



**Report of the  
Comptroller and Auditor General of India  
for the year ended March 2019**



**लोकहितार्थं सत्यनिष्ठा**  
**Dedicated to Truth in Public Interest**

**Union Government  
Department of Revenue – Direct Taxes  
Report No. 11 of 2020**



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Comptroller and Auditor General of India**

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Department of Revenue – Direct Taxes  
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**Laid on the table of Lok Sabha and Rajya Sabha on \_\_\_\_\_**



## Table of Contents

Contents		Pages
	<b>Preface</b>	<b>i</b>
	<b>Highlights</b>	<b>iii-x</b>
	<b>Chapter I: Direct Taxes Administration</b>	<b>1-13</b>
i.	Resources of the Union Government	1
ii.	Nature of Direct Taxes	1-4
iii.	Functions and responsibilities of the CBDT	4-5
iv.	Budgeting of Direct Taxation	5
v.	Growth of Direct Taxes	5-9
vi.	Revenue impact of tax incentives	9-10
vii.	Arrears of demand	11
viii.	Disposal of appeal cases	11-12
ix.	Search & Seizure and Survey	12-13
x.	Effectiveness of Internal Audit	13
	<b>Chapter II: Audit Mandate, Products and Impact</b>	<b>15-32</b>
i.	Authority of the CAG for audit of receipts	15
ii.	Examination of systems and procedures and their efficacy	15-18
iii.	Persistent and pervasive irregularities in respect of Corporation Tax and Income Tax assessments cases	18-23
iv.	Audit products and response to audit	23-25
v.	Audit impact	25-27
vi.	Time barred cases	27
vii.	TDS mismatch	27-31
viii.	Non-production of records	31-32
	<b>Chapter III: Corporation Tax</b>	<b>33-53</b>
i.	Introduction	33-34
ii.	Quality of assessments	34-40
iii.	Administration of tax concessions/exemptions/deductions	40-47
iv.	Income escaping assessments due to errors	47-52
v.	Over-charge of tax/interest	52-53

<b>Chapter IV: Income Tax</b>	<b>55-66</b>
i. Introduction	55-56
ii. Quality of assessments	56-58
iii. Administration of tax concessions/exemptions/ deductions	58-62
iv. Income escaping assessments due to errors	62-66
<b>Chapter V: Interest under sections 234A, 234B, 234C and 244A of the Act</b>	<b>67-94</b>
i. Introduction	67
ii. Why we chose this topic	67
iii. Audit objective	68
iv. Legal frame work	68
v. Audit coverage	68
vi. Sample size	69
vii. Non-production of records	69
viii. Audit findings	69-92
ix. Conclusion	92-93
x. Recommendations	93-94
<b>Chapter VI: Long term capital gain on Penny Stocks</b>	<b>95-103</b>
i. Introduction	95
ii. Background	95-96
iii. Modus operandi in brief	96
iv. Audit methodology	96-97
v. Audit objective	97
vi. Audit findings	97-102
vii. Conclusion	102-103
<b>Appendices</b>	<b>105-112</b>
<b>Abbreviations</b>	<b>113</b>

## **Preface**

This Report for the year ended March 2019 has been prepared for submission to the President under Article 151 of the Constitution of India.

The Report contains significant results of the compliance audit of the Department of Revenue-Direct Taxes of the Union Government.

The instances mentioned in this Report are those, which came to notice in the course of test audit for the period 2018-19 as well as those which came to notice in earlier years but could not be reported in the previous Audit Reports; instances relating to the period subsequent to 2018-19 have also been included, wherever necessary.

The audit has been conducted in conformity with the Auditing Standards issued by the Comptroller and Auditor General of India.



## Highlights

The Comptroller and Auditor General of India conducts the audit of receipts of the Union Government under section 16 of the Comptroller and Auditor General of India (Duties, Powers and Conditions of Service) Act, 1971. This Report primarily discusses compliance to the provisions of the Income Tax Act, 1961 and the associated rules, procedures, directives etc. as applied to all aspects related to the administration of direct taxes. The report is organised into six chapters, the highlights of which are described below:

### Chapter I: Direct Taxes Administration

Direct taxes receipts of Union Government in financial year (FY) 2018-19 amounting to ₹ 11,37,718 crore grew by 13.5 *per cent* over the FY 2017-18 (₹ 10,02,738 crore). Direct Taxes represented 6.0 *per cent* of the gross domestic products (GDP) in FY 2018-19. Share of direct taxes in gross tax revenue increased to 54.7 *per cent* in FY 2018-19 from 52.2 *per cent* in FY 2017-18.

Of the two major components of direct taxes, collections from Corporation Tax increased by 16.2 *per cent*, from ₹ 5.71 lakh crore in FY 2017-18 to ₹ 6.64 lakh crore in FY 2018-19. Collections from Income Tax increased to 13.1 *per cent* from ₹ 4.08 lakh crore in FY 2017-18 to ₹ 4.62 lakh crore in FY 2018-19. Voluntary compliance by assesseees (pre-assessment stage) accounted for 82.6 *per cent* of the total collections of Corporation and Income Tax in FY 2018-19.

The number of non-corporate assesseees increased from 5.38 crore in FY 2017-18 to 6.20 crore in FY 2018-19, registering an increase of 15.2 *per cent*. The number of corporate assesseees increased from 7.99 lakh in FY 2017-18 to 8.46 lakh in FY 2018-19, registering an increase of 5.9 *per cent*.

In last three financial years more than 40 *per cent* of Corporation Tax collection in first quarter as well as the total refund amount was refunded against the previous years' collection in the first quarters of FYs.

The arrears of demand increased from ₹ 11.1 lakh crore in FY 2017-18 to ₹ 12.3 lakh crore in FY 2018-19. However, the net collectible demand decreased to ₹ 14,593 crore in FY 2018-19 as compared to ₹ 20,159 crore in FY 2017-18 due to increase in demand difficult to recover. The Department indicated that more than 98.8 *per cent* of uncollected demand would be difficult to recover.

The number of appeals pending with CIT (Appeals) increased from 3.0 lakh in FY 2017-18 to 3.4 lakh in FY 2018-19. The amount locked up in these cases was ₹ 5.6 lakh crore in FY 2018-19. The total cases pending at higher levels (ITATs/High Courts/Supreme Court) increased from 0.82 lakh cases in FY 2017-18 to 1.35 lakh in FY 2018-19.

## **Chapter II: Audit Mandate, Products and Impact**

During FY 2017-18, the Income Tax Department (ITD) had completed 2.99 lakh scrutiny assessments in the units audited as per the audit plan of FY 2018-19, out of which we checked 2.72 lakh cases. Apart from this, we have also audited 0.60 lakh cases out of 1.59 lakh scrutiny assessments completed in the earlier financial years, during FY 2018-19. The incidence of errors in assessments checked in audit during FY 2018-19 was 5.95 *per cent* (19,768 cases), as against 6.45 *per cent* last year.

There have been persistent and pervasive irregularities in respect of Corporation Tax and Income Tax assessments cases over the years. Recurrence of such irregularities, despite being pointed out repeatedly in the earlier Audit Reports point to structural weaknesses on the part of Department as well as the absence of appropriate institutional mechanisms to address this. Such irregularities were particularly noticeable in the assessment charges in Maharashtra.

We have included 393 high value cases reported to the Ministry in Chapter III and IV of this Report. Of these, we received replies in respect of 190 cases as on 30 June 2020, of which, 174 cases (91.5 *per cent*) were accepted and 16 cases not accepted. In remaining 203 cases the Ministry/ ITD did not furnish replies. Besides, Chapter V brings out our report on a subject specific compliance audit on 'Interest under sections 234A, 234B, 234C and 244A of the Act'. The Chapter points out that the interest was wrongly computed either due to systemic deficiencies in Assessment Information System (AST) or due to incorrect interventions/ computation by the assessing officers (AOs). Availability of facility for manual intervention in AST was misused by AOs by way of modifying the interest at excess amount which led to blockade of refund to the assessee. The system deficiency with respect to calculation of interest still persisted in the new application, i.e. 'Income Tax Business Application'. In addition, one long draft paragraph viz. 'Long Term Capital Gain on Penny Stocks' has been separately included in Chapter VI of this Report.

In the last three years, the ITD recovered ₹ 657.94 crore from demands raised to rectify the errors in assessments that we had pointed out. There are 53,117 cases involving revenue effect of ₹ 1.20 lakh crore pointed out in audit which remained unsettled as of 31 March 2019 for want of replies from the ITD.

During FY 2018-19, 1,961 cases with tax effect of ₹ 2,237.05 crore became time-barred for initiating any remedial action.

During last three years, more than 82 *per cent* individual taxpayers faced the TDS mismatch problem due to the difference in the amount available in Form 26AS and that claimed by the assesseees through their ITR, majority being salaried taxpayers.

The possible reasons for mismatch of TDS amount may be – the deductor did not deposit TDS or file the quarterly TDS return on time, entered incorrect amount in the TDS return, quoted incorrect PAN, the deductor's TAN wrongly entered in ITR, mistake in selecting assessment year. As a result, ITD did not allow credit for TDS which resulted into either raising demand or not releasing refunds, causing harassment to the assesseees.

We tried to attempt an Audit to examine the reasons for TDS mismatches, status of their resolution, mode of the resolution, efforts of the department, as well as correctness and completeness of information shared by ITD etc.

However, we could not conduct the audit as the assessment records were not available with the jurisdictional assessing officers as these were not pushed to them by the CPC-Bengaluru, even after two years of the assessment year.

Inability of the department to furnish relevant information to complete the audit has prevented the C&AG from fulfilling his constitutional mandate.

The ITD needs to ascertain whether the mismatches were due to the IT systems or the failure of deductors in furnishing correct returns/ information. In cases of failure of the deductors, necessary action may be taken against the defaulting deductors under the Act by ITD. It also needs to be ascertained in how many cases the ITD raised demand from the taxpayers because of the mismatch, as such causing harassment to the taxpayer. ITD also needs to examine the mismatch to ensure that no tax is levied on the persons who are not required to pay tax.

### **Chapter III: Corporation Tax**

We pointed out 316 high value cases pertaining to corporation tax with tax effect of ₹ 8,210.43 crore. We classified these cases in four broad categories viz.

- (a) Quality of assessments involving tax effect of ₹ 1,477.60 crore (51 cases);
- (b) Administration of tax concessions/exemptions/deductions involving tax effect of ₹ 5,456.76 crore (176 cases);
- (c) Income escaping assessment due to errors involving tax effect of ₹ 1,043.41 crore (77 cases) and
- (d) Over-charge of tax/interest involving ₹ 232.66 crore (12 cases).

### **Chapter IV: Income Tax**

We pointed out 77 high value cases of income tax with tax effect of ₹ 170.36 crore. We classified these cases in four broad categories as follows:

- (a) Quality of assessments involving tax effect of ₹ 19.05 crore (29 cases);
- (b) Administration of tax concessions/exemptions/deductions involving tax effect of ₹ 121.72 crore (30 cases);
- (c) Income escaping assessments due to errors involving tax effect of ₹ 26.27 crore (17 cases); and
- (d) Over charge of tax/interest involving ₹ 3.32 crore (one case).

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

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

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

*It is recommended that the CBDT may examine whether the instances of "errors" noticed are errors of omission or commission and if these are errors of commission, then ITD should ensure necessary action as per law.*

#### **Chapter V: Interest under section 234A, 234B, 234C and 244A of the Act**

We audited 6,217 assessment cases which were processed/completed through AST module/system and examined the correctness of interest, calculated through the system and modified by AOs with respect to sections 234A, 234B, 234C and 244A of the Income Tax Act. We found that interest was calculated incorrectly through the AST system in 70.51 *per cent* cases. Incorrect amount of interest was calculated through the system despite the fact that the system was designed, inter alia, to undertake assessment functions of calculation of interest under various sections of Income Tax Act.

The audit findings are as under:

- a) The interest was wrongly computed by ITD, in 76.68 *per cent*<sup>1</sup> of cases of the sample of 6,217 selected out of a population of 8,35,727 records, either due to systemic deficiencies or due to incorrect interventions by the AOs.
- b) Input of the other ITD module was not being captured properly in the AST system leading to incorrect computation of interest in number of cases which has an impact on final tax collection and refund.
- c) AOs did not take any step to rectify the incorrect interest, under sections 234A, 234B, 234C and 244A of the Act, calculated through the system even though AST system allowed the AOs to modify the value of interest in accordance with the provisions of the Act, thereby leading to either short levy/payment or excess levy/payment of interest.
- d) AOs modified the interest under sections 234A, 234B, 234C and 244A of the Act against the incorrect interest calculated through the system in some cases. However, not all these cases were modified at correct amount, which resulted in either short levy/payment or excess levy/payment of interest.
- e) AOs manually modified the interest amount which was not warranted in instances where correct amount of interest was calculated through the system, leading to either short levy/payment or excess levy/payment of interest causing hardship and harassment to taxpayers.

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1 4,767 assessment cases out of 6,217 assessment cases which were audited

It is not clear why manual modification is permitted, that too apparently without a protocol for seeking senior level clearances if, in exceptional cases, manual intervention is required. In fact, if manual intervention at every level is needed, or continued, it either points to an ill designed IT System, or a deliberate attempt to retain discretion, for no apparent good reason.

- f) Incorrect levy of interest (excess levy) by AOs using modification feature of AST led to blockade of refunds due to the assesseees. This was not only violation of provisions of law but also resulted in non-fulfilment of Citizen's Charter. On the one hand the efficiency of the department was affected and on the other there was undue harassment to the assesseees.
- g) All Income Tax Returns (ITRs) are first summarily processed under section 143(1) at Centralized Processing Centre (CPC), Bengaluru. Processing of ITRs by CPC is supposed to be completely automated. However, refunds of the assesseees' were blocked by modifying the interest amount even in cases processed in summary manner through CPC.
- h) The net collection of taxes is computed by allowing for the refunds<sup>2</sup>. Blockade of refunds, therefore, have the result of inflating the net tax collection. Further, unreasonable tax demand from the assessee, by way of excess levy of interest, results in disputes and further snowballs into large arrears. Thus, the blockade of refund and excess demand would have consequent effect on the revenue collection of the Government.

*It is recommended that*

- a) *CBDT may institute appropriate checks and balances in Income Tax Business Application (ITBA) to prevent recurrence of error in computation of tax and interest.*
- b) *The IT system for direct taxes needs to be designed in such a way that it should ensure zero or minimal physical interface between the assessee and the tax officers. The Government may consider the IT System for direct taxes being placed at arms length from CBDT, with an independent governmental body or organisation.*

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2 Para 7.2.2. of CBDT Accounts Manual

- c) AST module allows manual modification of interest amount which resulted in errors in computation of interest. ITD needs to inquire into the reasons for errors in computation of interest through AST and reasons for allowing manual modification to co-exist with IT system.*
- d) The system should be designed to provide audit trail for modifications, if any, being carried out by AOs. All justifications for modification by AO must be available on the system.*
- e) CBDT may examine whether the instances of “errors” noticed are errors of omission or commission and if these are errors of commission, then ITD should ensure necessary action as per law.*
- f) The IT Department may fix accountability on the part of the AOs to ensure that the risk of recurrences of similar types of irregularities are minimised.*
- g) CBDT may ensure that the refund due to the assessee is released in prescribed time limit, upholding its commitment through the citizen charter, rather than to withhold/block it by manual intervention.*
- h) AO’s action regarding blockade of refund as well as under charging of interest may be investigated upon.*
- i) While audit carried out test check of a sample of cases, CBDT should examine all the cases where modifications were carried out in AST to identify instances of omission and commission and take necessary action as per law.*

## **Chapter VI: Long term capital gain on Penny Stocks**

We observed that the ITRs of the assesseees who traded in the shares of penny stock companies were neither selected for scrutiny nor reopened for scrutiny despite the ITD having information of claiming LTCG. The ITD failed to issue notices for filing ITRs, to the assesseees who were involved in trading penny stocks, but have not filed their ITRs. Even Non-filers Monitoring System had not been utilized effectively to identify such non-filers. The AOs had no uniformity in making additions of exempt LTCG, despite the fact that the grounds of additions were same. In some cases, AOs did not make any addition for claimed exempted LTCG, for which no justification was given in the assessment orders. Further, the AOs had made additions at different percentage where the assesseees traded in shares of same penny stock companies. The ITD did not have any systemic approach to deal with cases of beneficiaries traded in penny stock as in some cases entire sales consideration was disallowed whereas in some cases only claimed LTCG was disallowed. There is also variation in disallowance of commission received by entry and exit provider from beneficiary of penny stock.

It is recommended that

- (i) the ITD may design CASS parameters in such a way that all the relevant information with ITD, whether from ITR or other sources, may be used to select the cases for scrutiny.*
- (ii) the method of selection for scrutiny under CASS may be shared with the C&AG as was pointed out in the Audit Report No. 9 of 2019 of C&AG so that audit may see whether the selection of cases for scrutiny is as per CASS parameters.*
- (iii) the ITD may examine whether the errors in assessment of cases where LTCG on penny stock was claimed, are errors of omission or commission and if these are errors of commission, then ITD should ensure necessary action as per law.*

## Chapter I: Direct Taxes Administration

### 1.1 Resources of the Union Government

**1.1.1** The Government of India's resources include all revenues received by the Union Government, all loans raised by issue of treasury bills, internal and external loans and all moneys received by the Government in repayment of loans. Tax revenue resources of the Union Government consist of revenue receipts from direct and indirect taxes. Table 1.1 below shows the summary of resources of the Union Government for the financial year (FY) 2018-19 and FY 2017-18.

Table 1.1: Resources of the Union Government	₹ in crore)	
	FY 2018-19	FY 2017-18
<b>A. Total Revenue Receipts</b>	25,67,917	23,64,148
<i>i. Direct Taxes Receipts</i>	11,37,718	10,02,738
<i>ii. Indirect Taxes Receipts including other taxes<sup>3</sup></i>	9,42,747	9,16,445
<i>iii. Non-Tax Receipts</i>	4,86,389	4,41,383
<i>iv. Grants-in-aid &amp; contributions</i>	1,063	3,582
<b>B. Miscellaneous Capital Receipts<sup>4</sup></b>	94,979	1,00,049
<b>C. Recovery of Loans &amp; Advances<sup>5</sup></b>	30,257	70,639
<b>D. Public Debt Receipts<sup>6</sup></b>	67,58,482	65,54,002
<b>Receipts of Government of India (A+B+C+D)</b>	<b>94,51,635</b>	<b>90,88,838</b>

Source: Union Finance Accounts of respective years. Direct Tax receipts and Indirect Tax receipts including other taxes have been worked out from the Union Finance Accounts. Total Revenue Receipts include ₹ 7,61,454 crore in FY 2018-19 and ₹ 6,73,005 crore in FY 2017-18 directly assigned to states.

**1.1.2** In FY 2018-19, the increase in receipts of Government of India have mainly been contributed by increase in public debt receipts and in total revenue receipts. Direct Taxes accounted for 44.3 *per cent* of total revenue receipts in FY 2018-19, growing by 13.5 *per cent* over the last year's receipts.

### 1.2 Nature of Direct Taxes

**1.2.1** Direct taxes levied by the Parliament mainly comprise,

- i. **Corporation Tax** levied on income of the companies;
- ii. **Income Tax** levied on income of persons (other than companies);

3 Indirect taxes levied on goods and services such as customs duty, excise duty, service tax, Central Goods and Services Tax, Integrated Goods and Services Tax etc.;

4 This comprises of value of bonus share, disinvestment of public sector and other undertakings and other receipts;

5 Recovery of loans and advances made by the Union Government;

6 Borrowings by the Government of India internally as well as externally;

- iii. **Other direct taxes** including Securities Transactions Tax<sup>7</sup>, Wealth Tax<sup>8</sup> etc.

1.2.2 Table 1.2 provides a snapshot of direct taxes administration.

Table 1.2: Direct Taxes Administration					
	2014-15	2015-16	2016-17	2017-18	2018-19
<b>₹ in crore</b>					
<b>1. Direct taxes collection</b>	6,95,792	7,42,012	8,49,801	10,02,738	11,37,718
a. Corporation Tax	4,28,925	4,53,228	4,84,924	5,71,202	6,63,571
b. Income Tax	2,58,374	2,80,390	3,40,592	4,08,202	4,61,652
c. Other Direct Tax	8,493	8,394	24,285	23,334	12,495
<b>2. Refunds</b>	1,12,163	1,22,596	1,62,582	1,51,639	1,61,037
<b>Number in lakh</b>					
<b>3. Actual returns filed by</b>					
a. Non-corporate Assesseees	360.6	398.0	436.9	537.9	619.8
b. Corporate Assesseees	6.8	6.9	7.1	8.0	8.5
<b>4. Revenue expenditure (₹ in crore)</b>	4,148	4,689	5,623	6,172	7,168

Source: Sl. no. 1 and 4 – Union Finance Accounts; Sl. no. 2 - Pr. CCA, CBDT; Sl. no. 3 – CBDT

1.2.3 Table 1.3 below gives the details of non-corporate assesseees in different categories of income.

Table 1.3: Non-Corporate Assesseees						(Figures in lakh)
Financial Year	A <sup>9</sup>	B <sub>1</sub> <sup>10</sup>	B <sub>2</sub> <sup>11</sup>	C <sup>12</sup>	D <sup>13</sup>	Total
2014-15	76.32	216.31	46.11	21.80	0.01	360.55
2015-16	55.93	264.47	52.94	24.69	0.01	398.04
2016-17	54.17	290.16	61.85	30.69	0.02	436.89
2017-18	61.16	360.63	79.04	37.05	0.02	537.90
2018-19	68.08	403.35	103.36	44.96	0.03	619.78

Source: CBDT; These figures are based on actual returns filed during the respective year.

The number of non-corporate assesseees registered an increase of 15.2 per cent in FY 2018-19 in comparison to increase of 23.1 per cent in FY 2017-18. As can be seen from the Table 1.3 above and Chart 1.1, there has been increase of 11.8 per cent, 30.8 per cent and 21.3 per cent in Category 'B<sub>1</sub>', Category 'B<sub>2</sub>' and Category 'C' during FY 2018-19 in comparison to FY 2017-18. However, the increases in these categories were 24.3 per cent, 27.8 per cent and 20.7 per cent during FY 2017-18 in comparison to the previous year. There was an increase

7 Tax on the value of taxable securities purchased and sold through a recognized stock exchange in India.

8 Tax chargeable on the net wealth comprises certain assets specified under section 2(ea) of the Wealth Tax Act, 1957. The Wealth Tax has been abolished through the Finance Act, 2015.

9 Category 'A' assesseees – Assessments with income/loss below ₹ two lakh;

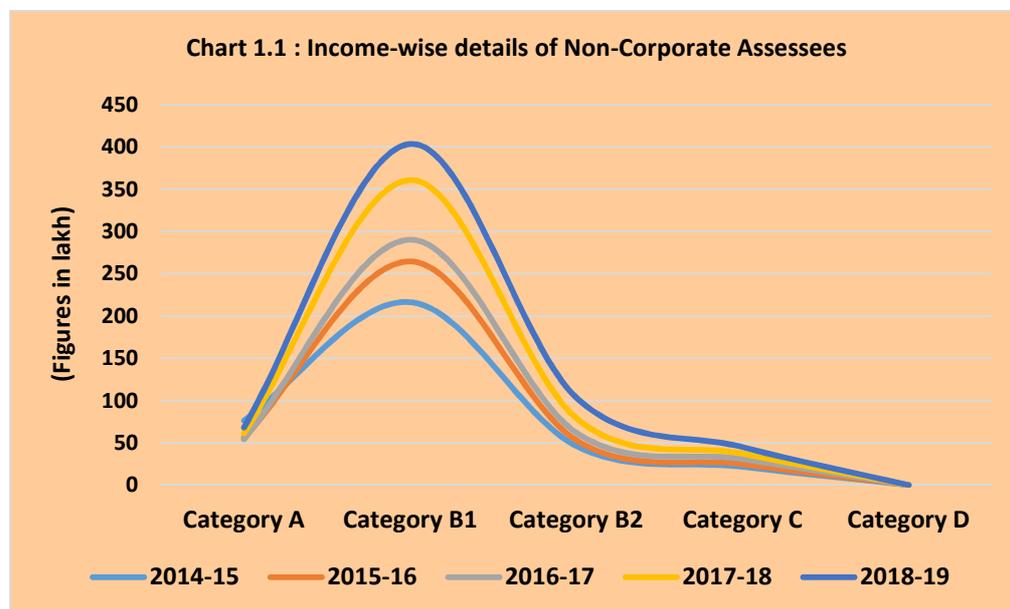
10 Category 'B<sub>1</sub>' assesseees (lower income group) - Assessments with income/loss above ₹ two lakh and above; but below ₹ five lakh;

11 Category 'B<sub>2</sub>' assesseees (higher income group) - Assessments with income/loss above ₹ five lakh and above; but below ₹ 10 lakh;

12 Category 'C' assesseees - Assessments with income/loss of ₹ 10 lakh and above;

13 Category 'D' assesseees – Search and seizure assessments;

of 71.9 per cent in non-corporate taxpayers during FY 2014-15 to FY 2018-19 whereas during the same period tax collection from non-corporate taxpayers increased by 78.7 per cent. Thus, growth in tax collection was more than the growth in non-corporate taxpayers.



