1.62 as deemed dividend. As this repayment of capital to the extent of Rs. 32.36 lakhs was out of the reserves representing accumulated profits of the two amalgamating companies, the entire amount of repayment should have been treated as deemed dividend and brought to tax. It was, however, seen that an amount of Rs. 1.05 lakhs only (at Rs. 1.62 per share for 64,720 shares) was brought to tax as dividend income. Thus the remaining amount of Rs. 31.31 lakhs (Rs. 32.36 lakhs minus Rs. 1.05 lakhs) representing deemed dividend escaped assessment involving a tax effect of Rs. 20.35 lakhs (approximately).

Alternatively, the deemed dividend of Rs. 31.31 lakhs should have been brought to tax as capital gains in the hands of the shareholders treating that the repayment of capital would involve extinguishment of right. This was also not examined by the department.

The paragraph was sent to the Ministry of Finance in October 1979; they have stated in January 1980 that the objection is under consideration.

(ii) Under the provisions of the Income-tax Act, 1961, where any depreciable asset is sold, discarded, demolished or destroyed, the difference between the sale price and written down value is chargeable to tax in the year in which such surplus arises. The Act further provides that such profits are chargeable to tax as business income notwithstanding that the business to which receipts relate, ceased to be in existence in the year in which they are received.

An assessee-company went into liquidation during the year 1966 and an official liquidator was appointed by the High Court. During the previous year relevant to the assessment year 1974-75, shed and structure of the company's factory building original cost of which was Rs. 14,19,467 were sold for a consideration of Rs. 5,25,000. As the written down value of the said building was only Rs. 3,74,812 as determined in the assessment for the assessment year 1964-65 wherein depreciation was allowed for the last time thereon, the sale resulted in a profit of Rs. 1,50,188. No such profit was, however, considered in the assessment for the assessment year 1974-75 completed in October 1977. The assessing officer while examining this aspect considered the written down value of both factory building and non-factory building and held that there was no profit in the transaction. Since only factory building was sold as evidenced from the details of sales and also from the calculations furnished by the assessee, the written down value thereof amounting to Rs. 3,74,812 only should have been taken into account for the purpose. The mistake resulted in escapement of income of Rs. 1,50,188 with consequent tax undercharge of Rs. 1,02,503 in the assessment year 1974-75.

The Ministry of Finance have accepted the objection.

(iii) In the revised assessment of a company for the previous year relevant to the assessment year 1971-72 in July 1975, a sum of Rs. 24,351 representing tax deducted at source on interest of Rs. 1,21,756 received by it in May 1970 was refunded on orders of the Appellate Assistant Commissioner. It was, however, noticed that the interest received in the previous year

relevant to the assessment year 1971-72 was neither returned by the assessee nor assessed to tax in that year nor in the following year. The income escaping assessment led to excess carry forward of loss of Rs. 1,21,756 for the assessment year 1971-72.

The paragraph was sent to the Ministry of Finance in October 1979; they have stated in January 1980 that the objection is under consideration.

32. *Mistakes in assessments while giving effect to appellate orders*

(i) In computing the business income of a previous year, provision made in accounts for bonus payable by the assessee is an admissible deduction, if the accounts are maintained on mercantile basis. When the bonus is actually paid subsequently, the payment would not qualify for deduction.

In its accounts for the year ended 31st March, 1972, relevant to the assessment year 1972-73, a private limited company engaged in transport business made a provision of Rs. 3.51 lakhs towards bonus payable to its employees for that year. The claim for deduction of the provision was disallowed (March 1973) by the department, but the actual payment (Rs. 3.95 lakhs) made in the subsequent year ended 31st March, 1973 was allowed (April 1976) as a deduction for the assessment year 1973-74. In the meantime, the assessee had preferred an appeal against the disallowance made for the assessment year 1972-73. As a result of the appellate orders, the department revised (September 1977) the assessment and allowed the bonus provision as a deduction. But the department failed to withdraw the deduction of the actual payment allowed in the assessment year 1973-74. This resulted in short demand of tax of Rs. 2,63,700.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been revised and an additional demand of Rs. 2,63,700 raised.

(ii) A private limited company (which was subsequently taken over by a State Government Corporation) was assessed to tax for the assessment years 1959-60 and 1961-62 (March 1964 and March 1966) at Rs. 16,09,506 and Rs. 4,93,851 respectively. These assessments were set aside by the Appellate Assistant Commissioner of Income-tax in August 1965 and July 1968 respectively with directions for re-assessing the income. While giving effect to the appellate orders the tax already paid by the assessee amounting to Rs. 15,86,263 (including advance payment of tax and tax paid on provisional assessment) was refunded to the assessee in September 1965 for the assessment year 1959-60 and in November 1969 for the assessment year 1961-62. In the year 1970, due to change in jurisdiction, the case was transferred from the charge of one Commissioner in a particular State to another Commissioner in another State. The statements accompanying the records transferred did not indicate that the re-assessments for these two years were pending. The income for both the assessment years had not been re-assessed, even till July 1978 when local audit was conducted.

The Ministry of Finance have accepted the factual position.

(iii) The Income-tax Appellate Tribunal in their order dated 31st July, 1976 reduced the assessed income of an assessee-company for the assessment year 1965-66 by Rs. 43,122. While giving effect to this order in March 1977 the assessing officer determined the refund due to the assessee at Rs. 1,45,581 which was far in excess of even the amounts of reduction allowed in the assessed income. This was due to the fact that, while calculating the tax, the dividend tax of Rs. 60,000 which should have gone to reduce the rebate on supertax admissible to the company, was actually added to the rebate on supertax normally admissible. Consequently, there was excess refund of Rs. 1,20,000.

The Ministry of Finance have accepted the objection.

33. *Excess or irregular refunds*

The Income-tax Act, 1961 lays down that while making a provisional assessment for refund, adjustments to the income

or loss declared in the return shall be made by the Income-tax Officer to the extent laid down in the Act. The Act provides for the adjustment of brought forward loss, development rebate etc. as computed in the regular assessments for the earlier assessment years. There is, however, no provision for allowing the loss, development rebate etc. of earlier years in respect of which assessments are still pending.

(i) In the provisional assessment of an assessee-company for the assessment year 1977-78 (made in July 1977), the assessee's claim for set off of carried forward loss of Rs. 6,75,310 for the assessment year 1976-77 was allowed to the extent of Rs. 5,00,364 and a refund of Rs. 94,404 was allowed (July 1977). The adjustment of the loss of Rs. 5,00,364 which was carried forward as computed in a provisional (and not regular) assessment and not for the assessment year 1976-77, was not in order. This resulted in irregular refund of Rs. 94,404.

The Ministry of Finance have accepted the objection.

(ii) In the provisional assessment of another assessee-industrial investment corporation for the assessment year 1975-76 made in February 1976, the assessee's claim for set off of business loss of Rs. 3,22,191 for the assessment year 1973-74 was admitted and the assessee was allowed refund of Rs. 1,86,065. Since the assessment for the assessment year 1973-74 had not been completed by February 1976, no set off could have been given in the provisional assessment for the assessment year 1975-76. This resulted in irregular refund of Rs. 1,86,065.

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

34. *Non-levy/Short levy of interest*

(i) Under the provisions of the Income-tax Act, 1961 where the amount specified as payable in any notice of demand is not paid within thirty-five days of the service of the notice, the assessee is liable to pay interest at prescribed rates from the day

commencing after the end of the period to the date on which such payment is made.

(a) In February, 1972 a company was served with a notice of demand for an aggregate tax of Rs. 6,48,704 in respect of the assessment year 1968-69. The assessee preferred an appeal against disallowance of tax holiday relief leading to tax demand of Rs. 3,90,404; it did not dispute the payment of balance demand of Rs. 2,58,300. The company succeeded in obtaining tax relief of Rs. 3,90,404 in appeal but paid the balance undisputed demand of tax of Rs. 2,58,300 only in February 1977. Omission to pay the amount of Rs. 2,58,300 within thirty-five days of demand made in February 1972 attracted levy of penal interest of Rs. 1,49,814, which was, however, not levied by the department.

The Ministry of Finance have accepted the objection. Interest of Rs. 1,49,814 has been recovered by adjustment.

(b) In the case of another assessee-company, where the demand notice for Rs. 71,11,905 for the assessment year 1972-73 was served on the assessee on 31st March, 1975, an amount of Rs. 10 lakhs was paid on 3rd December, 1975 and amounts of Rs. 52,265 and Rs. 8,84,304 were adjusted on the 4th and 25th of July, 1979 against refunds due to the assessee for other assessment years. For delay in payment of these amounts a sum of Rs. 88,731 was payable by the assessee as interest, which, however, was not levied by the department.

The Ministry of Finance have accepted the objection.

(ii) Under the provisions of the Income-tax Act, 1961 any person who has not previously been assessed by way of regular assessment is required to file an estimate of his current income and pay advance tax accordingly. Failure to comply with the aforesaid provisions will render the assessee liable to the charge of interest at the rate of 12 per cent per annum from the first day of April next following the financial year in which the advance tax was payable upto the date of the regular assessment.

A foreign company which had not been previously assessed by way of regular assessment upto 3rd March, 1977 and whose first assessment was completed in March 1977, failed to furnish an estimate of its own current income for the assessment year 1974-75 and to pay advance tax on that basis.

The return of income for the assessment year 1974-75 was filed on 20th June, 1974 only and the assessment was completed on 4th March, 1977. Failure to furnish an estimate of its current income for the assessment year 1974-75 and to pay advance tax on that basis rendered the assessee liable to interest of Rs. 5,12,256 for the period from 1st April, 1974 to 28th February, 1977 under the aforesaid provisions of the Act. This interest was not, however, levied by the department.

The Ministry of Finance have stated that against the assessed income of Rs. 46,24,478, the income returned by the assessee was only Rs. 5,35,790 and on that income tax had been deducted at source. Since there was no tax liability on the returned income, the assessee was not liable to the levy of interest. It has been pointed out to the Ministry that the obligation to file an estimate of advance tax was there because even on the assessee's own estimate there was positive income and on breach of such obligation interest was leviable on the basis of assessed tax.

(iii) Under the provisions of the Income-tax Act, 1961, interest is payable by an assessee in case the advance tax paid on the basis of his own estimate is less than seventy-five per cent of the assessed tax.

In the case of an assessee-company the department issued a notice for payment of advance tax of Rs. 1,44,447 for the financial year 1972-73. The assessee-company filed a higher estimate of advance tax for Rs. 13,84,632 and paid the tax accordingly. The regular assessment of the assessment year 1973-74 was finalised on the 22nd October, 1975 and as the advance tax paid was less than seventy-five per cent of the assessed tax, the assessee was liable to pay interest on the difference between the assessed tax and the tax already paid.

However, no interest was levied on finalising the assessment. Taking into consideration the assessed tax as reduced by the appellate orders subsequently *viz.* Rs. 18,66,291, the interest omitted to be levied amounted to Rs. 1,34,640.

The Ministry of Finance have accepted the objection.

(iv) Under the provisions of the Income-tax Act, 1961, simple interest at prescribed rates is chargeable for the delay in submission of return of income for the period from the due date to the date of submission 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 any tax deducted at source. As per Rule made in this regard with effect from 1st January, 1975 the period for calculation of interest is to be rounded off to a whole month or months and for this purpose any fraction of a month shall be ignored. Under the instructions issued by the Central Board of Direct Taxes in October 1975, the new rule took effect from 1st January, 1975 and the calculation of interest under the new rule could be made only for the period after 1st January, 1975.

(a) In the case of a company for the assessment year 1974-75, where the return was submitted on 28th August, 1974 instead of the due date of 30th June, 1974, the department incorrectly levied interest of Rs. 88,045 in August 1977, for delayed submission of return rounding off the period of delay to one month only. Since the period of calculation of interest fell prior to 1st January, 1975, the interest was correctly leviable for the entire period of 1 month and 28 days which worked out to Rs. 1,67,570. Failure to comply with the Board's instructions resulted in short levy of interest of Rs. 79,525.

The Ministry of Finance have accepted the objection.

(b) The income-tax assessment of an assessee-company for the assessment year 1974-75 was revised in March 1978 computing the taxable income at Rs. 4,91,515 on which tax worked out to Rs. 3,35,459. The company submitted its return

of income on 17th May, 1976 after the expiry of the due date *viz.* 30th June, 1974. For the period of delay of 22 months, a sum of Rs. 73,788 was payable by it as interest calculated at twelve per cent on the tax of Rs. 3,35,459. This was, however, not, levied by the department.

The Ministry of Finance have stated in February 1980 that the assessment in question has been rectified and that the amount of additional tax raised is Rs. 73,788.

35. *Avoidable or incorrect payment of interest by Government*

Under the provisions of the Income-tax Act 1961, where a refund that has become due to an assessee in pursuance of any order passed in appeal is not granted within a period of three months from the end of the month in which such order is passed, the Central Government shall pay simple interest at the appropriate rate on the amount of refund so due from the date immediately following the expiry of the period of three months aforesaid to the date on which the refund is granted.

Consequent upon certain orders passed in September 1974 in appeal by an Income-tax Appellate Tribunal, an assessee-company became entitled to a refund of Rs. 7,65,913 for the assessment year 1966-67. The refund, which should have been granted before the end of December 1974, was actually paid to the assessee-company only in November 1976 *i.e.* after a lapse of over 22 months. The delay in the grant of the refund resulted in payment of interest of Rs. 1,68,498 which could have been avoided had prompt action been taken by the department to grant in timely refund.

The Ministry of Finance have accepted the objection.

Other topics of interest

36. *Excess relief due to unconditional permission given for change of previous year*

Under the Income-tax Act, 1961, an assessee has the option to make up the accounts of his business upto any date in a year

and once the accounts are so made up for a year, he should not vary the dates in a subsequent year, except with the consent of the department. While giving the consent, the department may impose such conditions as it may think fit, to safeguard the interest of revenue. It might even refuse to give the consent for valid reasons.

A domestic public company manufacturing certain specified articles was entitled to the concession of tax credit certificates upto and inclusive of the assessment year 1970-71. Upto the assessment year 1969-70 it was closing its annual accounts on 30th September. In April 1969, it made a request to the department for changing the accounting year to 31st March. The request was granted by the department (July 1969) without imposing any conditions. Accordingly, for the assessment year 1970-71, which was the last year of the scheme for claiming the benefit of tax credit certificate, the assessee closed its accounts for the 18 month period ended 31st March, 1970. On the basis of the income of Rs. 50.09 lakhs assessed for the relevant previous year (comprising 18 months), the department allowed the assessee a tax credit certificate for Rs. 2.21 lakhs (representing 10 per cent of the tax due on the assessed income).

But for the consent given by the department for the change of the previous year, the assessee would have closed the accounts relevant to the assessment year 1970-71 on 30th September, 1969, comprising only the normal 12 months and become entitled to a concession of Rs. 0.40 lakh by way of tax credit certificate against Rs. 2.21 lakhs granted with reference to the income of eighteen months' period. The omission on the part of the department to notice the implication of the assessee's request made in respect of the last assessment year for which the benefit of tax credit certificate was available resulted in the grant of an excess benefit of Rs. 1.81 lakhs to the assessee.

The Ministry of Finance have stated in January 1980 that at the time change of previous year was granted by the Income-tax officer, he did not foresee any claim to relief under Section 280 ZB of the Act.

37. *Non-levy of additional income-tax*

Under the provisions of the Income-tax Act, 1961, where the profits and gains 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 (not being an investment or trading company) is liable to pay additional income-tax equal to 25 per cent of the distributable income as reduced by the amount of dividends actually distributed, if any.

An industrial company which was not a company in which the public were substantially interested declared a dividend of only Rs. 2,80,000 against the statutory sum of Rs. 3,66,848, being 45 per cent of the distributable income of Rs. 8,15,217 for the previous year relevant to the assessment year 1977-78. Thus additional tax of Rs. 1,33,804 (being 25 per cent of the difference between the distributable income of Rs. 8,15,217 and the actual dividend of Rs. 2,80,000 declared) was imposable on the assessee-company but no such tax was levied or collected by the department.

The Ministry of Finance have stated in February 1980 that the proposal under Section 104 of the Act was sent by the Inspecting Assistant Commissioner in August 1979 and the proceedings are pending.

SURTAX

38. *Surtax*

To act as 'a disincentive to excessive profits' and 'to help to keep down the prices', a special tax called super profits tax was imposed on companies making excessive profits during the asessment year 1963-64 under the Super Profits Tax Act, 1963. This tax was replaced, from the assessment year 1964-65, by surtax levied under the Companies (Profits) Surtax Act, 1964. Surtax is levied on the 'chargeable profits' of a company in so

far as they exceed the statutory deduction, which is an amount equal to 10 per cent (15 per cent from 1st April, 1977) of the capital of the company or Rs. 2 lakhs, whichever is greater.

During the period under review, under-assessment of super profit tax/surtax of Rs. 60.17 lakhs was noticed in 91 cases. A few illustrative cases are given in the following paragraphs.

39. *Incorrect computation of capital*

(i) Under the provisions of the Companies (Profits) Surtax Act, 1964, an amount standing to the credit of any account in the books of a company, if it is in the nature of liability or provision, shall not be regarded as reserve for the purposes of computation of capital. Further, where the balance in the general reserve as on the 1st day of the relevant previous year includes any sum proposed to be appropriated for distribution of dividend, the general reserve balance as reduced by such sum alone is to be included in the capital computation for the purpose of levy of surtax.

In the case of an assessee-company, the general reserve balance of Rs. 2,25,47,140 in the assessment year 1975-76 included a provision of Rs. 31,50,144 for payment of dividend for the year 1972-73. Under the provisions of the Surtax Act, the amount of dividend proposed to be paid out of general reserve was required to be deducted from the computation of capital while working out the statutory deduction. Failure to do so resulted in excess allowance of statutory deduction of Rs. 3,15,014 with tax undercharge of Rs. 1,49,632.

The Ministry of Finance have accepted the objection. The amount of additional demand of Rs. 1,49,632 has been raised and collected.

(ii) Under the Companies (Profits) Surtax Act, 1964, the dividend income received by an assessee-company from an Indian company or a company which has made the prescribed arrangements for the declaration and payment of dividends within

India is not to be included in the chargeable profits. Further, the investments made in respect of the shares of those companies so far as the value of investments exceeds the value of borrowings and certain reserves specified therein, are required to be deducted in computation of capital. While applying these provisions in the case of an assessee-company the value of only those shares which yielded dividend income during the relevant previous years was considered for deduction instead of the value of the entire investments in the shares of Indian companies.

Again under Rule 4 of the Second Schedule of the Companies (Profits) Surtax Act, 1964, where a part of income, profits and gains of a company is not includible in its total income, its capital shall be the sum ascertained in accordance with the said rules diminished by an amount which bears to that sum the same proportion as the amount of the aforesaid income, profits and gains bear to the total amount of its income, profits and gain.

Though from the dividend income received from the company deductions were allowed in respect of inter-corporate dividends and dividends in respect of tax free profits, its capital was not proportionately reduced.

These mistakes resulted in under-assessment of chargeable profits by Rs. 94,274, Rs. 1,56,220 and Rs. 2,52,361 for the assessment years 1973-74 to 1975-76 respectively with consequent undercharge of tax of Rs. 1,89,886 for all the three years.

