

## Chapter IV: Income Tax and Wealth Tax

### 4.1 Introduction

**4.1.1** We referred 137 high value cases pertaining to Income tax involving tax effect of ₹ 286.29 crore to the Ministry of Finance during May 2015 to September 2015 to elicit their comments. In addition, six cases pertaining to Wealth Tax amounting to ₹ 0.18 crore were also sent to the Ministry of Finance during the period.

**4.1.2** The Ministry has conveyed its acceptance in 33 cases involving tax effect of ₹ 106.73 crore (November 2015). In the remaining 110 cases, the Department (ITD) has accepted 22 cases involving tax effect of ₹ 28.38 crore while not accepted one case involving tax effect of ₹ 0.57 crore (referred to in para 2.6.3). ITD did not furnish replies in respect of remaining 87 cases. ITD has completed remedial action in 117 cases out of 143 cases, involving tax effect of ₹ 251.86 crore and initiated remedial action in 17 cases involving tax effect of ₹ 24.67 crore.

**4.1.3** This chapter discusses 137 income tax and six wealth tax cases, of which 136 cases involving undercharge of ₹ 275.47 crore and seven cases involve overcharge of ₹ 11.0 crore. These cases of incorrect assessment point towards weaknesses in the internal controls on the assessment process being exercised by the Income Tax Department.

**4.1.4** The categories of mistakes have been broadly classified as follows:

- i. Quality of assessments
- ii. Administration of tax concessions/exemptions/deductions
- iii. Income escaping assessments due to omissions
- iv. Others-overcharge of tax/interest etc

Table 2.4 (para 2.5.5) of this report shows the details of broad categories of mistakes and their tax effect.

### 4.2 Quality of assessments

**4.2.1** AOs committed errors in the assessments despite clear provisions in the Act. These cases of incorrect assessments point out weaknesses in the internal controls on the part of ITD which need to be addressed. Table 4.1 shows the sub-categories of mistakes (refer *Appendix 2.3*) which impacted the quality of assessments.

Table 4.1: Details of errors in quality of assessment			(₹ in crore)		
Sub-categories	Cases	TE	States		
a. Arithmetical errors in computation of income and tax	16	83.40	Delhi, Gujarat, Kerala, Maharashtra, Punjab, Rajasthan, Uttar Pradesh and West Bengal.		
b. Incorrect application of rates of tax, surcharge etc.	08	26.98	Delhi, Gujarat, Haryana, Maharashtra and Odisha.		
c. Mistakes in levy of interest	29	54.65	Andhra Pradesh, Delhi, Karnataka, Madhya Pradesh, Maharashtra, Tamil Nadu, UT Chandigarh and West Bengal.		
d. Mistake in assessment while giving effect to appellate orders	01	0.15	Bihar.		
<b>Total</b>	<b>54</b>	<b>165.18</b>			

#### 4.2.2 Arithmetical errors in computation of income and tax

We give below five such illustrative cases:

The Income Tax Act, 1961 provides that AO is required to make a correct assessment of the total income or loss of the assessee and determine correct amount of tax or refund, as the case may be.

**4.2.2.1** In Uttar Pradesh, CIT Gorakhpur charge, AO completed the assessment of a cooperative society, **Kisan Sahkari Chini Mills Limited**, for AY 2008-09 after scrutiny in December 2010 at a loss of ₹ 183.21 crore. Audit noticed that while computing the income of the assessee, AO adopted the loss at ₹ 189.40 crore (as per assessee's return of income) instead of admissible loss of ₹ 19.91 crore. The mistake resulted in excess computation of loss of ₹ 169.49 crore having potential tax effect of ₹ 52.37 crore. *ITD rectified the mistake under section 147 (March 2014).*

**4.2.2.2** In Gujarat, CIT-II Surat charge, AO completed the assessment of a Co-operative Society, **Sayan Vibhag Sahakari Khand Udhog Mandali Limited**, for AY 2010-11 after scrutiny in March 2013 at 'nil' income after setting off of business losses to the extent of income. The assessee had claimed and was allowed adjustment under section 145A for excise duty on sale and purchase of raw material along with opening and closing stock of finished goods. Audit scrutiny revealed that the assessee reduced ₹ 36.13 crore towards closing balance instead of adding the same and added ₹ 21.87 crore for opening balance instead of reducing the same. The mistakes resulted in underassessment of income of ₹ 28.51 crore involving potential tax effect of ₹ 8.81 crore. *ITD took remedial action under section 154 (March 2014).*

**4.2.2.3** In Delhi, CIT (Central)-III charge, AO completed the assessment of an individual, **Virendra Jain**, for AY 2006-07 in March 2013 under section 153A read with section 143(3) at an income of ₹ 243.13 crore and a tax of ₹ 78.80 crore thereon. Audit examination revealed that while computing tax demand, the assessed income was considered as ₹ 234.13 crore instead of correct figure of ₹ 243.13 crore. The mistake resulted in short levy of tax of ₹ 5.57 crore including interest. *ITD rectified the mistake under section 154 (March 2014).*

