P.A.C. No 590

PUBLIC ACCOUNTS COMMITTEE (1977-78)

(SIXTH LOK SABHA)

FIFTY FIRST REPORT

CORPORATION TAX

MINISTRY OF FINANCE

(DEPARTMENT OF REVENUE)

[Action taken by Government on the recommendations of the Public Accounts Committee contained in their 187th Report (Fifth Lok Sabha)]

Presented in Lok Sabha on 23-12-1977

Presented in Rajya Sabha on 23-12-1977

LOK SABHA SECRETARIAT
NEW DELHI

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PUBLIC ACCOUNTS COMMITTEE
(1977-78)

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2. Shri H. G. Paranjpe—*Chief Financial Committee Officer*
3. Shri Bipin Behari—*Senior Financial Committee Officer.*

* Elected with effect from 23 November 1977 *vice* Sarvashri Sheo Narain and Jagdambi Prasad Yadav ceased to be Members of the Committee on their appointment as Ministers of State.

INTRODUCTION

I, the Chairman of the Public Accounts Committee, as authorised by the Committee, do present on their behalf this Fifty-First Report on the action taken by Government on the recommendations of the Public Accounts Committee contained in their One Hundred and Eighty-Seventh Report (Fifth Lok Sabha) on paragraphs relating to Corporation Tax included in Chapter II of the Report of the Comptroller and Auditor General of India for the year 1972-73, Union Government (Civil).

2. On 10 August, 1977, an 'Action Taken Sub-Committee' consisting of the following members was appointed to scrutinise the replies received from Government in pursuance of the recommendations made by the Committee in their earlier Reports:

1. Shri C. M. Stephen—*Chairman*
2. Shri Asoke Krishna Dutt—*Convener*
3. Shri Gauri Shankar Rai
4. Shri Tulsidas Dasappa
5. Shri Kanwar Lal Gupta
6. Shri Zawar Hussain
7. Shri Vasant Sathe

(3 to 7) *Members*..

3. The Action Taken Sub-Committee of the Public Accounts Committee (1977-78) considered and adopted the Report at their sitting held on 29 November, 1977. The Report was finally adopted by the Public Accounts Committee (1977-78) on 20 December, 1977.

4. For facility of reference, the conclusions/recommendations of the Committee have been printed in thick type in the body of the Report. For the sake of convenience, the conclusions/recommendations of the Committee have also been appended to the Report in a consolidated form.

5. The Committee place on record their appreciation of the assistance rendered to them in this matter by the Comptroller and Auditor General of India.

C. M. STEPHEN,
Chairman,
Public Accounts Committee.

NEW DELHI ;

December 20, 1977

Agrahayana 29, 1899 (*S*).

CHAPTER—I

REPORT

1.1. This Report of the Committee deals with the action taken by Government on the Committee's recommendations/observations contained in their 187th Report (Fifth Lok Sabha) on paragraphs relating to Corporation Tax included in Chapter II of the Report of the Comptroller and Auditor General of India for the year 1972-73, Union Government (Civil), Revenue Receipts, Volume II, Direct Taxes.

1.2. The 187th Report was presented to the Lok Sabha on 29th January 1976 and contained 72* recommendations/observations. Action Taken Notes on all these recommendations/observations have been received from Government and these have been broadly categorised as follows:

(i) *Recommendations/Observations that have been accepted by Government:*
Sl. Nos. 1-3, 6, 8, 11-14, 16, 20-25, 31-35, 38-46, 48-56, 58, 60-62 and 67-72.

(ii) *Recommendations/Observations which the Committee do not desire to pursue in the light of the replies received from Government:*
Sl. Nos. 9, 30, 57, 59 and 63.

(iii) *Recommendations/Observations replies to which have not been accepted by the Committee and which require reiteration:*
Sl. Nos. 4, 7, 10, 15, 19, 28, 47, 64 and 66.

(iv) *Recommendations/Observations in respect of which Government have furnished interim replies:*
Sl. Nos. 5, 17, 18, 26, 27, 29, 36, 37 and 65.

1.3. According to the time schedule prescribed in the Committee's 5th Report (Fourth Lok Sabha) for the submission of Action Taken Notes on the Committee's recommendations/observations, the Notes indicating the action taken by Government on the recommendations/observations contained in the 187th Report (Fifth Lok Sabha) were required to be furnished to the Committee by 28th July 1976. The Committee are happy that the Department of Revenue & Banking have furnished all the Action Taken Notes relevant to this Report by the stipulated date and have also accepted most of the Committee's recommendations. This is a welcome trend which, the Committee trust, would be maintained in future.

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*As a result of a printing error, the total number of recommendations/observations in the 187th Report had been wrongly indicated as 73 in Appendix IV to the Report. The mistake has been rectified in this Report and the recommendations/observations have been suitably renumbered.

1.4. The Committee expect that final replies to those recommendations/observations in respect of which only interim replies have so far been furnished will be submitted soon, after getting them vetted by Audit.

1.5. The Committee will now deal with the action taken by Government on some of their recommendations/observations.

Pre-check of draft assessment orders by Internal Audit (*Paragraphs* 1.17 *and* 2.21—*Sl. Nos.* 4 *and* 15).

1.6. Dealing with mistakes in the computation of the business income of Britannia Biscuit Co. Ltd., resulting in the under-assessment of income for the assessment year 1968-69 by Rs. 2 lakhs, the Committee, in paragraph 1.17 of the Report, had recommended, *inter alia*, as follows:

"The Committee find that this case was not checked by the Internal Audit and the familiar plea of preoccupation with other cases has again been put forth by the Department. The Committee are unhappy that effective steps are yet to be taken by the Department to ensure that the computation of income and the assessment orders themselves are pre-checked preferably by Internal Audit, particularly in large income cases of foreign companies and Indian monopoly houses, though an earlier recommendation of the Committee in this regard contained in paragraph 2.66 of their 87th Report (Fifth Lok Sabha) had been accepted, in principle, by Government as early as December 1973. In view of the large number of mistakes in the computation of assessable income which have been brought to their notice year after year, the Committee strongly reiterate their earlier recommendation and would urge Government to act upon it without further loss of time."

1.7. Again, in paragraph 2.21 of the Report, commenting on the failure of Internal Audit in not detecting the omission to levy/incorrect levy of additional tax on dividends declared or distributed in excess of a specified percentage of the paid-up equity capital by Dunlop India Ltd. and United Commercial Bank Ltd., the Committee had reiterated their earlier recommendation and had, *inter alia*, observed.

"The Committee are also concerned to note that the relevant assessments relating to Dunlop India Ltd. had not been checked by Internal Audit, while in the case of United Commercial Bank Ltd., though the assessment for the year 1967-68 had been checked in Internal Audit, the patent short-levy of additional tax was not detected. What is more distressing is that this assessment relating to a banking concern, in the high income bracket, had been scrutinised only at the level of an Upper Division Clerk who has been warned for his failure to detect the mistake. In respect of the other three assessments, the explanation offered is one which has been too often placed before the Committee, namely, that the manpower resources of Internal Audit are inadequate. The Committee desire that the existing arrangements for Internal Audit should be reviewed and remedial steps taken forthwith. The Committee would also reiterate that all large

income cases should invariably be checked at the level of the Inspecting Assistant Commissioner (Audit). The Committee are of the view that a pre-check of draft assessment orders by Internal Audit, recommended in paragraph 2.66 of their 87th Report (Fifth Lok Sabha) and reiterated in paragraph 1.17 of this Report would largely eliminate such unpardonable mistakes in assessment."

1.8. In their Action Taken Note dated 21 April 1976, furnished in reply to the recommendation contained in paragraph 1.17, the Department of Revenue & Banking (Revenue Wing) have stated:

"It has already been intimated to the Committee that it may not be practicable to carry out pre-check of assessments for the following reasons:

(a) Such a course is likely to dilute the responsibility of the assessing officer;
(b) It is also likely to cause delays in the finalisation of assessments and issue of demand notices; and
(c) It may give rise to complaints that Audit is interfering in the judicial discretion of the assessing officer.

The question of strengthening the Internal Audit Organisation has already been taken up in consultation with the Associate Finance in order to make the post-audit checks more effective. The measures spelt out in reply to paras 1.14 and 1.15 (reproduced in Chapter II) and the proposed strengthening of Internal Audit will go a long way in improving the quality of assessment work, and preventing leakage of revenue."

Reiterating this view in their Action Taken Note dated 9 June 1976, furnished in response to the recommendation contained in paragraph 2.21, the Department have stated:

"It has already been elucidated in reply to para 1.17 of this Report that it is not feasible to prescribe pre-check of draft assessment orders. However, regarding the post-checking of assessment orders involving large incomes, necessary steps are being taken for strengthening the Internal Audit Organisation, both qualitatively and quantitatively. But it may not be possible for the I.A.C. (Audit) to check all large income cases as the number of IACs (Audit) in inadequate and they have to attend to a very large number of Receipt Audit objections and draft audit paras proposed by the C & A.G., apart from other administrative matters."

1.9. **It is not clear to the Committee how the pre-check by Internal Audit of the computation of income, suggested by them with a view to eliminating repetitive mistakes which have been coming to their notice year after year, is likely to dilute the assessing officer's responsibility or give rise to complaints that his judicial discretion is being hindered. The delays in the finalisation of assessments and issue of demand notices apprehended by the Department by prescribing such a countercheck before the assessments**

are finalised can also be overcome by prescribing a suitable time limit for the completion of the pre-check. The Committee regret that the Department have hardly given careful thought to a suggestion which could have been helpful. Government will do well to have the matter properly re-examined.

1.10. **The Department's reply to another important recommendation of the Committee that all large income cases should invariably be checked at the level of the Inspecting Assistant Commissioner (Audit) is entirely unconvincing. The scrutiny of large income cases, often involving complex points of law is found too often to have been left to Upper Division Clekrs, as in the case relating to the United Commercial Bank Ltd., with results that are detrimental to revenue and not particularly complimentary to the Department. The argument that it may not be possible for the Inspecting Assistant Commissioners (Audit) to check all large income cases on account of pre-occupation with numerous Receipt Audit objections and also the draft Audit paragraphs proposed by the Comptroller & Auditor General of India does not appear valid or even particularly happy. The Department should, on the contrary, know that by ensuring careful scrutiny of large-income cases the possibility of mistakes remaining undetected would be minimised and would, in turn, lead to fewer Receipt Audit objections and draft Audit paragraphs. The Committee are, therefore, unable to accept the Department's contention in this regard and would reiterate their earlier recommendation.**

Expenditure on scientific research. (Paragraphs 1.31 and 1.33—Sl Nos. 5 and 7).

1.11. Reviewing the deductions allowed by the Income-tax Officer under Section 35(1)(i) of the Income-tax Act, admittedly without adequate scrutiny, on account of expenditure claimed to have been incurred by Britannia Biscuit Co. Ltd., towards scientific research, the Commitee, in paragraph 1.31 of the Report, had recommended :

"The Committee are distressed to find that an expenditure of Rs. 0.99 lakh on scientific research had been allowed by the Income-tax Officer in this case without making precise enquiries as to what research was actually carried out and without ensuring whether it was a genuine expenditure on research and development related to the busines of Britannia Biscuit Co. Ltd. The Committee have been informed in this connection that apart from the amount of Rs. 0.99 lakh allowed on this account for the assessment year 1968-69, further sum of Rs. 1.66 lakhs and Rs. 0.04 lakh have been allowed in respect of the assessment years 1970-71 and 1972-73 respectively. The assessments for the years 1969-70 and 1971-72 are stated to be pending and in respect of these two assessment years, Rs. 1.28 lakhs and Rs. 1.29 lakhs respectively have been claimed by the assessee company towards scientific research. The Committee desire that these claims should be carefully scrutinised by reopening the cases where necessary, in order to ensure that the permissible deductions from the taxable income are fully justified. In case it is found that there had been misrepresentation of facts and that the

deductions were incorrectly allowed, immediate action should be taken to subject the amounts to tax. The Committee would await a further report in this regard."

1.12. In their Action Taken Note dated 21 April, 1976 furnished in this regard, the Department of Revenue & Banking (Revenue Wing) have stated:

"The Income-tax Officer concerned has been directed to scrutinise the claims made in the different years carefully and submit detailed reports for considering action u/s 147(a) and/or 263. However, in view of limitation for the assessment year 1967-68 the Income-tax Officers has been directed to take immediate action u/s 147(a) as a precautionary measure. The outcome of the scrutiny of the claims will be available only after some time. The Committee will be informed of the results in due course."

1.13. Dealing further with the general issue of deductions from taxable income, allowed under Section 35(1)(ii) of the Act, of the amounts paid to a scientific research association approved by the prescribed authority, the Committee, in paragraph 1.33, had recommended as follows:

"The Committee agree with the view of Audit that in Section 35(1)(ii) of the Income-tax Act, under which any sum paid to a scientific research association, having as its object scientific research, is allowed as a deduction provided the association is recognised by the CSIR, there is a lacuna which needs to be removed. It is not unlikely that ambiguity in the legal provision in this regard has led to a tendency on the part of some big industrial houses to sponsor so-called scientific research associations with a view to claiming deductions from taxable income. The Committee, therefore, desire that the existing provisions should be reviewed and the loophole in the Act plugged forthwith. This tendency could, perhaps, also be countered by prescribing ceiling on the sums payable to research associations for the purposes of computation of income-tax."

1.14. The Action Taken Note dated 16 July 1976 furnished in this connection by the Department is reproduced below:

"With a view to ensuring avoidance of misuse of the provisions of Section 35(1)(ii) of the Income-tax Act, 1961, the prescribed authorities have taken the following measures:

(i) A Committee consisting of experts in the field of research for which approval is asked for is to satisfy itself about the genuineness of the research association and research programme they intend to carry out before recommending approval;

(ii) In most of the cases, approvals are being given by the prescribed authorities for a limited period, generally, three years to be reviewed thereafter; and

(iii) The prescribed authorities insist on the furnishing of annual reports and returns by the institutions regarding scientific research activities for enabling the prescribed authorities to have an annual review and to see that the funds received under the approval are utilised exclusively for research purposes.

The Audit have already been informed regarding the system evolved in consultation with the prescribed authorities for ensuring the proper use of the concessions vide Board's letter F.No. 203/163/75-IT A. II dated the 22nd March, 1976.

The Indian Council of Medical Research i.e. prescribed authority, have already reviewed the performance of certain institutions and have recommended withdrawal of approval in eight cases so far.

The Central Board of Direct Taxes have, on its own, issued Instruction No. 896 (F. 203/8/75-ITA. II) dated the 4th November 1975, to all the Commissioners of Income-tax enclosing a list of institutions so far approved for making proper enquiries with a view to ensuring that the utilisation of funds is made for research purposes and with a view to referring the matter to the prescribed authority for withdrawal of approval if any deviation is noticed.

The suggestion of the Committee regarding fixation of ceiling on the sums payable to research associations has been carefully considered. The amount required for carrying out a particular scientific research programme would substantially vary from one programme to another depending upon the nature and type of research proposed to be undertaken which cannot be foreseen with any substantial accuracy. In view of this, it would not be feasible to fix a ceiling on such expenditure.

It is expected that the steps taken by the prescribed authorities as well as those by the Central Board of Direct Taxes for stricter control over the utilisation of such funds will ensure better discipline among the institutions and, in case of failure, the approval granted will be withdrawn."

1.15. The Committee note that in pursuance of their recommendation contained in paragraph 1.31 of the 187th Report (Fifth Lok Sabha), the Income-tax Officer has been directed to carefully scrutinise the deductions claimed in the different years by Britannia Biscuit Co. Ltd., under Section 35(1)(i) of the Income-tax Act, and to submit detailed reports for considering rectificatory action under Sections 147(a) and/or 263 of the Act. The Committee would urge Government to complete the examination soon and adopt all consequential action under the Law.

1.16. The Committee welcome the measures stated to have been taken to ensure that the provisions of Section 35(1)(ii) of the Income-tax Act relating to payments made to scientific research associations are not abused as they appear to have been by big industrial houses. It is felt, however, that a ceiling on such payments,

as recommended by them, would have a salutary effect. The fact that it has been found necessary, on a review by the Indian Council of Medical Research of the performance of certain institutions, to withdraw the approval accorded in as many as eight cases reinforces the Committee's impression that checks and controls, if hitherto exercised in this matter, has been perfunctory. The Committee, therefore, would like Government to re-examine this question and take necessary steps to amend the law in this regard. In the meantime, the prescribed authorities under the Act and the Central Board of Direct Taxes should ensure that the regulatory apparatus functions effectively and that the various measures enumerated are strictly enforced.

Production of biscuits in excess of licensed capacity by Britannia Biscuit Co. Ltd. (Paragraph 1.43—*Sl. No.* 10)

1.17. Commenting on the abnormal production of biscuits by Britannia Biscuits Co. Ltd. over its licensed capacity, the Committee, in paragraph 1.43 of the Report had recommended, *inter alia*, as follows:

"What is more distressing is the fact that even though this question of the company producing biscuits far in excess of the licensed capacity had been raised in the Lok Sabha in 1971, no concrete action has so far been taken against the company. The Committee can not understand why the Ministry of Industrial development merely remained content with calling for the explanation of the company and referring the case to the Ministry of Law. Besides though this case had been taken up with the Ministry of Law as early as August 1974 according to the information furnished to the Committee it remains still under examination. The Committee deprecate such unconscionable delay in cases especially relating to monopoly concerns and big foreign business houses. The Committee desire that the reasons for delay should be explained and responsibility fixed for appropriate action. The Committee would like to know the final decision since taken in this case."

1.18. In their Action Taken Note dated 1976, the Department of Industrial Development have informed the Committee in this connection as follows:

"M/s. Britannia Biscuits Comany operate three units manufacturing biscuits, one each in Calcutta, Bombay and Madras. The units in Calcutta and Madras are operated under Registration Certificates issued under Section 10 of the Industries (Dev. & Reg.) Act, 1951. These Registration Certificates, as per the then procedure, did not specify a particular figures as approved capacity. The unit at Madras is run under an Industrial Licence issued under the Industries (Dev. & Reg.) Act, 1951 for an annual capacity of 1200 tonnes for the manufacture of biscuits, but without specifying the number of shifts in the day to which this figure relates.

In July 1972, the Company had applied by way of substantial expansion licence, for recognition of its reassessed capacity of

33,536 tonnes per annum of all the three units put together including the unit at Madras. In consultation with the Licensing Committee, the application of the company was rejected in February 1974. The company made a representation against the above decision of the Government claiming, *inter alia*, that its increased production was attributable to normal circumstances and that there had been no increase in the means of production and consequently no violation of the provisions of the I (D&R) Act, 1951. This representation of the company was also rejected in August 1974. The question of the action that could be taken in regard to excess production and violation of the licensing provisions that this implied was taken up and the case referred for advice to the Law Ministry immediately thereafter. The Law Ministry raised certain points for clarifications to establish whether the expansion was in violation of the provisions of the Act.

About this time, there were similar other cases engaging the attention of the Department which were also being gone into by the Law Ministry. That Ministry was of the view that the penal provisions of the Act punish only contravention of the provisions of the Act and not of the conditions, such as level of authorised production, that might have been stipulated in the Industrial Licence.

In this connection it is also relevant to point out that certain cases of production in excess of the licensed capacity have been referred for enquiry by the Commission on Large Industrial Houses (Sarkar Commission). The Commission have yet to submit its report to the Government. Government have been awaiting the findings and recommendations of the Commission to decide on the course of action to be taken in such cases of excess production, as a matter of general policy.

Government fully share the concern expressed by the Committee about the delay that has occurred in finalising the course of action to be adopted in such cases. In the circumstances explained above, the Committee would, however, appreciate the procedural and legal constraints in the way of expeditious action. Suitable amendments to the Act to enable Government to deal with such cases firmly are now being processed.

One other consideration that has had to be kept in mind in this case has been that the Government of Tamil Nadu has been strogly arguing against any decision or action that would limit production of the Madras unit of the company below levels already reached. The State Government have been frequently writing to the Central Government for recoganising and regularising the enhanced production and the capacity that has been actually installed at this unit, on the ground that it offers sizeable employment opportunities in the State.

The Committee may be assured that the matter will be gone into in all its aspects—legal, administrative and technological and

a policy decision arrived at as urgently as possible, in the light of the weighty observations contained in its 187th Report."

1.19. The Committee are concerned to observe that the question of Britannia Biscuit Co. Ltd. producing biscuits far in excess of the licensed capacity has been hanging fire for over four years now and conclusive action is yet to be taken, in a principled manner, against a big foreign business house for contravention of the condition stipulated in the industrial licence. The elaborate explanation offered by the Department of Industrial Development for the delay is also by no means convincing. The Committee find from the sequence of events relating to this case that though the company had, as early as in July 1972, applied for recognition of its reassessed capacity of 33,536 tonner per annum of its three units located at Calcutta, Bombay and Madras, Government took nearly 19 months to reject the application. A further period of six months had elapsed before the advice of the Law Ministry was sought, in August 1974, on the action that could be taken against the company for the excess production and the violation of the licesing provision that this implied. Some two years have elapsed since then and Government appear still to have preferred to await the findings and recommendations of the Commission on large Industrial Houses (Sarkar Commission) to whom certain other cases of production in excess of the licensed capacity had been referred for enquiry, so as to decide, as a matter of general policy, on the course of action to be taken in such cases of excess production. The Committee are far from satisfied with this state of affairs and must insist on this long-pending issue being finalised without delay.

1.20. The Committee note the Law Ministry's view that the penal provisions of the Industrial (Development & Regulation) Act, 1951 punish only contravention of the provisions of the Act and not of the conditions, such as the level of authorised production, that might have been stipulated in the Industrial Licence, and that suitable amendment to the Act to enable Government to deal firmly with such cases are now being processed. The Committee would urge Government to complete this exercise early and remedy an unfortunate situation without further loss of time.

Remittances on account of technical know-how fees by Dunlop India Ltd. (Paragraphs 2.23 and 2.24—Sl. Nos. 17 and 18).