**1.2.4** Table 1.4 below gives the details of corporate assesseees belonging to the different categories of income.

Financial Year	A <sup>14</sup>	B <sub>1</sub> <sup>15</sup>	B <sub>2</sub> <sup>16</sup>	C <sup>17</sup>	D <sup>18</sup>	Total	Assesseees having income above ₹ 25 lakh	Working companies as per RoC as on 31 <sup>st</sup> March
2014-15	3.20	1.51	0.48	1.56	0.00 <sup>*</sup>	6.75	0.69	10.16
2015-16	3.08	1.59	0.50	1.71	0.00 <sup>^</sup>	6.88	0.76	10.82
2016-17	3.14	1.65	0.53	1.81	0.00 <sup>#</sup>	7.13	1.44	11.11
2017-18	3.57	1.85	0.58	1.99	0.00 <sup>\$</sup>	7.99	1.31	10.49
2018-19	3.66	2.00	0.61	2.19	0.00 <sup>@</sup>	8.46	1.45	11.56

Source: CBDT. These figures are based on actual returns filed during the respective year.

\* 256 assesseees; ^ 337 assesseees, # 134 assesseees, \$ 195 assesseees @ 146 assesseees

The corporate assesseees registered an increase of 5.9 per cent in FY 2018-19 in comparison to increase of 12.1 per cent in FY 2017.18. There was an increase

14 Category 'A' assesseees – Assessment with income/loss below ₹ 50,000;

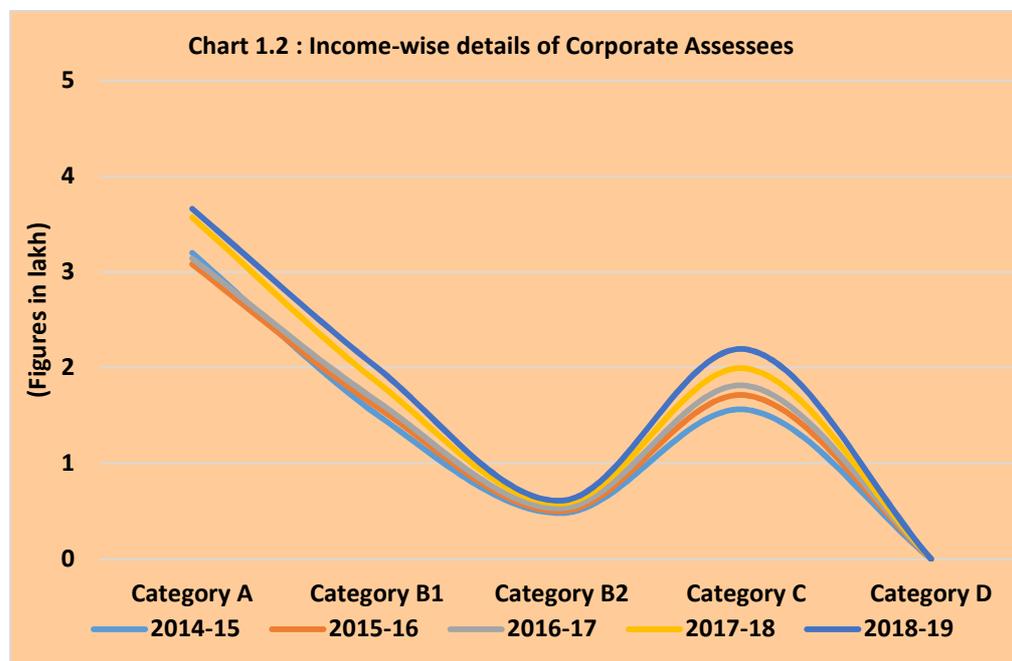
15 Category 'B1' assesseees (lower income group) – Assessment with income/loss of ₹ 50,000 and above; but below ₹ five lakh;

16 Category 'B2' assesseees (higher income group) - Assessment with income/loss above ₹ five lakh and above; but below ₹ 10 lakh;

17 Category 'C' assesseees - Assessment with income/loss of ₹ 10 lakh and above;

18 Category 'D' assesseees – Search and seizure assessment;

of 25.3 *per cent* in corporate taxpayers during FY 2014-15 to FY 2018-19 whereas during the same period tax collection from corporate taxpayers increased by 54.7 *per cent*. Thus, growth in tax collection was more than the growth in corporate taxpayers.



**1.2.5** A comparison of the figure on total working companies as per the Registrar of Companies (ROCs)<sup>19</sup> data with the total filers as per the ITD would suggest that ensuring compliance by identifying non-filers by the ITD was not effective. As in FY 2017-18, there were 10.49 lakh companies registered with ROC, against which it is observed that in FY 2018-19, 8.5 lakh companies only filed income tax returns. Though all working companies (whether profit earning or loss incurring) are required by the provision of the Income Tax Act, 1961 (the Act) to file their return of income, 19.4 *per cent* of such working companies registered with ROC in FY 2017-18 did not file their returns of income against 28.0 *per cent* in FY 2016-17.

### 1.3 Functions and responsibilities of the CBDT

**1.3.1** The Central Board of Direct Taxes (CBDT) under the Department of Revenue (DOR) in the Ministry of Finance provides essential inputs for policy and planning in respect of direct taxes in India. At the same time, it is also responsible for administration of direct taxes laws through Income Tax Department (ITD). ITD deals with matters relating to levy and collection of direct taxes and the issues of tax evasion, revenue intelligence, widening of tax-base, providing tax payers services, grievance redressal mechanism etc.

<sup>19</sup> Source: Ministry of Corporate Affairs, Statistics Division, New Delhi.

**1.3.2** As on 31 March 2019, the overall staff strength and working strength of the ITD was 76,243 and 46,264 respectively. The sanctioned and working strength of the officers<sup>20</sup> was 10,858 and 9,706 respectively. The revenue expenditure of ITD for the year 2018-19 was ₹ 7,168 crore<sup>21</sup>.

#### 1.4 Budgeting of Direct Taxation

**1.4.1** The Budget reflects the Government's vision and intent. The revenue budget consists of the revenue receipts of the Government (tax revenues and other revenues). Comparison of budget estimates with the corresponding actuals is an indicator of quality of fiscal management. Actuals may differ from the estimates because of unanticipated and random external events or methodological inadequacies or unrealistic assumptions about critical parameters.

**1.4.2** Table 1.5 below shows the details of Budget Estimates (BE), Revised Estimates (RE) and Actual collection of Direct Taxes during FYs from 2014-15 to FY 2018-19.

Table 1.5: Budget Estimates, Revised Estimates vis-à-vis Actual collection of Direct Taxes							(₹ in crore)	
Financial Year	Budget estimates	Revised estimates	Actual	Actual minus budget estimates	Actual minus Revised estimates	Difference as per cent of budget estimates	Difference as per cent of Revised estimates	
2014-15	7,36,221	7,05,628	6,95,792	(-) 40,429	(-) 9,836	(-) 5.5	(-) 1.4	
2015-16	7,97,995	7,52,021	7,42,012	(-) 55,983	(-) 10,009	(-) 7.0	(-) 1.3	
2016-17	8,47,097	8,47,097	8,49,801	2,704	2,704	0.3	0.3	
2017-18	9,80,000	10,05,000	10,02,738	22,738	(-) 2,262	2.3	(-) 0.2	
2018-19	11,50,000	12,00,000	11,37,718	(-) 12,282	(-) 62,282	(-) 1.1	(-) 5.2	

Source : BE and RE figures are as per respective Receipt Budget and Actual are as per respective Finance Accounts

**1.4.3** The variation between RE and actual collection ranged from (-) 5.2 per cent to 0.3 per cent of RE during the period from FY 2014-15 to FY 2018-19. The variation between RE and actuals were higher during FY 2018-19 as compared to BE and actuals.

#### 1.5 Growth of Direct Taxes

**1.5.1** Table 1.6 below gives the relative growth of direct taxes (DT) with reference to Gross Tax Receipts<sup>22</sup> (GTR) and Gross Domestic Products (GDP) during FY 2014-15 to FY 2018-19.

20 Pr. CCIT/Pr. DGIT, CCIT/DGIT, Pr. CIT/Pr. DIT, CIT/DIT, Addl. CIT/Addl. DIT/JCIT/JDIT, DCIT/DDIT/ACIT/ADIT and ITOS.

21 Union Finance Accounts for FY 2018-19.

22 It includes all direct and indirect taxes.

Financial Year	DT	GTR	DT as per cent of GTR	GDP	DT as per cent of GDP
2014-15	6,95,792	12,45,135	55.9	1,25,41,208	5.5
2015-16	7,42,012	14,55,891	51.0	1,35,76,086	5.5
2016-17	8,49,801	17,15,968	49.5	1,51,83,709	5.6
2017-18	10,02,738	19,19,183	52.2	1,67,73,145	6.0
2018-19	11,37,718	20,80,465	54.7	1,90,10,164	6.0

Source: DT and GTR - Union Finance Accounts, GDP-Central Statistical Office (CSO), Ministry of Statistics and Programme Implementation; GDP for FY 2018-19 – Press note released by CSO on 31 May 2019.

**1.5.2** Though the DT increased by 13.5 *per cent* in FY 2018-19 as compared to FY 2017-18, there was increase (2.4 *per cent*) in the share of DT to GTR in FY 2018-19 as compared to FY 2017-18. DT was 6.0 *per cent* of GDP during FY 2018-19 and FY 2017-18 as compared to 5.6 *per cent* in FY 2016-17.

**1.5.3** Table 1.7 below gives the growth of direct taxes and its major components i.e. Corporation Tax (CT) and Income Tax (IT) during FY 2014-15 to FY 2018-19.

Financial Year	Direct Taxes	Per cent growth over previous year	Corporation Tax	Per cent growth over previous year	Income Tax	Per cent growth over previous year	GDP	Per cent growth over previous year
2014-15	6,95,792	9.0	4,28,925	8.7	2,58,374	8.6	1,25,41,208	10.5
2015-16	7,42,012	6.6	4,53,228	5.7	2,80,390	8.5	1,35,76,086	8.3
2016-17	8,49,801	14.5	4,84,924	7.0	3,40,592	21.5	1,51,83,709	11.8
2017-18	10,02,738	18.0	5,71,202	17.8	4,08,202	19.9	1,67,73,145	10.5
2018-19	11,37,718	13.5	6,63,572	16.2	4,61,652	13.1	1,90,10,164	13.3

Source: Union Finance Accounts

**1.5.4** There was growth of 16.2 *per cent* in Corporation Tax and 13.1 *per cent* in Income Tax in FY 2018-19 as compared to growth of 17.8 *per cent* in Corporation Tax and 19.9 *per cent* in Income Tax in FY 2017-18. Growth of DT (13.5 *per cent*) and corporation tax (16.2 *per cent*) was more than the growth of GDP in 2018-19 which was 13.3 *per cent*.

**1.5.5** There are different stages of direct taxes collection such as Tax Deducted at Source (TDS), advance tax, self assessment tax, and regular assessment tax in respect of both Corporation and Income tax. The pre-assessment collection through TDS, advance tax and self assessment tax is indicative of voluntary compliance in the system. The collection of tax through regular assessment stage occurs post assessment.

**1.5.6** Table 1.8 below shows the collection of Corporation and Income Tax under different stages during FY 2014-15 to FY 2018-19.

Table 1.8: Collection of Corporation and Income Tax								(₹ in crore)
Financial Year	TDS	Advance Tax	Self assessment tax	Pre-assessment collection (Col. 2+3+4)	Percentage of total pre-assessment collection	Regular Assessment Tax	Other receipts	Total Collection (Col. 5+7+8)
1.	2.	3.	4.	5.	6.	7.	8.	9.
2014-15	2,59,106	3,26,525	52,050	6,37,681	79.8	80,189	81,589	7,99,459
2015-16	2,87,412	3,52,899	54,860	6,95,171	81.2	63,814	96,940	8,55,925
2016-17	3,43,144	4,06,769	68,160	8,18,073	82.8	74,138	95,887	9,88,098
2017-18	3,80,641	4,70,242	83,219	9,34,102	82.6	92,044	1,04,897	11,31,043
2018-19	4,50,769	5,27,529	84,174	10,62,471	82.6	99,032	1,24,757	12,86,260

Source: Pr. CCA, CBDT. The other receipts include surcharge and cess. The figures of collection comprises of refunds also.

**1.5.7** Table 1.8 shows that the voluntary compliance by assessees (pre assessment stage) accounted for 82.6 per cent in 2018-19 against 79.8 per cent in 2014-15 of the total collections of Corporation and Income Tax in FY 2018-19 whereas collection through regular assessment (post assessment) which was 10 per cent of total collection in 2014-15 reduced to 7.7 per cent in 2018-19. This shows that voluntary compliance by the assessees which was showing increasing trend during FY 2014-15 to FY 2016-17, has remained stable thereafter.

### 1.5.8 Trend of refunds

When the amount of tax paid exceeds the amount of tax payable, the assessees are entitled for a refund of the excess amount. The ITD releases this refund to the assessees from time to time. Table 1.9 below shows the quarterly trend of refunds made and revenue collection in respect of Corporation Tax and Income Tax during FY 2016-17 to FY 2018-19.

Table 1.9: Quarterly trend of refunds								(₹ in crore)
FY	Quarter ending	Corporation Tax			Income Tax			
		Gross collection	Refunds	Percentage of refunds with reference to collection	Gross collection	Refunds	Percentage of refunds with reference to collection	
2016-17	June 2016	1,05,330	51,320	48.7	74,081	7,257	9.8	
	September 2016	1,49,278	16,499	11.1	90,935	13,526	14.9	
	December 2016	1,57,724	24,232	15.4	93,954	13,946	14.8	
	March 2017	1,93,273	28,630	14.8	1,23,523	7,172	5.8	
	<b>Total</b>	<b>6,05,605</b>	<b>1,20,681</b>	<b>19.9</b>	<b>3,82,493</b>	<b>41,901</b>	<b>11.0</b>	

**Report No. 11 of 2020 (Direct Taxes)**

	June 2017	1,11,789	44,530	39.8	87,685	11,269	12.9
	September 2017	1,56,759	16,113	10.3	99,112	7,682	7.8
2017-18	December 2017	1,84,392	17,180	9.3	1,09,388	14,915	13.6
	March 2018	2,27,400	31,315	13.8	1,54,714	8,831	5.7
	<b>Total</b>	<b>6,80,340</b>	<b>1,09,138</b>	<b>16.0</b>	<b>4,50,899</b>	<b>42,697</b>	<b>9.5</b>
	June 2018	1,27,468	61,078	47.9	98,049	12,834	13.1
	September 2018	1,90,200	12,848	6.8	1,27,210	16,823	13.2
2018-19	December 2018	1,94,177	10,468	5.4	1,21,069	16,503	13.6
	March 2019	2,57,554	21,434	8.3	1,70,533	9,049	5.3
	<b>Total</b>	<b>7,69,399</b>	<b>1,05,828</b>	<b>13.8</b>	<b>5,16,861</b>	<b>55,209</b>	<b>10.7</b>

Source: Pr. CCA, CBDT

As can be seen from the Table 1.9 above, 48.7 per cent, 39.8 per cent and 47.9 per cent of gross collection of Corporation Tax during first quarter of FY 2016-17, FY 2017-18 and FY 2018-19 respectively was refunded against the previous year's collection, during the same quarter. Further, 42.5 per cent; 40.8 per cent and 57.7 per cent of total refund amount of Corporation Tax pertaining to previous year's collection was refunded during first quarters of FY 2016-17, FY 2017-18 and FY 2018-19 respectively. It is also noticed that refunds as a percentage of gross collection are higher in case of Corporation Tax as compared to Income Tax. The possible reason for this higher refund could be exaggerated demands raised by the department during the previous financial years to meet their revenue collection targets. The issue of exaggerated demands has also been raised in Chapter V of our Compliance Audit Report no. 40 of 2017. The ITD may examine the issue.

#### **1.5.9 Breach of Article 114(3) of the Constitution of India-Expenditure incurred on interest on refunds of taxes by the CBDT without appropriation**

Article 114(3) of Constitution of India stipulates that no money shall be withdrawn from the CFI except under appropriation made by the legislature. Payment of interest on refunds of excess tax is a charge on the CFI and can be made only if authorized under appropriation made by law. Further, as per Article 266(3) of the Constitution, until provided in the Appropriation law passed by Parliament, there is no legal authority to withdraw 'interest' on excess tax collected/refunds from the CFI. In addition, Rule 8 of DFPRs describes 'interest' as the primary unit of appropriation for classification of interest expenditure.

The Department of Revenue/Central Board of Direct Taxes (CBDT) has been classifying interest on refunds of excess tax as reduction in revenue in violation of the above mentioned constitutional provisions. This incorrect practice has been commented upon repeatedly in CAG's Audit Reports on Union

Government Accounts as well as in CAG's Reports on Direct Taxes, but no corrective action has been taken by the Department.

Audit observed that this issue was examined by the Public Accounts Committee (PAC). In its 66<sup>th</sup> Report (15<sup>th</sup> Lok Sabha 2012-13) the PAC had disapproved withdrawal of moneys out of CFI for interest payments on income tax refunds without Parliamentary approval. Subsequently, in their follow-up Report (96<sup>th</sup> Report of 15<sup>th</sup> Lok Sabha 2013-14 dated 31 January 2014) after considering the revised opinion of the Ld. Attorney General of 06 May 2013 and later testimony to it, the Committee concluded that the Constitution leaves no doubt about the manner of authorization of expenditure or withdrawal of moneys from and out of the CFI and hence the Department of Revenue has no option other than seeking *ex ante* approval under Articles 114 and 115(1)(a) or seeking *ex post facto* approval of Parliament under Article 115(1)(b) of the Constitution.

Audit noted that despite the position taken by PAC on the matter and the issue being repeatedly pointed out in the audit reports of the CAG the practice of not making budget provision for interest on refunds in the Budget Estimates and not seeking Parliament's approval for the payments continued in the financial year 2018-19. During the year expenditure on interest on refunds amounting to ₹ 20,566.33 crore was incurred and such payment was shown as reduction in Revenue.

The Department in its replies (January 2017 and January 2019) has continued to reiterate the opinion of Ld. AG of 06 May 2013, that the refund of excess tax and interest thereon is not an expenditure within the meaning of Article 112. The Department also stated that based on the above mentioned opinion of the Ld. AG, the Department with the approval of the Finance Minister, has not accepted the recommendations contained in the 96<sup>th</sup> Report of the PAC (15<sup>th</sup> Lok Sabha).

Audit however, observed that PAC had already considered the opinion of the Ld. AG while making its recommendations and noted that the Ld. AG had deposed that "an opinion ultimately is an opinion and it is for the Committee to decide what the correct procedure is".

## **1.6 Revenue impact of tax incentives**

**1.6.1** The primary objective of any tax law and its administration is to raise revenues for the purpose of funding government expenditure. The revenues raised are primarily dependent upon the tax base and effective tax rate. The determinant of these two factors is a range of measures which includes special tax rates, exemptions, deductions, rebates, deferrals and credits. These

measures are collectively called as “tax incentives or tax preferences”. These are also referred to as tax expenditure.

**1.6.2** The Income Tax Act, 1961 (the Act), *inter alia*, provides for tax incentives to promote exports, balanced regional development, creation of infrastructure facilities, employment, rural development, scientific research and development, growth of the cooperative sector and encourages savings by individuals and donations for charity. Most of these tax benefits can be availed of by both corporate and non-corporate taxpayers.

**1.6.3** The Union Receipt Budget depicts statement of revenue impact of major incentives on corporate taxpayers and non-corporate taxpayers based on returns filed electronically. Table 1.9 shows the revenue impact of major tax incentives for FY 2014-15 to FY 2018-19.

Table 1.9: Revenue impact of tax incentives (₹ in crore)				
Financial Year	Total Revenue impact of tax incentives	Revenue impact as <i>per cent</i> of		
		GDP	DT	GTR
2014-15	1,18,593	0.9	17.0	9.5
2015-16	1,38,658	1.0	18.7	9.5
2016-17	1,55,840	1.0	18.3	9.1
2017-18	1,83,580	1.1	18.3	9.6
2018-19	2,13,225	1.1	18.7	10.3

Note: The figures of revenue impact of tax incentives are actuals except FY 2018-19 (projected). These do not cover Charitable Institutions. However, the amount applied by Charitable Institutions was ₹ 5,03,783 crore in respect of 2,18,787 electronically filed returns till 31<sup>st</sup> March 2019. Source: Respective Receipt Budget.

As reported in the Receipts Budget for the FY 2019-2020, the effective rate of Corporation Tax for the FY 2017-18 was 29.5 *per cent*, as against the average statutory rate of 34.4 *per cent*.

**1.6.4** The major tax incentives given in FY 2018-19 were deductions on account of certain investments and payments under section 80C (₹ 75,244 crore), accelerated depreciation under section 32 (₹ 59,474 crore), deduction of export profits to SEZ units under section 10AA (₹ 24,839 crore), deductions to undertakings in generation/transmission and distribution of power under section 80-IA (₹ 15,677 crore), deductions under sections 35(1), (2AA) and (2AB) for expenditure on scientific research (₹ 7,950 crore).

**1.6.5** The revenue impact of tax incentives has increased by 79.8 *per cent* from ₹ 1,18,593 crore in FY 2014-15 to ₹ 2,13,225 crore in FY 2018-19. Though the tax incentives increased by 16.1 *per cent* in FY 2018-19 as compared to FY 2017-18, but increase in the share of revenue impact of tax incentives in DT and GTR was 0.4 *per cent* and 0.7 *per cent* respectively. Revenue impact of tax incentives was 1.1 *per cent* of GDP during FY 2018-19 and FY 2017-18 as compared to 1.0 *per cent* in FY 2015-16 and FY 2016-17.

## 1.7 Arrears of demand

1.7.1 Table 1.10 gives the trend of arrears of demand pending during the period FY 2014-15 to FY 2018-19.

Table 1.10: Arrears of Demand					(₹ in crore)
Financial Year	Arrears of earlier year's demand	Arrears of current year's demand	Total arrears of demand	Demand difficult to recover	Net collectible Demand
2014-15	5,68,724	1,31,424	7,00,148	6,73,032	27,116
2015-16	6,67,855	1,56,356	8,24,211	8,02,256	21,955
2016-17	7,33,229	3,11,459	10,44,688	10,29,725	14,963
2017-18	7,36,975	3,77,207	11,14,182	10,94,023	20,159
2018-19	9,46,190	2,87,888	12,34,078	12,19,485	14,593

Source: Directorate of Income Tax (Organisation & Management Services), Demand & Collection report (CAP-1) for the month of March of respective FY.

1.7.2 Demand & Collection report for the month of March of respective FYs analysed various factors viz. no assets/inadequate assets for recovery, cases under liquidation/BIFR, assessee not traceable, demand stayed by Courts/ITAT/IT authorities, TDS/prepaid taxes mismatch etc. leading to an estimation of the demands difficult to recover. Demands difficult to recover have been increasing year after year and accounted for 98.8 per cent of the total arrears of demands in FY 2018-19 as against 98.2 per cent in FY 2017-18. Though, total arrears of demand in FY 2018-19 amounted to ₹ 12,34,078 crore, increased by 10.8 per cent as compared to FY 2017-18 (₹ 11,14,182 crore) however, net collectible demand decreased to ₹ 14,593 crore in FY 2018-19 as compared to ₹ 20,159 crore in FY 2017-18 due to increase in demand difficult to recover. Increase in demand difficult to recover in FY 2018-19 was more than the increase in total arrears of demand during the same year by ₹ 5,566 crore.

## 1.8 Disposal of appeal cases

1.8.1 Table 1.11 gives the trend of disposal and pendency of appeal cases before CIT (Appeals) during FY 2014-15 to FY 2018-19.

Table 1.11: Disposal of Appeal Cases by CIT(A)					
Financial Year	Appeal cases due for disposal	Appeal cases disposed of	Appeal cases pending	Pendency in percentage	Amount locked up in Appeal cases
	(Number in lakh)				
2014-15	3.06	0.74	2.32	75.8	3,83,797
2015-16	3.53	0.94	2.59	73.3	5,16,250
2016-17	4.08	1.18	2.90	71.1	6,11,227
2017-18	4.25	1.21	3.04	71.7	5,18,647
2018-19	4.62	1.23	3.39	73.4	5,62,806

Source: CBDT

**1.8.2** The amount locked up in appeal cases with CIT (Appeals) is more than the revenue deficit of the Government of India in FY 2018-19.

**1.8.3** Table 1.12 below gives the position of Appeals pending with the Income Tax Appellate Tribunals (ITATs)/High Courts and Supreme Court during FY 2014-15 to FY 2018-19.

Financial Year	ITATs		High Courts		Supreme Court		Total	
	No.	Amt.	No.	Amt.	No.	Amt.	No.	Amt.
2014-15	37,506	1,45,535	34,281	37,684	5,661	4,654	77,448	1,87,873
2015-16	32,834	1,35,984	32,138	1,61,418	5,399	7,092	70,371	3,04,494
2016-17	37,968	1,43,771	38,481	2,87,818	6,375	8,048	82,806	4,39,637
2017-18	37,353	2,34,999	39,066	1,96,053	6,224	11,773	82,643	4,42,825
2018-19	92,205	NA	38,539	1,36,465	4,425	74,368 <sup>#</sup>	1,35,169	2,10,833

Source: CBDT # amount of appeals filed in Supreme Court by the assessee not available

**1.8.4** The cases pending with ITAT significantly increased in FY 2018-19 to 92,205 in comparison to FY 2017-18 (37,572 cases). The total cases pending at higher levels (ITATs/High Courts/Supreme Court) increased to 1.35 lakh in FY 2018-19 in comparison to 0.82 lakh cases in FY 2017-18.

## 1.9 Search & Seizure and Survey

The Search & seizure<sup>23</sup> and survey<sup>24</sup> are amongst the main evidence collecting mechanisms which are used in cases where credible information about tax evasion is in possession of the ITD. Table 1.14 below shows the details of search & seizure operations and surveys conducted and the undisclosed income admitted/detected during FY 2014-15 to FY 2018-19.

23 Search and Seizure is carried out under section 132 of the Act to unearth any undisclosed income or valuables.

24 Survey is carried out under section 133A and 133B of the Act for collecting any information, which may be useful for ITD in deterring tax evasion.

