Chapter IV: Income Tax

4.1 Introduction

4.1.1 This chapter discusses the result of audit of assessments related to income tax audited during 2017-18. A total of 4,36,89,274 income tax returns[88] were filed by non-corporate assessees during the FY 2016-17. ITD completed a total of 2,61,535 non-corporate scrutiny assessments in FY 2016-17 or in earlier years in those units which were audited during audit plan of 2017-18. Out of the 2,61,535 non-corporate scrutiny assessments, we checked 2,13,838 non-corporate scrutiny cases and found mistakes in 12,128 assessments. The incidence of errors in non-corporate scrutiny assessments checked in audit during 2017-18 was 5.67 *per cent*. The nature of the errors points to manual override of the AST. The department needs to investigate such errors and take action as per law against the officials concerned.

4.1.2 A total of 132 high value income tax cases were referred to the Ministry during April 2018 to October 2018. Of these, 123 cases involve undercharge of ₹ 320.94 crore and nine cases involving overcharge of ₹ 10.12 crore. These cases of incorrect assessment point towards weaknesses in the internal controls in the assessment processes of the ITD. Such errors have been continually pointed out in earlier audit reports as well. ITD may ascertain whether the instances of irregularities noticed are errors of omission or commission while ensuring necessary action as per law in cases involving errors of commission.

4.1.3 The categories of mistakes have been broadly classified as follows:

- Quality of assessments
- Administration of tax concessions/exemptions/deductions
- Income escaping assessments due to omissions
- Others-Overcharge of tax/interest etc.

The deficiency noticed in the Assessment Information System (AST) module/ Income Tax Business Applications (ITBA) with respect to computation of interest under sections 234A, 234B, 234C and 244A of the Income Tax Act, 1961 has been brought out in Para 4.2.4 of this Chapter. Table 2.10 (para 2.4.4) of this report shows the details of broad categories of mistakes in assessments and their tax effect. ITD needs to inquire into the reasons for errors in computation of interest through AST and reasons for allowing manual modification to co-exist with IT system particularly without approval

[88] Source: Pr. Directorate General of Income Tax (Admn. & Tax Payers Services), Research & Statistics Wing

of higher authority. The deficiency in the AST needs to be eliminated to ensure accuracy of tax demand generated through system.

4.1.4 The Ministry has conveyed its acceptance in 71 cases involving tax effect (TE) of ₹ 142.59 crore. The Ministry has not accepted one case involving tax effect of ₹ 1.0 crore. In the remaining 60 cases, the ITD has accepted nine cases involving tax effect of ₹ 56.95 crore while not accepting one case involving tax effect of ₹ 0.30 crore (referred to in para 2.4.4 of this report). Out of 132 cases, ITD has completed remedial action in 102 cases involving tax effect of ₹ 213.56 crore and initiated remedial action in 14 cases involving tax effect of ₹ 51.48 crore.

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 to continuing weaknesses in the internal controls on the part of ITD which need to be addressed on priority. Assessing Officers (AOs) committed errors in the assessments ignoring clear provisions in the Act. The cases of incorrect assessments involving arithmetical errors in computation of income and tax are difficult to accept as mere errors, in the days of calculators and computers. Further, application of incorrect rates of tax and surcharge, mistakes in levy of interest, excess or irregular refunds etc. point to either incompetence, or mischief, as well as weaknesses in the internal controls in ITD which need to be addressed. ITD may ascertain whether the instances of irregularities noticed are errors of omission or commission while ensuring necessary action as per law in cases involving errors of commission.

Table 4.1 shows the sub-categories of mistakes 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	14	52.03	Delhi, Gujarat, Himachal Pradesh, Karnataka, Madhya Pradesh, Maharashtra, Odisha and Uttar Pradesh
b. Incorrect application of rates of tax, surcharge etc.	24	163.66	Andhra Pradesh, Gujarat, Haryana, Karnataka, Kerala, Maharashtra, Odisha, Punjab, Tamil Nadu and Uttar Pradesh
c. Mistakes in levy of interest	47	60.84	Andhra Pradesh, Delhi, Gujarat, Haryana, Karnataka, Maharashtra, Odisha, Punjab, Tamil Nadu, UT Chandigarh, Uttar Pradesh and West Bengal
Total	**85**	**276.53**	

