

**FORTY-FIRST REPORT**  
**PUBLIC ACCOUNTS COMMITTEE**  
**(2002-2003)**

**(THIRTEENTH LOK SABHA)**

**EXPORT INCENTIVES AND DEDUCTIONS**  
**IN RESPECT OF PROFITS RETAINED FOR**  
**EXPORT BUSINESS**

*[Action Taken on 34th Report of Public Accounts Committee  
(13th Lok Sabha)]*



*Presented to Lok Sabha on : 19 December, 2002*  
*Laid in Rajya Sabha on : 19 December, 2002*

**LOK SABHA SECRETARIAT**  
**NEW DELHI**

*December, 2002/Agrahayana, 1924(Saka)*

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**COMPOSITION OF PUBLIC ACCOUNTS COMMITTEE  
(2002-2003)**

Sardar Buta Singh — *Chairman*

**MEMBERS**

*Lok Sabha*

2. Shri Haribhai Chaudhary
3. Shri M.O.H. Farook
4. Dr. Madan Prasad Jaiswal
5. Shri Bhartruhari Mahtab
6. Dr. K. Malaisamy
7. Dr. M.V.V.S. Murthi
8. Shri Rupchand Pal
9. Shri Prakash Paranjpe
10. Shri Ramsagar Rawat
11. Shri N. Janardhana Reddy
12. Shri Chhatrapal Singh
13. Shri Kirit Somaiya
14. Shri Chinmayanand Swami
15. Shri Brij Bhushan Sharan Singh

*Rajya Sabha*

16. Shri S. Agniraj
17. Shri Santosh Bagrodia
18. Shri Prasanta Chatterjee
19. Shri K. Rahman Khan
20. Shri Bachani Lekhraj
21. Dr. Alladi P. Rajkumar
22. Prof. Ram Gopal Yadav

**SECRETARIAT**

1. Shri P.D.T. Achary — *Additional Secretary*
2. Shri K.V. Rao — *Joint Secretary*
3. Shri Devender Singh — *Deputy Secretary*
4. Smt. Anita B. Panda — *Assistant Director*

## INTRODUCTION

I, the Chairman, Public Accounts Committee having been authorised by the Committee to present the Report on their behalf, do present this Forty-First Report on action taken by Government on the recommendations of the Public Accounts Committee contained in their 34th Report (13th Lok Sabha) on "Export Incentives and Deductions in Respect of Profits Retained for Export Business".

2. This Report was considered and adopted by the Public Accounts Committee at their sitting held on 17th December, 2002. Minutes of the Sittings form Part II of the Report.

3. For facility of reference and convenience, the observations and recommendations of the Committee have been printed in thick type in the body of the Report and have also been reproduced in a consolidated form in Appendix\* to the Report.

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

NEW DELHI;  
17 December, 2002  

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26 Agrahayana, 1924 (Saka)

SARDAR BUTA SINGH,  
*Chairman,*  
*Public Accounts Committee.*

## CHAPTER-I

### REPORT

This Report of the Committee deals with the Action Taken by the Government on the Observations/Recommendations of the Public Accounts Committee [13th Lok Sabha] contained in their 34th Report on Para 3.1 of the Report of the Comptroller and Auditor General of India for the year ended 31 March, 1998, No. 12 of 1999, Union Government (Civil) relating to "Export Incentives and Deductions in respect of Profits Retained for Export Business".

2. The Report was presented to Lok Sabha on 24 April, 2002 and contained six Observations/Recommendations. The Action Taken Notes have been received in respect of all observations/recommendations and have been categorized as follows:—

(i) Observations/Recommendations that have been accepted by the Government:—

Sl. Nos. 1, 2, 3, 4, 5 and 6  
[Paragraph Nos. 45, 46, 47, 48, 49 and 50]

(ii) Observations/Recommendations which the Committee do not desire to pursue in the light of the replies received from the Government:

NIL

(iii) Observations/Recommendations replies which have not been accepted by the Committee and requires reiteration:

NIL

(iv) Observations/Recommendations in respect of which the Government have furnished interim replies:

NIL

3. On examination of the subject the Committee had found several disquieting aspects in the working of the fiscal benefits scheme introduced by the Government under the Income Tax Act (Sections 10A, 10B of Chapter III and Section 80HHC of Chapter VI) in the 1980s with a view to encouraging establishment of export oriented industries to boost the foreign exchange earnings for the country, including irregular deductions involving and aggregate tax effect of Rs. 43874 lakh, incorrect computation of direct and indirect taxes, allowing deduction

despite non-realisation of foreign exchange and non-maintenance of records. The Committee therefore, had *inter-alia* recommended to the Government:—

- (i) To make optimum use of computronics and devise mechanism to receive, collate and maintain necessary data at a centralised level;
- (ii) To take appropriate remedial measures on the findings of Expert Committee which was appointed by the Government in the year 1999 to identify misuse of the export incentives and deductions and recommend thereon;
- (iii) To have a re-look at the tax exemptions for profits made from Domestic Tariff Area (DTA) sales;
- (iv) To revamp Internal Audit mechanism in the CBDT so as to keep stringent check on financial irregularities;
- (v) To prepare a compendium of common mistakes made by Assessing Officers as noticed at the time of internal as well as Receipt Audit; and
- (vi) To strengthen coordination mechanism between the Ministries of Commerce and Finance & Company Affairs.

**Revamping of Internal Audit setup and preparation of Compendium of common mistakes by the Assessing Officers**

[Sl. No. 2, Para No. 49]

4. The Committee had expressed their deep concern over the large scale irregularities involving substantial loss of Government revenue owing to mistakes committed by the A.Os during the course of assessment despite existence of Internal Audit wing in the CBDT. The Committee, therefore, had desired the Ministry to qualitatively strengthen their Internal Audit wing as well as to prepare a Compendium of common mistakes committed by the AOs and circulate it expeditiously for the guidance of AOs. The Committee had further observed that there was an immediate need for effective coordination between the Ministries of Commerce and Finance, particularly with respect to the exercise of delegated power by officials to monitor Export Processing Zones.

5. The Ministry of Finance and Company Affairs (Department of Revenue — CBDT) in their Action Taken replies have, *inter-alia*, stated that a new Internal Audit setup has been created by them under which each A.O. including the JCIT Ranges will do auditing on a chain basis (Annexure-I). The Ministry have also stated that a Compendium of common mistakes detected by the Receipt Audit and the internal audit parties during the last three years has been prepared for the guidance of A.Os (Annexure-II). Further, the

Ministry have noted comments of the Committee for improving the coordination between the Ministries of Commerce and Finance and Company Affairs.

6. The Committee are happy to note that the Ministry have accepted all the recommendations contained in their 34th Report. The Committee appreciate the efforts made by the Department of Revenue, Ministry of Finance and Company Affairs in introducing the concept of "audit chains" through a revised Internal Audit mechanism which is broad-based and has a wide scope to include audit relating to the work of Tax Recovery Officers (TROs) and the Office Superintendents/Administrative Officers. The Committee hope that the Compendium of Common mistakes containing selective instances of typical mistakes repeatedly committed by the A.Os as prepared by the Department would prove a handy guide and reference work for A.Os. The Committee, however, reiterate the need for sensitising the A.Os on a continuous basis so that recurring glaring mistakes in assessment leading to substantial revenue loss are avoided. The Committee also hope that the Internal Audit Manual would be updated expeditiously and the AOs imparted periodic orientation/training so as to update their knowledge of the case law.

7. In so far as the coordination between the Ministries of Finance and Commerce with respect to the exercise of delegated powers by officials to monitor Export Processing Zones is concerned, the Committee are far from satisfied. The Committee feel that their recommendations for effective inter-ministerial coordination has failed to evoke requisite response and, therefore, the Committee reiterate their recommendation for effective coordination between Ministries of Finance and Commerce.



## CHAPTER II

### RECOMMENDATIONS/OBSERVATIONS WHICH HAVE BEEN ACCEPTED BY GOVERNMENT

#### Recommendation

The Committee note that the Export Incentives and Deductions Scheme under the Income tax Act was initiated by the Government in the Eighties, when the country was facing a difficult external debt and balance of payment position, to encourage the establishment of Export-oriented industries and provide a boost to the foreign exchange earnings of the country. According to the scheme, Sections 10A, 10B and 80HHC were introduced in the Income Tax Act providing direct tax exemptions and deductions, subject to certain conditions, to assesseees engaged in export activity. The Committee's examination has revealed that the direct tax exemptions had a positive psychological effect on the exporters and helped them expand their capital base, and it also marginally contributed to the growth of export trade. The Committee, however, note that the Government paid a heavy price in the form of substantial direct revenue loss owing to misuse of the provisions by unscrupulous businessmen who channelised their unaccounted income into export profits to evade tax.

Audit appraisal of the scheme reveals that although there was a net increase by more than 3 times in net foreign exchange realizations from 1994-95 to 1996-97 and a sharp increase by more than two and a half times in the number of beneficiaries, irregular concessions to exporters in 1273 cases out of 6680 cases test-checked, led to short levy of tax of Rs. 43874 lakh, constituting 16 per cent of total revenue concession. Out of 6509 cases covered under Section 80HHC and test checked, the audit detected 1221 cases of irregular deductions involving Rs. 54607 lakh with a revenue effect of Rs. 37051 lakh constituting 13 per cent of revenue foregone as a direct result of irregular deductions/reliefs and concessions. The Committee cannot but express their dissatisfaction over the fact that it took the Government 16 long years (after C&AG's Audit) to set up an expert Committee to examine the efficacy of the provisions of the Income Tax Act offering special fiscal benefits for export of goods or merchandise.

[Para 45 of the 34th Report of the PAC (2001-2002)—13th Lok Sabha]

#### Action Taken

The Comments of the Committee are duly noted.

[Ministry of Finance & Co. Affairs/Department of Revenue O.M.  
No. 241/2002-A&PAC-II dated 22.11.2002]



### **Recommendation**

The Committee note that out of 81 illustrative cases contained in the report of C&AG which was presented in December, 1999, the Ministry were unable to submit their comments on 16 cases till September, 2001 on the ground that the requisite information was still awaited from the field formations. Obviously, the Committee considers it a reflection on the ability of the Board to glean information relating to cases test checked in Audit belonging to the Assessment Year as far back as 1992-93. In view of the deposition of the representatives of the Board before the Committee that no data registers have been maintained by CBDT in respect of assessee availing export incentives under the Sections 10A, 10B and 80HHC (or any other deduction under Chapter VIA of the Act), the Committee reiterate that it would not be possible to gauge the impact of the scheme in totality except with reference to the cases test-checked in Audit. The Committee observes that lack of proper data is a serious impediment in evaluating the efficacy/impact of the special schemes launched by the Government. The Committee, therefore, recommend that the Board should make optimum use of computronics and devise mechanism to receive, collate and maintain necessary data at a Centralised level so as to assessee the effectiveness of the special schemes/provisions of the Act. The Committee hopes that the Ministry will get necessary data from their field formations and submit final replies to the cases referred to in the Audit paragraph.

[Para 46 of the 34th Report of the PAC (2001-2002)—13th Lok Sabha]

### **Action Taken**

Comments have since been furnished to Audit in all the illustrative cases included in review.

Board have already taken up large scale computerization of the Department. The recommendations of the Committee have been communicated to all field formations for compliance.

[Ministry of Finance & Co. Affairs, Department of Revenue O.M. No. 241/2002-A&PAC-II dated: 22.11.2002]

### **Recommendation**

As regards the overall provisions in the Income Tax Act, which enable an assessee to obtain benefits out of the Export Incentives & Deductions, the Committee feel that the scheme suffers from gaping loopholes, particularly, of not providing certification of accounts by a Chartered Accountant while claiming incentives under Section 10A and 10B. Although the Committee note that the Government have amended section

10A to include a proviso that the deductions under 10A and 10B would not be admissible for the assessment year 2001-2002 onwards, unless the assessee furnishes a report from a Chartered Accountant about correctness of claims, the Committee feel that the non-provision of certification of the accounts of an assessee by a Chartered Accountant under Sections 10A & 10B must have led to a substantial number of cases of wrong claims being filed and entertained. They feel that the Ministry should have provided some in-built safeguard by making such a certification mandatory for assessees claiming exemption under Sections 10A & 10B of the Income Tax Act. The Committee are in agreement with the findings of the Expert Committee appointed by the Department which concludes that misuse of incentives and benefits provisions have resulted in unscrupulous exporters enjoying the subsidized credit facilities given by the Government who utilize their huge unaccounted tax-free profits not for export-oriented activities but for leading a lavish life style and other supposedly lucrative businesses, like shares, construction activity and film production etc. The Committee hopes the Department takes appropriate remedial measures on the findings of the Expert Committee to plug the loopholes.

[Para 47 of the 34th Report of PAC (2001-2002)—13th Lok Sabha]

#### **Action Taken**

Realizing that the fiscal incentives for the promotion of exports have been misused and have outlived their utility, the provisions are slowly being phased out. Accordingly, section 10A and 10B were substituted by new sections by the Finance Act 2000 wherein a sunset clause has been inserted so as to ensure that no exemption would be available from the assessment year 2010-11 onwards. The new sections also have made it mandatory for submitting a certificate from Chartered Accountant in order to be eligible for the exemption. Further, section 80HHC, 80HHD, 80HHE have also been amended to phase out the deductions available over the years so that no deduction is allowable from assessment year 2005-06 onwards.

[Ministry of Finance & Co. Affairs, Department of Revenue O.M. No. 241/2002-A&PAC-II dated: 22.11.2002]

#### **Recommendation**

Audit had observed that under the Exim Policy (1992-97), the industrial units in FTZs were liable to pay excise duty at a concessional rate on the goods sold in the DTA. The Department could not explain to the Committee as to why goods sold by such units in DTA could be treated as exports for availing the benefit of Sections 10A & 10B of the Income Tax Act. In view of the Audit observation that similar provisions should be made for taxing the profits earned by such units by DTA sales, since by selling their manufactured goods in the internal market, the assesseees were still making profits and by granting tax reliefs to such sales, the income earned within the country was being tax exempted through provisions

made for exports, the Committee feel that tax exemptions for profits made from DTA sales need a re-look so as to ensure that the interest of revenue is safeguarded and the provisions is not misused.

[Para 48 of the 34th Report of PAC (2001-2002)—13th Lok Sabha]

#### **Action Taken**

In the newly substituted section 10A and 10B (by the Finance Act 2000) the profits of the respective units eligible for exemption have been defined as the amount which bears to the total profits of the business, the same proportion as export turnover bears to the total turnover. From this it is clear that profits from DTA sales would not be exempted thereby plugging the earlier loophole.

[Ministry of Finance & Co. Affairs, Department of Revenue O.M. No. 241/1/2002-A&PAC-II dated: 22.11.2002]

#### **Recommendation**

The Committee reject the reason cited by the Ministry for large scale irregularities involving substantial loss of Government Revenue owing to mistakes said to be committed inadvertently during the normal course of assessment by the Assessing Officers. The Committee is disappointed to note that despite existence of an Internal Audit Wing in the CBDT, the cases mentioned in the C&AG's report could not be detected, ostensibly due to shortage of manpower in the Internal Audit Wing. The Committee reiterate their recommendation (75th & 194th Reports — 7th Lok Sabha) as to the need for qualitatively strengthening the Internal Audit Wing as they believe that any extra expenditure incurred on this account is certain to be more than compensated by increase in revenue as a result of detection of mistakes by the Internal Audit Wing. The Committee observe that there is an immediate need for effective coordination between the Ministries of Commerce and Finance, particularly with respect to the exercise of delegated powers by officials, to monitor Export Processing Zones. The Committee would also urge upon the Government to take essential remedial measures including the revamping of Internal Audit Wing and strengthen coordination mechanism between the Ministries of Commerce and Finance so as to keep stringent check on financial irregularities. The Committee would also like the Department to prepare the compendium of common mistakes made by the Assessing Officers as noticed at the time of Internal as well as Receipt audit and circulate it expeditiously, as proposed by it, for the guidance of assessing officers. [Para 49 of the 34th Report of PAC (2001-2002)—13th Lok Sabha]

#### **Action Taken**

The Comments of the Committee for improving the coordination between the Ministry of Commerce and Finance are duly noted.

With the restructuring of the Income Tax Department, a new internal Audit set-up has been created by the CBDT, *vide* Instruction No. 08/2001

dt. 6.12.2001 (Copy enclosed).<sup>\*</sup> In the new Internal Audit set-up each assessing officer including the JCIT Ranges are required to do auditing work on a chain basis. Thus the number of officers deployed for internal Audit work in the new set-up will be around 6000, which includes around 700 JCITs. The new audit set-up will become fully operational during 2002-2003 and as per the scheme of new internal audit system all the auditable cases have to be disposed off during the same financial year. Thus the new internal Audit set-up will give a better coverage and it will also give quality because almost all the assessing officers will be involved in the auditing function.

A Compendium of common mistakes detected by the Receipt Audit and the Internal audit parties during the last three years has been prepared for the guidance of assessing officers.<sup>\*\*</sup>

[Ministry of Finance & Co. Affairs, Department of Revenue O.M. No. 241/2002-A&PAC-II, dated 22.11.2002]

#### **Recommendation**

The Committee observe that the findings of the Expert Committee appointed by the CBDT open a Pandora's box insofar as it concerns various defects/loopholes/shortcomings in the operation of the scheme. In the considered opinion of the Committee, there could not, perhaps, be more severe indictment of the scheme than what the Expert Committee has concluded, namely, that the export benefits under the direct taxes have outlived their utility and were more relevant in the 80's and 90's and that they are currently being misused. The Committee, therefore, refrains from commenting further in the matter in view of the findings and observations of the Expert Committee and the steps already taken by the Government to phase out export deductions completely by 2005-06. The Committee, would, however, like to be apprised of the conclusive action taken on all the recommendations/observations of the Expert Committee in due course.

[Para 50 of the 34th Report of PAC(2001-2002)—13th Lok Sabha]

#### **Action Taken**

As stated in the reply to para 47 the export incentives under sections 10A, 10B and 80HHC, 80HHD, 80HHE are already in the process of being phased out.

[Ministry of Finance & Co. Affairs, Department of Revenue O.M. No. 241/2002-A&PAC-II, dated 20.11.2002]

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<sup>\*</sup>Annexure I

<sup>\*\*</sup>Annexure II

**CHAPTER III**

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

**—NIL—**

**CHAPTER IV**

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

**--NIL--**

**CHAPTER V**

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

—NIL—

NEW DELHI;  
17 December, 2002  

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26 Agrahayana, 1924 (Saka)

SARDAR BUTA SINGH,  
*Chairman,*  
*Public Accounts Committee.*

**APPENDICES**  
**APPENDIX I**  
**CONCLUSIONS AND RECOMMENDATIONS**

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Sl. No.	Para No.	Ministry concerned	Conclusions and Recommendations
1.	6	Finance and Company Affairs (Department of Revenue)	The Committee are happy to note that the Ministry have accepted all the recommendations contained in their 34th Report. The Committee appreciate the efforts made by the Department of Revenue, Ministry of Finance and Company Affairs in introducing the concept of "audit chains" through a revised Internal Audit mechanism which is broad-based and has a wide scope to include audit relating to the work of Tax Recovery Officers (TROs) and the Office Superintendents/Administrative Officers. The Committee hope that the Compendium of Common mistakes containing selective instances of typical mistakes repeatedly committed by the A.Os as prepared by the Department would prove a handy guide and reference work for A.Os. The Committee, however, reiterate the need for sensitising the A.Os on a continuous basis so that recurring glaring mistakes in assessment leading to substantial revenue loss are avoided. The Committee also hope that the Internal Audit Manual would be updated expeditiously and the AOs imparted periodic orientation / training so as to update their knowledge of the case law.

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Sl. No.	Para No.	Ministry concerned	Conclusions and Recommendations
2.	7.	Finance and Company Affairs (Department of Revenue)	In so far as the coordination between the Ministries of Finance and Commerce with respect to the exercise of delegated powers by officials to monitor Export Processing Zones is concerned, the Committee are far from satisfied. The Committee feel that their recommendations for effective inter-ministerial coordination has failed to evoke requisite response and, therefore, the Committee reiterate their recommendation for effective coordination between Ministries of Finance and Commerce.

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**APPENDIX II**

**INSTRUCTION NO. 08/2001**

**F.NO. 246/129/2000-A&PAC.I**

**GOVERNMENT OF INDIA  
Ministry of Finance  
Department of Revenue  
Central Board of Direct Taxes**

**New Delhi: Dated: 6-12-2001**

**To**

**All Chief Commissioners of Income-Tax  
All Directors General of Income-Tax,  
All Commissioners of Income-Tax**

**Sir,**

**SUBJECT: *Restructuring of the Internal Audit System—instructions-Reg.—***

As part of restructuring of Income-Tax Department, it has been decided to replace the existing internal audit system with a new system of internal audit from this financial year. Till now the work of internal audit was being conducted with manpower exclusively assigned the audit work (about 200 officers and 300 staff). The new system of internal audit would involve all the JCITs (Ranges) and the Assessing Officers in audit work about 6000 persons). The new system will be broad based and will have wider scope to include audit relating to the work of TROs and the Office superintendents/ Administrative Officers. Under the new system, audit work will be conducted on "chain basis" and the audit function will be a continuous process. For example, audit of Assessing Officers of one range will be conducted by the Assessing Officers of another range within a month of completion of assessment. The objective, scope and functions of the Internal Audit remain the same as mentioned in the existing Internal Audit Manual Volume-I.

**2.00 Creation of audit chains in metropolitan charges of Mumbai, Chennai, Delhi and Kolkata**

At present four CITs (Audit) have been posted in metropolitan charges. The concerned cadre controlling CCIT in these four metropolitan charges shall provide man-power to the CIT (Audit) similar to that of an

Administrative CIT as these posts of CIT (Audit) have been created by diverting the post of an administrative commissioner in these locations. It will be the duty of the CIT (Audit) to create "Audit Chains" indicating the CIT whose JCIT (Ranges), TROs and Office Superintendents will conduct the audit of various Ranges, TROs and Office Superintendents under the charge of another CIT. The audit chains will be set up in such a manner that all the audit work of one CIT will be conducted by the Ranges, TROs and superintendents posted under another CIT. The CIT (Audit) will keep a record of audit chains thus created and will inform the concerned CCITs, CITs, JCIT (Ranges), TROs and Superintendents. The JCIT Ranges in turn will create similar chains of the Assessing Officers for auditing the work of a particular Assessing Officer (Ward/Circle) of the Auditee Range [Example : ITO Ward (1)(1) will audit the work of ITO Ward (2)(1) in the chain of JCIT Range-1 assigned the Audit of JCIT range-2]. He will keep record of such chains and send copy to the CIT, JCIT (Auditee), Assessing Officers concerned and CIT (Audit). The work of audit chain creation should be completed within one month from the issue of this instruction. CIT (Audit) shall consolidate the audit chains created by him, by CIT (Admn.) and by the JCITs Ranges and send copy to the DIT (Audit).

### **3.00 Audit of Central Charges in four metropolitan charges of Mumbai, Chennai, Delhi and Kolkata**

In view of the complexities involved in Central Cases, and also in view of the heavy work load of JCIT Range in Central Circles, it has been decided that CIT (Audit) in the metropolitan charges will conduct the internal audit of CITs (Central) Charges. The CIT (Audit) will form audit parties headed by JCIT/DCIT/ACIT or ITOs/Inspectors, as the case may be, from the staff strength provided to the CIT (Audit). The CIT (Audit) will maintain all prescribed records for audit work and will also watch the settlement of audit objections. He will send the prescribed monthly reports to DGIT (Investigation), who will forward it to DIT (Audit)CBDT.

### **4.00 Other CCITs/DGITs (Investigation) charges**

In the non-metro CCIT/DGIT (Investigation) charges, the audit chains will be created by the CCIT/DGIT (Investigation) indicating the CIT charge whose JCITs Ranges and Assessing Officers will audit the work of another CIT charge in the same station if the particular station is multi-CIT charge. In single CIT charges, chains may be created from within the ranges under the same CIT charge. The CCIT/DGIT (Investigation) will keep record of such chains and send copy of the same to the cadre controlling CCIT, CITs/JCITs and to the DIT (Audit). The CITs will create further chains of JCITs who in turn will create further chains of

Assessing Officers, TROs and Administrative Officers/Superintendents and will maintain record of such chains, and send a copy of the same to the CCIT/DGIT (Investigation), concerned CITs, JCITs, Assessing Officers, TROs and Superintendents. This work should be completed within one month from the date of issue of this instruction. CCIT/DGIT (Investigation) shall consolidate the record of such chains created by them, by CITs (Administration) and JCITs Ranges and send copies of such consolidated orders to the DIT (Audit).

#### **5.00 Role and functions of various authorities in new audit set-up**

##### **5.01 Role of CCIT / DGIT (Investigation)**

Each CCIT/DGIT (Investigation) shall provide for a small unit in his office from the existing strength provided to him to ensure smooth functioning of both the Internal Audit work and the Receipt Audit work. Such unit should be under the control of a DCIT/ACIT, if required, as an additional charge. The CCIT/DGIT (Investigation) office shall be responsible for obtaining the statistical reports from the CIT/CIT (Audit) in four metropolitan charges and after consolidation, forward it to DIT (Audit)/CBDT. In non-metropolitan charges they will establish the audit chain and will monitor the audit work of CIT (Administration).

##### **5.02 Role of CIT (Administration)**

Each CIT (Administration) shall provide for a small unit in his office from the existing strength provided to him to ensure smooth functioning of both the Internal Audit work and the Receipt Audit work. Such unit should be under the control of a DCIT/ACIT, if required, as an additional charge. CIT (Administration) shall be responsible for audit work of his jurisdiction and the conduct of audit of the Ranges assigned to his JCITs. He shall monitor the smooth functioning of the audit chains, maintenance of proper records and settlement of objections. He shall maintain ledger cards in respect of officers for all the major internal audit objections. He will consolidate and send monthly report about the audit work in the prescribed proforma to the CCIT. He will provide training, audit-manuals, Circulars, Instructions and gist of common mistakes committed by the Assessing Officers as pointed out by C&AG in their annual audit reports submitted to the Parliament. He will also bring to the notice of CBDT any important point of law which comes to his notice during the audit work. Final acceptance/non-acceptance of audit objection will tax effect exceeding Rs. 50,000/- will be decided by CIT (Administration) and he shall ensure quick remedial actions in such cases. CIT (Administration) will comment on audit performances of JCITs and Assessing Officers/TROs/ Administrative Officers/Superintendents in their annual confidential reports.

### 5.03 Role of JCIT (Range)

Each JCIT shall provide for a small unit in his office from the existing strength provided to him to ensure smooth functioning of both the Internal Audit work and the Receipt Audit work. Such unit should be under the control of an Administrative Officer/Superintendents, if required, as an additional charge. He will have twin functions of being in charge of auditing range and also of the auditee range. His duties would therefore include:

#### (a) As JCIT (Auditing) Range

- (i) Creation of the audit chains of Assessing Officers, TROs and Superintendents and keeping record of such chains.
- (ii) Maintenance of audit records in prescribed registers and folders.
- (iii) Audit of cases with assessed income/loss of Rs. 25 lacs and above and cases involving refunds exceeding Rs. 10 lacs. These monetary limits will be Rs. 50 lacs and Rs. 20 lacs respectively for Mumbai, Delhi, Chennai and Kolkata. Such cases will be picked up by the JCIT (Auditing) Range from the monthly list of auditable cases received from JCIT (Auditee) Range. He will provide copies of the audit memo to the concerned Assessing Officer and to the JCIT (Auditee) Range.
- (iv) Consolidation of the list of audit paras raised by him and/or his officers (major and minor objections separately) and forwarding of the list alongwith copies of audit memos to the JCIT (Auditee) Range and to the concerned CITs by the 20th of each month.
- (v) Ensuring that audit work is undertaken continuously and that auditable cases received in a particular month are audited in the next month positively.

#### (b) As JCIT (Auditee) Range

- (i) Obtaining the list of auditable cases (category wise) from officers and after consolidation sending the list to the JCIT (auditing range) by the 10th of each month and he shall keep a monthly folder of such cases.
- (ii) Recording the receipt of audit objections in the prescribed register on monthly basis.
- (iii) Deciding acceptance/non-acceptance of audit objections with tax effect of Rs. 5,000/- to Rs. 50,000/- within a period of 3 months from the receipt of audit objections. Ensuring quick remedial actions in cases with tax effect of Rs. 5,000/- to Rs. 50,000/-.
- (iv) Assisting the CIT in deciding acceptance/non-acceptance

of audit objections with tax effect exceeding Rs. 50,000/- and in ensuring quick remedial actions in such cases.

- (v) Informing the auditing range about acceptance/non-acceptance of the audit objections within three months from the date of receipt of such objections.
- (vi) Helping the CIT in maintenance of ledger cards.
- (vii) Commenting on the audit performance of the Assessing Officers in their annual confidential reports.

**Note:** For JCIT (Auditing) Range the internal audit objections will be treated as settled as soon as he receives intimations of acceptance/non-acceptance from the Auditee Range. However, the audit objection shall be treated as settled by the Auditee Range only when remedial action is completed and additional demand is raised.

#### **5.04 Role of Assessing Officers**

##### **(a) Auditing Functions**

- (i) Each Assessing Officer shall keep record of auditable cases received each month from Auditee Assessing Officer.
- (ii) He shall inform the Auditee Assessing Officer about his audit programme at least a week before commencement of the audit so that the Auditee Assessing Officer keeps the records ready.
- (iii) He shall provide audit memo to the concerned Assessing Officer and shall send copy of the same in duplicate to his JCIT Range for onward transmission to the JCIT (Auditee) Range.
- (iv) He shall keep record of audit objections raised in the prescribed register.

##### **(b) Auditee Functions**

- (i) Each Assessing Officer shall prepare a list of auditable cases by the 7th of each month and send a copy to the Auditing Assessing Officer and also to the JCIT Range.
- (ii) He shall produce the auditable records before the Auditing Assessing Officer and also shall extend all cooperation to the auditing party.
- (iii) He shall keep record of audit objections received by him in the prescribed register.
- (iv) He will help the JCIT Range in the maintenance of the audit records pertaining to his jurisdiction.
- (v) He will decide the acceptance/non-acceptance of audit

objections with tax effect upto Rs. 5,000/-. In audit objection cases with tax effect of Rs. 5,000/ to Rs. 50,000/-, approval of JCIT Range and in audit objection cases with tax effect exceeding Rs. 50,000/-, approval of the CIT (Administration) shall be obtained by him for acceptance/non-acceptance of audit objections.

(vi) He shall initiate most appropriate remedial action if audit objection is found to be acceptable. The remedial action will be completed within a period of three months from the receipt of the audit objections.

(vii) He shall maintain audit registers **IAR-1A** and **IAR-2A** for watching and controlling his audit functions as Auditing Officer and as Auditee Officer respectively (specimen proforma of registers are enclosed).

#### **6.00 List of Auditable Cases**

The auditable cases shall be of the following categories:

##### **6.01 Immediate Cases (Target for Audit: 100%)**

- (i) All Search and Seizure cases
- (ii) All cases of foreign companies
- (iii) All scrutiny assessments under the Income Tax Act.
- (iv) Refund cases exceeding refunds of Rs. 10 lacs each.
- (v) TDS cases exceeding TDS of Rs. 50 lacs each.
- (vi) All summary assessments with assessed income/loss exceeding Rs. 10 lacs in each case.
- (vii) All scrutiny assessments under Other Direct Tax Acts.

##### **6.02 Priority Cases (Target for Audit 50%)**

- (i) TDS Cases with TDS of Rs. 10 lacs to Rs. 50 lacs in each case.
- (ii) Refund cases exceeding Rs. 5 lacs but below Rs. 10 lacs in each case

##### **6.03 Residual Cases**

- (i) Non-scrutiny company/non-company assessments with income/loss upto Rs. 10 lacs in each case.
- (ii) Refund cases upto Rs. 5 lacs in each case.
- (iii) TDS cases upto Rs. 10 lacs in each case.

### 7.00 Norms for Checking of Cases

7.01 Considering the fact that larger man-power will be available for audit work, the percentage of cases to be audited is fixed as under:—

Category	Description	Target for scrutiny assessments	Target for non-scrutiny assessments	Old Target
A	Company assessment with income/loss below Rs. 50,000 and non-company assessment with income/loss below Rs. 2 lacs.	100%	Company-5% Non-Company-2%	Company-2% Non-Company-2%
B	Company assessments with income/loss of Rs. 50,000/- and above but below Rs. 10 lacs and non-company assessments with income/loss of Rs. 2 lacs and above but below Rs. 10 lacs.	100%	Company-25% Non-Company-10%	Company-10% Non-Company-10%
C	Company and non-company assessments with income/loss of Rs. 10 lacs and above.	100%	100%	
D	Search and seizure assessments	100%	100%	
E	Foreign companies	100%	100%	
F	Expenditure Tax	100%	20%	
G	Wealth Tax Cases exceeding Rs. 20 lacs	100%	5%	2%
H	Sur Tax and Interest Tax Cases. Old Pending Cases etc.	100%		

### 7.02 Norms for TDS Cases

The percentage of TDS Returns for audit is fixed as under:—

(a) TDS upto Rs. 10 lacs	10%
(b) TDS from Rs. 10 lacs to Rs. 50 lacs	50%
(c) TDS exceeding Rs. 50 lacs	100%

### 7.03 Norms for Checking of Refund Cases

The percentage for checking of refund cases is fixed as under:—

(a) Cases with refund upto Rs. 1 lac	Salary cases—2% Others—5%
(b) Refunds exceeding Rs. 1 lac and upto Rs. 5 lacs—	20%
(c) Refunds exceeding Rs. 5 lacs and upto Rs. 10 lacs—	50%
(d) Refunds exceeding Rs. 10 lacs—	100%



#### **8.00. Audit by TROs**

The concept of "audit chains" and the process of setting up of such chains for TRO audit will be similar to those of Assessing Officers. The TRO shall audit the records/registers of another TRO and check the accuracy of arrear demands entered in the registers with the arrear demands certified by the Assessing Officer. He shall check the accuracy of interest charged u/s 220(2) of the IT Act.