Table 1.13: Status of search & seizure and survey cases					(₹ in crore)
Financial Year	Number of groups searched	Undisclosed income admitted (in search & seizure)	Number of surveys conducted	Undisclosed income detected (in surveys)	
2014-15	545	10,288	5,035	12,820	
2015-16	447	11,226	4,428	9,700	
2016-17	1,152	15,497	12,526	13,716	
2017-18	577	15,913	13,487	9,634	
2018-19	983	18,594	15,401	16,126	

Source: Investigation Wing, CBDT

During FY 2018-19, undisclosed income admitted during search & seizure increased by 16.8 *per cent* and undisclosed income detected during survey increased by 67.4 *per cent* as compared to the respective figures in FY 2017-18.

### 1.10 Effectiveness of Internal Audit

**1.10.1** Internal audit is an important part of the Departmental control that provides assurance that demands/refunds are processed accurately by the correct application of the provisions of the Act. The internal audit of ITD completed audit of 1,62,467 cases in FY 2018-19 as against 1,89,409 cases audited in FY 2017-18.

**1.10.2** Table 1.14 shows details of internal audit observations raised, settled and pending for each of the five years from FY 2014-15 to FY 2018-19.

Table 1.14: Details of Internal audit observations									(₹ in crore)
Financial Year	Opening balance <sup>^</sup>		Addition		Settled		Pending		
	Cases	Amount	Cases	Amount	Cases	Amount	Cases	Amount	
2014-15	20,834	8,368	9,927	2,292	15,586	3,805	15,175	6,855	
2015-16	19,137	8,023	13,148	6,463	12,891	2,205	19,394	12,281	
2016-17	19,405	12,283	12,972	2,451	11,256	3,352	21,121	11,382	
2017-18	21,129	11,295	13,297	2,562	9,062	1,283	25,364	12,575	
2018-19	25,408	12,602	16,975	3,147	11,847	4,334	30,536	11,415	

Source: Directorate of Income Tax (Income Tax & Audit); <sup>^</sup>Figures revised after verification by respective CsIT(Audit) subsequent to submission of quarterly statement for the quarter ending March

**1.10.3** Out of 7,818 major finding cases<sup>25</sup> raised by internal audit, the Assessing Officers (AOs) acted upon only in 1,923 (24.6 *per cent*) in FY 2018-19 in comparison to 1,613 cases (25.7 *per cent*) out of 6,267 cases in FY 2017-18. The follow up of the internal audit observations by the AOs need to be improved.

<sup>25</sup> The monetary limit of major internal audit objections has been raised from ₹ Two lakh to ₹ 10 lakh as per instruction no. 6 of 2017 dated 21.7.2017.



## Chapter II: Audit Mandate, Products and Impact

### 2.1 Authority of the CAG for audit of receipts

Article 149 of the Constitution of India provides that the Comptroller and Auditor General of India (CAG) shall exercise such powers and perform such duties in relation to the accounts of the Union and of the states and of any other authority or body as may be prescribed by or under any law made by the Parliament. The Parliament passed the Comptroller and Auditor General's DPC Act (CAG's DPC Act) in 1971. Section 16 of the CAG's DPC Act authorises CAG to audit all receipts (both revenue and capital) of the Government of India and of Governments of each State and Union Territory having a legislative assembly and to satisfy himself that the rules and procedures are designed to secure an effective check on the assessment, collection and proper allocation of revenue and are being duly observed. Regulations on Audit & Accounts, 2007 (Regulations) lay down the principles for Receipt Audit.

### 2.2 Examination of systems and procedures and their efficacy

**2.2.1** Audit of receipts includes an examination of the systems and procedures and their efficacy mainly in respect of:

- a. identification of potential tax assesseees, ensuring compliance with laws as well as detection and prevention of tax evasion;
- b. exercise of discretionary powers in an appropriate manner including levy of penalties and initiation of prosecution;
- c. appropriate action to safeguard the interests of the Government on the orders passed by departmental appellate authorities;
- d. any measures introduced to strengthen or improve revenue administration;
- e. amounts that may have fallen into arrears, maintenance of records of arrears and action taken for the recovery of the arrears;
- f. pursuit of claims with due diligence and to ensure that these are not abandoned or reduced except with adequate justification and proper authority.

**2.2.2** To achieve the above, we examined the assessments completed by the Income Tax Department (ITD) in the financial year 2017-18. In addition, some assessments which were completed in earlier years were also taken up for examination.

**2.2.3** The ITD undertakes scrutiny assessments in respect of a sample of returns filed by the assessee as per the Income Tax Act, 1961. The income tax returns (ITRs) are selected for scrutiny through Computer Aided Scrutiny Selection (CASS) on the basis of parameters identified and pre-defined by the ITD. These cases are then closely examined in respect of claims of deductions, losses, exemptions etc. to arrive at the correct assessments to ensure that there is no evasion of taxes. The assessee is given the opportunity to substantiate his claim with evidence failing which the assessing officer (AO) makes the assessment as deemed appropriate. The work of processing, completion and rectification of assessment order in respect of scrutiny cases is done by the AO in Assessment Information System (AST)/Income Tax Business Application (ITBA) module. AST/ITBA undertakes calculation of tax, calculation of interest under various sections of the Act, time barring checks etc. In the case of scrutiny assessments, rectification, appeal effect orders, figures are data-fed to the system by the AOs based on the orders. The payments made by assessee in respect of TDS/TCS and advance tax etc. are auto populated from 26AS application and OLTAS application respectively.

On the basis of examination of scrutiny assessment cases, Audit noticed that despite irregularities of certain types being pointed out repeatedly in the audit reports, there are continued occurrences of these irregularities in following the tax laws and instructions and directives of CBDT during scrutiny assessments completed by the AOs, raising questions about the efficiency of tax administration. Some of these cases are discussed in the subsequent paragraphs.

**2.2.4** A total of 545.89 lakh returns were filed during the FY 2017-18<sup>26</sup>. In the same FY the ITD completed 2,99,232 scrutiny assessments in those units which were audited during audit plan of FY 2018-19. Out of the 2,99,232 scrutiny assessments, we checked 2,72,110 assessment cases. Apart from this, we also audited during FY 2018-19, 60,129 cases out of 1,59,388 cases of scrutiny assessments completed in financial years prior to 2017-18. Total number of scrutiny assessments audited during 2018-19 was 3,32,239 and the number of scrutiny assessments in which audit noticed errors was 19,768. The incidence of errors in assessments checked in audit during FY 2018-19 was 5.95 *per cent* which was less than the previous year's 6.45 *per cent*. Out of cases of scrutiny assessments audited by us, Internal Audit of ITD had checked 18,747 cases. As we have seen only a limited number of assessment cases/records as per our sample, the Ministry needs to verify this in entirety and not only in the cases of sample.

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<sup>26</sup> Total number of returns filed during FY 2016-17 were 444.02 lakh.

**2.2.5** State-wise incidence of errors in assessments are given in *Appendix-2.1*. Table 2.1 below shows details of 11 states with highest percentage of assessments with errors where more than 10,000 assessments were checked in audit during FY 2018-19.

Table 2.1: Details of 11 states with highest incidence or assessments with errors where more than 10,000 assessments were checked					(₹ in crore)
State	Assessments			Total revenue effect of the audit observations	Percentage of assessments with errors
	completed in units selected for audit during 2018-19	checked in audit during 2018-19	with errors		
a. Tamil Nadu	23,843	20,466	1,899	2,373.66	9.28
b. Karnataka	12,737	12,342	1,071	6,380.78	8.68
c. Madhya Pradesh	25,626	20,091	1,512	4,750.27	7.53
d. Andhra Pradesh & Telangana	25,620	22,160	1,548	1,412.90	6.99
e. Kerala	11,080	10,770	725	251.16	6.73
f. Gujarat	16,291	15,923	1,049	2,146.06	6.59
e. West Bengal	42,078	39,632	2,271	2,313.85	5.73
g. Maharashtra	1,60,227	75,596	3,502	18,816.02	4.63
h. Rajasthan	15,530	14,988	665	170.26	4.44
g. Delhi	42,378	32,794	1,372	1,373.40	4.18
j. Uttar Pradesh	26,617	26,257	884	1,127.25	3.37

This indicates that Tamil Nadu (9.28 *per cent*) has the highest percentage of assessments with errors followed by Karnataka (8.68 *per cent*). The ITD needs to take corrective action in respect of errors noticed in the assessments.

**2.2.6** Table 2.2 below shows the details of observations noticed in local audit during FY 2018-19.

Table 2.2: Tax wise details of observations in assessments		(₹ in crore)
Category	No. of Observations	Tax effect (TE)
a. Corporation tax (CT) and Income tax (IT)	21,266	44,920.89 <sup>27</sup>
b. Other Direct taxes (ODT)	267	11.25
<b>Total</b>	<b>21,533</b>	<b>44,932.14</b>

Note: The above findings and all subsequent findings are based exclusively on audit of selected assessments.

**2.2.7** Table 2.3 below shows the category-wise details of observations related to underassessment in respect of Corporation Tax and Income Tax. *Appendix-2.2* indicates details in respect of sub-categories under them.

<sup>27</sup> Includes 393 cases of over assessment with tax effect of ₹ 752.25 crore.

Table 2.3: Category-wise details of Observations related to under assessments		(₹ in crore)	
Category	No. of Observations	Tax effect	
a. Quality of assessments	7,504	9,768.64	
b. Administration of tax concessions/exemptions/deductions	6,407	18,533.62	
c. Income escaping assessments due to errors	2,536	6,939.74	
d. Others	4,426	8,926.64	
<b>Total</b>	<b>20,873</b>	<b>44,168.64</b>	

### 2.3 Persistent and pervasive irregularities in respect of Corporation Tax and Income Tax assessments cases

The instances of non-compliance and irregularities noticed during audit examination of assessment cases completed by the AOs are brought out in our Compliance Audit Report-Department of Revenue-Direct Taxes every year. An irregularity may be considered persistent if it occurs year after year. It becomes pervasive, when it affects the entire system and is distributed over many assessment jurisdictions. We have been pointing out various irregularities with respect to assessment of corporation and income tax cases in the Compliance Audit Reports year after year, and some of these irregularities seem to be both persistent and pervasive including those relating to:

- (i) irregularities in allowing depreciation/business losses/capital losses etc.,
- (ii) instances of incorrect allowance of business expenditure,
- (iii) Excess or irregular refunds/interest on refunds, and
- (iv) Errors under special provisions including MAT/Tonnage Tax etc.

Recurrence of irregularities, despite being pointed out repeatedly in audit reports, is not only indicative of non-seriousness on the part of the Department in instituting appropriate systems to prevent recurrence of such repetitive errors. It also points the lack of effective monitoring and absence of an institutional mechanism to respond to the systematic and structural weaknesses leading to leakages of revenue. The audit observations included in the Compliance Audit Report<sup>28</sup> during the years 2015-16, 2016-17 and 2017-18 alongwith draft paragraphs (DPs) issued to the Ministry during 2019-20 were analysed to examine the persistence and pervasiveness of irregularities. Though the irregularities noticed in different states showed no

28 C&AG's Compliance Audit Report (Union Government – Department of Revenue – Direct Taxes) no. 2 of 2017 (for the year ended March 2016), no. 40 of 2017 (for the year ended March 2017) and no. 9 of 2019 (for the year ended March 2018).

distinctive pattern of occurrences among the states, they were occurring more frequently in some states than others; their occurrences were seen to be consistently high in Maharashtra.

Cases of such irregularities reported in the above mentioned categories are discussed below.

### 2.3.1 Administration of tax concessions/exemptions/deductions—Irregularities in allowing depreciation/business losses/capital losses etc.

We noticed irregularities related to incorrect allowance and set-off of business losses, capital losses and unabsorbed depreciation, incorrect allowance of depreciation etc. The nature of such irregularities included:

- (i) incorrect allowance of set-off of brought forward business losses and unabsorbed depreciation where no loss in respect of earlier assessment years (AYs) was available,
- (ii) adoption of incorrect figures viz. earlier years' business loss adopted as returned loss in current AY,
- (iii) incorrect allowance of carry forward of business loss although ITR for the said AY was filed after due date of filing of return, and
- (iv) double deduction on account of depreciation etc.

Such irregularities occurred due to non-correlation of assessment records which indicates failure of the AOs in applying due diligence and to comply with the law. Irregularities noticed in allowance of depreciation/business losses/capital losses etc. during 2015-16 to 2017-18, as brought out in the Compliance Audit Reports of past three years along with findings of the current year Audit Report (2018-19) are summarised in the Table 2.4 below.

Table 2.4: Irregularities noticed in allowing depreciation/business losses/capital losses etc.								(₹ in crore)	
Assessment	Audit Report for the year ended								
	March 2016		March 2017		March 2018		March 2019		
	No. of errors	Tax Effect	No. of errors	Tax Effect	No. of errors	Tax Effect	No. of errors	Tax Effect	
CT	71 <sup>29</sup>	590.75	81 <sup>30</sup>	1,144.10	66 <sup>31</sup>	1,796.86	75	2,655.15	
IT	9	15.72	9	24.41	7 <sup>32</sup>	9.19	14	21.29	

29 Andhra Pradesh & Telangana, Bihar, Delhi, Gujarat, Haryana, Jharkhand, Karnataka, Kerala, Maharashtra, Odisha, Rajasthan, Tamil Nadu and West Bengal.

30 Andhra Pradesh & Telangana, Delhi, Gujarat, Haryana, Jharkhand, Karnataka, Kerala, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh and West Bengal

31 Andhra Pradesh & Telangana, Assam, Delhi, Gujarat, Karnataka, Madhya Pradesh, Maharashtra, Odisha, Rajasthan, Tamil Nadu, UT Chandigarh, Uttar Pradesh and West Bengal

32 Bihar, Delhi, Rajasthan, Maharashtra and West Bengal.

During 2015-16, the non-compliance on this account was found highest in Maharashtra at 63 per cent of the total tax effect of DPs on Corporation Tax related to incorrect allowance of depreciation/business losses/capital losses etc. During 2016-17, it was found highest in Andhra Pradesh & Telangana (36 per cent) and Maharashtra (32 per cent). During 2017-18, irregularities on this account were found highest in Maharashtra (58 per cent) and during 2018-19 these were highest in Bihar (38.6 per cent) and Maharashtra (34 per cent). Further, tax effect of irregularities which was ₹ 590.75 crore in March 2016 increased to ₹ 2,655.15 crore in March 2019 showing an increase of more than 300 per cent over the period.

In respect of Income Tax, such irregularities were found to be highest in Maharashtra at 68 per cent of the total tax effect of DPs on Income Tax related to incorrect allowance of depreciation/business losses/capital losses etc. during 2015-16. During 2016-17 the tax effect on this account was found highest in Bihar (67 per cent) and in Maharashtra during 2017-18 (67 per cent). During 2018-19, these irregularities were highest in Bihar (30 per cent).

### 2.3.2 Administration of tax concessions/exemptions/deductions - Incorrect allowance of business expenditure

We noticed irregularities related to incorrect allowance of ineligible claims of business expenditure viz. capital expenditure, unpaid claims and provisions deemed as unascertained liability etc. Errors in incorrect allowance of expenditure noticed during 2015-16 to 2017-18, as brought out in the Compliance Audit Reports of past three years along with findings of the current year Audit Report (2018-19) are summarised in the Table 2.5 below.

Assessment	Audit Report for the year ended							
	March 2016		March 2017		March 2018		March 2019	
	No. of errors	Tax Effect	No. of errors	Tax Effect	No. of errors	Tax Effect	No. of errors	Tax Effect
CT	47 <sup>33</sup>	514.09	50 <sup>34</sup>	478.67	48 <sup>35</sup>	875.47	49	764.39

During 2015-16, such irregularities were highest in Maharashtra (23 per cent of the total tax effect of DPs related to incorrect allowance of business expenditure) and Andhra Pradesh & Telangana (30 per cent). During 2016-17 the non-compliance on this account was found highest in Maharashtra

33 Andhra Pradesh & Telangana, Assam, Delhi, Gujarat, Haryana, Karnataka, Maharashtra, Odisha, Punjab, Tamil Nadu and West Bengal.

34 Andhra Pradesh & Telangana, Delhi, Gujarat, Karnataka, Kerala, Maharashtra, Odisha, Rajasthan, Tamil Nadu and West Bengal.

35 Andhra Pradesh & Telangana, Karnataka, Kerala and Maharashtra.

(64 per cent) whereas in 2017-18 such non-compliance was highest in Maharashtra (60 per cent) and Tamil Nadu (28 per cent). During 2018-19, irregularities on this account were highest in Maharashtra (47 per cent) and Karnataka (22.5 per cent).

### 2.3.3 Quality of Assessments – Excess or irregular refunds/interest on refunds

We noticed irregularities emanating from excess or irregular refunds or interest on refunds caused by computing errors, not considering the refund already issued/adjusted, excess computation of interest on refund, etc. Errors noticed in this category during 2015-16 to 2017-18 as brought out in the Compliance Audit Reports of past three years along with findings of the current year Audit Report (2018-19) are summarised in the Table 2.6 below.

Table 2.6: Excess or irregular refunds/interest on refunds								(₹ in crore)	
Assessment	Audit Report for the year ended								
	March 2016		March 2017		March 2018		March 2019		
	No. of errors	Tax Effect	No. of errors	Tax Effect	No. of errors	Tax Effect	No. of errors	Tax Effect	
CT	6 <sup>36</sup>	49.46	6 <sup>37</sup>	50.35	4 <sup>38</sup>	30.98	5	1114.29	
IT	NIL	NIL	NIL	NIL	NIL	NIL	1	0.11	

During 2015-16, such irregularities were highest in Kerala (78 per cent of the total tax effect of DPs on Corporation Tax and Income Tax related to excess or irregular refunds/interest on refunds) and Maharashtra (17 per cent) whereas in 2016-17, it was found highest in Karnataka (78 per cent) and Maharashtra (22 per cent). During 2017-18, it was found 100 per cent in Maharashtra. During 2018-19, these irregularities were highest in Karnataka (99.6 per cent)<sup>39</sup>.

### 2.3.4 Income escaping assessment due to errors – Irregularities under special provisions including MAT/Tonnage Tax etc.

We noticed irregularities related to errors in levying tax under special provisions of the Act due to:

- (i) errors in computation of book profit,
- (ii) not considering the expenditure disallowed under normal provisions for computing book profit,
- (iii) not considering the specified expenditure for computing book profit,

36 Andhra Pradesh & Telangana, Bihar, Delhi, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Tamil Nadu and West Bengal.

37 Karnataka and Maharashtra

38 Maharashtra.

39 Wherever significance is mentioned, it is only with reference to the total tax effect and not in relation to the number of cases.

(iv) tax levied under normal provisions instead of special provisions, etc.

Errors noticed under special provisions of the Act during 2015-16 to 2017-18, as brought out in the Compliance Audit Reports of past three years along with findings of the current year Audit Report (2018-19) are summarised in the Table 2.7 below.

Table 2.7: Errors under special provisions including MAT/Tonnage Tax etc. (₹ in crore)								
Assessment	Audit Report for the year ended							
	March 2016		March 2017		March 2018		March 2019	
	No. of errors	Tax Effect	No. of errors	Tax Effect	No. of errors	Tax Effect	No. of errors	Tax Effect
CT	13 <sup>40</sup>	62.35	1 <sup>41</sup>	2.06	28 <sup>42</sup>	100.43	22	447.85
IT	NIL	NIL	NIL	NIL	1 <sup>43</sup>	0.22	2	1.26

During 2015-16, the non-compliance on this account was found highest<sup>44</sup> in Uttar Pradesh (52 *per cent* of the total tax effect of DPs on Corporation Tax and Income Tax related to errors noticed under special provisions including MAT/Tonnage Tax etc.) and Maharashtra (23 *per cent*). In 2016-17, the non-compliance was 100 *per cent* in Maharashtra whereas in 2017-18 such non-compliance was highest in Maharashtra (48 *per cent*) and in Karnataka (13 *per cent*). During 2018-19, these irregularities were highest in Delhi (68.8 *per cent*). These cases have been reported as DPs for Audit Report 2018-19. Further, tax effect of errors increased to ₹ 447.85 crore in March 2019 from ₹ 62.35 crore in March 2016 showing an increase of more than 600 *per cent* during the period.

Non-compliance of tax laws and instructions and directives of CBDT is one of the major risk areas affecting the efficiency of tax administration. In order to improve the same, the departmental systems and processes have significantly been computerised over the years for efficient processing and improved compliance at all stages of assessment. The ITD selects cases through CASS on the basis of pre-defined parameters for detailed scrutiny to be done by AO. During scrutiny assessment, AO calls for required information from the assessee and examines them in the light of applicable provisions of the Act. However, as seen from the above analysis, the risks of non-compliance still exists in above areas as indicated by the continuing occurrence of the similar types of irregularities over time, despite these being pointed out by audit from

40 Delhi, Gujarat, Rajasthan, Maharashtra, Tamil Nadu, Uttar Pradesh and West Bengal.

41 Maharashtra

42 Andhra Pradesh & Telangana, Delhi, Gujarat, Karnataka, Maharashtra, Odisha, Rajasthan, Tamil Nadu and West Bengal.

43 UTs of Jammu & Kashmir; and Ladakh

44 Wherever significance is mentioned, it is only with reference to the total tax effect and not the number of cases.

year to year and there seems to be no system to make the AOs more accountable for minimising, if not eliminating, repetition of similar or identical errors.

### Conclusion and Recommendation

*From the above analysis and also from our past experiences, it is clear that the required systems and processes to minimise the risk of recurrence and repetition of similar types of errors in computation of taxable income, once they are pointed out in audit, is absent in the Department. Once such an irregularity noticed in assessment completed by the AO has been pointed out in audit, it is expected that appropriate checks should be instituted by the Department to prevent recurrence of similar types of irregularities and errors in assessment in future, especially in view of the fact that now even the scrutiny assessments are being carried out by the AOs on the system, which is not seen to be the case.*

*It is recommended that the IT Department may (i) fix accountability on the part of the AOs (ii) accordingly improve the mapping of the business rules of their system to ensure that the risk of recurrences of similar types of irregularities are minimised, besides instituting systems and procedural checks to ensure this.*

## 2.4 Audit products and response to audit

**2.4.1** We elicit response from the audited entities at different stages of audit. As per provision of Regulations 193 on completion of field audit, we issue the local audit report (LAR) to ITD for comments.

**2.4.2** Table 2.8 below depicts the position of number of observations included in the LAR issued during FY 2016-17 to FY 2018-19 and replies received thereto and observations accepted (as on 31 March of respective financial year).

Financial Year	Observations raised	Reply received		Reply not received	Percentage of Observations accepted	Percentage of reply not received
		Observations Accepted	Observations not accepted			
2016-17	22,579	4,074	3,546	14,959	53.46	66.25
2017-18	24,502	3,983	2,882	17,637	58.02	71.98
2018-19	21,533	3,357 <sup>45</sup>	2,743	15,433	55.03	71.67

<sup>45</sup> 1,236 - Observations accepted and remedial action taken; 2,121- Observations accepted but remedial action not taken

From the above Table 2.8, it can be seen that percentage of replies not received increased consistently from 66.25 *per cent* in FY 2016-17 to 71.67 *per cent* in FY 2018-19.

**2.4.3** Table 2.9 below shows the position of pending observations.

Table 2.9: Details of outstanding audit observations (₹ in crore)								
Period	CT		IT		ODT		Total	
	No.	TE	No.	TE	No.	TE	No.	TE
Upto Mar 2017	15,845	58,688.78	12,305	8,923.22	1,855	361.24	30,005	67,973.24
March 2018	6,370	21,241.47	7,443	3,903.89	308	227.76	14,121	25,373.12
March 2019	3,407 <sup>46</sup>	18,817.95	5,448	7,362.39	136	7.97	8,991	26,188.31
<b>Total</b>	<b>25,622</b>	<b>98,748.20</b>	<b>25,196</b>	<b>20,189.50</b>	<b>2,299</b>	<b>596.97</b>	<b>53,117</b>	<b>1,19,534.67</b>

The accretion in pendency in replies to audit findings each year has resulted in accumulation of 53,117 cases involving revenue effect of ₹ 1,19,534.67 crore as of 31 March 2019.

The Audit Regulations 202 and 203 require establishment of system and procedures to ensure adequate, constructive and timely action on audit observations included in Inspection Reports/Audit Notes and establishment of audit committees for monitoring and ensuring compliance and settlement of pending audit observations. The Department's efforts to ensure that replies to audit are sent in the prescribed period have not been satisfactory. Provisions of the Audit Regulations need to be observed in letter and spirit by the ITD.

**2.4.4** We issue significant and high value cases noticed in audit to the Ministry for comments before inclusion in the Audit Report as per provision of Regulations 205 to 209. We give six weeks to the Ministry to offer their comments on cases issued to them before their inclusion in the Audit Report. We have included 393 high value cases in Chapter III and IV of this Report, out of which replies were received for 190 cases as of 30 June 2020. The Ministry/ITD accepted 174 cases<sup>47</sup> (91.5 *per cent*) having tax effect of ₹ 2,326.90 crore (92.8 *per cent*) while it did not accept 16 cases<sup>48</sup> having tax effect of ₹ 180.75 crore. Replies to remaining 203 cases having tax effect of ₹ 5,873.14 crore were not received. Table 2.10 shows category wise details of these cases<sup>49</sup>.