**4.2.2.4** In Delhi, CIT (Central)-I charge, AO completed the assessment of an individual, **Rishu Gupta**, for the AY 2008-09 in March 2013 at an income of ₹ 3.47 crore and a tax of ₹ 0.13 crore thereon. Audit examination revealed that the tax demand was computed at ₹ 0.13 crore instead of the correct amount of ₹ 1.17 crore in the Income Tax Computation Sheet (ITNS-150). The mistake resulted in short levy of tax of ₹ 1.67 crore including interest. *The Ministry accepted the audit observation (October 2015) and rectified the mistake under section 154 in November 2013.*

**4.2.2.5** In Delhi, CIT (Central)-II charge, AO completed the assessments of an individual, **Om Parkash Kukreja**, for the AYs 2006-07 to 2009-10 and AY 2011-12 in March 2014 under section 153(A) read with section 143(3) at incomes of ₹ 3.26 crore, ₹ 0.06 crore, ₹ 0.52 crore, ₹ 0.98 crore and ₹ 0.21 crore respectively. For AY 2012-13, assessment was completed after scrutiny in March 2014 at an income of ₹ 3.03 crore and a tax of ₹ 0.92 crore thereon. For AYs 2006-07 to 2009-10 and 2011-12, business income of the assessee was computed by invoking provisions of section 145(3) of the Act at five *per cent* of the estimated sales that was determined at ₹ 10 crore, ₹ 12 crore, ₹ 13 crore, ₹ 14 crore and ₹ 15 crore in AYs 2006-07 to 2009-10 and AY 2011-12 respectively. Audit examination revealed that the net business income was incorrectly computed as ₹ 0.32 crore instead of correct amount of ₹ 3.2 crore. The mistake resulted in underassessment of income of ₹ 2.88 crore involving short levy of tax of ₹ 1.50 crore including interest. Further, for AY 2012-13, net business income was taken five *per cent* of the estimated sales of ₹ 15.50 crore on the basis of unexplained investment made by the assessee, whereas while computing five *per cent* of estimated sales, net business income was shown at ₹ 0.08 crore instead of correct amount of ₹ 0.78 crore. The mistake resulted in underassessment of income of ₹ 0.70 crore involving short levy of tax of ₹ 0.27 crore including interest. Total short levy of tax for all the AYs amounts to ₹ 1.77 crore including interest. *The Ministry accepted the audit observation (October 2015) and rectified the mistakes under section 154 in September 2014.*

### 4.2.3 Incorrect application of rates of tax and surcharge

We give below four such illustrative cases:

Income tax including surcharge shall be charged at the rates prescribed in the relevant Finance Act.

**4.2.3.1** In Delhi, CIT (Central)-I charge, AO completed the assessment of an individual, **Sanjay Kumar Singh**, for AY 2011-12 under section 144 in March 2013 at an income of ₹ 47.42 crore. Audit examination revealed that while computing tax demand, amount of ₹ 1.42 crore was levied as surcharge (at the rate of 10 *per cent*) on applicable tax although there was no provision for levy of surcharge on income tax in the assessment year 2011-12. Further, in the Income Tax computation sheet, the figure of total tax demand was mentioned as ₹ 2.11 crore instead of correct figure of ₹ 21.09 crore, after adding interest under sections 234A and 234B of ₹ 1.45 crore and ₹ 3.54 crore respectively to the tax. The mistakes resulted in short levy of tax of ₹ 17.36 crore including interest. *The Ministry accepted the audit observation (October 2015) and rectified the mistake under section 154 in November 2013.*

Section 167B(2)(ii) of the Income Tax Act, 1961, provides that any member or members thereof is or are chargeable to tax at a rate or rates which is or are higher than the maximum marginal rate, tax shall be charged on that portion or portions of the total income of the association or body which is or are relatable to the share or shares of such member or members at such higher rate or rates, as the case may be, and the balance of the total income of the association or body shall be taxed at the maximum marginal rate

**4.2.3.2** In Odisha, CIT Bhubaneswar charge, AO completed the assessment of an AOP, **HCIL Adhikari ARSS (JV)**, for AY 2010-11 under scrutiny in March 2013 at an income of ₹ 94.23 crore. Audit scrutiny revealed that the assessee was a joint venture of three companies. Out of three member partners, M/s. Pt. Adhi Karya (Persero) Tbk, holding 30 *per cent* of equity participation, was an Indonesian Company. Thus, 30 *per cent* of the assessed income of ₹ 94.23 crore was required to be taxed at the rate of 42.23 *per cent* applicable for the year under consideration instead of at the maximum marginal rate of 33.99 *per cent* levied by the AO. Omission to do so resulted in short levy of tax including interest of ₹ 7.46 crore. *ITD intimated that the action has been initiated by issue of notice under section 148 (July 2014).*