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

40. *Non-levy/short levy of surtax*

Pursuant to the recommendations of the Public Accounts Committee contained in paragraph 6.7 of their 128th Report (Fifth Lok Sabha) the Central Board of Direct Taxes issued instructions in October 1974, that surtax assessment proceedings should be initiated along with the income-tax proceedings and the surtax assessments finalised within a month of the completion of the relevant income-tax assessments.

(i) The regular assessments of income-tax of an assessee-company for the assessment years 1974-75 and 1975-76 were finalised on the 15th December, 1976 and the 20th March, 1977 respectively. The information available in the assessment records including the final accounts of the respective previous years disclosed that the assessee was liable to levy of surtax for both the assessment years. However, neither the surtax returns had been filed by the assessee nor had they been called for till the date of audit (7/78). Hence, chargeable profits of Rs. 2,53,902 and Rs. 8,18,968 for the assessment years 1974-75 and 1975-76 escaped taxation resulting in non-levy of surtax of Rs. 63,572 and Rs. 2,85,371 for the assessment years 1974-75 and 1975-76 respectively.

The Ministry of Finance have accepted the objection.

(ii) In another case, the income-tax assessment of an assessee-company for the assessment year 1964-65 was revised in October 1971 computing the taxable income and tax payable thereon at Rs. 54,71,882 and Rs. 26,94,552 respectively. The surtax assessment was revised accordingly in October 1971 and a net chargeable profit of Rs. 10,22,820 was computed on which surtax of Rs. 3,27,303 was levied. The income-tax assessment was revised subsequently in August 1973 and again in October 1977 wherein the tax liability was reduced to Rs. 22,25,885 as a result of change in the rate of tax and qualifying income for tax relief on new industrial undertakings. Consequently, the net chargeable profits would work out to Rs. 14,67,620 and surtax of Rs. 4,69,639 would be leviable thereon. No action was, however, taken by the department to revise the surtax assessment. The omission to revise the surtax assessment resulted in short levy of surtax of Rs. 1,42,336 for the assessment year 1964-65.

While accepting the objection, the Ministry of Finance have stated that the assessment in question has been revised and that the amount of additional demand of Rs. 1,42,336 has been raised and collected.

(iii) In still another case, the income-tax assessment of an assessee-company for the assessment year 1974-75 was completed in September 1977 at Rs. 17,13,365. According to the accounts of the company filed for the purpose of income-tax assessment, its chargeable profits worked out to Rs. 3,71,974. The paid-up capital (including reserve) of the company amounted to Rs. 20,66,828 as on the first day of the relevant previous year. The chargeable profits of the company had thus, exceeded the amount of statutory deduction of Rs. 2,06,683 (being ten per cent of the capital employed in the company) by Rs. 1,65,291, thereby attracting levy of surtax. The company had neither filed a return in terms of Section 5(1) of the Surtax Act nor was any action initiated by the department to call for the same and frame assessment thereon. The chargeable amount of Rs. 1,65,291, therefore, escaped assessment on which surtax leviable as Rs. 44,419 was not charged. Besides, penalty provisions for default in filing the return were also attracted.

The Ministry of Finance have accepted the objection in principle.

(iv) In the case of a company-assessee, the chargeable profits, for the assessment year 1976-77 exceeded the amount of statutory deduction by Rs. 1,81,966 and this attracted the levy of surtax. The assessee did not file any return of chargeable profits for the assessment year 1976-77, and the department also failed to initiate any action for completion of surtax assessment. The omission in this regard resulted in non-levy of surtax of Rs. 46,896, besides making the assessee liable to a penalty of an equal amount.

The Ministry of Finance have accepted the objection.

41. *Mistakes in calculation of surtax*

Under the provisions of the Companies (Profits) Surtax Act, 1964 read with the Third Schedule thereto prescribing the rates of surtax for the assessment year 1975-76 and onwards, where the aggregate amount of the liability of a company in respect of

income-tax and surtax exceeds seventy per cent of the total income of the company, the surtax calculated according to the prescribed rates shall be reduced by the amount of such excess and the balance shall be the amount of surtax payable by the company, provided the company, *inter alia*, is a domestic company in which the public are substantially interested or a cent per cent subsidiary of such a company. Further, surtax is leviable with effect from 1st April, 1975, at the rate of forty per cent on the chargeable profits exceeding five per cent of capital as against thirty per cent.

In the case of a domestic company, which was not a company in which the public were substantially interested or a cent per cent subsidiary of such a company, the surtax leviable for the assessment year 1975-76 was erroneously restricted to seventy per cent of its total income. Besides, surtax was charged at thirty per cent instead of forty per cent of the chargeable profits exceeding five per cent of the capital of the company. These mistakes led to a total short levy of surtax of Rs. 1,31,876 in the assessment year 1975-76.

While accepting the objection, the Ministry of Finance have stated that the assessment in question has been revised and that the additional demand of Rs. 1,31,876 has been raised and collected.

CHAPTER III

INCOME TAX

42. Income-tax collected from persons other than companies is booked under the Major Head "021-Taxes on income other than Corporation Tax". Under Article 270 of the Constitution, 80 per cent of the net proceeds of this tax, except insofar as these are attributable to Union emoluments, Union Territories and Union Surcharges, is assigned to the States in accordance with the recommendations of the Sixth Finance Commission.

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

44. *Avoidable mistakes in computation of tax*

(i) The income-tax assessment of an assessee-individual for the assessment year 1974-75 was finalised on 29th December, 1976 under Section 144 of the Income-tax Act, 1961, determining the income at Rs. 7,54,360. While charging interest under Section 217 of the Act for failure to furnish an estimate of advance tax the period for calculation of interest was taken erroneously at 20 months instead of 32 months. This resulted in undercharge of interest by Rs. 83,242.

While accepting the objection the Ministry of Finance have stated that the assessment in question has been revised and an additional demand of Rs. 83,242 raised.

(ii) The Income-tax Act permits an assessee to file a revised return of income at any time before the assessment is made, in case he discovers any omission or wrong statement made in the original return. An assessee-registered firm filed a revised return

of income for the assessment year 1974-75 on 28th January, 1977 on the ground that a sum of Rs. 1,22,496 credited to the profit and loss account of the relevant previous year against export incentive receivable had not materialised as the consignment was not exported and the income to that extent, was required to be reduced. The assessment was finalised on 23rd March, 1977 accepting the claim made by the assessee in the revised return. The assessment for the assessment year 1975-76 was subsequently finalised on 2nd January, 1978 on the basis of the original return filed on 13th August, 1975 without corresponding adjustment of Rs. 1,22,496 though the profit and loss account of the relevant previous year was debited with Rs. 1,22,496, being the amount of unrealised export incentive written back. Further, though the assessee's letter indicated that a revised return was filed for the assessment year 1975-76 also, the return was not on record. This resulted in under-assessment of income by Rs. 1,22,496 with consequent undercharge of tax of Rs. 61,934 in the case of the firm and the partners.

The Ministry of Finance have accepted the objection.

45. *Incorrect status adopted in assessments*

Under the provisions of the Income-tax Act, 1961, income arising to a Hindu undivided family is to be assessed in the hands of that family unless a partition has taken place and an order recognising the partition has been passed by the Income-tax Officer.

In the case of a Hindu undivided family, capital gain arising on the sale of property was not assessed in the hands of the family but was assessed in the hands of the individual members of that family, though there were no orders passed by the Income-tax Officer recognising the partition of the joint family. This resulted in short levy of tax of Rs. 83,396 in the assessment year 1976-77.

The Ministry of Finance have stated that a notice under Section 147(a) of the Act has been issued to the family to verify the claim of partition.

46. *Incorrect computation of salary income*

A. *Assessment of foreign technicians*

(i) The Income-tax Act, 1961, allows, under certain conditions, exemption from tax to remuneration of foreign technicians in the employment of Government or a local authority or a statutory corporation or any business carried on in India. The exemption is admissible for a period of 36 months from the date of arrival in India in the case of technicians whose services as such commenced from a date prior to 1st April, 1971 and for a period of 24 months from the date of arrival in the case of those whose services commenced from a date on or after 1st April, 1971. One of the conditions to be fulfilled in this regard is that the contract of service should be approved by the Central Government, the application for such approval having been made to the Government before the commencement of such service or within six months of such commencement.

This period is further extended under certain conditions laid down in the Act. One of the conditions for the grant of aforesaid exemption is that the contract of service in which the amount of salary payable is specified should have the approval of the Central Government before the 1st day of October of the relevant assessment year.

(a) In the case of seven foreign technicians, the employers paid higher salaries as compared to those included in the contracts of service approved by the Central Government. As an important condition of the approval was violated in these cases, these could not be treated as cases carrying the approval of the Central Government. The erroneous exemption in this regard resulted in short levy of tax of Rs. 1,53,26,915 for the assessment years 1972-73 to 1977-78, including Rs. 135 lakhs (approx.) in one case wherein the specific condition that the income-tax on the salary should be paid by the employer was also violated.

The Ministry of Finance have accepted the objection in all the cases.

(b) In another case of a foreign technician, sanction for continued employment beyond the initial period of 24 months was accorded after 1st of October of the relevant assessment year. Further, salary was paid in excess of the amount approved in the contract. As such the assessee was not entitled to the exemption admissible to a foreign technician. The erroneous allowance of exemption resulted in short levy of tax of approx. Rs. 1,90,000 for the assessment year 1975-76.

The Ministry of Finance have accepted the objection.

(c) In the case of five foreign technicians, the exemption was granted although the condition regarding the application for the approval of contract of service having been made to the Government before the commencement of service or within six months of such commencement, was not fulfilled. The irregular exemption in these cases for the assessment years 1972-73 to 1978-79 amounted to Rs. 4,29,118, exclusive of interest that could be levied under the Act for non-deduction of tax at source by the employer. In two out of these five cases, salary was also paid in excess of that included in the approved contract of service.

The Ministry of Finance have accepted the objection in four cases. They have stated that in respect of one case the objection is under consideration.

(ii) According to the provisions of the Income-tax Act, 1961, if any amount specified as payable in a notice of demand is not paid within the period stipulated, simple interest shall be payable at the prescribed rate from the day commencing after the period stipulated.

As per the guarantee executed by a company on behalf of a foreign technician employed by it, the company was liable to pay the tax, interest etc. due to the Income-tax department from the foreign technician. Under a notice of demand issued by the department in May 1976, the employer company was liable to pay an amount of Rs. 44,43,854 being the income-tax due from the assessee-foreign technician on or before 29th June, 1976.

The payment was made by the company only on 6th January, 1977. Interest for delay in paying the tax was, however, not levied. The omission to do so resulted in non-levy of interest of Rs. 2,49,666 in June 1978.

The Ministry of Finance have accepted the objection.

(iii) Forty-six foreign technicians employed by a company furnished returns of income for the first time for the assessment year 1975-76 by June 1975 claiming exemption for the remuneration received for services rendered in India. In November 1977, the department issued notices to the employees and to the assessee-company for completion of assessment. Both the employer-company and the employees were not traceable at the addresses furnished in the returns of income. In August 1978, the Income-tax Officer made summary assessments in all 46 cases, contrary to the instructions of the Central Board of Direct Taxes of July 1977 granting the exemption claimed for. The assessees did not furnish full particulars justifying their claims for exemption, nor did the department ascertain the same and keep them on record before granting the exemption. The incorrect grant of exemption by the Income-tax Officer without satisfying himself about the assessees' entitlement thereto led to undercharge of tax of Rs. 8,69,149 for the assessment year 1975-76.

The paragraph was sent to the Ministry of Finance in October 1979 ; their reply is awaited (February 1980).

(iv) In the case of a foreign technician, the Government approval of his contract was not received and hence no exemption was allowed in the assessment year 1976-77 completed on 3rd December, 1977. It was, however, seen from the assessment records that tax on his emoluments was to be borne by the employer. But the tax payable by the employer was not treated as perquisite in the hands of the technician resulting in a short levy of tax of approx. Rs. 92,000 for the assessment year 1976-77.

The paragraph was sent to the Ministry of Finance in August 1979 ; they have stated in December 1979 that the objection is under consideration.

B. *Assessment of others*

Under the provisions of the Income-tax Act, 1961, any lumpsum payment of compensation, due to or received by an employee from his employer in connection with the termination of his employment or modification of the terms of his employment and any payment due to or received by an employee from any fund, other than an approved superannuation fund, to the extent to which it does not consist of contributions by the employee, is to be regarded as profits in lieu of salary and taxed as such. Compensation received by a pilot against loss of his flying licence falls under this category as confirmed by the Central Board of Direct Taxes in their instructions issued in July 1976. However, while assessing the income of two pilot assessees, one for the assessment year 1972-73 and the other for the assessment year 1975-76, compensation of Rs. 2,69,142 received by them from an insurance company towards loss of flying licence was omitted to be assessed to tax, resulting in under-assessment of income of Rs. 2,69,142 and short levy of income-tax of Rs. 2,04,120.

The Ministry of Finance have accepted the objection in both the cases.

47. *Incorrect computation of income from house property*

(i) Under the provisions of the Income-tax Act, 1961, the annual letting value of house property owned by an assessee is assessable as income from house property, irrespective of the fact whether the owner is actually in receipt of income or not. Where a property is let out and falls vacant during a part of the year, a vacancy allowance in the shape of proportionate deduction from the annual value is allowable. This vacancy allowance is not admissible where the property is vacant throughout the year.

An assessee did not return any rental income for the assessment years 1967-68 to 1973-74 in respect of the second floor of a building belonging to him on the ground that it was vacant right from its construction in 1965. The assessee's claim was accepted by the department. As a result, income of Rs. 46,300

escaped assessment in the assessment years 1967-68 to 1973-74 with an undercharge of tax of Rs. 36,173.

The Ministry of Finance have accepted the objection.

(ii) Interest on capital borrowed for the acquisition, construction, repair, renewal or reconstruction of the property and any annual charge on the property, (other than that created voluntarily or a capital charge) are allowable as deductions in computing income from house property.

As per the will of a deceased individual, a house property, purchased by him during his life-time in the name of his wife, the income from which was being assessed in his hands upto the date of his death, devolved on his wife and the other assets and liabilities (in respect of his money lending business) on his three daughters-in-law. After his death, the income from house property was assessed in the hands of his wife for the assessment years 1973-74 to 1976-77. In computing the income of his wife from house property for these assessment years, interest on a sum of Rs. 2,03,248, stated to be the liability taken over by the assessee along with the house property, was allowed as deduction. However, it was verified from the assessment records of the deceased that no deduction was claimed and allowed in his assessments on account of borrowals for house construction and that there was no liability on the property. In view of this and in view of the specific provision in the will that the liabilities of the deceased should be borne by the daughters-in-law, the deduction towards interest payment from property income was not in order. The incorrect deduction resulted in total undercharge of income-tax of Rs. 55,970 for these four years.

The Ministry of Finance have accepted the objection.

48. *Incorrect computation of business income*

(i) Under the provisions of the Income-tax Act, 1961, any expenditure laid out wholly and exclusively for the purposes of business or profession can be deducted while computing the income chargeable under the head "profits and gains of business

or profession". Interest paid on capital borrowed for the purposes of business or profession is an allowable deduction from taxable income. There is, however, no provision for allowing deduction of interest on moneys borrowed for payment of income-tax.

In the assessment of a registered firm for the assessment year 1970-71, the assessee's claim for deduction on account of interest paid on its overdrafts from banks was disallowed by the department on the ground that the borrowings were attributable to payment of income-tax arrears ranging from Rs. 2 lakhs to Rs. 3 lakhs made on behalf of the four partners. From the assessment year 1971-72 onwards, the firm charged interest on the sums withdrawn on this account by the partners who in turn claimed deduction thereof in their individual assessments. The deduction thus claimed by the partners was allowed by the assessing officer notwithstanding the fact that interest charges incurred for liquidating income-tax arrears cannot be held to have been laid out for the purposes of business.

The incorrect allowance of the deduction claimed by the four partners of the firm for the assessment years 1972-73 to 1975-76 led to short computation of taxable income aggregating Rs. 2.66 lakhs with a resultant tax undercharge of Rs. 2.20 lakhs.

The Ministry of Finance have partly accepted the objection.

(ii) The income chargeable under the head "Profits and gains of business or profession" is computed in accordance with the method of accounting regularly employed by the assessee. Where the Income-tax Officer is not satisfied about the correctness or the completeness of the accounts of the assessee, or where no method of accounting has been regularly employed by the assessee, the business income should be computed according to the best judgment of the assessing officer. In the case of liquor contractors, as the accounts maintained by them were normally not found to be reliable, the Commissioner of Income-tax of a charge had issued instructions that, after ascertaining the actual quantity of liquor lifted, the net profit on the sale of liquor should be calculated on a flat rate basis on the quantity of liquor lifted.

In the case of an assessee-individual deriving income from liquor contracts, the assessments for the assessment years 1965-66 to 1971-72 were made on 10th January, 1974 on a summary basis under Section 143(1) of the Act with reference to the income returned. Neither the details of liquor contracts of the assessee forwarded by the Commissioner of Income-tax on 8th July, 1970 nor the above mentioned instructions of the Commissioner were kept in view while making the assessments. Interest leviable for belated submission of returns was also noticed to have been charged less. These mistakes led to tax undercharge of Rs. 1,58,795 including interest amounting to Rs. 73,258.

The Ministry of Finance have stated that re-assessments made by the Income-tax Officer have been set aside by the Tribunal, with a direction to do fresh assessments.

(iii) The Act further provides that if an assessee offers no explanation about the source of amounts spent by him during the year either on acquisition of assets or on any other account, the unexplained amount should be deemed to be his income for the relevant assessment year.

For the previous year ended 31-3-1974 relevant to the assessment year 1974-75, an individual returned a sum of Rs. 6,510 as income from proprietory transport business and the same was accepted (January 1977) by the department.

The computation of business income, which was not supported by the profit and loss accounts etc., was made by the assessee on the basis that, against the total amount of Rs. 13.09 lakhs spent by him during the year on acquisition of assets (Rs. 4.07 lakhs) and repayment of loans (Rs. 9.02 lakhs), an amount of Rs. 10.50 lakhs was met from fresh borrowings and sale proceeds of certain vehicles and the balance of Rs. 2.59 lakhs from the cash profits of the business. Deducting Rs. 1.32 lakhs towards depreciation of assets, a sum of Rs. 1.27 lakhs should have been offered as business income. But the assessee claimed a further deduction of Rs. 1.21 lakhs towards interest paid on loans and offered only Rs. 6,510 as the business income. In the

method of computation adopted, no deduction was admissible for any expenses relating to the business. The basis of computation adopted was that the actual cash surplus arising after meeting all payments of revenue nature for carrying on the business was utilised for acquisition of assets and repayment of loans. In view of this, deduction of Rs. 1.21 lakhs on account of interest paid on loans was not in order and resulted in under-assessment of income to that extent.

It was further noticed that a loan of Rs. 50,000 repaid by the assessee in April 1973 was not taken into account in determining the total amount of loan repaid during the year (Rs. 9.02 lakhs). This resulted in a further under-assessment of income by Rs. 50,000.

There was thus total short levy of tax of Rs. 1,46,668.

The Ministry of Finance have accepted the objection in principle.

