

Chapter IV: Income Tax and Wealth Tax

4.1 Introduction

4.1.1 This chapter discusses 136 income tax and seven wealth tax cases, of which 133 cases involving undercharge of ₹ 183.53 crore and 10 cases involve overcharge of ₹ 277.64 crore which were issued to the Ministry during May 2016 to October 2016. These cases of incorrect assessment point towards weaknesses in the internal controls on the assessment process being exercised by the Income Tax Department.

4.1.2 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

4.1.3 The Ministry has conveyed its acceptance in 79 cases involving tax effect (TE) of ₹ 365.51 crore while not accepting two cases involving tax effect of ₹ 3.06 crore. ITD has completed remedial action in 132 cases involving tax effect of ₹ 451.93 crore and initiated remedial action in one case involving tax effect of ₹ 0.16 crore.

Table 2.6 (para 2.3.4) of this report shows the details of broad categories of mistakes and their tax effect (refer *Appendix 2.3*).

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 continuing weaknesses in the internal controls on the part of ITD which need to be addressed on the priority.

Table 4.1 shows the sub-categories of mistakes which impacted the quality of assessments.

Table 4.1: Sub-categories of mistakes under quality of assessments				(₹ in crore)
Sub-categories	Cases	TE	States	
a. Arithmetical errors in computation of income and tax	19	33.44	Bihar, Delhi, Madhya Pradesh (MP), Maharashtra, Odisha, Punjab, Rajasthan, and Uttar Pradesh (UP).	
b. Incorrect application of rates of tax, surcharge etc.	11	11.39	Delhi, Gujarat, Maharashtra, Rajasthan, Tamil Nadu (TN) and UP.	
c. Mistakes in levy of interest	36	61.97	Andhra Pradesh (AP), Delhi, Goa, Gujarat, Haryana, Kerala, Maharashtra, Punjab, Rajasthan, TN, UP and West Bengal (WB).	
d. Mistake in assessment while giving effect to appellate orders	02	0.47	Maharashtra, Rajasthan	
Total	68	107.27		

4.2.2 Arithmetical errors in computation of income and tax

We give below five such illustrative cases:

The Act 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 Delhi, CIT(Central)-2 charge, AO completed⁷⁹ the assessment of an individual, **Ramesh Chand** for AY 2012-13 in March 2015 at an income of ₹ 38.89 crore and tax of ₹ 12 crore thereon. While computing taxable income, AO computed the total disallowance on account of unexplained deposits in different bank accounts of the assessee at ₹ 38.79 crore instead of ₹ 44.12 crore. Further, AO did not levy interest under section 234A of the Act for non filing of return of income within due date. The mistakes resulted in under assessment of income of ₹ 5.33 crore involving short levy of tax and interest of ₹ 6.38 crore. *ITD rectified the mistake under section 154 of the Act (June 2015).*

4.2.2.2 In Odisha, CIT Sambalpur charge, AO completed the assessment of an AOP, **Bolangir District Central Co-operative Central Bank Ltd.** for AY 2012-13 after scrutiny in March 2014 at a loss of ₹ 29.77 crore. While computing the total income of the assessee, AO adopted returned income of ₹ (-)50.72 crore instead of ₹ (-)37.58 crore. Further, AO adopted the net profit as per profit and loss account at 'Nil' instead of ₹ (-)50.72 crore while quantifying the deduction under section 36(1)(vii) of the Act. The mistakes resulted in excess determination of loss of ₹ 16.94 crore involving potential tax effect of ₹ 5.24 crore. *The Ministry accepted the audit observation*

⁷⁹ Under section 153A read with section 144 of the Act

(December 2016) and rectified the mistake under section 147/143(3) (December 2015) and under section 154/147/143(3) (April 2016).

4.2.2.3 In Maharashtra, CIT Central IV charge, AO completed the assessment of an individual, **Manoj Kumar Babulal Punamiya** for AY 2010-11 after scrutiny in December 2011 at an income of ₹ 198.84 crore. AO made additions of ₹ 9.38 crore and ₹ 5.51 crore to the total income of the assessee on account of unexplained investment and short term capital gain respectively. However, only ₹ 5.51 crore had been considered for addition at the time of computation of total income and tax of the assessee. The mistake resulted in underassessment of income of ₹ 9.38 crore involving short levy of tax of ₹ 2.80 crore including interest. *The Ministry accepted the audit observation (November 2016) and rectified the mistake under section 154 (March 2016).*

4.2.2.4 In Delhi, CIT(Central)-1 charge, AO while completing the assessment of a company, **Sahara India** for AY 2011-12 after scrutiny in November 2014 at an income of ₹ 5.95 crore and tax of ₹ 1.84 crore thereon, computed the disallowances at ₹ 177.66 crore instead of ₹ 183.99 crore. The mistake resulted in underassessment of income of ₹ 6.33 crore involving short levy of tax of ₹ 1.95 crore. *ITD rectified the mistake under section 154 of the Act (December 2015).*

4.2.2.5 In Madhya Pradesh, CIT-1, Bhopal charge, AO completed⁸⁰ the assessment of an individual, **R. K. Lalwani** for AY 2010-11 in March 2015 at an income of ₹ 6.47 crore. While computing tax liability of the assessee, AO erroneously computed income tax at ₹ 0.93 crore instead of ₹ 1.93 crore resulting in short levy of tax of ₹ 1.56 crore including interest. *The Ministry accepted the audit observation and rectified the mistake under section 154 in August 2015.*

80 Under section 144/147 read with section 143(3) of the Act

4.2.3 Incorrect application of rates of tax and surcharge

We give below three such illustrative cases:

Section 115AD(1)(B) provides that where the total income of a foreign institutional investors (FII) arises by way of short term capital gain (STCG) or long term capital gain (LTCG) from the transfer of securities, the tax payable by the assessee on such total income shall be calculated at the rate of 30 per cent. Further, section 111A provides that if such transaction is chargeable to securities transactions tax (STT), the amount of income tax, calculated on income by way of STCG shall be at rate of 15 per cent.

