Chapter III: Corporation Tax

3.1 Introduction

3.1.1 This Chapter discusses the result of audit of assessments related to corporation tax audited during 2018-19. A total of 7.99 lakh returns[56] were filed by corporate assessees during the FY 2017-18. The ITD completed a total of 1,12,685 corporation tax scrutiny assessments in FY 2017-18 and 27,738 corporation tax scrutiny assessments in earlier years in those units which were audited during 2018-19. Out of the total 1,40,423 corporation tax scrutiny assessments, we checked 1,11,212 corporation tax scrutiny cases (99,316 assessment cases pertaining to FY 2017-18 and 11,896 assessments cases pertaining to earlier years) and found errors in 7,446 assessments. The incidence of errors in corporation tax scrutiny assessments checked in audit during 2018-19 was 6.70 *per cent* which was lower than the corresponding figure (8.15 *per cent*) during 2017-18. As we have examined a limited number of assessment cases/records as per our sample, the Ministry needs to verify this in entirety. The nature of the errors points to manual override of the AST. The department needs to investigate such cases and take action as per law against the officials concerned.

3.1.2 A total of 316 high value corporation tax cases were referred to the Ministry during July 2019 to November 2019. Of these, 304 cases involve undercharge of ₹ 7,977.77 crore and 12 cases involve overcharge[57] of ₹ 232.66 crore. These cases of incorrect assessment point towards weaknesses in the internal controls in the assessment processes of the ITD.

3.1.3 The categories of errors have been broadly classified as follows:

- Quality of assessments
- Administration of tax concessions/ exemptions/ deductions
- Income escaping assessments due to errors
- Others – Overcharge of tax/ Interest etc.

The deficiency noticed in the Assessment Information System[58] (AST) module/ Income Tax Business Applications[59] (ITBA) with respect to computation of interest under sections 234A, 234B, 234C and 244A of the Income Tax Act,

56 Source: CBDT

57 Overcharge is on account of errors in adoption of correct figures, arithmetical errors in computation of income, incorrect application of rates of tax/interest etc.

58 The AST module is an online, menu driven software capable of carrying out all assessment and related functions.

59 ITBA is a software application developed for computerising all internal processes of Income Tax Department.

1961 has been brought out in separate Chapter V on SSCA on 'Interest under sections 234A, 234B, 234C and 244A of the Act' of this Audit Report. Table 2.10 (*Para 2.4.4*) shows the details of broad categories of errors in assessments and their tax effect.

3.1.4 The Ministry has conveyed its acceptance of audit observations in respect of 82 cases involving tax effect of ₹ 828.03 crore while not accepting five cases involving tax effect of ₹ 89.33 crore. In one case the Ministry has conveyed partial acceptance involving tax effect of ₹ 118.45 crore. In the remaining 228 cases, the Department has accepted 61 cases involving tax effect of ₹ 1,415.74 crore while not accepting nine cases involving tax effect of ₹ 89.89 crore (*referred to in para 2.4.4*). Out of 316 cases, ITD has completed remedial action in 221 cases involving tax effect of ₹ 4,894.45 crore and initiated remedial action in 27 cases involving tax effect of ₹ 230.26 crore.

3.2 Quality of assessments

3.2.1 AOs committed errors in the assessments ignoring 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. 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 3.1 shows the details of sub-categories of errors (refer *Appendix 2.3*) which impacted the quality of assessments.

Table 3.1: Sub-categories of errors under quality of assessments (₹ in crore)

Sub-categories	Cases	Tax effect	States
a. Arithmetical errors in computation of income and tax	24	96.00	Delhi, Gujarat, Kerala, Madhya Pradesh, Maharashtra, Odisha, Uttar Pradesh and West Bengal.
b. Application of incorrect rate of tax and surcharge	11	196.83	Delhi, Karnataka, Madhya Pradesh, Maharashtra and UT Chandigarh.
c. Errors in levy of interest	3	4.07	Gujarat, Maharashtra and West Bengal.
d. Excess or irregular refunds/ interest on refunds	5	1,114.29	Karnataka and Maharashtra.
e. Errors in assessment while giving effect to appellate order	8	66.41	Delhi, Gujarat, Karnataka, Maharashtra and West Bengal.
Total	**51**	**1,477.60**	

3.2.2 Arithmetical errors in computation of income and tax

We noticed arithmetical errors in computation of income and tax in 24 cases involving tax effect of ₹ 96.0 crore in eight states.

Section 143(3) of the Income Tax Act, 1961, provides that the AOs, shall by an order in writing, make an assessment of the total income or loss of the assessee and determine the sum payable by him or refund of any amount due to him on the basis of such assessment after taking into account such evidence as the assessee may produce and such other evidence as the AO may require on specified points, and after taking into account all relevant material which he has gathered.

We give below four such illustrative cases:

3.2.2.1 In Maharashtra, Pr. CIT-LTU, Mumbai charge, AO completed the assessment of a company for the AY 2015-16 under section 143(3) in December 2017 determining income of ₹ 314.21 crore under normal provision of the Act. Audit examination revealed that while aggregating income from all the sources in para 16 of the assessment order, the figure arrived was ₹ 314.21 crore instead of correct figure of ₹ 341.21 crore. This errors had resulted in under assessment of income of ₹ 27 crore involving tax effect of ₹ 12.21 crore including interest. *The ITD accepted the audit observation and rectified the error (May 2018) under section 154 of the Act.*

3.2.2.2 In Madhya Pradesh, Pr. CIT Gwalior charge, AO completed the assessment of a company for the AY 2011-12 under Section 143(3), initially in March 2014 at income of ₹ 4.03 crore under normal provisions of the Act. Subsequently, income was revised under Section 263 at ₹ 22.58 crore in December 2016 after making addition of ₹ 18.55 crore. Further the case was reopened under section 147 on separate issue of cash transaction and income was reassessed under section 144 read with Section 147 in December 2017 at ₹ 12.50 crore by making addition of ₹ 8.47 crore on account of unverified/unexplained cash deposit. Audit examination revealed that AO, while completing the reassessment in December 2017 under section 144 read with section 147, did not consider the addition of ₹ 18.55 crore made under section 263 (December 2016). This error had resulted in under assessment of income of ₹ 18.55 crore involving short levy of tax of ₹ 10.01 crore including interest under section 234A and 234B. The *ITD rectified the error (December 2018) under section* 143(3) *read with section 147 of the Act.*