(iv) In the assessment for the assessment year 1972-73 of a Co-operative Society running a sugar factory, it was noticed in audit in June 1975 that there was under-assessment of income by Rs. 12,16,004 with consequent short demand of tax of Rs. 5,59,362 excluding interest under Sections 139 and 215 of the Act on account of the following mistakes :

	Rs.
1. Incorrect deduction of difference in value of closing stock	9,07,448
2. Bonus not relating to the year of account incorrectly allowed as deduction	1,84,162
3. Provision for mileage debited to the Manufacturing Account but omitted to be added back	1,00,000
4. Tax free interest received on investments erroneously allowed as straight deduction, instead of allowing rebate of tax thereon	41,894
5. Interest on fixed deposits erroneously deducted	2,500
TOTAL	12,36,004
6. Omission to allow deduction of Rs. 20,000 under Section 80P (2)(c)	20,000
Net under-assessment of income	12,16,004

The department accepted (April 1976) the objection in part and stated that the Income-tax Officer had been directed to examine the audit objection in proper perspective. During the subsequent audit conducted in July 1976 it was observed that a rectification order under Section 154 of the Act to set right the mistakes pointed out in the earlier Audit was passed by the Income-tax Officer in September 1975. The rectification order was, however, defective in the following respects :—

1. The interest element of Rs. 13,671 included in the refund of Rs. 66,737 relating to the assessment year 1967-68 was omitted to be brought to tax in the assessment year 1971-72.

2. Rebate on tax-free interest pointed out in item 4 above was allowed at the average rate of 38.84 per cent instead of restricting it to 27½ per cent as required under Section 86A of the Act.

3. Interest accrued on the investment was short taken by Rs. 6,246.

On a proposal by the Income-tax Officer, the Commissioner of Income-tax set aside the assessment order and the rectification order under Section 263 in March 1977 and directed the Income-tax Officer to re-do the assessment. It was verified in audit in July 1979 that reassessment in this case was completed by the Income-tax Officer in February 1979. The additional demand of tax attributable to the audit objection, as seen from the reassessment order, amounted to Rs. 6,44,421 including interest amounting to Rs. 1,10,797.

The Ministry of Finance have accepted the objection.

(v) Under the provisions of the Income-tax Act, 1961, where an assessee incurs any expenditure in respect of which payment is made in a sum exceeding two thousand five hundred rupees otherwise than by a crossed cheque drawn on a bank or by crossed bank draft, such expenditure shall not be allowed as deduction while computing the income.

In one case, the registered firm made payments of Rs. 75,000 in cash in excess of Rs. 2,500 to a firm in the assessment year 1973-74 otherwise than by a crossed cheque or bank draft. Omission to disallow this amount at the time of assessment resulted in under-assessment of income by Rs. 75,000 with a tax effect of Rs. 52,423 in the hands of the firm and the partners.

The Ministry of Finance have accepted the objection.

Irregularities in allowing depreciation and development rebate

49. *Depreciation on machinery obtained on hire-purchase*

The Income-tax Act, 1961, provides for depreciation allowance in respect of buildings, plant and machinery, owned by the assessee and used for the purposes of the business. Where plant and machinery are obtained on hire-purchase, the transfer of ownership thereon in favour of the hirer happens, only after the last instalment of the hire charges is paid to the vendors, and hence no depreciation is admissible till that date.

On the incorrect grant of depreciation and development rebate in such cases of hire purchase, being pointed out in the Audit Report 1966, the Public Accounts Committee recommended in February 1968, that, keeping in view the judicial pronouncements on the subject, an early decision should be taken as to whether the law itself required any amendment. The Ministry reported in December 1968 that an amendment to the Income-tax Act sponsored for the purpose would have to await the passing of the Hire Purchase Bill which was then before the Parliament.

The Hire Purchase Bill was passed by the Parliament in June 1972, but no amendment to the Income-tax Act has been made so far (February 1980). As a result, depreciation on plant and machinery obtained on hire purchase continues to be given contrary to the law.

Thus an assessee-firm claimed and the department allowed deduction of Rs. 3,86,588 and Rs. 3,55,959 for the assessment years 1974-75 and 1975-76 respectively on account of depreciation on assets acquired by the firm on hire purchase. As the ownership was not transferred to the firm in the relevant previous year, the firm was not eligible for the depreciation allowance. The erroneous allowance resulted in short levy of tax of Rs. 5,86,576 for the assessment years 1974-75 and 1975-76.

The Ministry of Finance have stated that the Board had through their executive instructions contained in their circular of March 1943, letters of June 1959 and July 1963 and Instruction of September 1977 authorised the grant of depreciation allowance in respect of assets acquired on hire purchase basis. It has been pointed out to them that the executive instructions cannot over-ride the clear provisions of law.

50. *Development rebate*

Under the provisions of the Income-tax Act, 1961, development rebate at higher rate was admissible on machinery or plant installed for the purposes of business of construction, manufacture or production of any one or more of the articles or things specified in the Fifth Schedule to the Act, which, *inter alia*, included the plant and machinery used for the purpose of vegetable oil manufactured by solvent extraction method from seeds.

(i) In the case of a registered firm, engaged in the extraction of oil out of rice bran by solvent extraction method, development rebate at higher rate of 35 per cent was allowed on solvent plant machinery worth Rs. 13,36,300 in the assessment year 1969-70, Rs. 1,25,224 in the assessment year 1970-71, and 25 per cent on Rs. 35,890 in the assessment year 1971-72, Rs. 14,32,546 in the assessment year 1972-73 and Rs. 2,72,160 in the assessment year 1973-74. Since the plant and machinery of the assessee were not used for the purpose of vegetable oil manufactured by solvent extraction process from seeds but from rice bran, the development rebate was admissible only at

the lower rate of 20 per cent, for the assessment years 1969-70 and 1970-71 and 15 per cent for the assessment years 1971-72 to 1973-74. The mistake resulted in excess allowance of development rebate of Rs. 3,93,271 in the assessment years 1969-70 to 1973-74 with consequent tax undercharge of Rs. 1,77,925 in these years.

The Ministry of Finance have accepted the objection.

(ii) The Act further provides that if the machinery or plant on which development rebate has been allowed in earlier assessment year, is transferred before the expiry of eight years from the end of the previous year in which it was installed, the development rebate so granted should be deemed to have been allowed wrongly and the same has to be withdrawn. The Act also provides exception to this provision of withdrawal in certain circumstances, where a firm is succeeded to, by a company which satisfies the conditions prescribed. One of the conditions is that all the property of the firm relating to the business immediately before the succession takes place, becomes the property of the company.

An assessee-firm was taken over by a company with effect from 30-11-1970. But one of the assets of the firm, namely the factory building, was not transferred to the company but was sold separately by the firm on 19-2-1971 to some other concern, for a sum of Rs. 1,75,000. As the conditions necessary for non-withdrawal of the development rebate were not fulfilled, the development rebate of Rs. 1,34,850 allowed in the assessment year 1972-73 should have been withdrawn. Failure to do so resulted in an avoidable loss of revenue to the extent of Rs. 85,416.

The Ministry of Finance have accepted the objection.

Irregular exemptions and reliefs given

51. *Charitable Trusts*

Under the provisions of the Income-tax Act, 1961, income derived from property held under trust for charitable

or religious purposes, is exempt from tax. By an amendment made with effect from 1st April, 1971, the exemption was made inadmissible if the funds of the trust were invested in a concern in which the author of the trust has substantial interest. If, however, the amount of investment of the funds of the trust in such a concern does not exceed 5 per cent of the capital of the concern, the exemption would be available for any income other than the income from the investment.

With a view to checking one of the abuses found in the management of companies *viz.*, voting rights attached to shares and debentures, held in trust, being used for the personal benefit of the founders of the trust, in 1963 a provision was made in the Companies Act, 1956 whereby the voting rights attached to shares and debentures held in trust are vested in the public trustee appointed by the Central Government. This provision is not applicable where the value of the shares or debentures of a company held in trust does not exceed Rs. 5 lakhs or 25 per cent of the paid-up share capital of the company, whichever is less.

(i) An individual created ninety-seven trusts through ninety-seven separate deeds, executed on a single day *viz.*, 8th February, 1973, with an initial contribution of Rs. 100 each. The objects of all the trusts were specified in identical terms as relief of the poor, education, medical relief, advancement of any object of general public utility, not involving the carrying on of any activity for profit. The assessee-founder and his wife were the only two trustees for all the trusts and all of them were denoted as functioning at the same address.

During the three years' period ended 31st March, 1976, the trusts received cash donations to form part of their corpus from one or the other of seven private companies, and such donations amounted to Rs. 18,76,150. The amount of donation received by each trust ranged from Rs. 14,200 to Rs. 20,200. These donations were utilised by the respective trusts for the purchase of equity and preference shares from the very same

companies, at their face value, to the extent of the amount of donations.

In the assessment of these trusts for the assessment years 1974-75 and 1975-76 and of one of the trusts for the assessment year 1976-77, the incomes of the trusts were held to be exempt under the provisions of the Income-tax Act. However, the creation of 97 trusts on the same date and the subsequent transactions and donations made by the founder, his family members and business concerns were inter-connected transactions which would make them subject to the provisions of Section 13(1)(h) of the Income-tax Act, 1961 and Section 21A of the Wealth-tax Act, 1957 and these trusts would not be exempt from tax. Exemption was, thus, incorrectly granted in these cases.

The Ministry of Finance have stated that the audit objection is under consideration (February 1980).

(ii) Donations received by a charitable trust with a specific direction that they shall form part of the corpus of the trust are not treated as its income.

(a) Donations in the form of unquoted equity shares of certain private limited companies received by two charitable trusts in March 1972 were taxed in their hands as the income for the assessment year 1973-74, rejecting the claim of the assessees that these donations were exempt having been made by the donor towards the corpus of the trusts. While assessing these donations, added to other income of the trusts, however, the money equivalent of these shares in one of these companies was determined at Rs. 2,253 per share on their returned value, based on their book value in the accounts of the donor. Even in the wealth-tax return for the assessment year 1972-73, the donor had returned the market value of the same shares at Rs. 3,186, as on 31st March, 1972. It was pointed out in audit (January 1978) that at even the value of Rs. 3,186 per share adopted in the wealth-tax assessments, the income of each trust was under-assessed by Rs. 83,037 with consequent undercharge

of tax of Rs. 1,62,336 in respect of both these trusts. The market value of these shares was required to be computed on the basis of the market value of the assets of the company including its goodwill for the levy of income-tax.

The Ministry of Finance have accepted the audit objection and stated that the demand for total tax of Rs. 8,55,210 has been raised on the basis of valuation of these shares at Rs. 7,035 per share.

(b) A charitable institution received a sum of Rs. 2,83,501 as donations to be spent in certain specified areas. There was no direction from the donors that the sum shall form part of the corpus of the institution and yet the department treated the donations as exempt.

Omission to treat the contributions as income of the institution resulted in under-assessment of income by Rs. 2,83,501 for the assessment year 1975-76 with consequent short levy of tax of Rs. 1,94,900.

The Ministry of Finance have accepted the objection.

(iii) 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. However, the Act permits trusts to accumulate or set apart income for future application, provided the trust specifies by notice, in writing given to the Income-tax Officer, the purposes for which the income is being accumulated and the period, not exceeding ten years, for which it is to be accumulated and the moneys so accumulated are invested in specified securities within the time prescribed.

However, in the case of a charitable trust, surplus income of Rs. 1,56,436 relating to the previous year ending 31-3-1975 relevant to the assessment year 1975-76 was exempted in the assessment concluded in July 1976. This exemption was granted even though the trust had not invested the surplus income of the previous year in the prescribed manner and also had not

notified to the Income-tax Officer of such accumulations upto 31-3-1975, the end of the previous year. This resulted in an irregular exemption leading to a short levy of tax of Rs. 1,12,180. This omission was pointed out in audit (July 1977). On local verification later on it was seen that action under Section 263 of the Income-tax Act, 1961 was initiated and the Income-tax Officer directed to re-do the assessment in accordance with law (July 1978).

The audit paragraph was sent to the Ministry of Finance in August 1979; their reply is awaited (February 1980).

(iv) A charitable trust had set apart an amount of Rs. 1,37,142 out of its surplus income of the previous year relevant to the assessment year 1973-74 for the purpose of establishment and equipment of hospitals. The assessing officer allowed exemption of the amount so set apart. During the previous years relevant to the assessment years 1973-74 and 1975-76, the amounts of Rs. 72,968 and Rs. 61,988 were utilised by the institution for purposes other than those for which it was intended to be accumulated. These amounts were, however, not brought to tax by the assessing officer during the relevant assessment years. The irregular exemption in this respect resulted in under-assessment of income by Rs. 72,968 and Rs. 61,988 in the assessment years 1974-75 and 1975-76 leading to an aggregate short levy of tax of Rs. 62,286 during these years.

The paragraph was sent to the Ministry of Finance in July 1979; they have stated in December 1979 that the objection is under consideration.

52. *Dividend income*

Where the gross total income of an assessee, being the owner of any share or shares in a company, includes any income from a company by way of dividends, a deduction is allowed of an amount equal to such part of dividends attributable to the profits and gains derived by the company from industrial undertakings, or ship on which no tax is payable by the company.

In the case of an assessee-shareholder, in computing the income, deduction was allowed at 95 per cent of the dividend income instead of 31 per cent *i.e.* the amount certified by the Income-tax Officer, assessing the company. This incorrect deduction resulted in under-assessment of income of Rs. 92,295 and consequent short levy of tax of Rs. 89,320.

The Ministry of Finance have accepted the objection.

53. *Irregular computation of capital gains*

(i) Any profit or gains arising from the transfer of a capital asset is chargeable to income-tax under the head "Capital gains". The term 'transfer' includes exchange of assets also.

The capital gain is determined by deducting the cost of acquisition of the asset and of any improvements thereto, from the value of the consideration received or accruing on the transfer. Where the fair market value of the asset on the date of transfer exceeds the declared value of consideration received, by an amount of not less than fifteen per cent of the declared value, the fair market value and not the declared value is to be taken into account for determining the capital gain arising on the transfer of the capital asset. The difference between the market value and the value declared for transfer is also liable to be assessed to gift-tax.

(a) During the previous year relevant to the assessment year 1974-75, two assessee-individuals who were co-owners of an immovable property consisting of land and buildings, sold a part of the property measuring 1,766 sq. yards for a consideration of Rs. 7,28,166. Acquisition proceedings were initiated against the property by the Inspecting Assistant Commissioner of Income-tax (Acquisition) on the ground that the consideration shown in the sale deed was not the correct consideration. After the proceedings, he determined the value of the property on the date of sale as Rs. 14,12,800 at Rs. 800 per sq. yard vide his order of the 31st March, 1976. In his order, a copy of which was sent to the ward having jurisdiction over the assessees

in August 1976, the Inspecting Assistant Commissioner stated that the difference between the fair market value and the apparent consideration, amounting to Rs. 6,84,634 would attract capital gains tax liability in the hands of the transferors. However, the income-tax assessments of both the assessees were finalised in March 1977 accepting the quantum of capital gain returned by the assessees based on the stated consideration of Rs. 7,28,166 and without making use of the information already available in the order of the Inspecting Assistant Commissioner of Income-tax (Acquisition). This resulted in under-assessment of income of Rs. 2,81,560 in the hands of each of the co-owners with consequent undercharge of tax of Rs. 2,05,719 in the hands of one co-owner and Rs. 2,05,839 in the hands of the other.

The Ministry of Finance have accepted the objection in principle.

(b) Two assessee-firms which were sister concerns and were engaged in tannery business exchanged buildings owned by them in July 1972. The building of one assessee firm was valued by it at Rs. 2.30 lakhs and that of the other at Rs. 3.50 lakhs. The properties were valued by the departmental Valuation Cell at Rs. 4.86 lakhs and Rs. 4.61 lakhs at the time of exchange. In computing the capital gains, the department took into account the excess of the consideration received over the market value of the property transferred, instead of comparing the cost of acquisition, with the market value which exceeded the declared value by over 15 per cent. As a result, there was short computation of capital gains of Rs. 3.02 lakhs (fair market value of Rs. 4.61 lakhs less Rs. 1.59 lakhs being the written down value as on 1-4-1966) and consequent undercharge of tax Rs. 1,33,650 in the hands of the firms and partners in one case where the department did not work out any capital gain. In the other case, the department computed capital gain at Rs. 0.95 lakh resulting in undercharge of capital gains of Rs. 1.36 lakhs approximately (fair market value of Rs. 4.86 lakhs less the cost of acquisition being taken at Rs. 3.50 lakhs in the absence of availability of exact figures) and consequent undercharge of tax of Rs. 61,000 in the hands of the firms and partners.

There was thus total undercharge of tax of Rs. 1,94,650.

The Ministry of Finance have accepted the objection in the first case and stated that the objection in the second case is under consideration.

(c) In another case, the capital gain derived by an assessee on sale of 4,730 square yards of land in the previous year relevant to the assessment year 1973-74 was computed with reference to a sale price of Rs. 30,006 returned by the assessee. This sale price worked out to Rs. 6 approximately per square yard. It was noticed in audit that the value was too low in comparison to the fair market value of Rs. 72 per square yard adopted by the department in respect of sale of 883 square yards of land held by the same assessee in the same locality in respect of the assessment year 1975-76. The value of the latter piece of land was estimated by the department at Rs. 90 per square yard in January 1976 and allowing a deduction of 10 per cent per annum a value of Rs. 72 per square yard was arrived at as the fair market value as on the date of sale. Following the same method and allowing further deduction of 10 per cent each for two more years, the fair market value of 4,730 square yards of land assessed to capital gain tax in 1973-74 was not likely to be less than Rs. 54 per square yard. The capital gain on the sale of the first piece of land was, therefore, found to have suffered an under-assessment of Rs. 48 per square yard. This led to short computation of income by Rs. 1,36,773 with a resultant short levy of tax of Rs. 1,00,363.

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

(d) In still another case of an assessee-firm for the assessment year 1975-76 completed in April 1977, capital loss of Rs. 2,61,082 was determined on the sale of 23,117 unquoted shares of five private companies costing Rs. 18,61,790 for a sale consideration of Rs. 16,00,708. The market value of the shares as adopted in the wealth-tax assessments, however, was Rs. 22,67,411. Even adopting the value followed in the

wealth-tax assessment, it was found that the market value exceeded the sale consideration by more than 15 per cent. Hence under the law the difference between the total market value of the shares adopted in the wealth-tax assessments and the total sale consideration should have been deemed as capital gains and brought to tax. The deemed capital gain amounted to Rs. 4,05,621 as against the capital loss of Rs. 2,61,082 computed by the department resulting in excess carry forward of loss of Rs. 6,66,703.

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

(ii) Further, under the Income-tax Act, 1961, capital assets are classified as 'short-term' and 'long-term', according to the period for which they are held by an assessee. Those held for not more than sixty months (thirty six months with effect from 1-4-1978)) are termed as 'short-term' assets and others as 'long-term' assets. Capital gains derived by non-corporate assessees from sale of long-term capital assets are included in the income chargeable to income-tax, after deducting a specified percentage of the gains. The benefit of such deduction is not available when short-term capital assets are sold.

(a) Bus route permits are granted by State Governments for a maximum period of five years. On the expiry of the specified period, permits would be issued for another term (not exceeding five years) but the applications would be treated as if they were for fresh permits. Thus, by virtue of the condition of issue, a permit sold by an assessee would constitute a short-term capital asset for purposes of levy of capital gains tax, not entitled to the deduction provided in the Income-tax Act.