4.2.2 Arithmetical errors in computation of income and tax

We give below two such illustrative cases

The Income Tax Act, 1961 provides that Assessing Officer (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 Maharashtra, CIT (Exemptions) Mumbai charge, AO completed the assessment of an AOP for AY 2013-14 after scrutiny in March 2016 at a loss at ₹ 255.78 crore. Audit examination revealed that, AO, in the assessment order, had made an addition of ₹ 111.39 crore on account of 'provision made for un-recovered estate rentals'. However, while computing taxable income of the assessee, had added ₹ 1.11 crore instead of ₹ 111.39 crore. The mistake had resulted in under assessment of income of ₹ 110.28 crore involving potential tax effect of ₹ 34.08 crore. *ITD rectified the mistake (March 2018) under section 154 of the Act.*

4.2.2.2 In Himachal Pradesh, Pr. CIT Shimla Charge, AO completed the assessment of an assessee for AY 2010-11 under the provision of section 143(3) read with section 148 of the Act in February 2015 at income of ₹ 2.15 crore. Audit examination revealed that, while computing the assessed income, AO adopted the figure of 'excess of income over expenditure' at ₹ 1.29 crore instead of correct amount of ₹ 1.92 crore. The mistake had resulted in under assessment of income of ₹ 63 lakh involving tax effect of ₹ 30.95 lakh including interest. *The Ministry accepted the audit observation (January 2019) and rectified the mistake (December 2017) under section 154 of the Act.*

4.2.3 Application of incorrect rates of tax and surcharge

We give below four such illustrative cases:

Section 4(1) of the Income Tax Act, 1961 provides that income tax is chargeable for every assessment year in respect of the total income of the previous year of an assessee, according to the rates prescribed under the relevant Finance Act. The Finance Act relevant to assessment year 2008-09 provides for levy of surcharge at the rate of ten per cent of income-tax in case of Association of Persons (AOP), if net income exceeds ₹ ten lakh. Similarly, the Finance Act relevant to assessment year 2014-15 provides for levy of surcharge at the rate of ten per cent of income-tax in case of Association of Persons (AOP) or local authority, if net income exceeds ₹ one crore.

4.2.3.1 In Haryana, Pr. CIT Panchkula charge, AO completed the assessment of a local authority for AY 2014-15 after scrutiny in December 2015 at an income of ₹ 1,733.09 crore. Subsequently, CIT (Appeals) assessed the income at ₹ 1,355.80 crore after giving relief of ₹ 377.29 crore in January 2017. Audit examination revealed that, while giving effect to the appellate order (February 2017), AO did not levy surcharge leviable at the rate of

10 *per cent* as per the relevant Finance Act provisions. The omission had resulted in short levy of tax of ₹ 50.87 crore including interest. *ITD rectified the mistake (December 2017) under section 154 of the Act.*

4.2.3.2 In Uttar Pradesh, Pr. CIT-Exemption Lucknow charge, AO completed the assessment of an AOP for AY 2008-09 after scrutiny in December 2010 at an income of ₹ 4.24 crore which was subsequently reassessed under section 147 of the Act in March 2016 at income of ₹ 452.36 crore. Audit examination revealed that, while computing tax demand, AO did not levy surcharge at the rate of 10 *per cent* as per the relevant Finance Act provisions. The omission had resulted in short levy of tax of ₹ 36.46 crore including interest. *The Ministry accepted the audit observation (January 2019) and rectified the mistake (October 2017) under section 154 of the Act.*

4.2.3.3 In Odisha, Pr. CIT Cuttack charge, AO completed the assessment of a local authority for AY 2014-15 after scrutiny in December 2016 determining income at ₹ 817.69 crore. Audit examination revealed that while computing tax demand, AO did not levy surcharge at the rate of 10 *per cent* as per the provision of relevant Finance Act. The omission had resulted in short levy of tax of ₹ 33.60 crore. *ITD accepted (October 2017) the mistake and stated that the remedial action under section 154 was being taken.*

4.2.3.4 In Gujarat, Pr. CIT-Exemption, Ahmedabad Charge, AO completed the assessment of an AOP for AY 2014-15 after scrutiny in December 2016 determining income of ₹ 436.16 crore. Audit examination of Income Tax Computation Form (ITNS-150), which was generated through system, revealed that though the assessed income of the assessee had exceeded rupees one crore, the system had not levied surcharge on the income tax on the assessed income. The failure of the system to compute the correct amount of tax and omission by AO to verify the correctness of the tax resulted in non-levy of surcharge of ₹ 18.19 crore including interest. *The Ministry accepted (January 2019) the audit observation and rectified the mistake (September 2017) under section 154 of the Act.*

4.2.4 Mistakes in levy of Interest

We give below five such illustrative cases:

The Income Tax Act, 1961 provides for levy of interest for omissions on the part of the assessee at the rates prescribed by the Government from time to time. Section 234A provides for levy of interest on account of default in furnishing return of income at specified rates and for specified time period. Section 234B provides for levy of interest on account of default in payment of advance tax at specified rates and for specified time period.