#### **9.00. Audit by Administrative Officers Superintendents**

The Administrative Officers/Superintendents shall audit the records, registers, arrear reconciliation statements, arrear carry-forward registers, all periodical statements and the statistical data pertaining to another Administrative Officers/Superintendents. They will check whether all records/registers/statements are properly maintained and whether the entries in the registers are accurately, authentically and properly made.

#### **10.00 Norms for attending to Receipt Audit Objections**

##### **10.01 Metropolitan Charges of Mumbai, Chennai, Delhi and Kolkata**

The CIT (Audit) will be the nodal officer for dealing with Revenue Audit. He will coordinate between the CIT and the C&AG for settling the pending receipt audit objections. Each CIT (Administration) shall be responsible for keeping record of receipt audit objections, ensuring remedial actions and for sending Proforma Reports in Part A and Part B to the CBDT and to the DIT (Audit) relating to draft audit paras. The existing procedure laid down in Audit Manuals, Circulars and Instructions of CBDT shall be applicable for Receipt Audit. The CIT (Audit) will obtain reports relating to remedial actions taken by the Assessing Officers and shall forward the report regarding settlement of audit objections to the DIT (Audit)/CBDT. CIT (Audit) will maintain the ledger cards in respect of Assessing Officers and corresponding Auditing Assessing Officers relating to the major receipt audit objections.

##### **10.02 Other CCIT/DGIT (Investigation) Charges**

In respect of other CCIT/DGIT (Investigation) charges, the CIT (Administration) will have the primary responsibility of coordination and planning work relating to Receipt Audit. He will keep the records of receipt audit objections, ensure prompt remedial action as per the existing Instructions of CBDT, maintain ledger cards, send reports to the CCIT and to the DIT (Audit)/CBDT in the cases involving draft audit paras. He will ensure that cases are audited by internal audit parties before the receipt audit is undertaken by the Receipt Audit parties.

**11.00 Records/Registers to be maintained****11.01 Internal Audit**

The JCIT Auditing Range shall maintain records of auditable cases received from the Auditee Range in the prescribed Internal Audit Register-I (**IAR-1**) (specimen format attached).

The JCIT Auditee Range shall maintain a folder of monthly auditable cases received from his Assessing Officers and forward them to the JCIT Auditing Range. The JCIT Auditee Range shall properly maintain Internal Audit Register-2 (**IAR-2**) (specimen format attached) for recording the audit objections received from the Auditing Range and for controlling the actions taken on the audit objections in this register.

The Assessing Officers shall properly maintain prescribed audit registers **IAR-1A** and **IAR-2A** for keeping records of audit objections raised by them and also relating to the audit objections received by them and the follow up actions taken by them (specimen proforma are enclosed).

The formats for preparing the lists of auditable cases relating to different categories in the form of Internal Audit Statements are prescribed as **IAS-1A**, **IAS-1B** and **IAS-1C**. The JCIT Auditee Range shall consolidate the statements received from the circles and wards in the similar proforma and forward the same to the Auditing Range on month-after-month basis and he will retain a copy in his office for record. Each JCIT Range shall send a monthly statement to the CIT in the form of Internal Audit Monthly Statement or **IAMS** in the prescribed proforma (specimen copy is enclosed).

**11.02 Receipt Audit**

The existing records and registers relating to receipt audit objections as prescribed in the Audit Manual shall continue.

**12.00 Clearance of Backlog**

The CIT (Administration) will ensure the Internal Audit of pending cases received by them on account of transfer of jurisdiction and will further ensure the audit of such cases before the audit by Receipt Audit Parties. The old pending receipt audit objections as well as old internal audit objections will be settled by him on priority basis.

13.00 The various Circulars/Instructions issued by the CBDT regarding functioning of the internal audit and the procedure/guidelines laid down in the Internal Audit manuals shall be followed to the extent these are not modified by the above instructions and till the Internal Audit Manuals are updated.

14.00 This instruction may be brought to the notice of all officers working in your region for compliance.

15.00 Hindi version will follow.

Yours faithfully,  
Sd./-

(N.N. Mishra)  
Director, Central Board of Direct Taxes.

Enclosure: As above.

Copy to:

1. All Officers/Technical Sections of CBDT.
2. All Directorates of Income Tax.
3. NADT Nagpur/All RTIs.
4. DDIT (RSP&PR), Hans Bhawan, New Delhi.
5. Bulletin Section, DIT(RSP&PR) Mayur Bhawan, New Delhi.
6. Joint Secretary & Legal Advisor, Ministry of Law, Justice & Company Affairs, Shashtri Bhawan, New Delhi.
7. C&AG of India, New Delhi (40 Copies).
8. Secretary, Settlement Commission, Lok Nayak Bhawan, New Delhi.
9. Director (O&MS), Level 5, East Block, Vivekanand Marg, RK Puram, New Delhi.
10. Commissioner (AAR), New Delhi.
11. Directors of Income Tax (Inv.)/IT/Audit/Vigilance/Intelligence (Inv.)/ Systems.
12. Commissioners of Income Tax (Computer Operation).

Sd./-  
(Rajneesh K. Arvind)

Under Secretary to the Govt. of India

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**INTERNAL AUDIT REGISTER (IAR)-1**

**FOR JCIT (AUDITING) RANGE**

**Auditing Range**  
**Auditee Range**

**REGISTER OF AUDITED CASES**

Sl. No	Name of assessee	PAN	Ward/ Circle	Asstt. Year	Date of Assessment /Rectification /appeal effect /revision	Total income/ loss	Date of Audit	Tax effect	Date of despatch of audit objection memo	Date of acceptance/ non-acceptance/remedial action taken

Note: To be maintained by the JCIT Auditing Range (to be prepared on the basis of list of auditable cases received from the Auditee Range and also on the basis of audit conducted by the Auditing Range)

The number of cases to be entered in this register should be on the basis of percentage fixed for audit relating to different categories of auditable cases which the JCIT (Auditing) range will randomly select from the list of auditable cases received from the Auditee Range. The list of auditable cases received will be kept in month-wise folders.

It will be preferable if the entries are made in a chronological order of Circles and Wards.





**INTERNAL AUDIT REGISTER (IAR)-1A**

**Auditing Range FOR AUDITING OFFICER Auditing Officer**  
**Auditee Range REGISTER OF AUDITED CASES Auditee Officer**

Name of assessee	PAN	Ward/ Circle	Asstt. Year	Gist of the Audit Objection	Total income/ loss	Date of Audit	Tax effect	Date of despatch of audit objection memo	Date of acceptance/ non-acceptance/remedial action taken

Note: To be maintained by the Auditing Officer (to be prepared on the basis of list of auditable cases received from the Auditee AO)

The number of cases to be entered in this register should be on the basis of cases selected by JCIT Range (Auditing out of the list of auditable cases received from JCIT (Auditee) Range.



**INTERNAL AUDIT STATEMENT (IAS)-1A**

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**FORMAT OF MONTHLY STATEMENT OF "IMMEDIATE CASES" TO BE FURNISHED BY THE ASSESSING OFFICER TO THE AUDITING OFFICER AND TO HIS JCIT RANGE (AUDITEE)**

Income-Tax Ward/Circle  
 JCIT Range (Auditee)  
 CIT Charge  
 JCIT (Auditing) Range

Statement for the month of  
 Name of the A.O.

**PART A: ALL SEARCH AND SEIZURE CASES**

Sl. No.	Name of assessee	PAN	Status	Assessment year	Date of Assessment/ Rectification/appeal effect/revision etc.,	Total Income/ Loss

**PART B: ALL CASES OF FOREIGN COMPANIES**

Sl. No.	Name of assessee	PAN	Status	Assessment year	Date of Assessment/ Rectification/appeal effect/revision etc.,	Total Income/ Loss

**PART C: ALL SCRUTINY ASSESSMENTS UNDER THE IT ACT, EXPENDITURE TAX, SUR TAX, INTEREST TAX AND WEALTH TAX**

Sl. No.	Name of assessee	PAN	Status	Assessment year	Date of Assessment/ Rectification/appeal effect/revision etc.,	Total Income/ Loss



**INTERNAL AUDIT STATEMENT (IAS)-1A (page-2)**

**PART D: REFUND CASES EXCEEDING REFUND OF RS. 10 LACS**

Sl. No.	Name of assessee	PAN	Status	Assessment year	Date of Assessment/ Rectification/appeal effect/revision etc.,	Total Income/ Loss

**PART E: TDS CASES OF RS. 50 LACS AND ABOVE**

Sl. No.	Name of assessee	PAN	Status	Assessment year	Date of Assessment/ Rectification/appeal effect/revision etc.,	Total Income/ Loss

**PART F: ALL SUMMARY ASSESSMENTS WITH ASSESSED INCOME/LOSS EXCEEDING RS. 10 LACS**

Sl. No.	Name of assessee	PAN	Status	Assessment year	Date of Assessment/ Rectification/appeal effect/revision etc.,	Total Income/ Loss

**INTERNAL AUDIT STATEMENT (IAS)-1B**

**FORMAT OF MONTHLY STATEMENT OF "PRIORITY CASES" TO BE FURNISHED BY THE ASSESSING OFFICER TO THE AUDITING OFFICER AND TO HIS JCIT RANGE (AUDITEE)**

Income-Tax Ward/Circle  
 JCIT Range (Auditee)  
 CIT Charge  
 JCIT (Auditing) Range

Statement for the month of  
 Name of the A.O.

**PART A: TDS CASES WITH TDS OF RS. 10 LACS TO RS. 50 LACS**

Sl. No.	Name of assessee	PAN	Status	Assessment year	Date of Assessment/ Rectification/appeal effect/revision etc.,	Total Income/ Loss

**PART B: REFUND CASES EXCEEDING RS. 5 LACS BUT BELOW RS. 10 LACS**

Sl. No.	Name of assessee	PAN	Status	Assessment year	Date of Assessment/ Rectification/appeal effect/revision etc.,	Total Income/ Loss

**INTERNAL AUDIT STATEMENT (IAS)-1C  
 FORMAT OF MONTHLY STATEMENT OF "RESIDUAL CASES" TO BE FURNISHED BY THE ASSESSING OFFICER TO THE  
 AUDITING OFFICER AND HIS JCIT RANGE (AUDITEE)**

**Income-Tax Ward/Circle  
 JCIT Range (Auditee)  
 CIT Charge  
 JCIT (Auditing) Range**

**Statement for the month of  
 Name of the A.O.**

**PART A: NON-SCRUTINY COMPANY AND NON-COMPANY ASSESSMENTS WITH INCOME / LOSS BELOW RS. 10 LACS**

Sl. No.	Name of assessee	PAN	Status	Assessment year	Date of Assessment/ Rectification/appeal effect/revision etc.,	Total Income/ Loss

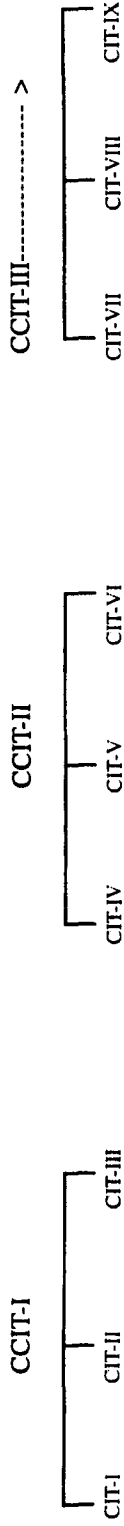
**PART B: REFUND CASES UPTO RS. 5 LACS**

Sl. No.	Name of assessee	PAN	Status	Assessment year	Date of Assessment/ Rectification/appeal effect/revision etc.,	Total Income/ Loss

**PART C: TDS CASES UPTO RS. 10 LACS**

Sl. No.	Name of assessee	PAN	Status	Assessment year	Date of Assessment/ Rectification/appeal effect/revision etc.,	Total Income/ Loss

**A-9**  
**A MODEL OF CHAINS TO BE CREATED BY CIT (AUDIT) / CCIT / JCIT (As they deem fit) IN METROPOLITAN CHARGES**



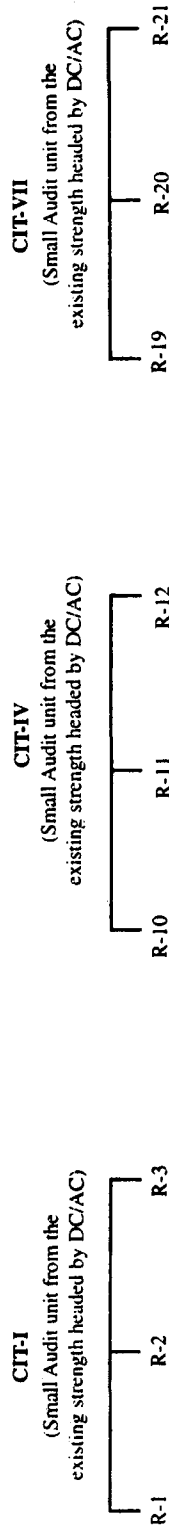
**CCIT-I (In charge of Audit Work)**  
 (He shall create a small unit from the existing strength provided to him for Audit Work)  
 (Headed by a DC/AC)

**CIT (AUDIT)**

[Having set-up of CIT (Admn.)]

1) Chains to be created by CIT (Audit) in metropolitan charges. He will keep record and send copy to DIT (Audit).

CIT-I-----> CIT-IV-----> CIT-VI----->

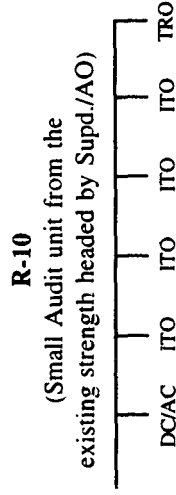
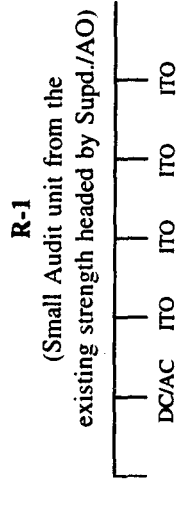


**A-10**

**2. Chains of JCIT Ranges to be created by CIT (Admn.)**

- R-1-----> R-10-----> R-19----->
- R-2-----> R-11-----> R-20----->
- R-3-----> R-12-----> R-21----->

**SET-UP OF JCIT RANGES**



- AUDIT CHAINS OF ASSESSING OFFICER'S (TO BE CREATED BY THE JCIT RANGE)**
- DC/AC. CIR(1)(1)-----> DC/AC CIR-10(1)----->
  - ITO W1(1) -----> ITO W 10(1)
  - ITO W1(2) -----> ITO W 10(2)
  - > -----> -----> ----->
  - TRO R-1 -----> TRO R-10----->

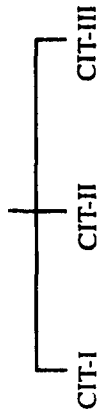
**ADMINISTRATIVE OFFICER/SUPERINTENDENT R-1-----> ADMN. OFFICER/SUPERINTENDENT R-10 ----->**

A-11

**OTHER CCIT / DGIT (Investigation) CHARGES**

**CCIT / DGIT (Investigation)**

(Shall provide a small unit in his office for Audit Work from his existing strength)



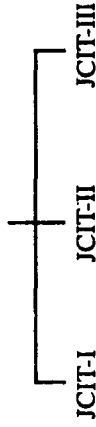
**AUDIT CHAIN TO BE CREATED BY CCIT**

CIT-I -----> CIT-II -----> CIT-III -----> CIT-I

Further audit chains of JCITs and AOs to be created by CIT and JCIT are similar to metropolitan charges

**SINGLE CIT-CHARGE**

(CCIT to decide if Internal Audit chains will be formed within the CIT charge only)



Chains of JCIT to be created by CIT (Admn.)

JCIT-I ---> JCIT-II -----> JCIT-III -----> JCIT-I

Further chains of AOs will be created by the JCIT in such a manner that the travelling involved is minimum

Note: 1) For metropolitan charges CIT (Audit) will consolidate the chains created by him, by CIT (Admn.) and by JCITs Ranges and keep records and a copy will be sent to the DIT (Audit).

2) In other CCIT / DGIT (Inv.) charges, the CCIT / DGIT (Inv.) shall consolidate the chains and he shall send copy to the Cadre Controlling CCIT and to the DIT (Audit).

**FUNCTIONS OF IT AUTHORITIES FOR INTERNAL AUDIT AND RECEIPT AUDIT**

**CCIT/DGIT (Investigation)**

(He shall provide from the existing strength a small unit in his office for Audit work headed by a DC/AC)

He shall ensure the smooth functioning of Audit Work and after consolidation, he will send reports to the DIT(A)/CBDT

**CIT (ADMINISTRATION)**

(He shall provide from the existing strength a small unit in his office for Audit work headed by a DC/AC)

Primarily responsible for both Receipt Audit and Internal Audit Work within his charge and also the Audit of CIT charge assigned to his JCITs. He shall send reports to CCIT (after consolidation)

**JCIT RANGE**

(He shall provide from the existing strength a small unit in his office for Audit work headed by an Administrative Officer/Superintendent)

He shall audit important cases and ensure the completion of Receipt Audit Work and Internal, Audit Work relating to his Range and also the audit of Range assigned to his AOs. He shall send reports to CIT (after consolidation).

**ASSESSING OFFICER**

(Having Inspectors/TAs/UDCs/LDCs)

He shall complete both Internal and Receipt Audit work pertaining to his jurisdiction and also complete the audit of Assessing Officers assigned to him. He shall send reports to JCIT Ranges.

INTERNAL AUDIT MONTHLY STATEMENT (IAMS)

- (i) To be sent by AO to JCIT Range by 5th of following month
- (ii) To be sent by JCIT Range to CIT by 10th of the following month
- (iii) To be sent by CIT to CCIT by 15th of the following month

MONTH .....  
 CHARGE .....

AUDITING OFFICER .....  
 AUDITEE OFFICER .....

PART-A-AUDITING FUNCTIONS

A: AUDITABLE CASES AND THEIR DISPOSAL	TARGET FOR AUDIT	Pendency as on 1st April	Prog Additions upto month end	Total	Prog Disp. upto month end	Balance at the month end	No. of objection raised+ Tax effect	
							Major objections No	Minor objections No.
							amt. (000)	amt. (000)
(a) above 25 lacs (50 lacs for Metro charges)	Scrutiny cases-100% Non Scrutiny-100%							
(b) Company cases below 50,000 and Non-company cases below 2 lacs	Scrutiny cases-100% Non-scrutiny-Comp.-5% Non-comp.-2%							
(c) Company cases from 50,000 to 10 lacs	Scrutiny cases-100% Non-scrutiny-25%							
(d) Non-company cases from 2 lacs to 10 lacs	Scrutiny cases-100% Non-scrutiny-10%							
(e) Company and non-company cases exceeding 10 lacs other than (a) above	Scrutiny cases-100% Non-scrutiny-100%							
(f) Search & Seizure Cases	Scrutiny cases-100% Non-scrutiny-100%							





**PART-B: AUDITEE FUNCTIONS (AUDIT OBJECTIONS AND THEIR DISPOSAL)**

	ARREAR PROGRESSIVE UPTO MONTHEND			CURRENT PROGRESS UPTO MONTHEND		
	Workload	Settlement	Balance	Work load	Settlement	Balance
Internal Audit Major obj. with RE above Rs. 50,000/-	No.					
	Amt. (000)					
Internal Audit Minor obj. with RE between Rs. 5,000/- to Rs. 50,000/-	No.					
	Amt. (000)					
Internal Audit Minor obj. with RE below Rs. 5,000/-	No.					
	Amt. (000)					
Receipt Audit Major Obj.	No.					
	Amt. (					

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**QUARTERLY AUDIT REPORT(QAR)**

AO will send to JCIT by 7th of the following quarter  
 JCIT will send to CIT by 12th of the following quarter  
 CIT will send to CCIT by 17th of the following quarter  
 CCIT will send to DIT by 20th of the following quarter

Quarter \_\_\_\_\_  
 Charge \_\_\_\_\_

**OFFICE OF THE CHIEF COMMISSIONER OF INCOME-TAX  
 QUARTERLY AUDIT REPORT OF THE AUDIT WORK  
 ASSESSING OFFICER**

1. AUDIT SET UP
  - (i) Sanctioned Strength
  - (ii) Working Strength
2. AUDITABLE CASES AND THEIR DISPOSAL. (Details to be provided as per proforma on the reverse side)

Pendency of auditable cases as on 1st April	Progressive additions upto quarter end	Total (1+2)	Progressive Disposal up to the quarter end	Balance at the quarter end	No. of obj. raised and Tax effect	
					Major Objections Amt.(000)	Minor objections No. Amt.(000)
					No.	Amt.(000)
					No.	Amt.(000)

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## 3. AUDIT OBJECTIONS AND THEIR DISPOSAL

		ARREAR PROGRESSIVE UPTO QUARTER END			CURRENT PROGRESSIVE UPTO QUARTER END		
		Workload	Settlement	Balance	Work Load	Settlement	Balance
Internal Audit Major obj. with tax effect above Rs. 50,000/-	No. Amt. (000)						
Internal Audit Minor obj. with tax effect between Rs. 5,000/- to Rs. 50,000/-	No. Amt. (000)						
Internal Audit Minor obj. with tax effect below Rs. 5,000/-	No. Amt. (000)						
Receipt Audit Major Obj.	No. Amt. (000)						
Receipt Audit Minor Obj.	No. Amt. (000)						

**4. NO. OF MEETINGS WITH AG AND OBJECTIONS SETTLED UPTO QUARTER END (TOTAL)**

Opening Balance with AG	No. of meetings	Major objection settled	Minor Objection settled	Pending with AG at the quarter end

**5. ANALYSIS OF PENDING OBJECTIONS**

ARREAR OBJECTIONS						
		Internal Audit Major	Internal Audit Minor	Receipt Audit Major	Receipt Audit Minor	
(i) Pertaining to 97-98 and earlier years	No. Amt. (000)					
(ii) Pertaining to 98-99	No. Amt. (000)					
(iii) Pertaining to 99-00	No. Amt. (000)					
(iii) Pertaining to 00-01	No. Amt. (000)					
(iii) Pertaining to 01-02	No. Amt. (000)					
<b>Total</b>	No. Amt. (000)					

**4. NO. OF MEETINGS WITH AG AND OBJECTIONS SETTLED UPTO QUARTER END (TOTAL)**

Opening Balance with AG	No. of meetings	Major objection settled	Minor Objection settled	Pending with AG at the quarter end

**5. ANALYSIS OF PENDING OBJECTIONS**

	ARREAR OBJECTIONS							
	No	Amt. (000)	Internal Audit Major	Internal Audit Minor	Receipt Audit Major	Receipt Audit Minor		
(i) Pertaining to 97-98 and earlier years								
(ii) Pertaining to 98-99								
(iii) Pertaining to 99-00								
(iii) Pertaining to 00-01								
(iii) Pertaining to 01-02								
<b>Total</b>								

**APPENDIX III**

**FOR DEPARTMENTAL  
USE ONLY**

**COMPENDIUM OF  
RECURRING  
MISTAKES  
DETECTED IN AUDIT**

**INCOME TAX DEPARTMENT**

**Directorate of Income Tax (RSP&PR)  
(RESEARCH, STATISTICS, PUBLICATIONS AND PUBLIC RELATIONS)  
MAYUR BHAWAN, NEW DELHI-110001**

## **FOREWORD**

From time to time the Directorate of Income-Tax (Audit) has been bringing out compilation of common mistakes committed by the assessing and other officers of the department. Last such compilation was brought out in 1994. An attempt has now been made again to bring out such compilation in this year named as "Compendium of Common Mistakes".

This booklet is a selective compilation of instances of typical mistakes repeatedly committed by the assessing officers. Efforts have been made to see that mistakes which are committed by the officers again and again, which have high revenue effect, which are important from legal angle and which occur due to system malfunctioning find a place in this compilation. For achieving this, selection has been made after careful study of the reports of the C&AG, Internal Audit, Inspections carried out by Directorate of Income-tax (Audit) etc.

It has been observed that mistakes occur due to careless completion of assessments by the assessing officers. Simple calculation mistakes, common mistakes committed due to not following the Act properly and mistakes committed due to shallow knowledge of law and of latest legal pronouncements have been detected during the course of study while compiling this booklet. Irregular allowance, exemption and relief's have also contributed to a number of mistakes. Most of these mistakes are avoidable in nature if the assessments are completed with a little more caution, understanding and clarity of mind.

Although, a number of instructions and notifications are issued by the Board from time to time and officers try to go through the latest legal pronouncements yet, the mistakes do take place. Such mistakes not only result in loss of revenue but also form part of the annual report of the Comptroller and Auditor General of India in the shape of draft paras and Systems (Audit), which is placed before the Parliament every year. This obviously brings a bad name to the Department. The present compilation will definitely make the officers alert and cautious about the common mistakes occurring while completing the assessments and will help them in avoiding such mistakes in future. This will also be helpful to the Supervisory officers who can bring such instances to the notice of the assessing officers and will also help them in updating their knowledge. This compilation will also help the staff *i.e.* Supervisors, Head Clerks and T.As and will make them cautious while preparing ITNs 150, making the calculations and computing the income etc.

I am sure that this book will prove to be of immense use to the officers and staff of the Department.

The efforts made by the officers and staff of Directorate of Audit in preparing the booklet are highly appreciable.

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## INTRODUCTION

Every year Internal Audit and Receipt Audit points out large number of mistakes having substantial tax effect. There has been a steep increase in the number of audit paras included by C&AG in their latest annual report. Most of the mistakes are recurring and are of avoidable nature. Earlier the Directorate (of Income Tax and Audit) has compiled instances of important common mistakes detected as a result of audit in the year 1992 and 1994.

A fresh compendium of common mistakes detected by Receipt Audit and Internal Audit in the last few years is prepared in the form of a booklet. The compendium is divided into 5 Parts, having 23 Chapters which are further sub-divided into sub-heads to facilitate the reader for a quick reference to the particular provisions of the I.T. Act.

The objective of the Directorate in bringing out this booklet is to create awareness among the assessing officers who in the restructured set up of the Income Tax Department will also be required to discharge the duties of auditing officers. This will help the officers in avoiding and detecting the glaring common mistakes having substantial revenue effect.

I hope that this Compendium of mistakes will prove very useful in making the officers more alert and cautious while carrying out their assessment and audit duties.

The efforts put in by the officers and staff of the Directorate of (Audit) in collecting the relevant mistakes from the audit reports is praiseworthy.

Hindi version will follow.

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**PART-**  
**CHAPTER-1**

**AVOIDABLE MISTAKES IN COMPUTATION OF  
INCOME AND TAX**

**1.1. OVER ASSESSMENT**

(i) The assessment of a company for the assessment year 1996-97 was completed at nil income after set off of unabsorbed losses of Rs. 5.96 lakh. Audit scrutiny revealed that the assessee company filed its return of income at loss of Rs. 6.02 lakh. The assessing officer after making disallowance of Rs. 6500 only completed the assessment at an income of Rs. 5.96 lakh as against the loss of Rs. 5.96 lakh.

(ii) The assessment of a widely held company for the assessment year 1994-95 was completed determining an income of Rs. 26,040.81 lakh which was set off against past losses. Audit scrutiny revealed that while computing the above income, a sum of Rs. 1,454.89 lakh was incorrectly added back instead of Rs. 1,428.41 lakh actually charged off on account of unascertained liability to the profit and loss account.

(iii) The assessment of a co-operative society for the assessment year 1994-95 was completed at a taxable income of Rs. 789.96 lakh. Audit scrutiny of the assessment records revealed that while computing the income of the assessee as against the correct amount of Rs. 394.75 lakh the disallowance to be added back was erroneously added back twice.

(iv) The assessment of a company for the assessment year 1995-96 was completed allowing carry forward of unabsorbed depreciation of Rs. 2.92 lakh. Audit scrutiny revealed that though the public issue expenditure of Rs. 32.22 lakh was not debited in the profit and loss account, the same was added back in the computation of taxable income.

**1.2. EXCESS LEVY OF INTEREST**

(i) The assessment of an assessee company completed for the assessment year 1992-93 was revised in February 1996 to give effect to appeal orders. Audit scrutiny revealed that interest for short payment of advance tax was levied at Rs. 65.26 lakh instead of Rs. 58.33 lakh leviable for 36 months from 1.4.92 to 31.3.95 after adjusting interest of Rs. 7.92 lakh out of aggregate tax of Rs. 39.33 lakh paid by the assessee in December 1992. This resulted in excess levy of interest of Rs. 6.93 lakh.

**1.3 ARITHMETICAL MISTAKE**

(i) The assessment of a company for the assessment year 1995-96 was completed for a loss of Rs. 302.98 lakh. Audit scrutiny revealed that the

allowable depreciation of Rs. 15.52 lakh was reduced from the loss instead of adding the same to the loss.

#### 1.4 MISTAKES WHILE MAKING COMPUTATION OF INCOME

In the assessment of the following assessee, audit scrutiny revealed that:—

(i) In the assessment of a company for the assessment year 1995-96 completed at an income of Rs. 22987.86 lakh, the assessing officer disallowed an amount of Rs. 1874.22 lakh towards depreciation on leased assets but a further amount of Rs. 103.24 lakh on the same account was not disallowed.

(ii) The assessment of a widely held company for the assessment year 1995-96 was completed at an income of Rs. 1190.77 lakh. As per the discussion and data furnished in the assessment order, the taxable income actually worked out to Rs. 2002.46 lakh as against Rs. 1190.77 lakh adopted in the assessment order.

(iii) In the assessment of a widely held company for the assessment year 1995-96 completed at taxable income of Rs. 8.95 lakh, the assessing officer made various additions to the extent of Rs. 112.88 lakh against which an amount of Rs. 101.41 lakh only added back to the total income leaving a balance of Rs. 11.47 lakh to be added back to taxable income.

(iv) The assessment of a foreign Banking company for the assessment year 1990-91 was originally completed after scrutiny in January 1992 and revised in March 1998 on the basis of the appellate order, determining the income at Rs. 1061.96 lakh. Audit scrutiny revealed that while computing the taxable income, the income from other sources was adopted as Rs. 549.91 lakh as against the correct figure of Rs. 599.91 lakh.

(v) In the assessment of a company for the assessment year 1985-86 completed after scrutiny in March 1989 and revised in March 1997, the assessing officer adopted incorrect figure of Rs. 137.16 lakh as assessee's income for the purpose of calculation of tax as against the correct amount of Rs. 147.16 lakh.

(vi) In the assessment of a company for the assessment year 1995-96, while framing the assessment, the assessing officer proposed to make an addition of Rs. 34.25 lakh. Audit scrutiny revealed that against the proposed addition of Rs. 34.25 lakh, a sum of Rs. 3.42 lakh only was added to the taxable income.

(vii) In the assessment of a company for the assessment year 1995-96 was completed determining a loss of Rs. 1153.10 lakh. It was found that instead of reducing the inadmissible amount from the loss computed, the same was inadvertently added to the loss. The mistake resulted in computation of excess loss of Rs. 34.02 lakh involving potential tax effect of Rs. 15.65 lakh.

(viii) In the assessment of a co-operative society for the assessment year 1995-96. The Audit scrutiny revealed that while computing the total income, the assessing officer erroneously deducted an amount of Rs. 10.56 lakh representing income from other sources' instead of adding the same to the total income.

(ix) In the assessment of an assessee firm for the assessment year 1994-95 it was found that even though no refund was due on regular assessment, the refund of Rs. 3.37 lakh granted under summary assessment was not treated as tax payable by the assessee firm, which resulted in short levy of tax of Rs. 3.37 lakh.

(x) In the assessment of an association of persons (co-operative society) for the assessment year 1994-95, the assessing officer had made an addition of Rs. 669.49 lakh and a deduction of Rs. 5.70 lakh. However, while computing the total income, net taxable income was computed at Rs. 212.89 lakh instead of correct taxable income of Rs. 600.11 lakh.

(xi) In the assessment of an association of persons for the assessment year 1994-95 completed at a taxable income of Rs. 141.40 lakh, it was noticed that while completing the assessment, the assessing officer disallowed the Tax Deducted at Source (TDS) claimed by the assessee on account of buying/selling transactions between two internal units of the assessee, as the conditions of seller and buyer as laid down in the provision of the Income Tax Act were not satisfied. However, while working out the tax demand, the TDS claim disallowed by the assessing officer amounting to Rs. 17.05 lakh and refund to the assessee was not included in the tax demand.

#### 1.5 NON-APPLICATION OF PROVISIONS OF SECTION 40A (3)

(i) The assessment of a Firm for A.Y. 1996-97 was completed u/s 143(3) of the I.T. Act on 18.11.98. The Audit scrutiny revealed that there were payments made in cash exceeding Rs. 10,000 to the extent of Rs. 11,06,455. As per the amended provisions of Sec. 40A (3) of the I.T. Act, 20% of such expenditure *i.e.* Rs. 2,21,299 was dis-allowable. However, the A.O. failed to invoke the provisions of Section 40A(3) of the I.T. Act which resulted in under assessment of income by Rs. 2,21,299.

(ii) The assessment of an individual assessee for the assessment year 1990-91 was completed after scrutiny in December 1992 allowing an expenditure of Rs. 2.86 lakh towards purchases in cash. Audit scrutiny revealed that the payment exceeding Rs. 10,000 was made in cash in contravention of the provisions of the Act. Neither the assessing officer nor assessee recorded any reasons as to whether these payments were made in exceptional circumstances as provided under the Rules. In the circumstances, the entire amount should have been disallowed and brought to tax.

#### 1.6. GIVING WRONG APPEAL EFFECT ON ISSUES OTHER THAN COVERED BY APPEAL

(i) In the assessment completed u/s 143(3) for the assessment year 1993-94 the Assessing Officer made addition on account of unsecured loans and disallowance of interest thereon aggregating to Rs. 14,30,104. The assessee filed an appeal to the CIT (Appeals) against the additions. While the appeal was pending before the CIT(A), the CIT set aside the assessment order on some other issue. While completing the set aside assessment the Assessing Officer, rather than confining the reassessment to the issue on which CIT set aside the assessment, considered the addition on account of unsecured loans and disallowance of interest thereon made in the order u/s 143(3) and deleted the same. The Assessing Officer did all this while the assessee's appeal was still pending before the CIT (Appeals).