During the period relevant to the assessment years 1974-75 to 1976-77, five assessees sold buses owned by them along with the route permits, which had been acquired on the expiry of the permits issued to them earlier. In their income-tax assessments (finalised during October 1976 to February 1977), the department treated the capital gains arising from the sales as long-term

capital gains, on the ground that, reckoning the duration of the holding from the dates of acquisition of the original permits, they had been held for more than sixty months at the time of sale. Accordingly, from the total capital gain of Rs. 1,55,500, statutory deductions were allowed to the extent of Rs. 87,040 and the balance amount of Rs. 68,460 was charged to tax. The erroneous allowance in this regard resulted in short levy of tax of Rs. 57,664.

The Ministry of Finance have accepted the objection.

(b) Certain lands owned jointly by two assessees were acquired by an Urban Development Authority and in lieu thereof alternate lands were allotted and taken possession of on 31-3-1973. Half of the allotted lands were sold by the assessees during August 1975 for a consideration of Rs. 2,97,500.

While computing the capital gain arising out of the sale, the deduction applicable to long-term capital assets was erroneously allowed in the assessment for the assessment year 1976-77 although the land had been held by the assessees only for a period of 29 months. This resulted in short assessment of income of Rs. 34,688 each in the hands of the two assessees leading to total undercharge of tax of Rs. 53,422.

The Ministry of Finance have accepted the objection.

(iii) It has been judicially held 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 loses his exclusive right over the said assets which become the property of the firm, his right in the assets being limited to his share in money representing the value of the property of the firm.

During a check of the wealth-tax assessments of two individuals, it was noticed that the assessees had each transferred during the previous year relevant to the assessment year 1974-75 non-agricultural lands to a firm in which they were partners and the firm had credited the assessees' capital accounts with

amounts of Rs. 3,00,000 each as the value of the land. A cross check of the relevant income-tax assessments, however, revealed that the capital gains on this account treating this as a transfer had not been brought to tax by the assessing officer on the basis of the information available in wealth-tax records. The capital gain on the transfer worked to Rs. 5,88,000 and tax thereon after admissible deduction under Section 80T worked out to Rs. 2,98,000.

The paragraph was sent to the Ministry of Finance in July 1979; they have stated in December 1979 that the objection is under consideration.

(iv) Under the provisions of the Income-tax Act, 1961, tax is leviable on the sale of agricultural lands also, if such lands are situated in any area within such distance, not being more than eight kilometres, from the local limits of any municipality as the Central Government may specify by notification in the Official Gazette.

(a) During the previous year relevant to the assessment year 1974-75, a film actress sold 6.94 acres of agricultural lands in a village situated within the notified area on the outskirts of a metropolitan city, for a declared consideration of Rs. 1,51,500. In the assessment for the assessment year 1974-75 (completed in December 1976), the department omitted to consider the capital gain arising from the sale of the lands.

The quantum of under-assessment could not be worked out in the absence of information regarding the cost of acquisition of the lands. But with reference to the value of Rs. 18,262 as on 31-3-1966 declared in the assessee's wealth-tax return, the under-assessment of capital gains would be Rs. 1,33,328.

The Ministry of Finance have accepted the objection.

(b) In another case of an assessee, the Land Acquisition Officer took advance possession of a plot of land owned by the assessee on 22nd March, 1974 and the Gazette notification for the acquisition of the land was published on 26th March, 1975.

The compensation money of Rs. 3,00,150 was paid in two equal instalments of Rs. 1,50,075 each on 16th October, 1974 and 9th May, 1975 respectively.

As the transfer of land became effective with the publication of the notification on 26th March, 1975, the assessee's income under the head "Capital gains" arising out of the receipt of the compensation money of Rs. 3,00,150 was assessable to tax taking the whole capital gain as pertaining to the previous year, 1974-75. But the assessing officer split up this capital gains as pertaining to two assessment years, *viz.*, 1975-76 and 1976-77, which resulted in under-assessment of tax to the extent of Rs. 57,439 and short levy of interest of Rs. 6,383 for late filing of the return.

The paragraph was sent to the Ministry of Finance in October 1979; they have stated in January 1980 that the objection is under consideration.

(v) The Income-tax Act, 1961 further provides that capital gains arising from the transfer of a land used for agricultural purposes in the two years immediately preceding the transfer, shall not be charged to tax in the year of transfer to the extent the amount was utilised for the purchase of another land, within a period of two years, for being used for agricultural purposes.

In the case of an assessee, the capital gains arising from the transfer of an agricultural land was computed for the assessment year 1974-75, after excluding Rs. 2,77,000, being the amount utilised for the purchase of another land, with a building thereon. From the details available in the wealth-tax assessment records of the assessee for the year 1976-77, it was noticed in Audit that out of Rs. 2,77,000 deducted, only the value of the agricultural land (Rs. 1,52,000) was deductible and the balance Rs. 1,25,000 being the cost of a residential house with appurtenant land, should not have been deducted.

The Ministry of Finance have accepted the objection and have stated that the assessment in question has been revised raising an additional demand of Rs. 73,739.

54. *Mistakes in assessment of firms partners*

Under the Income-tax Act, 1961, firms are classified into registered firms and unregistered firms. A registered firm pays only a small amount of tax on its income ; the rest of its income is apportioned among the partners and included in their individual assessments. An unregistered firm pays full tax on its total income. Where at the time of completion of the assessments of partners the assessment of the firm has not been completed and the final share income of the partners is not known, the assessments of partners are to be completed by taking their share income from the firm on a provisional basis. In such cases, the assessments of the partners are to be revised later to include the final share income when the assessment of the firm is completed. For this purpose the Income-tax officers are required under instructions from the Board, to maintain 'register of cases of provisional share income' so that timely action is taken to revise the partners' assessments.

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

(i) In spite of the above it was noticed in audit that in 30 cases the assessments of partners earlier completed on provisional basis were not revised although the assessments of firms had been revised subsequently. No indication was kept in the assessment records and also in the relevant registers regarding the need to revise the partners' assessments while revising the firm's assessment. Non-revision of the partners' assessments

adopting the correct share income from the firms as a result of revision of the firms' assessments resulted in short levy of tax of Rs. 1,29,381 for the assessment years 1969-70, 1970-71 and 1972-73 to 1975-76.

(ii) In accordance with the administrative instructions issued by the Central Board of Direct Taxes in March 1973 the rectification of the provisional share income of the partners is to be made within three months from the date of receipt of the intimation of the determined share.

It was noticed that in 11 cases involving short demand of Rs. 32,149, the share incomes of the partners for the assessment years 1973-74 to 1975-76 were not revised even after the expiry of 24 to 54 months from the dates of completion of assessments in the case of the firms.

The paragraph was sent to the Ministry of Finance in October 1979. They have accepted the objection in two cases. In the remaining cases their reply is awaited (February 1980).

55. *Omission to include income of spouse/minor children*

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

In 11 cases in 5 Commissioners' charges, spread over the assessment years 1970-71 to 1977-78, such incomes of spouse/

minor children were not included in the total income of the assessees concerned resulting in tax undercharge of Rs. 3,79,187 and penalty of Rs. 39,157.

(ii) The Act, as amended from 1st April, 1976, further provides that the income arising to a minor child of an individual from the admission of the minor to the benefit of partnership in any firm is also to be included in computing the income of that individual.

In 8 cases, in 6 Commissioners' charges, such incomes of minor children for the assessment years 1976-77 and 1977-78 were not included in the total income of the assessees concerned. The omission to do so resulted in tax undercharge of Rs. 1,02,186.

The total tax undercharge on account of the above mistakes amounted to Rs. 4,81,373.

The Ministry of Finance have accepted the objection in 8 cases. In 3 cases they have stated that the share from the partnership of the wife cannot be clubbed with the individual income of the Karta in view of a decision of the Gujarat High Court on the point. Their reply is awaited in 8 cases (February 1980).

56. *Income escaping assessment*

(i) The wealth-tax return of an assessee showed that he had wealth of house property and loans advanced to private parties. However, income from these sources was not returned by the assessee in the assessment years 1971-72 to 1975-76, nor was any action taken by the assessing officer to include the income from such sources in any of his assessments. As a result, aggregate income of the Karta in view of a decision of the Gujarat High a short demand of tax of Rs. 54,800 approximately for the assessment years 1971-72 to 1975-76.

The Ministry of Finance have accepted the objection.

(ii) Under the provisions of the Income-tax Act, 1961, any sum found credited in the books of an assessee maintained for any previous year may be charged to income-tax as income of the assessee of that previous year, if the assessee offers no explanation about the nature and source of the credit or the explanation offered by him is not, in the opinion of the Income-tax Officer, satisfactory.

In the capital account of an assessee, a sum of Rs. 1,99,192 was credited as transfers from suspense account and sundry creditors, for the previous year relevant to the assessment year 1973-74. No explanation about the nature and source of this credit was available in the assessment records. As only a sum of Rs. 38,241 had been added to total income representing intangible additions in the sundry creditor's account in the assessment year 1971-72, it was pointed out in audit (January 1977) that the balance amount of Rs. 1,60,951 required to be added as income for the assessment year 1973-74. Omission to do so resulted in tax undercharge of Rs. 1,62,278.

The Ministry of Finance have accepted the objection.

(iii) Assessments of two assessees, individuals, for the assessment year 1971-72 which were completed on 28th June, 1976 included interest income on investment of Rs. 5 lakhs each with a firm. It was seen in audit (February 1979), that the assessees did not file returns of income for the assessment years 1972-73 and onwards, nor any notice under Section 139 (2) of the Income-tax Act, 1961, calling for the returns of income, was issued by the department. As a result, income of at least Rs. 48,750 in the case of one assessee and Rs. 45,000 in the case of the other representing interest on investment with a firm escaped assessment for each of the assessment years 1972-73 to 1977-78, leading to abandoning of total revenue of Rs. 1,91,800 besides penalty for failure to furnish the return of income.

The Ministry of Finance have accepted the objection.

(iv) It was noticed from a letter dated the 4th December, 1976 addressed to the assessing officer by another Income-tax

Officer that during the previous years relevant to the assessment years 1974-75 and 1975-76, an individual assessee was in receipt of commission amounting to Rs. 17,613 and Rs. 46,375 respectively from another individual. The said receipts were, however, not brought to tax either in the original assessments completed in January 1978 or in the revised assessments made in February 1978. As a result, total income of Rs. 63,988 on account of commission escaped assessment in the two assessment years 1974-75 and 1975-76 with resultant total tax undercharge of Rs. 46,931. There was also consequent short levy of interest of Rs. 3,772 for belated submission of return.

The paragraph was sent to the Ministry of Finance in July 1979 ; they have stated in December 1979 that the objection is under consideration.

57. *Non-levy of interest*

Under the provisions of the Income-tax Act, 1961, where the tax payable on current income is likely to exceed the amount of advance tax demanded by more than 33⅓ per cent, the assessee is required to file an estimate of his income and pay the amount of advance tax according to such estimate on or before the due dates prescribed for payment of advance tax instalments. Where, on making the regular assessment, the Income-tax Officer finds that such an assessee has not sent the estimate of his current income, simple interest at the rate of 12 per cent per annum is leviable from the 1st day of April next following the financial year in which the advance tax was payable upto the date of the regular assessment upon the amount by which the advance tax paid fell short of the assessed tax.

In the case of an assessee, it was noticed that demand notice for payment of advance tax of Rs. 24,307 for the assessment year 1975-76 was issued on 7th June, 1974. The demand notice was, however, returned by the assessee stating that if the correct credit of tax deducted at source for the assessment year 1971-72 were accounted for, no advance tax would be payable by him in the previous year relevant to the assessment year 1975-76. The

assessee, however, had not filed his own estimate as provided in the Act. Omission to do so led to a short levy of interest of Rs. 47,583 for the assessment year 1975-76.

The Ministry of Finance have accepted the objection.

Other topics of interest

58. *Non-completion of cancelled assessments*

The assessment of a Hindu undivided family for the assessment year 1950-51 was completed on 31st March, 1955 on total income of Rs. 16,51,275 as best judgment assessment and those for the assessment years 1967-68, 1968-69 and 1969-70 were completed as best judgment assessments on 29th March, 1972, on total incomes of Rs. 3,35,029, Rs. 1,85,987 and Rs. 79,451 respectively. The assessment for the assessment year 1950-51 was cancelled on 22nd February, 1956 and those for the assessment years 1967-68 to 1969-70 on 12th February, 1973 for making fresh assessments. It was, however, seen in Audit (December 1978) that the fresh assessments had not been made in any of these cases. As a result, total revenue of Rs. 3.78 lakhs and Rs. 6.38 lakhs has remained unassessed and unrealised over a period of twelve years and five years respectively.

The Ministry of Finance have accepted the objection.

59. *Private family trusts*

59.1 In paragraph 62 of the Audit Report, 1977-78, a few illustrative cases of under-assessments of income-tax, wealth-tax and gift-tax relating to private family trusts were pointed out.

59.2 A 'trust' is an obligation annexed to ownership of property, and arising out of a confidence reposed in and accepted by the owner, or declared and accepted by him, for the benefit of another, or of another and the owner. Trusts where the benefit is provided for the public in general are public trusts. If, however, the benefit is restricted to a specified person or persons, individually or as a class, it would be a private trust.

59.3 The essentials of a valid trust are that (i) the settled property should be vested absolutely in the trustees (vesting declaration), (ii) there should be at least one certain and existing person on the date of the creation of trust, (iii) one such person should exist besides the settlor (if the settlor takes a benefit under it), (iv) terms of the trust should be certain or capable of being ascertained and (v) time and mode of distribution of its corpus should be certain or ascertainable from the terms of the trust deed. Thus, a trust for perpetuity or in which not a single beneficiary was in existence or ascertainable, beside the settlor also if he reserves an interest for himself, on the date of creation of the trust would be *void*.

59.4 The Income-tax Act, 1961 and the Wealth-tax Act, 1957 contain provisions to check evasion of tax in the following types of cases—

(a) Income is transferred but the asset from which the income arises is not transferred. The income remains clubbable with the income of the transferer.

(b) An asset is transferred without adequate consideration to the spouse or minor child (other than married daughter) of the transferer directly or through the medium of a trust. The income and the value of the asset is aggregable with the income and net wealth of the transferer.

(c) An individual reserves a right or interest for himself in a trust created by him. The trust is treated as revocable and income and its corpus are clubbable with the income and net wealth of the settlor.

(d) An individual, his or her spouse and/or minor child (other than a married daughter) are partners in a partnership firm. The income of the spouse or minor child is clubbed with the income of the other spouse or with the income of the parent. This provision does not apply if the spouse and minor child are beneficiaries in a trust and the trustee is a partner of the individual creating the trust.

(e) It was judicially held that the word 'child' does not include a grandchild. The provisions in the Wealth-tax Act and Income-tax Act were amended by the Taxation Laws (Amendment) Act, 1975 with effect from 1976-77 to provide that assets transferred without adequate consideration to grandchildren (also daughter-in-law) and income arising from such assets shall be clubbable with the net wealth and income of the transferer. Such clubbing is not to be made if the transfer to the grandchildren or daughter-in-law is through the medium of a trust, and

(f) If a trust is void *i.e.*, vesting of the settled property in the trustees does not take place, the income and corpus of the trust shall remain clubbable with the income and wealth of the settlor.

59.5 These Acts also provide for the manner of assessment of private family trusts. The income and assets of a private trust, where the shares of its beneficiaries are determinate and known are aggregable with their separate income and net wealth. Where the shares are unknown or indeterminate, the assessments, for the assessment years 1971-72 and onwards, are made in the hands of the trustees at the prescribed flat rates or at the schedule rates of tax, whichever is more beneficial to revenue. These flat rates were introduced with effect from the assessment year 1971-72, through an amendment.

59.6 While introducing the aforesaid amendment to section 164(1) of the Income-tax Act, 1961 and section 21(4) of the Wealth-tax Act, 1957 for application of minimum flat rates in the case of discretionary private trusts, the then Prime Minister and Finance Minister had stated :—

> "One of the major devices leading to tax evasion and avoidance is the creation of private trusts. At present the discretionary trusts are taxed on income and wealth at the rate applicable to individuals. These lower rates lead to the proliferation of such trusts. It is proposed that in future the discretionary trusts could be taxed at the flat rates of 65 per cent

on their income and 1.50 per cent on their wealth or at the rates applicable in the cases of individuals, whichever is higher."

59.7 During the course of a review of the assessments of private family trusts in some of the charges during 1977-78 it was seen that creation of a large number of such trusts with permutations and combinations of beneficiaries from amongst the kith and kin is a very common practice among large income assessees and family groups. A few examples of such multiplicity of trusts are given below :—

(i) Test check showed that ten members of a big industrial group in Tamil Nadu created 77 private family trusts upto the assessment year 1976-77. These trusts were for 18 years from the date of creation but could be foreclosed at the discretion of the trustees or if income-beneficiaries in a trust were reduced to one. The trustees had full discretion in the application of income and distribution of the corpus of these trusts. On a test check by Audit, it was noticed that tax advantage of Rs. 41.90 lakhs had resulted to the group upto the assessment year 1976-77 as against the gift-tax paid of Rs. 23.23 lakhs.

Further, 58 of these trusts had been created after the introduction of the aforesaid amendment of law raising the rates of tax.

Instances in this group were also noticed of cross trusts created by brothers for each others' sons, which being 'connected transfers' required to be assessed in the hands of the settlors. They were, however, incorrectly assessed separately.

(ii) In a test check by Receipt Audit in a Gujarat charge in 1978, it was noticed that a family group had set up 136 private family trusts upto 31st March 1978 which were assessed in one ward, out of which 124 were covered by the test check. They were created mostly by gifts of shares in the companies of the group and cash in some cases. The aggregate value of the initial corpus of these trusts was Rs. 82.51 lakhs. The book value of the final corpus, as on 31st March 1976, was Rs. 430.75 lakhs

as per the balance-sheets of the trusts (shares in companies Rs. 122.29 lakhs, interest in partnership firms of book value of Rs. 211.46 lakhs, advances to beneficiaries, bearing interest, Rs. 39.05 lakhs and others Rs. 57.95 lakhs). In 87 of these trusts created up to February, 1977, there were 74 beneficiaries from out of the members of the family and 95 from outside the family in different permutations and combinations. The outsiders were only income-beneficiaries, the corpus having been settled upon the family members. Twenty-seven beneficiaries appeared in 3 to 9 trusts. A few persons appeared as beneficiaries in as many as 14 trusts.

(iii) Similar test check in Bombay charges showed that members of another big industrial group had created 128 trusts up to February, 1977 by settling unquoted equity shares in limited companies (controlled by the group), cash, etc. worth over Rs. 2 crores for the benefit of 51 members of the family, in different permutations and combinations, including cross-benefits to the members *e.g.,* settlor of one trust was a beneficiary in another trust. The present value of the properties held by all these trusts was about Rs. 6 crores. The maximum number of trusts in which a person appeared as beneficiary was 20.

59.8 *Void trusts*

Instances were also noticed in test check by Audit where the trusts created for the benefit of family members failed as they violated the rule against perpetuity or the vesting declaration was not effective or the only beneficiary of the trust was an unborn or unknown person as on the date of the creation of such trusts but the benefits of tax concessions were nevertheless allowed.

(i) In 32 trusts created by 23 settlors beneficiaries were persons who were not born or were uncertain persons on the date of creation of the respective trust. The value of corpus held by these trusts on 31st March 1976 (or a date nearest thereto) was Rs. 86.98 lakhs. For want of details available in the wards concerned, tax effect could not be computed.