3.2.2.3 In Uttar Pradesh, Pr. CIT, Muzaffarnagar charge, AO completed the assessment of a company for the AY 2015-16 under section 143(3)/144 in September 2017, determining loss of ₹ 2.55 crore after making an addition of ₹ 3.03 crore to the returned loss. Audit examination revealed that AO, while finalising the assessment, erroneously reckoned the figure of returned loss of

₹ 5.57 crore instead of actual figure of loss of ₹ 1.23 crore as per the return filed by the assessee. This error had resulted in over assessment of loss of ₹ 2.54 crore and under assessment of income of ₹ 1.80 crore (against which brought forward loss to the extent of ₹ 1.80 crore could be adjusted) involving potential tax effect of ₹ 1.41 crore. The *ITD accepted the audit observation and rectified the error (February 2019) under section 154 of the Act.*

3.2.2.4 In Gujarat, Pr. CIT-1, Surat Charge, AO completed assessment of a company for the AY 2015-16 under section 144 in December 2017 determining total income of ₹ 17.44 crore. Audit examination revealed that the AO, while finalising the assessment, disallowed depreciation of ₹ 61.25 crore on the ground that there was no material available to prove that the assessee was actually using assets for the purpose of business. The assessee had not submitted bills and voucher for purchase of machinery or certificate in respect of fixed assets put to use on which depreciation was claimed. However, while error computing assessed income, the AO made addition of ₹ 35.31 crore only instead of ₹ 61.25 crore disallowed by the AO. The error had resulted in under-assessment of income of ₹ 25.94 crore (₹ 61.25 crore – ₹ 35.31 crore) with consequent short levy of tax of ₹ 11.72 crore including interest. The *ITD accepted (September 2018) the audit observation.*

3.2.3 Application of incorrect rates of tax and surcharge

We noticed application of incorrect rates of tax and surcharge in 11 cases involving tax effect of ₹ 196.83 crore in five states.

Section 4(1) of the Income Tax Act, 1961, provides that income tax is chargeable for every AY 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 AY 2012-13 provides for levy of surcharge at the rate of two per cent on income tax in the case of foreign companies if net income exceeds rupees one crore.

We give below one illustrative case:

3.2.3.1 In Maharashtra, CIT (IT)-3, Mumbai charge, AO completed assessment of a non-resident banking company, incorporated in the USA engaged in the activities of banking and treasury operation, for the AY 2012-13 after scrutiny in April 2016 determining total income of ₹ 899.68 crore after making certain additions and disallowance on account of transfer pricing order. Audit observed that AO, while computing tax demand of the assessee, levied tax at the rate of 30 *per cent* and surcharge at 5 *per cent* as against applicable rate of tax at 40 *per cent* and surcharge at 2 *per cent*. Audit also observed that the computation of tax was carried out manually and not through the AST. Audit could not ascertain the reason for computing the tax demand manually instead of through AST. This error had resulted in short levy of tax and surcharge of

₹ 86.18 crore. The *ITD rectified the error relating to rate of tax and surcharge under section 154 of the Act. However, ITD did not intimate whether any action was taken for preventing recurrence of such errors in future.*

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 2012-13 provides for levy of education cess at the rate of three per cent on income tax.

One illustrative case is given below:

3.2.3.2 In Karnataka, Pr. CIT-4 Bangalore charge, AO completed assessment of a company for the AY 2012-13 in January 2018 under section 143(3) read with section 144C and 92CD of the Act determining the income of ₹ 3,573.04 crore. Audit examination revealed that AO, while computing tax liability of the assessee, incorrectly levied education cess at the rate of one *per cent* as against the applicable rate of three *per cent*. Further, error in computation of interest under section 234B was also noticed. The errors had resulted in short levy of tax of ₹ 45.57 crore including interest. *The ITD rectified (June 2018) the* error *under section 154 of the Act. However, while passing rectification order under section 154 the AO did not levy interest of ₹ 11.27 crore under section 234C for deferment of advance tax.*

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 2016-17 provides for levy of surcharge at the rate of 12 per cent on income tax in the case of domestic companies if net income exceeds rupees 10 crore.

We give below one illustrative case:

3.2.3.3 In Madhya Pradesh, Pr. CIT-2, Jabalpur charge, AO completed the assessment of a company, for the AY 2016-17 after scrutiny in March 2018 determining income of ₹ 6,272.07 crore. Audit examination revealed that AO, while computing tax liability of the assessee in Income Tax Computation Form (ITNS-150), levied surcharge of ₹ 188.16 crore incorrectly at the rate of 10 *per cent* instead of ₹ 225.79 crore leviable at the rate of 12 *per cent*. Consequently, interest under section 234B and education cess was also short levied by ₹ 9.30 crore and ₹ 1.13 crore respectively. This error had resulted in short levy of tax of ₹ 48.06 crore. The *ITD accepted (March 2019) the audit observation.*

3.2.4 Errors in levy of interest

We noticed errors in levy of interest in three cases involving tax effect of ₹ 4.07 crore in three states.

As per provisions of section 234D of the Act where any refund granted to the assessee under sub section (1) of section 143 and subsequently no refund is found due on regular assessment or refund already granted is in excess, the assessee is liable for interest at the rate of half per cent on the excess amount so refunded for the period from date of grant of refund to the date of regular assessment. Further as per sub section (2) where as a result of an order under section 154, the amount of refund grant under sub-section (1) of section 143 is held to be correctly allowed, either in whole or in part, as the case may be, then, the interest chargeable, if any, under sub-section (1) shall be reduced accordingly.