**4.2.3.3** In Gujarat, CIT-III Ahmedabad charge, AO completed the assessment of HUF, **Balkrishna P. Trivedi**, for AY 2008-09 after scrutiny at returned income of ₹ 0.79 crore in September 2010. The assessment was revised under section 143(3) read with section 263 at an income of ₹ 3.92 crore including short term capital gain of ₹ 3.81 crore in March 2014. Audit scrutiny revealed that tax on short term capital gain was levied at the rate of 20 *per cent* instead of normal rate of 30 *per cent*. The mistake resulted in short levy of tax ₹ 0.56 crore including interest. *ITD took remedial action under section 154 (August 2014).*

**4.2.3.4** In Delhi, CIT (Central)-I charge, AO completed the assessment of an individual, **Rama Jain**, for AY 2009-10 in March 2013 under section 153C read with section 144 determining income of ₹ 4.46 crore. Audit examination revealed that while computing tax demand, surcharge leviable at the rate of 10 *per cent* was not levied by the department. The omission resulted in short levy of tax of ₹ 0.24 crore including interest. *The Ministry accepted the audit observation (October 2015) and rectified the mistake under section 154 in November 2013.*

#### **4.2.4 Mistakes in levy of Interest**

We give below four such illustrative cases:

The Income Tax Act, 1961 provides for levy of interest for different omissions on the part of the assessee at the rates prescribed by the Government from time to time.

**4.2.4.1** In Maharashtra, CIT (Central)-I Mumbai charge, AO completed the assessment of an individual, **Atul Amritlal Sanghvi**, for AY 2007-08 under section 153B(1) read with section 143(3) in December 2008 at an income of ₹ 310.11 crore which was later revised at ₹ 331.07 crore in December 2011 at the direction of Commissioner of Income Tax. Audit examination revealed that AO did not levy interest under section 234A despite the fact that assessee had filed its return of income belatedly in February 2008 instead of due date of filing of return in July 2007. The omission resulted in non levy of interest of ₹ 7.80 crore under section 234A. *The Ministry accepted the audit observation (October 2015) and rectified the mistake under section 154 in March 2015.*

**4.2.4.2** In Uttar Pradesh, CIT (Central) Kanpur charge, AO completed the assessments of an individual, **Sandeep Kumar**, for AYs 2010-11 and 2011-12 under section 153A/144 in March 2013 at an income of ₹ 96.45 crore and ₹ 90.50 crore respectively. Although the assessee had not filed the return of income, no interest was levied by the department under section 234A. The omission resulted in short levy of tax of ₹ 7.08 crore. *ITD rectified the mistake under section 154/144.*

**4.2.4.3** In Madhya Pradesh CIT (Central) Bhopal Charge, AO completed the assessment of an individual, **Mukesh Sangla**, for AYs 2010-11 and 2011-12 under section 153A/143(3) in March 2014 at income of ₹ 34.47 crore and ₹ 25.01 crore respectively. Audit examination revealed that the ITD levied interest under section 234B at ₹ 2.10 crore and ₹ 0.92 crore instead of correct amount of ₹ 3.25 crore and ₹ 2.76 crore for AYs 2010-11 and 2011-12 respectively. The mistakes resulted in short levy of interest of ₹ 2.99 crore. *ITD rectified the mistake under section 154 (November 2014).*

**4.2.4.4** In Andhra Pradesh, CIT (Central) charge, AO completed the assessment of an individual, **Raghu Rama Krishna Raju**, for assessment year 2010-11 under section 143(3) read with section 153A in March 2014 at an income of ₹ 32.11 crore. Audit scrutiny revealed that interest under section 234A and 234B was short levied to the tune of ₹ 2.47 crore. *ITD accepted and rectified the mistake under section 154 (January 2015).*

### 4.3 Administration of tax concessions/exemptions/deductions

**4.3.1** The Act allows concessions/exemptions/deductions to the assessee in computing total income under Chapter VI-A and for certain categories of expenditure under its relevant provisions. We observed that the assessing officers have irregularly extended benefits of tax concessions/exemptions/deductions to beneficiaries that are not entitled to them. These cases point out weaknesses in the administration of tax concessions/deductions/exemptions on the part of ITD which need to be addressed. Table 4.2 shows the sub-categories which have impacted the Administration of tax concessions/exemptions/deductions.

Table 4.2: Sub-categories of mistakes under Administration of tax concessions/exemptions/deductions				(₹ in crore)
Sub-categories	Nos.	TE	States	
a. Irregular exemptions/deductions/relief given to individuals	7	2.64	Karnataka, Kerala, Maharashtra, Rajasthan, Tamil Nadu, UT Chandigarh and Uttarakhand.	
b. Irregular exemptions/deductions/relief given to Trusts/Firms/Societies/AOPs	8	16.05	Andhra Pradesh, Bihar, Delhi, Gujarat, Tamil Nadu, Uttar Pradesh and West Bengal.	
c. Incorrect allowance of Business Expenditure	23	60.79	Gujarat, Haryana, Jammu & Kashmir, Karnataka, Maharashtra, Odisha, Tamil Nadu, UT Chandigarh, Uttar Pradesh and West Bengal.	
d. Irregularities in allowing depreciation/business losses/capital losses	11	13.70	Bihar, Delhi, Gujarat, Maharashtra and West Bengal.	
<b>Total</b>	<b>49</b>	<b>93.18</b>		

### 4.3.2 Irregular exemptions/deductions/relief to Individuals

We give below one such illustrative case.

