

Chapter IV

Income Tax

- ◆ Chapter summary
- ◆ Receipts from Income tax
- ◆ Results of Audit
- ◆ Status of the replies received from the Ministry
- ◆ Mistakes in:
 - Computation of business income, allowance of deduction to undertakings engaged in developing and building housing projects
 - Allowance of deduction in respect of export profits and application of incorrect rate of tax
 - Non/short levy of interest, computation of capital gains, incorrect deduction allowed to co-operative societies and allowance of liabilities
 - irregular refunds, adoption of correct figures, carry forward and set off of losses
 - allowance of depreciation, levy of surcharge, income not assessed and summary assessment
- ◆ Cases of overassessment/overcharge

Chapter Summary

Audit issued 198 observations with a revenue impact of Rs. 46.54 crore involving various irregularities, omissions and mistakes to the Ministry of Finance. The Ministry had accepted 66 observations involving revenue impact of Rs. 12.80 crore till 7 December 2007.

(Paragraphs 4.4 and 4.6)

Assessing officers committed mistakes in:

- ◆ computation of business income in 18 cases involving revenue impact of Rs. 7.58 crore.

(Paragraph 4.7.2)

- ◆ allowing deduction to an undertaking developing and building housing projects in six cases involving revenue impact of Rs. 5.65 crore.

(Paragraph 4.8.2)

- ◆ allowing deduction in respect of export profit in 22 cases involving revenue impact of Rs. 5.24 crore.

(Paragraph 4.9.2)

- ◆ application of correct rate of tax in eight cases involving revenue impact of Rs. 3.62 crore.

(Paragraph 4.10.1)

- ◆ levy of interest in 29 cases involving revenue impact of Rs. 2.98 crore.

(Paragraph 4.11.1)

- ◆ computation of capital gains in two cases involving revenue impact of Rs. 2.42 crore.

(Paragraph 4.12.1)

- ◆ allowing deduction to co-operative societies and allowance of liability in 10 cases involving revenue impact of Rs. 2.08 crore.

(Paragraphs 4.13.2 and 4.14.1)

- ◆ allowing refund, adoption of correct figures and carry forward and set off of losses in 12 cases involving revenue impact of Rs. 1.98 crore.

(Paragraphs 4.15.1, 4.16.1 and 4.17.2)

- ◆ computation of depreciation, levy of surcharge and not assessing income in 18 cases involving revenue impact of Rs. 80.48 lakh.

(Paragraphs 4.18.1, 4.19.1 and 4.20.1)

- ◆ underassessment of income in assessments processed in a summary manner in 43 cases involving revenue impact of Rs. 9.26 crore.

(Paragraph 4.21.1)

- ◆ overcharge of tax in 11 cases involving revenue impact of Rs. 1.97 crore.

(Paragraph 4.22)

CHAPTER IV: INCOME TAX

Number of assesses	4.1 The number of assesses (other than companies) borne on the books of the Income tax Department as on 31 March of 2006 and 2007 were 2.94 crore and 3.09 crore respectively as given in Table no. 2.7 of chapter II of this report.
Receipts from income tax	4.2 During 2006-07, income tax receipts were Rs. 75,079 crore compared to Rs. 55,985 crore in 2005-06 and constituted 32.62 percent of the direct taxes collection. Table no. 2.4 of chapter II of this report shows the details.
Status of assessments	4.3 Table no. 2.11 of paragraph 2.9 of chapter II of this report contains the particulars of assessments due for disposal, assessments completed and those pending. Details of demands remaining uncollected during the last five years are given in Table no. 2.13 of chapter II of this report.
Results of audit	4.4 Audit issued 187 draft paragraphs involving undercharge of tax of Rs. 44.57 crore and 11 draft paragraphs involving overcharge of tax of Rs. 1.97 crore to the Ministry of Finance between May 2007 and October 2007 for comments. The internal audit of the department had seen only 11 of these cases and had not noticed the mistakes pointed out in this report. 4.5 Out of the 198 draft paragraphs issued to the Ministry, 169 cases involving undercharge of Rs. 41.67 crore and 11 cases involving overcharge of Rs. 1.97 crore have been included in this chapter. Each paragraph indicates a particular category of mistake and starts with a suitable preamble followed by the combined/consolidated revenue impact of all observations of similar nature. Cases with money value of Rs. 75 lakh or more have been illustrated in the body of the chapter while those of Rs. 20 lakh or more but less than Rs. 75 lakh each are given in the table under the related category.
Status of replies received from the Ministry of Finance	4.6 Out of 180 cases included in this chapter, the Ministry of Finance have accepted audit observations in 66 cases involving aggregate revenue impact of Rs. 12.80 crore. In two cases, the Ministry have not accepted the audit observation. In the remaining cases, replies have not been received (till 7 December 2007). Replies of the Ministry wherever received, have been examined and suitably incorporated in the report. 4.7 Mistakes in computation of business income
Mistakes in computation of business income	4.7.1 The Income Tax Act, 1961, provides that in a scrutiny assessment, the assessing officer will make a correct assessment of the total income or loss of the assessee and determine the correct sum payable by him or refundable to him on the basis of such assessment. Income under the head “profits and gains of

business or profession” is computed in accordance with the method of accounting regularly employed by the assessee.