1.21. Dealing with a case, relating to Dunlop India Ltd., of non-observance of the provisions of the Finance Acts relating to the levy of additional tax on dividends declared or distributed in excess of a specified percentage of the paid-up equity capital, the Committee, in paragraphs 2.23 and 2.24 of the Report, had recommended, *inter alia*, as follows:

"2.23 Another feature which has come to the notice of the Committee in respect of Dunlop India Ltd. is that the company has been remitting large sums abroad every year on the plea of reimbursement of technical know-how fees. During the seven-year period from 1965-66 to 1971-72, the remittances made on this account totalled £ 1.46 millions. In addition, the company

has also claimed to have remitted, in 1972, a sum of Rs. 2.21 lakhs alleged to represent reimbursement of technical expenses incurred by the U.K. company during the year ended 31st December 1969 and this claim, according to the information furnished to the Committee by the Department of Revenue & Insurance, is to be considered by the Income-tax Officers in the pending assessments of the two companies, namely, Dunlop India Ltd. and Dunlop Holdings Ltd., U.K., for the year 1973-74. It would appear that the Indian subsidiary company has been allowed to remit large sums as payment of technical know-how fees to the foreign holding company. While the payments for technical know-how could, perhaps, be justified during the initial period of establishment of a company, the Committee are doubtful how far the technical know-how would be relevant in the case of a well-established company like Dunlop India Ltd. in an advanced stage of development."

"2.24 The Committee would therefore, like to be satisfied that the remittances made on account of technical know-how fees by Dunlop India Ltd. were, in fact, fully justified and genuine and have not served as an instrument of tax-avoidance. The Committee desire that the technical know-how agreement entered into by the company should be thoroughly examined by the department of Revenue & Insurance with a view to determining its relevance to the Indian business of Dunlop India Ltd. and ensuring that it is not a mere cloak for tax-avoidance. In case it is found that the remittances on this account have been claimed and allowed wrongly, appropriate action should be taken."

1.22. In their Action Taken Note dated 1 July 1976, relevant to these recommendations, the Department of Revenue & Banking (Revenue Wing) have replied:

"The Commissioner of Income-tax concerned as well as the Department of Industrial Development were requested to examine the points raised in these two recommendations for necessary action. The Commissioner of Income-tax has reported that the remittances have been made by the Indian concern as consideration for the rendering by the foreign company of current technical services.

The Department of Industrial Development have informed that the matter is under consideration."

1.23. It is not very clear from the Department's reply whether the report stated to have been received from the Commissioner of Income-tax in regard to the remittances made by Dunlop India Ltd. on account of technical know-how fees/ technical expenses claimed to have been incurred by the company's counterpart in the United Kingdom, pertains only to the claim of Rs. 2.21 lakhs remitted in 1972 which was to have been considered in the pending assessments of the two companies for the year 1973-74, or to the remittances of over two crores of rupees made during the seven-year period from 1965-66 to 1971-72. If the latter be the case, the Committee

are surprised over the extraordinary expedition with which the assessments spanning several years had been reviewed and a report also furnished to the Board. In any case, since technical know-how agreements, particularly between inter-related foreign companies often serve as instruments of tax-avoidance, the Committee wish that, as desired by them earlier the Department of Revenue& Banking had taken the initiative of re-examining this case and re-assured themselves of the corrections and genuineness of the claims made by the company. Such an examination should be undertaken forthwith. The examination of the case by the Department of Industrial Development also needs to be completed quickly.

The feasibility of reopening the relevant assessments of the Company with a view to safeguarding the interests of revenue, pending final determination of the relevancy of the technical know-how agreement in the changed circumstances that may be prevailing should be decided upon.

Review of technical collaboration agreements entered into by foreign enterprises operating in India (Paragraph 2.25—Sl. No. 19).

1.24. In paragraph 2.25 of the Report, the Committee had gone on to recommend further as follows:

"The Committee are also of the view that it would be worthwhile for Government to undertake a detailed review of all such technical collaboration agreements entered into prior to 1965 by foreign enterprises operating in India and still in force, with a view to determining how far such agreements could be considered relevant to the Indian business of such enterprises concerned in the light of the developments and changes that they might have undergone since the agreements were first entered into. In case the review discloses that some of the collaboration agreements have outlived their purpose and serve only as instruments of tax-avoidance, immediate action to treat the payments of technical know-how fees in these cases as inadmissible expenditure and subject them to tax should be initiated, in addition to terminating the agreements, by invoking, if necessary, the power of eminent domain that a sovereign country enjoys. In all future technical collaboration agreements approved by the Government it should also be ensured that a clause for a periodical review of the agreements from the point of view of their relevance in the changed circumstances that may prevail is invariably corporated. The Committee attach considerable importance to these recommendations and desire that they should be implemented expeditiously."

1.25. In an interim reply dated 1 July, 1976 to the above recommendation, the Department of Revenue & Banking (Revenue Wing)informed the Committee as follows:

"Department of Economic Affairs were requested to take necessary action and intimate the results to this Department so that remedial action from the income-tax angle could be taken in suitable cases. It appears that the Department of Economic Affairs

are compiling a list of such collaboration agreements in consultation with the Reserve Bank of India. Technical collaboration agreements now approved are valid for a period of 5 years from the date of commercial production and extensions of the agreements are approved by the Foreign Investment Board in exceptional cases. In view of this position, the Department of Economic Affairs have called for the comments of the Department of Industrial Development about the need for the inclusion of a clause for a periodical review of the agreements. Their final reply in the matter is awaited."

1.26. Subsequently, in another Note dated 7th September, 1976 furnished in this regard, the Department stated:

"Attention is invited to this Department's reply of even number dated the 1st July, 1976.

The Department of Economic Affairs have offered the following comments on the recommendations of the Public Accounts Committee:

"We have consulted the Department of Industrial Development and the Reserve Bank of India, Bombay in this matter. As regards the PAC's suggestion that Government should undertake a detailed review of all technical collaboration agreements entered into prior to 1965 and still in force, we feel that it may not be necessary to appoint a group of officers to carry out the review of such cases for the following reasons:—

(a) Prior to 1965, the policy of the Government was to approve technical collaboration agreements normally for a period of 10 years. It should, therefore, be presumed that most of the collaboration agreements approved prior to 1965 would have expired by now.

(b) In October 1969, this Ministry asked the RBI to advise Indian parties to terminate their collaboration agreements which had a run of 10 years and in case the Indian parties considered it necessary to have another agreement to replace the existing one, they should make a fresh application for the purpose of consideration by the Foreign Investment Board. (A copy of the letter dated 6th October 1969 from the Department of Economic Affairs to the Reserve Bank of India on the subject was also furnished to the Committee which is reproduced in Chapter IV).

(c) The RBI have instructed their offices to insist upon specific Government's approval before allowing remittances beyoned the period for which an agreement has been approved by Government or which had a run of ten years whichever is less.

As regards the PAC's suggestion for incorporating a clause in the future technical collaboration agreements approved by Government for a periodical review of the agreements from the point of view of the relevance in the changed circumstances, the Department of Industrial Development have rightly pointed out that

such a provision will scare away the prospective collaborator, because it will create an element of uncertainty regarding the compensation which they are likely to get for technology provided to the Indian company. That Department have added that such a provision will not only inhibit the flow of technology to the Indian company but also may create legal complications, because an agreement entered into between an Indian company and the collaborator is a legal document. Moreover the duration of the agreements now approved is for 5 years from the commencement of production and when an Indian company comes up for extension of the agreement, a review of the agreement automatically takes place and this may be considered as an in-built provision for review. We agree with the Department of Industrial Development.'

It is, therefore, submitted that the concerned Government departments and the Reserve Bank of India have already evolved a procedure for review of agreements which have had [illegible] ten years. New agreements are approved [illegible] period of five years with an in-built provision for review after [illegible] years.

The Department of Economic Affairs have been requested to communicate to this Department cases where the foreign collaboration agreements are terminated on the ground that these have outlived their purposes so that consequential remedial action, if any, from the income tax angle is taken."

1.27. Government's reluctance to undertake a review of all technical collaboration agreements entered into before 1965 by foreign enterprises operating in India with a view to determining their relevancy in the changed circumstances that may prevail is difficult to appreciate. It is clear that the main thrust of the Committee's recommendation has not been properly understood by the Department of Economic Affairs. What the Committee had in view was only a review of technical collaboration agreement entered into by foreign enterprises operating in India and it was not their intention that the review extend also to the agreements entered into by purely Indian enterprises. Since the agreements of the former category are not likely to be very large in number, it should not be difficult for Government to meet the Committee's desire in this regard. In the absence of such a review and the relevant statistical data, the mere presumption that since Government policy prior to 1965 provided for the approval of technical collaboration agreements normally for a period of ten years, such agreements approved prior to 1965 would have expired by now is not enough to set at rest the Committee's genuine apprehensions arising from the facts made available to them in regard to the collaboration between Dunlop India Ltd. and Dunlop Holdings Ltd., U. K. as well as the technical service agreement entered into between National & Grindlays Bank Ltd. and the First National City Bank [which the Committee had examined in their 176th and 192nd Reports (Fifth Lok Sabha)]. Besides, it would also appear from the Department's letter dated 6 October, 1969 thatp ending a decision on the question whether the existing agreement should be allowed to continue with or without amendments, which admittedly takes 'a long time' to reach, further payments continue to

accrue to the foreign collaborator. These payments would become payable even in the event to Government deciding not to approve of the continuance of the collaboration on account of the obligation to give due notice for the termination of the agreement. The extent of benefits that would have accrued in these circumstances to the foreign collaborator by way of know-how fees and to the Indian unit of the foreign enterprise in the form of tax concessions during the period when the agreement is in suspended animation, is anybody's guess. The Committee would, therefore, reiterate their earlier recommendation in this regard and desire that the review suggested by them should be set in motion without further delay.

1.28. As regards the incorporation of a clause in all future technical collaboration agreements to provide for a periodical review from the point of view of their relevance in the changed circumstances that may prevail, it has been contended by the Department of Industrial Development that such a provision will scare away prospective collaborators and inhibit the flow of technology to the Indian company. The Department have also added that such a provision may also create legal complications. While these 'legal complications' have not been spelt out clearly and should not in any case impede execution of our national policies, the Department's somewhat meticulous concern for foreign—collaborators appears to be an anachronism, when viewed against Government's own declarations, in the recent past, for the promotion of indigenous technologies and planned phasing out of foreign collaborations. In the Committee's opinion, Government's fears in this regard are unfounded. They would, therefore, urge Government to have this issue re-examined carefully. The implementation of this important recommendation should not be difficult, particularly in the context of Government's avowed policy in this regard.

Inadequate scrutiny of books accounts of multinational corporations (Paragraph 3.32—*Sl. No.* 24)

1.29. Examining a case of incorrect computation of the business income of IBM World Trade Corporation, a giant multinational corporation enjoying almost a virtual monopoly in computers and other data processing equipment, the Committee, in paragraph 3.32 of the 187th Report, had recommended, *inter alia,* as follows :

> "It would appear that the claims preferred by the company have been readily accepted by the Income-tax Officers without any genuine scrutiny, and often the books of account of such multinational corporations are not even called for and examined properly. The representative of the Department of Revenue and Insurance stated during evidence that 'in most of the cases or a large number of cases' it would not be possible for the Department to obtain the foreign accounts from the head offices of the companies for scrutiny. This is an impermissible situation, since our Income-tax Officers are driven to rely on the accounts certified by the company's own auditors or chartered accountants. This is a situation which needs to be rectified."

1.30. In their Action Taken Note dated 15th July, 1976 furnished in pursuance of the above recommendation, the Department of Revenue & Banking (Revenue Wing) have replied :

> "This has been considered in consultation with the Ministry of Law and they have advised that the Income-tax Officer has the power to call for the books of account of head office and in case of non-production of such books, it is open to the Income-tax Officer to draw an adverse inference, and further any requisition for such accounts has to be in precise terms and not be too general or vague."

1.31. The Law Ministry's view that the Income Tax Officer has the power to call for the books of account of the head office of foreign companies operating in India and that an adverse inference could be drawn in the event of non-production of such books reinforces the Committee's impression that the important question of admissibility, from the tax angle, of the head office expenses claimed by such companies as IBM World Trade Corporation, National & Grindlays Bank etc., still remains to be examined with any seriousness. It is surprising indeed that the Department of Revenue & Banking had formed the peculiar impression that 'in most of the cases or a large number of cases' it would not be possible to obtain the foreign accounts from the head offices of the companies for scrutiny. Now that the position has been clarified, the Committee trust that suitable instructions would be issued early so that a genuine scrutiny of the claims made by foreign companies can be effected.

Scrutiny of claims made by IBM on account of head office expenses.
(Paragraphs 3.33 to 3.36—Sl. Nos. 25 to 28).

1.32. The Committee, during their examination of the Income-tax assessments of IBM World Trade Corporation, had found that large amounts had been claimed by the Company, year after year, on account of head office expenses attributable to the company's Indian operations and that these claims had been allowed in full by the Income-tax Officers without any disallowance and on the basis of inadequate scrutiny. Dealing with this question, the Committee, in paragraphs 3.33 to 3.35 of the Report had recommended *inter alia*, as follows :

> "3.33 That the Income-tax Officers, however, had failed to make a proper assessment of amounts claimed by the company as head office expenses is also borne out by the company itself coming forward, in November 1974, with a voluntary disclosure under Section 271(4A)(ii) of the Income-tax Act, 1961, admitting an excess claim on account of head office expenses for the years 1966 to 1970 to the extent of US dollars 450 thousands and submitting amended tax returns. This is, indeed, a sad commentary on the functioning of our Income-tax Department."

> "3.34 In view of the far-reaching implications of the disclosure now made by IBM World Trade Corporation that 'certain errors in the principle of allocating Headquarters Expense to India had been detected by its head office in New York' and

that 'the erroneous calculations had resulted in excess claim on account of Headquarter Expense' for the years 1966 to 1970, the Committee desire that all claims made by the company on this account relating to periods prior to 1966 and after 1970 should be subjected to a thorough scrutiny by the Investigation Cell set up by the Central Board of Direct Taxes to look into leading cases of tax evasion and malpractices. Besides, all the assessments of the company from 1960 to 1974 should also be strictly reviewed, with reference to the books of accounts of the company so as to establish the accuracy of the statements of receipts and expenditure and the genuineness of the allocation of expenditure between the Head Office of the company and the Indian unit and to ensure that no inadmissible expenditure is allowed to escape taxation and be repatriated abroad in foreign exchange. In case the review reveals that there has been a deliberate attempt by the company to evade taxes, stringent penal action under the law should be taken forthwith against the company, besides levying and collecting the tax on the income that has escaped assessment. The correctness of recognising this multinational giant as a company under the Income-tax Act should also be looked into in detail. The Committee would await a detailed report in regard to the action taken by Government on these recommendations."

"3.35 The Committee also consider it rather significant that the application under Section 271(4A), admitting excess claims on account of head office expenses, had been made by the company after the Audit paragraph had appeared in the Report of the Comptroller and Auditor General of India and after the Committee had also probed into some of the Indian operations of IBM World Trade Corporation in their 127th Report (Fifth Lok Sabha) on the installation of IBM computers on Indian Railways, which was presented to the Lok Sabha in April 1974. Besides, the affairs of the Company have also been taken up for scrutiny by an inter-Ministerial Working Group constituted by the Department of Electronics. Under these circumstances, the Committee have grave doubts whether the disclosure made by the company only in November 1974 could be treated as voluntary and not as one prompted by the fear of exposure. The Committee would, therefore, recommend that pending the completion of the comprehensive review suggested in paragraph 3.34 above, the application made under Section 271(4A) of the Income-tax Act should be kept pending so that the assessee company does not excape the consequences of penalty and prosecution proceedings for claiming excess expenditure in a manner which, *prima facie,* appears to be dubious and even deliberate."

1.33. With reference to their observations contained in paragraph 3.33, the Committee have been informed by the Department of Revenue & Banking (Revenue Wing), in their Action Taken Note dated 15th July, 1976 that these 'have been noted'. As regards the recommendations contained in paragraph 3.34, the Department, in an interim reply dated 28th June, 1976, have stated :

"The Special Cell has been directed to have investigations in this case completed in consultation with the Commissioner of Income-tax

on a priority basis. The correctness of recognising this multinational corporation as a company under the Income-tax Act is also being examined."

1.34. The Action Taken Note dated 28th June, 1976 furnished by the Department in response to the recommendation contained in paragraph 3.35 is reproduced below :

"The Department of Electronics have been requested to send us a copy of the report of the Inter-Ministerial Working Group set up to look into the affairs of IBM World Trade Corporation. Meanwhile, the application u/s 271 (4A) of the Income-tax Act, 1961 is being kept pending."

1.35. The Committee note that the Special Cell set up in the Central Board of Direct Taxes has been entrusted with the task of investigating, on a priority basis, the claims made by IBM World Trade Corporation on account of head office expenses and that the correctness of recognising this multinational Corporation as a company under the Income-tax Act is also being examined. They would like these investigations to be completed quickly. As regards the question of recognising the corporation as a company under the Act, the Committee would invite attention to their observation contained in paragraphs 6.1.72 and 6.1.73 of their 221st Report (Fifth Lok Sabha). The stage at which the application made by the company under Section 271(4A)(ii) of the Income Tax Act stands at present should be intimated to the Committee forthwith.

1.36. In paragraph 3.36 of the Report, the Committee had further recommended as follows :

"Now that an inter-Ministerial Working Group has also been appointed to examine in detail the policies and procedures under which IBM World Trade Corporation operates in India, the Committee desire that the entire issue of head office expenses claimed by the company and the remittances made by it should be gone into by the Working Group with a view to quantifying, in concrete and specific terms, the extent to which the country's scarce foreign exchange resources have been frittered away and exposing all the devious methods employed by this multinational corporation to the detriment of the country's wider national interest."

1.37. In their Action Taken Note dated 14th July, 1976, the Department of Revenue & Banking (Revenue Wing) have replied :

"As has already been stated in reply to para 3.35 of this Report, the Department of Electronics have been requested to send a copy of the report of the Inter-Ministerial Working Group."

1.38. The Committee find that the reply furnished by the Department of Revenue & Banking to their recommendation contained in paragraph 3.36 of the 187th Report (Fifth Lok Sabha) that the entire issue of head office expenses claimed by IBM World Trade Corporation should be gone into by the inter-Ministerial

Working Group appointed to examine the policies and procedures under which company operates in India is not quite relevant. What the Committee had wanted was that this aspect should be included as one of the specific terms of reference of the Working Group. Action in this regard should be initiated forthwith so that all the devious methods adopted by the company to the detriment of the country's wider national interest are adequately exposed and appropriately dealt with.

Irregular extension of benefits admissible to priority industries to the manufacture of intermediate products (Paragraphs 4.22 and 4.23—Sl. Nos. 32 & 33).

1.39. Dealing with a case of irregular extension of the benafits admissible to priority industries, under Section 80/E/I of the Income-tax Act, and of higher development rebate available to the petro-chemical industry, to J.K. Synthetics Ltd., the Committee, in paragraph 4.22 and 4.23 of the Report, had observed, *inter alia*, as follows :

"4.22 The Committee view with concern the irregular extension of the benefits admissible to priority industries, under Section 80/E/1 of the Income-tax Act, and of higher development rebate permissible to the petrochemical industy, to a company (J. K. Synthetics Ltd.), controlled by a monopoly house, manufacturing nylon yarn, which is only a product derived from the petrochemical base, caprolactum. This has resulted in a short-levy of tax amounting to Rs. 73.57 lakhs for the three assessment years 1967-68 to 1969-70. In addition, an interest of only Rs. 1.05 lakhs had been levied, under Section 139 of the Income-tax Act, for the belated filing of the return of income for the assessment year 1968-69, as against Rs. 1.55 lakhs actually leviable."

"4.23 The Committee find that a strange procedure appears to have been adopted in this case by the Income-tax Officer who made the original assessment for the years 1967-68 to 1969-70 by asking the Indian Institute of petroleum. Dehradun, for a technical opinion on the subject when it would have been more appropriate to refer the case, if there was any doubt, to the Chief Chemist, Central Revenues Control Laboratory, New Delhi. In fact, when the Chief Chemist was consulted subsequently, in December 1973, he had categorically opined that Nylon-6 manufactured from caprolactum, being a finished article, was not covered by the term 'petro-chemical' referred to in item 18 of the Sixth Schedule to the Income-tax Act. Expert opinion apart, it is evident, from the purely common sense point of view, that the manufacture of intermediate of finished products from a basic petro-chemical, especially when the raw material base itself is manufactured elsewhere or is imported, cannot be deemed to be a petro-chemical, industry qualifying for the benefits of pririty industries. If one were to apply logically the standard adopted in this case by the Income-tax Officer initially then almost every article or product manufactured out of petro-chemicals should be subject to concessional rates *of tax, which would be clearly against the letter and spirit of the* concession given by the Parliament."

1.40. The Action Taken Note dated 28th June, 1976, furnished in this regard by the Department of Revenue & Banking (Revenue Wing) is reproduced below :

> "The observations of the Committee have been noted. However on an appeal filed by the company against the CIT's order under section 263 for the assessment year 1968-69, the Appellate Tribunal has held by its order dated 31-10-1975 that there was no justification in taking action u/s 263 withdrawing the relief allowed under section 80-I and the higher development rebate allowed u/s 33(1)(b)(B). It has further held that even on merits, Nylon-6 is a petro-chemical and is covered by item 18 of the Fifth and Sixth Schedules of the Income-tax Act. A reference application filed by the Income-tax Department u/s 256(1) requesting the Tribunal to refer the case to the High Court has also been rejected. The question of filing a reference u/s 256(2) before the High Court is under consideration."

1.41. **The Committee note that the Income-tax Appellate Tribunal has held, by its order dated 31st October, 1975, that there was no justification in taking acton, under Section 263 for the assessment year 1968-69, withdawing the relief allowed to J. K. Synthetics Ltd. under Section 80-I as well as the higher development rebate allowed under Section 33(1)(b)(B). Besides, it had also held that even on merits, Nylon-6, manufactured from caprolactum, is a petro-chemical and is covered by item 18 of the Fifth and Sixth Schedules of the Income-tax Act. A reference application (filed by the Department, under Section 256(1), having been rejected by the Tribunal, the question of filing a reference under Section 256(2) before the High Court was under consideration. Considerable time has elapsed since then. The Committee trust that an early decision will be taken by the Department in this matter.**

Non-disclosure by J.K. Synthetics Ltd., of refund received (Paragraph 4.29—Sl. No. 39)

1.42. During their examination of paragraph 34 of the Report of the Comptroller and Auditor General of India for the year 1972-73, Union Government (Civil), Revenue Receipts, Volume I, Indirect Taxes, the Committee had learnt that a large refund of Central Excise duty amounting to Rs. 1.37 crores had been granted, on revision, to J.K. Synthetics Ltd. Drawing the attention of the Central Board of Direct Taxes to this refund, the Committee, in paragraph 4.29 of their 187th Report, had observed :

> "The Committee had also had occasion to examine separately the grant of a large refund of Central Excise duty amounting to Rs. 1.37 crores, on revision, to J.K. Synthetics Ltd., The Committee have been informed by the Central Board of Direct Taxes that the Commissioner of Income-tax had been instructed, on 7th May, 1974, to look into this matter and verify that the refund had been fully accounted for in the books and the returns of income. A long time has passed since then, and the Committee would like to be apprised immediately of the results of the verification."