Further, Section 220(2) provides that, if the amount specified as payable in any notice of demand under section 156 is not paid within a period of 30 days of the service of notice, the assessee shall be liable to pay simple interest as per prescribed rates and for the period specified in the Act.

We give below one illustrative case:

3.2.4.1 In West Bengal, Pr. CIT-1, Kolkata charge, AO completed the assessment of a company for the AY 2010-11 under section 143(3)/144C in May 2014 determining income of ₹ 138.14 crore. The assessment order was further revised under section 143(3)/263/144C in December 2017 at an amount of ₹ 148.77 crore. Audit observed that as per the original assessment order passed in May 2014, the net demand of ₹ 15.35 crore was determined after levying interest of ₹ 1.77 crore under section 234D for excess payment of refund. Further, the assessee paid total tax of ₹ 17.65 crore in September 2015, which included interest of ₹ 2.30 crore under section 220(2) for 15 months as determined by the department in September 2015. Audit examination revealed that the AO, while determining the net demand after revision order under section 263/143(3), erroneously did not consider the interest of ₹ 4.07 crore under sections 234D and 220(2) of the Act. This error had resulted in under charge of tax by ₹ 2.49 crore. The *ITD rectified (October 2018) the error under section 154 of the Act.*

3.2.5 Excess or irregular refunds/interest on refunds

We noticed five cases relating to excess or irregular refunds/interest on refunds in involving tax effect of ₹ 1,114.29 crore in two states.

Section 244A(1)(a) of the Income Tax Act, 1961, provides for levy of interest on the amount of refund where refund arises due to excess payment of tax, at a specified rate from the first day of the assessment year to the date of grant of refund.

We give below one illustrative case:

3.2.5.1 In Karnataka, PCIT-4, Bangalore charge, final assessment order for the assessee company for the AYs 2010-11 and 2011-12 were passed under section 143(3) read with section 144C and 92CD of the Act in January 2018 determining income of ₹ 2,030.82 crore and ₹ 2,151.43 crore respectively. Audit examination revealed that while passing the final assessment orders refund of ₹ 291.38 crore and ₹ 170.98 crore issued under section 143(1) dated in July 2011 and October 2012 for the AYs 2010-11 and 2011-12 respectively were not considered. This had resulted in total short levy of tax of ₹ 941.56 crore including interest under section 234B and 234D for both the AYs. *The ITD rectified the error (June 2018) under section 154 of the Act.*

3.2.6 Errors in assessment while giving effect to appellate orders

We noticed errors in assessment while giving effect to appellate order in eight cases involving tax effect of ₹ 66.41 crore in five states.

Section 254 of the Income Tax Act, 1961, provides, that the Appellate Tribunal shall send a copy of any orders passed under this section to the assessee and to the Principal Chief Commissioner. Further, para 24.1 of Chapter 18 of Manual of Office Procedure (Volume II, Technical) of the Income Tax Department provides that on receipt of the Appellate Order in the Assessing Officer's office, immediate steps should be taken to revise the assessment in the light of the order.

We give below two illustrative cases:

3.2.6.1 In Karnataka, CIT LTU Bangalore charge, AO while giving effect to appellate order in respect of a company for the AYs 2010-11, 2011-12 and 2012-13 determined income of ₹ 360.55 crore, ₹ 351.50 crore and ₹ 3.94 crore after allowing deduction under section 36(1)(viia) of the Act and refund of ₹ 409.73 crore, ₹ 132.81 crore and ₹ 30.28 crore in January 2018, March 2018 and March 2018 respectively. Audit examination revealed that AO, while computing deduction under section 36(1)(viia) 10 *per cent* of Aggregate Average Advances (AAA), reckoned at ₹ 239.04 crore and ₹ 300.19 crore instead of ₹ 202.07 crore and ₹ 278.98 crore for AYs 2010-11 and 2011-12 respectively as per ITAT order. Further, for the AY 2012-13, deduction under section 36(1)(viia) was to be restricted to ₹ 414.08 crore (provision for bad and doubtful debts debited to the Profit and Loss account) instead of

₹ 447.02 crore. These irregularities had resulted in excess allowance of deduction of ₹ 36.97 crore, ₹ 21.21 crore and ₹ 32.94 crore involving total tax effect of ₹ 40.65 crore (₹ 18.41 crore + ₹ 7.05 crore + ₹ 15.19 crore for the aforesaid AYs respectively). *The ITD rectified the* irregularities *(November 2018) under section 154 of the Act.*

3.2.6.2 In West Bengal, Pr. CIT-4, Kolkata charge, AO completed the assessment of a company, for the AY 1998-99 after scrutiny in March 2001 determining net loss of ₹ 74.27 crore. Later the assessment order was passed under section 254/264/154/143(3) for giving effect to the appellate order in July 2016 at net loss of ₹ 131.61 crore providing a total relief of ₹ 63.60 crore. Audit observed that the assessee preferred an appeal before CIT (Appeal) against the disallowance of ₹ 72.14 crore made under section 36(1)(iii) during scrutiny assessment and got relief of ₹ 8.54 crore in December 2013. The assessee further preferred appeal before ITAT against the CIT(Appeal)'s order. The ITAT in its appellate order passed in December 2015 deleted the addition made by AO and thus provided the total relief of ₹ 72.14 crore. However, it was found that the AO, while giving effect to appellate order, provided a relief of ₹ 63.60 crore only as against the total relief of ₹ 72.14 crore. The error had resulted in under assessment of loss by ₹ 8.54 crore involving potential tax of ₹ 2.99 crore. *The ITD rectified (June 2018) the error by passing order under section 154/254/264/143(3).*

3.3 Administration of tax concessions/exemptions/deductions

3.3.1 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 AOs 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. Table 3.2 shows the details of sub-categories which have impacted the Administration of tax concessions/exemptions/deductions.