#### 1.7. NON-APPLICATION OF PROVISIONS OF SECTION 44 AD

(i) As per Sec. 44AD, the income of a civil contractor has to be assessed at 8% of the gross receipts if the accounts of the assessee have not been audited and a report under sec. 44AB has not been furnished alongwith the return of income. For the Assessment Year 1998-99, the assessee-firm, a civil contractor, accounted for gross receipts of Rs. 18,25,800. The accounts of the assessee were not audited and report u/s 44AB was not furnished as required u/s 44AD. Yet the return filed by the firm was accepted u/s 143(1) although the income shown was less than 8% of the gross receipts. Omission to assess the firm under sec. 143(3) by adopting the income of the assessee at 8% of the gross receipts, as provided for under sec. 44AD resulted in under assessment of income by Rs. 1,14,820 involving tax effect of Rs. 45,928. Further, the assessee was liable to penalty of Rs. 9125 under sec. 271B.

#### 1.8. ALLOWING WRONG DOUBLE TAXATION RELIEF

(1) The assessment of a Bank for A.Y. 1995-96 was completed after scrutiny u/s 143(3). Thailand income included in Indian Income subject to tax as per Return of Income filed was Rs. 3,94,70,224. Only such income as was taxed both in India and in Thailand should get the benefit of Double Income-Tax Relief (DITR). The Audit scrutiny revealed that in the case of the assessee such income was only Rs. 3,94,70,224 and not Rs. 4,77,46,974 on which DITR had been allowed. The mistake resulted in short levy of tax of Rs. 12,74,296.

#### 1.9 ADOPTING WRONG INCOME

(i) The assessment of a company for A.Y. 1995-96 was completed. The Audit scrutiny revealed that the business income was wrongly adopted at Rs. 2,29,69,192 instead of Rs. 2,42,22,762 as per revised return filed, resulting in under assessment of income of Rs. 12,53,570 with consequent short levy of tax of Rs. 5,76,650.

### INTERNAL AUDIT OBJECTIONS

(i) In a case while framing asstt. u/s 143(1) (a) on account of *Prima facie* adjustment addl. tax of Rs. 4.68 lac was levied. Later on when asstt. was made u/s. 143(3) additional tax was omitted to be incorporated in the order.

(ii) In a case assessee claimed depreciation of Rs. 193 lac which was disallowed after discussing the same in the assessment framed u/s 143(3). However, the Assessing Officer omitted the same to add while summing up the total income. Audit scrutiny revealed that there was under asstt. of income to the extent of Rs. 193 lac involving tax effect of Rs. 82 lac.

(iii) In a case of a company for the A.Y. 1997-98 the assessee returned a business income of Rs. 90.22 lac and after adjusting the carried forward business loss of Rs. 1656 lac admitted the total income at nil. But the assessing officer while framing asstt erroneously took the returned business loss figure at Rs. 90.23 lac and after making several additions computed the net loss at Rs. 50.17 lac. Audit scrutiny detected the mistake and potential tax effect amounted to Rs. 77.60 lac.

#### 1.10 ADOPTION OF WRONG FIGURE OF LOSS

(i) In the return of a company for the assessment year 1996-97 the business loss was shown at Rs. 34,60,75,691. The audit scrutiny revealed that this loss was shown at Rs. 36,60,75,700 in the intimation under section 143(1)(a) which resulted in notional tax effect of Rs. 1,19,94,817.

#### 1.11 FAILURE TO ACCOUNT CONSEQUENTIAL RELIEF ALLOWED BY CIT (A)

(i) The assessment of a company for the assessment year 1995-96 was completed after scrutiny in December 1997 disallowing a sum of Rs. 72.58 lakh on account of Modvat. Audit scrutiny revealed that while quantifying the disallowance in respect of Modvat the department had considered overvaluation in opening stock by Rs. 156 lakh in view of addition made on this account in the assessment order for assessment year 1994-95. However, it was revealed that the assessment for the assessment year 1994-95 was revised in the month of July 1997 to give effect to appellate order wherein the CIT (A) had granted relief in respect of addition made on account of Modvat. However, while framing the order for assessment year 1995-96 the department lost sight of the appeal effect order for assessment 1994-95 and again relief on Modvat was allowed.

#### 1.12 DISCUSSION OF DISALLOWANCE ETC. IN THE ASSTT. ORDER BUT FORGETTING TO COMPUTE IN THE TOTAL INCOME

(i) the assessment of a widely held company for the assessment year 1994-95 was completed determining income of Rs. 176.77 lakh. Audit scrutiny revealed that the assessing officer decided to disallow the

undischarged liabilities and provisions of Rs. 4.54 lakh in the body of the order but while computing the total income omitted to do so. Further, the withdrawal of demand of interest on refund to the extent of Rs. 3.36 lakh was also not made.

(ii) The assessment of a widely held company for the assessment year 1996-97 was completed after scrutiny in March 1998 disallowing depreciation of Rs. 3.89 lakh in respect of addition to plant and machinery on account of exchange rate difference. Similarly depreciation claim to the tune of Rs. 6.09 lakh was also not admitted as the machinery was not put to use. Audit scrutiny revealed that while computing total taxable income the above disallowances aggregating to Rs. 9.98 lakh remained to be considered.

(iii) The a assessment of an individual for the assessment year 1995-96 was completed on best judgement basis at an income of Rs. 49.09 lakh as against returned income of Rs. 0.64 lakh. Audit scrutiny revealed that while completing the assessment, assessing officer had rejected the claim of Rs. 5.85 lakh on account of relief in respect of profits from export business. However, while computing the total income of the assessee the amount remained to be added back to the income of the assessee.

(iv) The assessment of an assessee firm for the assessment year 1996-97 was completed and the assessing officer had proposed addition of Rs. 13.95 lakh. Audit scrutiny revealed that while computing gross total income, the said addition was not made.

### 1.13 WRONG DEDUCTION

(i) The assessment of a foreign bank for the assessment year 1993-94 was finalised allowing deduction of Rs. 27.60 lakh towards "provision for rent credited to the accounts but not allowed in earlier years". Audit scrutiny revealed that during the previous year relevant to assessment year 1992-93, the assessee had written back provision for rent amount to Rs. 27.60 lakh and the same was allowed as deduction during finalisation of assessment. In the previous year relevant to assessment year 1993-94 though the assessee neither credited the same in the profit and loss account nor claimed deduction for the same in the computation of income but the assessing officer granted this deduction which was incorrect.

(ii) The assessee was a firm constituted with as many as 17 partners. The partnership deed contained a clause for payment of minimum guaranteed profits called as 'user fee' to 8 partners of the firm. The payment of user fee was debited to the profit & loss account. In the statement of total income for the Assessment Year 1998-99, the user fee debited to the profits & loss account was not added back. Payment of user fee was not allowable as a deduction from the profits of the firm. The claim for deduction was required to be disallowed. Omission to add back the user fee, deducted from the profits of the firm resulted in under assessment of Rs. 4,32,000 invoiving tax effect of Rs. 1,60,613.



(iii) The assessment of a company for the assessment year 1994-95 was completed after scrutiny in February 1997, and for the year 1996-97 in a summary manner in August 1997 which was subsequently revised in October 1997 allowing deduction aggregating Rs. 3582.96 lakh towards interest on loan borrowed from its holding company as claimed by the assessee company in its own computation of income without debiting the aforesaid expenditure to the profit and loss accounts pertaining to the above assessment years. Audit scrutiny revealed that the holding company had waived the aforesaid liability for interest during the previous years relevant to the above assessment years. Since the liability of interest had been waived the deduction in respect of interest should have been disallowed being *prima-facie* apparent from the records.

(iv) The assessment of a company for the assessment year 1994-95 was completed allowing a deduction of Rs. 11.81 lakh in respect of intercorporate dividend. Audit scrutiny revealed that the assessee company made provisions for proposed dividend by debiting the profit and loss appropriation account by Rs. 155.78 lakh. The amount was also shown as liability in balance sheet for the year. However proof of distribution of dividend by the assessee company on or before the due date of furnishing the return of income was neither submitted by the assessee company nor called for by the assessing officer before allowing deduction of Rs. 11.81 lakh. The deduction of Rs. 11.81 lakh allowed was therefore irregular which resulted in under computation of income by the like amount with short levy of tax of Rs. 6.11 lakh.

(v) The assessments of a company for the assessment years 1994-95 and 1995-96 were completed, computing loss of Rs. 802 lakh and Rs. NIL respectively. Audit scrutiny revealed that the assessee had claimed and the department had allowed expenditure to the tune of Rs. 112.95 lakh and Rs. 133.95 lakh respectively on account of royalty payment outside India where the company had not deducted tax at source as required under the provisions of the Act on Rs. 112.95 lakh and Rs. 70.45 lakh. Since no tax was deducted the amounts were required to be disallowed.

#### 1.14 APPLYING HIGHER-RATE OF TAX

(i) The assessment of a closely held domestic company for the assessment year 1995-96 was completed at a total income of Rs. 60.48 lakh. Audit scrutiny revealed that the assessing officer charged tax at the rate of 55% as against the correct rate of 40%.

(ii) The assessment of a closely held domestic company for the assessment year 1995-96 was completed at a total income of Rs. 161.63 lakh. Audit scrutiny revealed that the department charged tax at the rate of 55% as against the correct rate of 40%. The incorrect application of tax rate led to excess levy of tax by Rs. 54.65 lakh including interest.

### 1.15 MISTAKE IN GIVING REFUNDS

(i) The assessment of a company for the assessment year 1995-96 was completed on an income of Rs. 1261.81 lakh. The net tax payable by the company after giving credit for advance tax, TDS and refunds already made was determined at Rs. 693.31 lakh. Audit scrutiny revealed that a refund of tax along with interest amounting to Rs. 29.75 lakh granted to the assessee by adjustment against the demand in respect of another assessee company of the Group was omitted to be considered even though full credit for advance tax was given. The omission resulted in short levy of tax to the extent of Rs. 29.75 lakh.

### 1.16 COMPUTATION OF INCOME UNDER WRONG HEAD & WRONG ADJUSTMENT OF BF LOSSES

(i) The assessment of a company for the assessment year 1994-95 was completed after scrutiny in July 1997 at a total income of Rs. 21.39 lakh. While computing the total income, the income from business was arrived at "Nil" after adjusting the income of Rs. 50.29 lakh against the unabsorbed business loss relating to earlier years. Audit scrutiny revealed that interest of Rs. 10.35 lakh received on refund of income tax was considered as business income instead of as income from other sources. The brought forward business losses should have been adjusted against business income only and interest on refund was to be taxed under the head "income from other sources".

### 1.17 WRONG CARRY FORWARD OF LOSS ON BELATED RETURN

(i) The assessment of a company for the assessment year 1994-95 was completed after scrutiny in February 1997 allowing carry forward of business loss of Rs. 17.80 lakh for future set off. Audit scrutiny revealed that the assessee submitted its return on 30 December 1994 against the due date of submission of return on 30 November 1994. As the return was submitted beyond due date, there was an irregular carry forward of loss of Rs. 17.80 lakh involving potential tax effect of Rs. 10.23 lakh.

(ii) The assessment of a company for the assessment year 1995-96 was completed allowing business loss of Rs. 9.90 lakh and unabsorbed depreciation of Rs. 5.75 lakh to be carried forward. Audit scrutiny revealed that the return of income was voluntarily filed after expiry of due date prescribed for filing the same. Further, the assessee carried out its business for only two months in the relevant previous year. As such depreciation was required to be restricted to Rs. 2.87 lakh, applying fifty percent of the prescribed rate as the plant and machinery was used for less than 180 days.

(iii) The assessment of an individual assessee for the assessment year 1994-95 was completed after allowing set off of carried forward speculation loss of Rs. 6.23 lakh pertaining to the assessment year 1992-93 and the

balance unabsorbed speculation loss of Rs. 7.45 lakh was allowed to be carried forward. Audit scrutiny revealed that the assessee submitted the returns of income for the assessment year 1992-93 on 11.1.1993 in place of prescribed due date of 31-10-92 and for the assessment year 1994-95 on 28-11-1994 in place of prescribed due date of 31-10-94. As the returns of losses had not been submitted within the prescribed due date, the carry forward of speculation losses pertaining to assessment year 1992-93 and subsequent set off in assessment year 1994-95 were irregular.

#### 1.18 SALES TAX COLLECTED NOT BROUGHT TO TAX

(i) The assessment of a company for the assessment year 1994-95 was completed at a loss of Rs. 7732.60 lakh. Audit scrutiny revealed that sales tax of Rs. 650.11 lakh collected from customers had not been passed through the relevant profit and loss account and remained outstanding till the end of the financial year. Since the amount was not paid to the government account during the relevant previous year or before the due date of the submission of return of income, it should have been treated as a trading receipt and brought to tax.

(ii) The assessment of a company for the assessment year 1995-96 was completed after scrutiny in March 1998. Audit scrutiny of various annexures accompanying the accounts revealed that sales tax of Rs. 49.05 lakh was collected but not paid to the Government account before the due dates. The assessing officer should have disallowed the same.

#### 1.19 TOTTALLING MISTAKE IN THE ASSESSMENT ORDER

(i) The assessment of an individual assessee for the assessment year 1995-96 was completed on a total income of Rs. 864.02 lakh. Audit scrutiny revealed that total income was short computed by Rs. 1.80 lakh due to totalling mistake, and tax and interest computed at Rs. 457.77 lakh instead of correct amount of Rs. 593.10 lakh resulting in under charge of tax and interest of Rs. 135.33 lakh.

#### 1.20 NON-LEVY OF SURCHARGE

(i) The assessment of an assessee (artificial juridical person) was completed and tax was worked out at Rs. 35.31 lakh. Audit scrutiny revealed that while computing chargeable tax, no surcharge was levied on the income tax of Rs. 35.31 lakh resulting in short levy of tax of Rs. 7.12 lakh (including interest).

(ii) The assessment of a firm for assessment year 1994-95 was completed at an income of Rs. 33.51 lakh. Audit scrutiny revealed that while computing the tax payable, surcharge of Rs. 1.61 lakh leviable on the tax of Rs. 13.40 lakh, was omitted to be levied.

#### 1.21 NON BUSINESS EXPENDITURE

(i) The assessment of a company for the assessment year 1992-93 was completed at a total income of Rs. 63.42 lakh. Audit scrutiny revealed that

out of a sum of Rs. 68.26 lakh debited to the profit and loss account under general expenditure, Rs. 8.22 lakh represented expenditure towards construction of 100 houses under a scheme called 'poor housing scheme' as part of centenary celebrations of the assessee. As the expenditure towards construction of houses was of a non-business nature, it should have been disallowed.

## CHAPTER-2

### MISTAKES IN ALLOWING DEPRECIATION

#### 2.1 APPLYING WRONG RATE OF DEPRECIATION

(i) The income of a company for the assessment years 1996-97 and 1997-98 was assessed at Rs. 'Nil' and loss of Rs. 3013.64 lakh respectively and revealed that depreciation for both the years on furniture and fixtures was allowed at the rate of hundred percent instead of at the prescribed rate of ten percent.

(ii) The assessment of a company for the assessment year 1990-91 was completed at a total income of Rs. 2027.39 lakh allowing depreciation of Rs. 156.77 lakh on plant and machinery installed at its chemical plant. Audit scrutiny revealed that the assessing officer while computing depreciation, adopted higher rate of 50% as against normal rate of 33.33% without ascertaining the fulfillment of certain conditions, for allowance of depreciation at higher rate as envisaged under the Income Tax Rules. Neither the assessment order nor the assessment records did, however, disclose any information to satisfy the allowance of such higher rate.

(iii) The assessment of three assessee companies for the assessment years 1995-96 and 1996-97 were completed, in the case of two companies in a summary manner and after scrutiny in the case of one company. Audit scrutiny revealed that deductions towards depreciation was allowed which were calculated at rates other than those prescribed in the Income Tax Rules, 1962. Depreciation on factory building was allowed at the rate of 25 percent instead of the correct rate of 10 percent, while on furniture and fixture, rate of 10 percent, 25 percent and 40 percent were applied as against the correct rate of 10 percent.

(iv) The assessment of a company for the assessment year 1993-94 was completed allowing depreciation of Rs. 33.53 lakh. Audit scrutiny revealed that depreciation was allowed at the rate of 100% on office equipment and computers while the assessee was entitled to depreciation of Rs. 6.87 lakh at an admissible rate of 10% and 25% on office equipment and computers respectively.

(v) The assessment of a company for the assessment year 1995-96 was completed after scrutiny and that of assessment year 1996-97 was completed in summary manner. Audit scrutiny revealed that depreciation aggregating to Rs. 92.57 lakh at the rate of 100% was allowed on moulds

used in the manufacture of plastic containers, against the admissible amount aggregating Rs. 63.47 lakh at the rate of 40%.

## 2.2 WRONG DEPRECIATION ON INTANGIBLE ASSETS

(i) The assessments of a company for the assessment years 1994-95 and 1995-96 revealed that the deduction aggregating Rs. 14.25 lakh towards depreciation on the capitalised portion of expenses for public issue of shares was allowed. Since the capitalised portion of share issue expenses does not result in the acquisition of any tangible, depreciable asset, it does not qualify for depreciation. Hence the deduction should have been disallowed.

(ii) The assessee claimed depreciation of Rs. 11,92,15,886 for the assessment year 1997-98. This included depreciation 10% on preliminary and public issue expenses amounting to Rs. 19,78,314. The Assessing Officer allowed this claim in the assessment made under sec. 143(3). In the computation of income, the Assessing Officer allowed further deduction of Rs. 13,35,555 under Sec. 35D. Allowing the deduction under Sec. 35D as above was in order. The claim for allowance of depreciation on the preliminary and public issue expenses was not proper.

## 2.3 DEPRECIATION ON WRONGLY BROUGHT FORWARD WRITTEN DOWN VALUE

(i) The assessment of a company for the assessment year 1995-96 was completed adjusting unabsorbed depreciation of Rs. 66.81 lakh relating to assessment years 1993-94 and 1994-95. Audit scrutiny revealed that in assessment year 1994-95, the assessee was allowed depreciation on the opening balance of written down value of assets for assessment year 1993-94 instead of allowing it on closing balance of the written down value.

(ii) The assessment of a company for the assessment year 1995-96 was completed allowing deduction on account of depreciation of Rs. 221.51 lakh. Audit scrutiny revealed that the written down value in respect of building, plant and machinery and furniture as on 31st March 1994 was not adopted as the opening written down value as on 1st April 1995. Instead of taking the written down value of assets from the depreciation schedule prepared as per Income Tax Act, the assessee adopted the value from the fixed asset schedule prepared as per Company's Act. The incorrect adoption of written down value resulted in excess allowance of depreciation of Rs. 196.67 lakh.

(iii) The assessment of a company for the assessment year 1995-96 was completed allowing depreciation of Rs. 17.72 lakh in respect of land and building. Audit scrutiny revealed that the assessee company had revalued the land and buildings in order to present a better picture of the company to the banks and other financial institutions. It was mentioned that the increase on account of revaluation would neither be treated as income nor would it be considered to reduce the losses. However, depreciation was

allowed on the revalued amount of the building. Depreciation of Rs. 5.65 lakh only was actually allowable as against Rs. 17.72 lakh allowed by the department.

(iv) The assessment of an 'Association of persons' for the assessment year 1996-97 was completed after scrutiny in March 1999 at a loss of Rs. 137.55 lakh and the assessment for assessment year 1997-98 was rectified determining a loss of Rs. 92.39 lakh. Audit scrutiny revealed that in the assessment year 1995-96, while allowing depreciation on fixed assets, written down value had been adopted as Rs. 736.51 lakh as against the correct written down value of Rs. 659.78 lakh.

#### 2.4 ALLOWING DEPRECIATION FOR FULL YEAR AGAINST USE OF ASSET FOR LESS THAN 180 DAYS

(i) The assessment of a company for the assessment year 1995-96 was completed allowing depreciation of Rs. 546.52 lakh which included depreciation of Rs. 124.14 lakh allowed at hundred per cent on a boiler. Audit scrutiny revealed that the boiler valuing Rs. 124.14 lakh was put to use for a period of less than one hundred and eighty days. Depreciation on this asset was therefore required to be restricted to fifty per cent of the amount calculated at the prescribed percentage.

(ii) The assessment of a company for the assessment year 1995-96 was completed after scrutiny in January 1998 at Rs. 18.10 lakh after allowing depreciation of Rs. 422.51 lakh. Audit scrutiny revealed that 100% depreciation was allowed on machinery of Rs. 39.87 lakh though the machinery was acquired after 30th September 1994 and put to use for less than 180 days.

(iii) The assessment of a company for the assessment year 1994-95 was completed allowing depreciation of Rs. 14.23 lakh at the rate of 25% on road rollers worth Rs. 56.91 lakh. Audit scrutiny revealed that the road rollers were purchased *vide* gate pass dated 30.09.93 from Bangalore and brought to the site in Orissa by self propulsion. Moreover, there was an indication on the copy of the invoice that the road rollers were received on 25.10.1993. Since the road rollers were used for less than 180 days depreciation should have been restricted to fifty per cent of the normal rate.

(iv) The assessment of an assessee company for the assessment year 1995-96 was completed on an income of Rs. 21.37 lakh after allowing depreciation of Rs. 51.88 lakh. Audit scrutiny revealed that full years depreciation on pollution control equipment worth Rs. 19.66 lakh and electrical equipment of Rs. 22.88 lakh was allowed even though the assets were put to use for less than 180 days.

(v) The assessment of a company for the assessment year 1995-96 was completed allowing aggregate depreciation of Rs. 14921.63 lakh on various assets valuing Rs. 65378.49 lakh in the aggregate. Audit scrutiny revealed

that out of the total value of the various assets of Rs. 65378.49 lakh, new assets valuing Rs. 2102.01 lakh were acquired between October 1994 and March 1995. As such, these new assets were put to use for a period of less than one hundred and eighty days in the relevant previous year. Depreciation on these assets was required to be restricted to fifty per cent of the amount calculated at prescribed normal percentage.

(vi) The assessment of a company for the assessment year 1993-94 was completed. Audit scrutiny revealed that depreciation of Rs. 17.92 lakh was allowed at 100% on an energy saving device Hot Air Stenter Machine commissioned in March 1993. Since the machine was used for less than 180 days, depreciation should have been restricted to fifty per cent of normal depreciation. The excess allowance of depreciation resulted in underassessment of income of Rs. 8.96 lakh.

(vii) In the case of a corporate assessee the commercial operation started only on 1.12.1994. Accordingly the assessee was eligible only for 50% of depreciation as against 100% claimed by the assessee. The excess depreciation claimed by the assessee at Rs. 41,06,559/- was to be disallowed. Further, the business loss already determined at Rs. 13,97,374/- and depreciation of Rs. 47,66,648/- had to be added back. Failure to do so in assessment order passed u/s 143(3) for A.Y. 1995-96 by the Assessing Officer resulted in under assessment of income to extent of Rs. 1,26,68,620/-.

(viii) In the case of a company assessee the assessment for the A.Y. 1997-98 was completed u/s 143(3) of the I.T. Act. During the course of scrutiny of accounts of the company, it was observed by the audit that the depreciation was allowed in excess on net value of machinery amounting to Rs. 37.40 lakhs. The Assessing Officer had allowed depreciation @25% while it should have been allowed @12.5% because the machinery was installed/put to use for less than 180 days during the relevant previous year.

## 2.5 ALLOWING DEPRECIATION TWICE

(i) The assessment of a company for the assessment year 1995-96 was completed after scrutiny in March 1998 allowing depreciation of Rs. 297.15 crores. Audit scrutiny revealed that the depreciation of Rs. 297.15 crores was allowed twice initially as claimed by the assessee and again at the time of computation of income by the assessing officer.

## 2.6. WRONG DEPRECIATION ON WRONG ASSET WHEN BUSINESS NOT STARTED

(i) The assessments of a company for the assessment years 1996-97 and 1997-98 were completed in a summary manner in March 1997 and November 1997 on returned loss of Rs. 41.68 lakh and Rs. 28.13 lakh respectively allowing depreciation of Rs. 11.88 lakh and Rs. 8.91 lakh on block of plant and machinery in respective years. Audit scrutiny revealed



that there was no manufacturing operation during the relevant previous years. The company did not file statutory audit reports. The internal auditor's report relevant to the assessment year 1997-98, filed along with the return, however, stated that there was no production during the year. As the plant and machineries were not used for business during the relevant previous year, and information to this effect was available from the records attached with the return, *i.e.* profit and loss accounts, balance sheet etc., allowance of depreciation was irregular.

(ii) The assessment of a company for the assessment year 1993-94 was completed after scrutiny in January 1996 allowing depreciation of Rs. 13.73 lakh. Audit scrutiny revealed that the depreciation was not allowable as there was no manufacturing activity in the previous year relevant to the assessment year 1993-94.

#### 2.6.1 INTERNAL AUDIT OBJECTIONS

##### **Incorrect Allowance of Depreciation**

(i) The assessee claimed depreciation of Rs. 11,92,15,886/- for the Assessment year 1997-98. This included depreciation 10% on preliminary and public issue expenses amounting to Rs. 19,74,314. The Assessing Officer allowed this claim in the assessment made under Sec. 143(3). The claim for allowance of depreciation on the preliminary and public issues was untenable. Omission to do so resulted in excess allowance of deduction of Rs. 19,74,314 involving tax effect of Rs. 6,92,410.

(ii) Assessee claimed depreciation on securities at Rs. 752 lac. While framing asstt., Assessing Officer disallowed 6.34 lac but omitted the balance of Rs. 118 lac which the assessee had debited in P & L account as provision. Assessee had also not disallowed this amount in the adjusted statement of total income. Omission to do so resulted in the revenue loss of Rs. 86 lac including interest.

#### 2.7 WRONG DEPRECIATION ON DISMANTLED ASSETS NOT USED FOR BUSINESS

(i) The assessment of a company for the assessment year 1994-95 was completed after scrutiny in January 1997 determining loss at Rs. 79.30 lakh after allowing deduction of Rs. 427.07 lakh. Audit scrutiny revealed that depreciation of Rs. 36.05 lakh was allowed on certain assets which had been dismantled in the previous year relevant to the assessment year 1993-94 and were pending ascertainment of scrap value. The incorrect allowance of depreciation on dismantled assets, not used by the assessee for the business in the relevant previous year, resulted in excess carry forward of unabsorbed depreciation of Rs. 36.05 lakh involving potential tax effect of Rs. 16.58 lakh.

#### 2.8 WRONG DEPRECIATION ON ASSETS DESTROYED IN FIRE

(i) The assessment of a company for the assessment year 1995-96 was completed after scrutiny in January 1998 allowing depreciation of Rs. 32.98

lakh on a written down value of Rs. 129.52 lakh in respect of the plant and machinery as at the end of the previous year. The company, had received insurance claim of Rs. 196.24 lakh for destruction of certain machinery in fire and the amount was stated to have been reduced from the written down value of assets. Audit scrutiny revealed that in the depreciation statement, reduction from the written down value was considered to the extent of Rs. 105.52 lakh only as against Rs. 196.24 lakh stated as deducted. If the full amount of compensation received of Rs. 196.24 lakh was deducted, the correct written down value would be Rs. 32.98 lakh only instead of Rs. 129.52 lakh as adopted. The correct amount of depreciation allowable would then be only Rs. 8.19 lakh.

## 2.9 MISTAKE IN ALLOWANCE OF DEPRECIATION IN GENERAL

(i) The assessments of an 'Association of persons' for the assessment year 1996-97 and 1997-98 were completed after scrutiny and in summary manner in October 1998 and March 1999 respectively after allowing depreciation of Rs. 13.68 lakh on buildings and furniture and fixtures. Audit scrutiny revealed that depreciation has been allowed at the rate of 10 per cent and 25 per cent as against the admissible rate of 5 per cent and 20 per cent.

(ii) The assessments of an assessee firm engaged in construction of roads for the assessment years 1992-93 and 1993-94 were completed allowing depreciation on trucks amounting to Rs. 12.72 lakh and Rs. 21.85 lakh calculated at the rate of 40 per cent (20 per cent for the trucks used for less than 180 days) on their written down value. Audit scrutiny revealed that the assessee firm was not engaged in the business of running the trucks on hire, it was, therefore, entitled to depreciation at the normal rate of 25 per cent (12.5 per cent for the trucks used for less than 180 days) which worked out to Rs. 7.95 lakh and Rs. 14.85 lakh for assessment years 1992-93 and 1993-94 respectively.

(iii) The assessment of a partnership firm for the assessment year 1994-95 was completed allowing the assessee's claim of Rs. 5.83 lakh towards depreciation in respect of two buildings. Audit scrutiny revealed that the assessee (firm) derived rental income in respect of these buildings which was shown separately as other income. As the buildings were not used for the purpose of the business, the depreciation allowed was irregular.

(iv) The assessment of an Association of Persons for the assessment year 1994-95 was completed for a loss of Rs. 18.02 lakh. Audit scrutiny revealed that while completing the assessment, the assessing officer disallowed expenditure of Rs. 10.13 crores on account of construction of temporary huts as being capital in nature and allowed depreciation of Rs. 50.65 lakh at the rate of 5 per cent. However, it was further revealed that the assessee had claimed 100 per cent depreciation again on the temporary structure at Rs. 701.04 lakh (which was included in the amount of Rs. 10.13 crores)

Omission to disallow the same resulted in underassessment of income to the same extent. Besides, the department did not disallow this dual deduction as *prima facie* adjustment when the depreciation statement as per Income Tax Rules was filed in November 1995. This mistake resulted in loss of revenue of Rs. 62.81 lakh towards additional tax which was leviable.

(v) In the return filed for the Assessment Year 1997-98, the assessee claimed depreciation 40% on trucks. The profit & loss account did not reveal that the assessee had received transport charges. The details furnished at the time of scrutiny also did not suggest that the assessee had given the trucks on hire. The assessee, therefore, had not deployed the trucks in the business of plying them on hire. In the circumstances, the trucks were eligible for depreciation at the ordinary rate of 25% only. In the assessment made under Sec. 143(3), the Assessing Officer, however, allowed depreciation 40% on the trucks.

(vi) The assessment of a company for A.Y. 1995-96 was completed. The Assessee had claimed depreciation of Rs. 14,94,654 as per I.T. Act which included Rs. 11,27,610 on premises. In the return and the other letters assessee was showing addresses of two buildings *i.e.* Taj Bldgs., D.N. Road and Shandeep-10, Attamound Road. Assessee had offered Rs. 6,26,275/- under the head Service charges received, which included rent received on Shandeep Premises (Rs. 2,52,000/-), Accommodation charges of B.R. Shah (Rs. 55790 + Rs. 56197) from Taj Bldg. Therefore it was clear that assessee company had let out the property and was not entitled for any depreciation as per section 32 of I.T. Act. Allowing depreciation on premises had resulted in under assessment of Rs. 11,27,610/-.

(vii) The assessment of a corporate assessee for A.Y. 1995-96 was completed. While computing the income depreciation of Rs. 11832696/- was allowed by the A.O. It was seen from the depreciation statement that depreciation of Rs. 10067585/- was allowed on Gas cylinders given on lease in bulk to others. As the Gas cylinders were purchased and leased out in bulk, it lost its individuality and the cumulative value of the plant was to be taken into consideration. Accordingly the assessee was not entitled to claim 100% depreciation as value less than Rs. 5000/-. This depreciation should have been allowed at the rate of 25% as against 100% allowed by the department. Omission to disallow the excess depreciation of Rs. 7550689/- resulted in under assessment of income of the same extent.

(viii) The assessment of a company assessee for A.Y. 1992-93 was completed. In the assessment order u/s 143(3), the Assessing Officer instead of withdrawing depreciation of Rs. 16,08,036/- on expenditure on Scientific research claimed u/s 35, added the same to the depreciation claimed at Rs. 8,43,23,160/- and allowed depreciation at Rs. 8,59,31,196/-. Thus excess depreciation of Rs. 32,16,072/- was allowed.

(ix) The assessment of a company assessee for A.Y. 1995-96 was completed. In this case the depreciation of Rs. 15,40,191/- was allowed twice-once for the period 1.4.1994 to 30.9.1994 and again for the period. 1.10.1994 to 31.3.1995, in the hands of both the amalgamating co. and the amalgamated co. The mistake resulted in under assessment of income of Rs. 42,29,658/- resulting in short levy of tax of Rs. 9,65,852/-.

(x) The assessment of company for A.Y. 1996-97 was completed. The Audit Scrutiny revealed that the depreciation on chlorine toners had been claimed and allowed at 100% amounting to Rs. 11,00,000/-. This item was not mentioned in Appendix I of I.T. Rules 1962 alongwith other items on which 100% depreciation was allowable. The mistake resulted in excess allowance of depreciation of Rs. 11,00,000/-

#### **INTERNAL AUDIT OBJECTIONS**

##### **Incorrect Allowance of Depreciation**

Higher depreciation @40% is admissible on trucks and buses if an assessee employs the trucks in the business of running them on hire for others. In the return filed for the Assessment Year 1997-98, the assessee claimed depreciation @40% on trucks. The profit and loss account did not revealed that the assessee had received transport charges. The details furnished at the time of scrutiny also did not suggest that the assessee had given the trucks on hire. The assessee, therefore, had not deployed the trucks in the business of plying them on hire. In the circumstances, the trucks were eligible for depreciation at the ordinary rate of 25% only. In the assessment made under Sec. 143(3), the Assessing Officer, however, allowed depreciation @40% on the trucks. Omission to disallow the claim of deduction of higher rate of depreciation on the trucks resulted in under assessment of Rs. 1,37,840 involving tax effect of Rs. 59,271.

### CHAPTER-3

#### 3.1 WRONG DEDUCTION US 80I & 80IA: RELATING TO PROFITS OF NEW INDUSTRIAL UNDERTAKING IN BACKWARD AREAS

(i) The assessment of an assessee for the assessment year 1994-95 was completed allowing a deduction of Rs. 14.69 lakh u/s. 80 IA of the IT Act out of the income determined at Rs. 44.63 lakh. Audit scrutiny revealed that the assessee was a new industrial undertaking which obtained the plant and machinery on lease from its sister concern engaged in the manufacture of the same products. As the prescribed condition was not fulfilled the said deduction of Rs. 14.69 lakh U/s. 80 IA was not allowable.