1.43. In their Action Taken Note dated 28th June, 1976, the Department of Revenue & Banking (Revenue Wing) have informed the Committee as follows :

> "The assessee company had received a sum of Rs. 1,36,78,459 as refund of Central Excise Duty during September/ December 1972. A further sum of Rs. 68,84,365 became due to the company but was not paid by the Central Excise Department. These amounts were neither shown in the P & L a/c nor in the returns of income. The entire question of assessing these refunds to Income-tax is under examination in detail during the course of pending assessment proceedings for the assessment year 1973-74."

1.44. **The Committee are surprised that a large sum of Rs. 1.37 crores received by J. K. Synthetics Ltd. as refund of Central Excise duty during September-December 1972 as well as a further sum of Rs. 68.84 lakhs which became due to the company on this account had not been disclosed either in their Profit & Loss Account or in the returns of income. The Committee expect that while examining in detail the question of assessinng these refunds to Income Tax during the course of pending assessment proceedings for the assessment year 1973-74, the question whether there has been deliberate concealment of Income will also be gone into.**

Postponement of collection of additional tax due from the Calcutta Electri Supply Corporation. (Paragraph 4.84—Sl. No. 47)

1.45. In paragraph 4.84 of the Report, the Committee had further observed as follows :

> "Another unhappy feature of the case under scrutiny is that the collection of the additional tax due from Calcutta Electric Supply Corporation should have been kept in abeyance by the Commissioner of Income Tax till the disposal of the first appeal filed by the company before the Income-tax Appellate Tribunal. The Committee are distressed that an extra-legal concession, and that too without obtaining any security for the additional demand, should have been extended to a defaulting but powerful and long entrenched foreign company on the basis of what has been described as 'the usual departmental practice.' The Chairman of the Central Board of Direct Taxes as well as the Commissioner of Income-tax, West Bengal-I, have admitted, before the Committee that if the Department wanted to and did take 'a very stern and rigid view of the matter', the recovery could be pressed and enforced. The Committee desire that, principled action, even on occasion, 'very stern and rigid' should be taken, which, it is feared, did not happen in this case. It would be of interest to know in how many cases a similar concession had been extended, if only as a matter of convention, by the Income-tax Department to the multitude of small assessees."

1.46. In their Action Taken Note dated 26 July 1976, the Department of Revenue & Banking (Revenue Wing) have replied :

"In this case the very basis of the jurisdiction of the Income-tax Officer to make fresh assessments stood challenged in appeal before the Income-tax Appellate Tribunal. As the assessee company had substantial assets and had not defaulted in the past, the Department did not expect any risk to revenue in granting the stay for payment of additional demands raised in fresh assessment proceedings. In granting such stays the furnishing of security is insisted upon only if there is any chance of loss of revenue. It my, however, be mentioned that granting stay of demand without any security is a fairly common practice."

1.47. Though the Committee, in paragraph 4.84 of their 187th Report (Fifth Lok Sabha) had specifically enquired into the number of cases relating to small assessees in which a stay of demand had been granted by the Department's if only as a matter of convention, they find the Department's reply in this regard to be vague. The Committee apprehend that this extra-legal concession is liable to be exploited more in the interests of large income assessees. The Department should examine the legality and wisdom of persisting with what has been described as 'the usual departmental practice'.

Failure on the part of supervisory officials to review a large income case. (Paragraphs 6.31 and 6·33—Sl. Nos. 64 and 66).

1.48. Examining a case relating to Gwalior Rayon Silk Manufacturing (Wvg.) Company Limited, the Committee, in paragraph 6.31 of the Report had recommended, *inter alia*, as follows :

"It is also surprising that neither the Inspecting Assistant Commissioner nor the Commissioner had looked into this case, even though the charge in which the case had been assessed does not appear to have more than a few large income cases of this type. The Committee would like Government to find out whether the supervisory officials had inspected the ward in which the case was assessed at any time after the assessment had been made and, if so, how this particular case had escaped their notice. In case there has been any remissness on their part in this regard, appropriate action should be initiated."

1.49. In their Action Taken Note dated 28 July 1976, the Department of Revenue & Banking (Revenue Wing) have replied :

"There is no doubt that this was t e biggest revenue yielding case in that Charge. The case of this company has always been handled by a senior Income-tax Officer and was being subjected to checking by the Internal Audit annually. Unfortunately, there has been a failure on the part of the supervisory officials to inspect this case during the said period. Moreover, there had been a difference of opinion on the correct interpretation of Rule 3 of the Second Schedule to the Companies (Profits)

Surtax Act, which was set at rest in April 1974. In the circumstances, no action is considered necessary against any official. Of late, a number of steps have been taken to avoid such mistakes. In this connection the Department's reply to para 1.8 of 192nd Report may be referred to."

1·50. **Since it has been conceded by the Department of Revenue & Banking (Revenue Wing) that there has been a failure on the part of the supervisory officials to inspect the case relating to Gwalior Rayon Silk Manufacturing (Wvg) Company Limited, even though this was the biggest revenue yielding case in that Charge. The Committee are unable to accept the plea that no action is considered necessary against any official for this failure. In view of the fact that responsible supervisory officers have been remiss in the discharge of the responsibilities cast on them, the Committee would reiterate that appropriate action should be taken.**

1·51. Dealing further with this case, the Committee, in paragraph 6·33 of the Report, had gone on to recommend as follows :

> "The Committee find that Gwalior Rayon Silk Manufacturing (Wvg.) Co. Ltd., is being assessed at Indore even though most of the assessments relating to the Birla Group of companies are centralised in Central Circles or Special Circles in Bombay and Calcutta and a special cell has also been set up in Delhi to deal with the income tax cases of this group. The response of the Ministry of Finance to an enquiry by the Committee into the reasons for this arrangement is a surprising silence. The Committee are of the view that the Income tax cases of this company should also be transferred to the special cell at Delhi so that all ramifications which this particular unit of the Birla Group may have with the other units of the group could be unravelled and properly looked into."

1·52. The Action Taken Note dated 28 July 1976 furnished in response to this recommendation by the Department of Revenue & Banking (Revenue Wing) is reproduced below :

> "The investigations in Gwalior Rayon Silk Manufacturing (Wvg.) Company Limited as also other cases of the Birla Group, wherever assessed, are presently being supervised by the Special Cell under the Directorate of Inspection (Investigation), Delhi."

1·53. **The Committee note that the investigations relating to Gwalior Rayon Silk Manufacturing (Wvg.) Company Limited are presently being supervised by the Special Cell under the Directorate of Inspection (Investigation). They, however, find that the reasons for not centralising the assessments relating to this company in a Central or Special Circle, as has been done in the case of other assessments relating to the Birla Group of companies, specifically enquired into by them, are yet to be intimated. The position requires to be fully clarified without delay.**

CHAPTER II

RECOMMENDATIONS/OBSERVATIONS THAT HAVE BEEN ACCEPTED BY GOVERNMENT

Recommendations

The Committee note that in computing the business income of Britania Biscuit Co. Ltd. for the assessment year 1968-69. the Income-tax Officer had added back to the net profit a sum of Rs. 20,93,532 instead of Rs. 22,93,532 actually debited to the Profit and Loss Account in respect of 'depreciation' resulting in under-assessment of income by Rs. 2 lakhs and that the mistake has been attributed to inadvertence on the part of Income-tax Officer. The Committee are disturbed to find that serious mistakes on account of negligence continue to recur every year. That this should be so despite repeated comments made in this regard in the earlier reports of the Public Accounts Committee and the assurances given by the Ministry of Finance that steps would be taken to avoid the recurrence of such mistakes, is regrettable. Such repetitive mistakes indicate that the instructions even of grave import, issued by the Central Board of Direct Taxes are not taken seriously enough by the assessing officers.

The Committee are concerned that no review having been undertaken by the Central Board of Direct Taxes regarding the effect of the Board's Instruction No. 598, dated the 25th August, 1973. The Board's responsibility does not end with merely issuing instructions based on the recommendations of the Committee. There should be regular review of such instructions to ensure that they were being implemented in the field. The Committee desire that the Central Board of Direct Taxes should undertake such a review and take all necessary remedial measures.

[S. Nos. 1, 2, Paras 1·14, 1·15 of Appendix IV of 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

The observations of the Committee in para 1·14 have been noted. Necessary instructions for preventing the recurrence of such mistakes have already been issued as stated in para 1·15. The Director of Inspection (Income-tax & Audit) has been directed to carry out a review of the impact of the Board's instructions. The review has not yet been completed. In the meantime, a quarterly bulletin incorporating important audit objections raised by both Internal as well as Receipt Audit is being issued for the guidance of assessing officers so that they may guard against mistakes of the nature pointed out therein. This is expected to serve as a constant reminder to be vigilant in completing the assessment.

[Department of Revenue & Banking No. 236/90/73-A &PAC II dated 21-4-1976].

Recommendation

In the instant case, the Committee have been informed that the return had been filed by Britania Biscuit Co. Ltd. on 26th September, 1968 and the assessment was completed only on 25th February, 1972. It would, therefore, appear that after having kept the assessment pending for more than three years it was completed in haste without adequate scrutiny and only when the assessment was to become time-barred. This indicates a kind of a chaos in the system of work and a failure to realise the importance of accuracy and expedition in completing cases, especially those with large revenue implication. The Committee desire that the existing methodology adopted by Income-tax officers for disposal of cases should be carefully examined and adequate measures taken to specify priorities of work allocation and disposal. The Committee's earlier recommendation contained in paragraph 1.72 of their 119th Report (Fifth Lok Sabha) is relevant in this regard.

[S. No. 3 (Para 1.16) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)]

Action taken

Kind attention of the Committee is invited to the Department's reply to S. No. 8 (Para 10.5) of the Appendix to 186th Report of the P.A.C. wherein the various steps taken by the Department are set out.

2. With the introduction of Section 144A and 144B in the Income-tax Act, 1961, it would now be possible for the Income-tax Officer to seek the guidance of his Inspecting Assistant Commissioner at the pre-assessment stage itself which will ensure quicker disposal of cases after proper scrutiny.

3. Instructions have also been issued to the Commissioners of Income-tax asking them to ensure completion of time-barring assessments of the firms by 30th September, 1976 so that a reasonable time is available for completing assessments of the partners after complying with the provisions of Section 144B of the Act. A copy of Instruction No. 948 dated the 26th April, 1976 is attached for Committee's perusal.

[Department of Revenue and Banking No. 236/90/73-A & HC-II dated 16-7-1976]

F. No. 236/90/73-A & PAC-II (F. 228/7/76-ITA-II) dated the 16th July, 1976.

(C O P Y)

MOST IMMEDIATE

INSTRUCTION No. 948

F. No. 201/21/76-IT (AII)
GOVERNMENT OF INDIA
Central Board of Direct Taxes

New Delhi, the 26th April, 1976

To

All Commissioners of Income-tax.

SUBJECT :— Forwarding of Draft Assessment orders in the case of partners under section 144B of the Income-tax Act, 1961—clarification regarding—

Sir,

Reference is invited to Board's Instruction No. 907 dated the 24th December, 1975 (F. No. 201/12-75-IT (AII) outlining the new assessment procedure as introduced by section 144A and 144B of the Income-tax Act, 1961. A copy of Board's order of even number dated the 23rd December, 1975 fixing the variation limit at Rs. 1 lakh for purposes of section 144B was also forwarded along with this Instruction.

2. A question has been raised where in completing the assessment of a firm under section 143(3), the Income-tax Officer proposes to make an addition to the returned income exceeding Rs. 1 lakh and as a result of the proposed addition in the firm's assessment, the share of income of any partner or partners is enhanced by an amount exceeding Rs. 1 lakh, whether the draft assessment order in the case of such a partner will be required to be forwarded under the provisions of Section 144B of the Act. The Board is of the view that the provisions of section 144B of the Act would be applicable to the case of partners as well, if the share of income stand enhanced by Rs. 1 lakh on the basis of the determined share of income in the case of the firm.

3. In view of this legal position, the Board have decided that time barring assessments of the firms must be completed by the 30th September 1976 so that reasonable time is available for completing assessments of the partners after complying with the provisions of section 144B of the Act. You may kindly issue necessary instructions to the Income-tax Officers to adhere to this time limit scrupulously. The Inspecting Assistant Commissioners may be directed to ensure that the Income-tax Officers take immediate steps for completing the assessments of the firms for the assessment year 1974-75 by 30th September 1976 and to keep a constant watch over the progress of such assessments.

4. If for any unavoidable reasons, it is not possible to complete the assessments of the firm early enough to give the Income-tax officer the time necessary for complying with the requirements of the section 144B in the case of the partners, the partners assessments may be completed on the basis of the returned income in respect of their share in the firm subject to rectification under section 155(1) when the firm's assessment is finalised. This procedure should be resorted to *only in exceptional cases and not as a matter of course.*

5. You are also requested to furnish details of the cases of the partners completed before 1-4-1976 where provisions of section 144B were applicable because the determined share of income from the registered firm was more than Rs. 1 lakh in comparison to the disclosed share of income, but the procedure laid down in the said section was not followed. You may kindly indicate the number of such cases along with the tax effect involved on account of variation in the disclosed share of income and/or loss in comparison to the determined share of income/or loss. This information may kindly be furnished by 1st June, 1976.

6. Please acknowledge receipt of this letter.

Yours faithfully,

Sd/-

(T. P. JHUNJHUNWALA)

Secretary, Central Board of Direct Taxes.

Copy forwarded to :—

1. The Comptroller & Auditor General of India (25 copies).
2. Bulletin Section (3 copies).
3. All Officers/Sections of Central Board of Direct Taxes.
4. Director of Inspection (Income-tax & Audit)/Investigation/Research & Statistics/Publication & Public Relations, New Delhi.
5. Director of O & M Services (Income-tax), 1st Floor, Aiwan-e-Ghalib, Mata Sundri Lane, New Delhi.
6. Shri M. B. Rao, Joint Secretary & Legal Adviser Ministry of Law & Justice, New Delhi.

Sd/-

(T. P. JHUNJHUNWALA)

Secretary, Central Board of Direct Taxes.

Recommendation

It is surprising that the Central Board of Direct Taxes have not considered it necessary to issue guidelines on what constitutes expenditure on scientific research for the guidance of the assessing officers. The Committee desire that this should be examined in depth and specific

instructions issued immediately so that ambiguities could be avoided and uniformity in assessment ensured.

[S. No. 6 (Para 1.32) of Appendix IV to the 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)]

Action taken

Scientific research has been specifically defined in Section 43(4) of the Income-tax Act, 1961 and the decision of the prescribed authority as to whether, and if so, to what extent, any activity constitutes or constituted, or any asset is or was being used for scientific research, is final *vide* sub-section (3) of Section 35 of the Act *ibid*. However, the Board have issued a confidential letter in March 1975 laying down broad guidelines and instructing the assessing officers to review such cases. The results of review indicate that mistake was noticed in 3 cases involving a tax effect of Rs. 7·68 lakhs for which remedial action has been initiated.

[Department of Revenue & Banking No. 236/90/73/A & PAC-II dated 23-4-1976]

Recommendation

The Committee also note that the Department of Science and Technology propose to set up a group to oversee the functioning of research institutions approved by them, so as to ensure that such institutions actually utilise the contribution received by them for the purpose for which they are given. The Committee would like to know the action so far taken in pursuance of this objective.

[Sr. No. 8 (Para 1.34) of Appendix IV to 187the Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)]

Action taken

For overseeing the functioning of the scientific research associations/institutions approved by CSIR/Secretary, DST the following action has been commenced :

(a) A group has been set up in the Department of Science & Technology for reviewing the annual returns received from the approved institutions/associations.

(b) After the scrutiny of these returns action will be initiated for the withdrawal of the approval where considered appropriate.

(c) Approvals granted to the scientific research associations/institutions set up by the business houses are usually being restricted to a limited period of 3 years at a time, so as to enable this Department to review the progress of the scientific research programmes of such institutions thoroughly before grant of renewals.

[Department of Science & Technology No. 4/3/76-R.A.].

Recommendation

The Committee would further urge that Department of Revenue & Insurance investigate immediately whether there has been any leakage of excise and customs revenues in respect of this company. The Committee would await a further report in this regard.

[Sr. No. 11 (Para 1.44) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

Central Board of Excise & Customs have ascertained from the Central Excise Department that no evasion of Central Excise duty by this Company has come to their notice.

2. All the Collectors of Customs, except the Collector of Customs, Calcutta have also reported that no case of evasion of Customs Duty by this Company has come to their notice. However, in this connection this Department's reply to para 1.42 may please be referred to.

[Department of Revenue and Banking F. No. 241/13/76-A & PAC II dated 19-7-1976].

Recommendations

The Committee view with serious concern the two cases of failure to levy/incorrect levy of additional tax on dividends declared or distributed on equity shares in excess of the specified percentage of the paid-up equity share capital as on the first day of the relevant previous year, resulting in short levy of tax amounting to Rs. 10.23 lakhs. In the first case relating to a company under foreign control (Dunlop India Ltd.), the Committee find that instead of levying the additional tax with reference to the paid-up equity capital of Rs. 8 crores as on the first day of the previous year relevant to the assessment year 1967-68, the tax had been computed after incorrectly taking into account the bonus shares valued at Rs. 2 crores issued towards the end of the previous year, thus resulting in a short levy of tax by Rs. 1.5 lakhs for the assessment year 1967-68. Again, in respect of the same company, no additional tax, which works out to Rs. 5.63 lakhs, had been levied on the equity dividends of Rs. 1.75 crores declared/distributed by the company during the previous year relevant to the assessment year 1967-68.

In the second case pointed out by Audit, which related to an Indian banking concern (United Commercial Bank Ltd.), the Committee find that the additional tax had not been levied on the dividends of Rs. 24.56 lakhs declared/distributed during the previous year relevant to the assessment year 1964-65 and had been incorrectly levied on the dividends declared/distributed during the previous year relevant to the assessment year 1967-68. These mistakes had resulted in a short levy of Rs. 3.10 lakhs.

The Committee are informed that the lapses pointed out by Audit have been accepted by the Department and necessary rectifications carried out. While the Committee note that the Central Board of Direct Taxes took prompt action to rectify mistakes pointed out by the Central Receipt Audit, they cannot ignore the basic issues involved in such recurrent cases

of under-assessment pointed out in test audit year after year. The Committee have been informed that both these cases were assessed in Company Circles which admittedly, have fewer cases for disposal and are manned by experienced senior officers. Such an arrangement is apparently designed to ensure that large income cases of the type commented upon by the Audit are thoroughly and properly scrutinised before the assessments are finalised. That mistakes of the nature pointed out by Audit should continue to recur, despite such an arrangement, would lead the Committee to infer that either the requisite competence is lacking in the officers posted to Company Circles or that such mistakes are deliberate and mala fide. The Committee, therefore, desire that the circumstances leading to the under-assessments in these two cases should be thoroughly investigated. The Committee are of the view that appropriate action is also called for against the officers, including those at the supervisory level, who have apparently been negligent in the discharge of their duties.

[S. Nos. 12-14 (Paras 2.18 & 2.20) of Appendix IV to the 187th Report of the Public Accounts Committee (1975-76)]

Action taken

The Department share the concern expressed by the Committee regarding the failure of the assessing officers to correctly apply the provisions of law. However, in view of the fact that the levy of additional tax has been discontinued with effect from assessment year 1969-70, no further action is called for in this respect.

The officers concerned have admitted their mistakes without reservations and they have been warned to be careful in future. As the mistakes were reported to be *bona fide,* no further action has been taken against the officers.

[Department of Revenue & Banking No. 236/7/73-A & PAC II dated 9-6-1976].

Recommendation

The Committee have been informed that Dunlop India Limited had gone in appeal in respect of computation of the company's income for the assessment year 1967-68, as a result of which the total taxable income had been reduced. It appears that one of the grounds of appeal related to the additions made on account of exchange fluctuations. The Committee understand that the question of assessability or non-assessability of profits accruing out of exchange transactions is not a simple issue and that in many cases, courts of law have upheld assessments of gains on exchange transactions. The Committee would, therefore, like to know whether Government have contested the order of the Appellate Assistant Commissioner in the present case.

[Sr. No. 16 (Para 2.22) of Appendix IV of 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)]

Action taken

The Income-tax Appellate Tribunal have allowed the Departmental appeal against the order of the Appellate Assistant Commissioner of Income-

tax. The assessee- company has moved the I.T.A.T. for making a reference to the High Court which has been opposed by the Income-tax Department.

[Department of Revenue and Banking No. 236/7/73-A & PAC II dated 28-7-1976].

Recommendations

This is yet another case relating to the assessment of a foreign company operating in India (IBM World Trade Corporation), which is a gaint multi-national corporation, enjoying almost a virtual monopoly in computers and other data processing machines. The gist of the audit objection in this case is that instead of apportioning the deductions allowed on account of the head office expenses attributable to the operations of the Indian branch on a time-basis as and when the Indian branch became liable to bear the expenditure incurred on its behalf by the head office and then applying the exchange rate prevailing during the relevant periods, the Income-tax Officer had converted the dollar expenses for the whole of the calendar year 1966 at the post-devaluation rate. It has been pointed out by Audit that this failure to apportion the expenses to the pre-devaluation and post-devaluation periods had resulted in an excess allowance of expenses in the assessment of the Indian branch amounting to Rs. 7.46 lakhs and consequential short-levy of tax on Rs. 5.22 lakhs for the assessment year 1967-68.

The Committee note that the Audit objection has not been accepted by the Department of Revenue & Insurance mainly on the ground that in this case, the liability on account of expenses incurred by the head office of the Indian branch of IBM World Trade Corporation crystallised yearly at the end of the accounting period and not on different dates during the accounting period and, therefore, the deduction had to be allowed for a sum calculated at the exchange rates prevailing at the end of the accounting period. In support of this contention, the Department have stated that the company had 'affirmed' that the debits on account of head office expenses allocable to the Indian branch had been received only in December by a single debit note.