Under Section 80IB(10) of the Income Tax Act, 1961, where the gross total income of an assessee includes any profits and gains derived from developing and building housing projects, hundred percent of the profits derived in the previous year relevant to AY from such housing project shall be allowed as deduction in computing the total income subject to the condition, inter alia, that the project is on the size of a plot of land which has a minimum area of one acre.

**4.3.2.1** In Kerala, CIT Kozhikode charge, AO completed the assessment of an individual, **P. V. Hemalatha**, for AY 2009-10 after scrutiny in November 2011 at an income of ₹ 0.25 crore and agricultural income of ₹ 0.05 lakh after allowing a deduction of ₹ 3.13 crore under section 80IB(10) in respect of a housing project at Katchery village, Kozhikode. Audit scrutiny revealed that the project was completed in October 2008 on a plot of land measuring only 70.57 cents. As the project was on a plot of land having an area of less than one acre, the assessee was not eligible for deduction under section 80IB(10). The irregular deduction of ₹ 3.13 crore allowed to the assessee has resulted in short levy of tax amounting to ₹ 1.41 crore including interest. *ITD took remedial action under section 143(3) read with section 263 (March 2015).*

### 4.3.3 Irregular exemptions/deductions/relief to Trusts/Firms/Societies/AOPs

We give below four such illustrative cases.

Section 37(1) of the Income Tax Act, 1961 provides that any expenditure (not being expenditure of the nature described in sections 30 to 36 and not being in the nature of capital expenditure or personal expenses of the assessee), laid out or expended wholly and exclusively for the purposes of business or profession shall be allowed in computing the income chargeable under the head Profits and gains of business or profession. Further, Section 36(1)(iv) provides that any sum paid by the assessee as an employer by way of contribution towards a recognized provident fund or an approved superannuation fund, shall be allowed as deduction

**4.3.3.1** In Tamil Nadu, CIT 1 Madurai charge, AO completed the income tax assessments of **Tuticorin Port Trust** for AYs 2009-10 and 2010-11 after scrutiny in December 2011 and March 2013 at a total income of ₹ 94.15 crore and ₹ 95.75 crore respectively. Audit scrutiny revealed that amount of ₹ 15.50 crore and ₹ 15.00 crore were debited towards contribution to pension and gratuity fund, apart from the amount of ₹ 12.61 crore and ₹ 15.78 crore towards pension payments in the Profit and Loss Account for FYs 2008-09 and 2009-10 respectively (relevant to AYs 2009-10 and 2010-11). As the payments for pension and gratuity are charged

to respective fund, the payments of ₹ 12.61 crore and ₹ 15.78 crore towards pension should not have been debited to the Profit & Loss Accounts. Further, the claim of contribution towards the Pension Fund is admissible under section 36(1)(iv) and hence it cannot be reclaimed under section 37. Therefore, expenditure of pension payments amounting to ₹ 12.61 crore and ₹ 15.78 crore was required to be disallowed and added back to income of the AYs 2009-10 and 2010-11 respectively. Omission to do so resulted in under assessment of income by an equal amounts involving aggregate tax effect of ₹ 9.16 crore. *ITD informed that remedial action under section 263 has been initiated for the AY 2010-11 and AO has been directed to invoke section 147 for AY 2009-10 (May 2015).*

Section 10B of the Income Tax Act, 1961, provides that a deduction of such profits and gains as are derived by a hundred *per cent* export-oriented undertaking from the export of articles or things or computer software for a period of 10 consecutive assessment years beginning with the assessment year relevant to the previous year in which the undertaking begins to manufacture or produce articles or things or computer software, as the case may be, shall be allowed from the total income

**4.3.3.2** In Uttar Pradesh, CIT 1 Kanpur charge, AO while completing the assessment of a partnership firm, **Mehra Brothers**, for AY 2011-12 after scrutiny in March 2014 at an income of ₹ 35.38 lakh, extended the benefit of deduction of profit of ₹ 4.62 crore for the 11<sup>th</sup> consecutive assessment year i.e. beyond permissible limit of 10 years (AY 2001-02 to AY 2010-11). The mistake resulted in underassessment of income of ₹ 4.62 crore involving tax effect of ₹ 1.94 crore including interest. *ITD informed that it had initiated action under section 263 (May 2015).* During the course of proceedings under section 263, assessee had surrendered the amount of ₹ 4.66 crore and deposited tax challans for AY 2011-12 (May 2015).