4.2.3.1 In Maharashtra, CIT(IT) III charge, AO completed the assessment of trust, **Platinum Investment Management Ltd. A/c Platinum International Fund** for AY 2009-10 after scrutiny in November 2011 accepting the returned income of ₹ 19.47 crore with STCG derived at concessional rate of 15 per cent as per section 111A of the Act. As the STCG of ₹ 19.47 crore derived from trading activity in derivatives did not attract any STT and hence, the same was required to be charged at the rate of 30 per cent instead of 15 per cent, omission resulted in under assessment of income of ₹ 19.47 crore involving short levy of tax of ₹ 4.37 crore including interest. *ITD accepted and rectified the mistake under section 154 of the Act (March 2016).*

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

4.2.3.2 In Uttar Pradesh, CIT Ghaziabad charge, AO while completing the assessment of an individual, **Ram Kumar Tyagi** for AY 2008-09 under section 143(3) read with section 147 in February 2015 at an income of ₹ 7.91 crore including income from long term capital gain of ₹ 7.89 crore levied the tax on long term capital gain at the rate of 10 per cent instead of applicable rate of 20 per cent. The mistake resulted in short levy of tax of ₹ 3.04 crore including interest. *The Ministry accepted the audit observation (November 2016) and rectified the mistake under section 154 of the Act (January 2016).*

4.2.3.3 In Maharashtra, Pr. CIT III(Central) charge, AO completed the assessment of an AOP, **The Board of Control for Cricket in India** for AY 2005-06 after scrutiny in November 2007 at 'Nil' income. The income was reassessed under section 147 in May 2012 at an income of ₹ 168.60 crore. While computing tax liability of the assessee, AO did not levy education cess applicable⁸¹ for the AY 2005-06 resulting in short levy of tax of ₹ 1.11 crore. *ITD rectified the mistake under section 154 of the Act (January 2016).*

81 For AY 2005-06, education cess at the rate of two per cent leviable on the amount of income tax and surcharge

4.2.4 Mistakes in levy of Interest

We give below five such illustrative cases:

The Act 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 erstwhile Andhra Pradesh, CIT-IV Hyderabad charge, AO while completing the assessment of **Andhra Pradesh Housing Board** for AY 2010-11 under section 144 read with section 147 in November 2014 at an income of ₹ 466.65 crore, levied interest under section 234A at ₹ 42.76 crore for 30 months as against the leviable interest of ₹ 57.01 crore for 40 months, resulting in short levy of interest of ₹ 14.25 crore. *The Ministry accepted the audit observation (December 2016) and rectified the mistake under Section 154 of the Act (September 2015).*

4.2.4.2 In Delhi, CIT (C)-2 charge, AO completed the assessment of an individual, **Ramesh Chand** for AYs 2007-08, 2008-09, 2009-10, 2010-11 and 2011-12 under section 153A read with section 144 of the Act in March 2015 at income of ₹ 0.55 crore, ₹ 15.23 crore, ₹ 135.93 crore, ₹ 13.44 crore and ₹ 57.86 crore respectively. Consequent upon the search, notices under section 153A had been issued to the assessee on 19 September 2013 to furnish his return of income for AYs 2007-08 to 2011-12 within sixteen days of service of notice. Even though the returns of income of these assessment years were not filed by the assessee till the completion of assessment, AO did not levy interest under section 234A of the Act. Further, for AY 2011-12, assessed income of ₹ 56.86 crore was rounded off to ₹ 57.86 crore. The mistakes resulted in non levy of interest of ₹ 12.75 crore. *ITD rectified the mistake under section 154 of the IT Act (June 2015).*

4.2.4.3 In Haryana, Pr. CIT Panchkula charge, AO completed the assessment of **Haryana State Pollution Control Board** for AYs 2006-07, 2008-09, 2009-10, 2010-11 and 2011-12 under section 143(3) read with section 148 of the Act in January 2013 at income of ₹ 9.60 crore, ₹ 14.18 crore, ₹ 18.96 crore, ₹ 34.06 crore and ₹ 12.67 crore respectively. In response to notices issued under section 148 on 31 October 2012, assessee filed its returns of income for AYs 2006-07, 2008-09 to 2011-12 on 30 November 2012 and hence interest under section 234A was leviable from due date of filing of return till the actual date of filing of return for all the AYs. However, AO levied interest of ₹ 0.12 crore for these AYs instead of leviable interest of ₹ 10.86 crore resulting in short levy of interest of ₹ 10.74 crore. *ITD rectified the mistake under section 154 of the IT Act (January 2016).*

4.2.4.4 In Gujarat, Pr. CIT-III Ahmedabad charge, AO completed the assessment of an individual, **Rajeshsingh G Rajput** for AY 2011-12 under section 144 read with section 147 of the Act in March 2015 at an income of ₹ 23.88 crore. Though the assessee had not filed its return of income in response to the notice issued under section 148(March 2014), AO did not levy interest under section 234A of the Act for non filing of return of income. The mistake resulted in non levy of interest of ₹ 3.24 crore. *The Pr. CIT-3, Ahmedabad had given approval (January 2016) for taking remedial action under section 154.*

4.2.4.5 In Tamil Nadu, CIT-I Chennai charge, AO completed the assessment of a firm, **Rathna Stores** for AYs 2007-08 to 2012-13 under section 143(3) read with section 147 of the Act in March 2015. The assessee neither filed its return of income as required under section 139(1) nor filed the same in response to the notice issued under section 148(January 2014). However, AO levied interest under section 234A from the date of issue of notice instead of levying it from the due date of filing of returns. The mistake resulted in short levy of interest of ₹ 1.97 crore. *The Ministry accepted the audit observation and rectified the mistake under section 154 in February 2016.*

4.2.5 Mistakes in assessment while giving effect to appellate orders

We give below two such illustrative cases:

Under the Income Tax Act 1961, an aggrieved assessee can appeal to the Commissioner of Income tax (Appeals) against the order of assessing officer who shall comply with the direction given by him in the appellate order. At the time of giving appeal effect under section 250 of Income Tax Act, the Assessing officer has to compute correct total income after going through the appellate order and determine tax payable after effect of relief.