4.7.2 Non compliance with the above provisions while computing business income was noticed in **18 cases**, resulting in short levy of tax aggregating to **Rs. 7.58 crore** in Gujarat, Himachal Pradesh, Maharashtra, Rajasthan, Uttar Pradesh and Union Territory of Chandigarh. **Three cases** are illustrated below:

4.7.3 “Dividend stripping transaction” in which shares/units are purchased “cum-dividend” and sold at a loss after receiving the dividend has been held to be a tax avoidance device, distinct from business or trading transaction. It has been judicially held¹ that purchase of shares with arrear dividend was a capital purchase and that the cost of acquisition of securities was required to be reduced by the amount of dividend. It has also been judicially held² that the loss arising from such “dividend stripping transaction” did not qualify for adjustment against business income. The Income Tax Act was subsequently amended by insertion of section 94(7) with effect from the assessment year 2002-03, which states that the loss arising out of purchase and sale of securities/units shall be ignored to the extent of dividend/income.

4.7.4 In Maharashtra, CIT Central II, Mumbai charge, the assessment of an individual, **Shri Vinod H. Biyani**, for the assessment year 2000-01 was completed after scrutiny in March 2002 determining an income of Rs. 33.56 lakh. Audit examination revealed that during the previous year relevant to the assessment year 2000-01, the assessee had purchased units from mutual funds of Rs. 21.00 crore and had received dividend of Rs. 4.88 crore on the date of purchase. The units were redeemed for an amount of Rs. 15.49 crore after two-three days of the purchase. Dividend of Rs. 4.88 crore received was claimed as exempt under section 10(33) and the total loss of Rs. 5.51 crore sustained by the assessee was adjusted against the short-term capital gain.

Units of the mutual funds had been purchased at ‘cum dividend NAV (net asset value) price’ and had been redeemed at ‘ex-dividend NAV price’. The investment was made with the intention of receiving the dividend, which was exempt under section 10(33) of the Act, with anticipated loss in sale. The purchase and sale were thus part of a dividend-stripping transaction. Therefore, in view of the Supreme Court’s ruling, the allowance of loss of Rs. 5.51 crore was not in order, resulting in underassessment of income of Rs. 5.51 crore involving short levy of tax of Rs. 2.43 crore (including interest).

4.7.5 In Maharashtra, DIT (Exemption), Mumbai charge, the income tax assessment of an AOP, **Mumbai Metropolitan Region Development Authority**, for the assessment year 2003-04 was completed after scrutiny in March 2006 determining an income of Rs. 5.21 crore. The assessing officer disallowed the exemption claimed by the assessee under section 11 of the Act

¹{75 ITR 191} CIT vs India Discount Company (SC) (1969)

²{75 ITR 544} Lupton (Inspector of taxes) vs F.A. & A. B. Ltd. (In the court of Appeal) (1969)

and taxed the income treating it as a local authority. Audit examination revealed that the assessee had not considered Rs. 2.46 crore receivable as penal interest on short-term deposits kept with public sector undertakings and Government of Maharashtra. Further, the assessee had also not accounted for lease premium of Rs. 2.82 crore receivable from Bombay Suburban Electric Supply Company. As the assessee was following the mercantile system of accounting, accrued income relating to these activities should have been added back. The omission to do so resulted in underassessment of income of Rs. 5.28 crore with consequent short levy of tax of Rs. 2.29 crore (including interest).

4.7.6 Section 69C of the Income Tax Act, 1961, provides that where, in any financial year, an assessee has incurred any expenditure and he offers no explanation about the source of income of such expenditure or part thereof, or the explanation, if any, offered by him is not satisfactory, the amount covered by such expenditure or part thereof is deemed to be the income of the assessee for such financial year. Further, notwithstanding anything contained in any other provisions of the Act, such unexplained expenditure which is deemed to be the income of the assessee shall not be allowed as deduction under any head of income.

4.7.7 In Maharashtra, CIT I, Pune charge, the assessment of a firm, **M/s Nav Maharashtra Port Land Cement Industries**, for the assessment year 2001-02 was completed after scrutiny in July 2003 determining a loss of Rs. 26.50 lakh. Audit examination revealed that during the previous year relevant to the assessment year 2001-02, the assessee had paid Rs. 2.50 crore to M/s N.M. Corporation Ltd., Sangli, for the purchase of animal feed. The amount was neither shown in the purchase/sales account, nor in the closing stock. Therefore, Rs. 2.50 crore should have been treated as unexplained expenditure and disallowed under section 69C of the Act and added back to the total income of the assessee. The omission resulted in underassessment of income of Rs. 2.50 crore involving short levy of tax of Rs. 1.19 crore.