46 Observations become pending after six months of issue of the observations

47 Ministry -96.cases; ITD -78 cases

48 Ministry -7 cases; ITD - 9 cases

49 Sub-categories-wise details are given in Appendix-2.3

Table 2.10 Category-wise details of errors of high value cases							(₹ in crore)
Category	CT		IT		Total		
	No.	TE	No.	TE	No.	TE	
a. Quality of assessments	51	1,477.60	29	19.05	80	1,496.65	
b. Administration of tax concessions/exemptions/ deductions	176	5,456.76	30	121.72	206	5,578.48	
c. Income escaping assessments due to errors	77	1,043.41	17	26.27	94	1,069.68	
d. Overcharge of tax/interest	12	232.66	1	3.32	13	235.98	
<b>Total</b>	<b>316</b>	<b>8,210.43</b>	<b>77</b>	<b>170.36</b>	<b>393</b>	<b>8,380.79</b>	

**2.4.5** Chapters III and IV bring out details of errors in assessments in respect of Corporation Tax and Income Tax respectively. Besides, Chapter V brings out our report on a subject specific compliance audit (SSCA) on 'Interest under sections 234A, 234B, 234C and 244A of the Act'. The Chapter points out that the interest was wrongly computed either due to systemic deficiencies in AST or due to incorrect interventions/computation by the AOs. Availability of manual intervention in AST was misused by AOs by way of modifying the interest at excess amount which led to blockade of refund of the assessee. The system deficiency with respect to calculation of interest still persisted in the new application, i.e. Income Tax Business Application.

**2.4.6** In addition, a long draft paragraph on 'Long Term Capital Gain on Penny Stocks' has been separately included in Chapter VI of this Report. The chapter includes audit observations from a test check of cases pertaining to Mumbai jurisdiction on the deficiencies in assessments of claim of Long Term Capital Gain (LTCG) by the beneficiaries identified by the Directorate of Income Tax (Investigation) Kolkata in its report 'Project Bogus LTCG/STCL through BSE Listed Penny Stocks', and absence of controls, if any.

## **2.5 Audit impact**

### **Amendments at the instance of Audit**

**2.5.1.** We analyse the impact of Audit resulting into amendments to the Income Tax Act and Rules framed thereunder, based on our observations/recommendations. During FY 2017-18, Performance Audit Report viz. Report No. 27 of 2017 – 'Assessment of Private Hospitals, Nursing Homes/Medical Clinics, Medical Colleges/Research Institutes, Diagnostic Centres, Pathological labs and other Medical supplies agencies/stores' was placed in the Parliament. Following paragraphs 2.5.2 to 2.5.5 enumerate the impact of Audit.

**2.5.2.** Audit examination of a sample of trust hospitals situated in Maharashtra revealed that the conditions specified in the Bombay Public Trust

Act, 1950 (BPT Act) were not fulfilled in some cases though exemptions were allowed to such trusts<sup>50</sup>. The Income Tax Act, however, did not identify non-compliance with the BPT Act as a ground to deny exemption and the Income Tax Act did not have its own criteria to identify and classify charitable institutions on the basis of measurable and quantifiable parameters, like those described under the BPT Act. Under such circumstances, trusts that were not fulfilling the criteria for charity prescribed under governing Acts of the State were able to claim exemptions under the Income Tax Act. Further in cases where registration status of the trust assessee changes under state laws, it could not be ascertained whether ITD had any mechanism to deal with the exemptions already allowed in such cases.

**2.5.3.** In a move to discourage such trusts from deviating from their objects, an amendment has been made in section 12AA of the Act in 2019 to empower the PCIT to cancel the registration of a trust violating the requirements of any other law, which was material for the purpose of achieving the objects after affording a reasonable opportunity of being heard.

**2.5.4.** Audit noticed<sup>51</sup> that section 80G certificates (receipts issued by the donees to donors for donation) were available in 10 *per cent* of cases. In the remaining cases, only a list of donations received was available. In the absence of section 80G certificates, it was not clear as to how the AOs cross-verified the donation receipts vis-à-vis the claims. In the absence of mechanism for cross verification of claims made by donors and donees, the chances of ineligible assessee getting deduction could not be ruled out. Therefore, the Audit recommended<sup>52</sup> that CBDT may consider the possibility of introducing automated generation of 80G certificates above a certain threshold.

**2.5.5.** To address the above issue, Section 80G has been amended in 2020 to provide that entities receiving donations shall file a statement of the donation received and shall issue a certificate to the donor.

## **2.6. Recovery at the instance of audit**

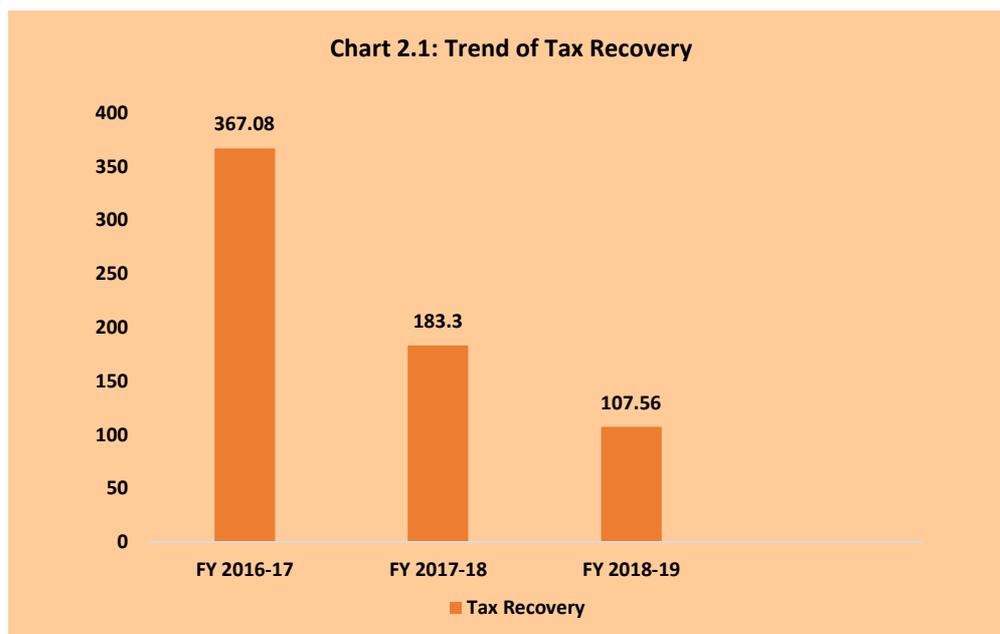
The ITD recovered ₹ 657.94 crore in the last three years (Chart 2.1) from demands raised to rectify the errors in assessments that we pointed out. This includes ₹ 107.56 crore recovered in FY 2018-19.

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50 Para no.3.2.1 of Report No. 27 of 2017

51 Para no.3.2.5 of Report No. 27 of 2017

52 Para No. 3.5(iii) of Report No. 27 Of 2017



## 2.7 Time barred cases

**2.7.1** Table 2.11 below shows the details of time-barred cases<sup>53</sup> during FY 2016-17 to FY 2018-19.

Table 2.11: Details of time-barred cases			(₹ in crore)
Year of Report	Cases	Tax effect	
2016-17	2,243	1,637.81	
2017-18	2,739	2,735.17	
2018-19	1,961	2,237.05	

**2.7.2** During FY 2018-19, 1,961 cases with tax effect of ₹ 2,237.04 crore became time-barred for remedial action, of which Odisha alone account for 28.91 *per cent* of this tax effect followed by West Bengal at 26.29 *per cent*. *Appendix-2.4* indicates state-wise details of such cases for FY 2018-19. Responsibility may be fixed for not taking remedial action in time in such cases. The Department should ensure that remedial action is taken in time so that such incidences do not recur in future.

## 2.8 TDS Mismatch

Tax deducted at source (TDS) aims to ensure collection of revenue at the instance of the transaction. TDS collection which was ₹ 3.43 lakh crore in FY 2016-17 increased to ₹ 4.51 lakh crore in FY 2018-19 and now contributes more than 35 *per cent* to the gross direct taxes collections, emphasizing its ever-growing importance. TDS on salary payment is the biggest component of TDS and has been around 43 *per cent* in the last three years.

<sup>53</sup> Notice under section 148 cannot be issued for reopening the case after six years from the end of the relevant AY.

### 2.8.1 TDS Mismatch cases

TDS has twin purposes namely collection of tax in advance i.e. before the end of financial year (i.e. 31<sup>st</sup> March) and creation of a foot print of the transaction so that the income, associated with the transaction, in the hands of the recipient does not go untraced or unreported. There are three elements to it:

- a. The party making the payment (Deductor);
- b. The party receiving the payment (Deductee); and
- c. The Income Tax Department.

An assessee may file his return of income as per details available with him in Form 16/16A and 26AS. However, the tax credit is given by the Income Tax Department (ITD) according to the details available in its Tax Information Network (TIN) (which contains details of advance tax, self-assessment tax, regular tax and *inter alia* TDS payments). Whenever the TDS deduction claimed by the assessee does not match with that in the TIN, it is a case of mismatch of TDS. Due to such mismatch TDS credit is denied to the assessee (taxpayer) despite receipt of the revenue by the ITD or presence of Form 16/16A issued by deductor in support of his claim. This results in disallowance of refunds and also in creation of infructuous demands for tax resulting in avoidable harassment to the taxpayer.

The TDS mismatch cases for the FY 2016-17 to FY 2018-19 are given below:

Table 2.12: PAN status wise difference between TDS amount available in Form 26AS and reported in ITR (₹ in crore)				
FY	PAN status <sup>54</sup>	Number of PAN where TDS mismatch reported by ITR	TDS Amount Claimed	TDS Amount available in Form 26AS
2016-17	P	2,27,738	1,772.42	1,249.04
	Others	1,07,344	11,344.63	10,361.63
	<b>Total</b>	<b>3,35,082</b>	<b>13,117.05</b>	<b>11,610.67</b>
2017-18	P	11,73,933	6,580.21	5,854.92
	Others	1,90,642	12,095.03	10,431.68
	<b>Total</b>	<b>13,64,575</b>	<b>18,675.24</b>	<b>16,286.60</b>
2018-19	P	2,318	2.12	2.19
	Others	3	0.01	0.02
	<b>Total</b>	<b>2,321</b>	<b>2.13</b>	<b>2.21</b>
<b>Grand Total</b>		<b>17,01,978</b>	<b>31,794.42</b>	<b>27,899.48</b>
Source: ITD				

It can be seen from the above that the majority of the assessees who face the TDS mismatch issues are individual taxpayers, majorly being salaried individuals.

<sup>54</sup> P – Individuals; Others include company, Association of Persons, Body of Individuals, Firm, Government Authority, HUF, Artificial Juridical Person, Local Authority;

## 2.8.2 Nature of TDS Mismatches

The TDS mismatches are due to the difference in the amount available in Form 26AS and that claimed by the assessee through his ITR. TDS mismatch may be on account of (i) amount in Form 26AS is more than the amount claimed through ITR by the assessee and (ii) amount claimed by the assessee in ITR is more than the amount in Form 26AS.

The number of cases where the amount available in Form 26AS was less than TDS amount claimed by the individual assessee during FYs 2016-17 to 2018-19 was 65 per cent of total TDS mismatch cases.

Table 2.13 below shows cases where amount available in Form 26AS was more than the amount of TDS amount claimed by the Individual assessee during FY 2016-17 to FY 2018-19.

Table 2.13: Difference where TDS amount available in Form 26AS was higher than ITR				(₹ in crore)
FY	Number of PAN where TDS mismatch reported by ITR	TDS Amount Claimed	TDS Amount available in Form 26AS	Diff (TDS amount available in Form 26AS - TDS amount claimed)
2016-17	64,972	203.42	325.19	121.77
2017-18	4,26,851	1,681.10	1,765.30	84.20
2018-19	1,441	0.90	1.44	0.54
<b>Grand Total</b>	<b>4,93,264</b>	<b>1,885.42</b>	<b>2,091.93</b>	<b>206.51</b>

Source: ITD

Table 2.14 below shows cases where the amount available in Form 26AS was less than TDS amount claimed by the Individual assessee during FYs 2016-17 to 2018-19.

Table 2.14: Difference where TDS amount available in Form 26AS was lower than ITR				(₹ in crore)
FY	Number of PAN where TDS mismatch reported by ITR	TDS Amount Claimed	TDS Amount available in Form 26AS	Diff (TDS amount available in Form 26AS-TDS amount claimed)
2016-17	1,62,766	1,569.00	923.85	(-) 645.15
2017-18	7,47,082	4,899.11	4,089.62	(-) 809.49
2018-19	877	1.22	0.75	(-) 0.47
<b>Grand Total</b>	<b>9,10,725</b>	<b>6,469.33</b>	<b>5,014.22</b>	<b>(-) 1,455.11</b>

Source: ITD

The difference in the amount under 26AS and claimed through ITR, indicates that the tax deductors, as mandated under the Act did not provide the complete information to ITD on the tax deducted, as claimed by the assessee through their return or the assessee did not claim the correct amounts.

The possible reasons for mismatch of TDS amount may be – the deductor did not deposit TDS on time, file the quarterly TDS return on time, incorrect amount entered in the TDS return, quoted incorrect PAN, the deductor's TAN wrongly entered in ITR, mistake in selecting assessment year. It may also include cases of assesseees who were not required to pay tax or file the ITR.

Therefore, ITD did not allow credit for TDS which resulted into either raising demand or not releasing refunds by ITD, causing harassment to the assesseees, especially individual assesseees.

Therefore, to examine the reasons for mismatch of TDS claims and corrective measures taken by the Department to match the claim of the individual salaried taxpayer, a study on 'Income Tax Demands raised on account of TDS mismatch', with focus on salary class assesseees, was taken up in June 2019.

**2.8.3** We had called for deductor-wise data relating to unconsumed challans and amount involved, PAN-wise granular data relating to TDS credit mismatch etc. from the ITD in June 2019. The partial data relating to the TDS mismatch was received in October 2019 and without the information on AO (assessment) jurisdiction. Therefore, the data could not be used for audit planning. CPC-TDS, subsequently informed that they did not have the information on the assessment jurisdiction of the cases of TDS mismatch provided by them.

We also tried to analyze the issue through test check. The study was started (September 2019) for a limited number of jurisdictions viz. Bengaluru, Delhi, Hyderabad, Mumbai and Jaipur. Audit was able to identify 2,264 assesseees having TDS mismatch from jurisdictional AOs (one circle and two wards from each jurisdiction) of salary circle.

However, we could not, further, examine the assessment records of the sample selected as the assessment records were not available with the jurisdictional assessing officers as the same was not pushed to them by the CPC-Bengaluru, even after two years of the assessment year. Therefore, the assessment records were sought from the CPC-Bengaluru (November 2019 and January 2020). The relevant information has not been provided by the CPC-Bengaluru (July 2020).

Consequently, the reasons for the TDS mismatches, status of their resolution, the mode of the resolution, efforts of the department, as well as correctness and completeness of information shared by ITD etc. could not be ascertained in audit.

Inability of the department to furnish relevant information to complete the audit has prevented the C&AG from fulfilling his constitutional mandate.

The ITD needs to ascertain whether the mismatches were due to the IT systems or the failure of deductors in furnishing correct returns/ information. It needs to be ascertained in how many cases the ITD raised demand from the taxpayers because of the mismatch, as such causing harassment to the taxpayer. In cases of failure of the deductors, necessary action may be taken against the defaulting deductors under the Act by ITD. ITD also needs to examine the mismatch to ensure that no tax is levied on the persons who are not required to pay tax.

The ITD needs to provide relevant data to audit, so that the audit could be conducted.

## 2.9 Non-production of records

**2.9.1** We scrutinize assessment records under section 16 of the C&AG's (DPC) Act, 1971 with a view to securing an effective check on the assessment and collection of taxes and examining that regulations and procedures are being duly observed. It is also incumbent on ITD to expeditiously produce records and furnish relevant information to Audit.

**2.9.2** The ITD did not produce 17,992 records out of 3,61,430 records<sup>55</sup> requisitioned during FY 2018-19 (4.98 *per cent*) which is an improvement over FY 2017-18 (8.27 *per cent*). Non-production of records has increased significantly in Assam, UTs of Jammu & Kashmir; and Ladakh, and Tamil Nadu during FY 2018-19 over previous year.

Appendix 2.5 shows the details of non-production of records during FY 2016-17 to FY 2018-19. Table 2.15 shows details of records not produced to audit pertaining to same assesseees in three or more consecutive audit cycles.

Table 2.15: Records not produced to Audit in three or more audit cycles	
States	Records not produced
a. Odisha	4

In FY 2018-19, four records pertaining to same assesseees in one state were not produced to audit in last three or more consecutive audit cycles.

**2.9.3** Directorate of Income Tax (Systems) instructed all PCCITs/CCIT(CCA) to send a Status Report, of verification of returns in cases where assesseees had returned income of more than ₹ one crore from agriculture, to DGIT(Systems) after examination of aspects such as whether tax payer may have made a data entry error while filling up the return.

In Report no. 9 of 2019 of the C&AG of India under chapter-5 on 'Assessments relating to Agriculture income' we had pointed out difference in amount of

<sup>55</sup> Includes 21,000 records not produced in earlier years and requisitioned again during current audit cycle

agricultural income as per the ITR filed by the assessee and the amount entered in AST system in 36 cases due to errors at data entry level in respect of agriculture income above one crore for which status report had been called for from 136 PsCIT by audit. Even after a duration of one year from placement of the report the Status reports from 82 PsCIT are still awaited (June 2020).

As the data entry errors reported above were based on information furnished by only few selected Commissionerates compliance to furnishing of status reports to DsGIT(System) could not be ascertained in all the Commissionerates selected for audit. Consequently, the status of corrections in respect of data entry errors in agricultural income in AST database for agricultural income claims greater than ₹ one crore could not be verified.

Thus, Audit could not discharge its constitutional mandate due to non-production of records.

## 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<sup>56</sup> were filed by corporate assesseees 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<sup>57</sup> 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<sup>58</sup> (AST) module/ Income Tax Business Applications<sup>59</sup> (ITBA) with respect to computation of interest under sections 234A, 234B, 234C and 244A of the Income Tax Act,

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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.

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.
<b>Total</b>	<b>51</b>	<b>1,477.60</b>	

### 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)(viiia) 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)(viiia) 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)(viiia) 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.	
<b>Total</b>	<b>176</b>	<b>5,456.76</b>		

### 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<sup>60</sup> 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.*

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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<sup>61</sup>, 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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61 Department of Scientific and Industrial Research

### 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.	
<b>Total</b>	<b>77</b>	<b>1,043.41</b>		

### 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's 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.*



## Chapter IV: Income Tax

### 4.1 Introduction

**4.1.1** This chapter discusses the result of audit of assessments related to income tax audited during 2018-19. A total of 537.90 lakh ITRs<sup>62</sup> were filed by non-corporate assessees during the FY 2017-18. The ITD completed a total of 3,18,197 non-corporate scrutiny assessments in FY 2017-18 or in earlier years in those units which were audited during 2018-19. Out of the 3,18,197 non-corporate scrutiny assessments, we checked 2,21,027 non-corporate scrutiny cases and found errors in 12,322 assessments. The incidence of errors in non-corporate scrutiny assessments checked in audit during 2018-19 was 5.57 *per cent* which was lower than the corresponding figure (5.67 *per cent*) during 2017-18. As the extent of examination by audit was limited to 69.46 *per cent* of non-corporate scrutiny assessments completed by AOs, Ministry may consider reviewing the cases 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.

**4.1.2** A total of 77 high value income tax cases were referred to the Ministry during July 2019 to November 2019. Of these, 76 cases involve undercharge of ₹ 167.04 crore and one case involves overcharge of ₹ 3.32 crore. These cases of incorrect assessment point towards weaknesses in the internal controls on the assessment process being exercised by the Income Tax Department. Such errors have been continually pointed out in earlier audit reports as well. ITD may ascertain whether the instances of irregularities noticed are errors of omission or commission while ensuring necessary action as per law in cases involving errors of commission.

**4.1.3** The categories of 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.

Table 2.10 (para 2.4.4) of this report shows the details of broad categories of errors in assessments and their tax effect.

**4.1.4** The Ministry has conveyed its acceptance in 14 cases involving tax effect (TE) of ₹ 11.85 crore. The Ministry has not accepted two cases involving tax effect of ₹ 1.53 crore. In the remaining 61 cases, the ITD has accepted

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62 Source: Central Board of Direct Taxes (CBDT)

17 cases involving tax effect of ₹ 71.28 crore (referred to in para 2.4.4 of this report). Out of 77 cases, ITD has completed remedial action in 48 cases involving tax effect of ₹ 83.88 crore and initiated remedial action in 12 cases involving tax effect of ₹ 53.50 crore.

## 4.2 Quality of assessments

**4.2.1** 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 4.1 shows the sub-categories of errors which impacted the quality of assessments.

Table 4.1: Details of errors in quality of assessment				(₹ in crore)
Sub-categories	Cases	TE	States	
a. Arithmetical errors in computation of income and tax	3	1.94	Maharashtra and Uttar Pradesh	
b. Incorrect application of rates of tax, surcharge etc.	23	16.23	Andhra Pradesh & Telangana, Assam, Chattisgarh, Gujarat, Haryana, Jharkhand, Maharashtra, Tamil Nadu, UT Chandigarh, Uttar Pradesh and West Bengal	
c. Errors in levy of interest	2	0.77	Punjab and Tamil Nadu	
d. Excess or Irregular refunds/ Interest on refunds	1	0.11	Madhya Pradesh	
<b>Total</b>	<b>29</b>	<b>19.05</b>		

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

We noticed arithmetical errors in computation of income and tax in three cases involving tax effect of ₹ 1.94 crore in two states.

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

We give below two such illustrative cases:

**4.2.2.1** In Uttar Pradesh, CIT Exemption Lucknow charge, AO completed the assessment of an Association of Person (AOP) for AY 2015-16 after scrutiny in December 2017 at an income of ₹ 99.22 lakh. Audit examination revealed that the AO had disallowed an amount of ₹ 39.44 lakh on account of addition of fixed asset. However, the said amount of ₹ 39.44 lakh was not added back to the income of the assessee while computing the taxable income. This error had resulted in short levy of tax of ₹ 22.65 lakh including interest. *The ITD rectified the error under section 154 of the Act (December 2018).*

**4.2.2.2** In Maharashtra, PCIT 19 Mumbai charge, AO completed the assessment of an individual for AY 2009-10 under section 144 read with section 147 in March 2015 determining income at ₹ 91.80 lakh which was revised to ₹ 2.87 crore in December 2016. Audit examination revealed that while computing revised assessed income, the addition was made to the returned income of the assessee of ₹ 3.13 lakh instead of originally assessed income of ₹ 91.80 lakh. Thus, incorrect adoption of figure resulted in underassessment of ₹ 88.67 lakh involving short levy of tax of ₹ 39.18 lakh including interest. *The Ministry accepted the audit observation (January 2020) and took remedial action (October 2019) under section 154 of the Act.*

#### **4.2.3 Application of incorrect rates of tax and surcharge**

We noticed application of incorrect rates of tax and surcharge in 23 cases involving tax effect of ₹ 16.23 crore in 11 states.

*Section 115BBE(1) provides that where the total income of an assessee includes any income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D, the income-tax payable shall be aggregate of the amount of income-tax calculated on income referred to in section 68, section 69, section 69A, section 69B, section 69C or section 69D, at the rate of 30 per cent.*

We give below two such illustrative cases:

**4.2.3.1** In West Bengal, Pr. CIT-Central 1 Kolkata charge, AO completed the assessment of a HUF for AY 2015-16 under section 143(3) read with section 153C of the Act in December 2017 at an income of ₹ 5.90 crore. Audit examination revealed that AO had made an addition of ₹ 5.84 crore to the income of the assessee under section 68 and 69 of the Act, as such, the addition made under the said section should have been taxed at the rate of 30 per cent. However, AO treated the addition of ₹ 5.84 crore as long term capital gain and taxed accordingly. This error had resulted in short levy of tax of ₹ 87.93 lakh including interest. *The Ministry accepted the audit observation (December 2019) and took remedial action (April 2018) under section 154 of the Act.*

**4.2.3.2** In Gujarat, Pr.CIT-5 Ahmedabad charge, AO completed the assessment of an individual for AY 2013-14 under section 143(3) read with section 147 of the Act in December 2017 at an income of ₹ 5.66 crore. Audit examination revealed that AO had added back an amount of ₹ 5.66 crore to the income of the assessee on account of unexplained cash credit. However, tax on income was levied at the rate of 20 *per cent* instead of applicable rate of 30 *per cent*. This error had resulted in short levy of tax of ₹ 75.50 lakh including interest. *The Ministry accepted the audit observation (December 2019) and took remedial action (July 2018) under section 154 of the Act.*

*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.*

We give below three illustrative cases:

**4.2.3.3** In Tamil Nadu, CIT-1 Madurai charge, AO completed the assessment of an artificial juridical person for AY 2009-10 in February 2016 at an income of ₹ 117.45 crore. Subsequently, the assessment was revised in March 2017 to give effect to the appeal order, wherein the income was reduced to ₹ 83.74 crore. Audit examination revealed that, while giving effect to the appellate order, AO did not levy surcharge leviable at the rate of 10 *per cent* as per the relevant Finance Act provisions. The error had resulted in short levy of tax of ₹ 2.59 crore.