4.2.5.1 In Maharashtra, Pr CIT I Nagpur Charge, AO completed the assessment of co-operative society (Bank), **The Washim Urban Co-op. Bank Ltd.** for the assessment year 2010-11 after scrutiny in March 2013 at an income at ₹ 3.56 crore which was revised to ₹ 3.68 crore while giving effect to CIT(A)'s order in February 2015. The total income computed after giving effect to CIT(A)'s order was wrongly entered into the ITD system at ₹ 2.86 crore and hence tax was levied at ₹ 88.47 lakh instead of correct amount of ₹ 1.14 crore resulting in short levy of tax of ₹ 25.35 lakh including interest. *The Ministry accepted the audit observation and rectified the mistake under section 154 in December 2015.*

4.2.5.2 In Rajasthan, CIT-III Jaipur charge, AO completed the assessment of an individual **Manoj Kumar Johari** for AY 2010-11 after scrutiny at an income of ₹ 1.34 crore in December 2012 which was revised at an income of

₹ 1.03 crore under section 250 in November 2013. The CIT(Appeals) vide his order of September 2013, allowed relief of ₹ 29.62 lakh against the disallowance made under section 80IB of ₹ 31.17 lakh, and dismissed the assessee's appeal regarding income of duty draw back of ₹ 1.80 crore and sale of import license of ₹ 4.68 lakh aggregating to ₹ 1.85 crore for forming part of net profit for claiming deduction under section 80IB. Further, the profit and loss account showed that there was net profit of ₹ 1.32 crore including duty draw back and sale of import license of ₹ 1.85 crore. Since the income of duty draw back and sale of import license is not eligible for exemption under section 80IB, there was a net loss of ₹ 53.11 lakh for claiming deduction under section 80IB. The deduction/relief of ₹ 29.62 lakh allowed under section 80IB was therefore not in order. The omission resulted into incorrect allowance of exemption of ₹ 29.62 lakh involving short levy of tax of ₹ 12.26 lakh including interest. *The Ministry accepted the audit observation and rectified the mistake under section 154 in October 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	06	3.92	Andhra Pradesh, Gujarat, Haryana, Jharkhand, UP and WB.		
b. Irregular exemptions/deductions/relief given to Trusts/Firms/Societies/AOPs	17	41.09	AP, Delhi, Gujarat, Haryana, Himachal Pradesh (HP), Jharkhand, MP, Maharashtra and WB.		
c. Incorrect allowance of Business Expenditure	06	2.56	Bihar, Delhi, Odisha, UT Chandigarh, Uttrakhand and WB.		
d. Irregularities in allowing depreciation/business losses/capital losses	09	15.71	Gujarat, Karnataka, Maharashtra, Odisha, UT Chandigarh and WB.		
Total	38	63.28			

4.3.2 Irregular exemptions/deductions/relief to Individuals

We give below four such illustrative cases.

Section 54F of the Income Tax Act provides that to claim the exemption under this section, the assessee should not own more than one residential house, other than the new asset, on the date of transfer of the original asset.

4.3.2.1 In AP, CIT-Central, Hyderabad charge, AO completed the assessment of an individual, **Sabbineni Surendra** for AY 2010-11 under section 143(3) read with section 153A in March 2014 at an income of ₹ 22.31 crore. Though the assessee had seven residential house properties on the date of transfer of shares held in M/s Coastal Projects Ltd., AO allowed deduction of ₹ 9.54 crore under section 54F of the Act. The mistake resulted in under assessment of income of ₹ 9.54 crore involving short levy of tax of ₹ 2.91 crore including interest. *ITD did not accept the audit objection stating that the properties were let out for commercial purpose and the term residential house was not defined in the Act and the same was to be interpreted as per usage of the property.* The reply of ITD is not tenable, because, as per the agreements, the nature of the properties was residential only and the assessee has further shown the income from these units under the head 'Income from House Property'. *ITD rectified the mistake under section 263 of the Act (March 2016).*

Section 54EC(1) of the Income Tax Act provides that where the capital gain arises from the transfer of a long-term capital asset (the capital asset so transferred being hereafter in this section referred to as the original asset) and the assessee has, at any time within a period of six months after the date of such transfer, invested the whole or any part of capital gains in the long-term specified asset, the capital gain to the extent is exempt from tax. Further, in the Judgment of jurisdictional ITAT in the case of Smt. Dakshaben R. Patel v/s ACIT Circle-2(1), Vadodara [(2012) 22 Taxmann.com 237 (Ahd.)] where in it was held that "where the assessee purchased REC Bonds prior to the date of sale of property, exemption under section 54EC is not allowable".