(ii) The assessment of a company for the assessment year 1995-96 was completed at Rs. 218.97 lakh after allowing Rs. 153.26 lakh as deduction in respect of profits from new industrial undertaking which started functioning after 1st April, 1991. Audit scrutiny revealed that the taxable income included commission income of Rs. 51.94 lac. As the deduction was admissible only in respect of profits derived by the assessee from its manufacturing activity, deduction allowed in respect of commission income was not in order.

(iii) The assessment of a closely held company for the assessment year 1994-95 was completed at Rs. 255.46 lakh after allowing a deduction of Rs. 68.92 lakh on account of profit from a newly established industrial undertaking. Audit scrutiny revealed that the profit included an aggregate sum of Rs. 80.61 lakh towards income from interest, dividend, agency commission, miscellaneous income and rental income. As the deduction is admissible only in respect of profits derived from manufacturing activity, inclusion of other income in the business profit for computation of qualifying amount of deduction was not in order.

(iv) The assessment of a company for the assessment year 1995-96 was completed allowing a deduction of Rs. 34.49 lakh in respect of profits from industrial undertakings. Audit scrutiny revealed that the government of India, Ministry of Tourism, granted approval to the assessee's hotel with specific effective date from 30 November 1995 in relation to section 80 HHD and 80 IA. As such the assessee was not entitled to deduction during the assessment year 1995-96.

(v) The assessment of a company for the assessment year 1996-97 was completed at Rs. 6.37 lakh after allowing a deduction of Rs. 185.40 lakh in respect of profits and gains from newly established industrial undertakings. As the production of the assessee started in the previous year relevant to

the assessment year 1988-89, the above deduction would be eligible only upto the assessment year 1995-96 being the eighth assessment year. Therefore, deduction beyond the eighth assessment year should have been disallowed by the assessing officer.

(vi) The assessment of a company for the assessment year 1995-96 was completed after allowing deduction of Rs. 285.38 lakh in respect of profits from new industrial undertakings in the backward area. Audit scrutiny revealed that interest income amounting to Rs. 102.44 lakh, which was not derived directly from industrial activity, was not deducted from the profits from business while computing the above deduction. The omission resulted in excess allowance of Rs. 20.49 lakh.

(vii) It was seen from the assessment order that deduction u/s 80 I had been allowed at Rs. 16580413/-. The deduction had been claimed by the assessee in respect of manufacturing division @30% on net profit of Rs. 5526804/-. The depreciation as per books of a/c i.e. Rs. 4078438/- was not added back and the depreciation as per I.T. Act. i.e. Rs. 11012199/- was not reduced from net profit for the purpose of claiming deduction u/s 80 I. Secondly, the assessee claimed deduction to the tune of Rs. 38721524/-, u/s 35 of I.T. Act on A/c of R&D expenditure towards scientific research. Out of Rs. 38721524/-, the A.O. disallowed Rs. 19308166/- allowing net deduction of Rs. 19413358/-. The amount of Rs. 19413358/- was not reduced from the profit of the manufacturing division for the purpose of claiming deduction u/s 80 I. The mistake resulted in excess allowance of deduction u/s 80 I by Rs. 7904136/-.

(viii) It was seen from the assessment order of a company assessee for A.Y. 1995-96 that the assessee had been granted deduction u/s 80HH and 80 I amounting to Rs. 303865/- & Rs. 379832/- respectively. As per the provisions of section 80HH clause 9 A of the I.T. Act, 1961 "in the case where the assessee is entitled also to the deduction u/s 80I or section 80J in relation to its profits & gains of an industrial undertaking or the business of a Hotel to which this section applies, effect shall first be given to the provision of this section". Therefore, the admissible profit for deduction u/s 80I was required to be reduced by the amount of deduction u/s 80HH. In the present case both 80HH & 80I had been allowed on the eligible profits of Rs. 1519327/- 20% & 25% respectively. The mistake resulted in an excess grant of deduction u/s 80I amounting to Rs. 75967/-.

(ix) In the case of a corporate assessee the Assessing Officer while completing the assessment u/s 143(3) r.w.s. 147 and also order u/s 154 dt. 12.4.99 for the AY 91-92, allowed deduction u/s 80I amounting to Rs. 47,203/- in spite of the fact that the old plant & machinery transferred from the existing unit to the New Unit exceeded 20% of the total value of the Plant & Machinery held in the new unit, even though the assessee was not entitled for such deduction. As a result, there was an excess deduction to the extent of Rs. 47,203/-. The revenue loss on account of this failure on

the part of the AO was Rs. 75,238/- including 234B interest. On same grounds the deductions already allowed to the assessee right from the AY 91-92 to 98-99 have to be withdrawn aggregating to Rs. 3,57,10,692/- with the tax effect of Rs. 1,42,84,385/-.

(x) The assessment of a widely held company for the assessment year 1995-96 was completed after scrutiny in March 1998 at nil income after allowing deduction of Rs. 1390.45 lakh in respect of its newly established unit being 30% of the profit of Rs. 4634.83 lakh. Audit scrutiny revealed that unabsorbed loss of Rs. 116.57 lakh relating to assessment year 1994-95 was not deducted from the profits while determining the quantum of deduction. After deducting the aforesaid amount, the profit of the unit would work out of Rs. 451.26 lakh and the allowable deduction to Rs. 1355.48 lakh as against Rs. 1390.45 lakh allowed.

## CHAPTER-4

### 4.1 WRONG DEDUCTION US 80 HHC RELATING TO EXPORT PROFITS

(i) The assessment of a widely held company engaged exclusively in export business for the assessment year 1996-97 was completed at nil income after allowing a deduction of Rs. 809.61 lakh in respect of export profits. Audit scrutiny revealed that the assessee company received interest of Rs. 31.63 lakh and after adjustment of an amount of Rs. 28.72 lakh representing interest paid by the assessee, the net amount of interest of Rs. 2.91 lakh was credited to the profit and loss account relevant to the assessment year 1996-97. However, while allowing deduction towards export profit, business profit was not reduced by Rs. 28.47 lakh being ninety per cent of interest income of Rs. 31.63 lakh.

(ii) The assessment of a widely held company for the assessment year 1991-92 was completed allowing a deduction of Rs. 238.86 lakh towards relief in respect of export profit as claimed after reducing proportionate disclaimed export profit of Rs. 15.17 lakh. Audit scrutiny revealed that the deduction was calculated on the gross total income of Rs. 1730.55 lakh which included income from house property and from other sources instead of on the income from business or profession of Rs. 1603.33 lakh.

(iii) The assessment of a company for the assessment year 1995-96 was completed for taxable income of Rs. 8384.70 lakh after allowing a deduction of Rs. 439.19 lakh towards export profits. Audit scrutiny revealed that while computing the deduction, central excise duty had not been included in the total turnover. After considering the same, the allowable deduction would work out to Rs. 358.93 lakh as against Rs. 439.19 lakh allowed by the department.

(iv) The assessment of a company for the assessment year 1995-96 was completed at Rs. 2008.08 lakh after allowing deduction of Rs. 126.18 lakh toward export profits on the basis of Tax Audit Report. Audit scrutiny revealed that while allowing the above deduction, the assessing officer had taken into consideration only profits of Rs. 125.82 lakh derived from export of manufacturing goods and Rs. 0.36 lakh in respect of export incentives but omitted to consider the loss of Rs. 32.51 lakh sustained by the assessee from export of trading goods. Thus after considering the loss of Rs. 32.51 lakh the net deduction admissible worked out to Rs. 93.67 lakh as against Rs. 126.18 lakh allowed by the assessing officer.



(v) The assessment of a company for the assessment year 1995-96 was completed, *inter alia*, allowing a deduction of Rs. 38.32 lakh toward export profits on the basis of Tax Audit Report. Audit scrutiny revealed that while allowing the above deduction, the assessing officer had taken into consideration only export incentives of Rs. 271.02 lakh but omitted to consider the loss of Rs. 353.28 lakh sustained by the assessee from export of manufactured/processed and trading goods. Had the loss been taken into account, the resultant amount would have been negative and no deduction would be admissible.

(vi) The assessment of a company for the assessment year 1994-95 was completed after scrutiny in March 1996 allowing a deduction of Rs. 52.17 lakh towards export profit. Audit scrutiny revealed that assessee had claimed deduction in respect of export profit subject to grant of permission by Commissioner of Income Tax of extension of time for realisation of sale proceeds which was to be received in convertible foreign exchange, on an application filed by the assessee company. There was no evidence in the assessment records that said permission was granted by the Commissioner. Therefore, the deduction allowed by the assessing officer was not in order.

(vii) The assessment of a company for the assessment year 1996-97 was completed at Rs. 630.57 lakh after allowing a deduction of Rs. 74.08 lakh in respect of export turnover. Audit scrutiny revealed that while allowing the deduction, the assessing officer had not reduced the profits by Rs. 147.64 lakh being 90% of the interest income, lease rent and management fees received by the assessee during the relevant previous year. Further, an amount of Rs. 517.63 lakh on account of central excise duty collected was not included in the total turnover. Considering the above, the allowable deduction would work out to Rs. 64.51 lakh as against Rs. 74.08 lakh allowed.

(viii) The assessment of an individual for the assessment year 1992-93 was completed allowing a deduction of Rs. 10.57 lakh in respect of export profits as claimed. Audit scrutiny revealed that the assessee was not a direct exporter, but only a supporting manufacturer as he was selling sea Goods processed by him to export/trading house without direct export and the deduction on account of export profits was required to be calculated as applicable to supporting manufactures. The assessing officer, however, allowed the deduction including proportionate increase on account of export incentives as in the case of direct exporters.

(ix) The assessments of a registered firm for the assessment years 1992-93 and 1993-94 were completed on a total income of Rs. 9.99 lakh and Rs. 15.35 lakh *inter alia* allowing deduction of Rs. 160.69 lakh and Rs. 29.74 lakh towards relief in respect of export turnover. Audit scrutiny revealed

that while computing the total turnover, the amount of foreign exchange of Rs. 35.95 lakh and Rs. 150.49 lakh not realised had not been included in the total turnover. Further, the assessee had not also included the profit of exchange fluctuation of Rs. 153.78 lakh and 81.13 lakh for purposes of export as well as total turnover.

(x) The assessment of a firm for the assessment year 1995-96 was completed after scrutiny in February 1998 at an income of Rs. 18.80 lakh allowing a deduction of Rs. 89.99 lakh towards export profits. Audit scrutiny revealed that no reduction was made in respect of export turnover amounting to Rs. 45.68 lakh not realised within time limit. Further, 90 per cent of insurance receipt of Rs. 42.04 lakh was not deducted from the business profit and loss in trading export of Rs. 28.20 lakh was not adjusted. Thus deduction of Rs. 89.99 lakh was erroneously allowed in place of the correct amount of Rs. 35.39 lakh allowable.

(xi) It was seen from assessment order and the return of income that the deduction u/s 80HHC had been claimed and allowed at Rs. 7056853/-. During the year the assessee had income from house property (Rs. 1909357), income from other sources (Rs. 3127323/-(+) Rs. 255815/-) and income from business (Rs. 5227044/-) out of export of trading goods. From the working of 80HHC deduction shown in form no. 10-CCAC it could be seen that the indirect expenses were not taken into account.

After excluding the proportionate indirect expenses, profit from the export of trading goods became a negative figure. There were no export incentives. Accordingly, the assessee was not eligible for any deduction u/s 80HHC, since the profits from the export of trading goods was a minus figure. No export of manufactured goods or local sales were made. The allowance of deduction of Rs. 7056853/- resulted in under assessment of income of like amount.

(xii) The case of a company assessee for A.Y. 1995-96 was completed u/s 143(3) in Feb., 1998. The assessee company had been allowed deduction u/s 80 HHC at Rs. 1,23,41,809/- as against Rs. 12,13,59,666/- claimed. However, a scrutiny of the working of deduction u/s 80HHC of the assessee company and that of the department revealed that the following amounts to arrive at the eligible export turnover were not considered by the assessee company and the department.

1. Amount not considered by the assessee company but considered by department Rs. 15873586/- on account of expenses incurred for rendering services outside India including telecommunication expenses.

2. Amount not considered by the department but considered by the assessee company.

(a) Payments not received before 30.11.95 Rs. 7817500/-

(b) Inter unit sale of fine wear Rs. 3,60,00,000/-

Had the amount stated above considered by the department there would

have been less amount of allowance of deduction u/s 80HHC (i.e. Rs. 102800924/- as detailed in audit query). This resulted in under assessment of income to the extent of Rs. 20617160/- involving short levy of tax of Rs. 16122685/- (including interest u/s 234B of Rs. 6638787/-)

(xiii) The assessment of a company assessee for A.Y. 1995-96 was completed after scrutiny in March, 1998. The Assessee was allowed deduction of Rs. 541572/- u/s 80HHC. As the assessee was engaged in the business of Publishing Magazine and selling data relating to stock market, there was no manufacturing activity of goods or merchandise and hence deduction u/s 80HHC was not allowable to the assessee company. Allowance of 80HHC deduction had resulted in under assessment of Rs. 541572/- leading to short levy of tax of Rs. 428492/- including interest u/s 234B. Without prejudice to above, it was seen that while allowing deduction the lease income of Rs. 15071374/- and the other income of Rs. 593649/- had also been considered which had resulted in excess allowance of deduction u/s 80HHC. The deduction u/s 80HHC allowable worked out to Rs. 466580/- as against Rs. 541572/- allowed by the Deptt. resulting in excess allowance by Rs. 74992/-, leading to short levy of tax of Rs. 59335/- including interest u/s 234B.

#### INTERNAL AUDIT OBJECTIONS

##### Excess Deduction U/s 80HHC

(xiv) Sec. 80HHC(3) provides a formula for computation of export profits eligible for deduction. It enjoins aggregation of export profits/losses and only the resultant profit has to be allowed as deduction under sec. 80HHC.

For the Assessment year 1996-97 the assessee exports trading goods as also manufactured goods. In the business of export of trading goods, the assessee made profit in some exports while incurring loss in some other. On trading export of agricultural goods of Rs. 2,57,02,663, the assessee incurred a loss of Rs. 11,56,620. The assessee should have reduced this loss from the profit earned from export of trading goods. The assessee, however, ignored this loss and accounted for only the profitable exports while computing profit u/s 80HHC for trading goods. The reason for exclusion of the loss according to the assessee, as per a note, is that for the purpose of profit u/s 80HHC, only exports resulting in profit have to be taken. This contention should not have been accepted since such segregation is not permissible under the law. Evidently, the assessee claimed deduction u/s 80HHC in excess by Rs. 11,56,620. Allowance of excess deduction as above resulted in under assessment by Rs. 11,56,620 involving tax effect of over Rs. 5 lakhs.

(xv) In the case of a company for the A.Y. 1998-99 incorrect claim of deduction u/s 80HHC was made and allowed by the Assessing Officer the asstt. was rectified to recover tax of Rs. 2,59,617.

## CHAPTER-5

### MISTAKES IN ASSESSMENT WHILE GIVING EFFECT TO APPELLATE ORDERS

(i) The assessment of a company for the assessment year 1995-96 was revised in March 1998 to give effect to appellate orders. Audit scrutiny revealed the following omissions: (i) the revised order was passed for an income of Rs. 613.64 lakh instead of Rs. 646.53 lakh as declared by the assessee in the revised return filed in February 1997 which resulted in underassessment of income of Rs. 32.89 lakh (ii) the credit for advance tax of Rs. 8.56 lakh pertaining to the assessment year 1996-67 was erroneously given in the assessment year 1995-96 (iii) while computing the net demand the refund of Rs. 5.86 lakh allowed to the assessee in January 1997 was not considered. Considering the above mistakes, the demand to be raised worked out to Rs. 28.68 lakh as against which the department allowed a refund of Rs. 3.32 lakh.

(ii) The assessment of a company for the assessment year 1993-94 originally completed after scrutiny in December 1995 was revised in March 1997 to give effect to the appellate orders. While computing the income, the department allowed deduction of Rs. 5.66 lakh after netting the adjustment for earlier years on account of modvat element not considered for valuing the closing stock. Audit scrutiny revealed that the assessee company preferred an appeal for earlier years in respect of modvat additions made by the department which were deleted by the appellate authority for earlier years and the said orders were given effect to in revised assessments for the concerned assessment years. Therefore, instead of allowing deduction of Rs. 5.66 lakh after netting an amount of Rs. 13.54 lakh was actually required to be added.

(iii) The assessment of a company for the assessment year 1992-93 initially completed after scrutiny in November 1994 was subsequently rectified in December 1994 and November 1995 computing income at Nil after allowing set off of brought forward losses of Rs. 70.34 lakh. The assessment was revised in March 1996 to give effect to the orders of CIT (Appeals) computing the income at a loss of Rs. 21.71 lakhs, which included deduction of Rs. 21.36 lakh in respect of new industrial undertaking. Audit scrutiny revealed that while giving effect to appellate orders the department allowed deduction in respect of new industrial undertaking which was not in order as there was no positive income after setting set off brought forward losses of earlier years. Incorrect grant of deduction resulted in excess carried forward of loss of Rs. 21.36 lakh.

(iv) The assessment of a widely held company engaged in the business of growing and manufacturing tea for the assessment year 1992-93 was completed after scrutiny in March 1995 allowing a deduction of Rs. 340 lakh on account of deposit under tea development account as it was less than twenty percent of the profits of such business amounting to Rs. 1846.47 lakh. The above assessment was revised in May 1997 to give effect to an appeal order and profits of tea business were determined at Rs. 1400.36 lakh. Audit scrutiny revealed that the assessing Officer while revising the amount of taxable income of the assessee, omitted to withdraw the excess allowance of deduction of Rs. 59.93 lakh in respect of deposit under tea development account as the amount of deduction calculated on the basis of revised profits of the business was less than the amount deposited with the nationalised bank.

(v) The audit scrutiny in the case of a company for assessment year 1996-97 revealed that additional tax of Rs. 6,51,849/- levied in intimation under section 143(1) (a) was erroneously omitted to be included in the order dated 18-5-1999, giving effect to the appellate order of CIT (A).

(vi) The Audit has pointed out that in an order u/s 143(3) dated 18.3.1992, deduction under Chapter VI A were allowed at Rs. 59,31,357/- computing taxable income at Rs. 41,95,44,392/-. In an order u/s 154 dated 25.6.1993, the income was reduced to Rs. 39,93,87,320/- after setting off brought forward losses and after allowing Chapter VI-A deductions at Rs. 59,31,357/-. While giving effect to order of the CIT (A) on 28.3.1995, the department has started computation of income with taxable income as per order dated 25.6.1993 at Rs. 39,93,87,320/- and allowed deduction under Chapter VI-A of Rs. 54,48,134/- without adding back the deduction under chapter VI-A already allowed at Rs. 59,31,357/- in order dated 25.6.1993.

(vii) In the case of a company for the assessment year 1996-97 the assessment under section 143(3) was completed on 26-3-1999. This order was modified on 18-5-1999 to give effect to the appellate orders of the CIT(A). In the original order "the profits of the business" were worked out at Rs. 6,09,45,048 for the purpose of section 80HHC. The audit scrutiny revealed that in the order giving effect to the appellate order, the deduction was worked out on this amount of Rs. 6,09,45,048 whereas the actual profits of the business worked out to Rs. 1,16,32,569 consequent to reduction of the total income in the appeal. This resulted in excess allowance of the deduction to the extent of about Rs. 48 lakhs.

## CHAPTER-6

### INCOME ESCAPING ASSESSMENT

(i) The assessment of a company for the assessment year 1995-96 was completed at Rs. 224.21 lakh. Audit scrutiny revealed that an incentive income of Rs. 20.37 lakh received on investments in Government securities and small saving schemes with postal department was granted exemption from total income, on the ground that it goes to reduce the cost of investments. As such incentive amounts are given separately after the cost of investment is paid in full, the same is a revenue receipt and assessable to tax.

(ii) The assessment of a domestic company for the assessment year 1995-96 was completed at a total income of Rs. 407.12 lakh. Audit scrutiny revealed that the assessee company received a sum of Rs. 36 lakh on 31 March 1995 in respect of rent for the year 1994-95 from a company for which the assessee had claimed and was allowed credit for tax deducted at source of Rs. 8.28 lakh. However, the income of Rs.36 lakh was neither credited to the profit and loss account relevant to the assessment year 1995-96 nor considered in the assessment.

(iii) The assessment of a company for the assessment year 1994-95 was completed at Rs. 228.68 lakh. Audit scrutiny revealed that though an amount of Rs. 11.53 lakh being 'unclaimed credit balances written back' was credited to profit and loss account, the same was allowed as deduction while computing the total income. As the sum constituted income of the assessee company in the light of the judgement of the Hon'ble Supreme Court, 222ITR 344(SC), the deduction of Rs. 11.53 lakh was irregular.

(iv) The assessment of a company for the assessment year 1992-93 was completed. Audit scrutiny revealed that a landed property was sold during the previous year for a consideration of Rs. 23.70 lakh. Taking the cost of acquisition at Rs.1.06 lakh as shown in the schedule of fixed assets and after allowing the statutory deductions, the long term capital gain on the transfer of the land would work out to Rs.20.24 lakh. But the same was however, not taken into account as income on the ground that the consideration money was not received and necessary approval for exemption under Urban Land (Ceiling and Regulations) Act, 1976 was not received. As the assessee maintained mercantile system of accounts, income from capital gains was to be included in the total income of the assessee.

(v) The assessment of a widely held manufacturing company for the assessment year 1991-92 was completed at a loss of Rs. 33.01 lakh. Audit scrutiny revealed that the assessee had collected an amount of Rs. 32.03 lakh representing employees' contribution to provident fund and employees' contribution to state insurance but failed to deposit the same to the respective funds within the due date. The sum of Rs. 32.03 lakh so collected therefore constituted a receipt to the assessee company and was required to be included in the computation of income.

(vi) The assessment of an individual for the assessment year 1992-93 was completed for a taxable income of Rs. 1,190. The assessee was a partner, alongwith three others, in a firm which commenced its business in June, 1984 and was dissolved in May 1991. The said business including capital assets was sold to an individual as per assignment made in April 1991 for a consideration of Rs. 16 lakh, which was distributed among the four partners equally. The share of the assessee was treated as capital gain and exemption was granted as the amount was invested in the purchase of a residential house property. Audit scrutiny revealed that the firm was in existence at the time the assignment was made and therefore the consideration of Rs. 16 lakh should have been treated as capital gain in the hands of the firm and the share of the assessee partner should have been treated as income. The incorrect grant of exemption resulted in under assessment of income of Rs. 4 lakh.

(vii) The assessment of a firm for the assessment year 1994-95 was completed at a total income of Rs. 6.78 lakh. Audit scrutiny revealed that two partners of the firm had retired on 24 August, 1993. Consequently the assets of the firm was revalued at Rs. 20.98 lakh and Rs. 6.29 lakh and was paid to each of the retired partners in addition to the amount standing to the credit of their capital account. The partial distribution of the value of assets to the partners on dissolution of firm are liable to tax.

(viii) The assessment of an assessee for the assessment year 1996-97 was completed at taxable income of Rs. 6.50 lakh. Audit scrutiny revealed that credit of Rs. 2,84,319 was given on account of tax deducted at source on receipt of commission of Rs. 1,41,43,550 but the said commission was not offered for taxation. As the credit of Rs. 2,84,319 was allowed by the department towards tax deducted at source, commission received/credited should have been added back to income of assessee.

(ix) For the Assessment Year 1998-99, the assessee filed the return declaring loss of Rs. 17,19,030. During the year, the assessee sold plant and machinery for a consideration of Rs. 12,48,082. The WDV of plant and machinery for the year was only Rs. 4,02,110. Since the block of plant and machinery was totally wiped out by the sale consideration, the remaining

sale consideration received by the assessee amounting to Rs. 9,45,972 had to be treated as short term capital gain in accordance with sec. 50 of the Income-tax Act. The assessee, however, did not include this short term capital gain as income in the return filed.

(x) The assessment of a company assessee for A.Y. 1998-99 was completed after scrutiny. The Audit scrutiny revealed that interest on securities of Rs. 18,15,052 was omitted to be assessed as income. Further, excess claim of depreciation to be disallowed on chassis was Rs. 14923.

(xi) In the case of a firm the assessee had entered into an agreement with a developer for the development of assessee's land into a commercial complex for which the assessee had agreed to transfer 55% of the land holding equivalent to 4950 sq.ft. of land to the developer. In return the transferee had to construct and deliver to the assessee 45% of super built area and car parking. On the basis of no objection certificate obtained by the assessee u/s 269-UL(I), it was evident that there was a transfer of 55% of that land area to the other party by the assessee as per provisions of sec. 2(47)(v). Accordingly, the value of 55% of the land at Rs. 41,42,450/- should have been brought to tax under long term capital gains. Failure to do so while completing the assessment u/s 143(3) for the A.Y. 95-96 resulted in a revenue loss of Rs. 21,38,482/- including interest u/s 234B.

(xii) In the case of a company the assessment was completed for the assessment year 1994-95 determining the total income at NIL. The audit scrutiny revealed that the Assessing Officer had issued a certificate under section 197(1) in Form No. 15EE on 19-6-1995 to another company to pay the rental income of Rs. 39,60,000/- without making TDS to the assessee company. This income from property was not declared to tax. The income was therefore underassessed by the same amount.

(xiii) In the case of an individual scrutiny under section 143(3) for the assessment year 1994-95 was completed by the AO by accepting the computation of capital gains as worked out by the assessee. The audit scrutiny revealed that the assessee had entered into a Joint development agreement with a builder in respect of land owned by the assessee. As per the agreement, the assessee transferred 5,914 sq. ft. of land for a built up residential flat measuring 6,228 sq. ft. For the purpose of computing the consideration received, the assessee adopted the value, as shown for the purpose of registration of the undivided share holding of the land by various flat owners, instead of offering the market value of built up area received as a part of the consideration, resulting in an under declaration of Rs. 37 lakhs.



**INTERNAL AUDIT OBJECTIONS****Withdrawal From NSS Not Accounted For As Income**

(i) Contributions to the NSS were allowed as deduction when subscribed. Withdrawals from the NSS (which may include interest), however are fully taxable. The Post Office is also obliged to deduct tax at source on the withdrawal made from the NSS. The assessee withdrew a sum of Rs. 129299 from the NSS. The Post Office deducted tax at source amounting to Rs. 25860 at the time of withdrawal. In the return of income for the Assessment Year 1997-98, the assessee claimed credit for TDS of Rs. 25860 effected on the amount of Rs. 1,29,299 withdrawn from the NSS. The assessee, however, did not include the amount withdrawn from the NSS in his total income. While processing the return under sec. 143(1)(a), the Assessing Officer allowed credit for TDS effected on the amount withdrawn from the NSS without realising the fact that the assessee had not accounted for the amount withdrawn as income. The mistake resulted in under assessment of income by Rs. 1,29,299 involving tax effect of Rs. 74,989.

(ii) In the case of a firm for the A.Y. 1998-99 & 99-2000 TDS on fixed deposit was allowed but the interest income on this fixed deposit was not taken into computation to income which resulted into short levy of tax to the tune of Rs. 2,41,260 and Rs. 1,94,863 respectively.

## CHAPTER-7

### INCORRECT SET OFF AND CARRY FORWARD OF UNABSORBED DEPRECIATION/INVESTMENT ALLOWANCE/ BUSINESS LOSS/CAPITAL LOSS

(i) The assessment of a company for the assessment year 1992-93 was completed allowing carry forward of unabsorbed depreciation of Rs. 405.88 lakh. Audit scrutiny revealed that while giving effect to the appellate orders for the assessment year 1991-92 in March 1997, the unabsorbed depreciation to be carried forward was determined at Rs. 395.94 lakh. The assessment for the assessment year was therefore required to be revised.

(ii) The assessment of a company for the assessment year 1995-96 was completed computing the income at Rs. 474.88 lakh after setting off brought forward unabsorbed depreciation of Rs. 11.61 lakh pertaining to the assessment years 1992-93 and 1993-94. Audit scrutiny revealed that the unabsorbed depreciation of Rs. 11.61 lakh was already set off in the assessment year 1994-95.

(iii) The assessment of a company for the assessment year 1995-96 was completed determining total income of Rs. 4330.77 lakh after allowing set off of unabsorbed depreciation allowance of Rs. 935.10 lakh relating to assessment year 1994-95. Audit scrutiny revealed that as per rectificatory order for the assessment year 1994-95 passed in March 1998, the loss (unabsorbed depreciation) for that assessment year was computed at Rs. 437.94 lakh. Since the scrutiny assessment for the assessment year 1995-96 was concluded subsequent to the revision of the assessment for the assessment year 1994-95, the set off of unabsorbed depreciation was required to be restricted to Rs. 437.94 lakh instead of Rs. 935.10 lakh.

(iv) The assessment of a company for the assessment year 1995-96 was completed determining loss at Rs. 74.30 lakh and allowing carry forward of unabsorbed investment allowance of Rs. 10.09 lakh relating to the assessment year 1986-87. Audit scrutiny revealed that the assessee was not entitled for carry forward of the above unabsorbed investment allowance as it had lapsed in the assessment year 1994-95 itself on expiry of eight assessment years as provided in the Act.

(v) In the case of the assessee company the assessment for the A.Y. 1993-94 was finalised by the Assessing Officer u/s 250/143(3) of the I.T. Act, 1961 *inter alia* determining the total income at Rs. 2,39,83,379/-. Audit scrutiny revealed that the assessee had been wrongly allowed set

off of short term capital loss of Rs. 7,95,733/- from share trading against business income in controvention of provisions of section 73.

(vi) The assessment of a company assessee for A.Y. 1995-96 was completed u/s 143(3) in Feb., 1998. It was seen from the assessment order that from the capital gain of Rs. 5,49,68,092/-, an amount of Rs. 1,12,66,462/- had been adjusted on account of b/f losses from earlier years. The balance amount of Rs. 4,37,01,620/- was adjusted against the business loss of Rs. 10,06,10,559/- along with dividend income of Rs. 5,69,08,929/- to arrive at the 'Nil' income. It was however, seen that the assessment orders of earlier years had taxable income after adjusting all sorts of losses from the inter heads of income and no loss either from the head business, capital gain or other sources was allowed to be set off in subsequent year. As such adjustment of Rs. 1,12,66,462/- on account of long term capital loss b/f from the capital gain of the year of Rs. 5,49,68,092/- was irregular and resulted in under assessment of income to that extent involving short levy of tax of Rs. 77,96,995/-.

(vii) The case of a company assessee for the A.Y. 1995-96 was completed by the assessing officer on 16.2.98 determining the taxable income as nil after adjusting against the income of Rs. 10,60,36,845/- sum of Rs. 7,62,93,613/- towards the carried forward unabsorbed depreciation and Rs. 2,97,43,232/- towards unabsorbed investment allowance relating to A.Y.'s 1987-88 to 1991-92. Audit security, however, revealed that in addition to unabsorbed depreciation and unabsorbed investment allowance the assessee company had current year's depreciation which was neither claimed by the assessee nor allowed by the assessing officer. The details thereof was also not kept on the record. The claim of depreciation as per company's a/c amounted to Rs. 4,35,30,036/-. The assessee company was not claiming depreciation since A.Y. 1992-93. According to the order of priority current year's depreciation and unabsorbed depreciation of earlier years have precedence over unabsorbed investment allowance carried forward. Hence Rs. 7,62,93,613/- should have been adjusted against unabsorbed depreciation and remaining Rs. 2,97,43,232/- against the current year's depreciation in order to bring the total income to nil. If this was done, there would be no opportunity for the assessee company to adjust the unabsorbed investment allowance relating to A.Y. 1987-88 as it continued to incur losses upto A.Y. 1995-96, beyond which unabsorbed investment allowance relating to A.Y. 1987-88 could not be carried forward. Omission to do so led to carry forward of excess unabsorbed investment allowance by Rs. 1,61,25,635/- involving potential demand of Rs. 74,17,792/-.

(viii) The assessment of an association of persons for the assessment year 1994-95 was completed at a total income of Rs. 32.96 lakh which was fully set off against carried forward unabsorbed business loss and depreciation relating to earlier years reducing the income to nil. Audit

scrutiny revealed that the assessing officer in arriving at the total income of Rs. 32.96 lakh erroneously allowed set off of long term capital loss on compulsory acquisition of land amounting to Rs. 45.79 lakh against income under the other heads.

(ix) In the best judgement assessment of a company for the assessment year 1994-95 set off of capital loss of Rs. 5.49 lakh pertaining to the assessment year 1992-93 and 1993-94 was allowed. Audit scrutiny revealed that the set off of capital loss was allowed against the income under the head other than 'capital gains' in contravention of the provisions of Income-Tax Act.

(x) The assessment of a company for the assessment year 1995-96 was completed for taxable business income of Rs. 2483.51 lakh where in set off of short term capital loss amounting to Rs.52.66 lakh was allowed. Since the set off of capital loss is allowable only against the income under the head 'capital gains' the set off allowed from the profits and gains of business was incorrect.

(xi) The assessment of a co-operative society for the assessment year 1994-95 was completed, *inter alia*, allowing unabsorbed investment allowance of Rs. 137.91 lakh pertaining to the assessment year 1984-85 to be carried forward. Audit scrutiny revealed that since carry forward of such unabsorbed investment allowance losses beyond eight years was not permissible the carry forward was irregular.

(xv) The assessment of a company for A.Y. 1997-98 was completed. The assessee had claimed a loss of Rs. 3,39,41,867 under the head business. This included a loss of Rs. 3.14 crores under the head 'difference in valuation of shares'. The Audit scrutiny revealed that the explanation to sec. 73 was not applicable in assessee's case as there was no transaction in shares at all during the relevant previous year. The assessee had held the shares as investments and a fall in the market value did not represent a revenue loss. The loss claimed was disallowable as capital loss. Failure to do so resulted in potential revenue loss of Rs. 1,36,02,672/-.

#### **INTERNAL AUDIT OBJECTIONS**

##### **Incorrect Set Off Of Capital Loss**

The assessee sold the entire block of buses and incurred a loss of Rs. 3,58,890 from the sale for the Assessment year 1998-99. The loss was required to be treated as short term capital loss in accordance with the provisions of Sec. 50. Since the assessee did not have any capital gain, the entire loss arising out of sale of buses was required to be carried forward. Instead, the assessee debited the loss to the profit & loss account. In effect, the assessee the loss treated as business loss and set off the same

against business income. Omission to disallow the set off resulted in under assessment of Rs. 3,58,890 involving tax effect of Rs. 1,44,264.