Further, all Income Tax (IT) returns are first summarily processed under section 143(1) at Centralized Processing Centre (CPC), Bengaluru before scrutiny assessments, thus all data

pertaining to summary assessments are directly captured in Assessment Information System (AST). The work of processing, rectification, completion of assessment order in respect of scrutiny cases is done by AOs in AST module, part of ITD module, for all returns transferred from CPC. AST undertakes various assessment functions such as calculation of tax, calculation of interest under various sections of Income Tax Act, 1961, time barring checks, deductions limit validations, due date checks, etc. The payments made by assessee in respect of TDS/TCS and Advance Tax etc. are auto populated from 26AS application and OLTAS application, respectively. In the case of scrutiny assessment, rectification, appeal effect orders in the field offices, figures are data-fed to the system by AOs based on the orders. With the new figures entered into different Heads of Income under additions, computation sheet for final demand is generated. If any increase in the value of above heads is to be done by the AO, the permission is needed from next higher authority through the system. However, no permission is required by AO to decrease the value under above heads in AST. AST module allows the AOs to modify the value of interest under section 234A/B/C/D and 244A under the head 'Modified'. These values can be changed (increased/ decreased) without approval of any higher authority. In cases of assessment done under Best Judgment under section 144, data are manually fed under various heads if assessee is non-filer and accordingly, computation is done. If assessee is late-filer, has filed IT return after section 148 notice, then interest under section 234A/B/C has to be calculated based on original due date for concerned Assessment year.

4.2.4.1 In Odisha, Pr. CIT Cuttack charge, AO completed the assessment of a firm for AY 2008-09 in March 2016 under the provision of section 144 read with section 147 of the Act determining income of ₹ 38.14 crore. Audit examination revealed that the assessee firm neither filed its return of income under section 139(1) of the Act nor filed the same in response to notice under section 148 of the Act. Thus, the assessee was liable to pay interest under section 234A for 90 months from October 2008[89] to March 2016. However, while computing tax liability, AO levied interest for 12 months instead of 90 months, resulting in under charge of interest of ₹ 10.11 crore. Audit further noticed that the amount of interest was calculated manually and the same was fed into the system (AST). Thus, the manual modification of interest through AST had resulted in incorrect levy of interest. It is not clear why manual modification is permitted, that too apparently without a protocol for seeking senior level clearances if, in exceptional cases, manual intervention is required. In fact, if manual intervention at every level is needed, or continued, it either points to an ill designed IT System, or a deliberate attempt to retain discretion, for no apparent good reason. This also points to the fact that the system was deficient in computing the period of delay. *ITD stated (October 2017) that rectification of mistake in computation of interest was being initiated under section 154 of the Act.*

[89] due date of filing of Return of Income for AY 2008-09 was 30th September 2008

4.2.4.2 In West Bengal, Pr. CIT-15 Kolkata charge, AO completed the assessment of an individual for AY 2009-10 in best judgement manner[90] in December 2016 at income of ₹ 20.12 crore. Audit noticed that the assessee had not filed its return of income for AY 2009-10 and had not also responded to the notice issued under section 148 or 142(1) of the Act. Audit further noticed that while computing tax demand, the system did not compute interest under section 234A for non filing of return of income as the period of delay was not entered by the AO. This showed that the system was deficient in computing interest under section 234A. The omission by AO to enter the period of delay resulted in non-levy of interest of ₹ 6.08 crore. ITD should investigate why the error was committed by the AO and take suitable action as per law. *The Ministry accepted the audit observation (December 2018). The mistake in computation of interest has been rectified under section 154 of the Act (December 2017).* As we have seen only the assessment cases in respect of units planned and audited during audit plan of 2017-18, the Ministry needs to verify all cases of interest levy and not only in the cases pertaining to units covered in audit.