**4.2.3.4** In CIT Panchkula, Haryana charge, AO completed the assessment of a Trust for AY 2014-15 after scrutiny in December 2016 at an income of ₹ 40.76 crore, which was further assessed at ₹ 29.15 crore under section 154 in March 2017. Audit examination revealed that while calculating tax liability under section 154 of the Act, the AO had not charged surcharge leviable at 10 *per cent*. The error had resulted in short levy of tax of ₹ 1.20 crore including interest. *The Ministry accepted (December 2019) the audit observation and rectified the error (July 2018) under section 154 of the Act.*

**4.2.3.5** In Uttar Pradesh, Pr. CIT Kanpur charge, AO completed the scrutiny assessment of an AOP for AYs 2014-15 and 2015-16 in December 2016 at an income of ₹ 8.09 crore and ₹ 10.18 crore respectively. Audit examination revealed that the AO, while computing tax demand for the respective AYs, did not levy surcharge applicable at the rate of 10 *per cent*. This error had resulted in short levy of tax of ₹ 35.49 lakh including interest for both the AYs. *The ITD rectified the error under section 154 of the Act (February 2019).*

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

**4.3.1** The Income Tax Act, 1961 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 ineligible beneficiaries. These cases point out weaknesses in the administration of tax concessions/deductions/exemptions on the part of ITD which need to be addressed. ITD may ascertain whether the instances of irregularities noticed are errors of omission or commission while ensuring necessary action as per law in cases involving errors of commission. Table 4.2 shows the sub-categories which have impacted the administration of tax concessions/exemptions/deductions.

Table 4.2: Sub-categories of errors under Administration of tax concessions/exemptions/deductions			(₹ in crore)		
Sub-categories	Nos.	TE	States		
a. Irregular exemptions/deductions/relief given to individuals	01	0.26	Delhi		
b. Irregular exemptions/deductions/relief given to Trusts/Firms/Societies/AOPs	05	18.73	Gujarat, Madhya Pradesh, Maharashtra and Rajasthan		
c. Incorrect allowance of Business Expenditure	10	81.43	Andhra Pradesh & Telangana, Delhi, Jharkhand, Maharashtra, Odisha, Uttar Pradesh, Uttarakhand and West Bengal		
d. Irregularities in allowing depreciation/business losses/capital losses	14	21.30	Andhra Pradesh & Telangana, Bihar, Delhi, Jharkhand, Kerala, Madhya Pradesh, Maharashtra, Punjab, Rajasthan and West Bengal		
<b>Total</b>	<b>30</b>	<b>121.72</b>			

#### 4.3.2 Irregular exemptions/deductions/relief given to Trusts/Firms/Societies/AOPs

We noticed irregular exemptions/deductions/relief given to trusts/firms/societies/AOPs in five cases involving tax effect of ₹ 18.73 crore in four states.

*The Income Tax Act, 1961 provides that AO is required to make a correct assessment of the total income or loss of the assessee and determine correct amount of tax or refund, as the case may be. Further, for the purposes of determining quantum of deduction under section 80-IA of the Act, the profits and gains of an eligible business shall be computed as if such eligible business was the only source of income of the assessee during the previous year.*

We give below one such illustrative case:

**4.3.2.1** In Rajasthan, Pr. CIT-I Jaipur charge, AO completed the assessment of a firm for AY 2015-16 after scrutiny in November 2017 at an income of ₹ 45.43 lakh after allowing deduction under section 80-IA of ₹ 41.14 lakh on profit from eligible business of 'Solar Energy Plant'. Audit examination revealed that the depreciation of ₹ 30.03 lakh pertaining to the 'Solar Energy

Plant' was debited to profits & gains of assessee's other business instead of profits & gains of eligible business of 'Solar Energy Plant'. This resulted in excess allowance of deduction under section 80-IA of ₹ 30.03 lakh involving short levy of tax of ₹ 11.58 lakh including interest.

#### **4.3.3 Incorrect allowance of Business Expenditure**

We noticed Incorrect allowance of Business Expenditure in 10 cases involving tax effect of ₹ 81.43 crore in eight states.

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

We give below one illustrative case:

**4.3.3.1** In Odisha, PCIT-II, Bhubaneswar charge, the assessment of an artificial juridical person for AY 2015-16 was completed after scrutiny in December 2017 determining loss at ₹ 165.90 crore. Audit examination revealed that liability of ₹ 269.39 crore towards "Employees benefit expenses" and "Interest on loan" for the previous year relevant to AY 2015-16 was payable on or before the due date of filing of return of income. However, as per the Auditor's Report (Form 3CD), the assessee had not paid the said liability on or before the due date of filing of return, which attracted the provisions of section 43B of the Act, and therefore the same was required to be disallowed. Non-disallowance of the unpaid liability had resulted in excess determination of loss to the extent of ₹ 112.20 crore, which resulted in potential tax effect of ₹ 38.14 crore. *The ITD accepted (November 2018) the audit observation and stated that remedial action under section 147/263 of the Act was being initiated.*

*Section 37 (1) of the Income Tax Act, 1961 provides that any expenditure not being in the nature of capital expenditure or personal expenses of the assessee, laid or expended wholly and exclusively for the purpose of the business or profession shall be allowed in computing the income chargeable under the head "profit and Gains of business or profession". Further, CBDT has clarified vide instruction number 17 of 2008 dated 26.11.2008 that section 37 of the Act envisages that an amount debited in the profit and loss account in respect of an accrued or ascertained liability only is an admissible deduction, while any provision in respect of any unascertained liability or a liability which has not accrued, do not qualify for deduction.*

We give below one illustrative case:

**4.3.3.2** In Maharashtra, Pr. CIT 2 Aurangabad charge, AO completed the scrutiny assessment of an AOP for AY 2013-14 in January 2016 determining total income at ₹ 7.01 crore. Audit examination revealed that the assessee had debited an amount of ₹ 34.94 crore to the Profit and Loss Account towards provision for overdue interest. As the said expenditure was merely a provision which was unascertained in nature and hence the same was required to be added back to the income of the assessee. The error had resulted in under

assessment of income of ₹ 34.94 crore involving short levy of tax of ₹ 14.47 crore including interest. *The ITD rectified the error (December 2018) under section 263 of the Act.*

*Section 40a(ii) of the Income Tax Act, 1961 provides that any sum paid on account of any rate or tax levied on the profits or gains of any business or profession shall not be deducted in computing the income chargeable under the head "Profits and gains of business or profession".*

We give below one illustrative case:

**4.3.3.3** In Maharashtra, Pr. CIT 1 Kolhapur charge, AO while completing assessment of an AOP for AY 2015-16 after scrutiny in December 2017 at an income of ₹ 56.47 crore, allowed expense of ₹ 4.01 crore towards income tax paid which was not an allowable expense as per the aforesaid provision of the Act. This error had resulted in under assessment of income of ₹ 4.01 crore involving short levy of tax of ₹ 1.81 crore including interest. *The Ministry accepted the audit observation (March 2020) and took remedial action (January 2019) under section 154 of the Act.*

#### **4.3.4 Irregularities in allowing depreciation/business losses/capital losses**

We noticed Irregularities in allowing depreciation/business losses/capital losses in 14 cases involving tax effect of ₹ 21.29 crore in 10 states.

*Under section 72 of the Income Tax Act, 1961, where for any assessment year, the net result of computation under the head 'Profits & Gains of Business or Profession' is a loss to the assessee, not being a loss sustained in a speculation business, and such loss cannot be wholly set off against income under any other head of income in accordance with the provisions of section 71, so much of the loss as has not been so set off or, where he has no income under any other head, the whole loss shall be carried forward to the following assessment year. 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:

**4.3.4.1** In West Bengal, Pr. CIT-4 charge, AO completed the assessment of an Individual for AY 2015-16 under section 144 of the Act in December 2017 at an income of ₹ 14.73 crore after allowing set-off of brought forward business loss of ₹ 4.74 crore. Audit examination revealed that brought forward business loss of ₹ 4.74 crore was inclusive of loss of ₹ 2.53 crore pertaining to AY 2011-12. However, for the AY 2011-12, assessee had a loss of ₹ 27.88 lakh only, and hence, excess set off of loss of ₹ 2.25 crore was allowed to the assessee. This irregularity had resulted in short levy of tax of ₹ 1.02 crore including interest.

**4.3.4.2** In Bihar, Pr. CIT Bhagalpur charge, AO completed the assessment of an AOP for AY 2013-14 after scrutiny in February 2016 at nil income after allowing set-off of losses of ₹ 15.45 crore relating to AY 2011-12. Audit examination revealed that return of income for AY 2011-12 was filed at a loss of ₹ 20.88 crore on 30 March 2012. As the return of income for the AY 2011-12 was filed after the due date<sup>63</sup> of filing of return of income under section 139(1), loss for the AY 2011-12 was not allowable to be carried forward and set-off in subsequent years. The error had resulted in short computation of income of ₹ 15.45 crore with consequent short levy of tax of ₹ 6.41 crore including interest. *The ITD accepted the audit observation (January 2018) and rectified the error under section 147 read with section 143(3) in November 2017.*

**4.3.4.3** In Rajasthan, Pr. CIT-1 Jaipur charge, AO completed the assessment of an Individual for AY 2010-11 under section 143(3) read with section 147 of the Act in December 2017 at an income of ₹ 2.32 lakh. Audit examination revealed that profit of ₹ 57.34 lakh was assessed as unaccounted income to be taxed under the head 'income from other sources' out of total business profit of ₹ 1.18 crore. Thus, only ₹ 60.88 lakh remained under the head profits and gains of business or profession against which brought forward business loss could be set off. However, the AO had allowed set off of brought forward business loss of ₹ 1.14 crore. This error had resulted in excess set-off of business loss of ₹ 53.49 lakh and under assessment of income by equal amount involving short levy of tax of ₹ 31.23 lakh including interest.

#### **4.4 Income escaping assessments due to errors**

**4.4.1** The Income Tax Act, 1961 provides that the total income of a person for any previous year shall include all incomes from whatever source derived, actually received or accrued or deemed to be received or accrued. We observed that the AOs did not assess/under assessed total income that was required to be offered to tax. Table 4.3 shows the sub-categories which have resulted in income escaping assessments.

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63 Due date for filing of return of income for AY 2011-12 was 30 September 2011.

Table 4.3: Sub-categories of errors under income escaping assessments due to errors				(₹ in crore)
Sub-categories	Nos.	TE	States	
a. Incorrect classification and computation of capital gains	06	1.93	Haryana, Himachal Pradesh, Madhya Pradesh, Maharashtra, Punjab and Rajasthan	
b. Incorrect computation of income	06	10.89	Maharashtra, Odisha, Rajasthan and Uttar Pradesh	
c. Income not assessed/under assessed under special provisions	02	1.27	Assam and Tamil Nadu	
d. Unexplained Investment/cash credit	03	12.18	Gujarat and Maharashtra	
<b>Total</b>	<b>17</b>	<b>26.27</b>		

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

We noticed Incorrect classification and computation of Capital Gains in six cases involving tax effect of ₹ 1.93 crore in six states.

*Under section 50C of the 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 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 illustrative case:

**4.4.2.1** In Rajasthan, Pr. CIT-1 Jaipur Charge, AO completed the scrutiny assessment of an individual for the AY 2015-16 at an income of ₹ 1.12 crore in December 2017. Audit examination revealed that the AO assessed long term capital gain of ₹ 1.02 crore on sale consideration received on sale of land of ₹ 1.23 crore (being one-fourth share of ₹ 4.92 crore). However, the value of land was assessed at ₹ 7.38 crore by sub-Registrar Amer, and thus, ₹ 7.38 crore was deemed to be the full value of the consideration for computing capital gain instead of ₹ 4.92 crore. Hence, long term capital gain was required to be computed at ₹ 1.85 crore (being one-fourth share of ₹ 7.38 crore). This error had resulted in short computation of capital gain of ₹ 61.50 lakh involving tax effect of ₹ 18.53 lakh including interest.

#### 4.4.3 Incorrect computation of income

We noticed Incorrect computation of income in six cases involving tax effect of ₹ 10.88 crore in four states.

*As per provision under section 143(3) of Income Tax Act, AOs are required to make correct assessment of income of the assessee and determine the correct amount payable by the assessee or refundable to the assessee as the case may be. The Board has also issued instructions to the AOs to ensure correct assessment of total income or loss of the assessee in a scrutiny assessment. Valuation of stock is a vital factor in determining the taxable income of an assessee from business as correct profits cannot be ascertained unless the opening and closing stock are valued correctly. Though the valuation of stock does not generate funds, it does affect taxable income of the business. It was judicially held by Apex Court that closing stock must be valued correctly for ascertainment of true trading results [A.L.A. firm v. CIT [1991] 189 ITR 285(SC)]. Further, it was also held in case of CIT v. British Paints India Ltd.[1991] 188 ITR 44(SC) that incorrect valuation of closing stock is likely to result in a distorted picture of the true state of the business for the purpose of computing the chargeable income. The profit of one year is likely to be shifted to another year which is an incorrect method of computing profits and gains for the purpose of assessment.*

We give below one illustrative case:

**4.4.3.1** In Odisha, PCIT-I Bhubaneswar charge, AO completed the assessment of a firm for AY 2014-15 after scrutiny in November 2017 determining total income at ₹ 17.80 crore. Audit examination of statutory return vis-à-vis quantitative details furnished in auditors report (form 3CD) revealed that the quantity of closing stock of iron ore was 82,888.29 MT, the value of which furnished by assessee through annual mining return (i.e. Form H-1) was computed at ₹ 18.81 crore. However, the assessee in its Profit & Loss Account as well as in the Balance Sheet for the year ending 31<sup>st</sup> March 2015 had disclosed the value of closing stock at ₹ 1.88 crore instead of ₹ 18.81 crore resulting in under valuation of closing stock to the extent of ₹ 16.93 crore (₹ 18.81 crore – ₹ 1.88 crore) involving tax effect of ₹ 7.69 crore. *The ITD replied (August 2018) that remedial action had been taken. However, copy of rectification order was not made available to audit.*

#### 4.4.4 Income not assessed under special provisions

We noticed Income not assessed under special provisions in two cases involving tax effect of ₹ 1.26 crore in two states.

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

We give below one illustrative case:

**4.4.4.1** In Tamil Nadu, PCIT-1, Chennai charge, AO completed the scrutiny assessment of a firm for AY 2014-15 in December 2016 at 'nil' income under normal provisions, after setting off of the brought forward losses. Audit noticed that alternate minimum tax on the total income as per section 115JC of the Act should have been levied as tax on regular assessment which was nil. The error had resulted in non-levy of tax under section 115JC of ₹ 1.15 crore. *The ITD rectified the error under section 263 of the Act (April 2019).*

#### 4.4.5 Unexplained Investment/cash credit

We noticed errors related to unexplained Investment/cash credit in three cases involving tax effect of ₹ 12.18 crore in two states.

*Section 68 of the Income Tax Act, 1961 provides that where any sum is found credited in the books of an assessee maintained for any previous year, and the assessee offers no explanation about the nature and source thereof or the explanation offered by him is not, in the opinion of the AO, satisfactory, the sum so credited may be charged to income-tax as the income of the assessee of that previous year.*

We give below one illustrative case:

**4.4.5.1** In Gujarat, Pr. CIT-I Ahmedabad Charge, AO completed the assessment of an Individual for AY 2015-16 under section 144 read with section 143(3) in December 2017 at an income of ₹ 29.79 crore. Audit examination revealed that AO had disallowed ₹ 29.76 crore on account of unexplained cash deposit under section 68 of the Act and added this amount to the income of the assessee. However, as per bank statement of the assessee, there was cash deposit of ₹ 30.88 crore which remained unexplained. Thus, instead of ₹ 29.76 crore, cash deposit of ₹ 30.88 crore was required to be disallowed under section 68 of the Act. This error had resulted in under assessment of income of ₹ 1.12 crore involving tax effect of ₹ 55.91 lakh including interest. *The ITD rectified the error under section 154 of the Act (May 2018).*

#### **4.5 Conclusion and Recommendation**

- (i) Assessing Officers (AOs) committed errors in the assessments ignoring clear provisions of the Act. The cases of incorrect assessments involving arithmetical errors in computation of income and tax are difficult to accept as mere errors, in the days of calculators and computers. Further, application of incorrect rates of tax and surcharge, errors in levy of interest, excess or irregular refunds etc. point to either incompetence, or mischief, as well as weaknesses in the internal controls in ITD which need to be addressed. The existing scrutiny assessment procedure is opaque.
- (ii) While the Ministry has taken action to initiate correction in these cases, it may be pointed out that these are only a few illustrative cases. In the entire universe of all assessments, including non-scrutiny assessments, there is every likelihood of such errors, of omission or commission, in many more cases. The CBDT not only needs to revisit its assessments, but also put in place a fool proof IT system and internal control mechanism to eradicate, so-called “errors”.
- (iii) In view of repetitive nature of the errors, ITD should take remedial steps to prevent recurrence.
- (iv) *The CBDT may examine whether the instances of “errors” noticed are errors of omission or commission and if these are errors of commission, then ITD should ensure necessary action as per law.*

## **Chapter V: Interest under sections 234A, 234B, 234C, and 244A of the Act**

### **5.1 Introduction**

Sections 234A, 234B and 234C of the Income Tax Act (hereinafter referred to as 'Act'), 1961 provide for levy of interest for errors on part of the assessee at the rates prescribed by the Government from time to time. Further, section 244A of the Act provides for payment of interest if there is a delay in the payment of refund due to the assessee.

Assessment Information System (AST), a software module of the Income Tax Department (ITD), inter alia, undertakes the functions of calculation of tax and calculation of interest under various sections of the Act. It is designed to automatically take details of prepaid taxes i.e. advance tax and self-assessment tax from Individual Running Ledger Account (IRLA)<sup>64</sup> of the assessee in order to determine the amount payable by him or refund of any amount due to him. The AST module, however, allows the Assessing Officer (AO) to modify the value of interest under sections 234A, 234B, 234C and 244A of the Act under the head 'Modified'.

ITD, in 2017, by way of re-writing the business processes of the AST and other modules of the ITD, adopted Income Tax Business Application (ITBA) module for electronic conduct of proceedings/assessments that would eliminate human intervention in respect of modification of interests under sections 234A, 234B, 234C and 244A of the Act.

### **5.2 Why we chose this topic**

The reasons for selecting this topic were as under:

- (a) During the earlier compliance audit, we noticed that though system (AST) had calculated correct amount of interest under various sections of the Act, the same was manually modified by Assessing Officers (AOs) to increase or decrease the chargeable interest.
- (b) We also noticed that AOs had blocked the refund by way of modification in system (AST) which involved overcharge of interest.
- (c) We received a communication from Central Vigilance Commission (CVC) sharing similar information as stated above that the AOs were blocking refunds to the assesseees by applying manual intervention in the system.

We, therefore, decided to cover the above aspects in a more comprehensive way through this Audit.

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<sup>64</sup> IRLA system has been developed to keep a record of all the demands raised and collections made by an Assessing Officer (AO) in a consolidated manner, and in a single location.

### 5.3 Audit objective

The objective of the Audit was to ascertain whether a system for calculating correct amount of interest arising due to-default in furnishing return of income, default/deferment in payment of advance tax and delay in payment of refund due to the assessee was in place.

Sub-objectives to achieve the above objective are:

1. Whether system calculated interest manually modified by the AOs was in accordance with the provisions of the Act? (SO-1)
2. Whether system calculated interest was modified manually by the AOs to block the refund payable to the assessee? (SO-2)
3. Whether after implementation of ITBA, calculation of interest was being done through system correctly and there was no manual intervention? (SO-3)

### 5.4 Legal frame work

Brief of provision of sections 234A, 234B, 234C and 244A of the Act prescribed in the Act is given below:

Section	Brief of provision
Section 234A	Section 234A of the Act provides for levy of interest on account of default in furnishing return of income at specified rates and for specified time period.
Section 234B	Section 234B of the Act provides for levy of interest on account of default in payment of advance tax at specified rates and for specified time period.
Section 234C	Section 234C of the Act provides for levy of interest on account of default in payment of instalments of advance tax at specified rates and for specified time period.
Section 244A	Section 244A of the Act provides for payment of interest on refunds arising due to excess payment of advance tax, Tax Deducted at Source (TDS) or Tax Collected at Source (TCS) at specified rates and for specified time period.

Details of legal provisions relating to the interest under sections 234A, 234B, 234C and 244A of the Act are given in *Appendix-5.1*.

### 5.5 Audit coverage

The audit covered the sample of cases where interest under sections 234A, 234B, 234C, and 244A of the Act were modified during processing in AST and orders passed in FY 2016-17 and FY 2017-18. For FY 2018-19, audit covered the cases<sup>65</sup> that were processed/completed in ITBA for examination in the context of calculation of interest under sections 234A, 234B, 234C and 244A of the Act.

<sup>65</sup> The cases selected for sample for FY 2016-17 and FY 2017-18 was further extended for FY 2018-19, that was processed/completed in ITBA in FY 2018-19

## 5.6 Sample size

ITD furnished assessee-wise data on interest under sections 234A, 234B, 234C and 244A of the Act modified by AOs during processing in AST in FY 2016-17 and FY 2017-18 which comprised 8,35,727 records. Out of 8,35,727 records, 6,544 assessment cases were selected as sample for audit after risk analysis. Further, 496 assessment cases were added to the sample that were processed/completed in ITBA in FY 2018-19. Thus, total 7,040 cases<sup>66</sup> were selected as sample for audit. State wise details of sample selected for audit is given in *Appendix-5.2*.

Besides 7,040 sample cases selected for audit, we also included 134 high value cases where we found observation on interest under sections 234A, 234B and 234C of the Act during our regular compliance audit conducted for the period 2018-19.

## 5.7 Non production of records

Out of the 7,040 cases requisitioned, 6,713 cases (6,217 cases<sup>67</sup> + 496 cases<sup>68</sup>) were produced to Audit. Records not furnished comprised 4.64 *per cent* of the requisitioned records. The non-production of the records was a constraint in complete coverage of the selected sample. Reasons furnished by ITD for non-production of records were, records lying with CIT (Exemption), prosecution council, vigilance, appeal and records not readily available.

## 5.8 Audit findings

Of the 6,217 cases (AST cases processed/completed in FY 2016-17 and FY 2017-18), checked by audit we found instances of systemic issues viz. deficiency noticed in AST system in calculating the correct amount of interest and absence of proper checks in the AST system to shield manual intervention. We also found instances concerning compliance issues where AOs did not modify the system calculated incorrect interest or if modified, modified it incorrectly. On the other hand, AO modified the system calculated correct interest which lead to short/excess levy of interest. Instances were also noticed where AO blocked the refund due to the assessee's by modifying the interest component causing undue hardship and harassment to the assessee. We noticed 7,385<sup>69</sup> observations under sections 234A, 234B, 234C and 244A of the Act in respect of 4,767 assessment cases<sup>70</sup> involving tax effect of

66 7,040 cases comprise 4,810 unique assesseees

67 For FY 2016-17 and FY 2017-18 processed/completed through AST; 6,217 cases comprise 4,551 unique assesseees

68 For FY 2018-19 processed/completed through ITBA; 496 cases comprise 354 unique assesseees

69 Overall tax effect with respect to 7,385 cases is ₹ 20,51,183.77 lakh; however, 7,385 includes 958 cases pertaining to same assessee for same AY but assessed separately, thus the effective tax effect is ₹ 19,09,054.91 lakh

70 7,385 instances pertaining to 4,767 assessments cases comprising 3,486 unique assessee

₹ 19,09,054.91 lakh<sup>71</sup> and blockade of refund/avoidable payment of interest amounting to ₹ 4,39,571.21 lakh/₹ 5,274.59 lakh. We also noticed systemic issues where wrong amount of interest was calculated through AST system in 1,400 cases, 1,744 cases, 1,900 cases and 1,585 cases with respect to interest under sections 234A, 234B, 234C and 244A of the Act respectively.

In addition, we noticed instances of incorrect calculation of interest through Income Tax Business Application (ITBA), which was adopted after re-writing the business process of AST in 2017. We also found errors in calculation of interest under sections 234A, 234B and 234C of the Act during our regular compliance audit conducted for the period 2018-19. Of the 496 cases that were processed/completed through ITBA in FY 2018-19, in 32 cases, we found that the interest was wrongly calculated involving a tax effect of ₹ 2,297.95 lakh<sup>72</sup>.

During our regular compliance audit conducted for the period 2018-19, we found 134 cases involving tax effect of ₹ 1,10,269.82 lakh<sup>73</sup> related to errors in calculation of interest under sections 234A, 234B and 234C of the Act.

Findings in respect of 6,217 audited cases (AST cases processed/completed in FY 2016-17 and FY 2017-18), have been discussed from **para 5.8.1 to para 5.8.4** of this report. Further, findings in respect of ITBA cases have been discussed in **para 5.8.5** and findings of cases noticed during our regular compliance audit have been discussed in **para 5.8.6** of this report.

We referred this report to the Ministry of Finance in April 2020 for its comments. Response of the Ministry was awaited (June 2020).