4.7.8 Three cases are shown in **Table no. 4.1** below:

(Rs. in lakh)

Sl. no.	Name of the assessee/ CIT charge	Assessment year	Type/ month of assessment	Nature of mistake	Revenue impact
1	M/s B. G. Chitale CIT I, Kolhapur	2003-04 2004-05 2005-06	Scrutiny December 2005 February 2006 March 2006	The assessee had earned aggregate interest income of Rs. 4.73 crore from fixed deposits and refund of income tax in these assessment years and included it in the business income for computation of eligible remuneration to its partners instead of reducing it (being the income from other sources) before computing eligible remuneration. This resulted in aggregate excess payment of remuneration of Rs. 1.26 crore involving revenue impact of Rs. 53.47 lakh.	53.47

Sl. no.	Name of the assessee/ CIT charge	Assessment year	Type/ month of assessment	Nature of mistake	Revenue impact
2	M/s Shivam Overseas CIT Central, Ludhiana	2004-05	Scrutiny March 2006	The assessing officer had failed to add back Rs. 64.45 lakh on account of unexplained investment from undisclosed sources, resulting in underassessment of income involving revenue impact of Rs. 28.90 lakh.	28.90
3	Shri Mukesh R. Shah CIT Central I, Ahmedabad	2001-02	Scrutiny March 2004	Closing stock of Rs. 47.10 lakh not credited to the profit and loss account and not considered while computing taxable income resulted in non levy of tax of Rs. 23.76 lakh.	23.76

4.7.9 The Ministry has accepted (December 2007) audit observation in the case at **Sl. no. 2** of **Table no. 4.1** above.

Incorrect allowance of deduction to undertakings engaged in developing and building housing projects

4.8 Incorrect allowance of deduction to undertakings engaged in developing and building housing projects

4.8.1 Section 80IB(10) of the Income Tax Act, provides that deduction to the extent of hundred per cent of the profits derived in any previous year is allowed in the case of an undertaking developing and building housing projects approved before the specified date by a local authority subject to the conditions specified therein. The provisions were amended with effect from 1 April 2005 inserting a clause which stipulated that exemption would be available to such an undertaking if the shops and commercial establishments included in the housing projects did not exceed five percent of the aggregate built up area or two thousand square feet, whichever was less. The ITAT Mumbai Bench held³ that the construction of shops or commercial place cannot be considered a housing project for the purposes of application of the provision of section 80IB (10) of the Act and that even if one condition is violated, the benefit of the entire deduction would not be available. The Tribunal also held that the aforesaid amendment in section 80IB would have prospective effect from 1 April 2005 and thus denied the deduction in respect of housing projects with commercial space, which were approved before 1 April 2005.

4.8.2 Audit noticed mistakes in allowance of deductions to undertakings developing and building housing projects resulting in short levy of tax aggregating **Rs. 5.65 crore** in **six cases** in Bihar, Maharashtra and Uttar Pradesh. **Four cases** are illustrated below:

4.8.3 In Maharashtra, CIT 25, Mumbai charge, the assessment of a firm, **M/s H. D. Enterprises**, for the assessment year 2004-05 was completed after scrutiny in January 2006 determining an income of Rs. 2.00 crore. Audit

³ M/s Kaukik Developers vs DCIT Circle 3, Thane (ITA, 1961, no. 532/M/06)

examination revealed that the assessee was allowed deduction of Rs. 5.38 crore under section 80IB (10) of the Act. Since the assessee had developed a residential housing cum commercial project with shops, the assessing officer had restricted the deduction to the proportionate amount of profit attributable to the construction of the residential built up area. However, in view of the aforesaid provisions of the Act and the ITAT's decision that the amendment in section 80IB would have prospective effect from 1 April 2005, the entire deduction should have been disallowed. The omission to do so resulted in underassessment of income of Rs. 5.38 crore with consequent revenue impact of Rs. 2.36 crore (including interest).

4.8.4 In Maharashtra, CIT 4, Mumbai charge, the assessment of a firm, **M/s Girilal & Co.**, for the assessment year 2001-02 was completed after scrutiny in May 2003 determining an income of Rs. 12.36 lakh after allowing a deduction of Rs. 2.75 crore under section 80IB in respect of the profits on development and construction of housing project. One of the conditions for claiming deduction under section 80IB for an undertaking engaged in developing and building housing project is that the size of plot of land should be a minimum of one acre (43,560 sq. ft.). Audit examination revealed that the assessee utilised land measuring 5,919 square feet for development and construction of the project. The condition for claiming deduction was, therefore, not fulfilled. The omission to disallow deduction under section 80 IB resulted in underassessment of income of Rs. 2.75 crore involving revenue impact of Rs. 1.43 crore (including interest).