4.2.4.3 In Delhi, PCIT-17 Charge, AO completed the assessment of a firm for AY 2009-10 under section 144 in December 2016 determining an income of ₹ 11.92 crore and a tax of ₹ 4.05 crore thereon. The assessee had neither filed its return of income for AY 2009-10 nor furnished the return in response to notice issued under section 148, till the date of assessment, as such, interest under section 234A was required to be levied for 87 months on the assessed tax of ₹ 4.05 crore. Audit examination of Income Tax Computation Form (ITNS-150) revealed that though the ITNS was generated through AST, interest for default in furnishing of return was not computed by AST system indicating the fact that the system was deficient in computing the interest for default in furnishing of return. The omission by AO to verify the correctness of interest depicted in ITNS resulted in short levy of interest of ₹ 3.53 crore. *The Ministry accepted (February 2019) the audit observation and rectified the mistake (March 2018) under section 154 of the Act.*

4.2.4.4 In Andhra Pradesh & Telangana state, Pr. CIT-Central, Hyderabad charge, AO completed the assessment of an individual for AY 2009-10 in December 2016 determining income ₹ 10.19 crore. Audit examination revealed that the interest for default in payment of advance tax under section 234B was worked out manually and not through the AST, and incorrectly levied at ₹ 94.72 lakh instead of correct amount of ₹ 3.17 crore which resulted in a short demand of tax of ₹ 2.22 crore. Audit could not ascertain the reasons for computing the tax on income and interest manually instead of through AST. The omission by AO to verify the correctness of interest depicted in ITNS resulted into short levy of interest of ₹ 2.22 crore.

[90] under section 147/143(3)/144 of the Income Tax Act, 1961

The Ministry accepted (February 2019) the audit observation and rectified the mistake (October 2017) under section 154 of the Act.

4.2.4.5 In Pr. CIT-2 Chandigarh charge, AO completed the assessment of an individual for AYs 2008-09 and 2009-10 under section 144 read with section 147 in March 2016 at income of ₹ 3.55 crore and ₹ 2.16 crore respectively. Audit noticed that the assessee had not filed the return of income for both the AYs. Notices were issued to the assessee under section 148 in March 2015 requiring him to furnish the return of income for AYs 2008-09 and 2009-10. However, no replies were furnished by the assessee till the date of assessment i.e. March 2016. As the assessee had not filed its returns of income for AYs 2008-09 and 2009-10, the assessee was liable to pay interest amounting to ₹ 1.10 crore and ₹ 57.87 lakh on the tax liability of ₹ 1.20 crore and ₹ 72.34 lakh under section 234A(1) for AYs 2008-09 and 2009-10 respectively. Audit examination of ITNS-150 of AYs 2008-09 and 2009-10 revealed that computation in ITNS-150 was done manually in both AYs and not through AST and interest under section 234A(1) for non-furnishing of return of income was omitted to be charged. Audit could not ascertain the reasons for computing the tax on income and interest manually instead of through AST. This had resulted in non levy of interest of ₹ 1.68 crore under section 234(1) of the Act during AYs 2008-09 and 2009-10. *The Ministry accepted the audit observation (January 2019). The mistake in computation of interest has been rectified under section 154 of the Act (February 2017).*

4.2.4.6 While the Ministry has taken action to initiate correction in these cases, it may be pointed out that these are only a few illustrative cases. In the entire universe of all assessments, including non-scrutiny assessments, there is every likelihood of such errors, of omission or commission, in many more cases. The CBDT not only needs to revisit its assessments, but also put in place a fool proof IT system and internal control mechanism to eradicate, so-called "errors".

The IT system for direct taxes needs to be designed in such a way that it should ensure zero or minimal physical interface between the assessee and the tax officers. Government may consider the IT System for direct taxes being placed at arms length from CBDT, with an independent governmental body or organisation.

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 who were not entitled for the same. These irregularities point out weaknesses in the administration of tax concessions/

deductions/exemptions on the part of ITD which need to be addressed. ITD may ascertain whether the instances of irregularities noticed are errors of omission or commission while ensuring necessary action as per law in cases involving errors of commission. 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	02	0.58	Maharashtra and Tamil Nadu
b.	Irregular exemptions/ deductions/relief given to Trusts/Firms/Societies/AOPs	06	3.66	Goa, Madhya Pradesh, Maharashtra, Rajasthan and Uttar Pradesh
c.	Incorrect allowance of Business Expenditure	11	25.80	Assam, Bihar, Gujarat, Himachal Pradesh, Maharashtra, Odisha, Tamil Nadu, Uttrakhand and West Bengal
d.	Irregularities in allowing depreciation/business losses/ capital losses	07	9.19	Bihar, Delhi, Maharashtra, Rajasthan and West Bengal
	Total	**26**	**39.23**	

4.3.2 Irregular exemptions/deductions/relief to Individuals

We give below one such illustrative case.