In the case of a private limited company for the A.Y. 1998-99, the assessing officer while framing the asstt. allowed carried forward of loss to the extent of Rs.2.33 lac while in fact there was no loss to be carried forward as per the asstt. order of earlier year *i.e.* A.Y. 1997-98. Omission to revise the asstt. u/s 143(1)(b) of IT Act resulted in a potential tax effect of Rs. 1.08 lac.

#### CHAPTER-8

##### MISTAKE APPARENT FROM RECORD

(i) The assessment of a company for the assessment year 1995-96 was completed under limited scrutiny in December 1997 for a taxable income of Rs. 9.90 lakh after allowing set off of unabsorbed investment allowance pertaining to assessment years 1989-90 and 1990-91 aggregating Rs. 69.11 lakh. Audit scrutiny revealed that the said unabsorbed investment allowance was already set off in the A.Y. 1994-95 on the income computed after scrutiny in December, 1996. Therefore, no unabsorbed investment allowance remained to be carried forwarded.

(ii) The assessment of a company for the assessment year 1995-96 initially processed in a summary manner in March 1996 was completed after scrutiny in December 1997 determining tax demand of Rs. 187.12 lakh including refund of Rs. 34.88 lakh allowed at the summary stage. Subsequently, the assessment was revised in February 1998 to give appeal effect determining refund of Rs. 19.09 lakh which included interest of Rs. 10.55 lakh allowed under section 244A from 1-4-1995 to 31-3-1998. Audit scrutiny revealed that the interest allowable worked out to Rs. 3.64 lakh as against Rs. 10.55 lakh allowed by the department. The resulted in excess allowance of interest of Rs. 6.91 lakh.

(iii) The assessment of a company for the assement year 1995-96 initially completed under summary manner in January 1997 was completed after scrutiny in March 1998. Audit scrutiny revealed that while computing the net demand at scrutiny stage, the assessing officer omitted to withdraw the interest of Rs. 20.91 lakh.

(iv) The assessment of a company for the assessment year 1991-92 completed after scrutiny in January 1994 was revised in December 1996 determining refund of Rs. 30.82 lakh which included an amount of Rs. 8.32 lakh interest payable to the assessee for the period from April 1991 to March 1994. Audit scrutiny revealed that interest of Rs. 2.93 lakh was allowable upto 31 March 1992 as against Rs. 8.32 lakh allowed as the refund of Rs. 38.15 lakh was adjusted against the demand for the assessment year 1986-87 in March 1992 while processing the return in a summary manner. The mistake resulted in excess payment of interest of Rs. 5.39 lakh.

(v) The assessment of a widely held company for the assessment year 1990-91 originally completed after scrutiny in March 1993 was revised in June 1996 determining refund of Rs. 36.31 lakh which included interest of Rs. 12.58 lakh paid to the assessee beyond January 1992. Audit scrutiny

revealed that refund payable to the assessee was reduced to nil by way of adjustment with earlier years demands in January 1992 and no interest was due to the assessee beyond the date of adjustment. The irregular allowance led to excess payment of interest on refund to the extent of Rs. 12.58 lakh.

(vi) The assessment of an assessee company for the assessment year 1994-95 originally completed after scrutiny in March 1997 was revised in March 1997 determining the refund of Rs. 89.59 lakh which included an amount of Rs.18.42 lakh interest payable to the assessee. Audit scrutiny revealed that the assessee had defaulted in filing the Tax Deducted at Source certificates in time and therefore no interest was allowable to the assessee for the period of delay in filing the Tax Deducted at Source certificates. The interest allowable to the assessee worked out to Rs. 1.12 lakh against the amount of Rs. 18.42 lakh actually allowed.

## CHAPTER-9

### FAILURE OF MAKE DISALLOWANCE US 43-B

(i) The assessment of a company for the assessment year 1995-96 was completed at a loss of Rs. 540.42 lakh. Audit scrutiny revealed that a sum of Rs. 11.58 lakh representing provident fund contribution debited to the profit and loss account of the relevant previous year was allowed by the assessing officer though the amount was not actually paid before the stipulated due date. The same should have been added back.

(ii) The assessment of a closely held company for the assessment year 1994-95 was completed determining taxable income at Rs. 10.50 lakh after allowing a deduction of Rs. 16.77 lakh relating to assessment year 1993-94 towards payment to provident fund but paid in previous year 1994-95 relevant to assessment year 1995-96 as claimed by the assessee. Audit scrutiny revealed that deduction of Rs. 16.77 lakh which included Rs. 7.07 lakh being the balance provident fund contribution relating to assessment year 1993-94 not paid before the stipulated due date as per the Provident Fund Act, 1924, was required to be disallowed.

(iii) The assessment of a company for the assessment year 1994-95 was completed at a total loss of Rs. 123450.97 lakh. Audit scrutiny revealed that the assessee was allowed deduction for an amount of Rs. 275.99 lakh on account of "Guarantee fee" payable to Government of India. The guarantee fee was not paid by the assessee within the due date as required by section 43B. Hence it was held by audit that the same was required to be disallowed.

(iv) The assessment of a private limited company for the assessment year 1995-96 was completed at a loss of Rs. 8.27 lakh. Audit scrutiny revealed that assessee failed to pay the Employer's contribution towards Provident Fund amounting to Rs. 13.12 lakh before due date and paid the penalty of Rs. 1.01 lakh for late payment of the same. The assessee also failed to pay contributions towards gratuity fund for Rs. 1.47 lakh but the same were allowed as deduction in contravention of the provisions of the Act.

(v) The assessment of a company for the assessment year 1994-95 was completed determining the loss of Rs. 8.26 lakh as returned by the assessee. Audit scrutiny revealed that interest of Rs. 10.39 lakh payable to financial institution though not actually paid was erroneously allowed as deduction.

(vi) In case of an individual for the assessment year 1997-98, the audit Scrutiny revealed that an amount of Rs. 14.99 lakh was debited to the

Profit and Loss Account in respect of 'house-tax'. The same was not paid during the assessment year 1997-98. In the absence of any proof of payment of tax, the assessing officer should have disallowed this amount.

#### INTERNAL AUDIT OBJECTIONS

##### Omission To Apply Provisions Of Sec. 43B

(i) The assessee debited a sum of Rs. 1,54,458 to the Profit & Loss account on account of provident fund for the Assessment Year 1998-99. As per the details furnished by the assessee along with the return of income, the assessee had remitted a sum of Rs. 1,31,426 to the provident fund account belatedly as below:—

	Amount (Rs.)	Date of Payment
January, 1998	44,739	27-4-1998
February, 1998	39,032	27-4-1998
March, 1998	47,655	28-7-1998

As per sec. 36(1)(va), it is obligatory for the assessee to remit provident fund dues within 15 days from the due date. Failure to do so calls for disallowance of the deduction forever. Since the assessee remitted the amounts to the provident fund authorities belatedly, the deduction of Rs. 1,31,426 claimed by the assessee has to be disallowed permanently. Further, provident fund not at all remitted amounting to Rs. 23,032 also is liable to be disallowed. Omission to disallow PF not remitted as required under the law resulted in under assessment of Rs. 1,54,458 involving tax effect of Rs. 53,000.

(ii) In the case of limited company for the A.Y. 1997-98 the assessee made a bonus provision of Rs. 25 lac. But in the adjusted statement of total income, the assessee had claimed a sum of Rs. 249 lac on the basis of the certificate filed by the Auditor, under the provisions of Section 43B the bonus provision alone can be allowed within the extended date and the balance can be allowed in the year of payment. Audit scrutiny detected the allowance of Rs. 224 lac allowed by the assessing officer was not proper. Resultant tax effect comes to Rs. 155 lac.

(iii) In the case of a company for the A.Y. 1998-99 the Assessing Officer allowed the sales tax liability while framing the asstt. Audit scrutiny revealed that the liability same was not paid within due date and hence it was not allowable. Asstt was rectified and add. tax of Rs. 40017 was levied and recovered.



## CHAPTER-10

### INCORRECT COMPUTATION OF CAPITAL GAINS AND INCORRECT ALLOWING OF CAPITAL EXPENDITURE

(i) The assessments of a closely held company for assessment years 1993-94 and 1994-95 were completed and revised later on an income of Rs. 3979.80 lakh and Rs. 3093.47 lakh respectively. The long term capital loss of Rs. 29.29 lakh claimed by the assessee was allowed to be carried forward and set off against long term capital gains for the assessment year 1994-95. The long term capital loss of Rs. 29.29 lakh had arisen from the sale of 14,50,000 units during the previous year 1992-93 which were acquired during April 1988, May 1990 and August 1990 respectively. Audit scrutiny revealed that only the 1,00,000 units acquired in April 1988 were held for more than 36 months and were long term capital assets while the remaining units (13,50,000) acquired in May 1990 and August 1990 were held for less than 36 months and should have been treated as short term capital assets only. The net short term capital gains arising out of sale of the entire 14,50,000 units after adjusting the long term capital loss arising from the sale of 1,00,000 units was Rs. 13.87 lakh. The treatment of all the units as long term capital assets as claimed by the assessee resulted in escapement of net short term capital gains of Rs. 13.87 lakh from assessment in assessment year 1993-94 and incorrect carry forward and set off of long term capital loss of Rs. 29.29 lakh in the assessment year 1994-95.

(ii) The assessment of a company for assessment year 1994-95 was completed at a taxable income of Rs. 9.72 lakh allowing carry forward of long term capital loss of Rs. 60.85 lakh. Audit scrutiny revealed that while computing the income under capital gains, though 2,47,500 shares were held for less than 12 months, the loss on sale of the above shares was treated as long term capital loss as against short term capital loss. Further another 20,500 shares were held by the assessee as stock in trade till October 1987 and were converted into investment in November 1987. However, for computation of capital gains the first year of holding was taken as 1979 and the benefit of cost indexation was arrived by adjusting fair market value as on 1981. As the asset was converted from stock-in-trade to investment only in November 1987, the first year of holding of the capital asset should have been treated as financial year 1987-88 and capital gains computed accordingly.

(iii) The assessment of a company for the assessment year 1992-93 completed on a loss of Rs. 43.78 lakh was revised and increased to

Rs. 57.94 lakh later on. Audit scrutiny revealed that the assessee company transferred lands measuring 5.84 acres to another company on lease for sixty years and a premium of Rs. 50 lakh received was credited to capital reserve but the same was not brought to tax as capital gains.

(iv) The assessment of a company for the assessment year 1995-96 was completed. Audit scrutiny revealed that the assessee claimed and was allowed Rs. 5.00 lakh being goodwill charges paid to a proprietary concern from whom the assessee had taken over all the assets and liabilities. As the goodwill charges are of capital nature, allowance of the same was not in order.

(v) The assessments of a company for the assessment year 1992-93 and 1993-94 were completed and revised later on at an income of Rs. 32.09 lakh and Rs. 1.55 lakh respectively allowing deduction of Rs. 11.92 lakh and Rs. 27.80 lakh towards cost of replacement of discarded, old machineries used in business with the new machineries treating the same as revenue expenditure. Audit scrutiny revealed that the replacement of old and discarded machineries with new machineries would constitute a capital expenditure and hence expenditure incurred on the same for the assessment years 1992-93 and 1993-94 was required to be disallowed.

(vi) The assessment of a company for the assessment year 1993-94 was completed after scrutiny in January 1996. Audit scrutiny revealed that an amount of Rs. 20.20 lakh was allowed toward "loss on sale of shares". As the "loss on sale of shares" constituted capital loss (shares being the investments of the assessee company), the amount of Rs. 20.20 lakh was required to be added back, which was not done.

(vii) The assessments of a company for the assessment years 1991-92 to 1993-94 were completed. In computing the total income for these years, the assessee company was allowed modernisation expenditure of Rs. 101.57 lakh, Rs. 64.72 lakh and Rs. 75.77 lakh which *inter alia* included purchase of new machineries for Rs. 73.19 lakh, Rs. 57.69 lakh and Rs. 46.03 lakh respectively. As the assessee had brought new assets into existence and derived advantage of an enduring nature the expenditure should have been treated as capital and disallowed after allowance of normal depreciation.

(viii) Audit scrutiny, however, revealed that since the assessee's gross turnover from business during the relevant previous year was Rs. 16.54 lakh only her accounts did not require to be audited and the due date of filing the return thus fell on 31 August 1994. This due date had been shown by the assessee as 31 August for the assessment year prior to 1994-95 and after 1994-95. Accordingly as the sum of Rs. 136.35 lakh was deposited in the capital gain account on 28-10-94 which was beyond the

due date of submission of return, exemption of Rs. 118.82 lakh was erroneously allowed. The mistake resulted in short computation of capital gains by Rs. 118.82 lakh.

(ix) The assessment of an individual for the assessment year 1995-96 was completed after scrutiny in January 1998 accepting long term capital gains of Rs. 69.04 lakh, on account of sale of capital asset, viz. Shares, offered by the assessee after deducting Rs. 20.33 lakh being the cost of construction of new house. Audit scrutiny revealed that the assessee had constructed the house before the date of transfer of capital asset and hence the deduction allowed was not in order. The mistake resulted in underassessment of capital gain by Rs. 20.33 lakh

(x) The assessment of a registered firm for the assessment year 1994-95 was completed at income of Rs. 18.94 lakh being long term capital gain. Audit scrutiny revealed that during the previous year relevant to assessment year 1994-95 assessee had sold land and factory building for a consideration of Rs. 103 lakh on which depreciation had been claimed by the assessee for earlier years. Since the capital gain related to a depreciable asset, the capital gain should have been assessed as short term capital gain. It was noticed that the assessing officer accepting the contention of the assessee had bifurcated the value of the land and building treating sale consideration received on building as short term capital gain and that on land as long term capital gain. Since the sale was a composite sale and the bifurcation was done by the assessee to avoid computation as short term capital gains, the assessing officer should have assessed it as short term capital gain. Omission to do so resulted in underassessment of capital gain of Rs. 68.74 lakh.

#### INTERNAL AUDIT OBJECTIONS

##### Assessment under wrong head of income

The assessee had constructed flats named "Happy Home" and sold three flats therein during the year. The assessee treated the flats as capital assets and admitted capital gains on the sale proceeds as reduced by the cost thereof. The assessee also sought the benefit of indexation on the cost. The assessee admitted long term capital gain of Rs. 1,58,910, which was arrived at after indexation of the cost of the flats sold. In the assessment made under Sec. 143(3) for the Assessment year 1997-98, the assessee's claim was accepted. The assessee built the flats as a part of a business venture and the profit from the sale of flats should be treated as a part of the business carried on by the assessee. Thus, the claim made by the assessee that she had derived income from capital gains was not tenable. Omission to assess the profit under the head 'Income from Business or profession' resulted in under assessment of Rs. 3,89,932 involving tax effect of Rs. 1,24,200 for the year. The issue has implications for the other years as well.

## CHAPTER-11

### MISTAKE IN ALLOWING DEDUCTION UNDER CHAPTER VI-A

(i) The assessments of a registered firm for the assessment years 1991-92 and 1992-93 were completed at a total income of Rs. 2.46 lakh and Rs. 1.63 lakh allowing deductions under Chapter VIA aggregating Rs. 1.64 lakh and Rs. 26.06 lakh respectively. Audit scrutiny revealed that refunds of central excise duty to the tune of Rs. 18.88 lakh and Rs. 100.70 lakh received by the assessee during the relevant previous years were also taken into consideration in computing the quantum of aforesaid deductions. As the Central excise duty refunds are not income of the nature as specified in Chapter VI-A of the Act, the deductions allowed on central excise duty refunds were irregular and resulted in underassessment of income aggregating to Rs. 27.70 lakh.

(ii) In the case of the assessee having a status of a Domestic Company, wherein the assessment for the A.Y. 1996-97 was finalised determining the total income at Rs. 2993279/-. Audit scrutiny revealed that the assessee had been allowed deduction u/s 80HH on gross total income which included Rs. 4084472/- as other income derived from activities which were not incidental to an industrial undertaking. After reducing the other income from gross total income the resultant figure was negative. Therefore, no deduction u/s 80-HH was allowable to the assessee.

(iii) In the return filed for the Assessment Year 1997-98 the assessee claimed deduction under Sec. 80G on donation of Rs. 1,34,075 made to Manikchand Dhariwal Institute of Management and Rural Technology. In support of the claim, the assessee filed a certificate issued by the above Institute. The certificate stated that the assessee made the amount of donation directly to Maxim Information Technologies Pvt. Ltd. Since the assessee made the payment to a company directly and not to the Institute, which was eligible for deduction u/s 80G, the claim made by the assessee was not acceptable. In the assessment, the AO overlooked description of the payment and allowed the claim made for the deduction under sec. 80G.

(iv) The assessee made a payment of Rs. 3,00,000 to the Naval Officers Contributory Education Fund. In return filed for Assessment Year 1993-94 assessee claimed contribution as 100% deductible u/s 80 G, relying upon Notification No. 2611 dated 12.12.1978. As per the Notification, the fund was granted exemption u/s 10(23C)(iv). The Notification, however, does not state that the contributions to the Fund are eligible for 100% deduction u/s 80 G. The contributions to the Fund are, in fact, eligible for

deduction u/s 80 G only to the extent of 50%. Consequently, a sum of Rs. 1,50,000 was allowed in excess.

(v) The assessee's earnings in foreign currency from hotel business amounted to Rs. 3,13,10,986. Besides, assessee received Rs. 95,65,075 in foreign currency on account of encashment of foreign currency as RMC license holder. While claiming the deduction under sec. 80HHD, assessee included foreign exchange receipts of Rs. 95,65,075. The benefit of deduction u/s 80HHD, was available on profits derived from services provided to the foreign tourists in the business of a hotel. deduction u/s 80HHD was not available in respect of foreign exchange earning through encashment as RMC license holder. Omission to compute deduction u/s 80HHD only with reference to foreign exchange earning derived from the services provided to the foreign tourists resulted in excess allowance of deduction under sec. 80HHD by Rs. 6,45,262.

(vi) It was seen from the computation of total income that the deduction u/s 80M had been claimed and allowed at Rs. 5,29,257/-. The gross dividend received was Rs. 5,29,257/- and the provision made for proposed dividend was Rs. 6,75,000/-. The annual dividend was not on record. In the computation of total income it was stated that the dividend of Rs. 6,75,000/- was provided for distribution to the share holder of the company. As per sec. 80M, if no dividend was distributed before the due date of filing the return of income, the entire amount of dividend income received would be taxable without any deduction. As no proof of dividend having been distributed before the due date of filing the return of income was on record, *prime facie* the allowance of deduction u/s 80M of Rs. 5,29,257/- did not appear to be in order. The mistake resulted in under assessment of income of Rs. 5,29,257/-.

(vii) It was seen in audit that while computing the income the assessee was allowed 100% deduction on the gross dividends of Rs. 1,25,90,068/- u/s 80M. As the deduction was admissible on the net dividend income the deduction allowed was not in order. The expenses as estimated by the assessing officer were 20% of the income from dividends. After deducting the expenses of Rs. 25,18,012/- being 20% of the gross dividend of Rs. 1,25,90,068/-, the deduction allowed by the Deptt. u/s 80M was found to be excess by Rs. 25.18 lakhs.

#### INTERNAL AUDIT OBJECTIONS

(viii) In the case of a company has shown dividend income of Rs. 18.7 lac received from UTI and claimed deduction u/s 80M. Audit scrutiny revealed that from the A.Y. 1996-97 onward the same is not admissible. Wrong deduction resulted in revenue loss of Rs. 5.16 lac.

(ix) The assessment of a company assessee for A.Y. 1995-96 was completed u/s 143(3) in March, 1998. The assessee was operating a Hotel Business and claimed deduction u/s 80HHD of the I.T. Act at Rs. 6,30,807/-. The assessing officer allowed the same at Rs. 4,94,633/- on the

basis of certificates in form 10-CCAE actually produced by the assessee before the assessing officer.

Total receipt considered by the assessee and the assessing officer for deduction u/s 80HHD was at Rs. 26,21,335/- which consisted of

Room service & food service	Rs. 1452426
Other income	Rs. 1168909
	Rs. 2621335

It was seen from the records that other income included interest income of Rs. 10,55,125/- & dividend of Rs. 2048/-. Section 80HHD stipulated that profit of the business for the purpose of deduction u/s 80HHD would be the profits computed u/s 28 of the I.T. Act. i.e. under the heads of 'Profits & Gains of Business & Profession'. The assessing officer wrongly considered interest income and dividend for the purpose of arriving at net profit of business. The interest and dividend were chargeable to tax as income from other sources under the provision of sec. 56 of the I.T. Act. The correct deduction u/s 80HHD worked out to Rs. 1,21,608/-. There was under assessment of Rs. 373035/-.

(x) The assessment of a company assessee for A.Y. 1996-97 was completed. It was seen from the assessment order that the assessee company had claimed deduction u/s 80-O at Rs. 4126418/- as per working of the assessee company attached with the return. From the statement it was seen that net fee received was Rs. 60,17,569/- and not Rs. 8252839/- taken by the deptt. The deduction admissible u/s 80-O would therefore worked out to Rs. 3008785/- being 50% of real receipt of Rs. 60,17,569/-.

(xi) In the case of a corporate assessee scrutiny under section 143 (3) for the assessment year 1995-96 was completed allowing a claim of Rs. 6,53,129 as a deduction under section 80HHA. Audit scrutiny revealed that the assessee did not satisfy the conditions for a small scale industrial undertaking as laid out in Explanation (b) of section 80 HHA which clearly stated that for an industry to be considered as small scale for the purpose of section 80 HHA, aggregate value of the plant and machinery shall not exceed Rs. 35 lakhs as on the previous year ending. In the case of the assessee, the cost of the plant and machinery as at the end of the previous year i.e. 31-3-1995 amounted to Rs. 67,99,935, far exceeding the limits thereon. Further the area where the assessee company was situated also did not fall within the meaning of "rural area" as explained in that section:

(xii) In the case of an individual scrutiny assessment for the assessment year 1996-97 was completed on 19.9.97. Audit scrutiny revealed that in the absence of separate P&L account for the income received in foreign exchange, to claim deduction u/s 80-O, corresponding expenses should have been deducted from gross foreign receipts and net income should

have been arrived at on which the assessee would be eligible for deduction at 50%. Deduction u/s 80-O had to be allowed only on net income and not on gross receipts. The AO allowed assessee's claim u/s 80-O of Rs. 9,34,770/- on gross receipts as against allowable deduction of Rs. 5,18,782/-.

(xiii) The assessment of the company for the assessment year 1997-98 was completed after scrutiny in March 2000 after allowing deduction of Rs. 117.59 lakh towards commission received from foreign enterprises. Audit scrutiny revealed that the assessee was provided commercial information to the foreign principals regarding their import of goods of India. These foreign principals receive commission 40% from concerned airlines and subsequently share it with the assessee firm in equal proportion. The assessee was as such getting commission as cargo agent and not providing any services eligible for deduction towards commission received from foreign enterprises. The incorrect allowance of deduction resulted in under assessment of income of Rs. 117.59 lakh involving tax effect of Rs. 78.55 lakh (including interest).

#### INCORRECT DEDUCTION U/S 80G

In the return filed for the Assessment year 1997-98 the assessee claimed deduction under sec. 80G on donation of Rs. 1,34,075 made to one Institute. In support of the claim, the assessee filed a certificate issued by the above institute. The certificate states that the assessee made this amount of donation directly to Maxim Information Technologies Pvt. Ltd. Since the assessee made the payment to a company directly and not to the institute, which is eligible for deduction u/s 80G, the claim made by the assessee is not acceptable. In the assessment made under sec. 143(3), the Assessing officer overlooked the description of the payment and allowed the claim made for the deduction under sec. 80G. Erroneous allowance of the deduction resulted in under assessment of Rs. 67,038 involving tax effect of Rs. 20,111.

#### DEDUCTION U/S 80G EXCESS ALLOWED

The assessee made a payment of Rs. 3,00,000 to the Naval Officers Contributory Education Fund. In the return filed for the Assessment Year 1993-94 the assessee claimed the contribution as 100% deductible under sec. 80G, relying upon the Notification No. 2611 dated 12-12-1978. As per the Notification, the Fund was granted exemption under sec. 10(23V)(iv). The Notification, however, does not state that the contributions to the Fund are eligible for 100% deduction under sec. 80G. The contributions to the fund are, in fact, eligible for deduction under sec. 80G only to the extent of 50%. Consequently, a sum of Rs. 1,50,000 was allowed in excess as deduction under sec. 80G, involving a tax effect of Rs. 77,625.

**EXCESS DEDUCTION US 80HHD**

The assessee's earnings in foreign currency from hotel business amounted to Rs. 3,13,10,986. Besides, the assessee received Rs. 95,65,075 in foreign currency on account of encashment of foreign currency as RMC license holder. While claiming the deduction under sec. 80 HHD, the assessee included foreign exchange receipts of Rs. 95,65,075. The benefit of deduction u/s 80 HHD is available on the profits derived from the services provided to the foreign tourists in the business of a hotel. Accordingly deduction u/s 80 HHD would not be available in respect of foreign exchange earnings through encashment as RMC license holder. Omission to compute deduction u/s 80 HHD only with reference to foreign exchange earnings derived from the services provided to the foreign tourists resulted excess allowance of deduction under sec. 80 HHD by Rs. 6,42,262 involving tax effect of Rs. 2,96,820/-.



## CHAPTER-12

### MISTAKE OF SHORT LEVY/NON-LEVY/EXCESS LEVY OF INTEREST

(i) The assessment of a Co-operative Society for the assessment year 1993-94 was completed. Audit scrutiny revealed that interest for short payment of advance tax was erroneously levied at Rs. 884.14 lakh instead of the correct amount of Rs. 909.71 lakh.

(ii) The assessment of an HUF for the assessment year 1995-96 was completed at a total income of Rs. 1701.84 lakh. Audit scrutiny revealed that the assessee company paid a sum of Rs. 4.85 lakh by way of advance tax. Since the advance tax paid fell short of ninety percent of the assessed tax, the assessee company was liable to pay interest of Rs. 472.93 lakh as against Rs. 356.45 lakh actually levied by the assessing officer.

(iii) The assessments of a firm for the assessment years 1989-90 and 1990-91, originally completed in December 1989 and January, 1991 respectively, were revised in March, 1998. Audit scrutiny revealed that although total income had been substantially increased and tax was also increased accordingly, the interest for short payment of advance tax levied earlier was not enhanced as required under the provision of the Act.

(iv) The assessment of an assessee 'firm' for the assessment year 1995-96 was completed at a taxable income of Rs. 69.63 lakh. Audit scrutiny revealed that while computing the tax demand, self assessment tax was adjusted directly against the tax demand instead of first adjusting the interest payable and then adjusting the balance of self assessment tax paid toward tax payable. The mistake resulted in short levy of interest for short payment of advance tax of Rs. 7.31 lakh.

(v) The assessments of an association of persons for the assessment years 1992-93, 1993-94 and 1994-95 originally processed in a summary manner were subsequently completed after scrutiny. Audit scrutiny revealed that the total demands of Rs. 46.32 lakh, Rs. 124.47 lakh and Rs. 19.76 lakh for the assessment years 1992-93 to 1994-95 respectively were paid on various dates after the due dates specified in the demand notices. As the demands were not paid within the permissible period from the date of service of demand notices, the assessee was liable to pay interest on the entire defaulted amounts for the period of default. However assessing officer levied interest for default in payment of original demands only in respect of assessment year 1992-93 and 1993-94,

omitting to levy interest for the defaulted additional demands for those years and for entire defaulted demands for assessment year 1994-95.

(vi) The assessment of a partnership firm for the assessment years 1993-94 and 1994-95 were completed under section 147/144 in March 1998 determining total income at Rs. 9.79 lakh and Rs. 7.09 lakh respectively. Audit scrutiny revealed that no surcharge was levied and interest for delay in filing of return and non payment of advance tax aggregating to Rs. 3.66 lakh was short levied for both the assessment years.

(vii) The assessments of an individual for the assessment years 1987-88 and 1988-89 were completed after scrutiny in March 1998 levying interest for non payment of advance tax by Rs. 0.84 lakh and Rs. 10.00 lakh respectively. Audit scrutiny revealed that the regular assessments of the assessee individual for the assessment years 1987-88 and 1988-89 completed in December 1991 were set aside by the Commissioner of Income-Tax (Appeals) in May 1992. The assessments for both the assessment years completed afresh in March 1995 were also set aside in September 1995. The Assessing Officer while completing assessments in March 1998 erroneously levied interest upto the date of latest assessments *i.e.* March 1998 instead of December 1991 *i.e.* upto the date of regular assessment.

(viii) The assessment of an individual assessee for the assessment year 1995-96 was completed on best judgement basis. Audit scrutiny revealed that even though the income considered for computation of tax was "Income from other sources" only, the due date for filing the return was taken as 30 August 1995. As there was no income from "Business or Profession" and the accounts was not to be got audited, the due date for filing the return should have been taken as 30 June 1995. The assessee was therefore, liable to pay interest of Rs. 26.85 lakh for the period from 1st July 1995 to 30 August 1995. The mistake resulted in short levy of interest of Rs. 26.85 lakh.

(ix) The assessments of an individual for the assessment years 1990-91, 1992-93 and 1993-94 were completed. Audit scrutiny revealed that the assessee had not filed returns of income for these years though notices were issued to him. The assessee was, therefore, liable to pay interest of Rs. 9.61 lakh, Rs. 71.24 and Rs. 27.94 lakh respectively for default in furnishing the return of income in time as against the interest of Rs. 7.76 lakh, Rs. 56.09 lakh and Rs. 9.25 lakh levied by the department.

(x) The assessments of an individual for the assessment years from 1990-91 to 1993-94 were completed in March 1996 on best judgement assessment basis. Audit scrutiny revealed that the assessing officer had levied the interest for non filing the returns from the date immediately

following the period allowed by notice under section 148 to the date of regular assessment instead of charging the interest from the date immediately following the due date of furnishing of return to the date of regular assessment. The mistake resulted in short levy of interest aggregating Rs. 45.93 lakh.

(xi) The assessment of a company for A.Y. 1992-93 was completed u/s 143(3)/147. The Audit scrutiny revealed that the interest u/s 234B on the difference of income originally assessed u/s 143(3) and the income quantified in the order passed under section 143(3) read with section 147 was not charged by the A.O. This resulted in under charge of interest u/s 234B to the tune of Rs. 14,90,540/-.

(xii) The assessment of a company for assessment year 1995-96 was completed after scrutiny in November 1997. Audit scrutiny revealed that the income tax assessments for the assessment year 1993-94 and 1994-95 were completed in March 1996 and March 1997 respectively and the Wealth tax assessments for the assessment year 1989-90 and 1992-93 were completed in March 1990 and March 1995 respectively. The total demand was raised for above assessments at Rs. 105.29 lakh and notices were served upon the assessee between March 1990 and March 1997. The entire demand of Rs. 105.29 lakh was adjusted against the refunds for the assessment year 1995-96 and 1996-97 in October 1997 and December 1997 respectively. As the demand was paid after the permissible period of 30 days from the date of service of demand notice, the company was liable to pay interest of Rs. 13.02 lakh which was not levied by the department.

(xiii) The assessment of a company for the assessment year 1995-96 was completed after scrutiny in March 1998 at a total income of Rs. 109.47 lakh determining tax at Rs. 55.80 lakh including the additional tax of Rs. 5.62 lakh. Audit scrutiny revealed that the assessee had paid a sum of Rs. 0.18 lakh only by way of tax deducted at source. Since the assessee did not pay any advance tax the assessee was liable to pay interest of Rs. 36.26 lakh at the rate of two percent for 36 months from 1 April 1995 to 31 March 1998 as against Rs. 11.04 lakh actually levied by the department.

#### **INTERNAL AUDIT OBJECTIONS**

##### **Failure to levy interest U/S 158BFA(1)(a)**

In response to notice u/s 158BC dated 30-3-1998, which was served on the assessee on 21-4-1998, the assessee filed the return of income for the block on 13-7-1999. In the assessment made the undisclosed income of the assessee stood determined at Rs. 34,79,967. The assessee was obliged to file the return of income for the block in Form No. 2B within 30 days from the date of receipt of notice. The return, therefore, was due by 21-5-1998. Since the assessee filed the return only on 13-7-1999, interest u/s 158BFA (1)(a) is leviable from 21-5-1998 to 13-7-1999 @ 2% of the tax on undisclosed income. Interest chargeable worked out to

Rs. 6,26,400. Omission to levy interest for filing the return belatedly resulted in short levy of tax by 6,26,400.

**SHORT LEVY OF INTEREST U/S 234C**

In the return filed for the Assessment Year 1997-98, the assessee calculated interest payable under sec. 234C at Rs. 4,80,030. In the assessment order under sec. 143(3) interest under sec. 234C has been computed at Rs. 3,90,030 whereas the correct interest chargeable works out Rs. 4,80,031, as has been correctly computed by the assessee in the return filed. The mistake of short computation of interest under sec. 234C arose on assuming that the assessee paid Rs. 135 lacs up to the instalment due on 15-9-1996 as against the correct amount of Rs. 115 lacs paid by that date. Interest under sec. 234C short computed works out to Rs. 90,000.

## CHAPTER-13

### INCORRECT VALUATION OF CLOSING STOCK

(i) The assessment of a firm for the assessment year 1994-95 was completed after scrutiny in October 1996. Audit scrutiny revealed that the aggregate value of stock as on 31.3.94 as per books of accounts was Rs. 26.90 lakh whereas the assessee had depicted a liability of Rs. 45.84 lakh as secured loan from a nationalised bank against hypothecation of stock in the balance sheet. In the absence of amount of declared stock to bank the difference in liability and closing stock, *i.e.* Rs. 18.94 lakh was required to be added back to the income of the assessee firm.

(ii) The assessment of a registered firm, exporter of polished diamonds, for the assessment year 1990-91 was completed after scrutiny in March 1993. Audit scrutiny revealed that the assessee had closed business on 31st December 1989 and declared closing stock of finished polished diamonds of 1017.06 carats the value of which was given as Rs. 62.94 lakh. It was further revealed that assessee had sold diamonds in December 1989 at the rate of Rs. 6800 per carat. As the firm had closed down the business, valuation of the closing stock was required to be done at market price to ascertain the true profit. Based on the sale price at Rs. 6800/- per carat as disclosed in the accounts, the value of closing stock would work out to Rs. 69.16 lakh as against Rs. 62.94 lakh valued by the assessee.