**4.3.3.3** In Andhra Pradesh, DIT(Exemptions) Hyderabad charge, AO completed the assessment of an assessee, **National Academy of Construction**, for AY 2009-10 after scrutiny in December 2011 at an income of ₹ 23.76 crore. Audit scrutiny revealed that the assessee debited an amount of ₹ 3.04 crore (₹ 0.92 crore pertaining to the year 2006-07 and ₹ 2.12 crore pertaining to the year 2007-08) towards income tax. Since the income tax paid cannot be treated and allowed as expenditure, the same should have been added back to income and brought to tax. The omission resulted in short computation of income of like amount with a consequential short demand of ₹ 1.31 crore including interest. *ITD rectified the mistake under section 143(3) read with section 147 (March 2014).*

As per sub-section (1) of section 10 of the Income Tax Act, 1961 in computing the total income of a year of any person, any income falling within the agricultural income would not be included in the total income of the assessee. Further in cases where Rule 8 of the Income Tax Rules, 1962, relating to the special case of manufacture of tea applies, the income derived from the sale of tea grown and manufactured by the seller in India shall be computed as it were income derived from business, and forty per cent of such income shall be deemed to be income liable to tax.

**4.3.3.4** In West Bengal, Pr. CIT-XII, Kolkata charge AO completed the assessment of a firm, **Atmaram & Company**, for AY 2012-13 after scrutiny in March 2014 at an income of ₹ 2.74 crore. The assessee was engaged in business of cultivation and manufacturing of tea and had offered 40 per cent of balance of profit as taxable income. Audit examination revealed that the assessee, during the year produced and sold a total of 33.07 lakh Kg of tea and shown balance of profit at ₹ 5.97 crore. Out of total quantity of tea sold during the year, 14.43 lakh Kg of Tea was manufactured out of green tea leaves purchased and not grown by the assessee. Hence, 100 per cent of proportionate profit of ₹ 2.60 crore derived from sale of tea manufactured out of green leaves purchased by the assessee is not entitled for benefit under rule 8 of the Income Tax Rule and therefore, entire profit there from should have been taxed as business income. Omission resulted in underassessment of income of ₹ 1.56 crore (60 per cent of ₹ 2.60 crore) involving tax effect of ₹ 59.89 lakh including interest. *The Ministry accepted the audit observation (August 2015) and taken remedial action under section 147 in January 2015.*

#### **4.3.4 Incorrect allowance of Business Expenditure**

We give below four such illustrative cases.

As per provisions of the Income Tax Act, 1961, AOs have to determine and assess the income correctly in scrutiny assessment. CBDT has also issued instructions from time to time to AOs and their supervising officers to ensure that mistake in scrutiny assessment do not occur.

**4.3.4.1** In Tamil Nadu, CIT 1 Chennai charge, AO completed the assessment of **Tamil Nadu Co-operative State Land Development Bank Limited** for AY 2009-10 after scrutiny in December 2011 at an income of ₹ 1.97 crore. Audit scrutiny revealed that a sum of ₹ 140.24 crore was debited towards 'provision for difference in SARDB FS Waiver blocked in downsizing' in the Profit and Loss Account. Since, the above sum was only a provision towards a non-statutory reserve, the same is not an admissible expenditure. Omission to disallow the same resulted in under assessment of income of ₹ 140.24 crore with consequential short levy of tax of ₹ 47.67 crore. *The Ministry accepted the audit observation (November 2015) and taken the remedial action under section 143(3) read with section 147 in March 2013.*

**4.3.4.2** In Haryana, CIT Panchkula charge, AO completed the assessment of **Haryana State Cooperative Apex Bank Limited** for the AY 2009-10 in December 2011 at an income of ₹ 12.35 crore. Audit examination revealed that amount of ₹ 3.01 crore (charged at 3 per cent of opening balance of Agricultural Credit Stabilization Fund ₹ 100.29 crore) was credited to Agricultural Credit Stabilization Fund of the Bank. The said amount was included in expenditure on account of interest paid by the bank and reflected as addition to Agricultural Credit Stabilization Fund which is a part of reserve and surplus. As addition to reserve and surplus is an appropriation to profit and not a charge to profit and loss account, it was required to be added back to the taxable income. Omission to do so resulted in under assessment of income of ₹ 3.01 crore involving short levy of tax of ₹ 1.24 crore. *The Ministry accepted the audit observation (November 2015) and taken remedial action under section 143(3) read with section 147 in July 2014.*

Section 43 B of the Income Tax Act, 1961 provides for deduction towards certain expenditure only when the same has actually been paid in the previous year on or before the due date of filing return of income

**4.3.4.3** In Uttar Pradesh, CIT Meerut charge, AO while completing the assessment of a Co-operative Society, **Ramala Sahkari Chini Mills Limited**, for AY 2008-09 after scrutiny in December 2010 at a loss of ₹ 1.83 crore, allowed ₹ 3.64 crore on account of interest accrued and due but not paid. As the amount was not deposited into the Government account till the due date of filing of return of income, the same should have been disallowed. Omission to do so resulted in positive tax effect of ₹ 36.17 lakh and potential tax effect of ₹ 85.13 lakh. *The Ministry accepted the audit observation (November 2015) and taken the remedial action under section 147 read with section 143(3) in March 2013.*