4.8.5 In Maharashtra, CIT 19, Mumbai charge, the assessment of a firm, **M/s Vinamra Developers**, for the assessment years 2002-03, 2003-04 and 2004-05 were completed after scrutiny in January 2006 determining an income of Rs. 1.00 lakh, Rs. 4.28 lakh and Rs. 1.85 lakh respectively. The assessee was allowed deduction of Rs. 28.01 lakh, Rs. 1.20 crore and Rs. 51.78 lakh under section 80IB (10) of the Act for these assessment years. Since the assessee had developed a residential housing cum commercial project with shops, the assessing officer had restricted the deduction to the proportionate amount of profit attributable to the construction of residential built up area. However, in view of the aforesaid provisions of the Act and the ITAT's decision, the entire deduction should have been disallowed. The omission to do so resulted in underassessment of income aggregating Rs. 2.00 crore with consequent revenue impact of Rs. 97.26 lakh (including interest).

4.8.6 The Ministry has accepted (December 2007) the above observation.

Other issues

4.8.7 Section 80IB of the Income Tax Act, 1961, provides that where the gross total income of an assessee includes any profit and gains derived from certain industrial undertakings, the assessee shall be allowed deduction of twenty-five

percent (or thirty percent where the assessee is a company), of the profit and gains derived from such industrial undertaking, for a period of ten consecutive assessment years (or twelve consecutive assessment years where the assessee is a cooperative society), beginning with the initial assessment year.

In Uttar Pradesh, CIT, Allahabad charge, assessment of a firm, **M/s ABC Industries, Tikara, Mirzapur**, for the assessment year 2004-05 was completed after scrutiny in December 2005 determining 'nil' income after allowing deduction of Rs. 3.32 crore under section 80 IB. Audit examination revealed that the income of Rs. 3.32 crore included Rs. 1.57 crore relating to duty drawback. As the income from duty drawback was not derived from an industrial undertaking engaged in eligible business, deduction on it was not admissible. The omission to disallow it resulted in short computation of income of Rs. 1.57 crore involving revenue impact of Rs. 77.39 lakh (including interest).

Incorrect allowance of deduction in respect of export profits

4.9 Incorrect allowance of deduction in respect of export profits

4.9.1 The method of allowance of deduction in respect of export profits has been described in **paragraph 3.19.1 of chapter III** of this report.

4.9.2 Audit noticed mistakes in computation of export profits resulting in short levy of tax aggregating **Rs. 5.24 crore** in **22 cases** in Delhi, Gujarat, Karnataka, Kerala, Maharashtra, Punjab, Tamil Nadu, Uttar Pradesh and West Bengal. **One case** is illustrated below:

4.9.3 In Maharashtra, CIT 27, Mumbai charge, the assessment of a firm, **M/s Aloka Exports**, for the assessment year 2001-02 was completed after scrutiny in February 2004 determining an income of Rs. 4.02 crore after allowing deduction of Rs. 8.93 crore under section 80HHC as claimed by the assessee. Audit examination revealed that 90 percent of the export incentives included DEPB licences of Rs. 4.19 crore. As export turnover of the assessee exceeded Rs. 10 crore, it was required to fulfill the eligibility criteria for availing the deduction of DEPB as per proviso inserted in section 80HHC(3) by Taxation Laws (Amendment) Act, 2005. The assessee failed to produce any evidence regarding fulfillment of the prescribed conditions and was thus not entitled to deduction in respect of DEPB credit. The omission to exclude it resulted in excess allowance of deduction of Rs. 3.01 crore under section 80HHC of the Act involving short levy of tax of Rs. 1.69 crore including interest.

4.9.4 The Ministry has accepted (December 2007) the above observation.

4.9.5 **Five cases** are shown in **Table no. 4.2** below:

(Rs. in lakh)