(iii) The assessment of a firm for the assessment year 1994-95 was completed after scrutiny in March 1997. Audit scrutiny revealed that firm was dissolved on 30 June, 1993 and the shares held by the firm were distributed among the two partners. It was further noticed that profit arising out of the distribution of shares held by the firm at the time of dissolution of the firm was assessed to tax under the head Capital gains which was worked out to Rs. 7.97 lakh. However as the assessee was a dealer in shares and the shares held by the assessee at the time of dissolution represented its stock-in-trade the closing stock should have been valued at market rate. By adopting the value of closing stock at market rate (Rs. 54.16 lakh), the profits on it would work out to Rs. 29.25 lakh after allowing interest on loan and other charges amounting to Rs. 1.19 lakh.

(iv) The Assessment of a company assessee for A.Y. 1997-98 was completed after scrutiny. The Audit scrutiny revealed that the assessee had disclosed opening stock of the Accessories & Spare Parts at Rs. 46.12 lakhs; purchases during the year at Rs 215.15 lakhs and sales at Rs. 156.43 lakhs. The assessee had shown closing stock under this category at

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Rs. 59.69 lakhs. Even assuming that the assessee had sold accessory and spare parts on cost to cost basis the closing stock should have been disclosed at Rs. 104.83 lakhs. Thus there was under valuation of closing stock to the tune of Rs. 45.14 lakhs with consequent tax effect of Rs. 18,05,706.

## CHAPTER-14

### INCORRECT ALLOWANCE OF DEDUCTION/ EXEMPTION/LIABILITY/PROVISION

(i) In the case of an assessee co-operative society engaged in marketing of agriculture produce, the assessment for assessment year 1993-94 was completed. Audit scrutiny revealed that the amount of Rs. 24.68 lakh being interest income from traders and depositors not wholly attributable to the co-operative venture was erroneously considered as exempt.

(ii) The assessments of a co-operative society for the assessment years 1990-91 and 1991-92 were completed. Audit scrutiny revealed that the entire receipts on account of auctions for cardamon sales credited to the profit and loss account was allowed as deduction instead of restricting it to the income included in the gross total income after taking into account the expenses incurred in connection with such auctions. It was also noticed that in order to work out deduction in respect of transaction with members, the percentage was worked out on the basis of sales turnover only ignoring other element like trade income and sales tax collected. The aforesaid mistakes resulted in underassessment of income of Rs.10.80 lakh in aggregate.

(iii) The assessment of an individual, a Development Officer of Life Insurance Corporation, for the assessment year 1992-93 was completed, and rectified to give appeal effect in February 1994 determining the total income at Rs. 8.41 lakh. Audit scrutiny of the assessment record, however, revealed that additional conveyance allowance amounting to Rs. 7.12 lakh was allowed as deduction, although in the certificate of tax deduction at source, the employer had not certified to the effect that the additional allowance had been utilized in full for the purpose it had been paid for. As such without valid certified from the employer, the deduction was allowed in contravention of the provision of the Act.

(iv) The assessment of a registered firm for the assessment year 1992-93 was completed allowing a deduction of Rs.26.95 lakh, being fifty percent of aggregate of sums of donations amounting to Rs. 53.90 lakh. Audit scrutiny revealed that as the gross total income of the assessee was Rs. 311.30 lakh, the aggregate of sums of donations was required to be restricted to Rs. 31.13 lakh. Thus, the assessee was entitled to deduction of Rs. 15.57 lakh being 50 percent of Rs. 31.13 lakh.

(v) The assessment of an individual for the assessment year 1993-94 was completed. While assessing the income from business a sum of Rs.14.86 lakh

being the revalued cost of the shuttering plates constructed as unserviceable and written off and debited to the profit and loss account was works expenditure under concrete structure had been allowed. Audit scrutiny revealed that the assessee was claiming depreciation on shuttering plates at normal rates upto assessment year 1992-93. Since the asset was charged to capital account its removal therefrom will only reduce the value of the fixed asset and will not constitute revenue expenditure. It was, therefore, not a proper charge on profit and loss account and was liable.

(vi) The assessment of a widely held company for the assessment year 1993-94 was completed. Audit scrutiny revealed that the assessing officer allowed deduction of Rs. 22.60 lakh and Rs. 27,455 being provisions for doubtful debts and doubtful advances respectively while completing the assessment. As the amounts debited in the accounts represented mere provisions and were not accrued or ascertained liabilities they should have been disallowed.

(vii) The assessments of a widely held company for the assessment years 1991-92 and 1992-93 were completed. Audit scrutiny revealed that the assessing officer allowed expenditure of Rs. 22.17 lakh and Rs. 21.15 lakh respectively on account of provisions for insurance premium on Marine Insurance Policy which were merely made on estimated basis. As the rate of premium was not finalised as well as premium were not paid within the relevant financial years, the same being mere provisions and not ascertained liabilities were not allowable and should have been disallowed.

(viii) In the case of an assessee who was assessed in the status of firm, the assessment was completed on total income of Rs. 47,67,064. While computing the total income the assessee claimed deduction of expenditure on scientific research u/s 35(1)(ii) amounting to Rs. 3,21,000/- which included payment of Rs. 3 lakhs to Gujarat Cancer Society, Ahmedabad. The audit found that the payment of Rs. 3 lakhs to said society was made by assessee through a cheque but copy of bank account which was on record revealed that assessee had no balance to honour the cheque issued. Further, the bank reconciliation statement was available on record which indicated that the cheque was shown as outstanding at the end of the year as not presented by Gujarat Cancer Society. The audit observed that the assessee had no funds to donate Rs. 3 lakhs but in collusion with Gujarat Cancer Society issued cheque for Rs. 3 lakhs towards donation and the said society acting under conclusion with the assessee never deposited the cheque for encashment. The entire exercise of assessee and Gujarat Cancer Society was a design to defraud revenue. Failure on part

of Assessing Officer to disallow deduction of Rs. 3 lakhs u/s 35(1)(ii) being non genuine payment resulted in under assessment of income by Rs. 3 lakhs and short levy of tax alone was worked out at Rs.1,20,000/-.

(ix) In the return for the Assessment Year 1997-98, the assessee claimed a contribution of Rs. 20 lacs made to Sanjeevani Medical Foundation as deduction under Sec. 35AC. The return did not contain any evidence in support of the contribution. Deduction under Sec. 35AC was admissible only if the assessee furnished the certificate in Form No.58A from the recipient institution along with the return of income. Since the assessee failed to comply with the statutory requirement, the claim of deduction was inadmissible. While completing the assessment under Sec. 143(3), the Assessing Officer overlooked the statutory requirement and allowed the claim made by the assessee. Omission to disallow the claim resulted in erroneous allowance of deduction under sec. 35AC amounting to Rs.20 lacs involving tax effect of Rs. 8,60,000/-.

(x) For the Assessment Year 1998-99, the assessee debited to the profit & loss account a sum of Rs. 1,50,000 described as "secret commission." This debit was in addition to the sales commission of Rs.15,79,200. Payment of secret commission by its very nature could not be supported by evidence nor could it be justified as paid for the purposes of business. The Bombay High Court in *Cit Vs. Woodless Nerolac Paints Ltd.* (Tax pert 534 of 1990) had held that secret commission was not admissible as deduction. Consequently, the claim for deduction was liable to be disallowed.

(xi) In case of a company for A.Y. 1998-99 the audit scrutiny revealed that A.O. had failed to add the provision for penalty of Rs. 74,50,000 which as per Explanation 2 to Sec. 37(1) was not an allowable expenditure. The omission resulted in under assessment of income of Rs. 74,50,000.

(xii) The assessment of a company assessee for A.Y. 1996-97 was completed after scrutiny. The assessee was in the business of export of software and provision of technical and professional services abroad. Upto the assessment year 1995-96 the assessee had claimed deduction u/s 80HHC. But, the Assessing Officer had allowed deduction u/s 80HHE since a specific provision would override the general provision. For A.Y. 1996-97 the Assessing Officer made a deduction and allowed the entire income u/s 10B. The Audit scrutiny revealed that the Assessing Officer failed to note that the assessee had not filed a declaration u/s 10(B5) and 10(B7). Such a declaration was required to be filed within the time limit given u/s 139(1). The second revised return claiming entire income exempt u/s 10B was filed on 13.1.1998, i.e. much beyond the time allowed u/s 139(1). In the absence of the declaration it was to be noted that the assessee had no intention to claim exemption u/s 10B. Besides, it was also seen that the profit of the undertaking included domestic income of Rs.7.1 crores and by purchase and sale of hardware to the extent of Rs. 19.27



crores. The assessee had also spent substantial amount no provision of foreign currency for technical services and deduction u/s 80O was separately allowed. Thus on merit also exemption u/s 10 B should not have been allowed since the total income included domestic income and income from trading and technical services. The mistake resulted in under-assessment of income with consequent non-levy of tax of Rs. 8,56,57,524 including interest.

(xiii) Assessee company in its return had claimed deduction of Rs. 3,87,21,524/- u/s 35 of I.T. Act being R&D expenditure which included Rs. 32,37,500/- being interest 18.5% for 6 months capitalized on fund of Rs. 3.50 crores used for R&D. During Scrutiny, the assessing officer had disallowed claim of Rs. 1,93,08,166/- as the assessee had failed to establish the genuineness of the expenditure and allowed only Rs. 1,84,13,358/- which included interest of Rs. 32,37,500/-. As the assessee company had failed to establish the genuineness of R&D expenditure of Rs. 1,93,08,166/- proportionate interest also should have been disallowed. Failure to do so had resulted in under assessment of Rs.17,86,005/- (i.e. 18.5% of Rs. 1,93,08,166/- for 6 months) leading to short levy of tax of Rs. 14,78,812/- including interest u/s 234 A&B.

(xiv) The assessee company belonged to a group of companies and during the year took over the financial obligation of payments of lease rentals on due date from 3 lessees who had taken 100% depreciable assets on lease from three lessors belonging to the same group of companies. In consideration of this, the assessee had received non refundable deposit without interest. The assessee had debited Rs.27,31,837/- being lease rentals. Audit scrutiny revealed that lease transactions of lessors had been investigated and it proved that lease transactions were not genuine in nature. Subsequently, two lessors had withdrawn the 100% depreciation claimed in respect of their lease transactions and declared the amount under VDIS 1997. Further in respect of the third lessor the block assessment for the period 1985-86 to 1995-96 and from 1.4.96 to 18.7.96 was completed u/s 158-BC on 31.7.97 and it was seen from the order that the assessing officer had held entire transaction with the lessee not genuine in nature.

It was clear from above that the assessee company had entered into tripartite agreement to avoid the tax liability as such allowance of write off of lease rentals of Rs. 27,31,837/- was not in order. This had resulted in under assessment of income of Rs. 27,31,837/- and short levy of tax of Rs. 21,61,429/- including interest u/s 234B.

(xv) During the previous year relevant to A.Y. 1995-96 the assessee's business income on hire charges of barge was Rs. 2,22,47,174/- (Rs. 2.23 crores). There was no other activity of the assessee during the year. After certain addition the Gross income for A.Y. 1995-96 worked out to Rs. 21,89,490/- and after allowing deduction u/s 33AC of the Act the

taxable income was brought to Rs. Nil. As per provision of Sec. 33 AC as applicable for A.Y. 1995-96, in case of an assessee being a Govt. Co. or Public Company formed and registered in India with main object of carrying on business of operation of ships, there shall in accordance with and subject to provisions of this section be allowed a deduction as is debited to P&L A/c. subject to certain conditions. The deduction u/s 33 AC was admissible for carrying on business of operation of ships only. The plain meaning of operation of ships means large sea going vessel one with bar spirit and three or more mass. Whereas barges means flat bottomed freight boat, House boat. The barges are mainly used for loading and unloading of ships between ports and mid-sea. The barges are not treated as ships also as per Appendix-I of Income-tax Rules 1962. The entire receipts of Rs. 2.23 Crores was from operation of barges and not from operation of ships. As such the deduction amounting to Rs. 21,89,490/- u/s 33AC was irregular and resulted in under assessment of income of Rs. 21,89,490/- and short levy of tax of Rs. 17,00,600/- inclusive of interest u/s 234 B&C.

(xvi) Audit scrutiny of a company's assessment for the assessment year 1996-97 revealed that the assessee had incurred an expenditure of Rs.1,66,43,614/- on a property held on lease by the assessee and the same was claimed as revenue expenses. As per Explanation 1 to section 32, any such capital expenses incurred even if it were on a leasehold property, the assessee was eligible to claim only depreciation. The mistake resulted in under assessment of income of Rs.1,49,79,253/-.

#### INTERNAL AUDIT OBJECTIONS

##### Omission to apply provisions of Sec. 44AD

As per Sec. 44AD, the income of a civil contractor has to be assessed at 8% of the gross receipts if the accounts of the assessee have not been audited and a report under sec. 44AB has not been furnished along with the return of income. For the Assessment year 1998-99, the assessee-firm, a civil contractor, accounted for gross receipts of Rs.18,25,800/-. The accounts of the assessee were not audited and report u/s 44AB was not furnished as required u/s 44AD. Yet the return filed by the firm was accepted u/s 143(1) although the income shown was less than 8% of the gross receipts. Omission to assess the firm under sec. 143(3) by adopting the income of the assessee at 8% of the gross receipts, as provided for under sec. 44AD resulted in under assessment of income by Rs. 1,14,820/- involving tax effect of Rs. 45,928/-.

##### DEDUCTION US 35AC WRONGLY ALLOWED

In the return for the Assessment year 1997-98, the assessee claimed a contribution of Rs.20 lacs made to Sanjeevani Medical Foundation as deduction under sec. 35AC. The return did not contain any evidence in support of the contribution. Deduction under sec. 35AC is admissible only if the assessee furnishes the certificate in Form No.58A from th

recipient institution alongwith the return of income. Since the assessee failed to comply with the statutory requirement, the claim of deduction is inadmissible. While completing the assessment under sec. 143(3), the Assessing Officer overlooked the statutory requirement and allowed the claim made by the assessee. Omission to disallow the claim resulted in erroneous allowance of deduction under sec. 35AC amounting to Rs. 20 lacs involving tax effect of Rs. 8,60,000.

#### INCORRECT ALLOWANCE OF EXPENDITURE

The assessee is a builder. For the Assessment year 1997-98, the assessee accounted for sale of flats at Rs. 2,04,10,317. The cost of construction of the flats sold as per schedule B-5 of the annual accounts is Rs. 93,36,563. Consequently, the profit of the assessee for the year should be Rs. 1,10,73,754. As against this profit, the assessee accounted for a profit of Rs. 78,43,580 only. The difference was on account of the fact that the assessee debited interest entirely to the profit & loss account. The Auditor in the report u/s 44AB has pointed out this as the reason for the profit being lower by Rs. 32,30,174 for the year. The assessee follows completed contract method of accounting. While following this method, the assessee has to account for interest as a part of cost of construction and include the same in the work in progress. Debiting interest to the profit & loss account in entirety for the year is at variance with the method of accounting followed by the assessee and cannot be accepted. Under assessment on account of this is Rs. 32,30,174.

In the case of a registered firm while framing assets the assessing officer allowed deduction u/s 40(b)(v) being remuneration to the partners violating Board's circular No. 739 dated 25-3-96 for the Asstt. years 1997-98 & 1998-99 which resulted in the short levy of tax of Rs. 1.46 lac and 1.05 lac respectively.

## CHAPTER-15

### OMISSION TO INITIATE AND LEVY PENALTY

(i) The assessments of a firm for the assessment years 1989-90 to 1992-93 were completed. Audit scrutiny revealed that the assessee accepted loan/deposits of Rs. 3.42 lakh in cash and made repayments of deposits of Rs. 3.17 lakh in cash. Therefore, the assessee was liable to pay penalty of Rs. 6.59 lakh.

(ii) The assessment of an assessee Association of persons for the assessment year 1992-93 was completed after scrutiny in March 1994. Audit scrutiny revealed that the assessee had accepted/repaid deposits aggregating Rs. 3 lakh in cash. The department did not levy penalty nor were any reasons recorded for not doing so. The omission resulted in non-levy of penalty of Rs. 5 lakh.

(iii) In the case of an assessee assessment was completed u/s 143 (1)(a) on total income of Rs. 2,05,210 in the status of firm. The assessee earned gross interest of Rs. 1,85,10,487 from a company. However, net amount of interest amounting to Rs. 3,08,461 only was transferred to P & L A/c. This indicated that assessee also paid interest on funds borrowed. The magnitude of loans raised by assessee from private parties was Rs. 15,65,24,037. This also indicated that net surplus of interest account was assessable as business receipt and not income from other Sources. The assessee by showing net surplus of interest account as other income escaped his liability to get his accounts audited u/s 44AB and also escaped levy of penalty u/s 271B. The quantum of penalty leviable was worked out at Rs. 1 lakh.

(iv) In the case of an individual for the A.Y. 1992-93 the assessment consequent to revision u/s 263 was completed by the A.O. on 25-2-99 bringing to tax an amount of Rs. 22,82,000 as unexplained cash credit. However no penalty u/s 271(1)(c) was initiated. Failure to initiate penalty proceedings u/s 271(1)(c) resulted in short/non-levy of penalty of Rs. 10 lakhs.

(v) In the case of a company for the A.Y. 1997-98 the return of income was filed without the Audited report u/s 44AB of the I.T.Act. No. penalty was initiated u/s 271B by the A.O. Failure to do so resulted in non-levy of penalty of Rs. 1 lakh.

(vi) In the case of an individual return of income was filed for the assessment year 1996-97 declaring total loss of Rs. 10,42,567. As per Annexure-I to tax audit report, Rs. 2,60,710 was repaid in cash in

contravention of section 269 TT. The assessee was liable to penalty under section 271E and the penalty leviable worked out to Rs. 2,60,710. A.O. failed to initiate penalty proceedings u/s 271E.

#### INTERNAL AUDIT OBJECTIONS

(vii) In a case of a private limited company for the A.Y. 1999-2000 the Audit Report submitted with the return by the assessee revealed that assessee had received Rs. 50,000 as loan in cash and also repaid the loans to various parties in cash amounting to Rs. 12.40 lac, thus contravening the provisions of section 269SS & 260TT respectively. Audit scrutiny made revealed that Assessing Officer has omitted to initiate penalty proceedings u/s 271 D & 271E. The omission resulted in the revenue loss of Rs. 12.90 lac.

(viii) In the case of an assessee for the A.Y. 1997-98 gross receipts have been reflected in the return of income at Rs. 3 crore. No audit of accounts as required u/s 44AB has been got made by an accountant before the specified date and no such Audit Report has been enclosed with the return too. Audit scrutiny revealed that assessing officer failed to detect this mistake. Failure to do so resulted in revenue loss of Rs. one lac on account of no initiating of penalty u/s 271B.

(ix) In the case of a company for the A.Y. 1996-97 it was noticed that assessee has not filed Audit report u/s 44AB within due date and penalty was also not levied. After the audit scrutiny the mistake was rectified and penalty of Rs. 74,992 levied u/s 271B.

## CHAPTER-16

### IRREGULAR GRANT OF CREDIT OF TAX DEDUCTED AT SOURCE

(i) The assessment of an association of persons for the assessment year 1995-96 was completed after scrutiny in March 1998. Audit scrutiny revealed that while determining the quantum of tax payable, credit was allowed for a sum of Rs. 5,58 lakh towards tax deducted at source from rent amounting to Rs. 27.25 lakh, out of which only Rs. 9.39 lakh was offered for tax. The remaining amount of rental income was offered for taxation in the succeeding assessment year. Thus the grant of credit in respect of tax deducted at source from rent which was not offered for taxation was irregular. The mistake resulted in excess carry forward of loss by Rs. 1.35 lakh involving potential tax effect of Rs. 0.29 lakh and under assessment of income by Rs. 16.51 lakh involving short levy of tax of Rs. 7.64 lakh (including interest).

(ii) The assessment of a firm engaged in the contract work for the assessment year 1996-97 was completed in a summary manner in January 1997 at a taxable income of Rs. 13.28 lakh, as returned by the assessee. The assessee was following mercantile system of accounting. Audit scrutiny revealed that an amount of Rs. 325 lakh on which TDS credit of Rs. 7.48 lakh was given to the assessee was not appearing in the profit and loss account but the same was shown as advances against contract receipt. As the advances against contract receipt were not income of the assessee for the assessment year, TDS credit given on the same by the department was not in order. As the mistake was apparent from the records, the assessing officers should not have granted TDS credit claimed by the assessee. Failure to make the *prima facie* adjustment resulted in excess credit of TDS of Rs. 7.48 lakh with consequent short levy of tax of Rs. 8.97 lakh including additional tax.

## CHAPTER-17

### MISTAKES IN COMPUTING CONCEALED INCOME u/s 158 BC/158 BD I.E. ASSESSMENT OF SEARCH 7 & SEIZURE CASES

(i) In the block assessment comprising the Assessment Years 1988-89 to 1998-99 made on 26.07.1999, the Assessing Officer reduced from the undisclosed income a sum of Rs. 4,76,677 being salary and income from house property for various years, although the assessee had not filed the returns of income for the respective years. Since the assessee had not filed the returns at all, the income for the years was required to be reckoned as undisclosed income of the block period. Omission to tax salary and house property income as undisclosed income resulted in under assessment of Rs. 4,76,6787 involving tax effect of Rs. 2,86,006.

(ii) In response to notice u/s 158BC dated 30.03.1998, which was served on the assessee on 21.04.1998, the assessee filed the return of income for the block on 13.07.1999. In the assessment made the undisclosed income of the assessee stood determined at Rs. 34,79,967. The assessee was obliged to file the return of income for the block in Form No. 2B within 30 days from the date of receipt of notice. The return, therefore, was due by 21.05.1998. Since the assessee filed the return only on 13.07.1999, interest u/s 158BFA(1)(a) was leviable from 21.05.1998 to 13.07.1999 @ 2% of the tax on undisclosed income. Interest chargeable worked out to Rs. 6,26,400. Omission to levy interest for filing the return belatedly resulted in short levy of tax by Rs. 6,26,400.

(iii) The assessee had assessable income of Rs. 31,400 and Rs. 1,74,100 respectively for the Assessment Years 1992-93 and 1997-98. The assessee, however, had not filed the returns of income for these years. During the Block Assessment proceedings, the assessee submitted copies of Form No. 24 which his employer had filed under Sec. 206C for the Assessment Years 1992-93 and 1997-98 and claimed that since the employer had submitted the returns before the date of search, the incomes for those years had to be treated as disclosed. The Assessing Officer accepted the explanation. In as much as the returns filed by the assessee's employers u/s 206C were not the same as the returns which the assessee was obliged to file in his individual capacity enabling reduction of the incomes from the block income, the Assessing Officer erred in excluding the incomes for the Assessment Years 1992-93 and 1997-98 aggregating to Rs. 2,15,500 from the undisclosed income. The mistake resulted in under assessment of block income of Rs. 2,15,500 involving tax effect of Rs. 1,29,300 and short levy of interest under Sec. 158 BFA (1)(a) of Rs. 36,204.

(iv) In the case of a firm the block assessment under section 158BC was completed on 23-3-1998 computing the total undisclosed income at Rs. 8,72,794. The audit scrutiny revealed that the assessee had declared an amount of Rs. 22,63,097 as undisclosed income on account of cessation of liabilities during the course of search. As per the details in part II of the return in Form No. 2B, the assessee had set off losses of Rs. 13,90,303 against the total undisclosed income of Rs. 22,63,097 arriving at the figure of Rs. 8,72,794. This mode of computation of the assessee was accepted by the Assessing Officer in his order cited supra. No. such losses are to be allowed against the undisclosed income as per the clear provisions of section 158BB. The mistake resulted in under assessment of the concealed income with consequent short levy of tax of Rs. 8,34,180.

(v) In the case of a company the assessment under section 158BC was completed on 27-6-1997 determining the total undisclosed income at Rs. 58,83,882. In computing the above income, the assessing officer had taken into account the total income of Rs. 7,25,236 declared for the assessment year 1993-94. The Audit scrutiny revealed that the return for the assessment year 1993-94 declaring a total income Rs. 7,25,236 was filed beyond the due date. Therefore the total income declared for the assessment year 1993-94 was to be treated as NIL for the purpose of computation of undisclosed income under section 158BB. The mistake resulted in short levy of tax of Rs. 4,67,776.

#### **INTERNAL AUDIT OBJECTIONS**

##### **Mistake in Computation of Undisclosed Income**

In the block assessment comprising the Assessment Years 1988-89 to 1998-99 made on 26-7-1999, the Assessing Officer reduced from the undisclosed income a sum of Rs. 4,76,677 being salary and income from house property for various years, although the assessee had not filed the returns of income for the respective years. Since the assessee had not filed the returns at all, the income for the years was required to be reckoned as undisclosed income of the block period. Omission to tax salary and house property income as undisclosed income resulted in under assessment of Rs. 4,76,677 involving tax effect of Rs. 2,86,006.

##### **INCORRECT DETERMINATION OF UNDISCLOSED INCOME**

While computing the undisclosed income for the block period, allowance is made for the income already assessed or income disclosed in the returns filed by the due date. The assessee had assessable income of Rs. 31,400 and Rs. 1,74,100 respectively for the Assessment Years 1992-93 and 1997-98. The assessee, however, had not filed the returns of income for these years. While making the block assessments the Assessing Officer inquired from the assessee as to why the incomes for the Assessment Years 1992-93 and 1997-98 should not be treated as undisclosed income without



reducing the same from the undisclosed income in view of the fact that the returns for these years were not filed. In response to his inquiry, the assessee submitted copies of Form No. 24 which his employer had filed under sec. 206C for the Assessment Years 1992-93 and 1997-98 and claimed that since the employer had submitted the returns u/s 206C before the date of search, the incomes for these years have to be treated as disclosed. The Assessing Officer accepted the explanation. In as much as the returns filed by the assessee's employer u/s 206C are not the same as the returns which the assessee was obliged to file in his individual capacity enabling reduction of the incomes from the block income, the Assessing officer erred in excluding the incomes for the Assessment Years 1992-93 and 1997-98 aggregating to Rs. 2,15,500 from the undisclosed income. The mistake resulted in under assessment of block income of Rs. 2,15,500 involving tax effect of Rs. 1,29,300 and short levy of interest under sec. 158BFA (1)(a) of Rs. 36,204.

## CHAPTER-18

### 2.5 INCORRECT ALLOWANCE OF BAD DEBTS/DOUBTFUL DEBTS

(i) The assessment of a banking company for the assessment year 1995-96 was completed after scrutiny in March 1998 allowing a deduction of Rs. 95.60 lakh in respect of bad debts written off. Audit scrutiny revealed that a provision for Rs. 40.63 lakh was made on account of bad debts in the assessment year 1994-95. Under the provisions of the Income Tax Act, 1961, allowable deduction on account of bad debts written off in assessment year 1995-96 was to be limited to Rs. 54.97 lakh instead of Rs. 95.60 lakh.

(ii) The assessments of a banking company for the assessment years 1987-88, 1988-89 and 1989-90 originally completed after scrutiny in January 1988, July 1989 and December 1991 were revised in March 1997 allowing deductions of Rs. 59.59 lakh, Rs. 119.73 lakh and Rs. 147.33 lakh respectively towards provision for bad and doubtful debts. The assessee was also eligible for deductions under Chapter VIA in respect of investment deposit account. Audit scrutiny revealed that the deductions in respect of provision for bad and doubtful debts were allowed on the total income computed before making deductions towards investment deposit account instead of allowing the deduction on the total income arrived at after making the deductions towards investment deposit account.

(iii) The assessment of a financial corporation for the assessment year 1998-99 was completed in a summary manner in March 1999. Audit scrutiny revealed that the assessee had made a provision of Rs. 2983.38 lakh on account of debtors, loans and advances and after adjustment of an amount of Rs. 267.68 lakh from special reserve created under section 36(i)(viii) only an amount of Rs. 306.58 lakh was added back to the income in computation. Since the special reserve had to be maintained and kept intact from assessment year 1998-99, the adjustment was not in order and the entire provision of Rs. 2983.83 lakh was required to be added back. Omission to do so resulted in under assessment of income by Rs. 2676.80 lakh involving tax effect of Rs. 1221.55 lakh (including additional tax and interest).

(iv) The assessment of a company for the assessment year 1997-98 was completed after scrutiny in March 2000. Audit scrutiny revealed that a sum of Rs. 24.96 lakh being provision for bad and doubtful debts and advances stood debited to the profit and loss accounts of the relevant previous year. As it was a mere provision the deduction was required to be disallowed by

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the assessing officer. Omission to disallow the same resulted in underassessment of income and Rs. 24.96 lakh involving potential tax effect of Rs. 10.73 lakh.

## CHAPTER-19

### MISTAKES IN LEVY OF MAT U/S 115JA

(i) The assessment of a company for the assessment year 1997-98 was completed in a summary manner at loss of Rs. 465.30 lakh as returned by the assessee. Audit scrutiny revealed that the taxable income under the special provisions of the Act worked out at Rs. 77.93 lakh but the department had not invoked special provisions. The failure resulted in underassessment of income by Rs. 77.93 lakh involving short levy of tax of Rs. 33.51 lakh. The interest leviable for short payment of advance tax worked out to Rs. 8.04 lakh.

(ii) The assessment of a company for the assessment year 1997-98 was completed in a summary manner in March, 1998 and income was assessed at a loss of Rs. 337.73 lakh. Audit scrutiny revealed that the assessee company filed its return showing deemed income of Rs. 7.59 lakh as against the loss of Rs. 337.73 lakh under normal provisions. Since the assessee company had incurred loss, the total income of the assessee chargeable to minimum alternate tax would be Rs. 7.59 lakh being thirty percent of the book profits of Rs. 25.31 lakh which was not adopted by the assessing officer. The mistake resulted in under assessment of income of Rs. 7.59 lakh with consequent short levy of tax of Rs. 3.26 lakh including surcharge.

(iii) In case of a company for A.Y. 1998-99, the provision for bad and doubtful debts of Rs. 53,89,624 was omitted to be added back as *prima facie* adjustment u/s 143(1)(a) while computing income u/s 115JA. The omission to do so resulted in under assessment of income of Rs. 16,16,887 with consequent tax effect of Rs. 7,60,583.

(iv) The assessment of a company for A.Y. 1997-98 was completed in a summary manner in March, 1998 at nil income under normal provisions. Audit scrutiny revealed that the assessee had a book profit of Rs. 1177.93 lakhs and as such 30 per cent thereof should have been brought to tax under the special provisions as *prima facie* adjustment, the facts being apparent from the return and accompanying records. Omission to apply the special provisions resulted in underassessment of income by 355.38 lakhs (30 per cent of Rs. 1177.93 lakhs) with consequent short levy of tax of Rs. 162.55 lakhs.

(v) In the case of a company assessee the Assessing Officer while processing return under section 143(1)(a) read with section 115JA for the assessment year 1997-98 ignored to add back the provisions made in

respect of bad debts of Rs. 13,09,148 and Rs. 22,11,466 towards earned leave encashment. Failure to do so resulted in under assessment of income resulting in a revenue loss of Rs. 5,44,988/-.

(vi) In the case of a corporate assessee, the assessee had determined the income under section 115JA at Rs. 7,88,022/- after reducing the capital gains (after indexation) and setting off of brought forward losses against the income to be assessed at Rs. 15,54,375/- under section 115JA which was accepted under section 143(1)(a) by the Assessing Officer for the assessment year 1997-98 resulting in a revenue loss of Rs. 7,31,214.

(vii) In the case of a Bank for the assessment year 1998-99 return of income was filed declaring a loss of Rs. 24,33,55,780/-. The return was processed under section 143(1)(a) granting a refund of Rs. 11,05,37,040. The assessee had computed loss of Rs. 2,08,25,771/- under section 115 JA. The audit scrutiny revealed that an amount of Rs. 114,44,96,000/- was claimed as deduction under section 36(1) (viiia). It was noticed that the same amount Rs. 114,44,96,000/- was also claimed as a deduction from the book profits computed under section 115JA. This amount, which was an allowable deduction under section 36(1)(viiia) in computing the total income under the provisions of the Act other than section 115JA was not an allowable deduction in computing the books profits under that section. The mistake resulted in under assessment with consequent tax effect of Rs. 12,88,05,334/-.

(viii) In the case of a company for the assessment year 1999-2000 an amount Rs. 65,71,682/- was computed as refund under section 143(1)(a). The audit scrutiny revealed that the book profits under section 115JA was computed by deducting the provisions for doubtful debts, prior period expenditure and provision for leave encashment amounting to Rs. 6,17,72,612/-. The book profit under section 115JA was re-computed by the audit resulting in the tax demand of Rs. 3,03,768/- after absorbing the refund of Rs. 65,71,682/-.

## INTERNAL AUDIT OBJECTIONS

### Incorrect set off of brought forward loss

The assessee filed return for the Assessment Year 1997-98 admitting income u/s 115JA of Rs. 59,34,165. The assessee's income for the year computed in the regular manner was arrived at Rs. 2,97,59,791 and this was completely set off against loss brought forward from the earlier years.

Thus, there was no regular income liable for tax during the year. It is noticed that the assessee incorrectly carried forward loss of Rs. 1,11,52,918 and set it off against the current income. The correct loss liable to be carried forward and set off against the income of the current year amounted to Rs. 1,87,90,976 only. If the set off is correctly done, the assessee would be liable to tax on the regular income as it exceeded income under sec. 115JA. Failure to set off the loss correctly resulted in under assessment of Rs. 50,34,650 involving tax effect of Rs. 21,64,900.

Further, it is noticed that the assessee was allowed MAT credit of Rs. 25,51,691 against tax payable for the Assessment Year 1998-99. Such credit is not admissible since the assessee was liable to tax in the normal manner for the Assessment Year 1997-98 as per the audit objection above. Thus, for the Assessment year 1998-99 credit given for Rs. 25,51,691 on account of MAT has to be withdrawn. Interest granted u/s 244A amounting to Rs. 1,64,682 also has to be withdrawn.