Table 3.2: Sub-categories of errors under Administration of tax concessions/exemptions/deductions				(₹ in crore)
Sub-categories		**Nos.**	**TE**	**States**
a.	Irregularities in allowing depreciation/ business losses/ capital losses	75	2,655.15	Andhra Pradesh & Telangana, Bihar, Delhi, Goa, Gujarat, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Rajasthan, Tamil Nadu and West Bengal.
b.	Irregular exemptions/ Deductions/ Rebates/ Relief/ MAT Credit	52	2,037.22	Andhra Pradesh & Telangana, Delhi, Gujarat, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Rajasthan, Tamil Nadu and West Bengal.
c.	Incorrect allowance of business expenditure	49	764.39	Andhra Pradesh & Telangana, Bihar, Delhi, Gujarat, Himachal Pradesh, Jharkhand, Karnataka, Kerala, Maharashtra, Odisha, Tamil Nadu and West Bengal.
Total		**176**	**5,456.76**	

3.3.2 Irregularities in allowing depreciation and set off and carry forward of business/capital losses

We noticed irregularities in allowing depreciation and set off and carry forward of business/capital losses in 75 cases involving tax effect of ₹ 2,655.15 crore in 13 states.

Section 72 of 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 head of a relevant year, so much 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 the business or profession'. Further, section 80 provides that no loss shall be allowed to be carried forward or set off if the return of income is not filed within the stipulated time.

We give below three such illustrative cases:

3.3.2.1 In Bihar, Pr. CIT-1, Patna charge, AO completed the assessment of a company for the AY 2012-13 under section 143(3) of the Act in February 2015 at nil income (allowing depreciation loss of ₹ 343.48 crore) and was subsequently revised under section 143(3) read with section 147 of the Act in December 2017 at nil income and allowed carry forward of entire assessed loss of ₹ 2,547.31 crore. Audit observed that the business loss of the assessee was ₹ 2,293.95 crore including depreciation loss of ₹ 343.48 crore for the AY 2012-13. It was further observed from ITR Schedule and the computation sheet that the assessee had claimed only depreciation loss of ₹ 343.48 crore for carry forward to future years. However, AO, while finalising the re-assessment, disallowed excess depreciation of ₹ 90.12 crore and assessed total loss of ₹ 2,547.31 crore and the entire loss was allowed to be carried forward to the assessee which was not in order as the ITR was filed belatedly

on 12 March 2014 after stipulated date of filing of return of income in this case. The error had resulted in excess carry forward of loss of ₹ 2,293.95 crore[60] involving potential tax effect of ₹ 744.27 crore.

3.3.2.2 In Maharashtra, CIT(LTU), Mumbai charge, AO completed the assessment of a company for the AY 2014-15 under section 143(3) read with section 144C(3) in February 2018 determining loss at ₹ 6,401.23 crore under normal provisions of the Act and book profit of ₹ 233.21 crore under special provisions of section 115JB. The tax was levied on ₹ 1,375.84 crore under section 115BBD of the Act. It was seen from computation of total income in the assessment order that department, after setting off with income under the heads 'Income from house property', 'Short term capital gains' and 'Income from other sources', arrived at business loss of ₹ 6,401.24 crore. Audit examination revealed that assessee had income of ₹ 1,381.34 crore under the head 'Long Term Capital Gain' (LTCG) and the same was allowed to be set off against brought forward 'Long Term Capital Loss' (LTCL) instead. However, as per Section 71(2) of the Act, LTCG was first required to be set off against the business loss of the current year. This error had resulted in excess carry forward of business loss of ₹ 1,381.34 crore involving potential tax effect of ₹ 469.52 crore. *The ITD accepted (June 2018) the audit observation and rectified (May 2018) the error under section 154 of the Act.*

3.3.2.3 In West Bengal, Pr. CIT-1, Kolkata charge, AO completed the assessment of a company for the AY 2015-16 in December 2017 after scrutiny determining net loss of ₹ 859.75 crore which included unabsorbed depreciation of ₹ 139.10 crore. Audit examination revealed that the AO allowed entire loss to be carried forward to the assessee for future years. However, the assessee had filed its return of income belatedly in March 2017 as against the due date of October 2015. This error resulted in irregular carry forward of business loss of ₹ 720.65 crore (₹ 859.75 crore – ₹ 139.10 crore) involving potential tax effect of ₹ 244.95 crore. *The ITD rectified (August 2018) the error under section 154 of the Act.*

60 (₹ 2,547.31 crore – ₹ 343.48 crore + ₹ 90.12 crore)

Section 32(1)(iia) of the Income Tax Act, 1961 provides that in the case of any new machinery or plant (other than ships and aircraft), which has been acquired and installed after the 31st day of March, 2005, by an assessee engaged in the business of manufacture or production of any article or thing or in the business of generation or generation and distribution of power, a further sum equal to twenty per cent of the actual cost of such machinery or plant shall be allowed as deduction under clause (ii).

We give below one such illustrative case:

3.3.2.4 In Gujarat, Pr. CIT-2, Baroda Charge, AO completed assessment of a Company for the AY 2014-15 in September 2016 after scrutiny under section 143(3) determining total loss of ₹ 282.72 crore. Audit examination revealed that the assessee company had claimed and was allowed by the AO depreciation of ₹ 749.26 crore on plant & machineries which includes additional depreciation of ₹ 190.48 crore for the addition made during the year. Since the assessee company was engaged in the business of distribution of electricity and not in the business of generation or generation and distribution of power, therefore, the assessee company was ineligible for additional depreciation. The error had resulted in excess assessment of loss of ₹ 190.48 crore involving short levy of potential tax of ₹ 64.75 crore. *The Ministry has accepted the audit observation (January 2020) and stated that remedial action has been taken (March 2019) by passing order under section 263 of the Act.*

3.3.3 Irregular exemptions/deductions/rebate/relief/MAT credit

We noticed 52 cases relating to irregular exemptions/deductions/rebate/ relief/MAT credit in involving tax effect of ₹ 2,037.22 crore in 11 states.

Section 115JAA of the Income Tax Act allows carry forward of MAT credit to an assessee when tax payable under normal provisions is more than tax under special provisions. However, such credit shall be limited to the difference of tax under normal provisions of the Act and tax under special provisions of the Act.