Table no. 4.2: Incorrect allowance of deduction in respect of export profits

Sl. no.	Name of the assessee/ CIT charge	Assessment year	Type/ month of assessment	Nature of mistake	Revenue impact
1	M/s Atlas Exports CIT 12, Mumbai	2001-02	Scrutiny March 2003	Export incentives of Rs. 7.44 crore considered for allowing deduction were inclusive of DEPB premium of Rs. 1.94 crore although the assessee was not entitled to the deduction as he failed to produce any evidence regarding fulfillment of the conditions given in the third proviso to section 80HHC (3) of the Act. This resulted in excess allowance of deduction of Rs. 1.40 crore.	71.44
2	Shri Satish Kumar Agrawal CIT Central II, Delhi	2002-03	Scrutiny March 2004	While calculating the deduction, the loss of Rs. 68.37 lakh incurred on the export of trading goods was not considered resulting in excess allowance of deduction of Rs. 1.37 crore.	53.74
3	Shri K. Ravindranathan Nair CIT, Thiruvananthapuram	2000-01	Scrutiny January 2005	Excess export turnover and claim of deduction relating to disclaimer certificate of Rs. 3.21 crore and Rs. 64.62 lakh respectively, were considered for allowance of deduction under section 80HHC resulting in excess allowance of deduction of Rs. 38.62 lakh.	38.62
4	Smt Seema Ajay Ranka CIT II, Baroda	2001-02 2002-03 2003-04	Scrutiny January 2004 October 2004 March 2004	While computing deduction under section 80HHC, deduction of Rs. 1.33 crore allowed under section 80IA was not reduced from the gross total income, resulting in excess allowance of deduction of Rs. 58.47 lakh.	29.09
5	M/s Shah Naresh Kumar & Company CIT 14, Mumbai	2003-04	Scrutiny March 2006	The assessee was allowed deduction under section 80HHC at the rate of 100 percent as against the allowable rate of 50 percent, resulting in excess allowance of deduction of Rs. 44.08 lakh.	22.24

4.9.6 The Ministry has accepted (December 2007) audit observations in the cases at **Sl. no. 1 and 5** of **Table no. 4.2** above.

**Application of
incorrect rate of
tax**

4.10 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.

4.10.1 Audit noticed that the assessing officer did not apply the above provision correctly in **eight cases** in Maharashtra, Madhya Pradesh, Punjab, Rajasthan and Tamil Nadu, which resulted in short levy of tax of **Rs. 3.62 crore**. **Three cases** are illustrated below:

4.10.2 In Tamil Nadu, CIT II, Chennai charge, the assessment of an AOP*, **M/s Tamil Nadu Urban Development Fund**, for the assessment years 2000-01 and 2002-03 to 2005-06 were completed between March 2003 and March 2006 under scrutiny determining an income of Rs. 21.41 crore, Rs. 33.36 crore, Rs. 25.01 crore, Rs. 19.02 crore and Rs. 7.60 crore respectively. The assessee filed its returns of income for these assessment years admitting 'nil' income after claiming exemption of its entire income under section 11 of the Act citing that it was a trust founded for serving the public interest. While completing the scrutiny assessments, the assessing officer rejected the claim and assessed the income treating it as AOP on the ground that the assessee's operations were conducted on commercial principles. Audit examination revealed that the profits were shared at percentages variable from year to year by its members and tax was levied at the rate applicable to the AOP/BOI*. However, where any member of the AOP was chargeable to tax at a rate higher than the maximum marginal rate, tax was required to be charged at the higher rate applicable on that portion of the total income of the AOP which was payable to the member. The omission to do so resulted in short levy of tax of Rs. 1.39 crore.

4.10.3 In Maharashtra, CIT 14, Mumbai charge, the assessment of a firm **M/s Krishnakumar & Co.**, for the assessment year 1994-95 was initially completed after scrutiny in March 2002, and was further revised in January 2005 to give effect to appellate order. Audit examination revealed that while revising the assessment, the assessing officer had levied tax on long term capital gain for the assessment year 1994-95 at the rate of 20 percent against the correct rate of 30 percent, resulting in short levy of tax of Rs. 96.40 lakh (including interest).

4.10.4 The Ministry has accepted (December 2007) the above observation.

4.10.5 In Punjab, CIT I, Ludhiana charge, the assessment of a firm, **M/s Eastman International**, for the assessment year 2003-04 was completed after scrutiny in March 2006 determining an income of Rs. 17.43 crore. Audit examination revealed that tax was incorrectly levied at the rate of 30 percent on the assessed income as against the correct rate of tax of 35 percent along with applicable surcharge, resulting in short levy of tax of Rs. 91.51 lakh.

4.10.6 The Ministry has accepted (December 2007) the above observation.

Non/short levy of interest

4.11 The provisions regarding levy of interest for delays in filing return of income, payment of advance tax and default in payment of demand have been described in **paragraph 3.12 of chapter III** of this report.

4.11.1 Audit noticed short levy of interest for delays in filing return of income, payment of advance tax and default in payment of demand aggregating **Rs. 2.98**

* AOP: Association of person

♦ BOI: Body of individual

crore in 29 cases in Bihar, Delhi, Gujarat, Karnataka, Madhya Pradesh, Maharashtra, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh and West Bengal.