**4.3.4.4** In Odisha, CIT Cuttack charge, AO completed the assessment of an assessee, **The Cuttack Development Authority**, for AY 2009-10 after scrutiny in November 2011 at 'Nil' income after setting off of brought forward losses. Audit scrutiny revealed that the assessee had debited ₹ 3.50 crore in its Profit & Loss account towards land premium which is in the nature of Capital expenditure. The allowance of inadmissible expenditure resulted in under assessment of income to the extent of ₹ 3.50 crore involving potential tax effect of ₹ 1.18 crore. *ITD accepted and rectified the mistake under section 263/143(3) (March 2015).*

#### 4.3.5 Irregularities in allowing depreciation/business losses/capital losses

We give below two such illustrative cases:

As per the Rule 5 of Income Tax Rules, 1962, the allowance under clause (ii) of sub section (1) of Section 32, depreciation on any block of assets shall be calculated at the percentages specified in Appendix-I of Income Tax Rules on the written down value of such block of assets as are used for the purposes of the business or profession of the assessee at any time during the previous year. Further, the rate of depreciation of Buildings other than those used for mainly residential purposes is 10 *per cent* and such Buildings includes roads, bridges, culverts, wells and tube-wells (notes 1 below new Appendix-I of Income Tax Rules, 1962.)

**4.3.5.1** In West Bengal, Pr. CIT-IX Kolkata Charge, AO completed the assessment of a local authority, **Haldia Development Authority**, for AY 2010-11 after scrutiny in March 2013 determining net loss of ₹ 46.11 crore. Audit noticed that the assessee was allowed depreciation of ₹ 57.02 crore which included depreciation of ₹ 17.29 crore on roads. It was further observed that the rate of depreciation allowed on the roads was 100 *per cent* instead of allowable rate of 10 *per cent*. The mistake resulted in excess allowance of depreciation of ₹ 15.56 crore involving potential tax effect of ₹ 4.81 crore. *ITD's reply is awaited (November 2015).*

As per section 72 of Income Tax Act, 1961 no loss under the head 'business income' shall be allowed to be carried forward and set off against business income of future years, unless the return of loss is filed on or before the due date. Further, section 2(11) provides for 13 block of assets on which depreciation is allowable as per the provisions in the Act. Land is not covered in any of the blocks of assets and is therefore not eligible for allowance of depreciation.

**4.3.5.2** In Bihar, CIT I Patna charge, the scrutiny assessment of a Local Authority, **Bihar Industrial Area Development Authority Patna**, for the AY 2011-12 was completed in March 2014 at a loss of ₹ 8.12 crore including unabsorbed depreciation of ₹ 1.03 crore. Audit examination revealed that return of income for the AY 2011-12 was filed on 26 March 2012 as against the due date on 30 September 2011 for furnishing the return of income under section 139(1). As such, the income of the assessee should have been determined at nil and the business loss of ₹ 7.09 crore should not have been allowed to be carried forward. It was further noticed that the assessee had claimed and was allowed depreciation of ₹ 50.31 lakh on land development, land acquisition and area development which was not allowable. The mistakes resulted in incorrect allowance of carry forward of business loss of ₹ 7.09 crore and depreciation loss of ₹ 50.31 lakh with consequent potential tax effect of ₹ 2.35 crore. *ITD has accepted (September 2014) the audit observation and stated that remedial action has been initiated.*

#### 4.4 Income escaping assessments due to omissions

**4.4.1** The Act provides that the total income of a person for any previous year shall include all incomes from whatever source derived, actually received or accrued or deemed to be received or accrued. We observed that the assessing officers did not assess/under assessed total income that was required to be offered to tax. There were also omissions in implementing TDS/TCS provisions which led to escapement of tax. Table 4.3 shows the sub-categories which have resulted in income escaping assessments.

Table 4.3: Sub-categories of mistakes under income escaping assessments (₹ in crore) due to omissions			
Sub-categories	Nos.	TE	States
a. Incorrect classification and computation of capital gains	03	1.41	Gujarat, Karnataka and Rajasthan.
b. Incorrect computation of income	13	10.26	Assam, Bihar, Chhattisgarh, Gujarat, Jharkhand, Maharashtra, Rajasthan, Uttar Pradesh and Uttarakhand.
c. Omissions in implementing provisions of TDS/TCS	05	2.88	Gujarat, Jharkhand and West Bengal.
d. Unexplained Investment/cash credit	06	2.38	Chhattisgarh, Gujarat, Rajasthan and West Bengal.
e. Non-levy/short levy of Wealth Tax	06	0.18	Gujarat, Karnataka, Maharashtra and West Bengal.
<b>Total</b>	<b>33</b>	<b>17.11</b>	

#### 4.4.2 Incorrect classification and computation of Capital Gain

We give below one such illustrative case.