4.3.2.2 In Gujarat Pr. CIT III Ahmedabad charge, AO completed the assessment of an individual, **Rajendra H. Prajapati** for AY 2011-12 after scrutiny in February 2014 at an income of ₹ 28.53 lakh. The assessee had earned long term capital gain of ₹ 8.04 crore by sale of three units of land and claimed deduction of ₹ 1.50 crore under section 54EC as investment in REC bonds despite the fact that REC bonds valuing ₹ 50 lakh were purchased on 31 March 2010, i.e. prior to the date of transfer of properties which was not admissible. Further, the assessee had purchased REC bond for ₹ 50 lakh each on 21 July 2010 and 08 April 2011, whereas capital gain of ₹ 55.10 lakh only was available for investment at the time of purchase of REC bonds. Hence, deductions claimed and allowed for investments in REC Bonds of

₹ 94.90 lakh was irregular. The mistake resulted in underassessment of income of ₹ 94.90 lakh involving short levy of tax of ₹ 26.39 lakh including interest. *The Pr. CIT-3, Ahmedabad had given approval (July 2015) for taking remedial action under section 263 of the Act.*

4.3.2.3 In West Bengal, CIT-17, Kolkata charge, AO completed the assessment of an individual, **Manas Roy Chowdhury** for AY 2012-13 after scrutiny in March 2015 at an income of ₹ 28.07 lakh. The assessee converted the value of flat as capital asset from stock in trade at the total consideration of ₹ 76.40 lakh and AO assessed the conversion of stock in trade into capital asset as short term capital gain of ₹ 76.40 lakh and allowed deduction of ₹ 50 lakh under section 54EC for investing the same into taxable bonds of REC. However, since the capital gain was not due to transfer of any long-term capital asset, deduction of ₹ 50 lakh was not admissible to the assessee. The irregular deduction resulted in underassessment of income of ₹ 50 lakh involving short levy of tax of ₹ 21.94 lakh. *The Ministry accepted the audit observation and rectified the mistake under section 154 in January 2016.*

Section 10B of the IT Act, 1961, provides 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 ten consecutive assessment years. Moreover, it was clarified that deduction to such units in any case will not be available after assessment year 2009-10

4.3.2.4 In UP, Pr. CIT-1, Kanpur charge, AO completed the assessment of an individual **Upendra Singh** for AY 2010-11 after scrutiny in March 2015 at an income of ₹ 3.90 lakh after allowing deduction of ₹ 49.12 lakh under section 10B. The assessee commenced operation as Domestic Tariff Area (DTA) unit and was accorded the status of 100 percent EOU in November 2002. However, deduction of ₹ 49.12 lakh under section 10B was allowed even though eligible period was over by AY 2009-10. Irregular allowance of deduction beyond the permissible period resulted in under assessment of income of ₹ 49.12 lakh involving short levy of tax including interest of ₹ 20.33 lakh. *ITD rectified the mistake under section 147 of the IT Act (February 2016).*

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

We give below four such illustrative cases.

4.3.3.1 In AP Pr. CIT, Vijayawada charge, AO completed the assessment of an assessee, **V. G. T. M. Urban Development Authority** for AYs 2009-10 and 2010-11 after scrutiny in November 2011 and December 2012 respectively at

'Nil' income. The assessee had claimed and was allowed the deduction of amounts of ₹ 11.02 crore and ₹ 9.72 crore for AY 2009-10 and 2010-11 respectively towards sinking fund. As the amount debited towards sinking fund was merely a provision to meet the future expenditure, the same was required to be added back to taxable income. Omission resulted in short computation of income of equal amounts for the AYs 2009-10 and 2010-11 with a short levy of tax of ₹ 3.83 crore and ₹ 4.14 crore respectively including interest besides potential tax effect of ₹ 1.10 crore for the AY 2009-10. *ITD accepted the audit observations and rectified the mistakes 147 (March 2015).*

4.3.3.2 In Maharashtra, Pr. CIT-III Nagpur charge, AO completed the scrutiny assessment of a co-operative bank, **The Gondia District Central Co-operative Bank Ltd.** for the AYs 2007-08, 2008-09, 2009-10 and 2010-11 in January 2013 and November 2011⁸² at an income of ₹ 5.63 crore, ₹ 8.14 crore, ₹ 9.94 crore and ₹ 14.05 crore respectively. While computing total income, AO allowed deduction under section 36(1)(viiia) of ₹ 0.62 crore, ₹ 0.66 crore, ₹ 0.81 crore and ₹ 1.14 crore being 7.5 per cent of the total income as claimed by the assessee but disallowed deduction of ₹ 7.61 crore, ₹ 8.14 crore, ₹ 9.94 crore and ₹ 14.05 crore being 10 per cent of aggregate average advances made by rural branches of the bank for the respective years on the ground that the assessee is not a schedule bank. Against the appeal filed by the assessee, CIT(A) in March 2014 held that the deduction under section 36(1)(viiia) to be limited to the actual amount debited on account of provisions of bad and doubtful debts to the books of accounts of the appellant. However, while giving effect to CIT(A) order, AO allowed entire deduction as claimed by the assessee of ₹ 8.23 crore, ₹ 8.80 crore, ₹ 10.75 crore and ₹ 15.19 crore as against ₹ 5.39 crore, ₹ 6.13 crore, ₹ 2.99 crore and ₹ 5.81 crore debited on account of provisions for bad and doubtful debts in the books of accounts for the respective years. This resulted in excess deduction of ₹ 22.65 crore (₹ 2.84 crore + ₹ 2.67 crore + ₹ 7.76 crore + ₹ 9.38 crore) involving short levy of tax of ₹ 7.37 crore excluding interest. *ITD accepted the objection and rectified the mistake under section 154 (March 2015) and demand raised of ₹ 6.99 crore was recovered in March 2015 as against ₹ 7.37 crore as worked out by audit for all the assessment years. ITD further replied (December 2015) that notice under section 154 has been issued for differential amount of ₹ 0.38 crore.*

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Section 11(1)(a) of the Act provides for the accumulation of 15 *per cent* of the income derived from property held under trust wholly for charitable or religious purposes. Further section 11(4A) provides that if any business is incidental to the attainment of the objectives of the trust and a separate books of account are maintained by such trust or institution in respect of such business, then the profits and gains of business should be included in the income of such trust and 15 per cent of total income including the profits and gains from business should be allowed to accumulated under the provisions of Section 11(1)(a) of the Act.