(ii) Gift of movable and immovable properties, out of the common property of a Hindu family, can be made only for certain limited purposes. Such property cannot be settled to change the line of succession sanctioned by Hindu Law. The trusts which are violative of these principles of Hindu law are *ab initio void.*

In 15 cases, the *kartas* of Hindu undivided families had transferred movable and immovable properties, comprising the common property of these families, to trusts for their male and female relatives. For reasons already stated, income and corpus in these cases would remain clubbable with the income and net wealth of the Hindu undivided family. The value of the assets held by these trusts was Rs. 86.64 lakhs. For want of details in the wards concerned, the additional tax effect of aggregation of income and wealth of these trusts with respective income and wealth of the respective family could not be worked out in audit.

(iii) An industrial group in Tamil Nadu set up, upto February, 1977, 15 trusts with a common purpose, *viz.*, for the discharge of the debts owed by the settlors of these trusts to a company owned by the family. Settlors themselves were, thus, the only beneficiaries till the discharge of the debts (others had only a contingent interest) and this would make these trusts revocable under the provisions of the Income-tax Act, 1961 with the result that the income and wealth of these trusts remained clubbable with the income and wealth of the settlors. Such clubbing had not been done in direct taxes assessments. Had this clubbing been done, there would have been an additional income-tax demand of Rs. 4.20 lakhs for the assessment years 1969-70 to 1973-74. Wealth-tax effect of non-aggregation of the assets valuing Rs. 33.67 lakhs could not be computed for want of details.

The paragraph was sent to the Ministry of Finance on 6th November, 1979; they have stated (December, 1979) that the audit objection is under their consideration.

(iv) A minor child in an industrial family group of Tamil Nadu purported to make gifts, in the period relevant to the assessment years 1971-72 to 1974-75, to as many as ten private family trusts by transfer of 15,000 unquoted equity shares in a company controlled by the family. The value of these transfers was Rs. 16,59,430. As a minor has no capacity to contract and as the transfers were without consideration *i.e.* not in discharge of any antecedent and enforceable obligation of the minor, even the execution of the transfers by the guardian of the minor was not for the benefit of the minor. Consequently, all these gifts were void and the income from and the value of these gifts were to be assessed in the hands of the settlor. The undercharge of tax, resulting from omission to do so was of Rs. 4,68,281 (Rs. 1,49,985 as income-tax and Rs. 3,18,296 as wealth-tax) upto the end of the assessment year 1976-77.

The Ministry of Finance have stated that the gifts were only voidable and when the settlor attained majority he retified these gifts. This view is not correct as void transfers could not have been validated by ratification.

(v) An individual created a private discretionary trust on 23rd March 1968 and placed certain equity shares at the disposal of the trustees for the benefit of the wife and unborn children of his grandson. The date of distribution was declared as the date when the youngest of such children attained the age of 18 years. As such a youngest child was an uncertain person, being unborn on the date of creation of the trust and one in a continuing class of unborn persons, the trust was void both for perpetuity and uncertainty. Consequently, the income and corpus of the trust were assessable in the hands of the settlor. This was not done. Tax effect could not be ascertained for want of details in the assessment records.

Even in the income-tax assessment of this trust in the hands of the trustees for the assessment years 1973-74 and 1975-76, sums of Rs. 22,000 and Rs. 20,000, paid by the trustees at their discretion to cerain beneficiaries were incorrecly deducted from

the income of the trust. This incorrect deduction led to undercharge of tax of Rs. 27,300.

The Ministry of Finance have stated (January 1980) that the audit objection is under consideration.

(vi) In a private discretionary trust, created by an individual on 23rd March 1973 by transferring Rs. 1,000 and 960 unquoted equity shares in one of the companies controlled by his family, the settlor reserved an interest as an income and corpus beneficiary. Consequently, its income and wealth were aggregable with the income and net wealth of the settlor under the provisions of the relevant Acts. The trust was, however, assessed separately both for income-tax and wealth-tax. The omission to aggregate the income and wealth of the trust with the income and net wealth of the settlor led to undercharge of income-tax of Rs. 21,594 and of wealth-tax of Rs. 27,215 upto the assessment year 1976-77.

The Ministry of Finance have stated (January 1980) that the audit objection is under consideration.

(vii) A big family group engaged in the production, distribution and exhibition of cinematograph films and having interest in a chain of cinema houses in Bombay created six private discretionary trusts for members of the family. These trusts were worded in such a way that, even when the shares of the beneficiaries in the income and wealth of the trusts were determinate, the clubbing provisions of section 64(1) of the Income-tax Act and section 4 of the Wealth-tax Act, 1957 could not be applied. All these trust deeds were similar in nature. A test check of one of these trusts showed that an individual belonging to this group created a private discretionary trust on 11th February 1965 for the benefit of her brothers' sons, their wives and children for a period of 18 years. The trustees were given power *inter alia* to invest the trust fund in any business (including the business for production, distribution and exhibition of cinematograph films) and to carry on the business with the trust fund. No provision

was, however, made in the trust deed for the incidence of losses, if they arose over and above the accumulations made in the trust fund. As the trustees were indemnified against any losses by the terms of the deed and as the separate property of the beneficiaries could not have been made liable for such losses of the trust, a provision in this regard was necessary for making the trust definite and certain under section 6 of the Indian Trust Act. The trust was, thus, *void* for uncertainty. Consequently, its income and corpus was aggregable with the income and net wealth of the settlor. No aggregation was however, done for any of the assessment years upto the assessment year 1974-75. Tax effect could not be worked out in the absence of necessary details available in the assessment records of the trust.

The Ministry of Finance have stated (January 1980) that the audit objection is under consideration.

59.9 *Omission to apply clubbing provisions.*

(i) In the case of an individual, 'income from house property' and income from 'other sources' derived by him through a trust, of which the assessee was the trustee as well as the sole beneficiary, were aggregated with his other individual income and assessed in his assessment for the assessment year 1972-73. But a separate assessment in respect of the net taxable 'long term capital gains' of Rs. 2,59,155 from transfer of land and buildings comprising the trust fund was made for the same assessment year 1972-73 in the hands of the trustees and tax of Rs. 1,68,450 was levied thereon at the rate of sixty-five per cent. As the assessee had been the sole beneficiary in both the income and the corpus of the trust from 28th April 1968 since the other beneficiary, his brother, had died and, as the law makes no distinction between capital gains and other income in the matter of their taxability in the case of trusts and their beneficiaries, net taxable long term capital gain derived by the trust was also aggregable with the individual income of the sole beneficiary. The omission to aggregate the incomes led to undercharge of income-tax of Rs. 84,873 for the assessment year 1972-73.

The audit paragraph was sent to the Ministry of Finance in July 1979; in December 1979 the Ministry of Finance have stated that the audit objection is under consideration.

(ii) A trust was created in November 1971 by the ruler of an erstwhile state by setting apart a sum of Rs. 6 lakhs for the benefit of his wife. The income from the trust for the assessment year 1973-74 was determined at Rs. 58,400 which was assessed separately in the hands of the trustees at the rate of 65 per cent instead of charging the tax by aggregating the income of the trust with the income of the settlor. The corpus of the trust was also not clubbed with the net wealth of the settlor. Income-tax and wealth-tax short levied could not be determined for want of necessary details in the assessment records.

The Ministry of Finance have stated in January 1980 that the audit objection is under consideration.

59.10 *Incorrect application of rates.*

In a number of cases of discretionary private family trusts, where the shares of the beneficiaries were not determinate and known, omission to apply the minimum rates of 65 per cent and 1½ per cent respectively in income-tax and wealth-tax assessments were noticed :—

(i) A family group created five private family trusts in April 1954 vesting in them a number of immovable properties in Calcutta for the benefit of their personal deities. The trust deed provided that the *shebaits* appointed for the service of the deities were entitled to occupy portions of the trust properties, as might be necessary for their residence along with their family members and were also entitled to receive the offerings. As the deities, being artificial persons, were dependent upon the *shebaits* and as *shebaits* had discretion in the application and use of the income and corpus of these trusts, the trusts were of discretionary nature and the shares of the beneficiaries

in them were indeterminate. These trusts were, thus, chargeable to income-tax and wealth-tax at the minimum rates of 65 per cent and 1½ per cent respectively for the various assessment years between 1971-72 and 1976-77. It was noticed, however, that the rates of tax charged were the lower rates given in the Schedule to the relevant Act. Besides,inadmissible exemption was allowed in respect of bank deposits, income from securities, interest, etc. in the cases of some of these trusts. Further, in the wealth-tax assessments of two of these five trusts, immovable property valued at Rs. 39,64,500, in the aggregate, escaped assessment in the assessment years 1967-68 to 1975-76. The combined effect of these mistakes was undercharge of income-tax of Rs. 1,38,998 and wealth-tax of Rs. 74,341 for all these assessment years.

The Ministry of Finance have stated in January 1980 that the audit objection is under consideration.

(ii) In one case of such a private discretionary trust, tax on its income was charged as if it were the income of an 'association of persons', although levying of tax at the minimum rate of sixty-five per cent of total income was more beneficial to the revenue. Omission to levy tax at the correct rate resulted in a short levy of tax of Rs. 92,224 for the assessment years 1971-72 to 1975-76. The omission was pointed out to the department in February 1979 but its final reply is awaited (March 1980).

The corpus of the trust was also liable to be assessed to wealth-tax as a discretionary trust. No wealth-tax was, however, levied. The matter of non-levy of wealth-tax for the assessment years 1971-72 to 1974-75 was pointed out to the department by Audit in January 1977. The Ministry of Finance intimated in April 1979 that the return for the assessment year 1971-72 had been filed by the trustees on 29-7-1971. The assessment was, however, made in March 1979. In respect of the assessment years 1972-73 to 1974-75, notices under section 17 of the Wealth-tax Act were stated to have been served on the

trustees on 14-2-1976, but duplicate returns received on 21-5-1979 were kept on the assessment records in which it was mentioned that the original returns had been filed on 15-5-1978. The avoidable delay in wealth-tax assessments for the assessment years 1971-72 to 1974-75, thus, resulted in avoidable postponement of demand of tax of Rs. 1,04,029 (approximately).

Further, no gift-tax had been levied on the original and subsequent donations to the trust. These gift-tax assessments had become time-barred when audit was done in January 1977.

59.11 *Other cases of escapement and under-assessment of tax.*

(i) In the wealth-tax assessments of a private family trust created on 15-5-1942 for 'regular worship of the settlors' deity and for helping the poor and destitutes in the *aggarwala* community, the Wealth-tax Officer determined that the trust was a discretionary trust assessable as an 'association of persons' for the assessment year 1957-58 and assessed its net wealth as Rs. 17,61,586 chargeable to wealth-tax. On appeal taken by the trustees, the Appellate Assistant Commissioner on 24-5-1959 held that 'association of persons' was outside the scope of levy of wealth-tax. He further held that though the properties were dedicated to the deity, the deity, being an invisible person was not their owner but was dependent upon the spending of the income at the discretion of the trustees, who were the legal owners of the properties. These orders of the Appellate Assistant Commissioner were accepted by the department. Thus, though the trustees had been found to be not liable to wealth-tax, they filed wealth-tax returns for the assessment years 1958-59 to 1972-73 which were closed by the Wealth-tax Officer as 'not assessable' on 10-10-1975 on the basis of the aforesaid appellate decision. This decision was not then relevant to these latter assessments, having regard to (i) the decision of the Supreme Court of November 1972 that the trustees of such discretionery trusts were liable to wealth-tax as 'body of individuals' and (ii) the amendment to the relevant section of the Wealth-tax Act, 1957. On this being pointed out in audit (August 1977) that the trust was liable to wealth-tax

for all the assessment years from 1958-59 to 1972-73 as a body of individuals at the minimum rate of 1½ per cent or the schedule rates of tax, whichever are higher, the Commissioner of Wealth-tax set aside all these assessments under section 25(2) of the Wealth-tax Act, 1957 to be re-done under the law. Report about completion of these assessments and levy of escaped tax is awaited (February 1980).

The Wealth-tax Officer had, however, levied tax for the assessment year 1973-74. He could have re-opened the assessments for 1958-59 to 1972-73 at that time also. This was not done.

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

(ii) During the previous year relevant to the assessment year 1974-75, eight discretionary private trusts of a big industrial family group transferred their investments in the shares of three family companies to the members or concerns of the group. These shares formed part of the corpus of the respective trust. Though the shares in the first two companies were transferred at the rate of Rs. 1,800 (Rs. 2,932 in one case) and Rs. 1,404 per share, the department was of the view that the transfers were made at rates far below their fair market value on the day of transfer and adopted the rates of Rs. 7,730 and Rs. 3,650 per share as their fair market value respectively for the levy of capital gains tax involved in the transfer. Further, even in the case of the shares in the third company, the fair market value of the shares, on the day of transfer, would be Rs. 219 per share approximately as against the declared consideration of Rs. 122 per share. However, in none of these cases action had been taken till the date of audit (October 1978) to bring to tax the excess of fair market value of the shares over the declared consideration. Thus, a deemed gift of Rs. 23,10,928 escaped assessment resulting in non-levy of gift-tax of Rs. 4,21,789.

The Ministry of Finance have stated that in one of these cases the Appellate Tribunal have held that no transfer was

involved in the transaction and capital gains tax was not leviable and that Commissioner (Appeals) following this decision has deleted capital gains from chargeable income in three other cases. In the view of Audit, the appellate decision has been incorrectly accepted by the Department.

(iii) The 'will' left by a deceased person provided that a hotel business with all its assets and liabilities should be held by the trustees under the will for the benefit of all his sons equally subject to payment of annuity of Rs. 84,000 per annum to each of his two wives and a charitable trust. In the assessment of the trust for the assessment years 1972-73 and 1973-74, completed in November 1974 and January 1976, the annuity of Rs. 1,68,000 for the two years debited to the trading and profit and loss account of the assessee was allowed as business expenditure in the process of computation of income from business. As the payment of annuity was not an expenditure laid out wholly and exclusively for the business and as it was only a distribution of the income under the will, the deduction so allowed was incorrect. The consequential short levy of tax was of Rs. 83,587 for the two assessment years 1972-73 and 1973-74. Similar incorrect allowance had also been made for the earlier two assessment years 1969-70 and 1971-72.

While not accepting the audit objection, the Ministry of Finance have taken the view that part of the income payable to the widows of the settlor was deductible as a diversion of income by an overriding title. In the view of Audit, however, the sums payable to the widows are merely application of the income of the trust as the widows derive title as beneficiaries from the same testamentary deed.

59.12 This review was sent to the Ministry of Finance on 4-11-1979 ; their reply is awaited (March 1980).

CHAPTER IV

OTHER DIRECT TAXES

A. Wealth-tax

60. The actual receipts under wealth-tax in the financial years 1974-75 to 1978-79 compared with the budget estimates in these years, thus :—

Year	Budget estimates	Actuals
	(Rupees in crores)	
1974-75	40	39.23
1975-76	43	53.73
1976-77	52	60.44
1977-78	55	48.46
1978-79	55	55.41 (provisional)

The arrears of demand and cases pending assessment as on 31-3-1979 were Rs. 184.08 crores and 3,31,561 respectively.

61. During the test audit of assessments made under the Wealth-tax Act, 1957, conducted during the period from 1st April, 1978 to 31st March, 1979, the following types of mistakes resulting in under-assessment of tax were noticed :—

(i) Mistakes in calculation of tax.

(ii) Wealth escaping assessment.

(iii) Incorrect valuation of assets.

(iv) Non-levy and short levy of additional wealth-tax.

(v) Mistakes in computation of net wealth.

(vi) Irregular/excessive exemptions.

(vii) Incorrect levy of penalty.

A few cases illustrating such mistakes are given in the following paragraphs.

62. *Mistakes in calculation of tax*

In test check by Audit, mistakes in calculation of tax resulting from arithmetical errors, application of incorrect rates, etc. continued to be noticed in various wards.

Application of incorrect rates

(i) In paragraph 61.2(i) and 61.3 of the Audit Report, 1977-78, instances of a large number of under-assessments resulting from omission to apply the higher rates prescribed in the schedule to the Income-tax Act and Wealth-tax Act in the cases of specified Hindu undivided families *i.e.* families which had at least one member with assessable income and wealth were pointed out and it was stated *inter alia* that the Central Board of Direct Taxes had ordered a review of cases of such specified Hindu undivided families for locating any other cases of undercharge of income-tax and wealth-tax. Results of that review are still awaited(March, 1980).

Test check by Audit revealed numerous other cases of undercharge of wealth-tax in the cases of such specified Hindu undivided families. In 25 cases in 20 Commissioners' charges involving tax effect of over Rs. 10,000, the undercharge of tax was above Rs. 25,000 in 3 cases, between Rs. 15,000 to 25,000 in 11 cases and above Rs. 10,000 in the remaining 11 cases in the various assessment years between 1974-75 and 1976-77. The cumulative effect of mistakes in these cases was short levy of tax aggregating Rs. 4,22,668.

The Ministry of Finance have accepted the audit objection in 23 cases.

(ii) In the Audit Reports for the previous years, cases have continuously been commented upon where undercharge of tax resulted from application of rates of one year to the assessments made for other assessment years. Such cases continued to be

noticed in test check by Audit. A few illustrative cases are given below :—

(a) The tax on net wealth of Rs. 9,04,929 and Rs. 9,44,099 for the assessment years 1974-75 and 1975-76 respectively works out to Rs. 12,841 and Rs. 17,789 against which tax of Rs. 6,049 and Rs. 13,882 was levied. The mistake resulting from the incorrect application of rates led to short levy of tax of Rs. 10,699 for the two assessment years.

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

(b) In 23 other cases in 14 Commissioners' charges, the application of rates of tax of earlier assessment years instead of the rates of tax for the relevant assessment year led to undercharge of total tax of Rs. 1,27,936 for the various assessment years between 1966-67 and 1977-78.

The Ministry of Finance have accepted the audit objection in all the cases.

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

The need for a proper co-ordination among the assessment records pertaining to different direct taxes to ensure an overall improvement in the administration of these taxes has been frequently emphasized by the Public Accounts Committee. The Committee has also laid stress on a critical examination of income-tax cases with a view to finding out cases of evasion of wealth-tax. Though such cases of lack of correlation have continuously been pointed out in the previous Audit Reports and the Central Board of Direct Taxes have also issued instructions on 10-1-1973, 15-11-1973 and 11-4-1979 for carrying out such correlation, instances of undercharge of tax resulting from omission to utilise information already available in the assessment records of certain direct taxes for levy of wealth-tax continue to be noticed. A few instances are given below :—

(i) Two assessees were assessed to wealth-tax for the assessment year 1971-72 on a total wealth of Rs. 5,00,000, and

Rs. 5,56,000 respectively which included investment of Rs. 5,00,000 each with a private firm. The assessees did not file any return of wealth for the assessment years 1972-73 to 1977-78. Although the fact of non-submission of returns of wealth by the assessees was brought to the notice of the department by Audit in October, 1977, it was seen in audit (February, 1979) that the notices calling for the returns of wealth had not been issued by the Wealth-tax Officer to the assessees even till then. The wealth of at least Rs. 5,00,000, thus, escaped assessment in the case of each of the assessees for the assessment years 1972-73 to 1977-78, leading to non-levy of total tax of Rs. 56,926 in these two cases.

The Ministry of Finance have accepted the audit objection and stated that assessment proceedings have been initiated in both the cases.