**4.4.2.1** In Gujarat, Pr. CIT IV Ahmedabad Charge, AO completed the assessment of an Individual, **Mayur Mukundbhai Desai**, for AY 2009-10 after scrutiny in November 2011 at an income of ₹ 0.69 crore and further revised it at ₹ 0.66 crore under section 250 in June 2012. The assessee claimed exempted income of long term capital gain (LTCG) of ₹ 2.32 crore on sale of shares under section 10(36) and adjusted short term capital loss (STCL) of ₹ 0.67 crore on sale of shares from the total income under different heads of income. Audit scrutiny revealed that these shares were not exhibited as investment, as admitted by assessee himself and hence the share transactions claimed as LTCG and STCL were required to be treated as business income and taxed accordingly. Omission to do so resulted in short levy of tax of ₹ 0.97 crore including interest and potential tax of ₹ 0.23 crore. *ITD took remedial action under section 143 read with section 147 (March 2015).*

#### 4.4.3 Incorrect computation of income

We give below four such illustrative cases:

Section 143(3) provides that AOs have to determine and assess the income correctly. Different types of claims together with accounts, records and all documents enclosed with the return are required to be examined in detail in scrutiny assessments. CBDT has also issued instructions from time to time in this regard.

**4.4.3.1** In Uttar Pradesh, CIT Ghaziabad charge, AO completed the assessment of AOP, **Ghaziabad Development Authority**, for AY 2009-10 after scrutiny in December 2011 at a loss of ₹ 133.17 crore. Audit noticed that though the assessee had provided interest bearing loan of ₹ 51.71 crore to Hapur Pilkhuwa Development Authority (HPDA) in March 2008, interest accrued thereon was not offered as income. The omission to add back the interest income resulted in excess assessment of loss of ₹ 5.80 crore involving potential tax effect of ₹ 1.96 crore. *ITD rectified the mistake under section 263/143(3) (March 2015).*

**4.4.3.2** In Jharkhand, CIT Ranchi charge, the scrutiny assessment of a firm, **Jharkhand Trading Company**, for the assessment year 2010-11 was completed in December 2012 at an income of ₹ 3.82 lakh. Audit examination revealed that the total purchase made by the firm was shown as ₹ 29.12 crore as per the Profit and Loss account for FY 2009-10, whereas the purchase ledger of the assessee's depot included purchases of ₹ 32.75 crore. The difference of ₹ 3.63 crore in the purchase amount was not considered in the scrutiny assessment, resulting in under assessment of income by equal amount involving short levy of tax of ₹ 1.49 crore including interest. *The Ministry accepted the audit observation (November 2015) and taken the remedial action under section 147 in May 2015.*

As per provision of section 28 of Income Tax Act, 1961 the profits and gains derived from any business or profession carried on by the assessee at any time during the previous year shall be chargeable to income tax under the head 'profits or gains of business or profession. Further, as per provisions of section 40A(3), where the assessee incurs any expenditure in respect of which a payments or aggregate of payments made to a person in a day otherwise than by an account payee cheque drawn on a bank or account payee bank draft, exceeds ₹ 20,000, no deduction shall be allowed in respect of such expenditure.

**4.4.3.3** In Chhattisgarh CIT Raipur charge, AO completed the assessment of an individual, **Atul Kumar Sinha**, for AY 2008-09 after scrutiny in October 2010 at an income of ₹ 0.09 crore. Audit examination revealed that the assessee had shown gross receipts of ₹ 0.40 crore in Profit and Loss Account whereas total receipts as per computation of income were shown at

₹ 2.28 crore. Further, the assessee had made a payment of ₹ 0.45 lakh to 'Rahul Communication' in cash, however, the department did not add this amount to the income of assessee. The mistakes resulted in underassessment of income of ₹ 1.88 crore involving short levy of tax of ₹ 0.81 crore including interest. *ITD rectified the mistake under section 147 (March 2014).*

**4.4.3.4** In Uttarakhand, CIT Haldwani charge, AO completed the assessment of an individual, **Sanjay Kumar Chauhan**, for AY 2010-11 after scrutiny in April 2012 at an income of ₹ 0.13 crore. Audit examination revealed that though the assessee was following mercantile system of accounting, he had accounted for contract receipts of ₹ 3.07 crore in his profit and loss account as against ₹ 3.92 crore as per the ledger accounts. The omission resulted in underassessment of income of ₹ 0.85 crore involving short levy of tax of ₹ 0.33 crore. *ITD initiated remedial action under section 148 (March 2015).*

#### **4.4.4 Omissions in implementing provisions of TDS/TCS**

We give below two such illustrative cases.

Section 40(a)(ia) provides that deduction of expenditure towards payments where TDS has not been deducted or after deduction, has not been paid on or before due date, shall not be allowed.