In the opinion of the Committee, this affirmation by the foreign company can at best be considered an after thought. No independent investigation appears to have been conducted in order to find out how often such debit notes had been received by the Indian unit of the company. Since the expenditure incurred by the head office was ascertainable, the logical and proper course in such a situation would be to value the liability of the Indian unit towards head office expenses at various rates of exchange, on a time-basis, with reference to the periods when the liabilities actually arose. The Committee have also been informed by Audit in this connection that a similar objection relating to M/s. Harrison & Cross-field (P) Ltd., had been earlier accepted by the Ministry who had then conceded that the correct procedure would be to allocate the expenses on a time-basis and apply the conversion factor by splitting up such expenses into relevant periods. Under these circumtances, the Committee are unable to approve the Ministry taking a different stand in the present case. The Committee desire that this case should be re-examined, in consultation with Audit and the outcome reported to them. Pending re-examination

of the case, the assessment should be rectified as a measure of abundant caution, in the light of the Audit objection.

Apart from this instance of under-assessment, the broader issue of remittance made abroad by IBM World Trade Corporation year after year on account of head office expenses causes even greater concern to the Committee. The Committee find that in respect of the assessment years 1967-68, 1968-69, 1969-70 and 1970-71, the company had claimed Rs. 46.92 lakhs, Rs. 45.95 lakhs, Rs. 50.24 lakhs and Rs. 56.76 lakhs respectively towards head office expenses directly attributable to the Company's Indian operations and that these claims had been admitted by the Income-tax Officers without any disallowance. Further, the remittance allowed by the Reserve Bank of India as head office expenses relating to the six-year period from 1965 to 1970 total US dollars 40.06 lakhs and these claims are also stated to have been admitted by the Income-tax authorities. According to a study note prepared by the Department of Revenue & Insurance on 'Head Office Expenses', the deduction claimed by IBM World Trade Corporation on account of head office expenses for the assessment year 1969-70 worked out to 78 per cent of the book profits prior to the charge of these payments. If this is any indication of the quantum of remittances allowed in respect of this company, then it would follow that a major portion of the surplus earned by the company by its Indian operations has been allowed to be repatriated abroad tax-free. Such a situation has also been facilitated to a certain extent by the fact that no ceiling has been prescribed by Government on remittances towards head office expenses and whatever amount is admitted by the Income-tax authorities is allowed to be remitted abroad by the Reserve Bank of India.

It would appear that the claims preferred by the company have been readily accepted by the Income-tax Officers without any genuine scrutiny, and often the books of account of such multinational corporations are not even called for and examined properly. The representative of the Department of Revenue & Insurance stated during evidence that 'in most of the cases or a large number of cases' it would not be possible for the Department to obtain the foreign accounts from the head offices of the companies for scrutiny. This is an impermissible situation, since our Income-tax Officers are driven to rely on the accounts certified by the company's own auditors or chartered accountants. This is a situation which needs to be rectified.

That the Income-tax Officers, however, had failed to make a proper assessment of amounts claimed by the company as head office expenses is also borne out by the company itself coming forward, in November, 1974, with a voluntary disclosure under Section 271(4A)(ii) of the Income-tax Act, 1951, admitting an excess claim on account of head office expenses for the years 1966 to 1970 to the extent of US dollars 450 thousand and submitting amended tax returns. This is indeed a sad commentary on the functioning of our Income-tax Department.

[S. Nos. 20 to 25 (Paras 3.28 to 3.33) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)]

Action taken

The Commissioner of Income-tax concerned has reported that on receipt of the Local Audit Objection, the assessment for 1967-68 was rectified u/s 154 of the Income-tax Act, 1961, but the assessee's appeal against

this order was allowed by the Appellate Assistant Commissioner of Income-tax. The Department has preferred an appeal to the Income-tax Appellate Tribunal which is pending. The assessment for 1967-68 has been re-opened on account of the assessee having filed a petition u/s 271(4A) of the Income-tax Act, 1961 and at the time of framing the re-assessment, the question of admissibility of Head-Office expenses will be examined.

As regards the recommendation that the case should be re-examined in consultation with Audit, the Committee's recommendation has been noted. The representatives of Audit were requested to attend a meeting to discuss the matter, but they have suggested that the meeting may be arranged after the results of the Department's investigations are available.

The Income-tax Act, 1961 has since been amended by the Finance Act, 1976 to provide a ceiling on the head office expenses which can be claimed by non-residents in their tax assessments in India, *vide* Section 44C of the Income-tax Act, 1961.

This has been considered in consultation with the Ministry of Law and they have advised that the Income-tax Officer has the power to call for the books of account of head office and in case of non-production of such books, it is open to the Income-tax Officer to draw an adverse inference, and further any requisition for such accounts has to be in precise terms and not be too general or vague.

The observations of the Committee have been noted.

[Department of Revenue and Banking No. 236/274/73-A&PAC II dated 15-7-1976].

Recommendation

In view of the fact that there has been a substantial increase in the remittances made by foreign companies towards head office expenses during the years 1965—69, the Committee feel that it would be worthwhile for Government to review the veracity of the claims admitted during this period in respect of other foreign companies and banks as well. Since such a review is likely to yield rich dividends, the Committee desire that it should be undertaken forthwith, and would await a detailed report in this regard. It is, however, regrettable that the Central Board of Direct Taxes had not taken up so far a careful study of this problem with a view to ascertaining its magnitude and taking adequate steps to ensure proper tax compliance.

[S. No. 31 (Para 3.39) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)]

Action taken

All the Commissioners of Income-tax have been asked to review the veracity of the claims made by foreign companies in the light of the detailed instructions contained in Board's letter F. No. 491/8/74-FTD (Instruction No. 846) dated 16th June, 1975 *vide* letter No. 500/11/76-FTD dated 23rd March, 1976 (copy attached). The results of the review are expected in the month of October, 1976.

[Department of Revenue & Banking No. 236/274/73-A&PAC II dated 14-7-1976].

(COPY)

F. No. 500/11/76-FTD

GOVERNMENT OF INDIA

Central Board of Direct Taxes

New Delhi, dated 23rd March, 1976.

To

All Commissioners of Income-tax (By name)

SUBJECT : P.A.C.—187th Report—Para 3.39—Review by Government of claims for head office expenses made by foreign companies and banks—

The Public Accounts Committee in their 187 th Report have, while dealing with the subject of head office expenses claimed by IBM World Trade Corporation, observed as under :—

"3.39. In view of the fact that there has been a substantial increase in the remittances made by foreign companies towards head office expenses during the years 1965—69, the Committee feel that it would worthwhile for Government to review the veracity of the claims admitted during this period in respect of other foreign companies and, banks as well. Since such a review is likely to yield rich dividends the Committee desire that it should be undertaken forth with, and would await a detailed report in this regard. It is, however, regrettable that the Central Board of Direct Taxes had not taken up so far a careful study of this problem with a view to ascertaining its magnitude and taking adequate steps to ensure proper tax compliance."

2. The Board desire that necessary action may be initiated to review the veracity of the claims made by foreign companies, including foreign banks, on account of head office expenses. This review should be carried out to cover the period from 1965 to 1969. Detailed instructions for the scrutiny of claims of head office expenses are contained in Board's letter F. No. 491/8/74-FTD (Instruction No. 846) dated 16th June, 1975.

3. The receipt of this letter should be acknowledged to the undersigned (by name) and the results of the review may please be intimated to the Board by 30th September, 1976.

Sd/-

(M. L. CHOUDHRY)

Secretary, Central Board of Direct Taxes.

Recommendation

The Committee view with concern the irregular extension of the benefits admissible to priority industries, under section 80E/1 of the Income-tax Act, and of higher development rebate permissible to the petrochemical industry, to a company (J. K. Synthetics Ltd.) controlled by

a monopoly house, manufacturing nylon yarn, which is only a product derived from the petrochemical base, caprolactum. This has resulted in a short levy of tax amounting to Rs.73.57 lakhs for the three assessment years 1967-68 to 1969-70. In addition, an interest of only Rs, 1.05 lakhs had been levied, under Section 139 of the Income-tax Act, for the belated filing of return of income for the assessment year 1968-69, as against Rs.1.55 lakhs actually leviable.

The Committee find that a strange procedure appears to have been adopted in this case by the Income-tax Officer who made the original assessments for the years 1967-68 to 1969-70 by asking the Indian Institute of Petroleum, Dehradun, for a technical opinion on the subject when it would have been more appropriate to refer the case, if there was any doubt, to the Chief Chemist, Central Revenues Control Laboratory, New Delhi. In fact, when the Chief Chemist was consulted, subsequently, in December 1973, he had categorically opined that Nylon-6, manufactured from caprolactum, being a finished article, was not covered by the term 'petrochemical' referred to in item 18 of the Sixth Schedule to the Income-tax Act. Expert opinion apart, it is evident, from the purely common sense point of view, that the manufacture of intermediate or finished products from a basic petrochemical, especially when the raw material base itself is manufactured elsewhere or is imported cannot be deemed to be a petrochemical industry qualifying for the benefits of priority industries. If one were to apply logically the standard adopted in this case by the Income-tax Officer initially, then almost every article or product manufactured out of pretro-chemicals should be subject to concessional rates of tax, which would be clearly against the letter and spirit of the concession given by the Parliament.

[S. Nos. 32, 33 (Paras 4.22, 4.23) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76)].

Action taken

The observations of the Committee have been noted. However, on an appeal filed by the Company against the C.I.T.'s order under sec. 263 for the assessment year 1968-69, the Appellate Tribunal has held by its order dated 31-10-75 that there was no justification in taking action u/s 263 withdrawing the relief allowed under sec. 80-I and the higher development rebate allowed u/s 33(1)(b)(B). It has further held that even on merits, Nylon-6 is a petro-chemical and is covered by item 18 of the Fifth and Sixth Schedules of the Income-tax Act. A reference application filed by the Income-tax Department u/s 256 (1) requesting the Tribunal to refer the case to the High Court has also been rejected. The question of filing a reference u/s 256(2) before the High Court is under consideration.

[Department of Revenue and Banking F. No. 236/335/73-A&PAC-II dated 28-6-1976].

Recommendation

What is even more strange about the manner in which this case has been handled is that the Central Board of Direct Taxes should have also initially agreed with the assessment of J. K. Synthetics Ltd. as a priority industry. This was done on a reference made in this regard by the Commissioner of Income-tax, in December 1972, after another Income-tax Officer had correctly decided to disallow the claim of the company for the

assessment year 1970-71. Though the reasons for the unusual enthusiasm shown in this case by the Commissioner of Income-tax are not entirely clear, having reagrd to certain serious allegations against the Commissioner of Income-tax that have been brought to the notice of the Committee and the influence known to be wielded by the monopoly group controlling the company, the Committee cannot held feeling that unseen forces have, perhaps, been at play in shaping the course of the case. The Committee would, therefore, like to be satisfied that no 'malafides' are involved and desire that a thorough probe should be conducted into the handling of the case at various stages and the conduct of the officials responsible for the misclassification of the company as a priority industry and the consequential under-assessment of tax as well as the short-levy of interest for the belated filing of the return for the assessment year 1968-69. The results of the probe, which needs to be completed expeditiously should also be intimated to the Committee early.

[S. No. 34 (Para 4.24) cf Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)]

Action Taken

The matter has been looked into as desired by the Committee and disciplinary proceedings have since been initiated against the officer concerned.

[Department of Revenue & Banking No. 236/73/335-A&PAC-II dated 26-7-1976]

Recommendation

One redeeming feature of the case is that the mistake has now been set right, though belatedly, and detailed instructions have been issued in October, 1974 that an industry manufacturing Nylon-6 from imported caprolactum is not a priority industry. The Committee also note that necessary steps have been taken to withdraw the relief already allowed and to carry out rectification in similar cases. The collection of the additional tax due in this case has, however, been thwarted by the assessee approaching the Income-tax Appellate Tribunal and Courts of Law. The Committee have been informed that the Appellate Tribunal has considered Nylon-6, manufactured out of caprolactum to be a 'petrochemical'. A writ petition filed by the assessee in the Allahabad High Court against the remedial action, under Section 262, by the Department for the assessment year 1967-68 has been allowed on the ground that the Income-tax Officer's order, in the circumstances of the case, had merged with the order of the Appellate Assistant Commissioner which was passed earlier to the order u/s 263. The Committee learn that as a result of the High Court's decision, the additional demand has been reduced to nil and that Government propose to file an appeal in the Supreme Court. The Department also propose to test the decision of the Income-tax Appellate Tribunal in the High Court. The Committee would urge Government to take all possible steps to expedite the appeal proceedings.

[S. No. 35 (Para 4. 25) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

The appeal filed before the Supreme Court on 18-7-1975 in the case of M/s. J. K. Synthetics is still pending. The Government Advocate has been requested to get the hearing and disposal of the appeal expedited. As regards the reference application filed u/s 256(1) against the Tribunal's order, the same is also reported to be still pending. The Commissioner concerned has been asked to get the hearing and disposal of the reference application expedited by the Tribunal.

[Department of Revenue and Banking No. 236/335/73-A & PAC-II dated 7-5-1976].

Recommendation

It is also extremely distressing that none of the three assessments relating to this company had been checked by Internal Audit, despite the fact that the assessments related to a large income monopoly group. The familiar but entirely specious excuse that the assessments could not be checked by the Inspector concerned on account of forgetfulness and by the Chief Auditor or on account of 'pressure of work' has once again been trotted out. The Committee gravely disapprove of such apathy on the part of the Department in regard to the important aspect of internal checking.

[S. No. 38 (Para 4. 28) of Appendix IV to the 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

The internal audit organisation is being strengthened as has already been stated in reply to para 1.17 of this Report of the Committee and considerable improvement in their performance is expected after the additional Audit Parties start functioning.

[Department of Revenue and Banking No. 236/335/73-A & PAC.-II dated 4-6-1976].

Recommendation

The Committee had also occasion to examine separately the grant of a large refund of Central Excise duty amounting to Rs. 1.37 crores, on revision, to J. K. Synthetics Ltd. The Committee have been informed by the Central Board of Direct Taxes that the Commissioner of Income-tax had been instructed, on 7th May, 1974, to look into this matter and verify that the refund had been fully accounted for in the books and the returns of income. A long time has passed since then, and the Committee would like to be apprised immediately of the results of the verification.

[S. No. 39 (Para 4. 29) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

The assessee company had received a sum of Rs. 1,36,78,459 as refund of Central Excise Duty during Sept./Dec. 1972. A further sum of Rs. 68,84,365/- became due to the company but was not paid by the Central Excise Deptt. These amounts were neither shown in the P & L a/c nor in the returns of income. The entire question of assessing those

refunds to Income-tax is under examination in detail during the course of pending assessment proceedings for the assessment year 1973-74.

[Department of Revenue and Banking No. 236/335/73-A & PAC-II dated 28-6-1976].

Recommendations

Incidentally, the Committee have received a representation alleging various corrupt practices on the part of the Commissioner of Income-tax concerned. The Committee have learnt from the Chairman, Central Board of Direct Taxes, in this connection that a series of allegations had been made against this particular officer and that these complaints were being investigated both by the CBI as well as the Department. While the Committee, naturally, would not express any opinion at this stage, they would, in view of the gravity of the charge and the status of the official urge Government to complete the investigations without delay and take all appropriate action.

It has been alleged that the transfers of the Income-tax Officer who had reopened the case of J. K. Synthetics Ltd. and of the Appellate Assistant Commissioner, who had upheld the contention of the Income-tax Officer were mala fide. The Committee have carefully considered the factual position in this regard with the assistance of the Department of Revenue Insurance. The Committee feel that they should, in general terms, impress upon Government the imperative need of ensuring that the assessing officers of a sensitive area like the Income-tax Department have the confidence that conscientious and capable work would receive recognition and approbation merited by it and that deflection from the path of duty would not be countenanced. This is a principle of conduct which the top echelons of the Department should keep constantly in mind.

[S. Nos. 40 & 41 (Paras 4·30 & 4·31) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

Investigations in respect of some of the allegations have been completed and the departmental proceedings started against the Officer concerned. The other allegations are still under investigation and the Board are keeping a watch over the progress of these investigations.

Suitable instructions in the matter have been issued to the Commissioners of Income-tax, *Vide* Board's letter F. No. A-22012/17/76-Ad. VI dated the 12th March, 1976 (copy enclosed).

[Department of Revenue & Banking No. 236/335/73-A & PAC-II dated 3-6-1976].

(COPY)

DOF No. A-22012/17/76 -Ad. VIA
Government of India
Central Board of Direct Taxes
New Delhi, the 12th March, 76'

P. S. MEHRA
SECRETARY

Dear Shri

The Public Accounts Committee has had occasion to examine the case of a company where it was alleged *inter alia*, that the Income-tax Officer who had reopened the case of the company and the Appellate Assistant Commissioner who had upheld the contention of the Income-tax Officer, were transferred from their respective postings for *mala fide* reasons. The Committee has made the following observations in this regard :

"....The Committee have carefully considered the factual position in this regard with the assistance of the Department of Revenue and Insurance. The Committee feel that they should, in general terms, impress upon Government the imperative need of ensuring that the assessing officers of a sensitive area like the Income-tax Department have the confidence that conscientious and capable work would receive recognition and approbation merited by it and that deflection from the path of duty would not be countenanced. This is a principle of conduct which the top echelons of the Department should keep constantly in mind."

The Board desire that the Commissioners of Income-tax should keep the observations of the P. A. C. carefully in mind while ordering transfers within their respective charges and while making recommendations to the Board for inter-charge-transfers. They should take particular care to see that there is no ground for suspicion that any of the transfer was motivated by considerations other than those of a purely administrative- character.

Yours sincerely,

Sd/-
(P. S. MEHRA)

Shri

Commissioner of Income-tax

Recommendation

This case is one more instance of a non-resident, foreign company (Calcutta Electric Supply Corporation Ltd.), with a returned income of over Rs. 9 crores for the three assessment years 1967-68, 1968-69 and 1969-70 benefiting substantially from negligence and oversight, at all levels

of the Income tax Department, in the computation of the depreciatior allowance admissible to it. The Committee have been informed that the company had all along submitted its depreciation schedules in Pound Sterling along with its returns of income. While preparing the schedule for Income-tax purposes, the company did not, however, start with the original rupee value of its assets for working out their written down value. Surprisingly, the different Income-tax Officers who assessed the company to tax did not also notice this anomaly and prepare a depreciation schedule showing the cost of the assets, their written-down value and the admissible depreciation terms of rupees. Instead, in accordance with the past practice in this regard, they computed the depreciation with reference to the written down value in Pound Sterling, even after the devaluation of the Rupee in June, 1966. This resulted in excess depreciation being allowed to the company, for the three assessment years, leading to an under-assessment of tax of Rs. 1.53 crores and corresponding excess payment of interest, amounting to Rs. 48.57 lakhs, on the advance tax paid by the company. This simple but costly mistake could have been avoided with a little more vigilance and care. The Committee find that the assessment for 1967-68 had been completed only on 1st October, 1971, even though the return of income had been filed on 29th December 1967. Similarly, the assessments for 1968-69 and 1969-70, were completed on 21st December, 1971, and 28th February, 1972 respectively. It is evident that proper attention had not been paid to the timely assessments of a large income company. The Committee take a very serious view of this egregious and expensive lapse.

The Committee find it even more disturbing that these assessments were checked neither by the Inspecting Assistant Commissioner concerned nor by Internal Audit. It has been stated by the Department of Revenue and Insurance that during the relevant period, the Inspecting Assistant Commissioner was holding additional charge of establishment and that due to 'heavy work', it was not possible for him to check the depreciation allowed in this case. Further, even though instructions had been issued by the Central Board of Direct Taxes, as early as 1965, that all company assessments should be checked cent-per-cent by Internal Audit and depreciation was also required to be checked by an Income-tax Officer specially entrusted with the task, the assessments for all the three years, though reported to the Internal Audit Party, could not be checked. The Committee learn from the Department that as it was not possible for the Special Income-tax Officer to check all cases, he was picking up some files, apparently at random, and checking them. The Committee would very much like to know the basis on which cases were selected for scrutiny by the officer, for it is incomprehensible how a case in which the depreciation allowance amounted to as high a sum as Rs. 2.19 crores could have escaped his notice.

In cases with large revenue implications, such as the one under the Committee cannot countenance what appears to be a casual approach on the part of the officials concerned. Neither can the Committee accept the plea of 'pressure of work' or 'over-work'. A system which allows for such explanations itself stands condemned. As has been pointed out by the Committee, in paragraph 3.63 of their 128th Report (Fifth Lok Sabha), it is up to Government to see that proper arrangements are made to ensure effective compliance with their instructions and to carefully assess the work-load, keeping in view the quality aspect, so as to provide adequate staff commensurate with the work load involved.

Having due regard to the revenue involved in the present case, the Committee must recommend a close investigation into the circumstances leading to the deplorable failure, at all levels of the Department, to detect the mistake, pointed out by Audit, and also fixation of responsibility for appropriate disciplinary action.

The Chairman of the Central Board of Direct Taxes has been good enough to admit before the Committee that whatever revenue Government would get out of this case is entirely attributable to Revenue Audit. However, Government should not merely rest content with acknowledgement of error and paying a graceful tribute to Audit for having done its duty. What is required, when such dereliction is brought to light through test check by Audit, is a more positive approach, a determined gearing up of the entire machinery for genuine scrutiny of all such cases and purposeful investigation with a view not only to rectification of errors but also to forestalling them. The Committee are, unhappy that the steps so far taken by the Ministry of Finance and the Central Board of Direct Taxes to ensure effective compliance with their own instructions and those issued at the instance of the Committee in the past, particularly those relating to the computation of depreciation and development rebate, leave much to be desired.

In this context, the Committee recall their oft-repeated concern over the large number of cases of under-assessment of tax on account of incorrect allowance of depreciation, commented upon in successive Audit Reports and Reports of the Committee year after year. It is disturbing that despite the Committee having made a number of suggestions in this regard, many of which had also been accepted by Government for inplementation, there appears to be no perceptible improvement in the situation. The Committee have attempted a review, in some detail, the implementation by Government of recommendations made by the Committee during the past decade relating among other things, to depreciation and development rebate in their 186th Report (Fifth Lok Sabha). The Committee are confident that if the measures suggested by them in this Report are implemented by Government, they would bring about significant improvement in the work of the Income-tax Department.