Under sub-section (1) of section 54F of the Income Tax Act, 1961 subject to the provisions of sub-section (4),where, in the case of an assessee being an individual or a Hindu undivided family, the capital gain arises from the transfer of any long-term capital asset, not being a residential house (hereafter in this section referred to as the original asset), and the assessee has, within a period of one year before or two years after the date on which the transfer took place purchased, or has within a period of three years after that date constructed, a residential house, (hereafter in this section referred to as the new asset), the capital gain shall be dealt with in accordance with the following provisions of this section, - (a) if the cost of the new asset is not less than the net consideration in respect of the original asset, the whole of such capital gain shall not be charged under section 45; (b) if the cost of the new asset is less than the net consideration in respect of the original asset, so much of the capital gain as bears to the whole of the capital gain the same proportion as the cost of the new asset bears to the net consideration, shall not be charged under section 45. It has also been provided that nothing contained in this sub-section shall apply where--- (a) the assessee--- (i) owns more than one residential house, other than the new asset, on the date of transfer of the original asset; or (ii) purchases any residential house, other than the new asset, within a period of one year after the date of transfer of the original asset; or (iii) constructs any residential house, other than the new asset, within a period of three years after the date of transfer of the original asset; and (b) the income from such residential house, other than the one residential house owned on the date of transfer of the original asset, is chargeable under the head "Income from house property"

4.3.2.1 In Tamil Nadu, Pr. CIT-7 Chennai charge, AO completed the assessment of an individual for AY 2014-15 after scrutiny in November 2016 determining income of ₹ 61.77 lakh. Audit observed that the assessee had earned Long Term Capital Gain (LTCG) of ₹ 82.46 lakh from sale of vacant lands. In addition, the assessee had offered LTCG of ₹ 20.08 lakh withdrawing exemption under sub-section (3) of section 54F, claimed earlier in assessment year 2013-14. The assessee had claimed and was allowed exemption under section 54F against total LTCG for the year amounting to ₹ 1.03 crore (₹ 82.46 lakh plus ₹ 20.08 lakh), as the assessee had proposed to construct a new house property. Audit examination revealed that the assessee was not eligible for exemption under section 54F since the assessee already had two residential house properties other than the self-occupied property. As the assessee did not fulfill the conditions prescribed for exemption under section 54F, therefore, exemption allowed under section 54F was not in order. The mistake had resulted in incorrect allowance of exemption of ₹ 1.03 crore with consequential short levy of tax of ₹ 23.24 lakh. *The Ministry accepted (February 2019) the audit observation and initiated the remedial action under section 148 (January 2019).*

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

We give below one such illustrative case:

Section 10A(1A) of the Income Tax Act, 1961 provides for deduction of profits & gains derived from an undertaking from the export of article or things or computer software for a period of ten consecutive years subject to certain conditions specified therein. However, the deduction under this section is available up to AY 2011-12 only.

4.3.3.1 In Uttar Pradesh, Pr. CIT Ghaziabad charge, AO completed the assessment of a firm for AYs 2012-13 and 2013-14 after scrutiny in January 2015 and December 2015 determining income of ₹ 3.22 crore and ₹ 3.87 crore respectively. Audit examination revealed that, AO allowed deduction of ₹ 1.59 crore for AY 2012-13 and ₹ 0.22 crore for AY 2013-14 to the assessee under section 10A(1A) of the Act, whereas deduction under this section was available up to AY 2011-12. The mistake had resulted in irregular allowance of deduction of ₹ 1.81 crore involving tax effect of ₹ 74.72 lakh including interest. *ITD accepted (June 2018) the audit observation and rectified the mistake under section 154 of the Act (November 2017).*

4.3.4 Incorrect allowance of Business Expenditure

We give below two such illustrative cases.

As per provision under section 36(1)(vii) of the Income Tax Act, 1961, the amount of any bad debt or part thereof which is written off as irrecoverable in the accounts of the assessee for the previous year is deductible. Provided that in the case of an assessee to which clause (viia) of section 36(1) applies, the amount of deduction relating to any such debt or part thereof shall be limited to the amount by which such debt or part thereof exceeds the credit balance in the provision for bad and doubtful debts account made under that clause. Further, clause (v) to sub-section (2) of section 36 provides that where such debt or part of debt relates to advances made by an assessee to which clause (viia) of sub-section (1) applies, no such deduction shall be allowed unless the assessee has debited the amount of such debt or part of debt in that previous year to the provision for bad and doubt debts account made under that clause.