We give below one such illustrative case:

3.3.3.1 In Tamil Nadu, Pr. CIT-LTU, Chennai charge, AO completed the assessment of a company for the AY 2011-12 in March 2014 which was reopened and completed in December 2017 on a total income of ₹ 837.37 crore. Subsequently, the assessment was revised under section 154 in February 2018 to give MAT credit of ₹ 66.53 crore pertaining to AY 2010-11. Audit examination revealed that there was no MAT credit available for AY 2010-11 as the tax was levied under normal provisions for AY 2010-11 after reassessment order passed under section 147 in March 2016. Irregular allowance of MAT credit had resulted in short levy of tax of ₹ 66.53 crore. *The Ministry has accepted the audit observation*

(December 2019) and stated that remedial action has been taken (September 2019) under section 154 of the Act.

Section 35 (2AB) of the Income Tax Act, 1961 (Act), provides where a Company, engaged in the business of bio-technology or in any business of manufacture or production of any article or thing, (except article specified under Eleventh Schedule of the Act), incurs any expenditure on scientific research (not being expenditure in the nature of cost of any land or building) on in-house research and development facility as approved by the prescribed authority, then, there shall be allowed a deduction of a sum equal 200 per cent of the expenditure so incurred

We give below two such illustrative cases:

3.3.3.2 In Karnataka, CIT LTU Bangalore charge, the assessment of a company for the AY 2014-15 was completed under section 143(3) read with section 144C in February 2018 determining income of ₹ 1237.64 crore. Audit observed that AO, while finalising the assessment, allowed deduction of ₹ 135.61 crore towards expenditure incurred on in-house R&D. It was also observed that DSIR[61], in Form No. 3CL, certified an amount of ₹ 22.42 crore as R&D expenditure eligible for deduction under section 35(2AB), which was net of R&D receipts. Further, Form 3CD also certified that only net expenditure was eligible for deduction. Thus, the assessee was eligible for a weighted deduction of ₹ 44.84 crore (200 *per cent*) instead of ₹ 135.61 crore. This error had resulted in underassessment of income of ₹ 90.77 crore involving tax effect of ₹ 31.78 crore**.** *The ITD accepted (April 2019) the audit observation.*

3.3.3.3 In Maharashtra, PCIT-15 Mumbai charge, AO completed the assessment of a company for the AY 2013-14 under section 144C(3) read with section 143(3) of the Act at an income of ₹ 749.11 crore. Audit examination revealed that the AO, while computing tax demand of the assessee, allowed MAT credit of ₹ 19.13 crore pertaining to AY 2010-11. However, no MAT credit was available to the assessee for the AY 2010-11 to be set off in subsequent year as the tax was levied under normal provisions for the said assessment year. Irregular allowance of MAT credit had resulted in tax effect of ₹ 29.65 crore including interest under section 234B. *The ITD accepted the audit objection and took remedial action by passing rectification order in November 2018.*

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3.3.4 Incorrect allowance of business expenditure

We noticed 49 cases relating to incorrect allowance of business expenditure involving tax effect of ₹ 764.39 crore in 12 states.

Under section 43B of the Income Tax Act, 1961, any sum payable by the assessee as interest on any loan borrowed from any public financial institution, bank etc. is allowed as deduction in the previous year only if the amount is actually paid during the previous year. Explanation 3C to the section has clarified that if any interest has been converted into a loan or borrowing shall not be deemed to have been actually paid. This has also clearly been explained in CBDT Circular No. 7/2006 dated 17th July 2006

We give below one illustrative case:

3.3.4.1 In Tamil Nadu, Pr. CIT-1 Chennai charge, AO completed the assessment of a company for the AY 2015-16 in December 2017 after scrutiny determining loss of ₹ 10.53 crore. Audit examination revealed that the assessee debited bank interest of ₹ 5.40 crore on term loan. Audit further observed that this interest was converted into 'Funded Interest Term Loan' (FITL) and no payment was made during the year. Hence the aforesaid interest was not allowable expenditure. The error had resulted in excess allowance of loss of ₹ 5.40 crore involving potential tax of ₹ 1.67 crore. *The Ministry has accepted (December 2019) the audit observation and stated that remedial action has been initiated (November 2019) under section 263 of the Act.*

According to Section 43 B of the Income Tax Act, any sum payable by the assessee as interest on any loan or borrowing or advance from any Public Financial Institution or a State Financial Corporation or State Industrial Investment Corporation or Scheduled Bank in accordance with the terms and conditions of the agreement governing such loan or borrowing or advance shall be allowed as deduction for computation of income tax. Further, according to explanation 3D under the said section, deduction of any sum being interest payable shall be allowed only if such interest has been actually paid and any interest referred above which has been converted into a loan or advance shall not be deemed to have been actually paid

We give below one illustrative case:

3.3.4.2 In Andhra Pradesh & Telangana, PCIT Central Hyderabad charge (presently the case is with PCIT-I, Hyderabad charge), AO completed assessment of a company for the AY 2015-16 after scrutiny in April, 2016 determining loss of ₹ 313.86 crore. Audit observed that the assessee entered into a Corporate Debt Restructuring (CDR) scheme and converted the interest portion of ₹ 413.86 crore (debited in the P&L account) into Funded Interest Term Loan (FITL). Audit examination revealed that the AO, while finalising the assessment, added back only ₹ 65.39 crore out of ₹ 413.86 crore whereas the entire amount converted as FITL should be treated as not paid and shall be added back to the income as per explanation 3D under section 43B. The error resulted in under assessment of income of ₹ 348.47 crore involving tax effect of ₹ 118.45 crore (positive tax ₹ 11.76 crore + potential tax ₹ 106.68 crore).

The Ministry has partially accepted (December 2019) the audit observation and stated that remedial action has been taken (July 2019) under section 143 read with section 263 of the Act.