Besides, though the Commissioner of Income-tax had agreed, during evidence, to consider revocation of the stay and enforcement of recovery of the arrears, it is required some positive intervention by the Committee to ensure that a considerable demand was realised, partly by cash and partly by adjustment of refunds due for the assessment years 1970-71 and 1971-72. It appears, however, that an amount of Rs. 70 lakhs was still to be recovered from the company as on 15th March, 1975. Now that the appeals of Calcutta Electric Supply Corporation against the orders of the Additional Commissioner of Income-tax, under Section 263 of the Income-tax Act have been dismissed by the Appelate Tribunal, the Committee desire that the balance of tax due should also be recovered forthwith, in case this has not already been done.

[Sr. Nos. 42 to 46 and 48 (Paras 4.79 to 4.83 and 4.85) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76)

Action taken

The rate of exchange of £ Sterling was fixed at 1s 6d per rupee before devaluation of the Indian Rupee on 6-6-1966. In view of this, probably the necessity of keeping the depreciation schedule in terms of rupees was not felt. Unfortunately, the effect of the devaluation of rupee and £ in June 1966 and November 1967 respectively, was lost sight of while framing the assessments of 1967-68 onwards.

As regards delay in completing the assessments, it may be stated that a majority of the companies assessed in the Company Distt. I are very important and big companies involving various complex issues and because of such preoccupation, timely attention could not be given to this company's assessments.

An Officer-on-Special Duty was entrusted in July, 1970 with 10-point checking of assessments made in the wards of Company Districts I & III. He had drawn a list of all the assessments made upto 1st July, 1970. He had picked up some cases on the basis of their importance from the revenue point of view or if they had some interesting features but it was not possible to conduct cent percent check. The assessments in this case were made much later and he could not draw a second list of similar cases before the case was taken up by the Receipt Audit. It is, however, unfortunate that in spite of instructions depreciation allowed in this case could not be checked either by the Range Inspecting Assistant Commissoner of Income-tax or by the Officer-on-Special Duty of the Internal Audit. The explanations given by the concerned officials have been considered satisfactory. It may, however, be mentioned, that some more posts have been sanctioned recently for qualitative and quantitative improvement of the performance of Internal Audit Organisation and the additional staff will be in position shortly. The strenghthened staff is likely to meet the deficiency in this respect.

In this connection attention is invited to this Department's reply to para 6.14 of 186 Report of the Committee elucidating the steps taken in minimising the mistakes in calculating depreciation and development rebate.

[Department of Revenue and Banking No. 236/330/73-A & PAC III, dated 26-7-1976.]

Recommendation

The unduly long time taken by the Income-tax Appelate Tribunal in passing final orders also causes concern to the Committee. Even though the hearing in this case had concluded on 17th February, 1975, the Tribunal took over two months to pass orders. Here again, the Committee had to enter into protracted correspondence with Government to ensure that the orders were announced expeditiously. The facts of the case had also to be brought to the notice of the Finance Minister himself before the orders were finally announced on 30th April, 1975. It is strange that the Tribunal should have taken so much time after the conclusion of the hearings to give its verdict even in important cases involving large revenues, when the very objective of setting up such Tribunals was to reduce the time spent in litigation in courts of

law and to expedite decisions in revenue matters. The Committee would like Government to consider the feasibility of prescribing a suitable time limit for the Appellate Tribunal to pass final orders after the conclusion of the hearing.

[S. No. 49 (para 4.86) of Appendix IV to the 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)]

Action taken

The Ministry of Law, Justice and Company Affairs who are concerned in the matter were requested to process the above recommendation. They have stated that the President of the Income Tax Appellate Tribunal has since advised the Members of the Tribunal that it is necessary that every effort is made by them to dispose of appeals as early as possible and that it is desirable that they should adhere to the administratively prescribed time limit of one month within which orders should be passed after the conclusion of the hearing of an appeal. The Members have also been advised that where orders are pending for more than one month, the Member concerned should inform the President of the Tribunal as to the reasons for the delay.

[Department of Revenue and Banking No. 236/330/73-A & PAC II dated 17-5-1976]

Recommendation

Yet another important issue arising out of the examination by the Committee is the appropriation by the company of the deposits made by the consumers towards the profits of the company and their transfer to its general reserves. Since this is tantamount to tax avoidance, as the Commissioner of Income-tax himself conceded, the Committee take a very serious view of this default. The Committee learn that the transferred deposits have been taxed for the assessment year 1972-73 and penalty proceedings initiated. The assessments for the earlier years are also being reopened simultaneously with penalty proceedings. The Department has taken the stand that in this case concealment has been effectively established. Since what rightly belongs to the consumers and was held in trust by the company has been utilised by it for its own gains without any corresponding benefit to the consumers, the Committee insist that this should be looked into from the tax angle on a top priority basis, under the direct supervision of the Commissioner and the Central Board of Direct Taxes, and stringent action, under the law, taken. In the present climate when concerted drive is always under way to combat tax evasion, this should not be too difficult a task.

[S. No. 50 (Para 4.87) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76)] (Fifth Lok Sabha)].

Action taken

In the light of the above observation of the Committee, Directorate of Inspection (Investigation) has been asked to associate itself with the Commissioner of Income-tax for carrying out investigations. Action as called for under the law will be taken in due course.

[Department of Revenue and Banking No. 236/330/73 A & PAC II dated 29-6-1976.]

Recommendation

The practice of receiving deposits from consumers is also prevalent in other public utility organisations. Since it is likely that such deposits might have also been appropriated by such organisations towards their own profits and transferred to their general reserves, the Committee desire that a review of all such cases should also be undertaken from the tax angle and necessary rectificatory action taken. The Central Board of Direct Taxes should issue general instructions in this regard for the guidance of the assessing officers in the light of the facts disclosed in the present case.

[Sl. No. 51 (Para 4.88) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha).]

Action taken

All the Commissioners of Income-tax have been requested to undertake a review of all the completed assessments for the assessment year 1972-73 and onwards and take action to retrieve the loss of revenue if any. A copy of Instruction No. 971 (F. 228/12/76-IT A. II) dated the 8th July, 1976, issued in the matter is attached.

[Department of Revenue and Banking No. 236/330/73-A&PAC - II dated 7-7-1976].

MOST IMMEDIATE

INSTRUCTION No. 971

F. No. 228/12/76-IT A. II

GOVERNMENT OF INDIA

Central Board of Direct Taxes

New Delhi, the 8th July, 1976.

From:

Director, Central Board of Direct Taxes.

To,

All Commissioners of Income-tax.

SUBJECT : Security deposits from consumers—Appropriation toward profit—whether revenue income—Taxability thereof—para 4.88 of the 187th Report of the Public Accounts Committee—regarding—

Sir,

It has been brought to the notice of the Board that certain public utility organisations are receiving deposits from the consumers as a security

to be refunded on demand but these deposits are appropriated towards their own profits by transferring the same to the general reserve.

2. The question of taxability of these deposits have been examined by the Board. Board are of the view that if the deposits received by a concern in substance partakes of the nature of a trading receipt than of a security deposit, such deposits would be taxable as revenue income in the year of receipt. In this context. reference is invited to the decision of the Supreme Court in the case of Punjab Distilling Industries Ltd. Vs C.I.T. (1959) 35 ITR 519. Even where the deposit is not a trading receipt at the time of its receipt, its appropriation by transferring it to general reserve would make it taxable as revenue receipt in the year of such transfer.

3. The Board desire that a review of all the completed assessments for assessment year 1972-73 and onwards may be undertaken in this regard and immediate action taken to retrieve the loss of revenue. The result of the review may be sent by 30th September, 1976 indicating the number of cases reviewed and the number in which mistakes have been noticed with the approximate tax effect involved.

Yours faithfully.

Sd/-

(K. R. RAGHAVAN)

DIRECTOR, CENTRAL BOARD OF DIRECT TAXES

Recommendations

The Committee deplore the inordinate delay of about four years that had occurred in the finalisation of assessments of a company (Indian Iron & Steel Co. Ltd.) in the large income bracket, as a result of which Government had to pay a large sum of Rs. 40.30 lakhs as interest to the assessee under Section 214 of the Income-tax Act. The Committee fined that even though the assessee company had filed its returns of income for the assessment years 1967-68 and 1968-69 on 15th November, 1967 and 26th September, 1968 respectively disclosing incomes of Rs. 1.74 crores and Rs. 0.42 crores the assessments were completed by the Income-tax Officer only in February, 1972 , and that even the first hearing for the asessment year 1967-68 was taken up as late as 24th January, 1972 and that for the assessment year 1968-69 on 2nd February 1972. As the amounts of advance tax of Rs. 2.12 crores paid for the assessment year 1967-68 and Rs. 0.80 crores for the assessment year 1968-69 far exceeded the tax payable on the basis of the respective returns of income, the Committee are of the view that the Income-tax Officer should have safeguarded the financial interests of Government by completing the regular assessments as soon as possible after the receipt of the returns so that the advance tax paid in excess could have been refunded to the assessee,

in terms of the Board's instructions dated 16th April, 1966. That the Income-tax Officer did not do so would indicate that the officer concerned had been negligent in the discharge of his duties.

The Committee learn that disciplinary proceedings have been initiated against the officer responsible for the delay in the present case. The Committee desire that these proceedings should be completed quickly and the final action taken against the officer intimated to them.

The Committee note the view taken by the Department of Revenue and Insurance that there had been no lapse in this case in so far as the question of making provisional assessments under Section 141A was concerned. The Committee, have been informed in this connection that provisional assessment under this Section could be made in law only in a case where the assessee had made a claim that the advance tax paid by him or the tax deducted at source in his case exceeded the tax payable on the basis of return of income filed by him and the statement of accounts, documents, etc. accompanying it, and that since no such claim had been made by the assessee in the present case, it would not be covered by the provisions of Section 141A. However, with a view to ensuring that adequate steps are taken to prevent avoidable payment of interest by Government in such cases, the Committee would suggest that Government should examine the feasibility of making provisional assessments by Income-tax Officers obligatory in cases in which the advance tax paid exceeds the income returned substantially.

[S. Nos. 52—54 (Paras 5.15 to 5.17) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)]

Action taken

This Department agree with the observation of the Committee in para 5.15 that the performance of the Income-tax Officer was not satisfactory in this case. Because of the ineffectiveness of the officer concerned, he was prematurely retired from service with effect from 31st December, 1975 under F.R. 56 (j).

Section 141A of the Income-tax Act has been amended with effect from 1st April, 1976 providing for making of regular and/or provisional assessment within six months from the date of filing of the return in such cases. Administrative instructions have also been issued to the officers of the Income-tax Department so that unnecessary payment of interest under section 214 of the Income-tax Act is avoided. A copy of Instruction No. 755 [236/34/73-A & PAC] dated the 5th September, 1974 is attached .

[Department of Revenue and Banking No. 236/222/73-A&PA C II dated 25-5-1976.]

INSTRUCTION NO. 755

F. No. 236/34/73-A & PAC

BHARAT SARKAR

Central Board of Direct Taxes

New Delhi, the 5th Sept., 1974.

From,

Shri K. C. Mahadevan, Director, C.B.D.T.

To,

All Commissioners of Income-tax

SUB.: Section 141A—provisional assessment for refund—Instructions regarding —

Sir,

Reference is invited to Board's Circular letter No. 12/91/65-IT (B) dated the 16th April, 1966, Para 89 of Circular No. 6P (LXXVI-66) of 1968 issued from F. No. 1(234)/68-TPL on the 6th July, 1968, Instruction No. 277 issued from F. No. 236/243/70- IT (Audit) on 17th March 1971, Para 10 of Circular No. 56 issued from F.No. 156 (27)70-TPL on 19th March, 1971 and Instruction No. 438 issued from F.No. 246/48/71-A & PAC on 14th July, 1972.

2. Instances have come to the notice of the Board that in spite of the above instructions regular assessments are unduly delayed and provisional assessments u/s 141-A of I.T. Act, 1961 are not being made in appropriate cases resulting in payment of avoidable interest under section 214 amounting to several lakhs. The Board desire that provisional assessments u/s 141-A of I.T. Act should be invariably made promptly in all appropriate cases, where regular assessments are likely to be delayed so that unnecessary payment of interest u/s 214 is avoided.

3. With a view to ensure strict compliance with the above instructions, it is suggested that in all catergory I cases, the returns should be scrutinised immediately on receipt, with a view to see whether action under section 141-A is attracted. All cases where the provisions of section 141-A are attracted should be entered in a separate register to be kept in the personal custody of the ITO. The ITO should give priority to the completion of these cases and whenver, it is found that the regular assessment in such cases cannot be completed within a period of six months from the date of filing the return provisional assessment u/s 141-A should be made forthwith and any refund due granted immediately. They should also leave a note in the file giving the reasons as to why regular assessment could not be completed, within 6 months.

4. Hereafter any payment. of avoidable interest u/s 214 will be seriously viewed. Cs. I. T. and I.ACs. may call for half-yearly statements

of interest paid by the Government exceeding Rs. 1,000 in each case to satisfy themselves that the payment of such interest was unavoidable.

5. These instructions may be brought to the notice of all officers working in your charge.

Yours faithfully,

Sd/-
(K. C. MAHADEVAN)
Director (PAC) CBDT

Copy forwarded to : (as usual)

Recommendation

The delay in finalising the assessments in this case had also not been noticed by the concerned Inspecting Assistant Commissioner or the Commissioner as the case never came into their orbit. All large income cases, however, are expected to be reviewed by the supervisory officials. The only inference the Committee can thus draw from the failure of the Inspecting Officers is that the middle management in the Income-tax Departemnt is somewhat lax. The Committee fear that if this continues, the maladies of the Department would persist. It is, therefore, urged that the Central Board of Direct Taxes should review seriously the duties and responsilities at present entrusted in the Inspecting Assistant Commissioners and the effectiveness of the supervision exercised by them with a view to evolving suitable remedial measures.

The Central Board of Direct Taxes should also devise immediately a fool-proof system for a regular and more efficient monitoring of the progress of assessments relating to large income cases and tighten the inspection machinery. The Directorate of Inspection and the Board have an inescapable obligation in this regard. In this context, the Committee reiterate their earlier recommendations in regard to the persistent tendency on the part of Income-tax Officers to complete assessments only towards the close of the limitation period. Apart from the loss that may arise on payment of interest in cases like the one discussed in the preceeding paragraphs, the Committee fear that by so rushing through assessments, there is the greater risk of the returns not being scrutinised properly and consequential loss of revenue through inadequate examination.

[Sr. Nos. 55 & 56 (Paras 5.18 & 5.19) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

The following measures have recently been taken to improve the position regarding completion of assessments in large income cases expeditiously after proper scrutiny and to strengthen the middle-level management of the Income-tax Department :

(*i*) This Department's reply to para 5.21 of their 186th Report may please be referred to. Directorate of (O. & M) Services is monitoring the progress on behalf of the Board ;

(*ii*) An Inspection Manual for the Inspecting Assistant Commisioners is being prepared by the Directorate of Inspection (Income-tax).

(*iii*) Instructions have been issued to ensure completion of time-barring assessments by Ist October and to ensure completion of important revenue cases by 31st i (ember. A copy of the instructions is attached.

(*iv*) A beginning has been made by assigning assessment functions in important cases involving tax evasion, fraud, etc. to the Inspecting Assistant Commissioners. In this connection a reference is invited to this Department's replies to para 1.8 of their 192 Report and para 12.7 of 186th Report : and

(*v*) With the introduction of Section 144A and 144B of the Income-tax Act, 1961, Inspecting Assistant Commissioners will associate themselves more closely with day to day assessment work in important cases.

[Department of Revenue and Banking No. 236/222/73-A & PAC-II, dated 20-7-1976].

INSTRUCTION No.975

F. No. 220/12/76-ITA. II

GOVERNMENT OF INDIA

Central Board of Direct Taxes

New Delhi, the 8th july, 1976.

From :

Director, Central Board of Direct Taxes.

To

All Commissioners of Income-tax.

Sir,

SUBJECT :—*Completion of important revenue cases and time barring assessments—Para 75 of the Minutes of the Commissioners Conference, 1976—Instructions reg.*

Inspite of repeated instructions of the Board to avoid postponement of assessments in important revenue cases to the last quarter of the year, it has been noticed that the practice continues unabated. The Board would like to reiterate these instructions and desire the Commissioners of Income-tax to ensure that the Income-tax Officer so plan their work that *all important revenue cases are disposed of in any case not later than 31st December, of the financial year.*

2. Pendency of a large number time-barring assessments every year has also been a source of concern to the Board. Board desire that while

taking up the time-barring assessments in a particular case, invariably the succeeding year's assessment should also be taken up and completed so as to reduce the burden of carry forward of time-barring assessments to the next year. It is further directed that all time barring assessments should be completed by 1st October, 1976.

3. As planning of assessments for the year is very important the Commissioners should personally oversee, the same and ensure that these instructions are strictly observed by the Income-tax Officers working under them.

Yours faithfully,
Sd.
(K. R. RAGHAVAN)
Director, Central Board of Direct Taxes

Recommendation

The Committee understand that remedial action, under Section 13, has been taken in respect of the assessments relating to the years 1970-71, 1971-72 and 1972-73 and necessary additional demands raised. For the assessment year 1966-67, while no remedial action under section 13 was possible, on account of the assessment having become time-barred, action under Section 8(a) of the Act has, however, been taken in time and an additional demand of Rs. 78,071 raised.

The Committee also view seriously the lapse on the part of the Internal Audit in not checking the assessment. Even though the Chief Auditors themselves were required to personally check these assessments, they had not done so and the failure on their part has been, as usual, attributed to 'pressure the work'. The Committee regret to observe that the same familiar excuse is offered by the Department time and again, which is only indicative of a definite weakness in the existing machinery for internal audit. The Committee need hardly emphasise the importance of a sound and efficient internal audit organisation and desire that the adequacy of the existing arrangements for internal audit should be reviewed in detail and necessary remedial steps taken.

In this connection the Committee, find that in all such cases where serious lapses have been found, Government merely rest content with obtaining an explanation from the concerned officials and issuing a warning. This ritual, in the opinion of the Committee will neither help the Administration nor the exchequer. The Committee are of the view that a more positive and dynamic procedure has to be evolved in this regard so that punishments are granted according to the magnitude and seriousness of the lapse committed by the officials and positive action taken even in two or three cases acts as a deterrent to others. The Committee are also of the view that where there has been a failure or lapse in the discharge of responsibility by an officer at any level, he should be procceeded against rather than some petty officials working under him.

[Sl. No. 58, 60-61 (Paras 6.13 6.15 to 6.16) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

The facts stated in this para are correct.

It has been the constant endeavour of this Department to improve the performance of the internal audit organisation. As has already been stated in reply to para 1.17 of this Report, necessary measures to strengthen this organisation are being taken on the basis of a study report of the Directorate of O & M Services

The observations of the Committee are noted. In accordance with the provisions of relevant Conduct Rules the disciplinary authorities do take into account all the circumstances with due regard to the seriousness of the mistakes of omission/commission by the officer concerned while awarding any punishment. This Department assure the Committee that no discrimination will be made on the basis of the status of the officer concerned.

[Department of Revenue and Banking No. 236/185/73-A & PAC. II dated 1-6-1976]

Recommendation

The Committee would also like to be informed of the final decision of the Income-tax Appeallate Tribunal on the assessee's appeal against the additional demand of Rs. 13.10 lakhs relating to the assessment year 1972-73.

[Sr. No. 62 (Para 6.17) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

The Income-tax Appellate Tribunal have decided the appeal in favour of the assessee upholding the plea that rule 4 of the Second Schedule to Sur-tax Act is not applicable in relation to deductions under Chapter VIA of the Income-tax Act. As a result of this decision the demand was reduced to Rs. 2,34,665 which has since been collected by adjustment.

[Department of Revenue and Banking No. 236/185/72-A & PAC-II dated 26-7-1976].

Recommendation

Another intriguing point emerging out of this case relates to the extension of the capital plus reserve base for the purpose of lowering the sur-tax liability. The Committee have come across a number of instances in the earlier Audit Reports where the profits of a particular year are first credited to the General Reserve and appropriations made thereafter for declaring dividends. Since such a transfer of the profits to the General Reserve may only be a ruse to lower the sur-tax liability, by claiming higher exemptions on an artificially enhanced capital base, the Committee would like to know whether Government have contemplated or conducted any study of the sur-tax assessments of companies which might have adopted such a method of tax avoidance. In case such a study has not so far been undertaken, the Committee would recommend that this should be initiated forthwith and the outcome of the study intimated as early as possible. Government should also examine whether any amendment to the existing Act and Rules is necessary to prevent such an abuse.

[Sr. No. 67 (Para 6.34) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action Taken

A new Rule '1A' has been inserted in the Second Schedule to Companies (Profits) Surtax Act, 1964 effective from 1-4-1975 *vide* clause 29(ii) of the Finance Act, 1976, which enables the income-tax Officer to reduce the capital base by the amount of defficiency in crediting proposed dividends and provision for taxation. The Board have issued Instructions No. 972(F. 228/ /25/76-ITAII) dated the 8th July, 1976 to all the Commissioners of Income-tax for conducting a review of the assessments completed for assessment year 1975-76 in the light of the above amendment. A copy of the Instructions is attached.

(Department of Revenue and Banking No. 236/23/73-A & PAC-II dated 21-7-1976).

COPY

INSTRUCTION No. 972

F. No. 228/25/76-ITA. II

GOVERNMENT OF INDIA

Central Board of Direct Taxes

New Delhi the 8th July, 1976.

From :

Director, Central Board of Direct Taxes.

To :

All Commissioners of Income-tax.

Sir,

SUBJECT:—*Companies (Profits) Sur-tax Act*, 1964, *Computation of Capital—Provision for taxation and proposed dividend—Clause* 29(*ii*) *of Finance Act*, 1976 —*Para* 6.34 *of the* 187*th Report of the* P.A.C. (1975-76)—*Instructions regarding*.:

Reference is invited to Board's Instruction No. 784 (F. No. 229/7/73-ITA II) dated 11th November, 1974 directing the Income tax Officers to examine each item of reserve carefully before allowing them to be included in the capital base and not being misled by the nomenclature given by the assessees in the Balance Sheet.