(ii) In a wealth-tax case, assessments for the years 1971-72 and 1972-73 were made on net wealth of Rs. 6,07,610 and Rs. 5,42,900 on the basis of original wealth-tax returns, although the assessee had already filed revised wealth-tax returns for net wealth of Rs. 11,75,040 and Rs. 11,75,490 respectively. Omission to assess net wealth as per the revised returns resulted in under-assessment of wealth of Rs. 5,67,430 and Rs. 6,32,590 with an aggregate short levy of wealth-tax of Rs. 27,470 for the assessment years 1971-72 and 1972-73.

The Ministry of Finance have accepted the audit objection.

(iii) A Commissioner of Wealth-tax informed (January, 1976) the assessing officer of the disclosure of concealed income (Rs. 1,25,000) by a firm under Section 14(1) of the Voluntary Disclosure of Income and Wealth Act, 1976 relating to the assessment year 1966-67 onwards. The assessing officer did not re-open the wealth-tax assessment of a partner of the firm (an assessee in the same ward) for adding his share in the net assets of the firm to his net wealth for the years 1966-67 to 1975-76. Even the pendency of the re-assessments had not been recorded in any of the prescribed registers. This failure to re-open assessments resulted in the non-levy of tax of Rs. 18,480.

The Ministry of Finance have accepted the audit objection. They have also stated that the assessments for the assessment years 1967-68 to 1968-69 had not been re-opened and as such no remedial action is possible now and that the rectification of the assessment for the assessment year 1966-67 had become time-barred at the time of audit. Result of the remedial action taken for the other assessment years is awaited (March, 1980).

64. *Incorrect valuation of partners' share interest in partnership firms.*

Four individual assessees were partners of two registered firms on the valuation dates relevant to the assessment years 1967-68 to 1971-72. In working out the share interest of each partner in the two firms for levy of wealth-tax for the assessment years 1967-68 to 1969-70 and 1971-72, the department did not adjust the value of assets of the firm to their market value even when it exceeded their book value by more than 20 per cent as prescribed in the Wealth-tax Rules, 1957. While adopting even the book values, the department took into consideration the balances of capital accounts of the partners together with their shares in the development rebate reserve and, in so doing, incorrectly deducted therefrom proportionate amount of depreciation on assets of the two firms when depreciation on such assets had already been debited to their profit and loss accounts in the respective account years. As the capital balances and the development rebate reserve represented the net assets of the firms, further reduction towards depreciation totalling Rs. 10,27,776 in the hands of each partner for the assessment years 1967-68 to 1969-70 and 1971-72 was not correct. The incorrect deduction for depreciation led to under-assessment of wealth aggregating Rs. 41,11,064 with consequent short levy of tax amounting to Rs. 51,360 in the hands of the four partners for the four assessment years. The under-assessment would be more if the valuation of the share interest of the partners was made on the basis of market value of the assets of the firms as required under the wealth-tax rules.

(b) Three individual assessees held unquoted equity shares in three different companies including investment companies on the valuation dates relevant to the assessment years 1971-72 to 1974-75. The department, while determining the value of the said unquoted shares of the assessees for these assessment years, adopted the value of shares held in trading companies at the average of the capitalised value of their average yield and their break-up value instead of at their break-up value under the relevant wealth-tax rule. Further, the value of shares held in investment companies was determined at the average of their break-up value and value on capitalisation of their average yield even when their break-up value itself was higher. The erroneous computation of the value of shares in each case led to under-valuation of assets with consequent undercharge of tax aggregating Rs. 68,389 for these assessees for the four assessment years.

The Ministry of Finance have stated (December, 1979) that the final action on the review of Board's instructions of October, 1967 may be awaited.

(c) Undervaluation of unquoted equity shares held by six other assessees in three Commissioners' charges, similarly caused by incorrect computation of their break-up value on making incorrect allowance for liabilities, depreciation, etc., was noticed in test check by Audit. The under-assessment of tax involved in these cases was Rs. 83,373 for the various assessment years between 1973-74 and 1977-78.

The audit paragraphs were sent to the Ministry of Finance in July, 1979 to September, 1979; their replies are awaited (March, 1980).

66. *Incorrect valuation of other assets*

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

With a view to checking leakage of tax by undervaluation of assets, a departmental Valuation Cell was set up in 1969 for valuation in cases referred to it by the assessing officer. The valuation done by the departmental Valuation Officer is binding on the Wealth-tax Officer but where it is *prima facie* incorrect, the Commissioner can set aside the assessment under his powers of revision. The Central Board of Direct Taxes have issued repeated instructions, the latest being on 27th April, 1979, laying down guidelines for cases of house properties which were required to be referred to the Valuation Officers of the department for valuation and emphasising that there should be no omissions in making such references. Cases of non-reference of valuation of properties required to be referred to departmental Valuation Cell continue to be noticed in Audit generally and in particular in the cosmopolitan cities like Bombay, Calcutta, Madras, Ahmedabad, etc. A number of such omissions have been reported below and in paragraph 67(iv) of this report.

(ii) In a cosmopolitan city, the value of one-half share in a building which belonged to an assessee (the other half was owned by his sister) was estimated by an approved valuer as Rs. 30,00,000 as on 19th August, 1968. Instead of returning his share in the value of the building as per this report, the assessee returned the value as per his books, by adding an *ad hoc* appreciation in the value. The department accepted the value as returned by the assessee and assessed the value of the property accordingly. This case was not referred to the departmental Valuation Officer for valuation as required in the Board's instructions of December, 1971.

While computing the wealth-tax chargeable, the department did not also charge additional wealth-tax.

The above omissions led to a total under-assessment of wealth of Rs. 23,86,400 for the assessment years 1970-71 to 1974-75 and an aggregate short levy of wealth-tax of Rs. 49,990 and of additional wealth-tax of Rs. 1,06,900, thus, totalling Rs. 1,56,890 for these five assessment years.

The Ministry of Finance have accepted the audit objection.

(iii) An individual having 2/10th share in a big house property in a posh locality in Bombay, returned the value of his share in it as Rs. 24,000 for the assessment years 1973-74 and 1974-75 in his wealth-tax returns filed on 23rd July, 1974 and 1st October, 1974. This property had, however, been sold for Rs. 25 lakhs by the co-owners on 20th February 1974 to a builder who in turn had sold it to the Unit Trust of India for Rs. 28 lakhs on 22nd February, 1974. The share of the assessee was thus, Rs. 5,60,000 as against the returned value of Rs. 24,000. Even though the value of the property at the time of sale was found to be above Rs. 5 lakhs, making it obligatory on the department under Board's instructions of December, 1971 to refer the asset to the departmental Valuation Cell for valuation, no such reference was made. Computed at the value of Rs. 5,60,000, the wealth under-assessed in this case was Rs. 10,72,000, in the aggregate, and wealth-tax under-assessed was of Rs. 17,920 for the assessment years 1973-74 and 1974-75. Past assessments would also have to be re-opened to consider the correct value of the share of the assessee in the property.

2. The Ministry of Finance have accepted the audit objection. Further report of rectification of assessments in this case and in the case of other co-owners having taxable wealth is awaited (March 1980).

(iv) A Hindu undivided family owned six urban immovable properties, including two residential-*cum*-commercial houses valuing more than Rs. 2 lakhs each. It was noticed in audit that the value of these properties for the assessment years 1971-72 to 1975-76 was determined at a consolidated figure of Rs. 5,60,438 for the assessment year 1971-72 and *ad hoc* additions were made in the assessments for the subsequent assessment years raising the value of these properties to Rs. 5,91,320 in the assessment year 1975-76. The additions so made had no relation to the market trends in that period. The valuation of the two properties had not been referred to the Valuation Cell in compliance with the

instructions of the Board of December, 1971. On these omissions and the omission to levy correct rates of tax being pointed out in audit, the mistakes were accepted by the department and, on the basis of the valuation of the two properties made by the Valuation Cell, the assessments for the assessment years 1969-70 to 1975-76 were revised in March 1978 and March 1979 resulting in increase in the net wealth for these years by Rs. 11.15 lakhs in the aggregate and creation of additional demand of tax totalling Rs. 67,938, including additional wealth-tax of Rs. 48,843.

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

67. *Non-levy/short levy of additional wealth-tax*

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

While considering paragraph 71 of the Audit Report, 1970-71, in which undercharge of additional wealth-tax of Rs. 1.36 lakhs in 67 cases was pointed out, the Public Accounts Committee in paragraph 2.60 of their 88th Report (Fifth Lok Sabha), desired a review of wealth-tax cases. Accordingly, the Board conducted a review between 1972 and 1975 in which omission to levy additional wealth-tax amounting to Rs. 3.25 lakhs was detected in 105 cases. However, as cases of non-levy/short levy of additional wealth-tax continued to be noticed and reported in the subsequent Audit Reports that review did not appear to be complete.

The Board of Direct Taxes was, therefore, requested in October, 1979 to have a complete review conducted. They have ordered in February 1980 for a fresh review. Results of

this review are awaited (March 1980). Some of the cases where such omissions have been noticed further are given below.

(i) In the wealth-tax assessments for the assessment years 1965-66 to 1973-74, completed in March 1978, although the net assessed wealth, comprising the estate of a deceased person included the value of urban assets amounting to Rs. 24,12,250 the levy of additional wealth-tax on the value of such urban properties was omitted. The omission resulted in non-levy of aggregate additional wealth-tax of Rs. 4,49,770 for all these assessment years.

The Ministry of Finance have stated that action would be taken alongwith the rectification on decision of the Appellate Tribunal in appeal made by the assessee.

(ii) The net wealth of an individual for the assessment years 1965-66 to 1976-77, assessed in October, 1977 included urban immovable properties on which additional wealth-tax, was leviable to the extent of Rs. 3,10,863, in the aggregate, for all these assessment years. The omission to levy such tax resulted in non-levy of total additional wealth-tax of Rs. 3,10,863.

The Ministry of Finance have accepted the audit objection and stated that demand for additional tax raised is of Rs. 3,10,863.

(iii) The net wealth of an individual for the assessment years 1971-72 to 1975-76 included urban immovable properties valued at Rs. 10,51,090, Rs. 10,55,090, Rs. 10,59,990, Rs. 9,50,090 and Rs. 7,12,090 on which additional wealth-tax was leviable to the extent of Rs. 26,276, Rs. 28,856, Rs. 29,169, Rs. 22,505 and Rs. 10,605 respectively. The department, however, did not levy the tax. The omission resulted in a total short levy of additional wealth-tax of Rs. 1,17,411.

The Ministry of Finance have accepted the audit objection and stated that additional tax of Rs. 1,43,700 has been collected.

(iv) The wealth-tax assessments of an individual for the assessment years 1965-66 to 1976-77 were completed in July

and August 1977. The net wealth included value of urban immovable properties exceeding the prescribed limit for levy of additional wealth-tax for each of the assessment years. The value of the immovable properties was determined by the departmental Valuer in August 1969 for the assessment years 1959-60 to 1969-70. The same valuation was followed in the assessments for the assessment years 1970-71 to 1976-77, though the properties were required to be revalued at normal intervals of three years by reference to the departmental Valuation Officer. Even adopting the value as determined by the departmental Valuer for all these assessment years, the assessee was liable to pay additional wealth-tax of Rs. 1,08,576.

The Ministry of Finance have accepted the audit objection and stated that the additional demand for tax of Rs. 1,08,576 has been raised.

(v) In the wealth-tax assessments of an individual for the assessment years 1971-72 to 1974-75, completed in March, 1978, levy of additional wealth-tax on urban properties valued at Rs. 9.81 lakhs, Rs. 8.80 lakhs, Rs. 7.18 lakhs and Rs. 6.45 lakhs respectively comprising the net wealth was not considered. This omission resulted in under-assessment of tax of Rs. 58,300.

The Ministry of Finance have accepted the audit objection.

(vi) In 17 other cases, involving tax effect of over Rs. 10,000 in 14 Commissioners' charges, non-levy of additional wealth-tax of Rs. 5,59,621 in the aggregate, for the various assessment years between 1965-66 and 1976-77 was noticed in test check by Audit.

The Ministry of Finance have accepted the audit objection in 15 cases.

68. *Incorrect computation of net wealth*

(i) A Hindu undivided family was a partner in a firm, sharing fifty per cent of its profits. It was claimed on behalf of the family that, on account of a demand for separation made by

widowed mother of the *karta* in her letter of October, 1963, a partition of its properties took place between the son and the widowed mother in November, 1963. It was also claimed that under the partition deed, the widowed mother received Rs. 50,000 and also the membership of the firm with 50 per cent share in profits. The partition was accepted by the assessing officer. In the previous years relevant to the assessment years 1969-70 and 1970-71, the mother also made gifts, out of the properties received by her on partition, to her daughter-in-law, the wife of the *karta*. As, however, the widowed mother was legally incompetent to call for a partition of the family and no partition could also take place with the sole purpose of allotting a share to a female member, there was no lawful partition of the family. The properties allotted to the mother, together with those alienated by her subsequently, continued to belong to the joint family. In view of this position, the separated properties were assessable to wealth-tax in the hands of the Hindu undivided family. As this was not done, short levy of tax totalling Rs. 17,140 took place in the assessment years 1966-67 to 1976-77.

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

(ii) The net wealth of an assessee means the aggregate value of all his assets, as reduced by the aggregate value of all debts owed by him on the valuation date. Debts which are secured on, or which have been incurred in relation to any property in respect of which wealth-tax is not chargeable, are not, however, to be deducted in computing the net wealth. In the wealth-tax assessments of an assessee Hindu undivided family for the assessment years 1966-67 to 1972-73, furniture articles valued at Rs. 1,24,411 were exempted as articles of assessee's personal or household use. The furniture had, however, been acquired out of borrowed funds and the debt incurred for their acquisition was outstanding on the relevant valuation dates. As such the corresponding amount of debt was not allowable as deduction in computing the net wealth. Similarly, while exemption of rupees one lakh was allowed in respect of the value of self-occupied

property for the assessment year 1966-67, the corresponding debt was not reduced from the debts though the entire cost of construction had been met out of borrowed funds. These mistakes resulted in total under-assessment of wealth by Rs. 9,70,877 for the assessment years 1966-67 to 1972-73, with consequent undercharge of tax of Rs. 25,561 (including mistake of Rs. 6,500 in calculation of tax for the assessment year 1969-70).

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

(iii) As mentioned in paragraphs 5.2 and 5.3 of the Public Accounts Committee's 186th Report (1975-76), the Committee have almost year after year commented upon the continuation of a very common mistake involving the dropping of one lakh of rupees or the wrong transcription of a digit from a substantial amount resulting in under-assessment of tax in big income cases. Similar mistakes still continue to occur. Instances of such errors were reported in paragraphs 34(vi) and 95 of the Audit Report, 1975-76 and paragraph 61.6 of the Audit Report, 1977-78. Another costly mistake is given below :—

An individual held shares in different companies valued at Rs. 11,67,954 on the valuation date relevant to the assessment year 1967-68. While computing the aggregate value of such shares, the department erroneously arrived at a figure of Rs. 12,17,954 (by overstating the total by Rs. 50,000). The figure of Rs. 12,17,954 so wrongly computed was, however, taken into the assessment, completed in March, 1978, only as Rs. 1,21,794. Thus, the dropping of a digit led to under-assessment of wealth of Rs. 10,46,160 (Rs. 11,67,954 minus Rs. 1,21,794) and short levy of tax of Rs. 23,725 for the assessment year 1967-68.

The Ministry of Finance have accepted the audit objection.

69. *Incorrect and excessive exemptions*

(i) Under the provisions of the Wealth-tax Act, 1957, value of shares, forming part of the initial issue made by a company after 31st March, 1964 but before 1st June, 1971, of equity

share capital of companies set up as new industrial undertakings, is to be excluded from the net wealth for a period of five years commencing with the assessment year next following the date on which the company commences its operations.

An assessee claimed and the department allowed exemption for the value of 960 such equity shares for the assessment years 1970-71 to 1975-76 *i.e.* for a period of six years instead of for five years. This resulted in an excess exemption of Rs. 2,91,552 and consequential short levy of tax of Rs. 21,598 for the assessment year 1975-76.

Though the case was seen in Internal Audit, the mistake was not noticed by it.

The Ministry of Finance, in accepting the audit objection, have stated that additional tax raised and collected is Rs. 21,598.

(ii) As an incentive to savings, the Wealth-tax Act, 1957 allows exemption from levy of wealth-tax to bank deposits, investments in securities, shares, capital invested in industrial undertakings, etc. upto an aggregate amount of Rs. 1,50,000.

In the case of two assessees, the department allowed the maximum admissible exemption of Rs. 1,50,000 on deposits with banks for the assessment years 1976-77 and 1977-78. In addition, exemption of Rs. 2,16,400 in one case and of Rs. 1,96,185 and Rs. 2,12,858 in the other case was allowed on other assets like capital in new industrial undertakings, shares, security bonds etc., which was not admissible. This resulted in under-assessment of tax aggregating Rs. 22,803 in the two cases for the assessment years 1976-77 and 1977-78.

The Ministry of Finance have accepted the audit objection in both the cases and stated that additional tax collected is Rs. 22,803.

(iii) With effect from 1st April, 1975, agricultural land for which a separate exemption was available upto the value of

Rs. 1.50 lakhs under the Wealth-tax Act, 1957, has been linked to other specified assets qualifying for exemption upto Rs. 1.50 lakhs in the aggregate.

In the case of four assessees in three Commissioners' charges, it was seen that exemption in respect of agricultural land was given in each case over and above the prescribed limit of Rs. 1.50 lakhs. This omission to apply the limit to the combined exemption resulted in an undercharge of tax of Rs. 17,591.

The Ministry of Finance have accepted the audit objection in all these cases.

70. *Short levy of penalty*

According to the Wealth-tax Act, 1957, as applicable for the assessment years earlier than 1976-77, where the value of any asset returned is less than 75 *per cent* of the value determined in the assessment, the assessee unless he proves that the failure to return the correct value did not arise from any fraud or gross or wilful neglect on his part, is deemed to have furnished inaccurate particulars of his wealth and is subject to a penalty which shall not be less than the value of assets in respect of which inaccurate particulars have been furnished.

For the assessment years 1968-69 to 1971-72, for failure to furnish the correct value of the house property owned by an individual, the department; in March 1978, levied penalty of Rs. 23,000 in respect of each assessment year. The Appellate Assistant Commissioner had, however, determined, in March 1977, the value of the property at Rs. 77,500 rejecting the assessee's returned value of Rs. 25,000 for the assessment years 1968-69 and 1969-70 and Rs. 31,844 for the assessment years 1970-71 and 1971-72. As the penalty for concealment was not computed by reference to the value of Rs. 77,500, as finally determined, there was short levy of penalty aggregating Rs. 1,04,312 for the aforesaid four assessment years.

Final reply of the Ministry of Finance to the audit paragraph sent to them in September 1979 in awaited (March 1980).