4.3.4.1 In Odisha, Pr. CIT Cuttack charge, AO completed the scrutiny assessment of a co-operative bank for AY 2014-15 in December 2016 determining total income at ₹ 23.28 crore. Audit examination revealed that AO had allowed an expense of ₹ 17.03 crore towards loss on 'One Time Settlement' (OTS) which was nothing but the bad debt written off during the year. The assessee had claimed and was allowed the deduction under section 36(1)(vii) of the Act against the OTS though the same had not exceeded the credit balance of ₹ 38.43 crore in the provision for bad and doubtful debts account. Non adherence to the provisions of Act in allowing bad-debt written off resulted in under assessment of income of ₹ 17.03 crore involving tax effect of ₹ 7.89 crore including interest. *ITD accepted (February 2018) the audit observation and stated that remedial action was being taken under section 263 of the Act.*

As per section 43B (f) of Income Tax Act, 1961 any provision made for leave encashment is allowable only when it is actually paid. Further, CBDT has clarified vide Instruction number 17 of 2008 dated 26.11.2008 that section 37 of the Act envisages that an amount debited in the profit & loss account in respect of an accrued or ascertained liability only is an admissible deduction, while any provision in respect of any unascertained liability or a liability which has not accrued, do not qualify for deduction.

4.3.4.2 In Bihar, Pr. CIT I Patna charge, AO completed the assessment of a Co-operative Society for AY 2013-14 after scrutiny in February 2016 determining income at ₹ 16.35 crore. Audit examination revealed that the assessee had claimed and was allowed expenditure of ₹ 8.50 crore on account of provision made towards leave encashment in the books of accounts on ad hoc basis. As provision made on ad hoc basis was not ascertained liability, it was required to be disallowed. The omission had resulted in underassessment of income of ₹ 8.50 crore involving short levy of tax of ₹ 3.55 crore including interest. *The Ministry accepted (February 2019)*

the audit observation and initiated remedial action (March 2018) under section 263 of the Act.

4.3.5 Irregularities in allowing depreciation/business losses/capital losses

We give below one such illustrative cases:

Under section 72 of the Income Tax Act, 1961, where the net result of computation under the head 'Profits & Gains of Business or Profession' is a loss to the assessee and such loss cannot be wholly set off against income under any other head of the relevant year, so much of the loss as had not been set off shall be carried forward to the following assessment year/years, to be set off against the profits and gains of business or profession of those years.

4.3.5.1 In Maharashtra, Pr. CIT-32 Mumbai charge, AO completed the scrutiny assessment of a firm for AY 2014-15 in November 2016 at an income of ₹ 41.42 lakh after allowing set off of brought forward losses of ₹ 9.33 crore pertaining to AYs 2011-12, 2012-13 and 2013-14. Audit noticed that the assessments for AYs 2011-12, 2012-13 and 2013-14 were completed at income of ₹ 26.38 lakh, ₹ 33.41 lakh and ₹ 13.26 lakh respectively. As such, there were no brought forward losses available for set off against the income assessed for AY 2014-15. Incorrect set off of brought forward losses had resulted in under assessment of income of ₹ 9.33 crore involving short levy of tax of ₹ 4.18 crore including interest. *The reply of the Ministry was awaited (March 2019).*

4.4 Income escaping assessments due to omissions

4.4.1 The Income Tax Act, 1961 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 AOs did not assess/under assess total income that was required to be offered to 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 due to omissions **(₹ in crore)**

Sub-categories	Nos.	TE	States
a. Incorrect classification and computation of capital gains	08	3.79	Haryana, Jharkhand, Karnataka, Rajasthan and Tamil Nadu
b. Incorrect computation of income	02	0.92	Assam and Gujarat
c. Income not assessed/under assessed under special provisions	01	0.22	Jammu & Kashmir
d. Unexplained Investment/ cash credit	01	0.23	Haryana
Total	**12**	**5.16**	

4.4.2 Incorrect classification and computation of Capital Gain

We give below one such illustrative case:

As per section 45(1) of the Income Tax Act, 1961, any profits or gains arising from the sale or transfer of a capital asset is chargeable to tax under the head "Capital gains". It is deemed to be the income of the previous year in which the transfer of the capital asset takes place. Capital gains arising from the transfer of immovable property are chargeable to tax in the previous year in which the effect of transfer of the title is conveyed and registered. Further, as per section 112 of the Income Tax Act, 1961, in the case of an individual or a Hindu undivided family the rate of tax on long term capital gains is 20 per cent and is subject to surcharge, education cess and secondary and higher education cess.