2. Finance Act, 1976 (66 of 1976) has inserted a new rule numbered rule 1A after rule 1 in the Second Schedule to the Companies (Profits) Sur-tax Act, 1964. The rule has retrospective effect from Ist April, 1975 and reads as under :—

"1A. Where a company has not made any credit in any account in its books as on the first day of the previous year relevant to the assessment year which is of the nature of item (i) or item (9) under the head "CURRENT LIABILITIES AND PROVISIONS" in the column relating to "LIABILITIES" in

the "FORM OF BALANCE SHEET", given in Part I of Schedule VI to the Companies Act, 1956, or where the Income-tax Officer is of opinion that the amount credited in such account falls short of the amount which should have reasonably been credited by it, the amount of its capital as computed under rule 1 shall be reduced by the amount which has not been so credited or, as the case may be, the amount of such shortfall.

Explanation.—For the purposes of this rule, the amount of credit which should have reasonably been made by a company in relation to any account of the nature of item (9) aforesaid, means the amount of dividend declared or paid by the company, on or after the first day of the previous year relevant to the assessment year, for the previous year immediately preceeding the first mentioned previous year.

3. It would be seen from the above that the Income-tax Officers have now been specifically empowered to see whether provision of adequate provision have been made in the balance sheet towards provision for taxation and proposed dividend and in cases of shorfall reduce the capital base accordingly.

4. Board desires that a review of assessments completed for the assessment year 1975-76 may be undertaken immediately in the light of the above amendment and the result of the review indicating the number of cases reviewed, number of cases in which such mistakes have been noticed and the likely tax effect thereon may be sent positively by 31st July, 1976.

Yours faithfully,
Sd.
(K. R. RAGHAVAN)
Director, Central Board of Direct Taxes.

Copy to :—

1. Comptroller and Auditor General of India (25 copies).
2. Director of Inspection (Income-tax & Audit)/investigation/Research & Statistics/Publication and Public Relations, New Delhi.
3. Directorate of O & M Services (Income-tax), Ist Floor, Aiwan-Ghalib, Mata Sundri Lane, New Delhi. (7 copies).
4. All Officers/Sections of Central Board of Direct Taxes.
5. Bulletin Section of D.I. (RS&P), New Delhi.
6. Joint Secretary & Legal Adviser, Ministry of Law & Justice, New Delhi.

Sd. (K. R. RAGHAVAN)
Director, Central Board of Direct Taxes.

Recommendations

The cases discussed herein reveal certain grave deficiencies in the functioning of the Income-tax Department, particularly in the arena of company taxation. They involve assessments where the returned income often

runs into crores of rupees. Only a test check by Statutory Audit of the assessments in nine cases of foreign and Indian companies, belong to multinational corporation or monopoly groups, has disclosed non-levy/under-assessment of tax and excess payment of interest, adding up to the staggering figure of Rs. 3.66 crores. Obviously there is something very worng with the administration of company taxation at various levels. The Committee feel considerable disquiet over the mistakes and omissions discussed at some length in this Report. These defaults have become almost repetitive in character, in spite of many recommendations made by the Committee in this regard in the past and the mass of detailed instructions issued from time to time by the Central Board of Direct Taxes.

The errors and omissions in the assessment of large-income cases which have come to the notice of the Committee are broadly attributable to one or the other of the following factors :—

(*i*) sheer negligence or laxity on the part of assessing officers;

(*ii*) inadequate and improper planning of work by the assessing officers and non-allocation of proper priorities for the timely completion of large-income cases, resulting in hasty assessments and disposal without adequate scrutiny towards the end of the limitation period;

(*iii*) complacency on the part of the Ministry of Finance and the Central Board of Direct Taxes towards issuing guidelines in respect of assessment of important items of expenditure such as 'Head Office Expenses' of foreign companies operating in India and 'expenditure on scientific research' which often serve a facades to facilitate tax-avoidance ;

(*iv*) inadequacy of internal control and supervision, particularly at the middle management level; and

(*v*) ineffectiveness of internal Audit.

In the preceding chapters, the Committee have tried not only to trace the reasons for such default but also to suggest remedial measures. The Committee trust that at least in the context of the present National Emergency, Government will take more serious notice of their observations and recommendations and display a less inhibited approach in implementing them.

The Committee would, in particular, like to draw Government's immediate attention to the deficiencies in internal control and supervision in the Income-tax Department, especially at the middle management level of Inspecting Assistant Commissioners, which have been brought into sharp focus in the cases discussed in this Report. It is distressing to observe these middle level officers often rather remiss in the discharge of the duties entrusted to them. The Committee emphasise that these officers have precise and purposeful role which they are enjoined to perform but with disappointing results so far.

Another reason for the recurrent mistakes in assessment, particularly in large income cases is that, in the absence of any categorisation of different types of cases and disposals on a selective basis, even assessments with large

revenue implications are left in the hands of Income-tax Officers with comparatively less experience. In the circumstances, Government should seriously consider the desirability of entrusting the assessment of such cases directly to the Inspecting Assistant Commissioners of Income-tax. The Chairman, Central Board of Direct Taxes has himself admitted, during evidence, that Government is 'very much conscious of this deficiency' and has assured the Committee that he would try to ensure concentration on large income group cases by experienced officers and to transfer certain cases to the Assistant Commissioners also. The Committee have examined the subject of supervision and internal control and the question of entrusting direct assessment work to the Inspecting Assistant Commissioners at considerable length in their 186th Report (Fifth Lok Sabha) and have made specific suggestions and recommendations which, it is urged, should be dealt with on a priority basis and implemented forthwith.

The Committee have not been able to examine some of the paragraphs relating to Corporation Tax included in Chapter II of the Report of the Comptroller and Auditor General for the year 1972-73, Union Government (Civil), Revenue Receipts, Volume II, Direct Taxes on account of paucity of time. They expect however, that the Department of Revenue and Insurance and the Central Board of Direct Taxes will take necessary remedial action in these cases, in consultation with Statutory Audit.

[S. Nos. 68 to 72 (Paras 7.1 & 7.5) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76)].

Action Taken

The steps taken in the matter have been elucidated in this Department's replies to paragraphs 1.14, 1.15, 1.17, 3.38, 4.22, 4.23 and 4.25 of this Report of the Committee as also to paragraph 1.16 which may please be referred to.

In this connection the Committee's attention is invited to this Department's reply to paragraph 1.8 of 192nd Report of the Public Accounts Committee.

Remedial action, wherever necessary and possible has been taken in all the cases, under intimation to Audit.

(Department of Revenue and Banking No. 241/13/76-A & PAC-II dated 17-7-1976.)

CHAPTER III

RECOMMENDATIONS/OBSERVATIONS WHICH THE COMMITTEE DO NOT DESIRE TO PURSUE IN THE LIGHT OF THE REPLIES RECEIVED FROM GOVERNMENT

Recommendation

The Committee are surprised to learn that as against the licensed capacity of 1200 tonnes of biscuits per annum, the actual production of Britannia Biscuit Co. Ltd. has far exceeded the licensed capacity in all the years since the factory commenced production in 1967. During the period from 1968 to 1973, the production ranged from 5278 tonnes to 8528 tonnes. In 1973, the production had exceeded the licensed capacity by over 700 per cent. The Committee find it difficult to accept the explanation that this phenomenal increase in production had been achieved by the company by improved technology without providing any additional machinery. As the increase in production over the licensed capacity, *prime facie*, appears to be abnormal and remains unexplained, the Committee are of the view that the possibility of the company having resorted to manipulation of the invoices to import additional machinery cannot be ruled out. The Committee desire that the said excess production should be thoroughly investigated into without losing further time and appropriate action taken without delay against the company if it is found to have violated the provisions of the Licensing Act.

[S. No. 9 (Para 1.42) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action Taken

There are two parts in the above recommendation viz. (i) violation of the provisions of the Licensing Act and (ii) under-invoicing in import of machinery. As the recommendation regarding the over-production was to be processed by the Ministry of Industrial Development, the Lok Sabha Secretariat was requested on 9th February, 1976 to obtain the requisite reply from that Ministry. Regarding the second part, it has been reported by the Central Board of Excise & Customs that only two cases of suspected manipulation of invoices by the company had come to their notice during 1973 and thereafter. Particulars of these two cases are given below :—

(*a*) It is reported that M/s. Britannia Biscuit Co. Ltd., Calcutta imported two second-hand Gem Icing Machineries in two consignments in the year 1975 and declared the value of the same as Rs. 20,434 and Rs. 189,907 respectively in the relative bills of entry. The two machines were imported by them from M/s. Associated Biscuit Ltd., U.K. In view of the fact that the value declared appeared to be low, investigations were made to ascertain the correct price as there was clear evidence in the correspondence that the machineries had been given to the importers

at a concessional price, as they were not being used by the seller in England and there was a special relationship between the seller in England and the buyer in India. Accordingly, the value of the machines were appraised on the basis of detailed examination of the machines and the assessable value so appraised of the two machines came to Rs. 71,194 and Rs. 68,737 respectively. Since there was no evidence that the importer was making extra payment to the suppliers by unauthorised means, the declared value was accepted for purpose of debit to the licence.

(*b*) In two other cases, spare parts of machinery were imported by this firm under cover of import licences and the importers sought clearance under the category permissible spares but as the goods were of small value and the importers were actual users, these were allowed clearance with a warning.

(Department of Revenue and Banking No. 241/13/76-A & PAC-II dated 16-7-1976).

F.No.241/13/76-A&PAC-II

(F.No-234/45/76-CX-7)

Dated the 16th July, 1976.

Recommendation

In paragraphs 9·13 and 9·14 of their 176th Report (Fifth Lok Sabha), the Committee had, *inter alia*, commented on the absence of any uniform guidelines for the assessing officers on the treatment of head office expenses for purposes of Income-tax and had desired that guidelines in this regard which were stated to be under finalisation on the basis of certain case studies and a study note prepared as early as August 1973, in consultation with a few Commissioners of Income-tax, should be finalised without further loss of time and necessary instructions issued to the assessing officers. The Committee have been informed by the Department of Revenue and Insurance, in October, 1975, that necessary guidelines in this regard had been issued only on 16th June, 1975. The Committee are perturbed over such egregious delay in taking a final decision on an issue which is vital both from the taxation and foreign exchange angles. The Committee would like very much to know the reasons for this delay and would reiterate their earlier recommendation that responsibility for it should be fixed for appropriate action. Now that the guidelines have at long last been issued, the Committee trust that real scrutiny of head office expenses by assessing officers would be facilitated and would produce the desired results. The adequacy of these guidelines should be reviewed later, on the basis of the experience gained in the field on their implementation and such improvements, as are found necessary, effected. The Committee would keenly watch the effect of these guidelines on the assessing officers.

[S. No. 30 (Para 3·38) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action Taken

As stated in the evidence before the Committee the draft of the guidlines drawn up on the subject of scrutiny of head office expenses claimed by foreign concerns was sent to some senior Commissioners of Income-tax, Director of Inspection (Investigation) for their comments/suggestions. As desired by the Committee, the draft guidelines together with the comments, received from the Commissoners/Director of Inspection (Investigation) were made available with the files of the Ministry to the Committee. The finalisation of the instructions was kept in abeyance pending the receipt of the Report of the Public Accounts Committee because it was considered expedient to take into consideration the observation of the Committee, if any, on this subject.

2. The 176th Report of the Committee was received on 6-5-1975. In the light of the observations of the Public Accounts Committee in this Report, the draft guidelines were suitably modified and issued on 16th June, 1975.

3. As regards the responsibility for the delay in issuing guidelines, attention of the Committee is invited to the Department's further reply to recommendation contained in para 9·13 of 1976the Report from file No. 241/2/75-A&PAC. I/441/2/76-FTD dated 19-3-76 intimating that Government are satisfied that in the finalisation of these guidelines there has been no delay calling for any action against any officer. The following note was approved by the Finance Minister on 18-10-1975:

> "This matter has been looked into carefully and the Government are satisfied that preparation of guidlines for Income-tax officers on the subject of head office expenses had received adequate attention along with the other items of work which were being handled by the Foreign Tax Division. The Study Note dated 18-8-73 prepared by one of the officers of the Foreign Tax Division to which a reference has been made in the Report of the P.A.C., was not considered adequate and it was felt that a lot more work remained to be done before the guidelines could be finalised. The Government are satisfied that in the finallisation of these guidelines there has been no delay calling for any action against any officer."

4. In so far as the question of review of guidelines issued is concerned, it is submitted that it has to wait for some time more and will be taken up towards the end of this year.

(Department of Revenue & Banking No. 241/13/76-A.&.-P.A.C. I dated 17-4-1976)

Recommendation

The Committee are concerned to note that while correctly excluding the deductions admissible under Sections 80E/I, 80J and 80MM of the Income-tax Act from chargeable profits, the assessing officer had failed, in this case relating to a foreign company (Union Carbide India Ltd.), to reduce proportionately the amount of the capital as required under Rule 4 of the Second Schedule of the Company (Profits) Surtax Act, 1964, which

led to an excess statutory deduction under Section 2(8) of the Act and consequent under charge of Surtax of Rs. 26·88 lakhs for the assessment years 1966-67, 1970-71, 1971-72 and 1972-73. That such a mistake should occurred despite the clear and unambiguous rules framed in this regard would indicate that the assessing officer had not exercised care in finalising the assessments. The Committee would like the circumstances leading to this mistake to be gone into and appropriate action taken thereafter.

The Committee find that the Audit Memo in this case had been issued on 13th March, 1973, and remedial action under section 13 of the Act in respect of the assessment year 1966-67 was permissible upto 7th September, 1973. If the Department had, therefore, taken prompt action on receipt of the Audit query, the rectification for the assessment year 1966-67 could also have been made under Section 13 before the assessment became time-barred. The Committee take a serious view of the delay in initiating action on Audit objections, and desire that responsibility for the failur should be fixed and the action taken intimated early to the Committee. A suitable time-limit for initiating rectificatory action in such cases shonld also be prescribed, in consultation with the Comptroller and Auditor General of India

[S. No. 57, 59 (Paras 6·12 6·14) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76)(Fifth Lok Sabha].

Action Taken

The point raised in this case, in fact, was a controversial one which could ultimately be settled with the issue of Board's Instructions on 28th September, 1973. The assessing officers completed the assessments long before the issue of these instructions. The Commissioner of Income-tax has reported that the mistake committed in interpreting the legal issue was bonafide. In the circumstances, it has not been considered necessary to take any action against the officers concerned.

As regards fixing the responsibility for delay in taking remedial action, it has already been stated above that the legal point raised in the audit objection was a subject matter of controversy and no assessing officer can be said to be responsible. In regard to the suggestion of the Committee for prescribing a time-limit for remedial action, it may be stated that a time limit for initiating action under different sections of the Income-tax Act already exists. The mistakes pointed out by the Audit have, therefore, to be rectified within the limitation laid down under different sections of the Act. Instructions also exist that remedial action should be initiated as a precautionary measure even in cases where objections pointed out by the Audit are disputed by the Income-tax Department.

[Department of Revenue & Banking No. 236/185/73-A & P.A.C. II dated. 1-6-1976

(R. S. CHADDA)
Additional Secretary to the Government of India.

Recommendation

The Committee take a serious view of the mistake that had occurred in this case relating to a company, Gwalior Rayon Silk Manufacturing (Wvg.) Company Limited, again linked with a monopoly group, in computing

the capital of the company, under Rule 3 of the Second Schedule of the Companies (Profits) Sur-tax Act, 1964. The incorrect augmentation of the capital proportionally, after taking into account the bonus shares worth Rs. 2·50 crores issued by the company by utilising a part of the accumulation in its general reserve, had resulted in an excess statutory deduction of Rs. 15·07 lakhs under Section 2(8) of the Act and consequent short-levy of tax of Rs. 5·27 lakhs. The circumstances in which a mistake like this had been committed by the Income-tax Officer has not been satisfactorily explained by the Department. Besides, the attempt at extenuation by reference to an unfortunate misreading of the Second schedule can only be considered as very special pleading and by no means convincing. The Committee cannot but take a grave view of lapses involving large losses to the revenue. The circumstances leading to this mistake required to be investigated with a view at least to ensuring that no malafied intentions were involved.

[Sr. Nos. 63 (Para 6·30) Appendix IV to 187th Report of the Public Accounts Committee (1975-76)]

Action taken

The issue involved was a controversial one. There is no material to hold that the assessing officer was guilty of any malafide or gross negligence.

(Department of Revenue and Banking No. 236/23/73-A & PAC II dated 28th July 1976).

CHAPTER IV

RECOMMENDATIONS/OBSERVATIONS REPLIES TO WHICH HAVE NOT BEEN ACCEPTED BY THE COMMITTEE AND WHICH REQUIRE REITERATION

Recommendation

The Committee find that this case was not checked by the Internal Audit and the familiar plea of preocccupation with other cases has again been put forth by the Department. The Committee are unhappy that effective steps are yet to be taken by the Department to ensure that the computation of income and the assessment orders themselves are pre-checked preferably by Internal Audit, particularly in large income cases of foreign companies and Indian monopoly houses, though an earlier recommendation of the Committee in this regard contained in paragraph 2·66 of their 87th Report (Fifth Lok Sabha) had been accepted, in principle, by Government as early as December, 1973. In view of the large number of mistakes in the computation of assessable income which have been brought to their notice year after year, the Committee strongly reiterate their earlier recommendation and would urge Government to act upon it without further loss of time.

[S. No. 4 (Paras 1·17 of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)]

Action Taken

It has already been intimated to the Committee that it may not be practicable to carry out pre-check of assessments for the following reasons:

(a) Such a course is likely to dilute the responsibility of the assessing officer;

(b) It is also likely to cause delays in the finalisation of assessments and issue of demand notices, and

(c) It may give rise to complaints that Audit is interfering in the judicial discretion of the assessing officer.

The question of strengthening the Internal Audit organisation has already been taken up in consultation with the Associate Finance in order to make the post-audit checks more effective. The measures spelt out in reply to paras 1·14 and 1·15 above and the proposed strengthening of Internal Audit will go a long way in improving the quality of assessment work, and preventing leakage of revenue.

(Department of Revenue and Banking No. 236/90/73-A&PAC II dated 21-4-1976)

Recommendation

The Committee agree with the view of Audit that in Section 35(i)(ii) of the Income-tax Act, under which any sum paid to a scientific research association, having as its object scientific research, is allowed as a deduction provided the association is recognised by the CSIR, there is a lacuna which needs to be removed. It is not unlikely that ambiguity in the legal provision in this regard has led to a tendency on the part of some big industrial houses to sponsor so-called scientific research associations with a view to claiming deductions from taxable income. The Committee, therefore, desire that the existing provisions should be reviewed and the loophole in the Act plugged forthwith. This tendency could, perhaps, also be countered by prescribing ceiling on the sums payable to research associations for the purposes of computation of income-tax.

[Sr. No. 7 (Para 1·33) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action Taken

With a view to ensuring avoidance of misuse of the provisions of section 35(1)(ii) of the Income-tax Act, 1961, the prescribed authorities have taken the following measures:

(i) A Committee consisting of experts in the field of research for which approval is asked for is to satisfy itself about the genuineness of the research association and research programme they intend to carry out before recommending approval;

(ii) In most of the cases, approvals are being given by the prescribed authorities for a limited period, generally, three years to be reviewed thereafter; and

(iii) The prescribed authorities insist on the furnishing of annual reports and returns by the institutions rgarding scientific research activities for enabling the prescribed authorities to have an annual review and to see that the funds received under the approval are utilised exclusively for research purposes.

2. The Audit have already been informed regarding the system evolved in consultation with the prescribed authorities for ensuring the proper use of the concessions *vide* Boards' letter F. No. 203/163/75-IT A. II dated the 22nd March, 1976 (copy attached).

3. The Indian Council of Medical Research *i.e.* prescribed authority, have already reviewed the performance of certain institutions and have recommended withdrawal of approval in eight cases so far.

4. The Central Board of Direct Taxes have, on its own, issued Instruction No. 896 (F. 203/8/75-ITA. II) dated the 4th November, 1975 to all the Commissioners of Income-tax enclosing a list of institutions so far approved for making proper enquiries with a view to ensuring that the utilisation of funds is made for research purposes and with a view to referring the matter to the prescribed authority for withdrawal of approval if any deviation is noticed.

5. The suggestion of the Committee regarding fixation of ceiling on the sums payable to research associations has been carefully considered. The amount required for carrying out a particular scientific research programme would substantially vary from one programme to another depending upon the nature and type of research proposed to be undertaken which cannot be foreseen with any substantial accurancy. In view of this, it would not be feasible to fix a ceiling on such expenditure.

6. It is expected that the steps taken by the prescribed authorities as well as those by the Central Board of Direct Taxes for stricter control over the utilisation of such funds will ensure better discipline among the institutions and, in case of failure, the approval granted will be withdrawn.

[Department of Revenue and Banking No. 236/90/73-A and PAC II, dated 16-7-1976]

(R. S. Chadda)

Additional Secretary to the Government of India

(COPY)

F. No. 203/163/75-ITA-II

GOVERNMENT OF INDIA

Central Broad of Direct Taxes

New Delhi, the 22nd March, 1976

From

Under Secretary, Central Board of Direct Taxes.

To

The Comptroller & Auditor General of India, New Delhi.

Sir,

SUBJECT : *Expenditure incurred on scientific Deductions allowed in the case of income from business of the official under section* 35(1)(ii) & *(iii) of the Income-tax Act,* 1961—*Position regarding*—

I am directed to refer to your letter No. 3071-Rec. A. II/18-74 I dated the 19th November, 1975, on the above subject and to furnish below the information received from the prescribed authorities in this regard:—

1. *Indian Council of Medical Research, New Delhi*

With a view to ensuring itself that the institutions approved by the Council for exemption from Income-tax under section 35(1)(ii) of the

Income-tax Act, 1961 contiue to be engaged in bio-medical research, the Council calls from the Institutions concerned annually a report on the researches carried out during a year and a statement of account of the donations received and expenditure actually incurred on research.

A copy of the proforma prescribed by the Council for submission of such information by the Institutions is enclosed for information. The information furnished by the Institutions is reviewed by the Special Committee of the Council constituted for the purpose. It may be mentioned that as a result of such review by the Committee, some of the Institions have been recommended by the Council for derecognition from exemption from income.

2. *Indian Council of Social Science Research, New Delhi*

While recommending approval of institutions/organisation under section 35(1)(iii) of the Income-tax, Act 1961, the Indian Council of Social Science research invariably insists on the following three conditions being fulfilled by the beneficiary organisations/institutions.

(i) That the organisations recommended for approval u/s. 35(1)(iii) of the Income-tax Act, 1961, shall maintain separate accounts of the funds collected by them under the exemption.