### **5.8.1 Incorrect calculation of interest through System (AST)**

All Income Tax Returns (ITRs) are first summarily processed under section 143(1) at Centralized Processing Centre (CPC), Bengaluru before scrutiny assessments, thus all data pertaining to summary assessments are directly captured in AST. The work of processing, rectification, completion of assessment order in respect of scrutiny cases is done by AOs in AST module, part of ITD module, for all returns transferred from CPC. AST, inter alia, undertakes assessment functions of calculation of tax and calculation of interest under various sections of the Act. In the case of scrutiny assessment,

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71 Short levy of interest amounting to ₹ 1,46,462.46 lakh and excess levy of interest amounting to ₹ 14,46,070.93 lakh under sections 234A, 234B and 234C; short payment of interest amounting to ₹ 1,11,141.46 lakh and excess payment of interest amounting to ₹ 205380.06 lakh under section 244A

72 Short levy of interest amounting to ₹ 284.29 lakh and excess levy of interest amounting to ₹ 1,635.24 lakh under sections 234A, 234B and 234C; short payment of interest amounting to ₹ 370.91 lakh and excess payment of interest amounting to ₹ 7.52 lakh under section 244A

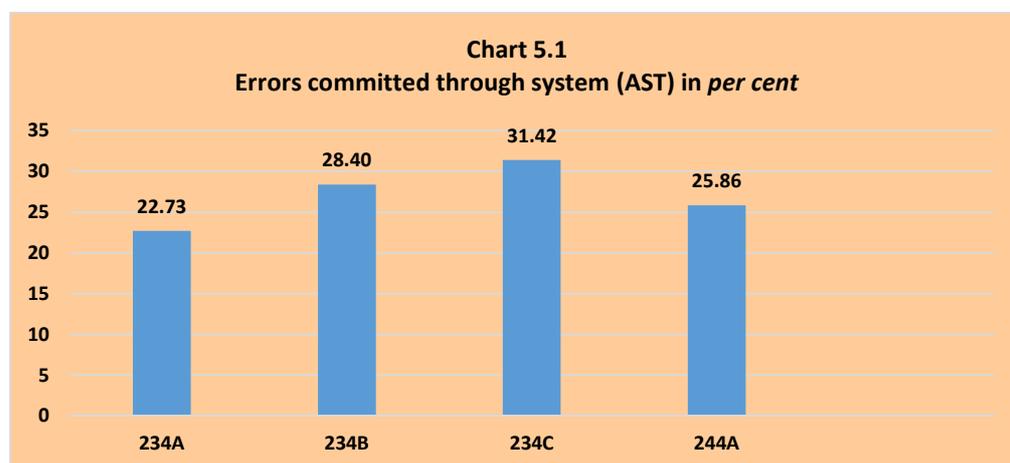
73 Short levy of interest amounting to ₹ 65,796.38 lakh and excess levy of interest amounting to ₹ 44,473.44 lakh under sections 234A, 234B and 234C

rectification, appeal effect orders in the field offices, figures are data-fed to the system by AOs based on the orders. With the new figures entered into different heads of income under additions, computation sheet for final demand is generated.

We examined calculation of interest, under sections 234A, 234B, 234C and 244A of the Act, done through AST system. In 1,400 cases, 1,744 cases, 1,900 cases and 1,585 cases with respect to interest under sections 234A, 234B, 234C and 244A of the Act respectively<sup>74</sup>, it was found that wrong amount of interest was calculated through system. Details of incorrect amount of interest calculated through system is shown in the Table 5.1 below:

Table 5.1: Incorrect amount of interest calculated through system (₹ in lakh)				
	Short calculation		Excess calculation	
	Number of cases	Amount	Number of cases	Amount
Interest under section 234A	419	12,561.10	981	58,306.18
Interest under section 234B	593	1,72,452.05	1,151	5,85,792.92
Interest under section 234C	696	24,640.48	1,204	1,43,547.74
Interest under section 244A	1,103	2,09,880.50	482	1,50,138.59

Trend of error committed through system (in *per cent*)<sup>75</sup> in calculating interest is shown in chart below:



Thus, percentage of error committed through system in calculating interest was significantly high with respect to sections 234C and 234B of the Act which was more than 31 *per cent* and 28 *per cent*, respectively, of the total cases.

74 We noticed errors in levy of interest in 2,921 cases under one section, 831 cases under two sections, 524 cases under three sections and 108 cases under all four sections (234A/234B/234C/244A).

75 1,400 cases out of 6,160 cases for section 234A; 1,744 cases out of 6,140 cases for section 234B; 1,900 cases out of 6,048 cases for section 234C and 1,585 cases out of 6,129 cases for section 244A

We noticed that 774 cases were processed under section 143(1) of the Act (summary assessment) and 5855 were assessed under other sections of the Act<sup>76</sup> (non-summary assessments). The percentage of errors committed through system in cases processed under section 143(1) of the Act, were 27.71 per cent<sup>77</sup>, 6.59 per cent<sup>78</sup>, 3.58 per cent<sup>79</sup> and 12.81 per cent<sup>80</sup> in respect of interest levied under section 234A, 234B, 234C and 244A, respectively. As the processing of ITRs was automated and was centrally done through CPC Bengaluru, the probability of occurrence of errors in levy of interest through AST systems should be 'nil' in such cases.

We further segregated the interest calculated incorrectly through the system, PAN category wise and compared it with total audited cases<sup>81</sup> (which was also segregated PAN category wise). Details of percentage of error in interest calculated through system with respect to total audited cases, PAN category wise, is shown in Table 5.2 below:

Type of Assessee	No. of cases where incorrect interest under section 234A was calculated through the system	Percentage of incorrect interest under section 234A through the system to total audited cases	No. of cases where incorrect interest under section 234B was calculated through the system	Percentage of incorrect interest under section 234B through the system to total audited cases	No. of cases where incorrect interest under section 234C was calculated through the system	Percentage of incorrect interest under section 234C through the system to total audited cases	No. of cases where incorrect interest under section 244A was calculated through the system	Percentage of incorrect interest under section 244A through the system to total audited cases
1	2	3	4	5	6	7	8	9
AOP	17	0.28	21	0.34	40	0.66	33	0.54
BOI	6	0.10	4	0.07	8	0.13	11	0.18
Company	320	5.19	619	10.08	741	12.25	767	12.51
Firm	118	1.92	179	2.92	240	3.97	121	1.97
Govt. Authority							2	0.03
HUF	27	0.44	19	0.31	13	0.21	12	0.20
Artificial Juridical Person	3	0.05	4	0.07	4	0.07	3	0.05
Local Authority	2	0.03	6	0.10	3	0.05	7	0.11
Individual	894	14.51	883	14.38	800	13.23	597	9.74
Trust	13	0.21	9	0.15	51	0.84	32	0.52
<b>TOTAL</b>	<b>1,400</b>	<b>22.73</b>	<b>1,744</b>	<b>28.40</b>	<b>1,900</b>	<b>31.42</b>	<b>1,585</b>	<b>25.86</b>

76 Sections 144, 154, 155, 250, 254, 262, 263, 264, 143(3), 147, 153C, 153A and 260 A of the Income Tax Act, 1961.

77 388 cases out of 1,400 cases

78 115 cases out of 1,744 cases

79 68 cases out of 1,900 cases

80 203 cases out of 1,585 cases

81 Of the 6,217 audited cases, audit could get the required information/document from the ITD for ascertaining the amount of interest in 6,160 cases, 6,140 cases, 6,048 cases and 6,129 cases under sections 234A, 234B, 234C and 244A respectively. Therefore, audit could ascertain the amount of interest under sections 234A, 234B, 234C and 244A in 6,160 cases, 6,140 cases, 6,048 cases and 6,129 cases respectively

From the above, it can be seen that for calculating interest, the error in respect of individual assessee was on the higher side. The scale of error is significant as the individual assessee constitute more than 90 *per cent* of total taxpayers. We further segregated the number of cases in respect of individual assessee where interest was short/excess levied through the system, which is shown in the Table 5.3 below:

Table 5.3: Incorrect interest calculated through the system, pertaining to individual assesseees						
Section	Total no. of Cases (individual assessee where interest was calculated through the system)	Short levy of interest (no. of cases)	Excess levy of interest (no. of cases)	% of no. of excess levy to no. of individual cases where wrong interest was calculated through the system		
1	2	3	4	5		
234A	894	275	619	69.24		
234B	883	315	567	64.29		
234C	800	210	590	73.75		
<b>Total</b>	<b>2,577</b>	<b>800</b>	<b>1,776</b>	<b>68.92</b>		

Thus, 68.92 *per cent* of cases with respect to individual assesseees were levied interest at excess amount through the system. Amount of excess levy of interest was charged against the individual assessee upto ₹ 803.35 lakh under section 234A of the Act, ₹ 2,728.31 lakh under section 234B of the Act and ₹ 559.59 lakh under section 234C of the Act, causing unnecessary harassment and hardship to the assessee.

We further examined the reason behind the incorrect calculation of interest through AST system and explanation from the ITD was sought in this regard. Though the ITD furnished the reply in 1,851 cases<sup>82</sup>, the reply was not specific to root cause of the deficiency in system and was only general in nature. One of the major reasons furnished by ITD was that the interest was wrongly calculated due to system error.

However, during the course of the audit, on comparison of the ITR, assessment order and the figures available in AST system, we found that:

- ❖ Of the 1,400 cases with respect to incorrect interest calculated through the system, under section 234A of the Act, system did not capture the tax amount/advance tax/TDS/TCS in 125 cases. Further, in 461 cases, system failed to compute the correct period of delay in filing of return. In 115 cases, though the system captured the tax component and period of delay of filing of return correctly, amount

82 Reply furnished in respect of 362 cases against 234A, 378 cases against 234B, 399 cases against 234C and 712 cases against 244A

of interest under section 234A of the Act was calculated through the system incorrectly.

Further analysis of 476 cases pertaining to capturing of incorrect period of delay through the system, revealed that period of delay reckoned through the system less than actual was ranging from one month to more than 36 months in 339 cases and period of delay reckoned through the system more than actual was ranging from one month to more than 36 months in 137 cases. Details are as follows:

<b>Table 5.4: Period of delay reckoned less/more than actual through system resulting in incorrect calculation of interest under section 234A of the Act</b>			
<b>Range of delay</b>	<b>No. of cases (period of delay reckoned less than actual)</b>	<b>No. of cases (period of delay reckoned more than actual)</b>	<b>Total no. of cases</b>
<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>
≤12 months	263	79	342
>12 months and ≤24 months	50	18	68
>24 months and ≤36 months	3	7	10
More than 36 months	23	33	56
<b>Total</b>	<b>339</b>	<b>137</b>	<b>476</b>

As such, in 134 cases out of 476 cases (constituting 28.15 per cent), system calculated incorrect amount of interest by capturing the period with a difference of more than 12 months and thus levied short/excess amount of interest for significant amount.

- ❖ With respect to section 234B of the Act, out of the 1,744 cases, system failed to capture the tax amount/TDS/TCS/SAT in 364 cases. In 130 cases, the system failed to capture the period of default correctly. Further, in 304 cases, though the system captured the tax component and period of default correctly, amount of interest under section 234B of the Act was calculated through system incorrectly.
- ❖ Of the 1,900 cases with respect to incorrect interest under section 234C of the Act, calculated through the system, the system did not capture the tax amount in 409 cases. Further, in 212 cases, system failed to capture the correct period of deferment of tax. We also found in 253 cases, where the system captured the tax component and period of interest payable, however, amount of interest under section 234C of the Act was calculated through system, incorrectly.
- ❖ Of the 1,585 cases with respect to incorrect interest under section 244A of the Act calculated through the system, the system failed to capture the tax amount/advance tax/TDS/TCS in 203 cases. We also found in 66 cases, where the system captured the tax component and period for which the interest was payable to assessee correctly,

however, amount of interest under section 244A was calculated through system, incorrectly. We also found 60 cases pertaining to period for which granting of refund due to assessee was delayed.

Thus, from the above, it can be seen that system failed to capture tax amount/TDS/TCS vis-à-vis period of delay/default which resulted in incorrect calculation of interest under sections 234A, 234B, 234C and 244A. As the AST system was designed to automatically take details of advance tax/TDS/TCS from other modules of IT Application, non-capture of such details indicates deficiency in the system. Further, where such details were captured correctly, incorrect interest was calculated through the system. This had an impact on final demand/refund due to the assessee.

In our earlier Performance Audit Report on 'IT Applications in Income Tax Department'<sup>83</sup>, we had highlighted the shortcoming in AST module and had recommended that 'Ministry may strengthen IT systems and iron out the incongruence between critical IT modules so that intended results are delivered'. The ministry had submitted to the Public Accounts Committee (PAC) that "the Department has started the process of re-writing the business processes of the AST and other modules of the Income Tax Department and bringing them under one common architecture through a project called the Income Tax Business Application"<sup>84</sup>. However, the fact remains that the AST was in operation till 2017-18 and the department did not ensure that the existing deficiencies were addressed for the assessments during these years, before they implemented ITBA. Further, even in ITBA, there have been instances of incorrect calculation of interest as brought out in para 5.8.5 of this report.

### **5.8.2 Failure of AOs in rectifying the incorrect interest calculated through the system**

AST module allows the AOs to modify the value of interest under sections 234A, 234B, 234C and 244A of the Act under the head 'Modified' wherein the value of interest can be changed (increased/ decreased) and calculation is done in accordance with the provisions of the Act. We found cases where the AOs did not utilise the 'modified' feature of the AST to rectify the incorrect calculation of interest through the system. Further, we also found other cases where the AOs misused the modification feature to levy wrong amount of interest. The number of such cases have been shown in Table 5.5 below:

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83 Report No. 23 of 2012-13, for the year ended March 2012; report tabled on the floor of the Parliament on 30 April 2013

84 The second report of the PAC 2014-15 (Sixteenth Lok Sabha) on IT Applications in IT Department, submitted to Lok Sabha and Rajya Sabha on 25-11-2014.

Table 5.5: Incorrect interest calculated through the system either not modified or modified incorrectly by AOs					
Interest under section	Incorrect interest calculated through the system (no. of cases)	Modified correctly by AOs out of column 2 (no. of cases)	Not modified by AOs out of column 2 though were incorrect (no. of cases)	Modified at incorrect amount by AOs out of column 2 (no. of cases)	
1	2	3	4	5	
234A	1,400	665	258	477	
234B	1,744	822	265	657	
234C	1,900	1,001	360	539	
244A	1,585	426	588	571	
<b>Total</b>	<b>6,629</b>	<b>2,914</b>	<b>1,471</b>	<b>2,244</b>	

It can be seen that the AOs modified the incorrect computation through the system in 5,158 (2,914+2,244) cases. However, more than 43 *per cent* of these modifications by the AOs were incorrect. Further, AOs did not correct 1,471 cases. Audit findings with respect to column 4 and column 5 of Table 5.5 above are discussed in the succeeding paragraphs.

#### 5.8.2.1 AOs did not use modification feature to correct the incorrect interest through the system

Audit examined the cases where the **incorrect interest** was calculated through the system (as discussed in para 5.8.1) to see whether AOs had taken corrective measures against such cases and modified it correctly. However, audit found in 1,471 cases where AOs did not take any action on incorrect interest, calculated through the system, to rectify it. Further details of 1,471 cases are shown in **Table 5.6** (cases related to short levy/payment of interest) and **Table 5.7** (cases related to excess levy/payment of interest) as below:

Table 5.6: Short levy/payment of interest where AOs did not modify the incorrect interest calculated through the system				
Interest under section	Number of cases where AOs did not modify the incorrect interest calculated through the system	Short levy/ payment <sup>85</sup> of interest (no. of cases)	Short levy/ payment of interest (amount ₹ in lakh)	
1	2	3	4	
234A	258	57	292.37 <sup>86</sup>	
234B	265	100	18,805.95	
234C	360	124	2,365.45	
244A	588	500	53,251.90	
<b>Total</b>	<b>1,471</b>	<b>781</b>	<b>74,715.67</b>	

85 Levy in respect of interest under sections 234A, 234B and 234C; payment in respect of interest under section 244A

86 Actual Money Value involved is ₹ 282.70 lakh as the two assesseees were assessed for same AYs passed under different assessment orders

Thus, failure of AOs to take the corrective action against incorrect interest calculated through the system had resulted in short levy of interest leading to undue benefit and potential gain to assessee as well as loss of revenue. Further, short payment of interest under section 244A of the Act had resulted in avoidable hardship and harassment to the assessee. One instance of short levy of interest is given below:

**(a) Charge: Pr. CIT-Central-3, Kolkata, West Bengal; AY 2010-11**

The AO assessed the income of the assessee company under section 144/147 of the Act in December 2017 at income of ₹ 126.93 lakh. Audit noticed that instead of calculating correct amount of interest under section 234B of the Act at ₹ 26.87 lakh, interest was calculated through the system under the said section at ₹ 19.52 lakh. Audit further noticed that AO did not modify the incorrect interest to rectify it, which resulted in short levy of interest of ₹ 7.35 lakh. *ITD replied (October 2019) that error in computation of interest under section 234B was due to some technical error in the system and the same was corrected as per provisions of the Act.*

We also found cases where, inaction on part of the AOs against incorrect interest calculated through the system, resulted in excess levy of interest having potential impact on withholding of refund/ excess payment out of exchequer in the form of interest on refund, apart from undue hardships/ harassment of assessee. Excess payment of interest under section 244A of the Act had resulted in loss of revenue. Section wise details of such cases have been shown in the Table 5.7 given below:

Table 5.7: Excess levy/payment of interest where AOs did not modify the incorrect interest calculated through the system				
Interest under section	Number of cases where AO did not modify the incorrect interest calculated through the system	Excess payment of interest (no. of cases)	Excess levy/ payment of interest (amount ₹ in lakh)	
1	2	3	4	
234A		258	201	5,773.96
234B		265	165	70,992.96
234C		360	236	21,593.37
244A		588	88	8,654.45
<b>Total</b>		<b>1,471</b>	<b>690</b>	<b>1,07,014.74</b>

The issues related to AST system were highlighted in our earlier report<sup>87</sup> wherein the need for strengthening the IT system of the department was emphasised. Thus, AOs should have re-verified the interest and tax calculated through the system, as the shortcomings in system were known to the department. However, no action had been taken by the AOs to rectify the

<sup>87</sup> Report No. 23 of 2012-13, for the year ended March 2012

incorrect interest calculated through the system leading to incorrect levy/payment of interest.

### 5.8.2.2 Errors in calculation of interest by AOs while rectifying incorrect interest calculated through the system using modification feature

Audit found in 2,244 cases where AOs used the modification feature to rectify the incorrect interest calculated through the system but modified it at incorrect amount of interest. Further details of 2,244 cases are shown in **Table 5.8** (cases related to short levy/payment of interest) and **Table 5.9** (cases related to excess levy/payment of interest) below:

<b>Table 5.8: Short levy/payment of interest where interest calculated through the system as well as by AOs was incorrect</b>				
<b>Interest under section</b>	<b>Number of cases where AO modified the interest amount incorrectly</b>	<b>Short levy/ payment of interest (no. of cases)</b>	<b>Amount of short levy/ payment of interest (amount ₹ in lakh)</b>	
<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	
234A	477	281	3,325.93	
234B	657	335	1,05,528.64	
234C	539	275	2,969.33	
244A	571	329	57,591.13	
<b>Total</b>	<b>2,244</b>	<b>1,220</b>	<b>1,69,415.03</b>	

Thus, failure of AOs in modifying the incorrect interest (as calculated through the system) at correct amount resulted in the short levy of interest leading to undue benefit and potential gain to assessee as well as loss to revenue. Further, short payment of interest under section had resulted in avoidable hardship and harassment to the assessee. Two instances where incorrect modification by AOs of incorrect interest calculated through the system led to short levy of interest are given below:

#### (a) Charge: Pr. CIT-Central-2, Kolkata, West Bengal; AY 2013-14

The case of the assessee company was processed under section 143(1) of the Act in August 2014 at income of ₹ 549.07 lakh and tax of ₹ 178.15 lakh thereon. The AO, further, assessed the income of the assessee under section 143(3)/153A of the Act in March 2016 at income of ₹ 1,768.55 lakh which was further rectified under section 154 of the Act in April 2016 at income of ₹ 1,675.92 lakh and tax of ₹ 543.75 lakh thereon. Audit noticed that the assessee, in response to notice under section 153A of the Act, filed its return of income after delay of six months. However, interest under section 234A of the Act was calculated through the system at ₹ 76.78 lakh instead of correct amount of ₹ 21.93 lakh<sup>88</sup>. The AO, further modified the interest amount at nil resulting in non levy of interest at ₹ 21.93 lakh. Reasons for carrying out the

88 Six per cent on enhanced tax of ₹ 365.60 (₹ 543.75-₹ 178.15)

incorrect modifications in AST system by the AOs could not be ascertained by audit, as there was no provision in the AST module to capture the reasons behind changes made by AOs.

**(b) Charge: Pr. CIT-IV, Pune, Maharashtra; AY 2010-11**

The assessment of the assessee company was rectified under section 154 of the Act in June 2016 at an income of ₹ 27,139.76 lakh. Audit noticed that the correct amount of interest of ₹ 336.59 lakh under section 234C of the Act was offered by assessee at the time of filing of return of income. However, interest of ₹ 347.21 lakh under the said section was calculated through the system against the correct amount of ₹ 336.59 lakh. The AO, further modified it to ₹ 186.42 lakh. The error had resulted in short levy of interest under section 234C of the Act of ₹ 150.17 lakh (₹ 336.59 lakh – ₹ 186.42 lakh) due to modification done by AO. Further, audit could not ascertain the reasons for carrying out the incorrect modifications in AST system by the AOs as there was no provision in the AST module to capture the reasons behind changes made by AOs.

Further, section wise details of **1,024 cases**, where AO's modification in incorrect interest calculated through the system led to excess levy/payment of interest is shown in Table 5.9 below:

Table 5.9: Excess levy/payment of interest where interest calculated through the system as well as by AOs was incorrect				
Interest under section	Number of cases where AO modified the amount incorrectly	Excess payment of interest (no. of cases)	levy/ payment of interest	Excess levy/ payment of interest (amount ₹ in lakh)
1	2	3	4	5
234A	477	196		9,357.25
234B	657	322		2,36,664.94
234C	539	264		1,27,682.28
244A	571	242		1,58,317.21
<b>Total</b>	<b>2,244</b>	<b>1,024</b>		<b>5,32,021.68</b>

Thus, AOs intervention, where the incorrect interest was computed through the system, led, to excess levy of interest having potential impact on withholding of refund/excess payment out of exchequer in the form of interest on refund, apart from undue hardships/ harassment of assessees in case of excess levy of interest. Further, excess payment of interest under section 244A of the Act had resulted in loss to revenue. One instance where interest calculated through the system as well as by the AO was incorrect leading to excess levy of interest is given below:

**(a) Charge: Pr. CIT-Central-I, Kolkata, West Bengal; AY 2010-11**

The AO assessed the income of the assessee company under section 143(3)/153A of the Act in December 2016 at nil income. As such, interest

under section 234B of the Act was not leviable since the assessed income was at nil amount. However, interest under section 234B of the Act was calculated through the system, amounting to ₹ 165.93 lakh resulting in overcharge of tax of ₹ 165.93 lakh. Further, the AO, instead of modifying the interest amount at zero, modified it at ₹ 768.15 lakh, as a result of which, over charge of interest amount was increased from ₹ 165.93 lakh to ₹ 768.15 lakh. Further, audit could not ascertain the reasons for carrying out the incorrect modifications in AST system by the AOs as there was no provision in the AST module to capture the reasons behind changes made by AOs.

### 5.8.3 Manual intervention and modification by AOs in correct interest calculated through the system

Where the correct amount of interest was calculated through the system, there was no scope for manual intervention and modification in the interest calculated through the system. However, we found instances where AOs manually modified the interest amount even though correct amount of interest was calculated through the system. Details of such cases have been shown in Table 5.10 below:

Table 5.10: Instances of modification by AOs in correct interest calculated through the system			
Interest under section	Correct interest calculated through the system (no. of cases)	Correct interest calculated through the system modified incorrectly by AOs (no. of cases)	
1	2	3	
234A	4,760	1,003	
234B	4,396	1,180	
234C	4,148	654	
244A	4,544	833	
<b>Total</b>	<b>17,848</b>	<b>3,670</b>	

5.8.3.1 Further, section wise details of cases, where AOs unwarranted modification in the **correct** interest calculated through the system led to **short levy/payment of interest** is shown in Table 5.11 below:

Table 5.11: Short levy/payment of interest with respect to cases where correct interest calculated by the system was modified incorrectly by AOs			
Interest under section	Modified incorrectly by AO (no. of cases)	Short levy/ payment of interest (no. of cases)	Short levy/ payment of interest (₹ in lakh)
1	2	3	4
234A	1,003	175	643.06
234B	1,180	105	36,160.06
234C	654	188	28,804.45
244A	833	134	1,303.15
<b>Total</b>	<b>3,670</b>	<b>602</b>	<b>66,910.72</b>

Thus, unwarranted modification by AOs in the correct interest calculated by the system resulted in short levy of interest leading to undue benefit and

potential gain to assessee as well as loss to revenue. Further, short payment of interest under section 244A of the Act had resulted in avoidable hardship and harassment to the assessee. One instance of short levy of tax is given below:

**(a) Charge: Pr. CIT-II, Kanpur, Uttar Pradesh; AY 2015-16**

The assessment of the assessee company was rectified under section 154 of the Act in March 2018 at an income of ₹ 60,577.02 lakh. It was noticed from the screen shot of the order that tax liability after giving credit to all pre-paid taxes was ₹ 20,590.44 lakh. As such, interest under section 234B of the Act amounting to ₹ 6,794.03 lakh was payable by the assessee which was calculated through the system at the correct amount. Though the correct amount of interest was calculated through the system, the AO manually modified the interest amount at nil, which resulted in short levy of interest of ₹ 6,794.03 lakh. *ITD replied (September 2019) that the error had been rectified.* However, ITD did not furnish any reason why the AO manually modified the correct interest calculated through the system.

Further, section wise details of cases where AOs unwarranted modification of the **correct** interest calculated through the system led to **excess levy/ payment of interest** are shown in Table 5.12 below:

<b>Table 5.12: Excess levy/payment of interest with respect to cases where correct interest calculated through the system was modified incorrectly by AO</b>				
<b>Interest under section</b>	<b>Modified by AO (no. of cases)</b>	<b>incorrectly</b>	<b>Excess levy/ payment of interest (no. of cases)</b>	<b>Excess levy/ payment of interest (amount ₹ in lakh)</b>
<b>1</b>	<b>2</b>		<b>3</b>	<b>4</b>
234A		1,003	828	1,25,694.69
234B		1,180	1,075	8,56,674.23
234C		654	466	77,158.39
244A		833	699	41,578.62
<b>Total</b>		<b>3,670</b>	<b>3,068</b>	<b>11,01,105.93</b>

Thus, AOs unwarranted intervention, where the correct interest was calculated through the system, led, to excess levy of interest having potential impact on withholding of refund/excess payment out of exchequer, apart from undue hardships/ harassment of assesseees in case of excess levy of interest. Excess payment of interest under section 244A of the Act had resulted in loss to revenue. One instance where AO modified the correct interest calculated through the system that led to excess levy of interest is given below:

**(a) Charge: Pr. CIT-II, Lucknow, Uttar Pradesh; AY 2015-16**

The AO assessed the income of an Individual in December 2016 after scrutiny at an income of ₹ 22,091.78 lakh. It was observed from the screen shot of the

order that interest under section 234A of the Act amounting to ₹ 525.49 lakh was payable by the assessee which was calculated through the system at correct amount. Though the correct amount of interest was calculated through the system, the AO manually modified this interest amount at ₹ 1,276.19 lakh resulting in excess levy of interest of ₹ 750.70 lakh. *ITD rectified the error under section 154 of the Act (January 2017)*. However, ITD did not furnish any reason why the AO manually modified the correct interest calculated through the system.