4.11.2 Three cases are shown in Table no. 4.3 below:

(Rs. in lakh)

Table no. 4.3: Non/short levy of interest

Sl. no.	Name of the assessee/ CIT charge	Assessment year	Type/ month of assessment	Nature of mistake	Revenue impact
1	M/s Narendra Trading Company CIT III, Baroda	1996-97	Scrutiny March 2004	Short levy of interest of Rs. 46.03 lakh for non filing of return.	46.03
2	M/s Swaminarayan Co-op Bank Ltd. CIT III, Baroda	1999-2000	Scrutiny March 2003	The assessee paid interest of Rs. 6.83 crore to various persons on fixed deposit receipt, but did not deduct tax at source resulting in non levy of interest of Rs. 45.42 lakh.	45.42
3	M/s New Gujarat Tin Printing Works CIT III, Baroda	2001-02	Scrutiny March 2006	The assessee was liable to pay interest of Rs. 21.27 lakh for late filing of return.	21.27

Incorrect computation of capital gains

4.12 The Income Tax Act, 1961, provides that any profit or gain arising from transfer of a capital asset effected in the previous year is chargeable to tax under the head 'capital gains' and shall be deemed to be the income of the previous year in which the transfer took place. Tax on such capital gains is chargeable at the rate prescribed.

4.12.1 Audit noticed mistakes in the computation of capital gain resulting in short levy of tax of **Rs. 2.42 crore** in **two cases** in Karnataka and Kerala. **One case** is illustrated below:

4.12.2 In Kerala, Trivandrum charge, the assessment of an individual, **Dr. P.N. Bhaskaran**, for the assessment year 1999-2000 was completed after scrutiny in January 2003 determining an income of Rs. 1.50 crore. While computing the total income, capital gain of Rs. 3.73 crore arising from the sale of land for a total consideration of Rs. 3.75 crore was allowed as exemption under section 54 EA, since the entire sale consideration was invested in UTI 64 scheme. Audit examination revealed that the assessee was in possession of the said asset for a period less than 36 months. The capital gain on its sale was, therefore, assessable as short-term capital gain and the assessee was not entitled to the exemption allowed under section 54 EA. The irregular allowance of exemption resulted in underassessment of income of Rs. 3.73 crore with consequent revenue impact of Rs. 2.27 crore.

4.13 Irregular deduction allowed to co-operative societies

4.13.1 The Income Tax Act, 1961, provides that where the gross total income of a co-operative society includes any income from carrying on the business of banking or providing credit facilities to its members, deduction shall be allowed on the whole of the amount of profits and gains of business attributable to any one or more of such activities of the co-operative society. It is further provided that deductions will be made from gross total income after setting off unabsorbed losses, depreciation, etc. of the earlier years, before allowing any deduction under chapter VIA.

4.13.2 Audit noticed mistakes in computation of deduction under section 80P in **five cases** resulting in short levy of tax aggregating **Rs. 1.18 crore** in Gujarat, Maharashtra, Rajasthan and West Bengal. **Three cases** are shown in **Table no. 4.4** below:

(Rs. in lakh)

Table no. 4.4: Incorrect allowance of deduction to cooperative societies

Sl. no.	Name of the assessee/ CIT charge	Assessment year	Type/ month of assessment	Nature of mistake	Revenue impact
1	The Churu Central Cooperative Bank Ltd. CIT III, Jaipur	2003-04	Scrutiny December 2005	The assessee had brought forward losses from earlier years and hence deduction of Rs. 1.06 crore was not admissible.	33.33 (P)
2	M/s Wardha District Central Cooperative Bank Ltd. CIT II, Nagpur	2002-03	Scrutiny December 2004	The assessee had received Rs. 64.54 lakh on account of commission and Rs. 0.50 lakh as income from other sources which were allowed as deduction though not admissible.	30.91
3	M/s Bardhaman Co-operative Milk Producers Union Ltd. CIT, Bardhaman	2003-04 2004-05	Scrutiny December 2005 February 2006	The assessee was a central cooperative milk producers union, which was not a primary co-operative society. Thus, it was not eligible for deduction. Deduction aggregating to Rs. 57.71 lakh was, however, incorrectly allowed.	27.09

(P: denotes potential tax)

4.13.3 The Ministry has accepted (December 2007) audit observations in the cases at **Sl. no. 1 and 2** of **Table no. 4.4** above.

Incorrect allowance of liabilities

4.14 Certain deductions being cess, fee or any sum payable by an assessee as employer by way of contribution to any provident fund, superannuation fund or gratuity fund etc. are deductible on actual payment basis. It is further provided that such expenditure would be allowable only if the payment is made before the due date of filing of the return.