4.3.3.3 In WB, DIT-Exemption charge, AO completed the assessment of a trust, **Sunmarg Welfare Society** for AY 2011-12 was under section 144 in March 2014 at an income of ₹ 24.96 lakh. While finalizing the assessment, AO allowed exemption (15 *per cent*) on gross receipt of ₹ 38.83 crore instead of income of ₹ 7.82 crore from different heads. The mistake resulted in under assessment of income of ₹ 4.65 crore involving tax effect of ₹ 1.96 crore. *ITD stated (June 2014) that accumulation under section 11(1) should be allowed on the gross income from finance activity plus income from other sources.* Reply of ITD is not tenable on the grounds that as per section 11(4A), the profits and gains of business activity should be included in the total income of the assessee and the accumulation should be provided on the total income of the assessee considering the gains from the business activity and not the total receipts from the business activity. *The Ministry accepted the audit observation and rectified the mistake under section 144/147 in March 2016.*

Section 40(b) of the Act provides that interest on partner's capital and remuneration to working partners are allowable for computation of income of a firm, if the Partnership Deed permits such payments to the partners. These are taxable in the hands of the partners, but the share of profit received from the firm is exempt in the hands of the partners. Further, as per section 80IB(10) of the Act, deduction in the case of an undertaking developing and building housing projects approved before the 31st day of March 2008 by a local authority shall be hundred per cent of the profits derived in the previous year relevant to any assessment year from such housing project.

4.3.3.4 In Gujarat, Pr. CIT-1, Surat charge, AO completed the assessment of a Firm, **Nilkanth Developers** for AY 2010-11 after scrutiny in March 2013 at 'Nil' income. It was noticed from clause 6 and 7 of Partnership Deed that provision had been made for payment of interest to Partners at the rate of 12 *per cent* and remuneration to its three working partners at the rate of 33 *per cent*, 33 *per cent* and 34 *per cent*. However, in the Profit & Loss Account, assessee had not debited any amount towards Interest or remuneration to partners though such payments were required to be made

by the firm as per the Partnership Deed. Further, the assessee firm had claimed and was allowed the entire profit of ₹ 3.18 crore as deduction under section 80IB(10) of Act. Had the profit been calculated after allowing deduction of interest on capital and remuneration to partners, the profit of the firm would have been less to that extent and the partners would have been liable for payment of tax on interest and remuneration received. The mistake resulted into excess deduction to the extent of unpaid interest of ₹ 37.19 lakh and remuneration of ₹ 1.69 crore aggregating to ₹ 2.07 crore involving short levy of tax of ₹ 63.85 lakh in the hands of the partners. *ITD accepted the audit observation and took remedial action under section 143(3) read with section 147 (February 2016).*

4.3.4 Incorrect allowance of Business Expenditure

We give below three such illustrative cases.

Section 43B of the Income Tax Act 1961 provides that any sum payable by the assessee by way of tax, duty, cess or fee, by whatever name called, under any law for the time being in force, shall be allowed as deduction only on actual payment.

4.3.4.1 In Delhi, Pr. CIT 21 charge, AO while completing the scrutiny assessment of **Brij Gopal Construction Company** for AY 2009-10 in December 2011 at an income of ₹ 1.37 crore and a tax of ₹ 46.62 lakh, allowed deduction of ₹ 2.08 crore on account of provision for sales tax debited to the Profit and Loss account. As the said amount was not actually paid during the year, it was required to be disallowed and added back to the taxable income. The omission resulted in underassessment of income of ₹ 2.08 crore involving short levy of tax of ₹ 70.65 lakh. *The Ministry accepted the audit observation and rectified the mistake under section 154 in August 2015.*

Section 40A(3) of the Act provides that where one incurs any expenditure in respect of which a payment 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 except in the cases and circumstances specified below Rule 6DD of Income Tax Rules, 1962.

4.3.4.2 In Uttaranchal Pr. CIT, Dehradun charge, while completing the assessment of an individual, **Itisha Goyal** for AY 2012-13 after scrutiny in February 2015 at an income of ₹ 40.13 lakh, AO allowed expenditure of ₹ 1.33 crore on account of purchase of land, cost of which was paid in cash. Audit noticed that the assessee was engaged in the business of development of land and sale of plots and hence was not allowed to make cash payment for such activity in excess of ₹ 20,000. The claim of expenditure for payment made in cash should have been disallowed by the AO at the time of assessment and expenditure added to the taxable income of the assessee.

The omission resulted in short levy of tax of ₹ 55.48 lakh including interest. *The Ministry did not accept the observation stating that the land purchased were agricultural land which were converted into stock in trade after purchase and were a capital asset at the time of purchase. Further, since the lands were purchased as a capital asset it was investment and not the expenditure, hence provisions of section 40A(3) are not applicable. The reply was not tenable as the assessee deals in sale and purchase of land/plots and after purchase of the said agricultural land, the assessee got it converted into residential plots in a colony, which clearly transpires the intention and modus operandi of the assessee to conduct its business for a good profit attracting the provisions of the section 40A(3). Further, the transactions for which payments were made were not covered by cases and circumstances specified below Rule 6DD of Income Tax Rules 1962. Judicial decision⁸³ that if the transaction is in the assessee line of business even a single transaction of dealing in land estate is an adventure in nature of trade, is also relevant.*

4.3.4.3 In Pr.CIT-1 Chandigarh charge, AO while completing the assessment of an individual, **Sewak Ram** for AY 2009-10 after scrutiny in December 2011 at income of ₹ 11.33.crore, allowed expenditure of ₹ 94.86 lakh under the head purchases which was paid in cash. As the payments were made in contravention of provision of section 40A(3) of the Act, the same was required to be disallowed and added back to the taxable income of the assessee. The omission resulted in under assessment of income of ₹ 94.86 lakh involving tax effect of ₹ 45.46 lakh including interest. *The Ministry accepted the audit observation (December 2016) and rectified the mistake under section 143(3) read with section 147 (March 2016).*

4.3.5 Irregularities in allowing depreciation/business losses/capital losses

We give below four such illustrative cases:

CBDT vide instruction no. 09/2007 dated 11.09.2007 has highlighted the instances in which substantial loss of revenue has occurred due to incorrect allowance of depreciation and incorrect set off of brought forward losses. Therefore, the Board directed that AOs should carry out necessary verifications at the time of undertaking scrutiny assessments with reference to physical records and the claims related to losses including unabsorbed depreciation should be linked with the assessment records so as to ensure correctness of the allowance of claims of brought forward losses and depreciation.