(ii) That such funds shall be utilised exclusively for promotion of research in social sciences.

(iii) That the organisations shall send an Annual Report to the Indian Council of Social Science Research showing the funds collected under the exemption and the manner in which they were utilised.

The Indian Council of Social Science Research takes prompt steps to obtain from the beneficiary organisation the documents referred to above to satisfy itself that the funds collected under the exemption are utilised for the purposes for which exemption under section 35(1((iii) of the Income-tax Act, 1961, was recommended by the Council.

3. *Department of Science & Technology, New Delhi*

This Department have prescribed an annual return of scientific research activities and have requested all the approved Associations, Universities, colleges and other Institutions to send them the return by 30th April of each year pertaining to the years ending with 31st March. The contents of the Annual Returns give this Department an idea whether the Association/Institution etc., are continuing to enagage themselves in scientific research. A copy of the prescribed proforma is enclosed for information.

As a general principle, the prescribed authority is approving Associations set up private business houses for a period of three years only.

4. *Indian Council of Agricultural Research, New Delhi*

The Council has adopted a set of guidelines for recommending cases grant of exemption u/s. 35(1)(ii) of the Income-tax Act,1961 (copy enclosed). The Council initially recommends cases for exemption for a period of two years. In the case of cases coming up for further extension, the proposed

exemption is examined on the basis of performance of the Organisation during the previous years. In case the Council are satisfied the exemption renewed for a period of three years in the first instance. With a view to ensure that the Organisation recognised u/s. 35 (1) (ii) of the Income-tax Act, 1961 do not deviate from the conducting of Scientific Research the Council have specified that such Organisations will have to send their Annual Report involving the physical and technical progress made during the year along with the audited accounts to the Indian Council of Agricultural Research every year within three months the close of the year.

Yours faithfully,
Sd/-
(M. K. PANDEY)
UnderSecretary, Central Board of Direct Taxes.

Copy forwarded to —

1. Indian Council of Medical Research, Ansari Nagar, Post Box No. 4508, New Delhi-110016, with reference to their letter No. 18/21/74-AA. II dated 4th December, 1975.

2. Indian Council of Social Science Research, 11 PA Hostel Indraprastha Estate, New Delhi-110001, with reference to their letter F. No. 6(1)75(A) dated 2nd December, 1975.

3. The Department of Science & Technology, N.C.S.T., Secretariat, Technology Bhavan, New Mehrauli Road, New Delhi-110029, with reference to their letter No. 3/3/75-R.A. Cell dated 26th December, 1975.

4. Indian Council of Agricultural Research, Krishi Bhavan, New Delhi-110001, with reference to their letter F. No. 16(4) 71-CDN (Tech.) dated 6th March, 1976.

Sd/-
(M. K. PANDEY)
Under Secretary, Central Board of Direct Taxes

Recommendation

What is more distressing is the fact that even though this question of the company producing biscuits far in excess of the licensed capacity had been raised in the Lok Sabha in 1974, no concrete action has so far been taken against the company. The Committee cannot understand why the Ministry of Industrial Development merely remained content with calling for the explanation of the company and referring the case to the Ministry of Law. Besides, though this case had been taken up with the Ministry of Law as early as August, 1974 according to the information furnished to the Committee it remains still under examination. The Committee deprecate such unconscionable delay in cases especially relating to monopoly concerns and big foreign business houses. The Committee desire that the reasons for delay should be explained and responsibility fixed for appropriate action. The Committee would like to know the final decision since taken in this case.

[Sl. No. 10 (Para 1·43) of Appendix IV to 187th Report of PAC (1975-76) (Fifth Lok Sabha)]

Action taken

M/s Britannia Biscuits Company operate three units manufacturing biscuits, one each in Calcutta, Bombay and Madras. The units in Calcutta and Madras are operated under Registration Certificates issued under Section 10 of the Industries (Dev. & Reg.) Act, 1951. These Registration Certificates, as per the then procedure, did not specify a particular figure as approved capacity. The unit at Madras is run under an Industrial Licence issued under the Industries (Dev. & Reg.) Act, 1951 for an annual capacity of 1200 tonnes for the manufacture of biscuits, but without specifying the number of shifts in the day to which this figure relates.

2. In July, 1972, the Company had applied by way of substantial expansion licence, for recognition of its reassessed capacity of 33,536 tonnes per annum of all the three units put together including the unit at Madras. In consultation with the Licensing Committee, the application of the Company was rejected in February, 1974. The Company made a representation against the above decision of the Government claiming, *inter alia*, that its increased production was attributable to normal circumstances and that there had been no increase in the means of production and consequently no violation of the provisions of the I (D & R) Act, 1951. This representation of the company was also rejected in August, 1974. The question of the action that could be taken in regard to excess production and violation of the licensing provisions that this implied was taken up and the case referred for advice to the Law Ministry immediately thereafter. The Law Ministry raised certain points for clarifications to establish whether the expansion was in violation of the provisions of the Act.

3. About this time, there were similar other cases engaging the attention of the Department which were also being gone into by the Law Ministry. That Ministry was of the view that the penal provisions of the Act punish only contravention of the provisions of the Act and not of the conditions such as level of authorised production, that might have been stipulated in the Industrial Licence.

4. In this connection it is also relevant to point out that certain cases of production in excess of the licensed capacity have been referred for enquiry by the Commission on Large Industrial Houss (Sarkar Commission). The Commission have yet to submit its report to the Government. Government have been awaiting the findings and recommendations of the Commission to decide on the course of action to be taken in such cases of excess production, as a matter of general policy.

5. Government fully share the concern expressed by the Committee about the delay that has occurred in finalising the course of action to be adopted in such cases. In the circumstances explained above, the Committee would, however, appreciate the procedural and legal constraints in the way of expeditious action. Suitable amendments to the Act to enable Government to deal with such cases firmly are now being processed.

6. One other consideration that has had to be kept in mind in this case has been that the Government of Tamilnadu has been strongly arguing against any decision or action that would limit production of the Madras unit of the Company below levels already reached. The State Government have been frequently writing to the Central Government for recognising and

regularising the enahanced production and the capacity that has been actually installed at this Unit, on the ground that it offers sizeable employment opportunities in the State.

7. The Committee may be assured that the matter will be gone into in all its aspects—legal, administrative and technological and a policy decision arrived at as urgenly as possible, in the light of the weighty observations contained in its 187th Report.

Recommendation

The Committee are also concerned to note that the relevant assessments relating to Dunlop India Ltd. had not been checked by Internal Audit, while in the case of United Commercial Bank Ltd. though the assessment for the year 1967-68 had been checked in Internal Audit, the patent short levy of additional tax was not detected. What is more distressing is that this assessment relating to a banking concern, in the high income bracket had been scrutinised only at the level of an Upper Division Clerk who has been warned for his failure to detect the mistake. In respect of the other three assessments, the explanation offered is one which has been too often placed before the Committee, namely, that the manpower resources of Internal Audit are inadequate. The Committee desire that the existing arrangements for Internal Audit should be reviewed and remedial steps taken forthwith. The Committee would also reiterate that all large income cases should invariably be checked at the level of the Inspecting Assistant Commissioner (Audit). The Committee are of the view that a pre-check of draft assessment orders by Internal Audit, recommended in paragraph 2·66 of their 187th Report (Fifth Lok Sabha) and reiterated in paragraph 1·17 of this Report would largely eliminate such unpardonable mistakes in assessment.

[S. No. 15 (Para 2·21) of Appendix IV to the 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

It has already been elucidated in reply to para 1·17 of this Report that it is not feasible to prescribe pre-check of draft assessment orders. However, regarding the post-checking of assessment orders involving large incomes, necessary steps are being taken for strengthening the Internal Audit organisation, both qualitatively and quantitatively. But it may not be possible for the IAC (Audit) to check all large income cases as the number of IACs (Audit) is inadequate and they have to attend to a very large number of Receipt Audit objections and draft audit paras proposed by the C&AG, apart from other administrative matters.

[Department of Revenue and Banking No. 236/7/73-A & PAC. II dated 9-6-1976].

Recommendation

The Committee are also of the view that it would be worthwhile for Government to undertake a detailed review of all such technical collaboration agreements entered into prior to 1965 by foreign enterprises operating in India and still in force, with a view to determining how far such agreements could be considered relevant to the Indian business of such enterprises concerned in the light of the development and changes that they might have undergone since the agreements were first entered into. In case the review discloses that some of the collaboration agreements have outlived their purpose and serve only as instruments of tax-avoidance, immediate action to treat the payments of technical know-how fees in these cases as inadmissible expenditure and subject them to tax should be initiated, in addition to terminating the agreements, by invoking, if necessary, the power of eminent domain that a sovereign country enjoys. In all future technical collaboration agreements approved by the Government, it should also be ensured that a clause for a periodical review of the agreements from the point of view of their relevance in the changed circumstances that may prevail is invariably incorporated. The Committee attach considerable importance to these recommendations and desire that they should be implemented expeditiously.

[S. No. 19 (Para. 2.25) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76)].

Action taken

2.25. Department of Economic Affairs were requested to take necessary action and intimate the results to this Department so that remedial action from the income-tax angle could be taken in suitable cases. It appears that the Department of Economic Affairs are compiling a list of such collaboration agreements in consultation with the Reserve Bank of India. Technical collaboration agreements now approved are valid for a period of 5 years from the date of commercial production and extensions of the agreements are approved by the Foreign Investment Board in exceptional cases. In view of this position, the Department of Economic Affairs have called for the comments of the Department of Industrial Development about the need for the inclusion of a clause for a periodical review of the agreements. Their final reply in the matter is awaited.

[Department of Revenue and Banking No. 236/7/77—A & PAC. II, dated 1-7-1976].

Further Information

"Attention is invited to this Department's reply of even number dated the 1st July, 1976.

The Department of Economic Affairs have offered the following comments on the recommendations of the Public Accounts Committee:

"We have consulted the Department of Industrial Development and the Reserve Bank of India, Bombay in this matter. As regards the PAC's suggestion that Government should undertake a detailed review of all technical collaboration agreements entered into prior to 1965 and still in force, we feel that it may not be necessary to appoint a group of officers to carry out the review of such cases for the following reasons:

(a) Prior to 1965, the policy of the Government was to approve technical collaboration agreements normally for a period of 10 years. It should, therefore, be presumed that most of the collaboration agreements approved prior to 1965 would have expired by now.

(b) In October 1969, this Ministry asked the RBI to advise Indian parties to terminate their collaboration agreements which had a run of 10 years and in case the Indian parties considered it necessary to have another agreement to replace the existing one, they should make a fresh application for the purpose of consideration by the Foreign Investment Board. (A copy of the letter dated 6th October, 1969 from the Department of Economic Affairs to the Reserve Bank of India on the subject was also furnished to the Committee which is reproduced in Chapter IV).

(c) The RBI have instructed their offices to insist upon specific Government's approval before allowing remittances beyond the period for which an agreement has been approved by Government or which had a run of 10 years whichever is less.

As regards the PAC's suggestion for incorporating a clause in the future technical collaboration agreements approved by Government for a periodical review of the agreements from the point of view of the relevance in the changed circumstances, the Department of Industrial Development have rightly pointed out that such a provision will scare away the prospective collaborator because it will create an element of uncertainty regarding the compensation which they are likely to get for technology provided to the Indian company. That Department have added that such a provision will not only inhibit the flow of technology to the Indian company but also may create legal complications, because an agreement entered into between an Indian company and the collaborator is a legal document. Morever the duration of the agreements now approved is for 5 years from the com-cement of production and when an Indian company comes up for extension of the agreement, a review of the agreement automatically takes place and this may be considered as an in-built provision for review. We agree with the Department of Industrial Development."

[Department of Revenue and Banking No. 236/7/73-A & PAC. II dated 7 September, 1976].

Recommendation

Now that an inter-Ministerial Working Group has also been appointed to examine in detail the policies and procedures under which IBM World Trade Corporation operates in India, the Committee desire that the entire issue of head office expenses claimed by the company and the remittances made by it should be gone into by the Working Group with a view to quantifying, in concrete and specific terms, the extent to which the country's scarce foreign exchange resources have been frittered away and exposing all the devious methods employed by this multi-national corporation to the detriment of the country's wider national interest.

[S. No. 28, (Para 3.36) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76)].

Action taken

As has already been stated in reply to para 3.35 of this Report, the Department of Electronics have been requested to send a copy of the report of the Inter-Ministerial Working Group.

[Department of Revenue and Baking No. 236/274/73—A & PAC-II dated 14-7-1976].

(COPY)

F. No. 500/11/76—FTD

GOVERNMENT OF INDIA

Central Board of Direct Taxes

New Delhi, Dated: 23rd March, 1976.

To

All Commissioners of Income-tax (By name)

SUB. : P.A.C.—187th Report—Para 3.39—Review by Government of claims for head office expenses made by foreign companies and banks—

The Public Accounts Committee in their 187th Report have, while dealing with the subject of head office expenses claimed by IBM World Trade Corporation, observed as under:—

"3.39. In view of the fact that there has been a substantial increase in the remittances made by foreign companies towards head office expenses during the years 1965—69, the Committee feel that it would be worthwhile for Government to review the veracity of the claims admitted during this period in respect of other foreign companies and banks as well. Since such a review is likely to yield rich dividends, the Committee desire that it should be undertaken forthwith, and would await a detailed report in this regard. It is, however, regrettable that the Central Board of Direct Taxes had not taken up so far a careful study of this problem with a view to ascertaining its magnitude and taking adequate steps to ensure proper tax compliance."

2. The Board desire that necessary action may be initiated to review the veracity of the claims made by foreign companies, including foreign banks, on account of head office expenses. This review should be carried out to cover the period from 1965 to 1969. Detailed instructions for the scrutiny of claims of head office expenses are contained in Board's letter F. No. 491/8/74—FTD (Instruction No. 846) dated 16th June, 1975.

3. The receipt of this letter should be acknowledged to the undersigned (by name) and the results of the review may please be intimated to the Board by 30th September, 1976.

Sd/-
(M. L. CHOUDHRY)
Secretary, Central Board of Direct Taxes.

Recommendation

Another unhappy feature of the case under scrutiny is that the collection of the additional tax due from Calcutta Electric Supply Corporation should have been kept in abeyance by the Commissioner of Income-tax till the disposal of the first appeal filed by the company before the Income-tax Appellate Tribunal. The Committee are distressed that an extra-legal concession, and that too without obtaining any security for the additional demand should have been extended to a defaulting but powerful and long entrenched foreign company on the basis of what has been described as 'the usual departmental practice'. The Chairman of the Central Board of Direct Taxes as well as the Commissioner of Income-tax, West Bengal-I, have admitted before the Committee that if the Department wanted to and did take 'a very stern and rigid view of the matter'. the recovery could be pressed and enforced. The Committee desire that principled action, even on occasion 'very stern and rigid', should be taken, which, it is feared, did not happen in this case. It would be of interest to know, in how many cases a similar concession had been extended, if only as a matter of convention, by the Income-tax Department to the multitude of small assessees.

[Sr. No. 47 (Para 4-84)of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)]

Action taken

In this case the very basis of the jurisdiction of the Income-tax Officer to make fresh assessments stood challenged in appeal before the Income-tax Appellate Tribunal...As the assessee company had substantial assets and had not defaulted in the past, the Department did not expect any risk to revenue in granting the stay for payment of additional demands raised in fresh assessment proceeding s.In granting such stays the furnishing of security is insisted upon onlyif there is any chance of loss of revenue It may, however, be mentioned that granting stay of demand without any security is a fairly common practice.

[Department of Revenue and Banking No. 236/330/73—A. & P.A.C. II dated 26-7-1976]

Sd/-
(R. S. CHADDA)
Additional Secretary to the Govt. of India

Recommendation

It is also surprising that neither the Inspecting Assistant Commissioner nor the Commissioner had looked into this case, even though

the charge in which the case had been assessed does not appear to have more than a few large income cases of this type. The Committee would like Government to find out whether the supervisory officials had inspected the ward in which the case was assessed at any time, after the assessment had been made and, if so, how this particular case had escaped their notice. In case there has been any remissness on their part in this regard, appropriate action should be initiated.

[Sr. No. 64 (Para 6.31) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

There is no doubt that this was the biggest revenue yielding case in that Charge. The case of this company has always been handled by a senior Income-tax Officer and was being subjected to checking by the Internal Audit annually. Unfortunately, there has been a failure on the part of the supervisory officials to inspect this case during the said period. Moreover, there had been a difference of opinion on the correct interpretation of Rule 3 of the Second Schedule to the Companies (Profits) Surtax Act, which was set at rest in April, 1974. In the circumstances, no action is considered necessary against any official. Of late, a number of steps have been taken to avoid such mistakes. In this connection the Department's reply to Para 1.8 of 192nd Report may be referred to.

[Department of Revenue and Banking No. 236/23/73—A&PAC II, dated 28-7-1976].

Recommendation

The Committee find that Gwalior Rayon Silk Manufacturing (W'vg.) Company Limited is being assessed at Indore even though most of the assessment relating to the Birla Group of companies are centralised in Central Circles or Special Circles in Bombay and Calcutta and a special cell has also been set up in Delhi to deal with the income-tax cases of this group. The response of the Ministry of Finance to an enquiry by the Committee into the reasons for this arrangement is a surprising silence. The Committee are of the view that the Income-tax cases of this company should also be transferred to the special cell at Delhi so that all ramifications which this particular unit of the Birla Group may have with the other units of the group could be unravelled and properly looked into.

[Sr. No. 66 (Para 6.33) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

The investigations in Gwalior Rayon Silk Manufacturing (W'vg.) Company limited as also other cases of the Birla Group, wherever assessed, are presently being supervised by the Special Cell under the Directorate of Inspection (Investigation), Delhi.

[Department of Revenue and Banking No. 236/23/73-A&. PAC II, dated 28-7-1976].

CHAPTER V

RECOMMENDATIONS/OBSERVATIONS IN RESPECT OF WHICH GOVERNMENT HAVE FURNISHED INTERIM REPLIES

Recommendation

The Committee are distressed to find that an expenditure of Rs. 0.99 lakh on scientific research had been allowed by the Income-tax Officer in this case without making precise enquiries as to what research was actually carried out and without ensuring whether it was a genuine expenditure on research and development related to the business of Britannia Biscuit Co. Ltd. The Committee have been informed in this connection that apart from the amount of Rs. 0.99 lakh allowed on this account for the assessment year 1968-69, further sum of Rs. 1.66 lakhs and Rs. 0.04 lakh have been allowed in respect of the assessment years 1970-71 and 1972-73 respectively. The assessments for the years 1969-70 and 1971-72 are stated to be pending and in respect of these two assessment years, Rs. 1.28 lakhs and Rs. 1.29 lakhs respectively have been claimed by the assessee company towards scientific research. The Committee desire that these claims should be carefully scrutinised by reopening the cases where necessary, in order to esure that the permissible deductions from the taxable income are fully justified. In case it is found that there had been misrepresentation of facts and that the deductions were incorrectly allowed, immediate action should be taken to subject the amounts to tax. The Committee would await a further report in this regard.

[S. No. 5 (Para 1.31) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

The Income-tax officer concerned has been directed to scrutinise the claims made in the different years carefully and submit detailed reports for considering action u/s 147 (a) and/or 263. However, in view of limitation for the assessment year 1967-68 the Income Tax officer has been directed to take immediate action u/s 147 (a) as a preliminary measure. The outcome of the scrutiny of the claims will be informed of the results in due course.

A reference is invited to this Department's reply of even number dated the 21st April, 1976. The assessment for the assessment year 1968-69 has since been set aside by the Commissioner of Income-tax concerned with the direction to the Income-tax Officer to make a fresh assessment. The reassessment will be made after making proper enquiries as to the precise nature of the scientific research carried out.

[Department of Revenue & Banking No. 236/90/73—A & PAC II dated 21-4-1976 and 13-9-76].

Recommendations

Another feature which has come to the notice of the Committee in respect of Dunlop India Ltd. is that the company has been remitting large sums abroad every year on the plea of reimbursement of technical know-how fees. During the seven-year period from 1965-66 to 1971-72 the remittance made on this account totalled £1.46 millions. In addition, the company has also claimed to have remitted, in 1972, a sum of Rs. 2.21,

lakhs alleged to represent reimbursement of technical expenses incurred by the U.K. company during the year ended 31st December, 1969 and this claim, according to the information furnished to the Committee by the Department of Revenue & Insurance, is to be considered by the Income-tax Officers, in the pending assessments of the two companies, namely, Dunlop India Ltd. and Dunlop Holdings Ltd., U.K., for the year 1973-74. It would appear that the Indian subsidiary company has been allowed to remit large sums as payment of technical know-how fees to the foreign holding company. While the payments for technical know-how could, perhaps, be justified during the initial period of establishment of a company, the Committee are doubtful how far the technical know-how would be relevant in the case of a well-established company like Dunlop India Ltd. in an advanced stage of development.

The Committee would, therefore, like to be satisfied that the remittances made on account of technical know-how fees by Dunlop India Ltd., were, in fact, fully justified and genuine and have not served as an instrument of tax-avoidance. The Committee desire that the technical know-how agreement entered into by the company should be thoroughly examined by the Department of Revenue & Insurance with a view to determining its relevance to the Indian business of Dunlop India Ltd. and ensuring that it is not a mere cloak for tax-avoidance. In case it is found that the remittances on this account have been claimed and allowed wrongly, appropriate action should be taken.

[S. Nos. 17, 18 (Paras 2.23 to 2.24) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76)].

Action taken

The Commissioner of Income-tax concerned as well as the Department of Industrial Development were requested to examine the points raised in these two recommendations for necessary action. The Commissioner of Income-tax has reported that the remittances have been made by the Indian concern as consideration for the rendering by the foreign company of current technical services.

The Department of Industrial Development have informed that the matter is under consideration.