4.14.1 Assessing officers allowed liabilities without actual payment by the due date or payments being made before the due date of filing of the return, resulting in short levy of tax of **Rs. 90.24 lakh** in **five cases** in Gujarat, Maharashtra, Rajasthan and West Bengal. **One case** is shown in **Table no. 4.5** below:

(Rs. in lakh)

Table no. 4.5: Incorrect allowance of liability

Sl. no.	Name of the assessee/CIT charge	Assessment year	Type/ month of assessment	Nature of mistake	Revenue impact
1	Shri Bharat S. Shah CIT 2, Mumbai	2001-02	Scrutiny March 2004	The bank interest and charges debited to the profit and loss account included Rs. 1.44 crore, which was due to exchange loss on foreign currency loan. This was only a notional loss, for which no payment had been made to the bank. The omission to disallow this inadmissible deduction resulted in overassessment of loss involving potential revenue impact of Rs. 50.39 lakh.	50.39(P)

(P: denotes potential tax)

Irregular refunds

4.15 The Income Tax Act, 1961, provides that where, as a result of any order passed in assessment, appeal, revision or any other proceedings under the Act, refund of any amount becomes due to the assessee, the assessing officer may grant the refund or adjust or set off the refund against outstanding dues of the assessee for any assessment year.

4.15.1 Audit noticed that assessing officers had allowed excess refund and interest in **four cases** in Andhra Pradesh, Gujarat, Haryana, Himachal Pradesh, and Karnataka involving revenue impact of **Rs. 84.14 lakh**. **One case** is shown in **Table no. 4.6** below.

(Rs. in lakh)

Table no. 4.6: Irregular refunds

Sl. no.	Name of the assessee/ CIT charge	Assessment year	Type/ month of assessment	Nature of mistake	Revenue impact
1	Shri Dinesh Kumar Singh CIT I, Bangalore	2005-06	Scrutiny March 2006	Excess interest on the refund of Rs. 68.68 lakh was allowed due to mistake in adoption of period of interest in excess by 14 months while calculating interest.	68.68

4.15.2 The Ministry has accepted (December 2007) the above observation.

Mistakes in adoption of correct figures

4.16 Assessing officers have to determine and assess the income correctly in scrutiny assessments. Accounts, claims, records and all documents are to be examined in scrutiny assessments. The Board have issued instructions to the assessing officers and their supervising officers to ensure that mistakes in assessments do not occur.

4.16.1 Audit noticed that assessing officers had adopted incorrect figures and committed mistakes in computation of total income resulting in short levy of tax aggregating to **Rs. 57.44 lakh** in **five cases** in Karnataka, Madhya Pradesh, Maharashtra and Tamil Nadu. **One case** is shown in **Table no. 4.7** below:

(Rs. in lakh)

Table no. 4.7: Mistake in adoption of correct figure

Sl. no.	Name of the assessee / CIT charge	Assessment year	Type/ month of assessment	Nature of mistake	Revenue impact
1	Symbiosis International Centre for Education CIT III, Pune	2003-04	Scrutiny March 2006	The assessing officer had adopted assessed income as Rs. 1.12 crore against Rs. 1.62 crore, resulting in short levy of tax of Rs. 22.23 lakh.	22.23

Incorrect carry forward and set off of losses

4.17 The Income Tax Act, 1961, provides that where the net result of the computation under the head 'profits and gains of the business or profession' is a loss to the assessee and such loss, including depreciation, cannot be wholly set off against income under any other head of the relevant year, so much of the loss as has 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'.

4.17.1 No loss under the head ‘business income’ shall be carried forward and set off against business income of future years, unless the return of loss was filed on or before the due date.

4.17.2 Audit noticed short levy of tax aggregating to **Rs. 56.55 lakh** in **three cases** in Gujarat, Maharashtra and Rajasthan, as the assessing officers did not apply the above provisions correctly. **One case** is shown in **Table no. 4.8** below:

(Rs. in lakh)

Sl. no.	Name of the assessee/ CIT charge	Assessment year	Type/ month of assessment	Nature of mistake	Revenue impact
1	M/s Orgo Pharma Chemicals CIT 19, Mumbai	2003-04	Scrutiny March 2006	The assessing officer had allowed excess carry forward of business loss of Rs. 1.33 crore resulting in potential revenue impact of Rs. 48.71 lakh.	48.71 (P)

(P: denotes potential tax)

Incorrect allowance of depreciation

4.18 The Income Tax Act, 1961, provides that in computing the business income of an assessee, a deduction on account of depreciation on the fixed assets is admissible at the prescribed rates and on the written down value.

4.18.1 Assessing officers committed mistakes in allowing depreciation in **seven cases**, which resulted in short levy of tax aggregating to **Rs. 34.47 lakh** in Andhra Pradesh, Delhi, Gujarat, Punjab and Uttar Pradesh.