**4.4.4.1** In Jharkhand, CIT-Ranchi charge, the scrutiny assessment of an individual, **Om Prakash Singh**, for AY 2010-11 was completed in December 2012 at an income of ₹ 0.58 crore. Audit examination revealed that AO allowed payment of ₹ 4.65 crore made to the sub-contractor on which tax was not deducted at source. As tax had not been deducted, the payment of ₹ 4.65 crore was required to be disallowed. Omission to do so resulted in underassessment of income of ₹ 4.65 crore involving tax effect of ₹ 1.86 crore including interest. *ITD accepted (January 2015) the audit observation and stated that remedial action has been taken under section 147.*

**4.4.4.2** In West Bengal, CIT-Burdwan Kolkata charge, the assessment of an individual, **Bishnu Ghosh**, for AY 2008-09 was completed after scrutiny in December 2010 determining income of ₹ 9.13 lakh. Audit observed that the AO allowed payment of ₹ 0.69 crore towards 'Labour charges and Job Works' on which tax was deducted but was not deposited within the due date of filing return for the assessment year. As tax had not been deposited within the due date, the payment of ₹ 0.69 crore was required to be disallowed. Omission to do so resulted in underassessment of income of ₹ 0.69 crore

involving tax effect of ₹ 0.31 crore including interest. *ITD rectified the mistake under section 263 (January 2014).*

#### 4.4.5 Unexplained Investment

We give below one such illustrative case.

**4.4.5.1** In West Bengal, CIT (Central) XXV Kolkata charge, AO completed the assessment of an individual, **Madan Mohan Chowdhury**, for AY 2008-09 under 144 in December 2010 at an income of ₹ 1.91 crore, which was further revised under section 263 read with section 144 in December 2011 at an income of ₹ 4.82 lakh. Audit scrutiny revealed that in the original assessment, AO added an amount of ₹ 1.86 crore on account of unexplained cash deposit. It was further observed that the said assessment order was set aside by passing order under section 263 with the direction to the assessing officer to frame a fresh assessment after conducting proper enquiry and also by giving proper and reasonable opportunity to the assessee of being heard. Audit noticed that the department deleted the addition of unexplained cash credit of ₹ 1.86 crore and only added an amount of ₹ 3.72 lakh as commission income, though the department did not receive any new facts or information either from the assessee or the beneficiaries of the unexplained cash credits. Omission to include the income from unexplained sources resulted in income escaping assessment of ₹ 1.86 crore involving tax effect of ₹ 0.92 crore. *ITD rectified the mistake under section 147 (November 2014).*

#### 4.4.6 Non-levy/short levy of Wealth Tax

Six cases of wealth tax involving tax effect of ₹ 0.18 crore were reported to the Ministry during May 2015 to September 2015. We found that AO did not comply with CBDT's instructions<sup>51</sup> in these cases in Gujarat, Karnataka, Maharashtra and West Bengal. We give below one such illustrative case:

**4.4.6.1** In Karnataka, CIT III Bangalore charge, AO completed the income tax scrutiny assessment of an Individual, **Lohit Puneet Rajkumar**, for AY 2010-11 in November 2012. Audit scrutiny of the Income tax assessment records revealed that the assessee had a net wealth (immovable and movable assets) of ₹ 4.05 crore for the assessment years 2010-11. However, the assessee neither filed the return nor the department initiated any wealth tax assessment proceedings. The omission resulted escapement of wealth of ₹ 4.05 crore with a consequential tax effect of ₹ 3.75 lakh. *The assessee filed the return (May 2014), and the assessment was concluded (October 2014) accepting the net wealth returned under section 17 read with section 16(3)*

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51 CBDT's instructions issued to the AOs in November 1973, April 1979 and September 1984.

raising a demand of ₹ 4.18 lakh and the same was paid by the assessee (May 2014).

#### 4.5 Over charge of tax/Interest

**4.5.1** We noticed over assessment of income in seven cases involving overcharge of tax/interest of ₹ 11.0 crore in Delhi, Gujarat, Haryana, Odisha, Punjab and UT Chandigarh. We give below two such illustrative cases.

**4.5.1.1** In Delhi CIT (Central)-I Charge, assessment of an individual, **Sanjay Kumar**, for AY 2010-11 was completed in March 2013 at an income of ₹ 89.54 crore and a tax of ₹ 30.42 crore thereon. Audit noticed that, an amount of ₹ 2.69 crore was levied as surcharge on applicable tax despite the fact that there was no provision for levy of surcharge on income tax for the assessment year 2010-11. The mistake resulted in over charge of tax of ₹ 4.04 crore including interest. *ITD accepted and rectified the mistake under section 154 (November 2013).*

**4.5.1.2** In Haryana, CIT Central Gurgaon charge, the assessment in the case of **Swami Devi Dyal Hi Tech Educational Academy**, for AYs 2008-09 and 2009-10 was completed in July 2011 under section 153A(1)(b) read with section 143(3). Subsequently, while giving appeal effect, the taxable income was revised to ₹ 23.37 crore for the assessment year 2008-09 and ₹ 18.21 crore for the assessment year 2009-10. Audit examination revealed that although assessment was completed by treating the assessee as AOP, tax demand was calculated at the rates applicable to society. The mistakes in application of incorrect rates of tax resulted in overcharge of tax and interest amounting to ₹ 3.03 crore (₹ 1.91 crore for AY 2008-09 and ₹ 1.12 crore for AY 2009-10). *The Ministry accepted the audit observations (November 2015) and rectified the mistakes under section 154 for both AYs in December 2014.*