4.3.5.1 In Maharashtra, Pr. CIT 6 Pune Charge, AO completed the assessment of a co-operative society, **Loknete Baburao Patil SSK Ltd.** for AY 2010-11 after scrutiny in December 2012 at an income of ₹ 53.63 crore. The assessee filed its return of income for AY 2010-11 at 'Nil' after setting off of brought

83 Saroj Kumar Majumdar Vs CIT (371 ITR 242) (SC)

forward business losses and depreciation aggregating ₹ 8.29 crore pertaining to AYs 2005-06, 2007-08, 2008-09 and 2009-10. However, the losses pertaining to AYs 2005-06 and 2007-08 were already set off against income of AYs 2008-09 and 2009-10. Hence, incorrect set-off of losses resulted in underassessment of income of ₹ 8.29 crore involving short levy of tax of ₹ 2.56 crore. *The Ministry accepted the audit observation (November 2016) and rectified the mistake under section 154 (June 2014).*

Section 72 provides for carry forward and set off of net loss of an assessment year against profits and gains of the following eight AYs. Under the Act, an Assessing Officer is required to determine and assess the income or loss correctly in scrutiny assessment and allow set off and carry forward of losses accordingly. Further, CBDT vide instruction No.574 dated 27-07-1973 to all Assessing Officer directed that over assessment resulting into exaggerated demands unnecessarily inflating arrear figures needed to be avoided.

4.3.5.2 In Odisha, CIT Cuttack charge, AO completed the assessment of a co-operative bank, **Cuttack Central Co-operative Bank Ltd.** for AY 2012-13 after scrutiny in March 2015 at an income of ₹ 35.79 crore. It was noticed that the brought forward losses of ₹ 5.71 crore of AY 2011-12 were not allowed to set off against the income of AY 2012-13 resulting in over assessment of income to that extent involving tax effect of ₹ 2.51 crore. *ITD rectified the mistake under section 154 of the Act (July 2015). However, Ministry did not accept (August 2016) the audit observation stating that order under section 154 was made on 03 July 2015 suo moto, before the objection was communicated.* The reply of the Ministry is not factually correct as the audit observation was communicated to the AO on 02 July 2015 and after going through the observation, the AO rectified the mistake on 03 July 2015.

4.3.5.3 In Gujarat, Pr. CIT Valsad Charge, AO completed the scrutiny assessment of an AOP, **Maroli Vibhag Khand Udhog Sahkari Mandali Ltd.** for AY 2011-12 in February 2014 at 'Nil' income after setting off of unabsorbed business losses of ₹ 27.60 crore to the extent of income. AO further allowed carry forward of business loss of ₹ 4.29 crore pertaining to AY 2009-10 and unabsorbed depreciation of ₹ 13.24 crore pertaining to AYs 2003-04 to 2009-10. However, business loss of AYs 2003-04 to 2006-07 had already been set-off against the income of AY 2008-09 and amount of ₹ 18.12 crore (₹ 2.33 crore for AY 2006-07 + ₹ 15.79 crore for AY 2009-10) was only available for set-off instead of ₹ 27.60 crore in AY 2011-12. Hence, carry forward of business loss of ₹ 4.29 crore of AY 2009-10 was incorrect as the loss should have been set off against the income of AY 2011-12. The mistake resulted into excess carry forward of losses of ₹ 4.29 crore involving short levy of potential tax of ₹ 1.21 crore and positive tax of ₹ 12.22 lakh

aggregating to ₹ 1.33 crore. ITD rectified the mistake under section 155(4) (February 2015).

4.3.5.4 In Karnataka, CIT-Central Bangalore charge, AO completed the assessment of an individual, **B. V. Sreenivasa Reddy** for AY 2012-13 under section 143(3) read with section 147 in March 2015 at an income of ₹ 1.30 crore. The assessee filed its return of income of ₹ 0.34 lakh after setting off of brought forward business loss of ₹ 1.64 crore even though there was no loss available for set off. Incorrect setting off of loss of ₹ 1.64 crore resulted in short levy of tax of ₹ 81.06 lakh including interest. ITD accepted the audit objection and rectified the mistake under section 154 (March 2016).

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 due to omissions				(₹ in crore)
Sub-categories	Nos.	TE	States	
a. Incorrect classification and computation of capital gains	07	5.60	Gujarat, Rajasthan, TN and UP	
b. Incorrect computation of income	08	6.27	Gujarat and Maharashtra	
c. Omissions in implementing provisions of TDS/TCS	03	1.18	Chhattisgarh, Jharkhand and UP	
d. Unexplained Investment/cash credit	02	0.33	Chhattisgarh and Haryana	
e. Incorrect estimation of Arm's Length Price	01	1.64	AP	
f. Non-levy/short levy of Wealth Tax	07	0.47	Gujarat, Karnataka, Rajasthan and WB	
Total	28	15.49		

4.4.2 Incorrect classification and computation of Capital Gain

We give below two such illustrative cases:

Section 50C provides that where the consideration received or accruing, as a result of the transfer by an assessee of a capital asset being land or building or both, is less than the value adopted by any Stamp Value Authority of a State Government for the purpose of payment of stamp duty in respect of such transfer, the value determined by state Government be deemed to be full value of consideration received or accruing as a result of such transfer.