**PART-II**  
**CHAPTER-20**

**MISTAKES IN SUMMARY ASSESSMENT**

**CASES COMPLETED UNDER THE SUMMARY ASSESSMENT  
SCHEME US 143 (1)(A) WHICH RESULTED IN  
MISTAKES POINTED OUT BY REVENUE AND  
INTERNAL AUDIT INVOLVING HUGE UNDER  
ASSESSMENT OF INCOME & CONSEQUENT  
NON-LEVY OF INTEREST, TAX AND  
ADDITIONAL TAX**

**20.1 Mistakes in Assessments of Corporate and Non-Corporate assess**

(i) The assessment of a banking company for the assessment year 1996-97 was completed allowing 100% depreciation of Rs. 43.61 lakh on computer software and it revealed that no special rate had been prescribed for computer software in the Income Tax Rules and therefore it was eligible for depreciation only at the general rate of 25 per cent.

(ii) The assessment of a company for the assessment year 1997-98 was completed allowing depreciation amounting to 235.86 lakh which included depreciation on written down value of Rs. 931.95 @ 25 per cent amounting to Rs. 232.99 lakh and it revealed that the gross block in the balance sheet was shown at Rs. 168.05 lakh only. The written down value could not be more than the gross block reflected in the balance sheet. To confirm this, previous year's records of the assessee were seen and it was observed that the correct written down value was Rs. 93.19 lakh. Thus, it was clear from the return itself that higher written down value was incorrectly adopted and excess depreciation allowed. The excess written down value adopted worked out to Rs. 838.77 lakh and depreciation allowed on this amounted to Rs. 209.69 lakh. This resulted in under assessment of income to that extent.

(iii) The assessment of a company for the assessment year 1995-96 was completed allowing depreciation of Rs. 44.49 lakh on Energy Saving Devices and it revealed that out of the total value of Energy Saving Devices of Rs. 44.49 lakh, plant and machinery valuing Rs. 43.11 lakh was acquired during the year and put to use for a period of less than one hundred and eighty days. As the information was available in the documents attached with the return, the depreciation on these assets was required to be restricted to fifty per cent of the amount calculated at the prescribed percentage.

(iv) The assessments of a company for assessment years 1994-95 and 1995-96 were completed in a summary manner in July 1996 and after

scrutiny in March 1997 respectively and it revealed that the assessee was allowed deduction of Rs. 14.79 lakh and Rs. 15.19 lakh towards intercorporate dividends received for the two assessment years respectively before setting off unabsorbed depreciation of earlier years. The incorrect allowance of deduction resulted in excess carry forward of unabsorbed depreciation aggregating Rs. 29.98 lakh.

(v) The assessment of a public limited company for the assessment year 1996-97 was completed at Rs. 694.69 lakh after allowing deduction of Rs. 231.56 lakh towards profits and gains from a new industrial undertaking established after 31 March 1981. Audit scrutiny revealed that the qualifying profits included dividend income of Rs. 168.79 lakh earned from UTI Scheme 1964. As the deduction was admissible only in respect of profits derived by the assessee from its manufacturing activity deduction should have been disallowed as *prima facie* inadmissible.

(vi) The assessments of a closely held company for the assessment year 1993-94 and 1994-95 were completed. In the assessment year 1993-94 the taxable income was determined at 'NIL' after allowing deductions to the extent of available profits of Rs. 55.89 lakh and it revealed that unabsorbed depreciation of Rs. 9.45 lakh for the assessment year 1992-93 was not set off before allowing the deductions under Chapter VIA and Rs. 7.89 lakh out of unabsorbed depreciation of Rs. 9.45 lakh was allowed to be set off in subsequent assessment year 1994-95. The omission resulted in underassessment of income of Rs. 7.89 lakh.

(vii) The assessments of a company for the assessment years 1994-95 to 1996-97 were completed in a Summary assessment after allowing special deduction aggregating Rs. 8.24 lakh in respect of profits from new industrial undertaking as claimed by it and it revealed that the special deduction was allowed in respect of income derived from poultry farming only which was not an industrial activity qualifying for special deduction as has been judicially held. The incorrect allowance resulted in underassessment of income of Rs. 8.24 lakh.

(viii) The assessment of a widely held company for the assessment year 1996-97 was completed at nil income after setting off of unabsorbed business loss and depreciation aggregating Rs. 129.43 lakh out of unabsorbed brought forward losses of Rs. 232.65 lakh and it revealed that the total income of Rs. 129.43 lakh was computed after allowing deduction of Rs. 40.46 lakh under Chapter VIA. As the gross total income of the assessee before allowing the above deductions

under Chapter VIA worked out to 'nil' income, the assessee was not eligible for the deduction under Chapter VIA. As the above information was available in the return and accompanying documents, the deductions should have been disallowed.

(ix) The assessment of a company for the assessment year 1993-94 was completed at a loss of Rs. 45020.95 lakh after disallowing loss of Rs. 27711.94 lakh by way of prescribed adjustments to the returned loss of Rs. 72732.89 lakh. Audit scrutiny revealed that though the additional income tax of Rs. 2868.18 lakh was required to be levied, the assessing officer levied additional income tax of Rs. 2494.07 lakh. The mistake led to short demand of additional income tax by Rs. 374.11 lakhs.

(x) The assessment of a widely held company for the assessment year 1996-97 was completed determining taxable income at Rs. 5586.16 lakh as against Rs. 2516.54 lakh offered by the assessee and it revealed that the company had paid advance tax of Rs. 290.00 lakh upto 15th June, 1995 and Rs. 870.00 lakh upto 15th September, 1995 and Rs. 1445.00 lakh upto 15th December, 1995 as against Rs. 301.98 lakh, Rs. 905.95 lakh and Rs. 1887.41 lakh payable respectively. Interest for the shortfall in payment of advance tax leviable as per provisions of the Income Tax Act was not levied. The omission resulted in non levy of interest of Rs. 35.65 lakh.

(xi) The assessment of a closely held company for the assessment year 1993-94 originally completed under summary and subsequents after scrutiny. The assessment was subsequently revised with a tax demand of Rs. 5659.05 lakh including the earlier refund and it revealed that though original demand notice was served upon the assessee on 29th March, 1996, the assessee paid tax demand by way of adjustment against refund of earlier years on 27th March 1997. As the demand was not paid by the assessee within the permissible period of 30 days from the date of serving of demand notice, the assessee was liable to pay interest of Rs. 512.94 lakh which was not levied by the department.

(xii) The assessment of a company for the assessment year 1995-96 was completed at a total income of Rs. 193.85 lakh including Long Term Capital gain of Rs. 50.73 lakh and tax of Rs. 107.38 lakh was levied and it revealed that the assessee furnished the return of income on 14th August 1996 though the specified due date for furnishing the return was 30th November 1995. For belated filing of return the assessee was liable to pay interest of Rs. 14.60 lakh which was not levied by the department. Further it was noticed that no surcharge was levied on the tax on Long Term Capital gains, although the same was leviable. The mistake resulted in short computation of tax by Rs. 3.33 lakh including short levy of interest for short payment of advance tax.

(xiii) The assessments of a Government financial company for the assessment years 1994-95 to 1997-98 were completed on an income Rs. 1347.53 lakh, Rs. 697.88 lakh, Rs. 553.31 lakh and Rs. 773.74 lakh



respectively. The assessee company was allowed deduction aggregating Rs. 9959.72 lakh and Rs. 278.61 lakh towards bad debts written off on loans and reserve for bad debts created respectively, for the above assessment years. Audit scrutiny revealed that while allowing the deduction of Rs. 9959.72 lakh towards bad debts written off, the provision of Rs. 278.61 lakh made in the accounts, was not adjusted against such debts. The assessee was eligible for a deduction aggregating Rs. 9681.11 lakh only as against the allowance of Rs. 9959.72 lakh made. Excess allowance of Rs. 278.61 lakh was required to be withdrawn.

(xiv) The assessment of a company for the assessment year 1996-97 was completed on "nil" income after *inter-alia* setting off of losses including unabsorbed depreciation of Rs. 88.37 lakh carried forward from the assessment year 1995-96, against the long term capital gains of Rs. 123.99 lakh. The balance unabsorbed loss of Rs. 14.72 lakh was allowed to be carried forward. Audit scrutiny revealed that in the scrutiny assessment for the assessment year 1995-96, subsequent to the processing of the return of income filed for the assessment year 1996-97, the unabsorbed depreciation to be carried forward to subsequent assessment years was reduced to Rs. 6.74 lakh from Rs. 88.37 lakh. The intimation sent for the assessment year 1996-97 was therefore required to be revised to withdraw the excess set off of loss, and fresh intimation sent under the provisions of the Act. Omission to do so, resulted in under assessment of income by Rs. 75.94 lakh.

(xv) The assessment of a widely held company for the assessment year 1993-94 was processed allowing an exemption of Rs. 1084.82 lakh in respect of profit earned from a hundred per cent export oriented undertaking and it was found that the details of miscellaneous income furnished with the return, the said exempted profit included an amount of Rs. 55.80 lakh on account of sale of Exim scrips/REP licence fees. Since the income by way of sale of Exim Scrips/licence does not fall under the category of income by way of manufacture or production of any article or thing, the said income was not an income exempt under the aforesaid provisions of the Act. The incorrect exemption resulted in underassessment of income Rs. 55.80 lakhs.

(xvi) The assessment of a company for the assessment year 1996-97 was completed at nil income after allowing set off of unabsorbed investment allowance of earlier years to the tune of Rs. 5.43 lakh and carry forward of balance of Rs. 15.20 lakh and it revealed that the company had neither created an investment allowance reserve in the year of installation of plant and machinery nor during the previous year relevant to assessment year in which set off was allowed. Therefore, set off of investment allowance allowed was irregular and was required to be withdrawn.

(xvii) The assessment of a company for the assessment year 1997-98 was

completed and it was found that the assessee had claimed and was wrongly allowed deductions, aggregating to Rs. 15.47 lakh in respect of Provident Fund and E.S.I. Contributions though not paid by the due date.

(xviii) The income tax assessment of two assessee companies for the assessment year 1996-97 were completed on an income of Rs. 1231.08 lakh/nil income determining refund aggregating Rs. 75.58 lakh including interest of Rs. 11.04 lakh and it was found that in respect one assessee refund of Rs. 24.36 lakh was granted including the interest of Rs. 4.06 lakh. Since the amount of refund was less than ten percent of the tax determined in the assessment no interest on excess amount was admissible. In respect of another assessee period of delay for filing of revised return in January 1998 in place of original return filed in December 1996 was attributed to assessee and no interest was admissible for the period from December 1996 to January 1998. The interest allowable to the assessee worked out to Rs. 2.91 lakh against the amount of Rs. 6.98 lakh actually allowed.

(xix) The assessment of a company for the assessment year 1995-96 was completed at a loss of Rs. 765.16 lakh after allowing a deduction of Rs. 48.54 lakh being one tenth of preliminary expenses incurred towards formation of the company and public issue expenses and it revealed that the capital employed of Rs. 120 crore was more than that of the cost of project of Rs. 99.74 crore. As such, the deduction towards preliminary expenses should have restricted to Rs. 3 crore being 2.5 percent of the capital employed and a deduction of Rs. 30 lakh being one tenth of Rs. 3 crore should have been allowed instead of Rs. 48.54 lakh actually allowed.

(xx) The assessment of a banking company for the assessment year 1996-97 was completed and it revealed that Rs. 124.21 lakh was allowed as share issue expenses as claimed in the return. The share issue expenses should have been treated as capital expenditure and disallowed.

(xxi) The assessment of a company for the assessment year 1997-98 was completed at Rs. 139.43 lakh and audit scrutiny revealed that the assessee company had debited its profit and loss account of the relevant previous year by an amount of Rs. 16.01 lakh being the loss on sale of assets. The loss which was capital in nature being *prima facie* apparent from records should have been disallowed.

(xxii) The assessment of a company for the assessment year 1996-97 was completed and audit scrutiny revealed that the assessee had claimed and was allowed Rs. 969.34 lakh being expenditure on interest and finance charges incurred on a new project prior to commencement of commercial production. In the books of accounts, the assessee had capitalised this amount being pre-operative expenditure. As the mistake was apparent from the records available with the return of income, the assessing officer should have *prima facie* disallowed the amount being capital expenditure.

(xxiii) The assessment of a company for the assessment year 1997-98 was

completed at a loss of Rs. 465.30 lakh as returned and audit scrutiny revealed that the taxable income under the special provisions of the Act worked out at Rs. 77.93 lakh but the department had not invoked special provisions. The failure resulted in underassessment of income by Rs. 77.93 lakh involving short levy of tax of Rs. 33.51 lakh and interest leviable for short payment of advance tax worked out to Rs. 8.04 lakh.

(xxiv) The assessment of a company for the assessment year 1997-98 was completed at a loss of Rs. 337.73 lakh and it revealed that the assessee company filed its return showing deemed income of Rs. 7.59 lakh as against the loss of Rs. 337.73 lakh under normal provisions. Since the assessee company had incurred loss, the total income of the assessee chargeable to minimum alternate tax would be Rs. 7.59 lakh being thirty percent of the book profits of Rs. 25.31 lakh which was not adopted by the assessing officer.

(xxv) The assessment of an assessee firm for the assessment year 1996-97 was processed on an income of Rs. 11.05 lakh and a deduction of Rs. 38.48 lakh was allowed in respect of export profits. Audit scrutiny revealed that while determining the deduction of Rs. 38.48 lakh the business profits before allowing deductions towards interest paid to partners and remuneration to working partners aggregating Rs. 16.17 lakh was considered instead of the correct amount of Rs. 49.53 lakh arrived at after allowing the above deductions if the correct amount of profit of Rs. 49.53 lakhs was adopted the assessee would be eligible for relief on exports of Rs. 29.01 lakh only as against Rs. 38.48 lakh allowed.

(xxvi) The assessment of a firm for the assessment year 1996-97 was processed at returned income of Rs. 3.62 lakh and a refund of Rs. 2.20 lakh was granted to the assessee and audit scrutiny revealed that while computing the income of the assessee income tax of Rs. 6.92 lakh debited to the profit and loss account of the relevant previous year was wrongly allowed.

(xxvii) The assessment of an individual, who was also a film artist, for the assessment year 1993-94, was processed at an income of Rs. 22.18 lakh and a special deduction of Rs. 33.84 lakh was allowed on income from foreign sources. Audit scrutiny revealed that the assessee was eligible for a special deduction of Rs. 24.88 lakh only at 75 percent of Rs. 33.17 lakh earned from foreign sources and brought into India, as against Rs. 33.84 lakh allowed at 50 percent on total professional income of Rs. 67.67 lakh.

(xxviii) An assessee firm filed original and revised return of income for the assessment year 1996-97 declaring income of Rs. 25.77 lakh and Rs. 26.05 lakh respectively after adjusting loss of Rs. 5.32 lakh relating to assessment year 1995-96. Both these returns were processed accepting the income declared. Audit scrutiny revealed that the scrutiny assessment for the assessment year 1995-96 was concluded in July 1997 and the loss of Rs. 5.32 lakh for this assessment year returned by the assessee firm was converted into positive income of Rs. 4.10 lakh. The assessment for the

assessment year 1995-96 was concluded after filing/processing the return for assessment year 1996-97, action to revise the intimation in respect of assessment year 1996-97 was required to be taken as provided in the Act.

(xxix) The assessment of a co-operative society, for assessment year 1995-96 was completed allowing the returned loss of Rs. 192.17 lakh to be carried forward. Audit scrutiny revealed that since the assessee had filed its return on 27 December 1996 i.e. after the due date, it was not entitled to carry forward of loss. The mistake resulted in irregular carry forward of loss of Rs. 192.17 lakh involving a potential tax effect of Rs. 67.22 lakh and additional tax of Rs. 13.44 lakh.

(xxx) The assessment of a company for the assessment year 1997-98 was completed at a loss of Rs. 1285.41 lakh. Audit scrutiny revealed that depreciation of Rs. 30.74 lakh was allowed on different assets though actual allowable depreciation worked out to Rs. 18.89 lakh only.

(xxxi) The assessments of a company for the assessment years 1996-97 and 1997-98 were completed on returned loss of Rs. 41.68 lakh and Rs. 28.13 lakh respectively allowing depreciation of Rs. 11.88 lakh and Rs. 8.91 lakh on block of plant and machinery. Audit scrutiny revealed that there was no manufacturing operation during the relevant previous years. The company did not file statutory audit reports. The internal auditor's report relevant to the assessment year 1997-98, filed along with the return, however, stated that there was no production during the year. As the plant and machineries were not used for business during the relevant previous years, and information to this effect was available from the records attached with the return, i.e. profit and loss accounts, balance sheet etc., allowance of depreciation was irregular.

(xxxii) The assessment of a private company for the assessment year 1995-96 was completed on a total income of Rs. 122.03 lakh after allowing a deduction of interest of Rs. 32.13 lakh paid to Industrial Finance Corporation of India. Audit scrutiny revealed that out of the above interest relating to assessment year 1993-94, Rs. 21.76 lakh was already allowed in the assessment year 1993-94 on payment basis in the assessment completed in February 1996. The balance of Rs. 10.37 lakh only was to be allowed in the assessment year 1995-96 as against Rs. 32.12 lakh claimed and allowed being *prima facie* apparent from records.

(xxxiii) The assessment of a company for the assessment year 1997-98 was processed determining a loss of Rs. 62.46 lakh. Audit scrutiny revealed that while processing the return the assessing officer erroneously adopted the current year's income of Rs. 65.63 lakh before set off of the loss and after disallowing undercharged liability of Rs. 3.17 lakh determined the net loss for the assessment year at Rs. 62.46 lakh instead of determining current year's income of Rs. 68.80 lakh and

setting off of the same against past losses. The mistake resulted in short computation of income of Rs. 131.26 lakh involving potential short levy of tax of Rs. 56.44 lakh.

(xxxiv) The assessment for the assessment year 1996-97 of an assessee company was processed taking the current year's income of Rs. 7.94 lakh before set off, incorrectly as loss and after making certain adjustments to the extent of Rs. 0.65 lakh determined the loss at Rs. 7.29 lakh instead of determining the income before set off at Rs. 8.59 lakh and adjusting past losses to that extent.

(xxxv) The assessment of a firm engaged in the contract work for the assessment year 1996-97 was completed at a taxable returned income of Rs. 13.28 lakh. The assessee was following mercantile system of accounting. Audit scrutiny revealed that an amount of Rs. 325 lakh on which TDS credit of Rs. 7.48 lakh was given to the assessee was not appearing in the profit and loss account but the same was shown as advances against contract receipt. As the advances against contract receipts were not income of the assessee for the assessment year, TDS credit given on the same by the department was not in order. As the mistake was apparent from the records, the assessing officers should not have granted TDS credit claimed by the assessee.

(xxxvi) In this case the assessee company filed its return of income for A.Y. 1996-97 for Rs. 428796117/- on 30.11.1996 and the intimation u/s 143 (1)(a) was issued on 23.2.98. The A.O. has allowed deduction of Rs. 37162266/- u/s 80HHC.

The Audit Scrutiny revealed that the assessee had collected sales tax of Rs. 18401287/- during the year which was debited to P&L A/c. This amount was not included in the total turnover for the purpose of deduction u/s 80HHC. It has been judicially held [Mc Dowell & Co. Ltd. Vs. CIT 154 ITR 148 (SC)] that central excise duty and sales tax collected form part of the turnover of the manufacturers. In view of this position an amount of Rs. 18401287/- was to be included in the total turnover. Further, it was seen from the accounts of the assessee that the assessee's other income included.

(1) Bank interest	4253134
(2) Int. recd. from customer	63502937
(3) Commission on export	6014782
(4) Brokerage	6997941
(5) Misc. receipts	502505
	81271299

As per explanation to Sec. 80HHC 90% of receipts for brokerage, commission, interest, rent etc. was to be reduced from the profit of the business computed under the head profits & gains of the business. In view of this position Rs. 73144169/- was to be reduced from the profits & gains

of the business of Rs. 429129868/- as arrived by the A.O. Taking into account the mistakes as pointed, deduction u/s 80HHC worked out to Rs. 28575319/- as against Rs. 37162266/- claimed by the "a". This resulted in under assessment of income of Rs. 8586947/- and consequent short levy of tax of Rs. 5766933/- including interest u/s 243B and Non-Levy of addl. tax of Rs. 789999/-.

(xxxvii) In the case of the assessee having a status of company the assessment for A.Y. 1997-98 was finalised by the Assessing Officer u/s 143(1)(a) of the I.T. Act, 1961 at a loss of Rs. 16,09,69,002/-. Audit scrutiny revealed that in the Schedule 10 of other income, the assessee had shown interest income (gross) at Rs. 8,51,691/-. However, the gross total receipt of interest amount was Rs. 3,61,17,052/- as per the TDS certificates. Thus, there was under assessment of Rs. 3,52,65,361/- with additional tax of Rs. 30,32,821/- and withdrawal of interest granted u/s 244A of Rs. 3,13,386/-.

(xxxviii) In the case of the assessee company, the assessment for A.Y. 1997-98 was finalised by the Assessing Officer u/s 143(1)(a) of the I.T. Act, 1961. Audit scrutiny revealed that in schedule M, amount of job work was shown at Rs. 85,27,551/- as against total of Rs. 93,23,831/- as per TDS certificates. Further, in Schedule P, quantity of purchases was shown at Rs. 1,90,54,955/- whereas in profit & Loss account, it was shown at Rs. 1,93,09,712/-.

(xxxix) In the case of the assessee the assessment for A.Y. 1998-99 was finalised by the Assessing Officer u/s 143(1) (a) of the I.T. Act, 1961. Audit scrutiny revealed that subsidy of Rs. 25 lacs received from Ministry of Food Processing Industry in the form of Seed Capital Assistance was not added in the total income. Besides, donation receipt of Rs. 25,000/- did not bear validity of exemption u/s 80G which required withdrawal of deduction of Rs. 12,500/- u/s 80G and unpaid entry tax of Rs. 2,672/- was to be disallowed.

(xxxx) In the case of the assessee firm the assessment for the A.Y. 1998-99 was finalised by the A.O. u/s 143 (1)(a) of the Income Tax Act, 1961. Audit scrutiny revealed that as per the return of income furnished by the assessee it had claimed credit of TDS amount deducted by the payer, but not shown the amount of interest paid/received by the assessee during the year under reference. Moreover, from the perusal of profit and loss account, it was not found credited on the credit side or netted out on the debit side, *mutatis mutandis*. The total amount of interest received based on the TDS certificates furnished alongwith the return of income amounted to 6,16,353/- resulting into underassessment with a short levy of tax of Rs. 2,15,925/- and non levy of additional tax of Rs. 43,145/- and interest u/s 234B of Rs. 47,460/-

(xxxxi) Contributions to the NSS were allowed as 100% deduction at the time of subscription. Withdrawals from the NSS (which may include

interest), however, were fully taxable. The assessee withdrew a sum of Rs. 129299 from the NSS. The Post Office deducted tax at source amounting to Rs. 25860 at the time of withdrawal. In the return of income for the Assessment Year 1997-98, the assessee claimed credit for TDS of Rs. 25860 effected on the amount of Rs. 129299 withdrawn from the NSS. The assessee, however, did not include the amount withdrawn from the NSS in his total income. While processing the return under sec. 143(1) (a), the Assessing Officer allowed credit for TDS effected on the amount withdrawn from the NSS without realising the fact that the assessee had not accounted for the amount withdrawn as income.

(xxxii) In the case of firm the return of income for the assessment year 1997-98 was processed under section 143(1) (a). On going through the return of income, it was observed that the firm had transferred its only asset *i.e.* lorry to its partner and did not offer the short term capital gain arising on its transfer. Applying the provisions of section 50, the short term capital gains worked out to Rs. 4,17,286 involving tax effect of Rs. 1,66,914.

(xxxiii) The case of a company assessee for A.Y. 1998-99 was processed u/s 143(1) (a). The Audit scrutiny revealed that the assessee had claimed and was allowed 100% depreciation on wind mills. The assessee was only a manufacturer of wind turbines. Only those concerns which had installed wind mills for production of energy were entitled to 100% depreciation. As the assessee was only a manufacturer, the allowance of the claim of 100% depreciation was wrong. It was entitled to only normal depreciation.

(xxxiv) The assessment of a company assessee for A.Y. 1996-97 was completed summarily in Jan., 1998. The depreciation as per I.T. Act had been claimed at Rs. 2083367. However, from the statement of depreciation as per I.T. Act, it could be seen that depreciation on fishing Trawlers had been claimed @25% as against allowable 20% as per section 32 of I.T. Act. The depreciation allowable @20% worked out to Rs. 3,52045.

(xxxv) In the case of the assessee having a status of firm the assessment for the A.Y. 1998-99 was finalised by the A.O. u/s 143(1) (a) of the Income Tax Act, 1961. Audit scrutiny revealed that in the profit and loss account, the assessee had debited interest expenses of Rs. 26,96,784 whereas as per the abstracts of interest account furnished alongwith the return of income the debit of the interest account was Rs. 16,04,113 only. Thus the assessee had debited excess interest expenses of Rs. 10,92,671 which had resulted in over-assessment of loss by Rs. 10,92,761 with notional tax effect of Rs. 382435 and non levy of additional tax of Rs. 76,487.

(xxxvi) While computing the income from a house property, the assessee claimed deduction of legal fee and legal expenses amounting to Rs. 55,990. The return was accepted u/s 143(1) (a) for the Assessment Year 1998-99 without making any adjustment. Omission to disallow the

claim for deduction of inadmissible expenses on account of legal fee and expenses while computing income under the head 'House Property' resulted in under assessment of Rs. 55,990.

(xxxxvii) The case of a company assessee for A.Y. 1996-97 was processed u/s 143(1) (a) in November, 1997, From the TAR Form 3 - CD enclosed with the return it was noticed that the following items of expenditure debited to P&L A/c should have been disallowed and added to the income of the assessee company under *prima facie* adjustment for the reasons stated against each.

Items of Expenditure	Amount	Reasons
1. Payment on a/c of goodwill of purchase of business from Nelco	750000	Capital expenditure as per Annexure 2 clause 4(1)
2. Provision for commission	216000	It is mere provision Annexure 3 clause 4 (x)
	966000	

Failure to do so resulted in under assessment of income of Rs. 966000 involving short levy of tax of Rs. 533232 including addl. tax. In addition interest amounting to Rs. 111979 u/s 244A was required to be withdrawn.

(xxxxviii) The assessment of an assessee individual for the assessment year 1995-96 was processed in summary manner in November 1995 determining tax payable at Rs. 4.26 lakh and a sum of Rs. 5.53 lakh including interest was refunded to the assessee in March 1996. Subsequently, the assessment was completed in March 1997 after scrutiny determining income at Rs. 46.6 lakh. Audit scrutiny (July 1998) revealed that while computing the net demand even though credit for prepaid taxes was taken into account, refund of Rs. 5.53 lakh granted in March 1996 was omitted to be added. Though a notice was issued to the assessee in October 1997 to rectify the mistake, the mistake was not rectified even in July 1998 when the assessment was revised to give effect to the orders of the appellate authority.

(xxxxix) The assessment of a company for the assessment year 1993-94 was completed after scrutiny in March 1996 allowing an amount of Rs. 7.09 lakh towards bad debts written off. Audit scrutiny revealed that there was nothing on record to show that the said amount had been taken into account in computing the income of the relevant previous year or earlier previous years in the absence of which the allowance of deduction was irregular. The mistake resulted in underassessment of income of Rs. 7.09 lakh with consequent short levy of tax of Rs. 7.02 lakh including interest.

(xxxxx) The assessment of a banking company for the assessment year 1995-96 was completed after scrutiny in March, 1998 allowing a deduction of Rs. 41.54 lakh towards provision made in respect of bad and doubtful



debts for twenty eight rural branches of the bank. Audit scrutiny revealed that out of twenty eight rural branches, twenty one branches for which deduction of Rs. 38.72 lakh was allowed towards bad and doubtful debts were situated in places with a population exceeding ten thousand according to the last census. As such those branches did not fall within the meaning of rural branches and were not entitled to the said deduction. The mistake in allowing deduction resulted in under assessment of income by Rs. 38.72 lakh involving potential tax effect of Rs. 17.81 lakh including interest.

## 20.2 Over Payment of Interest

(i) The assessment of a banking company for the assessment year 1994-95 was processed in a summary manner in August 1995 and completed after scrutiny in February 1997. Audit scrutiny revealed that the department failed to reduce the interest initially paid to the assessee, consequent on enhancement of the income and the tax payable. This resulted in payment of excess interest of Rs. 426.03 lakh to the company.

(ii) The assessments of a banking company for the assessment years 1994-95 and 1995-96 were processed under summary manner in January 1995 and September 1996 and completed after scrutiny in January 1997 and March 1997 respectively. Audit scrutiny revealed that the department had withdrawn only Rs. 6.38 lakh and Rs. 37.82 lakh for the assessment years 1994-95 and 1995-96 in place of the interest of Rs. 119.71 lakh and Rs. 172.95 lakh respectively paid earlier on refunds.

## 20.3 Internal Audit Objections

### BENEFIT OF INDEXATION OF COST WRONGLY ALLOWED PRIMA FACIE ADJUSTMENT NOT MADE

(i) Sec. 2(42A) defines short term capital asset as a capital asset, being land or a building appurtenant thereto, held for less than three years. Sec. 48 permits the benefit of indexation on the cost only if the asset is a long term capital asset. The assessee sold a piece of land on 18-2-1994 for Rs. 22,94,473. The assessee acquired this piece of land on 2-5-1991 for Rs. 7,92,260. Since the land was held for less than three years, it was a short term capital asset for the benefit of indexation of cost for the land sold, therefore, is not admissible as per the second proviso to sec. 48. While computing capital gains consequent to the transfer of land, the assessee assumed the asset to be a long term asset and deducted the indexed cost of acquisition from the sale proceeds. The claim of indexation was patently wrong and it called for adjustment. The return filed by the assessee for the Assessment Year 1994-95, however, was accepted under sec. 143(1)(a) without making any *prima facie* adjustment. Omission to make the *prima facie* adjustment resulted in under assessment of Rs. 1,79,154 involving tax effect of Rs. 80,619.

**20.4 Incorrect Allowance of Deduction from Income From House Property**

(i) While computing the income from house property, the annual rent has to be reduced by the specified deductions. Legal fees, however, is not one of the admissible deductions. While computing the income from a house property, the assessee claimed deduction of legal fee and legal expenses amounting to Rs. 55,990. The return was accepted u/s 143(1)(a) for the Assessment Year 1998-99 without making any adjustment. Omission to disallow the claim for deduction of inadmissible expenses on account of legal fee and expenses while computing income under the head "House Property" resulted in under assessment of Rs. 55,990 involving tax effect of Rs. 19,597.

**PART-III**  
**CHAPTER-21**  
**MISTAKES UNDER THE INTEREST TAX ACT**

**21.1 Omission to make assessment of interest tax**

(i) The audit scrutiny of the income tax assessment records of a company for the assessment years 1993-94 and 1994-95 revealed that the assessee received a sum of Rs. 6.91 lakh and Rs. 6.25 lakh as interest and 'Bills discounting charges' during the relevant financial years which being chargeable interest attracted levy of interest tax. However, the assessee did not file any interest tax returns nor did the department initiate any interest tax proceedings.

(ii) Audit scrutiny of the income tax assessment records of a financial company for the assessment years 1995-96 and 1996-97 revealed that the company earned income of Rs. 34.52 lakh and Rs. 87.17 lakh respectively during the relevant previous years from bills discounting charges, finance and service charges in respect of finance provided under hire purchase scheme and interest on loans and advances and hence liable to interest tax. However, the assessee did not file return of chargeable interest for the above assessment years, nor did the department initiate any interest tax proceeding.

(iii) Audit scrutiny of the income tax assessment records of a closely held company for the assessment years 1993-94, 1994-95 and 1995-96 revealed that the assessee had received Rs. 135.92 lakh, Rs. 117.15 lakh and Rs. 117.14 lakh towards interest income on loans and advances made to different parties other than the cooperative societies which provided credit facilities to the farmers and village artisans etc. during the relevant previous years. The interest income attracted levy of interest tax under the provisions of the Act. However, the assessee company did not file any return of chargeable interest for any of the assessment years, nor did the department initiate interest tax proceedings.

(iv) Audit scrutiny of the income tax assessment records of a financial company for the assessment years 1994-95 to 1996-97 revealed that the assessee company had received interest aggregating Rs. 307.98 lakh on loans and advances made and finance charges of Rs. 16.65 lakh on hire purchase loans during the relevant previous years. These interests were chargeable to Interest tax. However, the company did not file interest tax returns for any of the assessment year, nor did the department initiate any interest tax proceedings.

(v) Audit scrutiny of the income tax assessments of three finance companies revealed that these assesseees received interest of Rs. 349.53 lakh, Rs. 15.19 lakh and Rs. 100.69 lakh during the financial years

relevant to the assessment years 1995-96 to 1997-98 but neither did the assessee file the interest tax returns nor did the department initiate interest tax proceedings. This resulted in non levy of interest tax of Rs. 21.26 lakh.

(vi) Audit scrutiny of the income tax records of a co-operative bank for the assessment year 1992-93, revealed that the interest and discount income was shown at Rs. 3998.96 lakh and advances and loans to individuals were shown in the balance sheet at more than Rs. 75 crores. Thus a return for interest tax was required to be filed but the same was neither filed by the assessee nor was called for by the department. This resulted in short taxation apart from interest and penalty. Audit scrutiny pointed out that a token tax of Rs. 5.00 lakh was taken at the initial stage but the actual tax worked out to Rs. 70.39 lakh including interest.

(vii) The income tax assessment records of a company engaged in hire purchase, leasing finance and bill discounting activities for the assessment year 1995-96 disclosed that while finalising the assessment the assessing officer disallowed the depreciation on the leased assets and it was established that the lease transactions were nothing but hire purchase transaction in the garb of lease. Audit scrutiny revealed that though the transactions were treated as hire purchase loan transactions no interest tax was charged on the interest element of Rs. 43.43 lakh included in the lease rentals. The omission resulted in non-levy of interest tax of Rs. 1.30 lakh.