**5.8.3.2** It is seen further, from the **Table 5.11 and Table 5.12 above** that the number of cases where excess interest (**2,369 cases**) was levied by the AOs against correct interest calculated through the system was on much higher side as compared to number of cases where the interest was short levied (**468 cases**). We further analysed the number of cases vis-à-vis amount of excess levy of interest (**under sections 234A, 234B and 234C-column 3 and column 4 of Table 5.12 above**) and short payment of interest (**under section 244A-column 3 and column 4 of Table 5.11 above**) with respect to assessee's status. The details are shown in Table 5.13 below:

Table 5.13: Distribution of number of cases vis-à-vis amount of excess levy/ short payment of interest-status wise								
Status/ Particulars	Excess levy of interest under section 234A (No. of cases)	Excess levy of interest under section 234A (Amount- ₹ in lakh)	Excess levy of interest under section 234B (No. of cases)	Excess levy of interest under section 234B (Amount- ₹ in lakh)	Excess levy of interest under section 234C (No. of cases)	Excess levy of interest under section 234C (Amount - ₹ in lakh)	Short payment of interest under section 244A (No. of cases)	Short payment of interest under section 244A (Amount- ₹ in lakh)
1	2	3	4	5	6	7	8	9
AOP	25	4,695.44	13	1,767.20	6	1,177.35	1	0.04
Company	299	105,964.13	529	845,105.22	175	7,1043.83	10	1,272.67
Firm	85	3,308.38	73	4,732.94	41	1,209.61	6	0.29
Govt. Authority	1	0.11	2	10.00	1	7.07	3	3.96
HUF	8	0.57	7	7.40	4	0.02	2	0.14
AJP	2	162.1						
Local Authority	1	24.65	2	1,539.17	5	1,643.44		
Individual	390	6,101.14	445	2,598.66	229	283.49	107	25.95
Trust	17	5,438.17	4	913.64	5	1,793.58	5	0.10
<b>Total</b>	<b>828</b>	<b>125,694.69</b>	<b>1075</b>	<b>8,56,674.23</b>	<b>466</b>	<b>77,158.39</b>	<b>134</b>	<b>1,303.15</b>

It is seen that the maximum number of modifications were done in respect of individual cases followed by company assesseees. Excess levy of interest has the direct impact on refund, if the refund is due to assessee. Else, it creates undue demand on the assesseees. As such, by way of levy of excess interest, the assesseees were put to unnecessary harassment and undue hardship, as either refund was blocked due to excess levy of interest or undue demands were raised on the assesseees. We have found such instances where the refund due to the assessee was blocked by the AOs by tweaking interest component and the same has been discussed in the para 5.8.4 given below:

#### **5.8.4 Irregularities in issue of refund**

As per provisions of section 237 of the Act, if any person satisfies the AO that the amount of tax paid by him or on his behalf or treated as paid by him or on his behalf for any assessment year exceeds the amount with which he is properly chargeable under this Act for that year, he shall be entitled to a refund of the excess.

As such, in cases where the aggregate of advance tax, regular tax, tax deducted at source etc. so collected exceeds the tax determined on completion of the assessment, then the assessee is entitled for refunds. Timely disposal of refund claims is a key measure of the operational efficiency of tax administration. Prompt refunds instil confidence among taxpayers and increase tax compliance.

Citizen's Charter 2014 of Income Tax Department commits issue of refund including interest under section 143(1) and proceedings other than section 143(1) of the Act within six months and one month respectively from the date of processing/completion of order.

##### **5.8.4.1 Blockade of refund by way of unwarranted modification by AOs in the interest component causing hardship and harassment to taxpayers**

Audit noticed 1,130 instances<sup>89</sup> where modification by AOs in interest amount resulted in blockade of refund amounting to ₹ 4,39,571.21 lakh which was due to be payable to the concerned assessee. This was done by AO through manual modification in the interest under sections 234A, 234B and 234C of the Act at excess amount thereby creating unreasonable demand and as a result of this, the refund due to the assessee was denied, apart from violation of sections 234A, 234B and 234C of the Act.

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<sup>89</sup> The overall blockade of refund in respect of 1,130 cases is ₹ 4,39,571.21 lakh; however, 1,130 cases includes 35 cases pertaining to same assessee for same AY but assessed separately

We segregated the 1,130 instances into PAN category wise vis-à-vis amount of blocked refund, details shown in Table 5.14 below:

Table 5.14: Details of cases of blocked refund-PAN category wise		
Type of Assessee	Amount of blocked refund (₹ in lakh)	No. of Cases
1	2	3
AOP	2,761.45	19
Company	4,15,787.61	610
Firm	7,585.35	85
Govt. Authority	17.06	1
HUF	47.54	2
Artificial Juridical Person	161.44	3
Local Authority	1,411.76	3
Individual	7,079.18	395
Trust	4,719.82	12
<b>Total</b>	<b>4,39,571.21</b>	<b>1,130</b>

From the above, it can be seen that majority of the cases where the refund was blocked pertained to companies, individuals and firms. However, the maximum amount of blocked refund pertained to companies only. Of the 1,130 blocked refund cases, we found that 197 cases were processed under section 143(1)<sup>90</sup> of the Act and 660 cases were processed under section 143(3)<sup>91</sup> of the Act, wherein by way of modification in the interest component, refund of ₹ 96,662.32 lakh and ₹ 2,10,788.58 lakh, respectively, was blocked.

Processing of ITRs under section 143(1) of the Act, through CPC Bengaluru, is supposed to be automated. Details of cases processed under section 143(1) of the Act, with reference to range of amount are shown in Table 5.15 below:

Table 5.15: Blocked refund cases processed under section 143(1) of the Act		
Range of Amount (in ₹ )	Number of blocked refund cases	Amount of blocked refund (₹ in lakh)
1	2	3
≤10000	73	2.17
>10000 and ≤100000	68	23.04
>100000 and ≤500000	14	28.93
>500000	42	96,608.18
<b>Total</b>	<b>197</b>	<b>96,662.32</b>

Out of the 197 cases, there were 40 cases of company assesseees and 149 cases of individual assesseees whose refunds amounting to ₹ 93,785.82 lakh and ₹ 2,450.21 lakh, respectively, were blocked.

Six instances where AOs had blocked the refund of the assessee are discussed below:

90 Cases under section 143(1) are processed through CPC-Bengaluru

91 Cases under section 143(3) are scrutiny assessments completed by the assessing officer

**(a) Charge: Pr. CIT (Int. Tax)-III; DDIT(Int. Tax)- Noida AY: 2015-16**

The assessment of the assessee company was processed under section 143(1) of the Act in March 2017 wherein the AST system calculated interest under section 234B of the Act at nil, as the same was not leviable. Audit noticed that at the time of assessment under section 143(1) of the Act, the assessee had TDS credit of ₹ 19,369.84 lakh against the tax due amounting to ₹ 1,995.10 lakh. However, instead of issuing the refund amount of ₹ 17,374.74 lakh (₹ 19,369.84 lakh – ₹ 1,995.10 lakh) to the assessee, the AO modified the interest under section 234B of the Act at ₹ 17,374.74 lakh which resulted in blockade of refund. *ITD, in its reply, stated (November 2019) that the matter is sub-judice and proceedings for different years are pending before Hon'ble High Court. Any rectification, if required, will be made as per decision of Hon'ble High Court.* However, ITD did not furnish the reason behind modification in the interest amount, which was not warranted.

**(b) Charge: Pr. CIT (Int. Tax)-III, DDIT(Int. Tax)-I-Dehradun; AY: 2010-11**

In the case of an assessee company, an appellate order under section 254 of the Act was implemented in November 2017 wherein interest under section 234B of the Act was calculated through AST system at nil. Audit noticed that the company had total tax credit of ₹ 62,532.21 lakh consisting of TDS credit of ₹ 16,830.73 lakh, advance tax credit of ₹ 43,437.49 lakh and other tax credits ₹ 2,263.99 lakh against the tax due amounting to ₹ 50,577.28 lakh. However, instead of issuing the refund of ₹ 11,954.93 lakh (₹ 62,532.21 lakh – ₹ 50,577.28 lakh) to the assessee, the AO modified the interest under section 234B of the Act of the same amount, which resulted in blockade of refund.

**(c) Charge: Pr. CIT IX, Mumbai; AY: 2015-16**

The AO completed the scrutiny assessment of the assessee company in December 2017 under normal provisions at nil income and under special provision (Section 115JB of the Act) at book profit of ₹ 9,517.65 lakh. Audit noticed that the company had TDS credit of ₹ 7,666.47 lakh against the demand of ₹ 1,994.95 lakh. However, instead of issuing refund of ₹ 5,671.52 lakh (₹ 7,666.47 lakh – ₹ 1,994.95 lakh), the AO modified the interest under section 234B of the Act of the same amount which indicates that AO intentionally modified the interest amount just to block the refund that was due to the assessee. The rectification under section 154 of the Act was done in December 2018 to issue the refund of ₹ 5,671.52 lakh including avoidable payment of interest of ₹ 170.15 lakh.

**(d) Charge: Pr. CIT (Central)-3, Delhi; AY: 2015-16**

The AO completed the scrutiny assessment in October 2017 under normal provisions at nil income and under special provision (Section 115JB of the Act) at book profit of ₹ 12,755.93 lakh. Audit noticed that the company had filed its return of income on September 2015 i.e. within the prescribed time limit as stipulated in section 139(4) of the Act. As such, the assessee was not liable to pay interest under Section 234A of the Act. Audit examination revealed that though no interest under section 234A of the Act was computed through the system, AO modified it through manual intervention and levied the interest under this section amounting to ₹ 1,563.74 lakh without giving any justification in its assessment order. It was further noticed from Income Tax Return (ITR) of the assessee that the assessee had claimed the same amount of ₹ 1,563.74 lakh as a refund.

Audit further noticed that the ITD rectified the error when the assessee filed its grievance on Centralized Public Grievance Redress and Monitoring System (CPGRAMS) in February 2018. ITD issued the refund of ₹ 1,837.39 lakh in April 2018, which included interest under section 244A of the Act of ₹ 273.65 lakh including avoidable payment of interest of ₹ 39.09 lakh.

*The ITD in its reply (October 2019) stated that the modification of the interest under section 234A of the Act was an error of data feeding due to human error. Subsequently, rectification order under Section 154 was passed in April 2018 and thereafter the refund as claimed by the assessee was granted and issued.*

The reply was unacceptable as the refund was withheld with the directions of the PCIT (Central-3) at the time of assessment. Thus, the action of the ITD is affirmative of harassment and financial hardship to the compliant tax payer.

**(e) Charge: Pr. CIT (Central)-3, Delhi; AY: 2014-15**

In this case, a rectification order under section 154 of the Act was passed on May 2017 at an income of ₹ 221.92 lakh under normal provisions and ₹ 1084.79 lakh under special provisions of the Act with a tax liability of ₹ 227.37 lakh thereon. As per the snapshot of order under Section 154 of the Act, the TCS/TDS of ₹ 1243.96 lakh was available to the company, therefore, the company was not liable to pay the interest under section 234C of the Act. No interest under section 234 C was computed through the AST, as shown in snapshot, as it was not due from the assessee. The AO, however, levied interest under section 234C of the Act amounting to ₹ 966.58 lakh through manual modification without giving any justification. Audit further noticed that the ITD rectified the error only after the assessee filed repeated requests for refund and finally took up the grievance on CPGRAMS in April 2018. The process of refund of ₹ 966.58 lakh including avoidable payment of interest of

₹ 125.66 lakh was initiated by the ITD in May 2018. Thus, the AO resorted to manual intervention in the system to block the refund which was due to assessee.

**(f) Charge: Pr. CIT (Central)-2, Delhi; AY: 2014-15**

AO completed the scrutiny assessment in March 2016 at a loss of ₹ 12,485.58 lakh. As the assessment was made at a loss, therefore, the company was not liable to pay the interest under section 234B of the Act. It was further noticed from the ITR filed by the assessee that the assessee had claimed the tax credit of TDS amounting to ₹ 2,711.96 lakh as a refund. But, AO modified the interest component through manual intervention and levied interest of ₹ 2,695.29 lakh under section 234B of the Act and ₹ 16.66 lakh as dividend distribution tax under section 115O of the Act (which was already paid by the assessee). Thereafter, ITD passed the rectification order under section 154 of the Act in July 2016 and released the refund amounting to ₹ 2,711.96 lakh including avoidable payment of interest of ₹ 40.68 lakh. Thus, the action of AO indicates that AO resorted to manual intervention in the system to block the refund which was due to assessee.

It was evident from the above cases that, AO had withheld the refund amount admissible to the assessee by making manual modification through levy of interest to the extent of the amount of refund, when available tax credit was more than the tax or cases where no tax was leviable. It was done without entering the reason for modification in the relevant column of the AST snapshot.

Further, of the 1,130 cases where refunds were blocked by AOs by way of modifying the interest amount, audit could identify 175 cases where refunds were released to the assessee after a delay ranging from one month to 156 months. Details of such 175 cases are given in Table 5.16 below:

<b>Table 5.16: Details of cases related to blocked refund</b>			
<b>Range of delay in issuing the blocked refunds to the assesseees</b>	<b>Number of blocked refund cases</b>	<b>Amount of blocked refund (₹ in lakh)</b>	<b>Additional (avoidable) payment of interest under section 244A of the Act (₹ in lakh)</b>
<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>
≤12 months	86	47,179.78	1,842.69
>12 months and ≤24 months	49	22,493.88	2,121.79
>24 months and ≤36 months	25	5,537.44	831.92
More than 36 months	15	1,983.70	478.19
<b>Total</b>	<b>175</b>	<b>77,194.80</b>	<b>5,274.59</b>

Thus, by way of irregular levy of excess interest by AOs, not only refund amount was blocked causing undue harassment and hardship to the assesseees, but it also put an additional burden on the exchequer in the form of avoidable

payment of huge amount of interest on refunds. This also led to non-adherence to the commitment made in the Citizen's Charter by the ITD, as, instead of issuing refunds to the assessee within the timeframe, refunds were blocked through manual modification by AOs in the interest component.

#### **5.8.4.2 Refund not due to the assessee issued irregularly**

In Punjab, Pr. CIT-3, Ludhiana charge, audit found in 146 cases that no refund was due to the assessee as processed under section 143(1) of the Act. However, refund amounting to ₹ 63.63 lakh was issued (from September 2016 to February 2018) to the assessee by way of rectification under section 154 of the Act. Based on the internal enquiry conducted (from January 2018 to March 2018) by the department, a First Information Report (FIR) was lodged (April 2018).

*On being pointed out by the Audit why refund was issued to such assessee against whom no refund was due, the ITD stated (in 135 cases) that these refunds were not issued by the AOs as the case was processed centrally at CPC-Bengaluru. The system was unauthorisedly accessed by the data entry operator in connivance with an advocate and issued refunds by carrying illegitimate rectifications. First Information Report (FIR) had been lodged against them.*

This points to the fact that the ITD does not have effective access control in place to manage unauthorized access to system. This also indicates inadequate internal control mechanism that do not address different security risks.

#### **5.8.5 Incorrect Interest calculated through Income Tax Business Application (ITBA)**

The essence of any robust Information Technology (IT) system is that all calculation especially, in case of interest calculation system, should be based on a proper formula fed into the system and there should be no need for carrying out any modification. In view of the above, the ITD adopted Income Tax Business Application (ITBA) module from the financial year 2017-18 to eliminate the human intervention in respect of modification of interests under sections 234A, 234B, 234C and 244A of the Act as the same prevailed in earlier software namely AST. Thereafter, the assessment proceedings in ITD are being carried out on ITBA only.

We found that of the 6,217 cases (checked by audit) which were processed through AST in FY 2016-17 and FY 2017-18, 496 cases were processed/completed through ITBA in FY 2018-19. We further examined the 496 cases which were processed through ITBA to see whether correct calculation of the interest was being done through this application. Of the 496 cases, we found

32 cases involving tax effect of ₹ 2,297.95 lakh where calculation of interest was done wrongly through ITBA. Thus, the system deficiency with respect to calculation of interest still persisted in the new application, i.e. ITBA.

Three such cases are illustrated below:

**(a) Charge: Pr. CIT-II, Mumbai; AY: 2016-17**

The AO assessed the income of a Bank after scrutiny in December 2018 through ITBA at an income of ₹ 4,177.23 lakh<sup>92</sup>. Audit noticed that the assessee had filed its return of income on the due date of filing of return, i.e. on 30 November 2016. Further, the assessee had filed its revised return of income on 27 March 2018 against the due date of 31 March 2018. As such, the interest under section 234A of the Act in respect of default in furnishing the income tax return was not leviable in the instant case. However, while calculating the tax demand generated through ITBA, interest under section 234A of the Act amounting to ₹ 395.08 lakh was levied. The error had resulted in excess levy of interest under section 234A of the Act by an equal amount.

**(b) Charge: Pr. CIT DDIT(Int)-I, Dehradun; AY: 2016-17**

The AO assessed the income of the assessee company after scrutiny in January 2019 through ITBA. Audit noticed that at the time of filing of return of income, the assessee had TDS credit of ₹ 12,628.87 lakh against tax payable of ₹ 7,549.58 lakh. Further, the computation sheet generated through ITBA depicts that the department had allowed TDS credit of ₹ 10,812.50 lakh against the tax liability of ₹ 9,147.09 lakh, therefore, there was no scope for levying the interest under section 234C of the Act. However, the ITBA module had levied the interest under section 234C of the Act amounting to ₹ 246.19 lakh. The incorrect levy of interest under section 234C of the Act by the system in ITBA module reflects the error in application part which needs improvement.

**(c) Charge: Pr. CIT (LTU) Bengaluru; AY: 2015-16**

The AO assessed the income of the assessee company after scrutiny in December 2018 through ITBA at an income of ₹ 58,754.86 lakh. Audit noticed that assessee filed its return of income on 23 November 2015 as against due date of filing of return of income on 30 November 2015. As such, the interest under section 234A of the Act in respect of default in furnishing the income tax return was not leviable in the instant case. Audit noticed that, while calculating the tax demand generated through ITBA, interest under section 234A of the Act amounting to ₹ 697.06 lakh was levied. *The ITD in its reply (November 2019) stated that in the assessment order, the interest is calculated by the ITD in an automated environment and AO has no role in computation.*

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92 Under special provision (Section 115JB of the Act)

*Thus, this mistake is not on part of AO. ITD rectified this error under section 154 of the Act in January 2019.*

In our earlier performance audit on 'IT Application in Income Tax Department' (Report no. 23 of 2012-13), Ministry after acknowledging the deficiency in AST system, had stated that Income Tax Business Application (ITBA) was being developed by ITD to replace the existing ITD Application and all issues related to existing system would be taken into consideration in the new application, i.e. ITBA. Further, in the Report of the Tax Administration Reform Commission (TARC) submitted to the Government of India on 30 May 2014, it was highlighted that core module of the ITD application, viz. AST has been patchy and uneven, leading to creation of incorrect demands in the system. It was further stated in the report that 'The CBDT, however, plans to overcome the major gaps through ITBA'.

However, observation with respect to 32 cases where calculation of interest was done wrongly through ITBA, is indicative of the fact that system deficiency with respect to calculation of interest persists in the new application, i.e. ITBA.

#### **5.8.6 Other compliance issues**

This para pertains to observation noticed during our regular audit conducted for the period 2018-19. We found 134 cases involving tax effect of ₹ 1,10,269.82 lakh with respect to interest under sections 234A, 234B and 234C of the Act.

Six such cases are illustrated below:

##### **(a) Charge: PCIT -1, Coimbatore, Chennai; AY: 2009-10**

The AO completed the assessment of the assessee company under section 144 read with section 147 of the Act in December 2016 at an income of ₹ 761.50 lakh. Audit scrutiny revealed that interest under section 234A of the Act at ₹ 20.71 lakh was computed through the system (AST) instead of ₹ 225.19 lakh for the period from October 2009 to December 2016. The error had resulted in short levy of interest under section 234A of the Act amounting to ₹ 204.48 lakh. *ITD rectified the error by passing orders under Section 154 of the Act (September 2017).*

##### **(b) Charge: PCIT (Central)-1, Delhi; AYs:1995-96, 1996-97 & 1997-98**

The AO assessed the income of an Individual for AYs 1995-96, 1996-97 and 1997-98 at ₹ 1,527.39 lakh, ₹ 5,572.94 lakh and ₹ 15,441.84 lakh in March 1998, March 1999 and March 2000 respectively. Assessee's appeals against these assessment orders before CIT (Appeals), Lucknow were finally decided by the Hon'ble Supreme Court vide its order dated 04 July 2016. The appeal effects were given by the AO in August 2016, wherein the AO wrongly used

lower rate of interest than the rate prescribed under section 234B of the Act for default in payment of advance tax by the assessee. The error had resulted in short levy of interest of ₹ 3,352 lakh. *ITD accepted (October 2017) the audit observation and rectified the error by passing orders under section 154 of the Act (September 2017).*

**(c) Charge: CIT LTU, Bengaluru, Karnataka; AY: 2015-16**

The AO completed the assessment of a Bank in December 2017 after scrutiny at an income of ₹ 7,82,161.61 lakh. Audit examination revealed that, while computing interest under section 234B of the Act, ITD short levied the interest amount by ₹ 3,934.44 lakh. *ITD rectified the error by passing order under section 154 of the Act (March 2019).*

**(d) Charge: PCIT – 4, Delhi; AY: 2015-16**

The AO assessed the income of the assessee company in December 2017 at ₹ 1,66,028 lakh and tax liability of ₹ 56,432.90 lakh thereon. Audit noticed that the AST system as well as AO had not levied the interest under section 234C of the Act, despite the fact that the advance tax paid by the assessee was less than the tax due on the returned income. The error in computing the interest resulted in short levy of tax of ₹ 955.38 lakh. This also points to the fact that ITD had failed to levy correct interest under section 234C of the Act and even the system was deficient in computing the final demand of the assessee. *ITD rectified the error (February 2019) by passing order under section 154/250 of the Act.*

**(e) Charge: PCIT –I, Bhubaneswar, Odisha; AY: 2014-15**

The AO assessed the income of the assessee company in December 2017 at an income of ₹ 1,68,887.69 lakh. Audit noticed that though the assessee company was in default in payment of instalment of advance tax, interest under section 234C of the Act was not levied. Failure on the part of ITD to adhere to provision of section 234C of the Act resulting in non-levy of interest of ₹ 111.78 Lakh. *ITD rectified the error by passing rectification order under section 154 of the Act (November 2019).*

**(f) Charge: PCIT -II, Hyderabad; AY 2008-09**

The case of assessee company was assessed under section 147 read with 143(3) of the Act in March 2016 an income of ₹ 4,094.11 lakh and a tax of ₹ 1,293.13 lakh thereon. Audit examination revealed that, instead of calculating correct amount of interest at ₹ 956.85 lakh under section 234B of the Act, interest was calculated through AST at ₹ 237.81 lakh. Further, AO did not take any action to correct the incorrect interest calculated through the system. Thus, the error in computation through the system and no remedial action taken by AO in this regard had resulted in short levy of interest ₹ 719.04

lakh. ITD rectified the error by passing order under section 154 of the Act (February 2019).

## **5.9 Conclusion**

- a) The interest was wrongly computed by ITD, in 76.68 *per cent*<sup>93</sup> of cases of the sample of 6,217 selected out of a population of 8,35,727 records, either due to systemic deficiencies or due to incorrect interventions by the AOs.
- b) Input of the other ITD module was not being captured properly in the AST system leading to incorrect computation of interest in number of cases which has an impact on final tax collection and refund.
- c) AOs did not take any step to rectify the incorrect interest, under sections 234A, 234B, 234C and 244A of the Act, calculated through the system even though AST system allowed the AOs to modify the value of interest in accordance with the provisions of the Act, thereby leading to either short levy/payment or excess levy/payment of interest.
- d) AOs modified the interest under sections 234A, 234B, 234C and 244A of the Act against the incorrect interest calculated through the system in some cases. However, not all these cases were modified at correct amount, which resulted in either short levy/payment or excess levy/payment of interest.
- e) AOs manually modified the interest amount which was not warranted in instances where correct amount of interest was calculated through the system, leading to either short levy/payment or excess levy/payment of interest causing hardship and harassment to taxpayers.

It is not clear why manual modification is permitted, that too apparently without a protocol for seeking senior level clearances if, in exceptional cases, manual intervention is required. In fact, if manual intervention at every level is needed, or continued, it either points to an ill designed IT System, or a deliberate attempt to retain discretion, for no apparent good reason.

- f) Incorrect levy of interest (excess levy) by AOs using modification feature of AST led to blockade of refunds due to the assesseees. This was not only violation of provisions of law but also resulted in non-fulfilment of Citizen's Charter. On the one hand the efficiency of the department was affected and on the other there was undue harassment to the assesseees.