Non levy of surcharge

4.19 Income tax including surcharge is charged at the rates prescribed in the relevant Finance Act.

4.19.1 Assessing officers did not levy surcharge at the rate prescribed in the Finance Act resulting in short demand of **Rs. 25.16 lakh** in **six cases** in Jharkhand, Madhya Pradesh and Punjab.

Income not assessed

4.20 The Income Tax Act, 1961, provides that income tax shall be charged for every assessment year in respect of total income of the previous year of every person. The term “income” has an inclusive definition under the Act and includes capital gains, unexplained investment etc.

4.20.1 Audit noticed short levy of tax aggregating to **Rs. 20.85 lakh** in **five cases** in Bihar, Karnataka, Maharashtra, Punjab, Rajasthan and Tamil Nadu as the assessing officers had not assessed all income to tax.

Mistake in summary assessments

4.21 Consequent to the amendment of the Income Tax Act, 1961 with effect from 1 June 1999, no prima facie adjustment can be made by the assessing

officers in an assessment processed in a summary manner. However, benefits availed of by the assessee in summary assessments to which he is not entitled, can be withdrawn and mistakes rectified under the powers separately available to assessing officers under the Income Tax Act.

4.21.1 During test check of income tax assessments, audit noticed mistakes in **43 cases** of summary assessments involving revenue impact of **Rs. 9.26 crore** in Bihar, Gujarat, Haryana, Himachal Pradesh, Jharkhand, Karnataka, Kerala, Maharashtra, Orissa, Punjab, Tamil Nadu, Uttar Pradesh, and West Bengal. **One case** is illustrated below:

4.21.2 In Orissa, CIT, Cuttack charge, the assessment of a co-operative society, **Baaitarani Gramya Bank**, for assessment year 2002-03 was processed in summary manner in October 2002. Audit examination revealed that although as per the tax auditor's certificate, the brought forward loss was only Rs. 24.67 crore, the assessee had adopted a figure of Rs. 39.64 crore and had set off the current year's income of Rs. 14.40 lakh against the loss, carrying forward Rs. 39.49 crore as the net loss. This resulted in excess carry forward of loss of Rs. 14.96 crore involving potential revenue impact of Rs. 4.58 crore.

4.21.3 Four cases are shown in **Table no. 4.9** below:

(Rs. in lakh)

Table no. 4.9: Mistakes in summary assessments

Sl. no.	Name of the assessee/ CIT charge	Assessment year	Type/ month of assessment	Nature of mistake	Revenue impact
1	M/s Booz Allen & Hamilton (India) Ltd. DIT, Mumbai	2004-05	Summary February 2005	Excess set off of brought forward business loss of Rs. 1.22 crore.	66.30
2	M/s Kalahandi Anchalick Gramya Bank CIT, Sambalpur	2005-06	Summary September 2005	The assessee had debited a provision of Rs. 2.04 crore to the profit and loss account resulting in underassessment of income by a similar amount.	62.71 (P)
3	M/s D-2 International; CIT XVIII, Kolkata	2002-03	Summary February 2003	Excess claim of deduction of Rs. 60.94 lakh under section 80HHC.	24.71
4	M/s Ambika Cotton Ginning Factory CIT III, Baroda	2004-05	Summary December 2004	The assessee had not taken into account sales income of Rs. 52.74 lakh resulting in underassessment of income by a like amount.	20.67

4.21.4 The Ministry has accepted (December 2007) the audit observation in the case at **Sl. no. 2** of **Table no. 4.9** above.

Cases of over assessment/
overcharge

4.22 Audit noticed avoidable mistakes attributable to negligence on the part of the assessing officers resulting in overcharge of tax aggregating to **Rs. 1.97 crore** in **11 cases** in Bihar, Gujarat, Jharkhand, Maharashtra, Rajasthan and West Bengal. **Four cases** are shown in **Table no. 4.10** below:

(Rs. in lakh)

Sl. no.	Name of the assessee/ CIT charge	Assessment year	Type/ month of assessment	Nature of mistake	Revenue impact
1	Shri M. P. Ramachandran CIT I, Mumbai	1999-2000 2000-01	Scrutiny March 2004	Excess levy of interest of Rs. 43.15 lakh under section 234B.	43.15
2	M/s Panchdeep Consultant CIT IV, Ahmedabad	2002-03	Scrutiny September 2005	Excess levy of interest of Rs. 34.33 lakh under section 234A.	34.35
3	Shri H. H. Maharao Bhim Singh CIT, Kota	1998-99 1999-2000	Scrutiny March 2001	Excess levy of interest of Rs. 33.93 lakh under section 234A and 234B.	33.93
4	Shri Ketan B. Shah CIT I, Baroda	2000-01	Scrutiny March 2003	Excess levy of interest of Rs. 22.34 lakh under section 234B.	22.34

4.22.1 The Ministry has accepted (December 2007) all the audit observations in **Table no. 4.10** above.