71. *Multiple mistakes in certain cases*

(i) Two individuals held respectively 73,090 and 89,662 unquoted equity shares of Rs. 10 each in a company on the valuation date relevant to the assessment year 1971-72 and 1,46,180 and 1,79,324 shares on the valuation dates relevant to the assessment years 1972-73 and 1973-74. In computing the market value of these shares at Rs. 30.47, Rs. 16.39 and Rs. 16.20 each respectively for their wealth-tax assessments for the assessment years 1971-72, 1972-73 and 1973-74, completed in September 1977, the department allowed proposed dividends of Rs. 1,18,000 in each of the assessment years 1971-72 and 1972-73 and a provision made for gratuity of Rs. 1,85,417 in the assessment year 1973-74 as liabilities. These liabilities, being future and contingent liabilities, were not allowable as deduction. On adding back these liabilities, the correct value of each share would be Rs. 30.90, Rs. 16.60 and Rs. 16.54 respectively in the above three assessment years. The undervaluation of these shares led to aggregate under-assessment of net wealth by Rs. 2,49,010 in these two cases for the three assessment years. Further, the total value of 1,79,324 such shares held by one of them was taken in his revised assessment for the assessment year 1973-74, made in November 1977, erroneously at Rs. 28,05,049 instead of the correct figure of Rs. 29,05,049, adopted in his original assessment. This mistake led to further under-assessment of his wealth for the assessment year 1973-74 by Rs. 1,00,000. Further still, in computing the tax liability of both the assessees for the above three assessment years the rates of tax prescribed for the slabs of net wealth in excess of Rs. 15,00,000 were not applied correctly. When these mistakes causing under-assessment of wealth-tax of Rs. 92,921 for the assessment years 1971-72 to 1973-74 were pointed out in June 1978, the department accepted and rectified them.

The Ministry of Finance have accepted the audit objection.

(ii) Despite the increase in the price of gold and silver in recent years, articles of jewellery held by four assessees on the valuation dates relevant to the assessment years 1973-74 to 1976-77 were valued, in the aggregate, at Rs. 12,92,400 being the value returned by the assessees. On the basis of the prices circulated by the Central Board of Direct Taxes in May 1976, the correct aggregate values worked out to Rs. 32,18,870. The under-valuation of jewellery and consequent under-assessment of wealth led to total undercharge of wealth-tax of Rs. 22,390 for the assessment years 1973-74 to 1976-77 for all the four assessees.

The Ministry of Finance have accepted the audit objection and stated that rectification in three cases had been done and is time-barred in the fourth case for the assessment years 1973-74 to 1975-76.

B—GIFT TAX

72. The receipts under gift-tax in the financial years 1974-75 to 1978-79 compared as under with the budget estimates of these years :—

Year	Budget estimates	Actuals
	(Rupees in crores)	
1974-75	4.00	5.06
1975-76	4.50	5.11
1976-77	4.75	5.67
1977-78	5.50	5.55
1978-79	5.75	5,85 (provisional)

The arrears of demand and cases pending assessment as on 31st March, 1979 were Rs. 17.72 crores and 21,807 respectively.

73. During the test audit of assessments made under the Gift-tax Act, 1958 conducted during the period from 1st April,

1978 to 31st March, 1979, the following types of mistakes were noticed :—

(i) Gifts escaping assessment.

(ii) Incorrect valuation of gifts.

(iii) Mistakes in calculation of tax.

(iv) Omission to charge interest.

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

74. *Gifts escaping assessment*

(i) In paragraph 3.10 of their 50th Report (Fifth Lok Sabha) and 1.28 of their 103rd Report (Fifth Lok Sabha), the Public Accounts Committee called for a review by the Board of gift deeds to locate escapement of gift-tax resulting from lack of co-ordination between the Gift-tax authorities and the State Government agencies like registering offices. The results of this review disclosed that levy of gift-tax of Rs. 2.72 crores had escaped in 34,364 cases of gifts valuing Rs. 32.68 crores. Having regard to this escapement of gifts, the need to introduce a suitable procedure for collection of information from State Government agencies in respect of cases where the apparent consideration is not an adequate consideration and in respect of gift-deeds, settlement deeds, trust deeds and deeds where the transferers purport to distribute their individual properties, designating the deeds as instruments of partition, etc., was pointed out in paragraph 78 of the Audit Report, 1975-76. The Central Board of Direct Taxes issued instructions in August 1979 for collection of information about the aforesaid categories of registered deeds "under the garb of which it is possible to evade gift-tax".

In paragraph 4.12 of their 186th Report (Fifth Lok Sabha), the Public Accounts Committee also commented on the lack of co-ordination (i) among the assessing officers of the department itself (ii) among the assessment records pertaining to different direct taxes, particularly income-tax and wealth-tax and (iii) among the income-tax Department and the other tax collecting departments of the Central and State Governments.

Nevertheless cases of escapement of gifts due to lack of such co-ordination were reported in paragraph 93(vii) of the Audit Report. 1976-77 and paragraph 75.1 of the Audit Report, 1977-78.

(ii) Some instances of cases of undercharge of wealth-tax resulting from omission to carry out such correlation have been pointed out in paragraph 63 of this Audit Report. Similar cases of undercharge of gift-tax are given below :—

(a) An assessee exchanged agricultural land of the value of Rs. 3,40,000 with agricultural land of the value of Rs. 1,16,650 of his relatives without receiving adequate consideration for giving up his interest in the difference. The difference in the value of the pieces of land exchanged amounting to Rs. 2,23,350 was a gift by the assessee to his relatives for the purpose of gift-tax. The department did not levy any gift-tax on the value of this gift. On the omission being pointed out in audit (October 1975), the department created (August 1978) an additional demand of Rs. 36,088.

The Ministry of Finance have stated that gift-tax assessment has been made on the basis of the audit objection.

(b) From the wealth-tax return of an assessee for the assessment year 1974-75, it was noticed that she had transferred 82 acres of cardamom plantation, owned by her and valued in her wealth-tax assessment at Rs. 1,64,000, to her daughter during the relevant previous year. The assessee did not file gift-tax return nor did the department consider the levy of gift-tax. At the value so adopted in wealth-tax assessment, the gift-tax leviable on this transfer was Rs. 23,300.

The Ministry of Finance have accepted the objection.

(c) If a partnership firm is reconstituted either with the same old partners or on retirement of one of the partners or due to admission of new partners or if a sole proprietorship is converted into a partnership, resulting in revision of the profit sharing radios, the part of the interest which is surrendered or relinquished by one or more of such persons without consideration in favour of others would attract levy of gift-tax. Valuation of the interest surrendered or relinquished is required to be done on the basis of the market value of the assets of the business including the value of its goodwill.

It was noticed in ten cases that such surrender of interest on reconstitution of firms, on admission of minors to the benefits of partnership, on retirement of partners and on conversion of sole proprietorships into partnerships, was not brought to gift-tax. The omission led to non-levy of a total gift-tax of Rs. 83,017 in the assessment years 1972-73 to 1975-76.

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

75. *Failure to bring 'deemed gifts' to tax*

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

While issuing instructions on the need for proper co-ordination among assessments under different tax laws in November 1973, the Central Board of Direct Taxes had specifically required Gift-tax Officers to levy gift-tax on 'deemed gift' in cases where they, as Income-tax Officers, noticed and brought to capital gains

tax, the excess of fair market value over declared consideration. Nevertheless, failure to bring such 'deemed gifts' to tax continues to be noticed as was pointed out in paragraph 80 of the Audit Report, 1975-76, paragraph 92 of the Audit Report, 1976-77 and paragraph 76 of the Audit Report, 1977-78. A few illustrative cases are again given below :—

(i) In the case of an individual, capital gain on the sale of lands had been computed for the assessment year 1973-74, adopting the fair market value of the property at Rs. 25,46,758 in accordance with the departmental Valuer's report as against the consideration of Rs. 21,43,898 declared by the assessee. No action was, however, taken to levy gift-tax on the difference between the fair market value so determined and the declared consideration. The gift-tax leviable on this escaped gift was of Rs. 52,074.

Though the case was seen in Internal Audit, the omission was not noticed.

The Ministry of Finance have accepted the audit objection and stated that additional tax demand of Rs. 52,074 has been raised.

(ii) An assessee declared a consideration of Rs. 8,45,760 for sale of certain properties made by him on 5th September, 1973. The Income-tax Officer finding that the value of the said properties was understated, referred the case to the departmental Valuation Officer for valuation. The Valuer determined the market value of the properties at Rs. 11,89,379. This value was adopted by the Income-tax Officer for levy of capital gains tax for the assessment year 1974-75. This property was actually sold later on at Rs. 12,15,780 through successive agreements to sell, the last confirming party taking at that value. The difference even of Rs. 3,43,619 between the fair market value

of Rs. 11,89,379 and the declared consideration of Rs. 8,45,760 was not brought to tax as a 'deemed gift'. The gift-tax chargeable on this deemed gift was Rs. 66,155.

Though the case was seen in Internal Audit, the Omission was not noticed.

The Audit paragraph was sent to the Ministry of Finance in September, 1979; their reply is awaited (March 1980).

(iii) In the case of an individual, capital gain on the sale of a landed property has been computed for the assessment year 1974-75, adopting the fair market value of the property at Rs. 25.49 lakhs according to the departmental Valuer's report as against the consideration of Rs. 14 lakhs declared by the assessee. No action was, however, taken to levy gift-tax on the difference between the market value so adopted and the declared consideration, treated as 'deemed gift'. A gift of Rs. 11.49 lakhs, thus, escaped assessment, resulting in non-levy of gift-tax of Rs. 3,14,000.

The Ministry of Finance have stated that assessment has been made as a precautionary measure pending decision in the appeal by the assessee in the capital gains tax case.

(iv) A firm, belonging to a big industrial group, during the previous year relevant to the assessment year 1975-76, sold certain shares in five private companies within the group at an aggregate declared consideration of Rs. 16,00,708. Under the Gift-tax Act read with the rules framed thereunder, the shares were to be valued at the market value of the assets of the companies, including their goodwill. It was, however, noticed that the assessing officer did not ascertain the market value of the assets of the

companies and compute the value of their goodwill for valuation of these shares. The market value of the shares even on the break-up value basis was Rs. 22,67,411. The excess of this value over the declared consideration amounting to Rs. 6,66,703, was taxable as deemed gift. However, neither the assessee had filed any return of gift-tax nor had the department called for the same. A gift of not less than Rs. 6,66,703, thus, escaped assessment in the assessment year 1975-76 resulting in non-levy of gift-tax of Rs. 1,56,510. Under-assessment of tax would be more if the market value of the assets of the companies and the value of their goodwill were adopted for the valuation of these shares.

The Ministry of Finance have stated (December 1979) that the audit objection is under consideration.

76. *Incorrect valuation of unquoted equity shares*

Under Section 6(1) of the Gift Tax Act, 1958, the value of a gifted property has to be estimated to be the price which in the opinion of the Gift-tax Officer it would fetch if sold in the open market. Rule 10(2) of the Gift-tax Rules lays down that the value of unquoted equity shares in a company should be ascertained with reference to the value of the total assets of the company. As the provisions of the Gift-tax Act are in *pari materia* with those of the Estate Duty Act, 1953 in regard to the valuation of unquoted equity shares, the instructions issued by the Board under the Estate Duty Act for valuation of such shares, are equally applicable to gift-tax cases. Under the Estate Duty Act, the Board had issued instructions in May, 1965 and July, 1965 that the value of unquoted shares should be determined on the basis of the market value of the assets of the company and not the book value of the said assets.

The provisions on valuation of unquoted equity shares in the Wealth-tax Act, 1957 and rules framed thereunder are different from those in the Gift-tax Act and Estate Duty Act.

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

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

(i) In gift-tax cases of 9 assessees, belonging to a big family group, the valuation of unquoted equity shares of two companies, belonging to the group, gifted by them was done incorrectly under the wealth-tax rule which no longer applied to gift-tax cases, after its application to gift-tax cases was cancelled in October, 1974. In so valuing these shares, the value of assets of the company was taken at their book value instead of at their market value and the value of the goodwill of these companies was also not included. Even under the wealth-tax rule, there was undervaluation of shares in one company by Rs. 4,247 per share and Rs. 4,367 per share as on 30th March, 1972 and 29th March, 1973 respectively and in the other company by Rs. 190 per share as

on 30th March, 1972, leading to under-assessment of gifts by Rs. 34.05 lakhs and gift-tax of Rs. 10.33 lakhs for the assessment years 1972-73, 1973-74 and 1974-75.

The Ministry of Finance have accepted the audit objection in all the cases.

(ii) An individual sold 5,000 unquoted equity shares in a company to a partner of a firm in which the assessee's three sons, including a minor, had 34 per cent share interest and gifted 17,500 shares of the same company to his wife and sons on the same date in the previous year relevant to the assessment year 1973-74. The returned value of Rs. 21 per share was accepted in respect of the shares sold while the shares gifted were valued at Rs. 28.50 per share, thus, adopting two values for the same shares on the same date. No attempt was made by the department to compute the break-up value of these shares on the basis of the market value of the assets of the company including the value of its goodwill under the provisions of the Act and rules framed thereunder. It was noticed in audit that the value of these shares would work out to Rs. 63 per share even if the market value of closing stock of the company were taken, the value of goodwill were included and the value of other assets of the company were taken at their book value, in the absence of their market value having been ascertained and recorded by the assessing officer. The under-assessment of the gift in this case was of Rs. 8,13,750 and of tax was of Rs. 2,75,875 in the assessment year 1973-74.

The Ministry of Finance have stated (January, 1980) that the audit objection is under consideration.

(iii) In paragraph 94 of the Audit Report, 1976-77, the manner of correct computation of the valuation of unquoted shares in companies for purposes of levy of capital gains tax and gift-tax was stated and undercharge of tax of Rs. 1.85 crores was pointed out. Final action on the recommendations of the Public Accounts Committee contained in paragraph 2.17 of their 147th Report (Sixth Lok Sabha) in this regard is yet to be taken by the Ministry of Finance (January, 1980). Another similar case of underassessment is given below :

An assessee gifted 2,000 unquoted equity shares in a private limited company during the period 8th March, 1973 to 2nd April, 1973 *i.e.*, relevant to assessment years 1973-74 and 1974-75. The assessing officer computed the break-up value of these shares on the basis of book value of the assets of the company as shown in its balance-sheet as on 31st March, 1973 and allowed discount of 25 per cent also by application of the wealth-tax rule to this gift in September, 1977 *i.e.*, after October, 1974, when the extension of the wealth-tax rule to gift-tax cases had already been withdrawn by the Board. The valuation was required to be done on the basis of the market value of the assets of the company, including the value of its goodwill.

The incorrect valuation of these shares by incorrect allowance of the discount led to underassessment of tax of Rs. 38,000. The undercharge of tax would be higher if correct valuation were done on the basis of the market value of the assets of the company including also the value of its goodwill.

The Ministry of Finance have accepted the audit objection.

(iv) An assessee gifted 100 unquoted equity shares of a private limited company on 2nd September, 1975.

The break-up value of the shares gifted was arrived at Rs. 3,411 per share on the basis of the balance-sheet of the company as on 13th November, 1974 and this value was discounted by 20 per cent as provided in the rule framed under the Wealth-tax Act, 1957, thus adopting the rate of Rs. 2,729 per share in the assessment. The valuation so done was computed under the wealth-tax rule which was not then applicable to gift-tax cases. Correct valuation was required to be done on the basis of the market value of the assets of the company including the value of its goodwill and not on the basis of the value reflected in its balance-sheet. This was not done. Even the valuation done by application of incorrect rule applicable to wealth-tax cases was incorrect as, while working out the break-up value,

(i) liability for proposed dividend which had not been declared in the general meeting (Rs. 1,30,000) was incorrectly allowed, and

(ii) the provision for taxation allowable on the basis of returned profits only (Rs. 84,31,796) was allowed as Rs. 1,09,36,187 as depicted in the balance-sheet of the company.

In the absence of the Gift-tax Officer having ascertained and placed on record the market value of the assets and goodwill of the company, the computation of the break-up value on the basis of value reflected in the balance-sheet of the company would be Rs. 5,266 per share. The gift was, thus, under-assessed by Rs. 2,53,700 leading to total short levy of gift-tax of Rs. 64,505. Under-assessment caused would be more if the assets of the company were taken at their market value, including also the value of its goodwill.

The Ministry of Finance have accepted the audit objection partly.

77. *Incorrect computation of taxable gift*

In paragraph 68(iii) of this Audit Report, a case of dropping of a digit in total in the case of a big income assessee resulting in under-assessment of wealth has been reported. In another case, the value of a taxable gift made by an individual for the assessment year 1975-76 was Rs. 2,11,000 on which gift-tax of Rs. 34,250 was chargeable at the prescribed rates. The department, however, levied a tax of only Rs. 13,700 which was referrable to taxable gift of Rs. 1,11,000. The incorrect totalling led to an under-assessment of tax of Rs. 20,550 for the assessment year 1975-76. On the mistake being pointed out in audit (September, 1978) the department rectified the assessment raising and collecting additional tax of Rs. 20,550.

The Ministry of Finance have accepted the audit objection.

78. *Incorrect valuation of other assets*

(i) An individual returned the value of gifts of Rs. 1,09,767 for the assessment year 1970-71, including the value of a landed property in Calcutta. A part of this land was on lease with the Municipal Corporation of Calcutta, the capitalized value of which fixed on the basis of rents determined in arbitration was Rs. 1,56,750. The remaining land, about five times the leased land in area, was valued by an approved valuer only at Rs. 31,000. The value of the entire land considered in the gift-tax assessment was of Rs. 31,000 as against Rs. 1,87,750. The undervaluation of this land by not less than Rs. 1,56,750 led to undercharge of tax of Rs. 23,979 for the assessment year 1970-71.

The Ministry of Finance have stated (December, 1979) that the audit objection is under consideration.

(ii) An individual gifted 3/8th portion of a house property each to his married daughter and jointly to his two grandsons in September, 1969. The gifts were taken at the returned value of Rs. 45,000 for each of the above portions in the original assessment completed in December, 1973. The same value was taken

in the fresh assessment made in December, 1977 pursuant to appellate orders of March 1975, though, on a reference made to the Valuation Cell, in the meanwhile, the Valuation Cell had in July, 1977 determined the market value of the two portions of property gifted in September, 1969 as Rs. 1,74,682. Omission to adopt the correct value in the revised assessment in December, 1977 or to rectify the original assessment thus led to under-valuation of the gift by Rs. 84,682 and to undercharge of gift-tax of Rs. 19,670.

The Ministry of Finance have accepted the audit objection.

79. *Incorrect calculation of tax*

A new section 6A has been introduced in the Gift-tax Act, 1958 by the Taxation Laws (Amendment) Act, 1975 with effect from 1-4-1976. As a result of this new provision, gifts spread over five previous years are aggregable. Gift-tax is now first computed on the gift of the relevant previous year aggregated with gifts of the 'preceding four previous years' (excluding gifts made before 1-6-1973), at the rates of the assessment year in hand. From the gift-tax so computed, gift-tax on the gifts of these preceding four previous years at the same rate is then deducted. The balance is the gift-tax payable.

A number of cases of failure to apply the aforesaid provision for aggregation of gifts with consequential tax undercharge of Rs. 1,01,180 were pointed out in para 78 of the Audit Report, 1977-78. Cases of such failure continue to be noticed in audit. Thus, in 18 cases in 11 Commissioners' charges, an undercharge of tax of Rs. 49,299 in the assessment years, 1976-77 and 1977-78 resulting from similar omission to aggregate gifts in the prescribed period was again noticed in test audit.

The Ministry of Finance have accepted the omission in all the cases.

80. *Omission to charge interest*

Under the provisions of the Gift-tax Act 1958, the amount of gift-tax specified as payable in a notice of demand is to be paid within a period of thirty-five days of the service of notice to the assessee. If the amount is not paid within that period, the assessee is liable to pay simple interest at the rate of twelve per cent per annum from the day commencing after the end of the period of thirty-five days.