Section 143 (3) of the Income Tax Act, 1961, provides that in a scrutiny assessment, the AO is required to 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

We give below one illustrative case:

3.3.4.3 In Delhi, PCIT 3 charge, AO completed the assessment of the company for the AY 2015-16 after scrutiny in December 2017 determining income of ₹ 99.61 lakh. Audit examination revealed that the assessee had made 'provision for sales return' of ₹ 6.0 crore. As per note no. 30(a) of exceptional items of profit and loss account, the provision up to March 2014 amounting to ₹ 2.62 crore was disclosed as an exceptional item and ₹ 3.38 crore related to current year was netted off from Sales. Thus, the assessee had claimed and was allowed the provision of ₹ 6.0 crore, which should have been disallowed being provision for unascertained liability. The error had resulted in under assessment of income of ₹ 6.0 crore involving short levy of tax of ₹ 2.59 crore including interest. *The ITD rectified the error by passing an order under section 154 in February 2019*.

As per Section 43B of the Income Tax Act 1961, notwithstanding anything contained in any other provision of this Act, a deduction otherwise allowable under this Act in respect of any sum payable by the assessee as interest on any loan or advances from a scheduled bank in accordance with the terms and conditions of the agreement governing such loan or advances shall be allowed, only in the previous year in which such sum is actually paid.

We give below one illustrative case:

3.3.4.4 In Maharashtra, Pr. CIT-5, Mumbai charge, AO completed the assessment of a company for AY 2015-16 after scrutiny in November 2017 accepting returned loss of ₹ 9.66 crore. Audit examination of 'Note 20' (Finance Charges) of the profit and loss account revealed that an amount of ₹ 42.70 crore was debited towards 'Interest on borrowings'. Further, as per clause 26(i)(B)(b) of the 'Tax Audit Report' (Form 3CD), 'Interest on loan from scheduled banks incurred in the previous year and not paid on or before the due date', therefore disallowable under section 43B, was at ₹ 34.81 crore. However, assessee in its computation of income had reduced interest of ₹ 21.34 crore only instead of ₹ 34.81 crore and the same was accepted in the assessment order. The error had resulted in under assessment income of ₹ 13.47 crore involving potential tax effect of ₹ 4.58 crore. *The ministry has*

accepted (February 2020) the audit observation and rectified the error under section 154 in September 2019.

3.4 Income escaping assessment due to errors

3.4.1 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 AOs either did not assess or under assessed total income that was required to be offered to tax. Table 3.3 shows the sub-categories which have resulted in Income escaping assessments.

Table 3.3: Sub-categories of errors under Income escaping assessments due to errors **(₹ in crore)**

Sub-categories		Nos.	TE	States
a.	Income not assessed/ under assessed under special provision	22	447.85	Andhra Pradesh & Telangana, Delhi, Gujarat, Karnataka, Madhya Pradesh, Maharashtra, Punjab, Rajasthan, Tamil Nadu and West Bengal.
b.	Income not assessed/ under assessed under normal provision	29	242.22	Andhra Pradesh & Telangana, Bihar, Delhi, Goa, Gujarat, Jharkhand, Karnataka, Madhya Pradesh, Maharashtra, Odisha, Rajasthan, Tamil Nadu, Uttar Pradesh and West Bengal.
c.	Incorrect classification and computation of capital gains	5	14.04	Tamil Nadu, Uttar Pradesh and West Bengal
d.	Incorrect estimation of Arm's Length Price	13	290.81	Delhi and Karnataka.
e.	Errors in implementing provisions of TDS/ TCS	8	48.49	Bihar, Delhi, Jharkhand, Karnataka and Maharashtra.
Total		**77**	**1,043.41**	

3.4.2 Income not assessed/under assessed under special provisions

We noticed that AO either did not assess income or under assessed income under special provisions in 22 cases involving tax effect of ₹ 447.85 crore in 10 states.

Section 115JB of the Income Tax Act, 1961, provides for levy of Minimum Alternate Tax (MAT) at prescribed percentage of book profit if the income tax payable on the total income computed under the normal provisions is lesser than MAT.

We give below two such illustrative cases:

3.4.2.1 In Tamil Nadu, Pr. CIT-LTU, Chennai charge, AO completed the assessment of a company for the AY 2015-16 in December 2017 after scrutiny assessing 'Nil' income under normal provision and book profit of ₹ 12.20 crore under special provisions of section 115JB. Audit examination revealed that AO,

while finalising the assessment, worked out book profit as ₹ 12.20 crore after making addition of ₹ 7.03 crore taking returned book profit of ₹ 5.17 crore instead of returned book profit of ₹ 27.93 crore. Audit further noticed that while computing the tax liability of the assessee in the income tax computation form, the book profit was taken as ₹ 27.93 crore instead of the correct amount of ₹ 34.96 crore (₹ 27.93 crore + ₹ 7.03 crore). The error had resulted in short levy of tax of ₹ 1.47 crore. *The Ministry has accepted (December 2019) and rectified the error under section 154 in August 2019.*

3.4.2.2 In Gujarat, Pr. CIT-2, Baroda Charge, AO completed the assessment of a company for the AY 2014-15 after scrutiny in December 2016 determining income of ₹ 17.55 crore under normal provision and book profit of ₹ 49.88 crore under special provision of section 115JB. Audit observed that the assessee had claimed depreciation at the rate of 15 *per cent* on the assets on which subsidies/grants were received. It was further observed from the assessment order that the assessee company had to account for 15 *per cent* of subsidies/grants i.e. ₹ 153.81 crore instead of 10 *per cent* i.e. ₹ 102.54 crore in its profit and loss account resulting in short transfer of ₹ 51.27 crore to profit & loss account. However, AO, while computing the book profit, added ₹ 24.22 crore only instead of ₹ 51.27 crore on account of difference in disallowance of subsidies/grants. This error had resulted in underassessment of book profit of ₹ 27.04 crore with consequent short levy of tax under MAT of ₹ 7.66 crore. *The Ministry has accepted (February 2020) and rectified the error under section 154 in July 2019.*

3.4.3 Income not assessed/under assessed under normal provisions

We noticed that AO either did not assess income or under assessed income under normal provisions in 29 cases involving tax effect of ₹ 242.22 crore in 14 states.