4.4.2.1 In Rajasthan, CIT-I Jaipur charge, AO completed the assessment of an individual, **Sunil Sankhala** for AY 2011-12 after scrutiny in March 2014 at an income of ₹ 27.94 lakh. The assessee purchased agriculture land during FY 2006-07 for ₹ 19.27 lakh and incurred ₹ 5.62 lakh for conversion of land use from agriculture purpose to residential purpose and hence the total cost of acquisition was ₹ 24.89 lakh. The assessee sold the land for a total sale consideration of ₹ 53.00 lakh during FY 2010-11 and shown transaction under the head of income from business for ₹ 27.94 lakh. The value of converted residential land for the purpose of stamp duty was determined at ₹ 8.23 crore by Stamp Registration Department. This sale transaction has resulted into long term capital gain of ₹ 7.90 crore. The omission resulted in under computation of long term capital gain by ₹ 7.62 crore involving tax effect of ₹ 2.12 crore including interest. *ITD rectified the mistake by passing order under section 263 prejudicial to interest of revenue and set aside for afresh orders (February 2016).*

Section 45(1) of the Act provides that any profit and gains arising from the transfer of a capital asset shall be chargeable to income tax under the head 'capital gains' and is taxable in the year in which the transfer took place.

4.4.2.2 In Gujarat, Pr. CIT-III, Ahmedabad Charge, AO completed the assessment of an Individual, **Ileshbhai P. Shah** for AY 2012-13 after scrutiny in June 2014 at returned income of ₹ 2.82 crore. The assessee had purchased two agriculture lands at Gandhinagar for ₹ 7.61 lakh and ₹ 10.51 lakh in March 2009 and sold both lands for ₹ 84.00 lakh and ₹ 1.16 crore respectively in May 2011. The assessee had declared short term capital gain (STCG) of ₹ 64.81 lakh from the sale of land at Gandhinagar after deducting acquisition cost of ₹ 19.19 lakh (of both the lands) from sale value of ₹ 84.00 lakh. However, the assessee had not offered for taxation the sale consideration of ₹ 1.16 crore received from the second land. The mistake resulted in underassessment of STCG of ₹ 1.16 crore involving short levy of tax of ₹ 45.52 lakh including interest. ITD stated that the objection is acceptable and proposal for remedial action had been submitted to Pr. CIT-3 Ahmedabad.

4.4.3 Incorrect computation of income

We give below two such illustrative cases:

4.4.3.1 In Maharashtra, Pr CIT I Pune Charge, AO completed the scrutiny assessment of an AOP (co-operative society), **Vridheshwar Sahakari Sakhar Karkhana Ltd.** for AY 2009-10 in November 2011 at 'Nil' income after setting off of brought forward losses. In the assessment order, AO did not make any addition on account of excess cane purchase price stating that the assessee paid the price below Statutory Minimum Price (SMP) for both the seasons 2007-08 and 2008-09. Further, the assessee had paid additional sugarcane price of ₹1600 PMT to the members and ₹ 1595.63 PMT to non-members for season 2008-09. However, the sugar cane price worked out as per Government's instructions⁸⁴ of ₹ 1300.03 only should have been considered for 165832 MT (57804 MT to members and 108028 MT to Non members) the sugar cane purchased during season 2008-09. Adjustment of extra cane price was not in accordance with the formula prescribed for sugar cane price under clause 5A by Sugarcane (Control) Order 1966. The excess payment of sugar cane price of ₹ 4.93 crore resulted in underassessment of income to that extent involving potential short levy of tax of ₹ 1.52 crore. *The Ministry accepted the audit observation (December 2016) and rectified the mistake by passing order under section 143(3) r.w.s. 147 (March 2015).*

4.4.3.2 In Gujarat, Pr. CIT Valsad Charge, AO completed the assessment of an individual, **Sanjit J. Biswas** for AY 2011-12 after scrutiny at an income of ₹ 26.13 lakh in January 2014. In the assessment order, it was noticed that the assessee had failed to record job work receipt of ₹ 64.23 lakh. Further, AO assessed that cash deposit of ₹ 84.75 lakh in the bank was the unrecorded receipts and the same was required to be taxed. However, AO had added profit of ₹ 16.80 lakh only on account of suppressed receipt not recorded in the books of account and cash deposit, Since, the assessee did not produce any evidence in support of said cash deposit and admitted suppression of job work receipt, the total amount of ₹ 1.49 crore was required to be disallowed. The omission resulted in under assessment of income of ₹ 1.32 core (₹ 1.49 crore - ₹ 16.79 lakh) with consequent short levy of tax of ₹ 54.74 lakh. *The Ministry accepted the audit observation and rectified the mistake under section 144 read with section 147 in March 2016.*

84 Clause 5A of the Sugarcane (Control) Order 1966 (SMP+5A)

4.4.4 Omissions in implementing provisions of TDS/TCS

We give below one such illustrative case.

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

4.4.4.1 In Pr. CIT Allahabad charge, AO while completing the assessment of an individual, **Lal Chand Yadav**, for AY 2009-10 in November 2011 at an income of ₹ 55.91 lakh allowed expenses made by assessee amounting to ₹ 1.83 crore towards 'Crain Hire Charges' on which tax has not been deducted while making payments. The mistake resulted in under assessment of income of ₹ 1.83 crore having a tax effect of ₹ 82.30 lakh including interest. *The Ministry accepted the audit observation and rectified the mistake under section 143(3)/263 in March 2015.*

4.4.5 Unexplained Investment

We give below two such illustrative cases.

Section 69C of Income Tax Act provides that where in any financial year, an assessee has incurred any expenditure and he offers no explanation about the source of such expenditure or part thereof, or the explanation, if any, offered by him is not, in the opinion of the Assessing officer, satisfactory, the amount covered by such expenditure or part thereof, as the case may be, may be deemed to be the income of the assessee for such financial year.