(Department of Revenue & Banking No. 236/7/73—A & PAC II, dated 1-7-1976)

Recommendations

In view of the far-reaching implications of the disclosure now made by IBM World Trade Corporation that 'certain errors in the principle of allocating Headquarters Expense to India had been detected by its head office in New York' and that 'the erroneous calculations had resulted in excess claim on account of Headquarter expense' for the years 1966 to 1970, the Committee desire that all claims made by the Company on this account relating to periods prior to 1966 and after 1970 should be subjected

to a thorough scrutiny by the Investigation Cell set up by the Central Board of Direct Taxes to look into leading cases of tax evasion and malpractices. Besides, all the assessments of the company from 1960 to 1974 should also be strictly reviewed, with reference to the books of accounts of the company so as to establish the accuracy of the statements of receipts and expenditure and the genuineness of the allocation of expenditure between the Head Office of the company and the Indian unit and to ensure that no inadmissible expenditure is allowed to escape taxation and be repatriated abroad in foreign exchange. In case the review reveals that there has been a deliberate attempt by the Company to evade taxes, stringent penal action under the law should be taken forthwith against the company, besides levying and collecting the tax on the income that has escaped assessment. The correctness of recognising this multi-national giant as a company under the Income-tax Act should also be looked into in detail. The Committee would await a detailed report in regard to the action taken by Government on these recommendations.

The Committee also consider it rather significant that the application under section 271(4A), admitting excess claims on account of head office expenses, had been made by the company after the Audit paragraph had appeared in the Report of the Comptroller and Auditor General of India and after the Committee had also probed into some of the Indian operations of IBM World Trade Corporation in their 127th Report (Fifth Lok Sabha) on the installation of IBM computers on Indian Railways, which was presented to the Lok Sabha in April, 1974. Besides, the affairs of the company have also been taken up for scrutiny by an inter-Ministerial Working Group constituted by the Department of Electronics. Under these circumstances, the Committee have grave doubts whether the disclosure made by the company only in November, 1974 could be treated as a voluntary and not as one prompted by the fear of exposure. The Committee would, therefore, recommend that pending the completion of the comprehensive review suggested in paragraph 3.34 above, the application made under section 271(4A) of the Income-tax Act should be kept pending so that the assessee company does not escape the consequences of penalty and prosecution proceedings for claiming excess expenditure in a manner which, *prima facie*, appears to be dubious and even deliberate.

[S. Nos. 26&27 (Paras 3.34 & 3.35) of Appendix IV of 187th Report of the Public Accounts Committee (1975-76) (Fifth Lok Sabha)].

Action taken

The Special Cell has been directed to have investigations in this case completed in consultation with the Commissioner of Income-tax on a priority basis. The correctness of recognising this multinational Corporation as a company under the Income-tax Act is also being examined.

The Department of Electronics have been requested to send us a copy of the report of the Inter-Ministerial Working Group set up to look into the affairs of I.B.M. World Trade Corporation. Meanwhile, the application u/s 271(4A) of the Income tax Act, 1961 is being kept pending.

(Department of Revenue and Banking No. 236/274/73—A & PAC-II dated 28-6-1976).

Recommendation

Another distressing feature which has come to the notice of the Committee during their examination is the virtually passive role played by the Reserve Bank of India in the matter of permitting remittances by foreign companies from India towards head ofice expenses. The Committee have been informed that the Rseserve Bank does not undertake any scrutiny of the amounts applied for by foreign companies/banks towards remittances of head office expenses; nor does the bank call for a break-up of the items constituting the head office expenses. Prior to 1973, such remitances had been allowed by the Reserve Bank on a provisional, on-account basis, subject to the acceptance of the expenditure by the Income-tax authorites From the year 1973 onwards, the Bank has, however decided not to accept the claims on account of Head Office Expenses without the production of evidence by the foreign company/bank concerned that its claim that a part of the surplus is non-taxable—as being head office expenses chargeable to its Indian operations—has been accepted by the Income-tax authorities. Considering the fact that the scrutiny exercised in this regard by the Income-tax Officers appears to have been superficial and cursory, the Committee are doubtful how far the excessive reliance that is now being placed by the Reserve Bank on the Income-tax Department could be considered satisfactory. As the guardian of the country's scarce foreign exchange resources, the Committee feel that the Reserve Bank of India could and should play a more responsible and dynamic role in this regard. The Committee, therefore, desire that the adequacy of the existing procedures should be reviewed immediately and necessary measures taken to plug all loopholes in relation to operations by unscrupulous foreign investors.

The Committee would like Government to examine seriously how far remittances by foreign companies towards head office expenses should if at all, be permitted, and the Reserve Bank should move positively in this matter and take appropriate action thereatfter. In this context, the Committee consider it pertinent to draw the attention of Government to Article 2 of the UN Charter of Economic Rights and Duties adopted on 12th December, 1974 by the United Nations General Assembly, according to which each State has the right to regulate and exercise over foreign investment within its national jurisdiction in accordance with its laws and regulations and in conformity with its national objectives and priorities and to regulate and supervise the activities of transnational corporations within its national jurisdiction and take measures to ensure that such activities comply with its laws, rules and regulations and conform with its economic and social policies.

[S. No. 29 (Paras 3.37) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76)].

Action taken

The recommendations of the Committee have been brought to the notice of the Department of Economic Affairs and the Banking Wing of this Department and are presently under their consideration in consultation with the Reserve Bank of India.

(Department of Revenue & Banking No. 236/274/73—A & PAC-II, dated 14-7-1976).

Recommendation

As regards the short levy of interest for the belated filing of the return of income for the assessment year 1968-69, the Committee have been informed that additional demands totalling Rs. 50,318 have now been raised and that bulk of the additional demand has also been collected. The Committee desire that early steps should be taken to recover the balance also.

The Committee had also occasion to examine separately the grant of a large refund of Central Excise duty amounting to Rs. 1·37 crores on revision to J.K. Synthetics Ltd. The Committee have been informed by the Central Board of Direct Taxes that the Commissioner of Income-tax had been instructed, on 7th May, 1974, to look into this matter and verify that the refund had been fully accounted for in the books and the returns of income. A long time has passed since then, and the Committee would like to be apprised immediately of the results of the verification.

[S. No. 37 (Para 4.27) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76)].

Action taken

The ITO's order u/s 154 dated 3-12-73 creating an additional demand of Rs. 50,380 for the assessment year 1968-69 on account of short charge of interest u/s 139 has been set aside by the Appellate Tribunal *vide* its order dated 29-10-75. The Tribunal held that there was no mistake apparent from the records and therefore the provisions of sec. 154 are not applicable. A reference application u/s 256(1) filed before the Tribunal was rejected. The question of filing a reference application u/s 256(2) before the High Court is now under consideration. In the circumstances, the entire demand of Rs. 50,380/- stands wiped out and the question of collection of balance demand does not arise.

Recommendation

In this context, the Committee would once again draw the attention of Government to an earlier recommendation of theirs contained in paragraph 2.30 of their 128th Report (Fifth Lok Sabha), wherein the Committee, commenting on the part of some assessees to frustrate the rectification of even patent mistakes by seeking legal remedies on mere technical grounds, had suggested that Government should examine whether any amendment to the Act was necessary to ensure that the rectification of patent mistakes was not frustrated by assessees on such technical grounds. The Committee had then been informed by the Department of Revenue and Insurance that a similar recommendation of the Direct Taxes Enquiry Committee (Wanchoo Committee), that revenue matters, in respect of which adequate remedies are provided in the respective statutes themselves, should be excluded from the purview of Article 226 of the Constitution, was being examined by Government. The Committee would like to be informed of the final decision, if any, in this regard. In case a decision is yet to be taken on this recommendation, the Committee desire that this should be processed on a priority basis and the necessary amendment made, as this would greatly facilitate the collection of revenue.

The Committee note that the rectificatory proceedings under section 13 of the Act has been stayed by the Madhya Pradesh High Court on a writ petition filed by the assessee, challenging the issue of notice under section 13. This is one more instance where the rectification of even patent mistake has been frustrated by the assessee seeking a legal remedy. In this connection, the Committee would invite the attention of Government to an earlier recommendation of theirs contained in para 2.30 of their 128th Report (Fifth Lok Sabha) and reiterated in para 4.26 of this Report on the question of amending Article 226 of the Constitution in so far as it relates to revenue matters, in respect of which adequate remedies are provided in the respective statutes themselves.

[S. Nos. 36 & 65 (Paras 4.26 & 6.32) of Appendix IV to 187th Report of the Public Accounts Committee (1975-76 (Fifth Lok Sabha)]

Action taken

The question of barring the writ jurisdiction of courts in revenue matters is under consideration of the Ministry of Law and a decision thereon will be taken along with the decisions on other proposals for general amendment to the Constitution.

(Department of Revenue & Banking No. 241/13/76/A&PAC-I, dated 14-4-1976).

NEW DELHI;

December 20, 1977

Agrahayana 29, 1899 (*S*).

C. M. STEPHEN,

Chairman,

Public Accounts Committee.

STATEMENT OF CONCLUSIONS/RECOMMENDATIONS

Sl. No.	Para No. of Report	Ministry/Deptt. Concerned	Conclusion/Recommendation
1	2	3	4
1	1.3	Ministry of Finance (Department of Revenue)	According to the time schedule prescribed in the Committee's 5th Report (Fourth Lok Sabha) for the submission of Action Taken Notes on the Committee's recommendations/observations, the Notes indicating the action taken by Government on the recommendations/observations contained in the 187th Report (Fifth Lok Sabha) were required to be furnished to the Committee by 28 July, 1976. The Committee are happy that the Department of Revenue & Banking have furnished all the Action Taken Notes relevant to this Report by the stipulated date and have also accepted most of the Committee's recommendations. This is a welcome trend which, the Committee trust, would be maintained in future.
2	1.4	Do. . . .	The Committee expect that final replies to those recommendations/observations in respect of which only interim replies have so far been furnished will be submitted soon, after getting them vetted by Audit.
3	1.9	Do. . . .	It is not clear to the Committee how the pre-check by Internal Audit of the computation of income, suggested by them with a view to eliminating repetitive mistakes which have been coming to their notice year after year, is likely to dilute the assessing officer's responsibility

			or give rise to complaints that his judicial discretion is being hindered. The delays in the finalisation of assessments and issue of demand notices apprehended by the Department by prescribing such a counter-check before the assessments are finalised can also be overcome by prescribing a suitable time limit for the completion of the pre-check. The Committee regret that the Department have hardly given careful thought to a suggestion which could have been helpful. Government will do well to have the matter properly re-examined.
4	1.10	Do. . . .	The Department's reply to another important recommendation of the Committee that all large income cases should invariably be checked at the level of the Inspecting Assistant Commissioner (Audit) is entirely unconvincing. The scrutiny of large income cases, often involving complex points of law is found too often to have been left to Upper Division Clerks, as in the case relating to the United Commercial Bank Ltd., with results that are detrimental to revenue and not particularly complimentary to the Department. The argument that it may not be possible for the Inspecting Assistant Commissioner (Audit) to check all large income cases on account of pre-occupation with numerous Receipt Audit objections and also the draft Audit paragraphs proposed by the Comptroller & Auditor General of India does not appear valid or even particularly happy. The Department should, on the contrary, know that by ensuring careful scrutiny of large-income cases the possibility of mistakes remaining undetected would be minimised and would, in turn, lead to fewer Receipt Audit objections and draft Audit paragraphs. The Committee are, therefore, unable to accept the Department's contention in this regard and would reiterate their earlier recommendation.
5	1.15	Do. . . .	The Committee note that in pursuance of their recommendation contained in paragraph 1.31 of the 187th Report (Fifth Lok Sabha), the Income-tax Officer has been directed to carefully scrutinise the deduc-

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			tions claimed in the different years by Britannia Biscuit Co. Ltd., under Section 35(1)(i) of the Income-tax Act, and to submit detailed reports for considering rectificatory action under Sections 147(a) and/or 263 of the Act. The Committee would urge Government to complete the examination soon and adopt all consequential action under the Law.
6	1.16	Ministry of Finance (Deptt. of Revenue)	The Committee welcome the measures stated to have been taken to ensure that the provisions of Section 35(1)(ii) of the Income-tax Act relating to payments made to scientific research associations are not abused as they appear to have been by big industrial houses. It is felt, however, that a ceiling on such payments, as recommended by them, would have a salutary effect. The fact that it has been found necessary, on a review by the Indian Council of Medical Research of the performance of certain institutions, to withdraw the approval accorded in as many as eight cases reinforces the Committee's impression that checks and controls, if hitherto exercised in this matter, had been perfunctory. The Committee, therefore, would like Government to re-examine this question and take necessary steps to amend the law in this regard. In the meantime, the prescribed authorities under the Act and the Central Board of Direct Taxes should ensure that the regulatory apparatus functions effectively and that the various measures enumerated are strictly enforced.
7	1.19	Do. . . .	The Committee are concerned to observe that the question of Britannia Biscuit Co. Ltd., producing biscuits far in excess of the licensed capacity has been hanging fire for over four years now and conclusive action is yet to be taken, in a principled manner, against a big foreign business

			house for contravention of the conditions stipulated in the industrial licence. The elaborate explanation offered by the Department of Industrial Development for the delay is also by no means convincing, The Committee find from the sequence of events relating to this case that though the company had, as early as in July 1972, applied for recognition of its reassessed capacity of 33,536 tonnes per annum of its three units located at Calcutta, Bombay and Madras. Government took nearly 19 months to reject the application. A further period of six months had elapsed before the advice of the Law Ministry was sought, in August 1974, on the action that could be taken against the company for the excess production and the violation of the licensing provision that this implied. Some two years have elapsed since then and Government appear still to have preferred to admit the findings and recommendations of the Commission on large Industrial Houses (Sarkar Commission), to whom certain other cases of production in excess of the licensed capacity had been referred for enquiry, so as to decide, as a matter of general policy, on the course of action to be taken in such cases of excess production. The Committee are far from satisfied with this state of affairs and must insist on this long-pending issue being finalised without delay.
8	1.20	Do.	The Committee note the Law Ministry's view that the penal provisions of the Industrial (Development & Regulation) Act, 1951 punish only contravention of the provisions of the Act and not of the conditions, such as the level of authorised production, that might have been stipulated in the Industrial Licence, and that suitable amendment to the Act to enable Government to deal firmly with such cases are now being processed. The Committee would urge Government to complete this exercise early and remedy an unfortunate situation without further loss of time.
9	1.23	Do.	It is not very clear from the Department's reply whether the report stated to have been received from the Commissioner of Income-tax in regard

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		—	to the remittances made by Dunlop India Ltd. on account of technical know-how fees/technical expenses claimed to have been incurred by the company's counterpart in the United Kingdom, pertains only to the claim of Rs. 2·21 lakhs remitted in 1972 which was to have been considered in the pending assessments of the two companies for the year 1973-74, or to the remittances of over two crores of rupees made during the seven-year period from 1965-66 to 1971-72. If the latter be the case, the Committee are surprised over the extraordinary expedition with which the assessments spanning several years had been reviewed and a report also furnished to the Board. In any case, since technical know-how agreements, particularly between inter-related foreign companies, often serve as instruments of tax-avoidance, the Committee wish that, as desired by them earlier, the Department of Revenue & Banking had taken the initiative of re-examining this case and re-assured themselves of the correctness and genuineness of the claims made by the company. Such an examination should be undertaken forthwith. The examination of the case by the Department of Industrial Development also needs to be completed quickly. The feasibily of reopening the relevant assessments of the company with a view to safeguarding the interests of revenue, pending final determination of the relevancy of the technical know-how agreement in the changed circumstances that may be prevailing, should be decided upon.
10	1·27	Ministry of Finance (Deptt. of Revenue)	Government's reluctance to undertake a review of all technical collaboration agreements entered into before 1965 by foreign enterprises operating in India with a view to determining their relevancy in the changed circumstances that may prevail is difficult to appreciate. It is clear that the main thrust of the Committee's recommendation has not been pro-

perly understood by the Department of Economic Affairs. What the Committee had in view was only a review of technical collaboration agreements entered into by foreign enterprises operating in India and it was not their intention that the review extend also to the agreements entered into by purely Indian enterprises. Since the agreements of the former category are not likely to be very large in number, it should not be difficult for Government to meet the Committee's desire in this regard. In the absence of such a review and the relevant statistical data, the mere presumption that since Government policy prior to 1965 provided for the approval of technical collaboration agreements normally for a period of ten years, such agreements approved prior to 1965 would have expired by now is not enough to set at rest the Committee's genuine apprehensions arising from the facts made available to them in regard to the collaboration between Dunlop India Ltd. and Dunlop Holdings Ltd., U.K. as well as the technical services agreement entered into between National & Grindlays Bank Ltd. and the First National City Bank [which the Committee had examined in their 176th and 192nd Reports (Fifth Lok Sabha)]. Besides, it would also appear from the Department's letter dated 6 October 1969 that pending a decision on the question whether the existing agreement should be allowed to continue with or without amendments, which admittedly takes 'a long time' to reach, further payments continue to accrue to the foreign collaborator. These payments would become payable even in the event of Government deciding not to approve of the continuance of the collaboration on account of the obligation to give due notice for the termination of the agreement. The extent of benefits that would have accrued in these circumstances to the foreign collaborator by way of know-how fees and to the Indian unit of the foreign enterprise in the form of tax concessions during the period when the agreement is in suspended animation, is anybody's guess. The Committee would, therefore, reiterate their earlier recommendation in this regard and desire that the review suggested by them should be set in motion without further delay.

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11	1·28	Ministry of Finance (Deptt. of Revence)	As regards the incorporation of a clause in all future technical collaboration agreements to provide for a periodical review from the point of view of their relevance in the changed circumstances that may prevail, it has been contended by the Department of Industrial Development that such a provision will scare away prospective collaborators and inhibit the flow of technology to the Indian company. The Department have also added that such a provision may also create legal complications. While these 'legal complications' have not been spelt out clearly and should not in any case impede execution of our national policies, the Department's somewhat meticulous concern for foreign collaborators appears to be an anachronism, when viewed against Government's own declarations, in the recent past, for the promotion of indigenous technologies and planned phasing out of foreign collaborations. In the Committee's opinion, Government's fears in this regard are unfounded. They would, therefore, urge Government to have this issue re-examined carefully. The implementation of this important recommendation should not be difficult, particularly in the context of Government's avowed policy in this regard.
12	1·31	Do.	The Law Ministry's view that the Income Tax Officer has the power to call for the books of account of the head office of foreign companies operating in India and that an adverse inference could be drawn in the event of non-production of such books reinforces the Committee's impression that the important question of admissibility, from the tax angle, of the head office expenses claimed by such companies as IBM World Trade Corporation, National & Grindlays Bank, etc. still remains to be examined with any seriousness. It is surprising indeed that the Department of Revenue & Banking had formed the peculiar impression that 'in most of the cases or a large number of cases' it would

			not be possible to obtain the foreign accounts from the head offices of the companies for scrutiny. Now that the position has been clarified, the Committee trust that suitable instructions would be issued early so that a genuine scrutiny of the claims made by foreign companies can be effected.
13	1·35	Do.	The Committee note that the Special Cell set up in the Central Board of Direct Taxes has been entrusted with the task of investigating, on a priority basis, the claims made by IBM World Trade Corporation on account of head office expenses and that the correctness of recognising this multinational Corporation as a company under the Income-tax Act is also being examined. They would like these investigations to be completed quickly. As regards the question of recognising the corporation as a company under the Act, the Committee would invite attention to their observations contained in pagragraphs 6.1.72 and 6-1-73 of their 221st Report (Fifth Lok Sabha). The stage at which the application made by the company under Section 271(4A)(ii) of the Income Tax Act stands at present should be intimated to the Committee forthwith.
14	1·38	Do.	The Committee find that the reply furnished by the Department of Revenue & Banking to their recommendation contained in paragraph 3.36 of the 187th Report (Fifth Lok Sabha) that the entire issue of head office expenses claimed by IBM World Trade Corporation should be gone into by the inter-Ministerial Working Group appointed to examine the policies and procedures under which company operates in India is not quite relevant. What the Committee had wanted was that this aspect should be included as one of the specific terms of reference of the Working Group. Action in this regard should be initiated forthwith so that all the devious methods adopted by the company to the detriment of the country's wider national interest are adequately exposed and appropriately dealt with.

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15	1.41	Ministry of Finance (Deptt. of Revenue)	The Committee note that the Income-tax Appellate Tribunal has held, by its order dated 31 October 1975, that there was no justification in taking action, under Section 263 for the assessment year 1968-69, withdrawing the relief allowed to J.K. Synthetics Ltd. under Section 80-I as well as the higher development rebate allowed under Section 33(1)(b)(B). Besides, it has also held that seven on merits, Nylon-6, manufactured from caprolactum, is a petrochemical and is covered by item 18 of the Fifth and Sixth Schedules of the Income-tax Act. A reference application filed by the Department, under Section 256(1), having been rejected by the Tribunal, the question of filing a reference under Section 256(2) before the High Court was under consideration. Considerable time has elapsed since then. The Committee trust that an early decision will be taken by the Department in this matter.
16	1.44	Do.	The Committee are surprised that a large sum of Rs. 1.37 crores received by J.K. Synthetics Ltd. as refund of Central Excise duty during September-December 1972 as well as a further sum of Rs. 68.84 lakhs which became due to the company on this account had not been disclosed either in their Profit & Loss Account or in the returns of income. The Committee expect that while examining in detail the question of assessing these refunds to Income Tax during the course of pending assessment proceedings for the assessment year 1973-74, the question whether there has been deliberate concealment of Income will also be gone into.
17	1.47	Do.	Though the Committee, in paragraph 4.84 of their 187th Report (Fifth Lok Sabha) had specifically enquired into the number of cases relating to small assessees in which a stay of demand had been granted by the

			Department, if only as a matter of convention, they find the Department's reply in this regard to be vague. The Committee apprehend that this extra-legal concession is liable to be exploited more in the interests of large income assessees. The Department should examine the legality and wisdom of persisting with what has been described as 'the usual departmental practice'.
18	1.50	Do.	Since it has been conceded by the Department of Revenue & Banking (Revenue Wing) that there has been a failure on the part of the supervisory officials to inspect the case relating to Gwalior Rayon Silk Manufacturing (Wvg) Company Limited, even though this was the biggest revenue yielding case in that Charge. The Committee are unable to accept the plea that no action is considered necessary against any official for this failure. In view of the fact that responsible supervisory officers have been remiss in the discharge of the responsibilities cast on them, the Committee would reiterate that appropriate action should be taken.
19	1.53	Do.	The Committee note that the investigations relating to Gwalior Rayon Silk Manufacturing (Wvg.) Company Limited are presently being supervised by the Special Cell under the Directorate of Inspection (Investigation). They, however, find that the reasons for not centralising the assessments relating to this company in a Central or Special circle, as has been done in the case of other assessments relating to the Birla Group of companies, specifically enquired into by them, are yet to be intimated. The position requires to be fully clarified without delay.

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