Section 143(3) of the Income Tax Act, 1961, provides that the AOs, shall by an order in writing, make an assessment of the total income or loss of the assessee and determine the sum payable by him or refund of any amount due to him on the basis of such assessment after taking into account such evidence as the assessee may produce and such other evidence as the AO may require on specified points, and after taking into account all relevant material which he has gathered.

We give below one illustrative case:

3.4.3.1 In Karnataka, Pr. CIT -3 Bangalore charge, the scrutiny assessment of a company for the AY 2012-13, was completed under section 143(3) in February 2017 determining income at ₹ 11,860.23 crore. Audit examination revealed that the dividend income from Australian subsidiary at ₹ 484 crore (exceptional item) has been shown as net of taxes in the Profit and Loss Account. However, in the income computation statement, while computing the business income

the dividend income from the Australian subsidiary was incorrectly reduced by the assessee at gross value of ₹ 578.32 crore (inclusive of tax) instead of adopting the value of ₹ 484 crore (net of taxes) as credited to the Profit and Loss Account and was allowed in the assessment. This had resulted in under assessment of business income of ₹ 94.32 crore involving tax effect of ₹ 48.66 crore including interest under section 234B. *The ITD did not accept (June 2018) the audit observation stating that in the detailed Profit and Loss account an amount of ₹578.32 crore has been shown as revenue from dividend from overseas subsidiary and the resulting net profit has been reconciled with the book profit of ₹8,469.85 crore which has been disclosed in tax payer' books and also the starting point for income tax computation. Thus, the audit's observation that the business income was understated is incorrect.* The reply of the department was not acceptable because the detailed Profit and Loss Account disclosed the amount of both dividends from overseas subsidiary (₹ 578.32 crore) and the corresponding provision for taxation of ₹ 94.32 crore, while the abridged Profit and Loss Account disclosed them at net values of ₹ 484 crore with no corresponding tax provision. Thus if revenue from dividend from overseas subsidiary was considered at gross value then the corresponding amount of provision of ₹ 94.32 crore was also required to be added back. Incidentally, it was also seen from the Profit and Loss Account of the assessee for the subsequent year i.e. FY 2012-13, wherein the figures for previous year i.e. FY 2011-12, had been regrouped and above mentioned dividend income was shown at ₹ 578 crore (i.e. gross dividend) and simultaneously provision for tax including ₹ 94.32 crore, which substantiated the contention of audit.

Section 5 of the IT Act, 1961 provides that the taxable income of any previous year of person who is a resident includes all income from whatever source derived which is received or is deemed to be received or accrues or arises to him during such previous year

We give below one illustrative case:

3.4.3.2 In Uttar Pradesh, Pr. CIT, Meerut charge, AO completed assessment of a company for AY 2015-16 in December 2017, at loss of ₹ 315.05 crore which was subsequently revised to loss of ₹ 1491.41 crore in June 2018 after giving appeal effect under section 251 of the Act. Audit examination revealed that the assessee company in the previous year received subsidy for operational loss for FYs 2012-13, 2013-14 and 2014-15 amounting to ₹ 75.96 crore, ₹ 65.55 crore and ₹ 145.60 crore respectively. Although the amount of ₹ 145.60 crore was offered for tax the subsidy totalling to ₹ 141.51 crore (₹ 75.96 crore + ₹ 65.55 crore) was not considered for taxation. Further, interest of ₹ 136.10 crore on bond related to prior period reimbursed by the Government of Uttar Pradesh during the year was also not offered for tax. The

error had resulted under assessment of income ₹ 277.61 crore (₹ 141.51 crore + ₹ 136.10 crore) involving potential tax of ₹ 94.36 crore. *The ITD rectified (August 2018) the error under section 154*.

3.4.4 Incorrect computation/ classification of capital gains

We noticed five cases relating to incorrect computation/classification of capital gains involving tax effect of ₹ 14.04 crore in three states.

Section 50C(1) of Income Tax Act, 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 or assessed or assessable by any authority of a State Government (hereafter in this section referred to as the "stamp valuation authority") for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed or assessable shall, for the purposes of section 48, be deemed to be the full value of the consideration received or accruing as a result of such transfer.

We give below one such illustrative case:

3.4.4.1 In West Bengal, Pr. CIT-1, Kolkata charge, AO completed the assessment of a company for AY 2014-15 after scrutiny in December 2016 at net Income of ₹ 135.48 crore**.** Audit examination revealed that the AO, while finalising the assessment, computed short term capital gain of ₹ 3.16 crore which was computed by taking the sale proceed of ₹ 8.02 crore. However, the short term capital gain should have been computed based on stamp duty valuation of the flat i.e. ₹ 9.91 crore as required by the provision of the Act. This error had resulted in under assessment of short term capital gain by ₹ 1.89 crore involving tax effect of ₹ 65.67 lakh including interest. *The ITD accepted the observation.*

3.4.5 Incorrect estimation of Arm's Length Price

We noticed 13 cases relating to incorrect estimation of Arm's Length Price involving tax effect of ₹ 290.81 crore in two states.

Section 92CA of the Income Tax Act, 1961 provides that where any person, being the assessee has entered into an international transaction in any previous year and the AO considers it necessary or expedient so to do, he may, with the previous approval of Principal Commissioner refer the computation of the arm's 'length price in relation to the said international transaction to the Transfer Pricing Officer (TPO). Section 92C(1) provides that the arm's length price' in relation to an international transaction shall be determined by any of the methods, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the Board may prescribe. Provision under section 92C(4) provides that no deduction under chapter VIA shall be allowed in respect of the amount of income by which the total income of the assessee is enhanced after computation of income.