#### **21.2 Omission to Make Assessment of Interest Tax and Non-L Levy of Interest Tax**

1. The income tax assessment of a company engaged in the business of financing and investment in shares and securities, for the assessment year 1997-98 was completed after scrutiny in March, 2000. The assessee had received interest income of Rs. 46.93 lakh. Audit scrutiny revealed that the interest tax return was neither filed by the assessee nor did the department initiate the proceedings which resulted in escapement of chargeable interest involving tax effect of Rs. 2.46 lakh (including interest).

2. The assessment of a finance company for the assessment year 1998-99 was completed in April 1999 in a summary manner. Audit scrutiny revealed that the assessee had received interest income of Rs. 10.79 lakh from various companies. Audit scrutiny revealed that neither the assessee had filed the interest tax return nor did the Assessing officer call for the same. The omission resulted in escapement of interest income of Rs. 10.79 lakh with consequent short levy of interest tax of Rs. 0.45 lakh including interest.

3. The Income-tax assessment of a company for the assessment year 1997-98 was completed in scrutiny manner in March, 2000 at an assessed income of Rs. 572.36 lakh. Audit scrutiny revealed that the assessee had income of Rs. 1110 lakh being income on account of lease rent, hire purchase finance charges, bills discounting charges and was therefore liable to file interest tax return also. Neither did the assessee file the interest tax return nor did assessing officer take any action to call for the same. The mistake resulted in escapement of interest income of Rs. 1110 lakh with non-levy of interest tax of Rs. 33.10 lakh. In addition to this, interest under Interest Tax Act was also leviable.

### **21.3 Escapement of Chargeable Interest Income Resulting into Short Levy of Interest Tax**

1. The Income-tax assessment of a finance company for the assessment year 1997-98 was completed in a scrutiny manner in March, 2000. Audit scrutiny revealed that, the assessee had received interest income of Rs. 170.23 lakh, which would attract the provisions of Interest Tax Act. It is however, noticed that interest tax return was not filed. The omission resulted in interest income of Rs. 170.23 lakh escaping assessment involving revenue effect of Rs. 8.60 lakh including interest.

2. The interest tax assessment of a finance company for the assessment years 1995-96 and 1996-97 were completed in November 1998. Audit scrutiny revealed that overdue charges which are in nature of interest on hire purchase charges amounting of Rs. 4.37 lakh and Rs. 2.11 lakh received during the previous years relevant to the assessment years 1995-96 and 1996-1997 were required to be added back while computing chargeable interest by the assessing officers. The omission resulted in short levy of interest of Rs. 0.44 lakh which was raised by the department in order.

### **21.4 Under Assessment of Chargeable Interest**

The Interest tax assessment of a non-banking financial institution for the assessment years 1995-96 and 1996-97 were completed in March 1998 and March 1999 on a chargeable interest of Rs. 1222.08 lakh and Rs. 1142.25 lakh respectively. Audit scrutiny revealed that while computing the chargeable interest, the assessing officer considered interest actually received by the company ignoring the interest incomes of Rs. 901 lakh and Rs. 1323 lakh accrued during the relevant previous years. As the chargeable interest should include interest income of Rs. 901 lakh and Rs. 1323 lakh were required to be included in the computation of chargeable interest. The mistake resulted in an underassessment of chargeable interest of Rs. 901 lakh and Rs. 1323 lakh involving short levy of interest tax of Rs. 105.17 lakh in aggregate.

### **21.5 Avoidable Payment of Interest by Government to the Assessee**

The interest tax assessment of a company for the assessment years 1993-94 and 1994-95 originally completed in December 1995 and December 1996 respectively were revised in April 1997 to give effect to the order of the

appellate authority determining aggregate amount of refund of Rs. 349.25 lakh (Assessment year 1993-94 Rs. 209.16 lakh, assessment year 1994-95 Rs. 140.09 lakh). Out of this refund sum of Rs. 293.14 lakh was adjusted by the assessing officer against the Income-Tax demand for the assessment year 1994-95 and the balance amount of Rs. 56.11 lakh was refunded to the Assessee in April 1997. However, in pursuance of decision of Hon'ble Court dated 5th May, 1999, the amount of refund of Rs. 293.14 lakh adjusted earlier against the demand of Income-tax for the assessment year 1994-95 had been allowed to the assessee company (July 1999) alongwith interest of Rs. 82.08 lakh. Audit scrutiny revealed that since the assessee had not been given prior information before adjustment of refund by the assessing officer and moreover it had already been judicially held that no inter-statute adjustment of tax can be made the payment of entire refund of Rs. 349.25 lakh instead of Rs. 56.11 lakh should have been made in April 1997 itself. The omission resulted in avoidable payment of interest of Rs. 82.08 lakh from April 1997 to July 1999 by the Government to the assessee.

#### **21.6 Short levy of interest for default in payment of interest tax in advance**

The Interest Tax assessment of a company for the assessment year 1997-98 was completed after scrutiny in March, 2002. Audit scrutiny revealed that the interest leviable for default in payment of interest tax in advance was short levied by Rs. 57.99 lakh which resulted in short levy of interest by an identical amount. (21)(00-01)

#### **21.7 Omission to charge interest for default in payment of interest tax in advance**

The assessment of an assessee company for the assessment year 1994-95 was completed after scrutiny in March, 1998 on a chargeable interest of Rs. 72.96 lakh determining a tax of Rs. 4.27 lakh including interest. Audit scrutiny revealed that the interest leviable for default in payment of interest tax in advance was levied at Rs. 1.57 lakh against the correct amount of Rs. 2.09 lakh leviable. The mistake resulted in short levy of interest of Rs. 0.52 lakh.

#### **21.8 Non-levy of interest for belated payment of interest tax demand**

The Interest tax assessment of a financial company for the assessment year 1993-94 was completed in March 1997 on a chargeable interest of Rs. 1196.23 lakh. Audit scrutiny revealed that the demand of Rs. 14.40 lakh was paid belatedly in August 1997 against the due date of 2nd May 1997. As the demand was not paid within due date. The assessee company was liable to pay interest of Rs. 0.86 lakh which was not levied.

**PART-IV**  
**CHAPTER 22**

**MISTAKES UNDER THE WEALTH TAX ACT**

**22.1 Avoidable mistakes in the computation of wealth tax**

(i) In the wealth tax assessment of a company for the assessment year 1995-96 completed after scrutiny, audit scrutiny revealed that wealth tax refund of Rs. 77,564 lakh allowed in summary assessment was not taken into account while completing the scrutiny assessment. The mistake resulted in short levy of wealth tax of Rs. 77,564.

**22.2 Wrong application of W.T. rates**

(i) The wealth tax assessments of a Hindu undivided family (specified) for the assessment years 1989-90 and 1990-91 completed after scrutiny on a net wealth of Rs. 66.81 lakh and Rs. 74.66 lakh levying the tax of Rs. 1.50 lakh and Rs. 1.79 lakh respectively revealed that as per rates specified for the relevant assessment years, wealth tax leviable for two assessment years aggregated Rs. 3.80 lakh as against Rs. 3.29 lakh levied.

(ii) The wealth tax assessment of a company for assessment year 1993-94 completed in scrutiny on a net wealth of Rs. 136.92 lakh and the wealth tax of Rs. 2.72 lakh was levied revealed that wealth tax was levied at the rate of two percent instead of one percent. The tax leviable would be Rs. 1.22 lakh as against Rs. 2.74 lakh levied. The mistake resulted in over charge of wealth tax of Rs. 1.52 lakh.

(iii) Assessment of an individual for the assessment year 1992-93 was completed in summary manner on the net wealth of Rs. 50.60 lakh including an addition of Rs. 13.14 lakh made towards *prima facie* adjustment. Audit scrutiny revealed that wealth tax was levied at the rates applicable for the assessment year 1993-94, instead of the rates applicable for the assessment year 1992-93. Further, the additional tax of Rs. 5,256 leviable towards *prima facie* addition carried out was also omitted to be levied.

(iv) Assessments of a "Hindu Undivided Family" for the assessment years 1991-92 and 1992-93 were completed after scrutiny determining net wealth of Rs. 11.27 lakh and Rs. 13.77 lakh respectively and levied an aggregate tax of Rs. 18,330 at the rate applicable to Hindu undivided family (ordinary). It was found that a member of the family had taxable wealth in his individual capacity and as such the assessee was required to be charged to tax on net wealth at higher rates applicable to Hindu

undivided family (specified). On the basis of higher rate of tax, the tax leviable worked out to Rs. 58,797 (including interest) as against the tax of Rs. 18,330 levied by the department.

### **22.3 Non levy of surcharge**

(i) The wealth tax assessment of a company for the assessment year 1988-89 was completed after scrutiny determining a net wealth of Rs. 732.89 lakh and tax of Rs. 14.65 lakh. It was found that surcharge leviable @ 10% on the wealth tax of Rs. 14.65 lakh amounting to Rs. 1.46 lakh was not levied.

### **22.4 Wealth escaping assessment**

(i) Income tax assessment records of closely held company for the assessment years 1989-90 to 1993-94 revealed that the assessee company acquired a house property during the previous year relevant to the assessment year 1989-90 and earned rental income therefrom. For owning such specified asset the assessee company was liable to wealth tax on the value of the said house property.

(ii) Income tax assessment records of four companies for the assessment year 1997-98 revealed that the assessee companies derived rental income of Rs. 124.90 lakh, Rs. 12 lakh, Rs. 17.50 lakh and Rs. 15.44 lakh respectively from let out immovable commercial properties owned by them during the relevant previous year. The commercial properties constituted their wealth. One of the assessee companies also owned motor cars of the value of Rs. 4.94 lakh which being specified assets also attracted levy of wealth tax.

(iii) The income tax assessments of an individual for the assessment year 1993-94 were completed after scrutiny in August, 1995. Audit scrutiny revealed that the assessee derived rental income of Rs. 9.44 lakh in aggregate from let out house property owned by her during the relevant previous year. Considering the rent capitalisation, the net value of the property after reducing debts owned as loan or advances worked out to Rs. 33.24 lakh which constituted wealth of the assessee attracting levy of wealth tax.

(iv) The income tax assessment records of a closely held company for the assessment years 1991-92 and 1992-93 revealed that the company owned two office premises during the relevant previous years which were let out on a security deposit of Rs. 95 lakh and rental income @ Rs. 8.56 lakh per year from these properties was derived. The properties being specified assets constituted wealth of the assessee company attracting levy of wealth tax.

(v) The income tax assessment records of four individuals for the assessment years 1988-89 to 1992-93 revealed that after partition of joint properties, the value of properties owned by each individual exceeded the non-taxable limit and became liable to wealth tax.



(vi) The income tax assessments records of a closely held company for the assessment years 1992-93 and 1993-94 revealed that the assessee company had purchased a house property at a cost of Rs. 152.46 lakh in July 1991, with an addition of Rs. 5.58 lakh during 1992-93, which was let out on rent for residential purposes. The rental income derived from it was assessed in income tax assessment under the head "Income from house property". There were debts of Rs. 73.66 lakh and Rs. 66.40 lakh relating to the said property for the assessment years 1992-93 and 1993-94 respectively. As the assessee was a company in which public were not substantially interested and the house being a residential one, the assessee was liable to pay wealth tax in respect of the value of the said house property for the two assessment years.

(vii) The income tax assessment records of an individual for the assessment year 1991-92 completed *ex parte* revealed that certain movable and immovable properties owned by the assessee together with cash, gold and silver ornaments worth Rs. 28.64 lakh were seized during search operations and brought to income tax. These items constituted wealth of the assessee attracting levy of wealth tax.

(viii) The wealth tax assessments of an Artificial juridical person for the assessment years 1988-89 to 1991-92 were completed after scrutiny in March 1992, March 1993 and March 1994. Audit scrutiny revealed that the wealth returned by the assessee included certain immovable properties at Pune, valued at Rs. 0.91 lakh, portions of which were acquired by the Pune Municipal Corporation in August 1990. The total compensation awarded on acquisition was Rs. 30.16 lakh which was returned as capital gains in the assessee's income tax returns for the assessment year 1992-93 filed in June, 1992 and the valuation date reckoned was 24th September 1987, being the date of publication of the notification for acquisition under the Land Acquisition Act, 1894. However, while concluding the assessments for the assessment years 1988-89, 1989-90, 1990-91 and 1991-92, the value of unacquired portions of the property only was recomputed adopting the price in September, 1987 in the acquisition proceedings. The value of the acquired portions in respect of which compensation was receivable during the four assessment years was not recomputed. While the compensation receivable for the assessment years 1990-91 and 1991-92 ought to have been adopted in the scrutiny assessments for these years concluded in March 1993 and March 1994, subsequent to June, 1992 when the fact of receipt of compensation during 1991-92 came to the notice of the assessing officer, the assessments for the assessment year 1988-89 and 1989-90 ought to have been reopened under section 17 of the Wealth Tax Act.

(ix) The assessment of a closely held company for the assessment year 1992-93 was completed after scrutiny adopting the value of building and

land appurtenant thereto *inter alia* owned by the company, of Rs. 10.67 lakh as per balance sheet as against 'nil' value returned by the assessee. Income tax assessment records revealed that the assessee acquired this property in December, 1985 at a cost of Rs. 7 lakh and its value was taken to be Rs. 100 lakh in assessment years 1993-94 when the land was converted into stock in trade. The assessee did not file W.T. Returns for A.Ys. 1986-87 to 1991-92 for which it was liable to wealth tax. The department did not initiate any wealth tax proceedings. Considering the market value of land in assessment year 1993-94 and going back with appropriate reduction in the value of land, the omission resulted in wealth aggregating Rs. 272 lakh escaping assessment with consequent short levy of wealth tax of Rs. 5.39 lakh.

(x) The wealth tax assessments of a company for assessment years 1990-91 to 1992-93 were processed in a summary manner in September, 1993 on a net wealth of Rs. 0.81 lakh, Rs. 0.15 lakh and Rs. 1.82 lakh respectively being the value of cars. Audit scrutiny of the income tax assessment records of the company for the assessment year 1992-93 revealed that it owned several buildings at Bombay and Madras and vacant land at Madras which were not used for its business. Except for one building which was occupied by the Managing Director of the Company, others were let out and the rental receipts were charged under the head "Income from House Property". The above properties were already assessed to wealth tax for the assessment years 1988-89 and 1989-90 and their assessment was also confirmed by the appellate authority in March, 1994. Considering rent capitalisation, the value of these properties would work out to Rs. 125.85 lakh, Rs. 166.35 lakh and Rs. 168.32 lakh for assessment years 1990-91 to 1992-93 respectively, which being the value of specified assets were required to be included in the net wealth. Omission to do so resulted in short levy of wealth tax aggregating Rs. 9.21 lakh.

#### 22.5 Incorrect computation of net wealth

(i) Assessment of an individual for the assessment year 1995-96 was completed after scrutiny which revealed that Rs. 103.46 lakh was erroneously arrived at instead of the correct figure of Rs. 182.80 lakh of the net taxable wealth of the assessee.

(ii) Tax assessment of a company for the assessment year, 1994-95 was completed after scrutiny at a total wealth of Rs. 376.89 lakh which revealed that the value of residential houses given to the employees drawing salary in excess of rupees two lakh was shown at Rs. 110.55 lakh and the same was deducted from the wealth stating that all the flats were mortgaged in favour of debenture Trustees to the extent of value of assets and the value of the flats was taken as 'nil'. As this liability was not incurred to acquire the assets, the same should not have been deducted from the wealth of the assessee.

(iii) Assessments of a Hindu undivided family for the assessment years 1993-94 and 1994-95 were completed after scrutiny on a net wealth of Rs. 64.28 lakh and Rs. 46.80 lakh respectively and tax assessment records for the assessment year 1992-93 revealed that the assessee owned a plot of land valued at Rs. 26.06 lakh at Hyderabad city which was not included in the net wealth of the assessee for the above assessment years. Further there was no indication to show that the property was disposed off after 31 March, 1992. The omission resulted in underassessment of wealth of Rs. 26.06 lakh in each of the two years.

(iv) The wealth tax assessments of an individual for the assessment years 1989-90, 1991-92 and 1992-93 were completed after scrutiny which revealed that while determining the value of a building in a metropolitan city, the assessing officer omitted to include 15% of rent advance in the gross maintainable rent for assessment years 1991-92 and 1992-93. Further, while allowing the loan liability on the assets for which exemption was claimed, the liability was not reduced to the extent of the exemption claimed and allowed for all the assessment years. Also for assessment year 1992-93, the assessee being an Indian Citizen who had returned from Srilanka was allowed exemption in respect of the assets acquired out of money brought into India which was not in order as the maximum limit of seven assessment years had already expired upto assessment year 1991-92.

(v) An assessee had filed its returns of net wealth for the assessment years 1989-90 and 1990-91 at 'Nil' wealth on the ground that all immovable and movable properties valued at Rs. 22.54 lakh and Rs. 23.52 lakh on the valuation dates relevant to the aforesaid assessment years were given as security to the IDBI and Bank of Baroda against the secured loans of Rs. 16.45 lakh and Rs. 179.37 lakh obtained from them. The assessee's returns for the assessment year 1989-90 was treated as non-existent in June 1990 and that for 1990-91 was completed after scrutiny in October 1992, admitting the assessee's claim. Audit scrutiny revealed that debt of Rs. 179.37 lakh secured from the Bank of Baroda (claimed and allowed as debt owed by the assessee) was secured against the assets other than the specified assets owned by the company. Another loan of Rs. 16.45 lakh from IDBI was secured on the entire movable and immovable properties of the company and as such only that part of the loan, on pro rata basis, attributable to the specified assets was allowable as debt owed by the company. Since the entire value of debts owed was not secured on or incurred in relation to the specified asset, the same was not allowable as debt owned.

(vi) Assessment of a closely held company for the assessment year 1993-94 was completed after scrutiny after allowing a deduction of Rs. 95 lakh in respect of advance received, on 31 March, 1993, against the sale of land owned by the assessee company during relevant previous year and it revealed that the assessee had received merely advance against the sale of land for which the sale deed was not executed till the end of year and as such the ownership vested with the assessee as on 31 March, 1993. Since

the advance received by the assessee can't be treated as debt owned by assessee in relation to the asset, the deduction allowed was irregular.

## 22.6 Incorrect valuation of assets

(i) Audit scrutiny of the wealth tax assessment of an individual for the assessment year 1992-93, completed after scrutiny revealed that the value of 81066 quoted equity shares of several companies held by the assessee was adopted at Rs. 101.05 lakh on the basis of the average quoted value under the special valuation provisions of schedule III to the Act as opted and returned by the assessee. For adoption of such average value, the assessee was required to get a certificate of valuation by an accountant and attach the same with the return, which was however not done. Since the statutory requirement of furnishing the certificate of an accountant with the return was not fulfilled by the assessee to substantiate his claim, the value of the shares should have been adopted at Rs. 294.04 lakh on the basis of the quoted rates of shares on the valuation date, i.e. 31 March 1992 which was higher than the adopted average quoted value.

(ii) In the wealth tax assessment of two individuals holding 7000 shares and 3400 unquoted equity shares in an investment company for assessment year 1990-91 and 1991-92 completed after scrutiny the value of each unquoted equity share of the company was adopted at Rs. 421.90 and 443.62 in the case of one assessee and Rs. 50.59 and Rs. 50.59 in the case of the other assessee. Audit scrutiny revealed that in working out the value the income tax and wealth tax liabilities amounting to Rs. 31.29 lakh relating to assessment year 1983-84 to 1988-89 not shown in the balance sheet were deducted from the value of assets. Further the break up value of Rs. 421.90 lakh for the assessment year 1990-91 was arrived at after allowing a deduction of twenty percent applicable for non investment companies. Similarly in the wealth tax assessment of the aforesaid assessee and one Hindu undivided family (specified) for the assessment years 1992-93 completed after scrutiny between January 1995 and March 1995, the value of 12,900 unquoted equity shares (of the same investment company) owned by them was incorrectly adopted at Rs. 50.59, Rs. 424.92 and Rs. 100 per share respectively due to identical mistakes pointed out above for assessment years 1990-91 and 1991-92. Incorrect adoption of the value of shares resulted in underassessment of wealth aggregating Rs. 246.33 lakh

(iii) The wealth tax assessment of a company for the assessment year 1994-95 was completed after scrutiny in October 1996 adopting the value of a plot of land owned by the assessee and included in the wealth at Rs. 6.07 lakh. Audit scrutiny of the income tax assessment records for the assessment year 1995-96 (assessment completed after scrutiny in October 1996) revealed that the said plot of land was sold in August 1994 for a consideration of Rs. 72.29 lakh which was much higher than the value adopted in the wealth tax assessment for assessment year 1994-95.

Considering the sale value of the land in August 1994 and on the basis of cost deflation method the value of the land as on 31 March 1994 would work out to Rs. 68.10 lakh which was required to be adopted.

#### 22.7 Irregular allowance of exemption

(i) Audit scrutiny of the wealth tax assessments of a company for the assessment years 1994-95 to 1996-97 completed in a summary manner in February 1997 revealed that the assessee company claimed in its return and computation of wealth, exemption of one house worth Rs. 119.60 lakh in each year. The same was allowed by the Assessing Officer. As the assessee was a company, it was not entitled to such an exemption. The exemption being *prima facie* inadmissible should have been disallowed. However, it was not done.

(ii) The wealth tax assessments of a Hindu undivided family (specified) for the assessment years 1990-91 to 1992-93 were completed after scrutiny in December 1993. Audit scrutiny revealed that while arriving at the value of interest of HUF in a firm, the assessee claimed and was allowed an exemption of Rs. 6.70 lakh in each of the three assessment years representing cost of a flat which actually was stock in trade of the firm. Since the cost of the flat was stock in trade of the firm, the assessee was not entitled for the above exemption from the value of its interest in the firm. The incorrect exemption allowed thus resulted in underassessment of wealth aggregating Rs. 20.10 lakh with consequent short levy of tax of Rs. 78,120 (including interest)

(iii) Audit scrutiny of income tax assessment records of an individual for the assessment years 1990-91 and 1993-94 revealed that the assessee possessed NRI Bonds worth US \$ 1.30 lakh which were encashed prematurely for Rs. 25 lakh in July 1991 relevant to assessment year 1992-93 and the whole amount was deposited in cumulative deposit account in a Bank on which interest of Rs. 4.36 lakh was received which constituted wealth of the assessee and being in addition to the other wealth of Rs. 25 lakh, was chargeable to wealth tax. However, the assessee did not file return of wealth nor did the department initiate any wealth tax proceedings.

#### 22.8 Short levy of interest

(i) The wealth tax assessments of three individuals for the assessment years 1989-90 to 1992-93 were completed after scrutiny in March 1998 on the basis of return submitted in response to notices issued to the assesseees in December 1996. Returns of wealth submitted originally on various dates between October 1991 and April 1994 in respect of the relevant assessment years were either invalid or non-existent being outside the time limit or net wealth being below taxable limit. Audit scrutiny revealed that while charging interest for belated filing of returns the assessing officer calculated the period of delay from the respective due dates to the date of filing of original invalid returns, instead of upto December 1996 the date of

submission of returns in response to the notices issued. The mistake resulted in short levy of interest aggregating Rs. 2.71 lakh.

(ii) The wealth tax assessment of a company for the assessment year 1994-95 was completed in a summary manner on a net wealth of Rs. 299.38 lakh. Audit scrutiny revealed that the assessee filed the return of wealth belatedly on 29 November 1995 against the specified due date of 30 November 1994 for which assessee was liable to pay interest. The omission resulted in non levy of interest of Rs. 71,832.

(iii) The wealth tax assessment of an individual for assessment years 1982-83 to 1984-85 completed after scrutiny were revised subsequently in on a net wealth aggregating Rs. 133.72 lakh raising demand of Rs. 5.09 lakh. Audit scrutiny revealed that the above demand was paid belatedly by the assessee on 8 May 1996 against the due date in May 1987, May 1988 and May 1989 for the assessment years 1982-83 to 1984-85 respectively for which assessee was liable to pay interest which was not levied. Omission to levy the interest resulted in non levy of interest of Rs. 5.62 lakh.

**PART-V**  
**CHAPTER-23**

**MISTAKES RELATING TO EXPENDITURE TAX**

**23.1 Short levy of expenditure tax**

(i) The expenditure tax assessment of a closely held company running hotel as well as restaurant for the assessment year 1992-93 completed after scrutiny in February 1997 was subsequently revised in November 1997 at chargeable expenditure of Rs. 495.42 lakh consisting of chargeable expenditure of Rs. 462.83 lakh on hotel and Rs. 32.59 lakh on restaurant and tax of Rs. 86.70 lakh was levied. Audit scrutiny revealed that expenditure tax was incorrectly charged at the rate of 20 percent for the period from 1st April 1991 to 30th September 1991 and at 15 percent from 1st October 1991 to 31st March 1992 on the entire amount of expenditure instead of the correct amount of Rs. 97.45 lakh at the rate of 20 percent on Rs. 462.83 lakh and 15 percent of Rs. 32.59 lakh as per provisions of the Act. The mistake resulted in short levy of tax of Rs. 10.76 lakh.

(ii) The expenditure tax assessment of a widely held company, running a hotel, for the assessment year 1992-93 was completed after scrutiny in March, 1997 at chargeable expenditure of Rs. 4138.05 lakh leaving tax of Rs. 814.92 lakh. Audit scrutiny revealed that tax leviable at the prescribed rate worked out to Rs. 827.61 lakh as against Rs. 814.92 lakh levied by the department. The mistake resulted in short levy of tax of Rs. 12.69 lakh.

(iii) The expenditure tax assessments of a widely held company, running a hotel, for the assessment years 1991-92 and 1992-93 were completed after scrutiny in February 1996 and January 1997 at chargeable expenditure of Rs. 3452.22 lakh and Rs. 4684.60 lakh respectively leaving tax of Rs. 684.72 lakh and Rs. 930.36 lakh as returned. Audit scrutiny revealed that the tax leviable correctly worked out to Rs. 690.44 lakh and Rs. 936.92 lakh at the prescribed rate of 20 percent as against the tax of Rs. 684.72 lakh and Rs. 930.36 lakh levied by the department. The mistake resulted in short levy of tax aggregating Rs. 12.29 lakh.

(iv) The expenditure tax assessment of a closely held company, running a hotel for the assessment year 1993-94 was completed after scrutiny in September, 1997 at a chargeable expenditure of Rs. 9.69 lakh and tax of Rs. 19,380 was levied. Audit scrutiny revealed that the assessee had collected expenditure tax of Rs. 1.94 from the customers against total chargeable expenditure of Rs. 9.69 lakh and deposited the amount to the



credit of Government. As such the tax of Rs. 19,380 levied by the department was not in order. The mistake in calculation of tax resulted in short levy of expenditure tax of Rs. 1.74 lakh.

### **23.2 Mistake in computation of chargeable expenditure**

(i) The expenditure tax assessment of a hotel for the assessment year 1993-94 was completed in February 1998. Audit scrutiny revealed that while determining chargeable expenditure a sum of Rs. 47.62 lakh representing "Service charges" was not taken into account. But as per provisions of expenditure tax Act, the said sum was includible in computing chargeable expenditure. Omission to do so resulted in underassessment of Rs. 47.62 lakh leading to short levy of expenditure tax of Rs. 9.52 lakh.

(ii) The expenditure tax assessments of a hotel for the assessment years 1992-93 and 1993-94 were completed in November 1994 determining the chargeable expenditure at Rs. 94.11 lakh and Rs. 19.63 lakh respectively. Audit scrutiny revealed that while determining chargeable expenditure, a sum of Rs. 21.12 lakh and Rs. 5.04 lakh representing property tax, urban land tax, sales tax, additional sales tax, motor vehicle tax and expenditure tax were allowed as deductions. The action of the department was not in order as these taxes did not form part of the gross chargeable expenditure collected from customers and their exclusion was irregular. The irregular allowance of deductions resulted in short levy of expenditure tax aggregating Rs. 7.18 lakh (including interest).

### **23.3 Short levy of expenditure tax due to mistake in calculation**

The expenditure tax assessment of a widely held company for the assessment year 1991-92 and 1993-94 were completed after scrutiny in February 1996 and March 1998 determining chargeable expenditure at Rs. 3490.09 lakh and 9120.19 lakh including Rs. 1.48 lakh for running restaurant respectively. Audit scrutiny revealed that the expenditure tax for the assessment year 1991-92 and 1993-94 would be leviable at Rs. 698.02 lakh and Rs. 1828.96 lakh including Rs. 22,179 for running restaurant respectively instead of Rs. 653.38 lakh and Rs. 1696.25 lakh levied respectively by the department. The mistake resulted in under charge of tax of Rs. 172.35 lakh in aggregate for the two assessment years.

### **23.4 Non initiation of action to bring the chargeable expenditure to tax**

Audit scrutiny of the income tax assessment records of a widely held company, engaged in the business of running an airconditioned restaurant,



for the assessment year 1993-94 revealed that the assessee received an amount of Rs. 59.66 lakh towards sale of food and soft drinks in the air conditioned restaurant during the relevant previous year. In the absence of actual figures of chargeable expenditure for April 1992 and May 1992, proportionate amount of chargeable expenditure worked out Rs. 9.94 lakh on which the assessee was liable to collect and remit to the credit of Central Government expenditure tax @ 15 percent as prescribed in the Act. However, the assessee did not comply with the provisions of the Expenditure Tax Act nor did the department initiate action to bring the chargeable expenditure to tax. The omission resulted in the chargeable expenditure of Rs. 9.94 lakh escaping assessment with consequent non-levy of expenditure tax of Rs. 2.51 lakh (including interest).

### **23.5 Omission of levy interest**

The expenditure tax assessments of a company carrying on hotel business for the assessment years 1991-92 and 1992-93 were completed in February 1996 and December 1996 and the assessment for 1991-92 was revised in June 1996. Audit scrutiny revealed that the assessee hotel collected expenditure tax of Rs. 18.26 lakh and Rs. 17.26 lakh during the relevant previous years and remitted to Government account after a delay of 5 to 9 months and 3 to 16 months relevant to assessment years 1991-92 and 1992-93 respectively attracting the levy of interest. The same was not however, levied. The omission resulted in non-levy of interest aggregating Rs. 5.99 lakh.

**23.6 Non-levy of interest and penalty for failure to pay expenditure tax**

The audit scrutiny of the income tax assessment records of a company for the assessment records of a company for the assessment year 1994-95 completed after scrutiny in January 1997 revealed that expenditure tax to the extent of Rs. 8.67 lakh was collected by the assessee company during the relevant previous year. However, as certified by the Chartered Accountant in Form 3CD the tax collected was not paid to the credit of the Central Government. Moreover, return of expenditure tax was also not filed by the assessee for the assessment year 1994-95. As such the failure to pay the collected tax attracted both interest and penalty under the provisions of the Act. Interest and penalty for failure on the part of the assessee to furnish prescribed return was also leviable. The omission resulted in non-levy of expenditure tax of Rs. 6.74 lakh (including interest and penalty).

**23.7 Mistake in application of rate of expenditure tax**

The expenditure tax assessments of two closely held companies running a hotel for the assessment years 1990-91 and 1991-92 were completed/ revised after scrutiny between March 1995 and March 1996 at chargeable expenditure aggregating Rs. 832.93 lakh and the tax levied aggregated Rs. 83.29 lakh. Audit scrutiny revealed that expenditure tax was incorrectly charged at 10 percent instead of 20 percent of the chargeable expenditure. The mistake resulted in short levy of tax aggregating Rs. 83.29 lakh.

**PART II**

**MINUTES OF THE FORTEENTH SITTING OF THE PUBLIC  
ACCOUNTS COMMITTEE (2002-2003)  
HELD ON 17 DECEMBER, 2002**

The Committee sat from 1500 hrs. to 1700 hrs. on 17 December, 2002 in committee Room "B", Parliament House, New Delhi.

**PRESENT**

Sardar Buta Singh — *Chairman*

**MEMBERS**

*Lok Sabha*

2. Shri Haribhai Chaudhary
3. Shri M.O.H. Farook
4. Shri Bhartruhari Mahtab
5. Shri Chattrapal Singh
6. Shri Brij Bhushan Sharan Singh

*Rajya Sabha*

7. Shri Santosh Bagrodia
8. Shri Prasanta Chatterjee
9. Shri K. Rahman Khan
10. Shri Bachani Lekhraj

**SECRETARIAT**

1. Shri K.V. Rao — *Joint Secretary*
2. Shri Devender Singh — *Deputy Secretary*
3. Shri R.C. Kakkar — *Under Secretary*

**Officers of the Office of C&AG of India**

1. Shri S. Satyamoorthy — *Addl. Dy. CAG of India*
2. Shri S.K. Bahri — *Pr. Director of Audit (INDT)*
3. Shri P. Sesh Kumar — *Pr. Director of Audit (DT)*

**Representatives of the Ministry of Finance (Department of Revenue), RBI  
and DGFT**

1. Shri C.S. Rao — *Secretary (Revenue)*
2. Shri M.K. Zutshi · *Chairman, CBEC*
3. Dr. U.K. Sen · *Member, Customs & Export  
Promotion*

- |                       |   |                           |
|-----------------------|---|---------------------------|
| 4. Shri S.S. Renjhen  | — | Joint Secretary, Drawback |
| 5. Shri L. Mansingh   | — | DGFT                      |
| 6. Shri R.D. Mishra   | — | Addl. DGFT                |
| 7. Dr. Anup K. Pujari | — | Addl. DGFT                |
| 8. Smt. K.J. Udeshi   | — | Executive Director, RBI   |

2. At the outset, the Chairman, PAC welcomed the Members of the Committee.

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3. A copy of the verbatim proceedings of the sitting has been kept on record.

4. After the withdrawal of the witnesses, the Committee took up for consideration and adoption the following three draft reports:

(i)                    \*\*\*                    \*\*\*                    \*\*\*                    \*\*\*                    \*\*\*

(ii) Action Taken on the recommendations contained in 34th Report of PAC (13th Lok Sabha) relating to "Export Incentives and Deductions in respect of Profits retained for Export Business."

(iii)                    \*\*\*                    \*\*\*                    \*\*\*                    \*\*\*                    \*\*\*

5. The Committee adopted the reports without any modification/ amendment.

6. The Committee authorised the Chairman to finalise the draft reports in the light of changes arising out of the factual verification by Audit, if any, and also to present these reports to Parliament.

*The Committee then adjourned.*