4.4.2.1 In Jharkhand, Pr. CIT (Central), Patna charge, AO completed the assessment of an individual for AY 2012-13 under section 153A read with section 144 of Act in March 2016 determining income of ₹ 3.55 crore. As per the assessment records, the assessee had earned long term capital gains of ₹ 3.54 crore on sale of an ancestral property (land) during 2011-12 relevant to AY 2012-13. Audit examination revealed that, while computing tax demand, AO erroneously levied tax of ₹ 54.19 lakh on long term capital gains of ₹ 3.54 crore at the rate of ten *per cent* instead of leviable amount of tax of ₹ 1.39 crore at the applicable rate of twenty *per cent*. The mistake had resulted in short levy of tax of ₹ 84.94 lakh including interest. *The Ministry accepted the audit observation (August 2018) and rectified the mistake (April 2017) under section 154 of the Act.*

4.4.3 Incorrect computation of income

We give below one such illustrative case:

Section 145(3) provides that where the Assessing Officer (AO) is not satisfied about the correctness or completeness of the accounts of the assessee, or where the method of accounting provided in sub-section (1) has not been regularly followed by the assessee, or income has not been computed in accordance with the standards notified under sub-section (2), the AO may make an assessment in the manner provided in section 144. Further, section 144 provides that, the AO, after taking into account all relevant material which the AO has gathered, shall, after giving the assessee an opportunity of being heard, make the assessment of the total income or loss to the best of his judgement and determine the correct sum payable by him or refundable to him on the basis of such assessment.

4.4.3.1 In Gujarat, Pr. CIT-4 Ahmedabad Charge, AO completed the assessment of a firm for AY 2013-14 under section 143(3) read with section 144 in November 2015 determining income of ₹ 1.34 crore. Audit examination revealed that AO had rejected the books of account under Section 145(3) and assessed the income of assessee at ₹ 1.34 crore at the rate of eight *per cent* of gross receipts of ₹ 16.75 crore. However, AO did not consider the interest income of ₹ 1.95 crore being income from other source for taxation. Omission had resulted in under assessment of income of

₹ 1.95 crore with consequent short levy of tax of ₹ 79.58 lakh including interest. *The Ministry accepted the audit observation (January 2019) and took remedial action (September 2018) under section 147 of the Act.*

4.4.4 Income not assessed under special provisions

We give below one such illustrative case:

115JC of the Income Tax Act, 1961 provides that where the regular income tax payable for a previous year by a person, other than a company, is less than the alternate minimum tax payable for such previous year, the adjusted total income shall be deemed to be the total income of the person for such previous year and he shall be liable to pay income-tax on such total income at the rate of eighteen and one-half per cent.

4.4.4.1 In Jammu & Kashmir, Pr. CIT Jammu charge, AO completed the assessment of an individual for AY 2014-15 after scrutiny in October 2016 at income of ₹ 1.59 lakh. Audit examination revealed that the assessee had a net profit of ₹ 1.03 crore as per Profit & Loss account. The assessee had filed revised return for AY 2014-15 on 18 March 2015 at 'nil' income after setting off brought forward business losses and unabsorbed depreciation against the net profit. As alternate minimum tax payable under special provisions was greater than regular income tax payable for the previous year, the assessee was liable to be taxed as per special provisions under section 115JC applicable to a person, other than a company. However, while completing the scrutiny assessment, AO did not compute the alternate minimum tax as per special provisions under section 115JC. The mistake had resulted in non-levy of alternate minimum tax of ₹ 21.61 lakh. *The reply of the Ministry was awaited (March 2019).*

4.4.5 Unexplained Investment/cash credit

We give below one such illustrative case:

As per section 68 of Income Tax Act, 1961, where any sum is found credited in the books of an assessee maintained for any previous year and the assessee offers no explanation about the nature and source of the same or the explanation offered by him is not satisfactory in the opinion of Assessing Officer, the sum so credited may be charged to Income tax as income of the assessee of that previous year.