We give below one such illustrative case:

3.4.5.1 In Delhi, CIT(2) charge, the AO referred the case of a company for the AY 2014-15 to TPO under CIT (TPO-1) charge, Delhi for determination of Arm's Length Price (ALP) in respect of domestic transactions entered into by the assessee. The TPO determined (October 2017) the ALP in respect of the assessee under section 92CA(3) proposing upward adjustment of ₹ 415.57 crore on account of intra-unit transaction of electricity i.e. specified domestic transaction. Subsequently, in CIT(2) Delhi charge, the AO completed the scrutiny assessment of the assessee for the AY 2014-15 in January 2018 at nil income under normal provisions of the Act after allowing the deduction on TPO adjustment and 'other operating income' and at ₹ 17.11 crore under special provisions section 115JB of the Act. Audit examination revealed that TPO had incorrectly computed the upward adjustment of ₹ 415.57 crore by applying monthly average method of per unit of the electricity sold instead of correct amount of ₹ 501.47 crore as per the yearly average method. This resulted in short adjustment of ALP by ₹ 85.89 crore. TPO rectified the transfer pricing order in July 2018. Audit examination further revealed that AO, while finalising the assessment, allowed the entire TPO adjustment amount as deduction under section 80-IA which was not allowable. This had resulted in under assessment of income by ₹ 501.47 crore involving short levy of tax of ₹ 248.85 crore. *The ITD rectified the error (February 2019) by way of passing an order under section 154.*

3.4.6 Errors in implementation of TDS/TCS provisions

We noticed error in implementation of TDS/TCS provisions in eight cases involving tax effect of ₹ 48.49 crore in five states.

Section 143(3) provides that the AO is required to make a correct assessment of the total income or loss of the assessee and determine the correct amount of tax or refund as the case may be.

We give below one illustrative case:

3.4.6.1 In Maharashtra, PCIT(Central)-2, Mumbai charge, AO completed assessment of a company for the AY 2014-15 under section 143(3) of the Act in December 2016 determining income at ₹ 77.42 crore. Audit noticed from para 7 of the assessment order that total TDS credit claim of ₹ 17.73 crore, on account of amount received as 'contractee advances' and 'advances against material and works', was rejected. The aforesaid credit was denied to the assessee as the advances received, against which TDS was made, were not credited to profit and loss account. Audit examination of the assessment records revealed that the assessee had claimed TDS of ₹ 42.21 crore. Out of which the department allowed TDS claim of ₹ 41.83 crore. Thus, it was evident that though TDS claim of ₹ 17.73 crore was rejected in assessment order, the

same was allowed in ITNS. This error had resulted in excess allowance of TDS claim of ₹ 17.73 crore involving tax effect of the same amount. *The ITD rectified (April 2018) the error under section 154 of the Act.*

As per the provisions of 194J of the Income tax Act, 1961, any person, who is responsible for paying to a resident any sum by way of fees for professional services, fees for technical services, royalty, non-compete fees, director's fees shall deduct tax at source at the rate of ten per cent of such sum as income-tax on income comprised therein. Further, under section 40(a)(ia) of the Act notwithstanding anything to the contrary in sections 30 to 38, any fees for technical services payable to a resident, shall not be deducted in computing income tax on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction has not been paid on or before due date as specified in section 139(1) of the Act.

We give below one illustrative case:

3.4.6.2 In Jharkhand, Pr. CIT Ranchi charge, AO completed the scrutiny assessment of a company for the AY 2014-15 in December 2016 at an income of ₹ 2.99 crore. Audit observed from the profit and loss account that the assessee had paid supervision charges of ₹ 15.52 crore. The assessee was in mining business and the supervision charges of mining is a technical job. As supervision charges are technical services, tax was required to be deducted at source at the rate of ten *per cent* on the payment made. Since the assessee had not deducted tax at source on payment made towards supervision charges, the same should have been disallowed and added back to the taxable income. The error to disallow the same had resulted in incorrect allowance of expenditure of ₹ 15.52 crore involving short levy of tax of ₹ 7.40 crore including interest. *The ITD rectified (December 2018) the error under section 147 read with section 144 of the Act.*

3.5 Over-charge of tax/Interest

3.5.1 We noticed that AOs over assessed income in 12 cases involving over-charge of tax and interest of ₹ 232.66 crore in Andhra Pradesh & Telangana, Delhi, Maharashtra, Odisha, and West Bengal. We give below two such illustrative cases:

3.5.1.1 In Maharashtra, CIT (Exemption), Mumbai charge, assessment of an association of persons (Trust) for the AY 2012-13 was originally completed in March 2015 and reassessed under section 143(3) read with section 250 of the Act giving effect to appellate order in June 2017 determining income at ₹ 1,345.65 crore. Audit examination of ITNS 150A Form revealed that, while giving effect to CIT(A)'s order tax payable was computed through AST at ₹ 512.85 crore instead of correct amount of ₹ 415.81 crore. The error had resulted in excess levy of tax and interest of ₹ 132.02 crore (tax ₹ 97.04 crore + interest under section 234B of ₹ 34.98 crore). Further, lacuna in the AST system also needs to be addressed.

3.5.1.2 In Odisha, Pr. CIT-I, Bhubaneswar charge, the assessment of a company for the AY 2013-14 was completed after scrutiny in February 2016 followed by rectification under section 154 in March 2016 at an income of ₹ 1,614.62 crore. The case was reassessed under section 147/143(3) in December 2017 determining total income at ₹ 1,851.92 crore. Audit examination revealed that AO, while computing the income of the assessee in the reassessment, added back ₹ 197.30 crore towards 'understatement of sales income' to total income determined under section 154 dated 23 March 2016 *[erroneously mentioned as income as per order under section 143(3) of the act]* and determined total income at ₹ 1,851.92 crore instead of correct income of ₹ 1,811.92 crore. The error had resulted in over assessment of income of ₹ 40 crore involving excess levy of tax of ₹ 29.61 crore. *The ITD stated (April 2019) that while giving effect under section 250 of the Act to the CIT (A)'s order in ITA No. 0521/15-16 dated 31 March 2017 the above error i.e. excess addition of ₹ 40 crore was also taken into account and accordingly order passed in AST in January 2019.*