4.4.5.1 In Pr. CIT Gurgaon charge, AO completed the assessment of an individual, **Naresh** for AY 2009-10 after scrutiny in December 2015 at an income of ₹ 128.61 lakh. During assessment proceedings, the assessee did not provide explanation in respect of the cash deposits of ₹ 59.50 lakh in Axis Bank, Sector-14, Gurgaon and ₹ 111.89 lakh in State Bank of Hyderabad, VPO Narsingpur. While completing the assessment, AO added back unexplained deposit of ₹ 1.12 crore treating it as 'income from undisclosed sources' whereas the amount of ₹ 59.50 lakh remained to be added back. The omission resulted into under assessment of income of ₹ 59.50 lakh including tax effect of ₹ 20 lakh. *ITD rectified the mistake under section 154 (December 2015).*

4.4.5.2 In Chhattisgarh CIT Bilaspur charge, AO completed the assessment of an individual, **Bishambhar Dayal Agrawal** for AY 2010-11 after scrutiny in March 2013 at an income of ₹ 10.00 lakh and the source of receipt of assessee was mainly from State Government Department i.e. from PWD. Examination of details annexed with Form 16A issued by the PWD revealed that the department has deducted a sum of ₹ 30.45 lakh towards

Performance Guarantee and other deposit from the gross amount of bill. These deductions are depository in nature and refundable after a period of time mutually agreed upon. Thus the same should have been shown under deposit head in asset side of balance sheet. It was however seen from the Balance Sheet that these deductions were not accounted for at all which indicates that these deductions are met out of other source of income which should have been disallowed and added back to the income of the assessee as undisclosed investments under section 69 of the Act. Omission to do so resulted in under assessment of income to that extent involving short levy of tax of ₹ 12.80 lakh including interest. *ITD rectified the mistake under section 143(3)/147 of the Act (January 2015).*

4.4.6 Incorrect estimation of Arm's Length Price

The Computation of Arms Length Price (ALP) under section 92C of Income Tax Act 1961, should be referred to the Transfer Pricing Officer (TPO). The TPO, after hearing the assessee, the evidence produced by him after considering the evidence as required on any specified points and after taking into account all relevant materials which he has gathered, shall by order, in writing, determine the ALP in relation to the international transaction in accordance with provisions of Section 92C(3) and send a copy of his order to the Assessing Officer and to the assessee. Further, under section 92E, the person who entered into an international transaction shall obtain a report from an Accountant in prescribed form 3CEB showing all details relevant to international transactions.

4.4.6.1 In AP, CIT(IT & TP) charge, the Transfer Pricing Officer (TPO-3) made adjustment of ₹ 2.96 crore for AY 2012-13 in January 2016 in the case of **Value Labs LLP**. The adjustments were made in respect of transactions with three Associated Enterprises (AE's) reported in Form 3CEB. However, an International transaction of ₹ 67.41 crore with AE M/s Value Lab FZ LLC, UAE was not reported in 3CEB and hence not included in the Operating Revenue of ₹ 42.14 crore. The value of sale (operating Revenue) to AEs thus worked out to ₹ 109.54 crore (₹ 42.14 + ₹ 67.41). After considering the Arm Length Price, proportionate operating cost comes to ₹ 117.41 crore and price received against this amounted to ₹ 109.54 crore. Hence adjustment under section 92CA comes to ₹ 7.87 crore and not ₹ 2.81 crore made by the TPO. The omissions resulted in short adjustment of ₹ 5.05 crore involving short levy of tax of ₹ 1.64 crore. *The Ministry accepted the audit observation (December 2016) and rectified the mistake under section 154 (March 2016).*

4.4.7 Non-levy/short levy of Wealth Tax

Seven cases of Wealth Tax involving tax effect of ₹ 0.47 crore were reported to the Ministry during May 2016 to October 2016. We found that AO did not comply with CBDT's instructions⁸⁵ in these cases in Gujarat, Karnataka, Rajasthan and West Bengal. We give below one such illustrative case.

4.4.7.1 The Income-Tax scrutiny assessments of an individual, **A. Abdul Rafeekh** for AYs 2008-2009 to 2012-2013 were completed by the Deputy Commissioner of Income Tax, Central Circle-2(2), Bangalore in March 2014. It was noticed that the assessee had a net wealth of ₹ 18.46 crore for AYs 2008-2009 to 2012-2013. However, neither the assessee filed the return nor the department initiated any wealth tax assessment proceedings. The omission resulted in wealth escaping assessment of ₹ 18.46 crore with a consequential tax effect of ₹ 23.45 lakh including interest under section 17 B of the Act. *ITD rectified the mistake under section 16(3) r.w.s. 17 of the Wealth tax Act, 1957 (October 2015).*

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 ₹ 275.13 crore in Assam, Delhi and Punjab. We give below two such illustrative cases.

4.5.1.1 In Punjab, CIT Central Ludhiana charge, AO completed the assessment of **Tilak Raj Bedi**, Proprietor of Puneet Exports for AY 2007-08 under section 144 read with section 153 in November 2013 at an income of ₹ 34.02 crore. While computing the tax demand, AO charged interest of ₹ 9.07 crore under section 234B for the period of 80 months instead of correct amount of ₹ 5.33 crore for the period of 47 months. The mistake resulted in excess levy of interest of ₹ 3.74 crore under section 234B. *ITD rectified the mistake under section 154 (December 2015).*

4.5.1.2 In Assam, Pr. CIT-2, Guwahati charge, AO while completing the assessment of an individual **Sovinder Singh Sethi** for AY 2008-09 under Block assessment in March 2014 at an income of ₹ 22.58 lakh, computed tax liability at ₹ 31.55 lakh instead of ₹ 6.86 lakh. The mistake resulted in over charge of tax of ₹ 24.69 lakh. *The Ministry accepted the audit observation and rectified the mistake under section 154 in October 2015.*

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