4.4.5.1 In Haryana, CIT (Exemptions) Chandigarh charge, AO completed the assessment of AOP for AY 2012-13 after scrutiny in March 2015 at an income of ₹ 4.68 lakh. As per Income and expenditure Account for AY 2012-13, against the receipt of ₹ 91.35 lakh, expenditure of ₹ 67.88 lakh was incurred leaving a surplus receipt of ₹ 23.47 lakh. Audit examination revealed that the assessee had shown a liability of ₹ 55.36 lakh on account of university fees payable in the balance sheet (Schedule VI) as on 31 March 2012. After making deduction of a similar provision of ₹ 0.35 lakh made during the preceding previous year, the liability of university fee worked out to

₹ 55.01 lakh for AY 2012-13. Since the expenses payable on account of university fee were not routed through profit and loss account, it was evident that receipts on account of university fee were not accounted for. Thus, the amount equal to the expenses payable at ₹ 55.01 lakh was required to be treated as unexplained cash credit. The omission had resulted in under assessment of income of ₹ 55.01 lakh involving tax effect of ₹ 23.12 lakh including interest. *ITD rectified the mistake (June 2017) under section 147 of the Act.*

4.5 Over Charge of Tax/Interest

4.5.1 We noticed over assessment of income in nine cases involving overcharge of tax/interest of ₹ 10.12 crore in Delhi, Haryana, Madhya Pradesh, Rajasthan, UT Chandigarh, Uttar Pradesh and West Bengal. We give below three such illustrative cases.

4.5.1.1 In Uttar Pradesh, Pr. CIT-Exemption Lucknow charge, AO completed the assessment of local authority for AY 2013-14 after scrutiny in March 2016 at income of ₹ 200.84 crore. Audit examination revealed that while computing tax demand, AO levied interest of ₹ 4.34 crore under section 234A despite the fact that assessee had filed its return of income within due date. The mistake had resulted in overcharge of interest under section 234A of ₹ 4.34 crore. *The Ministry accepted (February 2019) the audit observation and rectified the mistake (January 2017) under section 154 of the Act.*

4.5.1.2 In Madhya Pradesh, Pr. CIT (Central) Bhopal charge, AO completed the assessment of an individual for AY 2013-14 after giving effect to the order of Income Tax Settlement Commission under section 245D(4) of the Act in January 2017 at an income of ₹ 7.55 crore. Audit examination of Income Tax Computation Form (ITNS- 150), which was prepared manually and not generated through AST, revealed that the interest amounting to ₹ 1.34 crore for default in filing of return of income was erroneously levied, despite the fact that the assessee had filed its return of income on 29 September 2013 against the due date of filing of return of 30 September 2013. Audit could not ascertain the reasons for computing the tax on income and interest manually instead of through AST. The mistake had resulted in excess levy of interest of ₹ 1.34 crore under section 234A of the Act. *ITD rectified the mistake in computation of interest under section 154 of the Act (June 2017).*

4.5.1.3 In Rajasthan, Pr. CIT Alwar Charge, AO completed the assessment of an individual for AY 2010-11 under section 147 read with section 144 in November 2016 at income of ₹ 8.64 crore. Audit noticed that AO had made addition of ₹ 6.96 crore to the income of the assessee on account of cash deposited by assessee in bank. However, while computing total income of

the assessee, AO erroneously adopted the figure at ₹ 8.62 crore instead of correct amount of ₹ 6.96 crore. The mistake had resulted in over assessment of income of ₹ 1.66 crore involving tax effect of ₹ 1.31 crore including interest. *ITD accepted the audit observation and rectified the mistake (October 2017) under section 154 of the Act.*

4.6 Conclusion

(i) Assessing Officers (AOs) committed errors in the assessments ignoring clear provisions in the Act. The cases of incorrect assessments involving arithmetical errors in computation of income and tax are difficult to accept as mere errors, in the days of calculators and computers. Further, application of incorrect rates of tax and surcharge, errors in levy of interest, excess or irregular refunds etc. point to either incompetence, or mischief, as well as weaknesses in the internal controls in ITD which need to be addressed. The existing scrutiny assessment procedure is opaque.

(ii) AST module allows manual modification of interest amount which resulted in mistakes in computation of interest. ITD needs to inquire into the reasons for errors in computation of interest through AST and reasons for allowing manual modification to co-exist with IT system. ITD may ascertain whether the instances of irregularities noticed are errors of commission and take necessary action as per law in such cases.

(iii) In view of repetitive nature of the errors, ITD should take remedial steps to prevent recurrence.