A demand notice for Rs. 1,72,980 was raised against an assessee on the 21st June, 1976 in respect of net taxable gift of Rs. 7,21,600 made during the previous year relevant to the assessment year 1973-74. Without paying the tax as per the demand notice, the assessee went in appeal to the Appellate Assistant Commissioner who reduced the value of the taxable gift to Rs. 4,24,010. The reduced demand in consequence of the appellate orders was paid by the assessee on 23-3-1978 as against the due date of 26-7-1976. Though the assessee was liable to pay interest for delayed payment of Rs. 70,303 from the 26th July, 1976 to the 23rd March, 1978, no interest was charged by the department. Interest not charged amounted to Rs. 13,357.

The Ministry of Finance have accepted the audit objection.

C—ESTATE DUTY

81. The receipts under estate duty in the financial years 1974-75 to 1978-79, compared as under with the budget estimates of these years :—

Year	Budget estimates	Actuals
	(Rupees in crores)	
1974-75	9.00	10.94
1975-76	9.25	11.65
1976-77	9.75	11.73
1977-78	10.75	12.30
1978-79	12.00	13.08

The arrears of demand and the number of assessments pending as on 31st March 1979 were Rs. 17.11 crores and 28,278 respectively.

82. During the test audit of assessments made under the Estate Duty Act, 1953, conducted during the period from 1st April, 1978 to 31st March 1979, the following types of mistakes resulting in under-assessments of duty were noticed :—

(i) Estate escaping assessment.

(ii) Incorrect valuation of assets.

(iii) Mistakes in computation of principal values of estates.

(iv) Irregular/excessive deductions and reliefs.

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

83. *Estates escaping assessment*

(i) A comparison of the details of immovable properties owned by a deceased person (died on 25-1-1969) available in the assessment records of the ward with the principal value of his estate, as computed, disclosed that the value of non-agricultural lands measuring 3417 sq. yds. was omitted to be included. This omission resulted in an under-assessment of the principal value of the estate by Rs. 1,70,850, leading to a short levy of duty of Rs. 51,255.

Though the case was seen by Internal Audit, the omission remained unnoticed.

The Ministry of Finance have stated (December, 1979) that the audit objection is under consideration.

(ii) In the estate duty assessment of another deceased person, who died on the 21st November 1972, it was noticed that the properties which he had owned separately and which he had thrown into the joint family hotchpot in 1963 and in 1967 were taken together as comprising the common properties of the

family and only his share in them was included in the principal value of his estate, though such throwing of properties by him into the 'common hotchpot' of the family was a 'disposition' attracting levy of estate duty in respect of the full value of the properties. This mistake resulted in short levy of estate duty of Rs. 49,880.

The Ministry of Finance have accepted the audit objection.

(iii) In the estate duty assessment, completed in August 1977, in respect of a deceased person (died in May 1968), the assessing officer, while aggregating the values of all properties to determine the net principal value of the estate, omitted to include a sum of Rs. 1,51,395 being the value of five movable properties. This omission resulted in under-assessment of the estate by Rs. 1,51,395 with consequent undercharge of duty of Rs. 45,418.

The Ministry of Finance accepted the audit objection.

(iv) Under the provisions of the Estate Duty Act, 1953, property owned by a person at the time of his death or which he was capable of disposing of at that time is liable to be included in the principal value of the estate passing on his death.

A person, who died in January 1973, had constructed a house property on land belonging to his wife in the year 1961 *viz.*, more than two years prior to his death. The deceased during his life-time claimed that the house property had been gifted to the wife in 1961. He also filed a gift-tax return and the gift was subjected to gift-tax. It was, however, noticed in audit that no gift deed had been executed and registered by the deceased in respct of the property, in the absence of which the gift had no effect. Further, the deceased continued to reside in the house with his wife till his death and, therefore, right of the ownership of the wife by the doctrine of adverse possession could also not

have been asserted by her against her husband. The property was, thus, includible in the principal value of the estate of the deceased. It had been, in fact, so included in the assets of the deceased for levy of wealth-tax and exemption of Rs. 1 lakh had been allowed to the deceased person in respect of this house as belonging to him. The Assistant Controller, however, omitted to include the value of the house in the principal value of his estate. This omission resulted in short levy of estate duty of Rs. 50,000 from which rebate in respect of gift-tax of Rs. 4,400, if paid, would be allowable.

The Ministry of Finance have stated that the land had been purchased by the deceased person in the name of his wife and in the Municipal records the land and the building (constructed by the deceased person on that land) was recorded in the name of his wife and that transfer took effect due to this overt act. Audit feels, however, that the transfer had no effect without execution and registration of relevant transfer deeds.

84. *Incorrect computation of share interest of deceased partners in partnership firms*

(i) One of the methods of computation of the value of goodwill of a business is the 'super-profits' method, in which its average super-profits are capitalised at the appropriate number of years' purchase. Such computation of the value of goodwill of a business is necessary for inclusion in the assets of the business for working out the interest of a deceased person in it for levy of estate duty.

In the estate duty case of a deceased person (died on 31-12-1970), the value of goodwill of a partnership firm in which he was a partner was determined at half years' purchase of three years' average super-profits instead of the usual 1½ years' or two years' purchase. Even in so doing, super-profits for two years were incorrectly taken for averaging at net figure after deduction of income-tax while that for the third year they were correctly taken as before-tax. Further, the share of the deceased

partner in the goodwill of the firm so computed was incorrectly taken as one-third instead of as one-half. The combined effect of these mistakes was under-assessment of estate duty of Rs. 1,33,515.

The case was seen by Internal Audit Party; these mistakes, however, remained unnoticed.

The Ministry of Finance have stated (December, 1979) that the audit objection is under consideration.

(ii) In an estate duty case, the share interest of the deceased person in the goodwill of the partnership firm, in which he was a partner was computed short by Rs. 74,646, due to an arithmetical error. Further, refund of income-tax amounting to Rs. 39,400 due to him and payments aggregating Rs. 27,548 made by him on behalf of his wife and grandchildren within two years before his death were includible in the principal value of his estate but were not included. These errors pointed out by Audit in May, 1978 were rectified in August, 1978, raising additional duty of Rs. 22,546.

The Ministry of Finance have accepted these errors.

(iii) In 17 other cases in a Controller's charge the share interest of the deceased partner in the partnership firm was computed on the basis of the book value of their closing stocks instead of at their market value under section 37 of the Estate Duty Act 1953, resulting in total undercharge of estate duty of Rs. 2,46,105.

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

85. *Incorrect computation of deceased's interest in heritable estate*

In the Estate Duty assessment of a *Shia* Muslim, who died on 11-2-1974, the gross value of his estate was determined as Rs. 6,40,873, which included Rs. 6,03,582 as one-third share of the deceased person in the property left by his mother. It

was pointed out in audit that, under the law of succession applicable to *Shia* Muslims, when a person dies leaving behind sons and daughters, each son takes twice the share allotted to a daughter and that, as the deceased had a brother and a sister, the deceased person was entitled to 2/5th and not 1/3rd share of the property of Rs. 18,10,746 left by his deceased mother.

Accordingly the value of estate inherited by him should have been taken in the estate duty assessment at Rs. 7,24,300 instead of Rs. 6,03,582. The mistake resulted in under-assessment of duty of Rs. 36,215.

The Ministry of Finance have accepted the audit objection and stated that the additional demand of Rs. 36,215 has been raised.

86. *Incorrect valuation of unquoted equity shares*

In paragraph 82 of the Audit Report, 1977-78, cases of under-assessment of estate duty resulting from incorrect application of a wealth-tax rule to estate duty cases were reported. Cases of similar under-assessments continue to be noticed in test audit. A few illustrative cases are given below :—

(i) In the case of a deceased person, who died on 14-4-1973, the valuation of 1,250 partly paid and 180 fully paid unquoted equity shares in a private limited investment company (belonging to his family) was not done on the basis of market value of the assets of the company. This omission in not taking the investments of the company in other companies at their market value alone led to undervaluation of its unquoted shares comprising the estate of the deceased person and thereby the principal value of his estate by Rs. 1,50,140 with consequent short levy of duty of Rs. 53,145.

In the same case further, 500 partly paid unquoted equity shares of this private limited investment company, gifted by him within two years prior to his death and which were added to the principal value of his estate, were also not similarly valued, adopting the market value of the assets of the company in accordance with the instructions of the Board issued in October, 1974.

The combined effect of these mistakes was under-assessment of the estate by Rs. 1,94,140 and of estate duty of Rs. 70,745.

The Ministry of Finance have accepted the audit objection.

(ii) In the case of a deceased person, who died on 22-11-1973, the assessing officer had, while computing the break-up value of certain unquoted equity shares held by him in two 'closely held companies', allowed a discount of 15 per cent from the break-up value so computed under a wealth-tax rule. The application of the wealth-tax rule to estate duty case was cancelled by the Board in October, 1974 whereupon the incorrect valuation done under that rule was required to be rectified by re-doing the valuation on the basis of the market value of the assets of the company including its goodwill without allowance of any discount. The incorrect allowance of discount under the wealth-tax rule alone resulted in the under-assessment of estate duty of Rs. 42,212.

The audit objection is stated (December 1979) to be under consideration of the Ministry of Finance.

87. *Mistakes in the computation of principal values of estates*

(i) In an estate duty case (death on 30-4-1971), though the tax refunds, becoming due to the deceased person for the period before her death, totalled Rs. 2,88,174, tax refunds only of Rs. 13,497 were included in the principal value of her estate. This mistake in computation of the value of her estate resulted in short levy of estate duty of Rs. 2,33,475.

(ii) Cases of under-assessment of wealth-tax and gift-tax resulting from dropping of total by one lakh are reported in paragraph 68(iii) and paragraph 77 of this Audit Report. Two similar cases were noticed in the audit of estate duty assessments also. In these cases, the principal values of the estates were

respectively adopted as Rs. 2,36,157 and Rs. 1,95,500 instead of Rs. 3,36,157 and Rs. 2,95,500, causing undercharge of estate duty of Rs. 24,853.

The Ministry of Finance have accepted the audit objection in both the cases.

88. *Omission to include certain dispositions*

Under the provisions of the Estate Duty Act, 1953, a disposition made by a person within a period of two years prior to his death, is to be treated as property deemed to pass on death. It has been judicially held that where, on a partition of a Hindu undivided family, a deceased coparcener had taken less than his due share, there was such a 'disposition' in favour of relatives to the extent of share less taken by the deceased.

In the estate duty assessment of a deceased *karta* of a Hindu undivided family, it was noticed that on a partial partition of properties between the deceased, his wife and son, made within two years before his death, the deceased had taken only Rs. 48,509 as against his due share of Rs. 1,72,916. The difference of Rs. 1,24,407 was, thus, includible in the principal value of the estate of the deceased. It was not, however, included. The omission resulted in under-assessment of the estate of the deceased by Rs. 1,24,407 with consequent short levy of estate duty of Rs. 21,753.

The Ministry of Finance have accepted the omission.

89. *Irregular/excessive allowance of deductions and reliefs*

(i) Under the provisions of the Estate Duty Act, 1953, where any fees have been paid under any law relating to court fees for obtaining succession certificate in respect of any property on which estate duty is payable, the amount of the estate duty payable shall be reduced by an amount equal to the court fees so paid.

In the case of a deceased coparcener, who died on 28th January 1977, the court fees amounting to Rs. 26,730 paid for obtaining succession certificate in respect of the common property of the Hindu undivided family was allowed in full, as a deduction from the duty chargeable, instead of restricting it to one-third *viz.*, Rs. 8,910, being the share interest of the deceased in the property. The excessive allowance of this relief resulted in a short levy of estate duty of Rs. 17,820.

The Ministry of Finance have accepted the audit objection.

(ii) In an estate duty case, the deceased person (died on 8th December, 1975) had created a trust by transfer of an immovable property valuing Rs. 3,80,000 and gift-tax of Rs. 84,860 payable on this transfer was paid by its trustees. This amount of Rs. 84,860 was allowed as deduction of debt payable to the trustees by the deceased person on his death. However, this debt was not allowable as deduction, as the value of the property transferred by the deceased to the trust was more than the debt payable by him to the trust. The incorrect allowance of deduction of Rs. 84,860 led to under-assessment of estate duty of Rs. 21,550.

The Ministry of Finance have stated that the audit objection in under their consideration (January 1980).

CHAPTER V

OTHER RECEIPTS

90. *Emergency Risks (Goods/Undertakings) Insurance Schemes*

1. In pursuance of the Emergency Risks (Goods) Insurance Act, 1971, and the Emergency Risks (Undertakings) Insurance Act, 1971, enacted in the wake of the emergency, the Government of India framed the Emergency Risks (Goods) and (Undertakings) Schemes effective from 10th December, 1971, for the compulsory insurance of goods and undertakings against damage arising from emergency risks. All goods meant for sale or supply exceeding Rs. 50,000 in value in any district and all undertakings specified in the Act were compulsorily insurable with the Central Government.

2. The Oriental Fire and General Insurance Company Ltd. was appointed as the agent of the Government to issue insurance policies against challan receipts produced by parties in support of payments of premia into the treasury for credit to Government account. The administration of the Schemes was entrusted to the Directorate of Emergency Risks Insurance which had been set up in September 1965 under the Ministry of Finance to administer similar Schemes under the corresponding Acts of 1962 and which had continued in existence to complete the residual work of these Schemes after the lifting of the 1962 emergency in January 1968.

3. The two Acts of 1971 were allowed to expire on 27th March, 1977 when the proclamation of emergency was withdrawn. The total amounts of receipts and expenditure under the two Schemes upto 31st March 1979, came to Rs. 24.65 crores and Rs. 0.54 crore respectively.*

*Figures given by the Ministry of Finance.

4. The two Acts provided for transfer, after appropriation made by Parliament by law, in each financial year of such sums as may be considered necessary to the Emergency Risks (Goods) and (Undertakings) Insurance Funds from out of which claims arising under the Schemes were to be met. It was clear that the premia receipts were to form part of the Consolidated Fund of India. This was further clarified in the detailed accounting procedure laid down in December 1971. In April 1972, it had also been specifically mentioned to the Ministry that with the enactment of the Comptroller and Auditor General (Duties, Powers and Conditions of Service) Act, 1971, the premia receipts under the two Schemes would come within the purview of statutory audit by the Comptroller and Auditor General of India. Nevertheless, when the audit of these receipts was taken up in January 1977, the Directorate of Emergency Risks Insurance did not produce the records for audit on the plea that the collections of insurance premia were not payable into the Consolidated Fund of India and the receipts were not, therefore, subject to audit by the Comprtoller and Auditor General of India. The Directorate insisted in this view till April 1978 when instructions were issued by the Ministry of Finance to the effect that the premia receipts were subject to audit by the Comptroller and Auditor General of India.

The Ministry of Finance have stated that right from 1963 audit of expenditure under the Schemes was being conducted but no formal receipt audit was taken up so that there was no reason to believe that Audit would like to examine the accounts of the Schemes under the Act of 1971 in a different fashion. The Ministry have apparently not appreciated the provisions of Section 16 of the Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971, despite the provisions of that Act having been specifically brought to their notice in the context of the receipts under the 1971 Schemes in April 1972 itself.

5. While the jurisdiction of Audit was still in question by the Directorate, a proposal was framed in December 1977, for

the weeding out of the records of the Directorate though according to the administrative instructions of the Directorate itself these were required to be preserved upto 1982. Instructions for the actual weeding out of the records were issued on 17th January, 1978. By the time the aforesaid instructions about the jurisdiction of Audit were issued by the Ministry of Finance in April 1978, virtually all the 1.75 lakh files (with the exception of 5000 odd cases) had been destroyed. The fact that Audit had already asked for these records was not mentioned in the proposal made to weed out these records.

6. As a result, a proper audit of these receipts could not be conducted.

The Ministry of Finance have stated that the decision to weed out records, after curtailing the retention period was taken with the approval of the administrative Ministry, in view of the fact that on the closure of the Directorate most of the personnel were to be reverted to the parent departments. They have added that in the proposal submitted to the Ministry by the Directorate no specific reference was made to the pendency of the question relating to the jurisdiction of Audit because the matter was within the knowledge of the administrative Ministry.

7. A limited review of the residual records of Delhi Centre in the Directorate in August 1978 revealed the following points :—

(i) It was not possible to reconcile the number of cases verified with the enforcement files weeded out. The department stated that compliance of instructions regarding maintenance of the records relating to weeding out of files was not uniform at different regional centres and such a reconciliation was not feasible.

In respect of Delhi Centre alone it was noticed that against 36,269 cases of Goods and 6,457 cases of Undertakings surveyed and verified during the years 1972-73 to 1977-78 demands amounting to

Rs. 46.45 lakhs and Rs. 55.48 lakhs had been raised only in 18,877 and 3,601 cases respectively. It was stated "in many of the cases the parties had taken adequate insurance cover, whereas in many cases they were not covered by the Act either because their stocks were less than Rs. 50,000 or the stocks consisted of non-insurable goods. Thus the demands could be raised only in cases where there had been some default and not in each case". No details of 17,395 cases of Goods and 2,856 cases of Undertakings, in which demands had not been raised, were, however, supplied.

(ii) The Acts provided also that their expiry "shall not affect anything done or omitted to be done before such expiry". Government's right to recover the insurance premia due or in default during the operation of the Schemes was, therefore, preserved even after their expiry. Government could exempt any class of 'goods' by notification which had to be laid on the table of each House of Parliament. Most of the cases of pending survey/verification of goods were, however, dropped after the lifting of the emergency on the plea that 'labour and expenditure involved might not be commensurate with the amounts involved'. No details of cases so dropped and the likely amounts foregone were produced.

(iii) Under the Acts, in the event of any default in the payment of insurance premium an equivalent amount could be recovered by way of penalty as arrears of land revenue. The defaulter could also be proceeded against for punishments provided under the Acts. It was, however, noticed that in January 1978 a decision was taken not to launch prosecutions in cases involving premia in default upto Rs. 20,000. The number of such cases was estimated at 1970.

(iv) Despite the above relaxations 4,759 recovery certificates for an amount of Rs. 1.43 crores were pending as on 28th February, 1978.

(v) In 276 cases it was noticed that cheques for a total amount of Rs. 95,673 on account of insurance premia were dishonoured. There was no evidence to show that fresh cheques in lieu of the dishonoured cheques were obtained from the parties concerned and credited to Government account. It was stated that the enforcement files had been weeded out and it was not possible to produce the challans.

The Ministry of Finance have stated *ad seriatim* :

(i) in view of the limitation of time and available hands, it was not possible to undertake the requisite reconciliation and that the records pertaining to cases in which no action was pending including cases in which no demand needed to be raised had already been weeded out ;

(ii) it was felt that completion of pending verification work may be hampered by resistence from the parties in the changed atmosphere and no verification having been done in smaller cases, it was not possible to make any precise estimate of the receipts given up in the process ;

(iii) pending cases of default were dropped as it was felt that in most cases it may not be possible to sustain a successful prosecution and the amounts of compounding fees involved (50 per cent of defaulted premia) would not be commensurate with the time, effort and expense required for prosecution ;

(iv) recovery certificates had been issued in all cases pending for recovery, major recovery actions pending being either under litigation or pertaining to sick mills ; and

(v) there was difficulty in complying with audit requirement for verification because wherever recovery had been completed and no other action was pending, the file was weeded out.

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

NEW DELHI
The....., 1980.

2nd April, 1980

Countersigned

(GIAN PRAKASH)
Comptroller and Auditor General of India.

NEW DELHI
The....., 1980.

3rd April, 1980