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93 4,767 assessment cases out of 6,217 assessment cases which were audited

- g) All Income Tax Returns (ITRs) are first summarily processed under section 143(1) at Centralized Processing Centre (CPC), Bengaluru. Processing of ITRs by CPC is supposed to be completely automated. However, refunds of the assessee's were blocked by modifying the interest amount even in cases processed in summary manner through CPC.
- h) The net collection of taxes is computed by allowing for the refunds<sup>94</sup>. Blockade of refunds, therefore, have the result of inflating the net tax collection. Further, unreasonable tax demand from the assessee, by way of excess levy of interest, results in disputes and further snowballs into large arrears. Thus, the blockade of refund and excess demand would have consequent effect on the revenue collection of the Government.

#### 5.10 Recommendations

- a) *CBDT may institute appropriate checks and balances in Income Tax Business Application (ITBA) to prevent recurrence of error in computation of tax and interest.*
- b) *The IT system for direct taxes needs to be designed in such a way that it should ensure zero or minimal physical interface between the assessee and the tax officers. The Government may consider the IT System for direct taxes being placed at arms length from CBDT, with an independent governmental body or organisation.*
- c) *AST module allows manual modification of interest amount which resulted in errors in computation of interest. ITD needs to inquire into the reasons for errors in computation of interest through AST and reasons for allowing manual modification to co-exist with IT system.*
- d) *The system should be designed to provide audit trail for modifications, if any, being carried out by AOs. All justifications for modification by AO must be available on the system.*
- e) *CBDT may examine whether the instances of "errors" noticed are errors of omission or commission and if these are errors of commission, then ITD should ensure necessary action as per law.*
- f) *The IT Department may fix accountability on the part of the AOs to ensure that the risk of recurrences of similar types of irregularities are minimised.*

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94 Para 7.2.2. of CBDT Accounts Manual

- g) CBDT may ensure that the refund due to the assessee is released in prescribed time limit, upholding its commitment through the citizen charter, rather than to withhold/block it by manual intervention.*
- h) AO's action regarding blockade of refund as well as under charging of interest may be investigated upon.*
- i) While audit carried out test check of a sample of cases, CBDT should examine all the cases where modifications were carried out in AST to identify instances of omission and commission and take necessary action as per law.*

## Chapter VI: Long Term Capital Gain on Penny Stocks

### 6.1 Introduction

Penny stocks<sup>95</sup> are stocks, listed on stock exchange that trade at a very low price, have very low market capitalization, are mostly illiquid. These stocks are very speculative in nature and are considered highly risky because of lack of liquidity, smaller number of shareholders and limited disclosure of information.

For making available information related to Penny Stock to the Assessing Officers (AOs), the Income Tax Department (ITD) has added a new button 'Penny Stock' on Individual Transaction Screen (ITS) in Income Tax Application Systems to display information related to penny stock<sup>96</sup>. Further, the Systems Directorate has uploaded details of assesseees who have made transactions in such penny stock<sup>97</sup>. The ITD has issued a standard operating procedure (SOP) dated 21<sup>st</sup> November 2016 detailing various aspects, the AO is expected to consider inter alia, during scrutiny of a particular case.

As per Finance Bill 2017, it has been noticed that exemption provided under section 10(38)<sup>98</sup> of the Income Tax Act, 1961 (the 'Act') is being misused by certain persons for declaring their unaccounted income as exempt Long-Term Capital Gains (LTCG) by entering into sham transactions.

### 6.2 Background

The Directorate of Income Tax (Investigation), Kolkata had investigated the Accommodation Entry Operators<sup>99</sup> within their jurisdiction i.e. Kolkata and had identified 84 BSE listed penny stocks and conducted number of search and surveys in the office premises of more than 32 share broking entities. The entities accepted that they were actively involved in the bogus LTCG. The DIT (Investigation) conducted surveys in the office premises of many accommodation entry<sup>100</sup> providers and their statement was recorded.

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95 Refer "Investigation Report of the Directorate of Income Tax (Investigation) Kolkata, in case of Project Bogus LTCG through BSE Listed Penny Stocks".

96 Enforcement Information System (EFS) Instruction no. 53 of Directorate of Systems dated 08.03.2016.

97 CBDT Letter No. - F.No.287/30/2014-IT (Inv. II)-Vol-III dt. 16th March, 2016

98 Section 10(38) of the Income-tax Act, 1961 exempts long term capital gains (LTCG) arising from transfer of listed equity shares, where transfer of shares is on or after 1st October 2004 and the transaction of sale is chargeable to Securities Transaction Tax (STT).

99 As per the DIT (investigation) report, an entry operator is the person who is in the business of giving accommodation entries in lieu of cash/cheque of equal amount after charging certain percentage of commission in cash.

100 As per the DIT (investigation) report, Accommodation entry is a financial transaction between the two parties where one party enters the financial transaction in its books to accommodate the other party in lieu of cash of equal amount and commission charged over and above at certain fixed percentage. These accommodation entries are taken by various beneficiaries for introducing their unaccounted cash into their books of accounts without paying the due taxes.

The DIT (Investigation) Kolkata, from the records of the Accommodation Entry Providers identified 64,811 pan-India Beneficiaries involving suspicious exempt LTCG of ₹ 38,000 crore (approx.) and sent their report to Jurisdictional assessment wings through the DGITs.

We selected Mumbai charge for audit, as out of total suspicious exempt LTCG of ₹ 38,000 crore, ₹ 12,234 crore (32 *per cent*) involving 17,344 beneficiaries (27 *per cent*) was falling under Mumbai charge.

### **6.3 Modus operandi in brief**

As per the “Report of the DIT (Investigation), Kolkata”, the modus operandi was to make the beneficiary<sup>101</sup> buy some shares of pre-determined penny stock company controlled by the entry operators<sup>102</sup> at a very low price through exchange itself or through preferential allotment i.e. through private placement. The beneficiary holds the shares for one year, the statutory period after which LTCG received over penny stock was exempt under section 10(38) of the Act till 31<sup>st</sup> March 2018. In the meantime, operators rig the price of stock and gradually raise its price many times, often 20 to 25 times. When the prices reach desired level, the beneficiary who bought the shares at nominal price, is made to sell it to a dummy paper company of the operator. For this, the report says unaccounted cash was provided by the beneficiaries which were routed through a few layers of paper companies by the operator and finally parked with the dummy paper company also known as the Exit Provider which will buy the shares.

### **6.4 Audit Methodology**

As per the Report of the DIT (Investigation) Kolkata, there were 17,344 beneficiaries in Mumbai who claimed exempt LTCG. A test check of cases under the Mumbai jurisdiction of the Income Tax Department was carried out by the Audit with audit objectives as given below. For the audit of assessments, 547 cases were selected across 29 CITs, out of which 499 cases have been audited. Out of the 48 cases not audited, 14 cases constituted non-production of records and remaining due to non-existence of PAN, non-availability of data, Jurisdictional charge out of Mumbai etc.

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101 Person who is in possession of unaccounted money and wants to bring this into his books without paying any tax whatsoever.

102 As per the DIT (investigation) report, an entry operator is the person who is in the business of giving accommodation entries in lieu of cash/cheque of equal amount after charging certain percentage of commission in cash.

We referred the matter to the Ministry of Finance in April 2020 for its comments. Response of the Ministry was awaited (June 2020).

## **6.5 Audit Objectives**

- a) To examine whether the Department has targeted all beneficiaries identified by the DIT (Investigation), Kolkata who were claiming exempt LTCG under section 10(38) of the Act through Penny Stock.
- b) To examine whether the AOs have followed Board Instructions and SOP issued by the ITD on assessment of LTCG claims involving penny stocks.

## **6.6 Audit Findings**

The verifications of the assessment records of beneficiaries who had traded in penny stock involving suspicious exempt LTCG under section 10(38) of the Act, were test checked and following were the findings:

### **6.6.1 Beneficiaries neither selected for scrutiny nor reopened under section 148 of the Act despite claiming LTCG**

We noticed that in 71 cases wherein assessees involving exempt capital gain claim, the department had not taken any action in the light of report of the DIT (Investigation), where in these exempt capital gain have been treated as suspicious. Despite a new button 'Penny Stock' added on Individual Transaction Screen (ITS) in Income Tax Application Systems to display information related to penny stock and the uploading of details of assessees who had traded in such penny stock by the System Directorate, the ITD failed to scrutinize or reopen these cases in the light of claim of exempt capital gain.

**6.6.1.1** In 36 cases, the assessees had claimed exemption of LTCG in ITRs but the Department failed to select these cases for scrutiny or reopen under section 148 of the Act in the light of claim of exemption of LTCG and CBDT instructions<sup>103</sup> on penny stock. Illustration of one case is as follows:

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103 CBDT Letter No. - F.No.287/30/2014-IT (INV.II)-Vol-III dt. 16th March, 2016

(a) In the case of an Individual assessed in ACIT 17(2), Mumbai for the assessment year (AY) 2013-14, the assessee had filed ITR 2 whose schedule EI on details of exempt income revealed that the assessee had claimed ₹ 15.47 crore as exempt LTCG. In AY 2013-14 assessee had traded in shares of such companies, which were recognized as Penny stock as per DIT(Investigation), Kolkata report, with trade value of ₹ 15.37 crore. However, no action was taken to examine the veracity of the transaction in spite of the magnitude of the exempt LTCG.

**6.6.1.2** In 28 cases, the assessees had not shown any capital gain in their ITRs and were neither selected by the department under CASS nor reopened under section 148 of the Act. However, as per the DIT (Investigation) Kolkata, these assessees had traded in Penny Stocks involving exempt LTCG claim. Despite availability of information in the report of the DIT (Investigation), Kolkata in respect of these assessees and CBDT instructions on penny stock, the ITD failed to examine the escapement of income under the head LTCG. One case is illustrated below:

(a) In the case of a assessee company assessed in ITO 4(3)(4), Mumbai, the return filed for *AY 2010-11 and 2011-12* in ITR 6, schedule EI of details of exempt income revealed that the assessee had shown nil exempt income. The stock exchange data used by DIT(Investigation), Kolkata showed that the assessee had traded in shares of a company (penny stock as per DIT(Investigation), Kolkata report) with trade value of ₹ 13.51 crore and ₹ 7.70 crore for AY 2010-11 and 2011-12 respectively. However, no action was taken by the Department in order to examine the escapement of income under the head LTCG.

**6.6.1.3** In seven cases, audit noticed that, these assessees were involved in trading in penny stocks as per the report of the DIT (Investigation), Kolkata. However, these assessees had not filed their ITRs. The ITD neither issued notices to these assessees for filing the ITRs nor initiated any assessment procedure under section 144 of the Act. Even NMS<sup>104</sup> had not been utilized effectively in respect of these non-filers, which indicate the weakness of the NMS as well. One case is illustrated below:

(a) In the case of an Individual assessed in ITO 32(2)(1), Mumbai, the returns were not filed by the assessee for AYs 2014-15 and 2015-16. This case was neither selected for scrutiny nor any notice provided by the department to show the efforts taken to trace the assessee. Assessee had traded in shares of such companies which were recognized as Penny stock as per DIT

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104 Non-filers Monitoring System

(Investigation), Kolkata Report with trade value of ₹ 3.89 crore. However, ITD failed to issue notice to the assessee for filing the ITR in spite of the magnitude of the exempt LTCG which might be bogus in nature. This also indicates failure of the Non-filers Monitoring System.

In reply, the department stated that, from the individual transaction Statement (ITS) query, no specific trade data regarding penny stock companies had been received in the system. Hence, audit query is not acceptable. However, the case will be reopened as a remedial action.

Department reply is not tenable as it is seen from the report of the DIT(Investigation), Kolkata that assessee has traded in these penny stocks.

#### **6.6.2 Beneficiaries selected for scrutiny but addition in respect of Exempt LTCG involved was made inconsistently or not made.**

**6.6.2.1** In 21 cases we observed that Department had selected the cases for scrutiny but addition was not made in respect of the exempt capital gain claimed, despite having information available with AO through the new tab 'Penny Stock' developed in ITS and under Actionable Information Monitoring System (AIMS). The AO had not given any justification for not disallowing Exempt LTCG even though the case was selected for verifying Exempt LTCG through Penny Stock, which indicates a lackadaisical attitude of the AO and non-transparency in the workings of the Department and also non-compliance to the SOP issued by the department on assessment of penny stock cases. Three cases are illustrated below:

**(a)** In the case of an individual assessed in ACIT Circle 15(2)(1) for the AY 2013-14, notice under section 148 was issued in September 2016 and reason for reopening was sale of shares of penny stock company and total sale consideration was ₹ 14.82 crore. The proceeding under section 148 was dropped on 08.05.2017 by ACIT 22(3) stating that case was transferred to ACIT 15(2)(1) charge. However, no further action has been taken by the current AO charge. This indicates a weak monitoring of actionable cases subsequent to transfer of charge which could be misused by assesseees.

**(b)** In the case of an individual assessed in Ward ITO 22(3)((2) Mumbai for AY 2014-15, the AO in his letter dated 19.10.2016 supplied reason for reopening under section 147, that as per the DIT(Investigation), Kolkata the assessee has earned LTCG exempt of ₹ 3.21 crore from trading of penny stocks for a total trade value of ₹ 3.30 crore. Therefore, the income of ₹ 3.30 crore chargeable to tax had escaped assessment within meaning of section 147 of the Act. However, while passing the assessment order (October

2017) the AO did not discuss anything about the investment and sale consideration in respect of penny stocks and accepted the income as per return without any disallowance for LTCG on penny stocks.

(c) In the case of an individual assessed in DCIT, Central Circle-I Kanpur for AY 2012-13, search and seizure operation was conducted in July 2014 at the residential premises of the assessee. Cash of ₹ 0.10 crore and jewellery of ₹ 0.97 crore were seized. The case was centralized in this circle. Assessment order was passed in May 2017 under section 153A of the Act. It was observed from the computation of Income statement that assessee has claimed exempt LTCG of ₹ 6.06 crore from sale of shares of a company which was one of the penny stocks reported by the DIT(Investigation), Kolkata. Therefore, LTCG claimed exempt should have been disallowed by the department. However, while passing the assessment order the AO did not discuss about Exempt LTCG and sale consideration in respect of penny stock despite having information available with him through a new tab 'penny stock' developed in ITS and under Actionable Information Monitoring System (AIMS) and allowed the same.

**6.6.2.2** In seven cases, AO had made disallowance in case of Entry-Exit provider as a percentage of the trade value. As per assessment orders of these individuals, all of them were used by entry provider for providing bogus accommodation entries to various beneficiaries. However, in another similar cases which were used by same entry provider, AO had made 100 *per cent* disallowance. Thus there is inconsistency in the disallowance made during the assessments. One case is illustrated below:

(a) In the case of an individual, assessed in ITO 30(1)(5), Mumbai for AY 2014-15. The case has been selected for scrutiny under CASS with a reason suspicious sale transactions in shares (Penny stock in ITS). The assessee being one of the exit provider, had purchased the penny stock shares of company. In the assessment order, department disallowed five *per cent* of the total cash deposit of ₹ 6.36 crore amounting to ₹ 0.32 crore stating that assessee is an Exit Provider. However, in a similar case of a company assessed in DCIT(CC) - 8(3), Mumbai, where assessee company was an exit provider and trading in shares of same company, the department had disallowed 100 *per cent* of total purchase and entire amount was added. Thus, clear inconsistency is evident in assessments.

### 6.6.3 Inconsistency in dis-allowance of Sale consideration and commission expenses

**6.6.3.1** We noticed that in the treatment of bogus LTCG transactions there was no uniformity in additions made in the Assessment orders passed by the AOs. The SOP issued by the department on assessment of penny stocks prescribes that in case of prearranged claim of LTCG entire sale proceeds received on sale of shares is to be added as taxable income under section 68 of the Act, without any eligibility of exemptions under section 10(38) of the Act. Moreover, while disallowing the bogus LTCG in 32 cases department had disallowed the total sale consideration, where as in 43 cases department disallowed claim of net LTCG only. One case is illustrated below:

*Section 68 of the Act provides that, if assessee offers no explanation about the nature and source of any sum credited in the books of the assessee, the sum so credited may be charged to income tax as income of the assessee.*

In the case of an individual assessed in Circle 31(3) Mumbai for AY 2013-14, the assessee had claimed ₹ 5.20 crore exempt under section 10(38) of the Act. Assessee has received ₹ 5.41 crore as sale proceeds. The ITD had disallowed the net capital Gain of ₹ 5.20 crore only which was claimed exempt, under section 68 of the IT Act, 1961. However, in the case of an another individual assessed in Ward ITO 17(3)(1) Mumbai, for the AY 2014-15, the assessee had claimed ₹ 10.82 crore exempt under section 10(38) of the Act. The ITD had disallowed the amount of ₹ 11.01 crore received as sales proceeds of shares under section 68 of the Act.

**6.6.3.2** There is a cost attached to getting undisclosed income converted into disclosed income, disallowed by the department as commission expenditure. We noticed that there was no consistency in the approach in disallowing the same. In 40 cases disallowance on account of commission was not made whereas in 69 cases commission disallowance varied from 0.5 to 5 per cent. Two cases are illustrated below:

*Section 69C of the Act provides that, if assessee offers no explanation about the source of any expenditure incurred by the assessee in any financial year such expenditure may be deemed to be the income of the assessee for charged to income tax as income of the assessee for such financial year.*

**(a)** In the case of an individual assessed in December 2017 in Ward ITO 18(2)(5) Mumbai for AY 2015-16, the assessee had taken entry from an entry operator who had admitted in his statement recorded by the investigation Wing, Kolkata that he was providing the accommodation entries to beneficiaries by charging commission. The ITD disallowed ₹ 5.27 crore as unexplained investment being bogus profit on sale of shares of penny stock company. Further, the commission at the rate of 0.50 *per cent* was disallowed by the department as unexplained expenditure under section 69C of the Act.

**(b)** In the case of an individual assessed in December 2017 in Central Circle 2(2), Mumbai for AY 2014-15, the assessee had taken entry from entry operator. The operator had admitted in his statement recorded by the investigation Wing, Kolkata that he was providing the accommodation entries to beneficiaries by charging commission. The ITD disallowed ₹ 12.74 crore as unexplained investment being bogus profit on sale of shares. Also the ITD disallowed the payment of commission at the rate of five *per cent* as unexplained expenditure under section 69C of the Act.

## **6.7 Conclusion**

The ITRs of the assesseees who traded in the shares of penny stock companies were neither selected for scrutiny nor reopened for scrutiny despite the ITD having information of claiming LTCG. The ITD failed to issue notices for filing ITRs, to the assesseees who were involved in trading penny stocks, but have not filed their ITRs. Even Non-filers Monitoring System had not been utilized effectively to identify such non-filers. The AOs had no uniformity in making additions of exempt LTCG, despite the fact that the grounds of additions were same. In some cases, AOs did not make any addition for claimed exempted LTCG, for which no justification was given in the assessment orders. Further, the AOs had made additions at different percentage where the assesseees traded in shares of same penny stock companies. The ITD did not have any systemic approach to deal with cases of beneficiaries traded in penny stock as in some cases entire sales consideration was disallowed whereas in some cases only claimed LTCG was disallowed. There is also variation in disallowance of commission received by entry and exit provider from beneficiary of penny stock.

It is recommended that

- (i) *the ITD may design CASS parameters in such a way that all the relevant information with ITD, whether from ITR or other sources, may be used to select the cases for scrutiny.*
- (ii) *the method of selection for scrutiny under CASS may be shared with the C&AG as was pointed out in the Audit Report No. 9 of 2019 of C&AG so that audit may see whether the selection of cases for scrutiny is as per CASS parameters.*
- (iii) *the ITD may examine whether the errors in assessment of cases where LTCG on penny stock was claimed, are errors of omission or commission and if these are errors of commission, then ITD should ensure necessary action as per law.*

New Delhi  
Dated: 03 August 2020

  
(Neelesh Kumar Sah)  
Principal Director (Direct Taxes-I)

Countersigned

New Delhi  
Dated: 04 August 2020

  
(Rajiv Mehrishi)  
Comptroller and Auditor General of India



# **Appendices**



## Appendix 2.1 (Reference: Paragraph 2.2.5)

State-wise incidence of errors in assessments						
State	Assessments completed in units selected for audit during 2018-19	Assessments checked in audit during 2018-19	Audit observations <sup>105</sup> (Nos.)	Assessments with errors (Nos.)	Total revenue effect of the audit observations (₹ in crore)	Percentage of assessments with errors (Col. 5/ Col. 3x100)
1	2	3	4	5	6	7
Andhra Pradesh & Telangana	25,620	22,160	1,598	1548	1,412.91	6.99
Assam	3,618	3,540	290	275	47.31	7.77
Bihar	2,248	2,180	149	150	950.53	6.88
Chhattisgarh	6,724	3,747	258	253	96.49	6.75
Delhi	42,378	32,794	1,454	1,372	1,373.40	4.18
Goa	1,222	1,193	120	120	81.88	10.06
Gujarat	16,291	15,923	1,214	1,049	2,146.06	6.59
Haryana	13,061	9,748	1,019	915	635.99	9.39
Himachal Pradesh	1,710	1,212	122	117	49.77	9.65
UTs of Jammu & Kashmir; and Ladakh	843	597	40	39	0.44	6.53
Jharkhand	3,799	2,370	141	117	47.84	4.94
Karnataka	12,737	12,342	1,142	1,071	6,380.78	8.68
Kerala	11,080	10,770	744	725	251.16	6.73
Madhya Pradesh	25,626	20,091	1,512	1,512	4,750.27	7.53
Maharashtra	1,60,227	75,596	4,013	3,502	18,816.02	4.63
Odisha	4,680	4,404	528	496	477.39	11.26
Punjab	12,845	7,474	677	510	199.57	6.82
Rajasthan	15,530	14,988	678	665	170.26	4.44
Tamil Nadu	23,843	20,466	2,061	1,899	2,373.66	9.28
UT Chandigarh	4,927	3,844	297	243	1,164.31	6.32
Uttarakhand	916	911	37	35	65.09	3.84
Uttar Pradesh	26,617	26,257	946	884	1,127.25	3.37
West Bengal	42,078	39,632	2,493	2,271	2,313.85	5.73
<b>Total</b>	<b>4,58,620</b>	<b>3,32,239</b>	<b>21,533</b>	<b>19,768</b>	<b>44,932.14</b>	<b>5.95</b>

105 This includes all audit observations of under assessment as well as over assessment in Corporation Tax, Income Tax and other direct taxes.

## Appendix 2.2 (Reference: Paragraph 2.2.7)

Category wise details of underassessment in respect of Corporation tax and Income tax detected during local audit		
	(₹ in crore)	
Sub category	No. of errors	Tax effect
<b>A. Quality of assessments</b>	<b>7,504</b>	<b>9,768.64</b>
a. Arithmetical errors in computation of income and tax	1,663	2,963.66
b. Incorrect application of rate of tax, surcharge etc.	695	218.51
c. Non/short levy of interest/penalty for delay in submission of returns, delay in payment of tax etc.	4,874	4,669.98
d. Excess or irregular refunds / interest on refunds	120	319.08
e. Error in assessment while giving effect to appellate orders	152	1,597.41
<b>B. Administration of tax concessions/exemptions/ deductions</b>	<b>6,407</b>	<b>18,533.62</b>
a. Irregular exemptions/deductions/reliefs given to Corporates	287	1,244.86
b. Irregular exemptions/deductions/reliefs given to Trusts/Firms/Societies	618	1,576.28
c. Irregular exemptions/deduction/reliefs given to individuals	465	156.24
d. Incorrect allowance of Business Expenditure	4,255	11,575.09
e. Irregularities in allowing depreciation/business losses/Capital losses	745	3,064.33
f. Incorrect allowance of DTAT relief	37	916.82
<b>C. Income escaping assessments due to errors</b>	<b>2,536</b>	<b>6,939.74</b>
a. Under Special Provisions including MAT/Tonnage Tax etc.	250	498.74
b. Unexplained investments/ cash credits etc.	582	1,160.10
c. Incorrect classification and Computation of Capital Gains	666	240.70
d. Incorrect estimation of arm's length price	306	291.06
e. Error to club income of spouse, minor child etc.	144	237.00
f. Incorrect computation of Income from House Property	83	53.20
g. Incorrect computation of salary income	65	104.67
h. Errors in implementing provisions of TDS/ TCS	440	4,354.27
<b>D. Others</b>	<b>4,426</b>	<b>8,926.64</b>
<b>Total</b>	<b>20,873</b>	<b>44,168.64</b>

## Appendix 2.3 (Reference: Paragraphs 2.4.4)

Category wise details of observations in respect of DPs sent to the Ministry		
Sub category	Cases	Tax Effect (₹ in crore)
<b>A. Quality of assessments</b>	<b>80</b>	<b>1,496.65</b>
a. Arithmetical errors in computation of income and tax	27	97.94
b. Incorrect application of rate of tax, surcharge etc.	34	213.06
c. Non/short levy of interest/penalty for delay in submission of returns, delay in payment of tax etc.	5	4.84
d. Excess or irregular refunds/interest on refunds	6	1,114.40
e. Errors in assessment while giving effect to appellate orders	8	66.41
<b>B. Administration of tax concessions/exemptions/deductions</b>	<b>206</b>	<b>5,578.48</b>
a. Irregular exemptions/deductions/reliefs given to Corporates	52	2,037.22
b. Irregular exemptions/deductions/reliefs given to Trusts/Firms/Societies	5	18.73
c. Irregular exemptions/deductions/reliefs given to individuals	1	0.26
d. Incorrect allowance of Business Expenditure	59	845.82
e. Irregularities in allowing depreciation/business losses/Capital losses	89	2,676.45
<b>C. Income escaping assessment due to errors</b>	<b>94</b>	<b>1,069.68</b>
a. Under special provisions including MAT/Tonnage Tax etc.	24	449.12
b. Incorrect classification and Computation of Capital Gains	11	15.97
c. Incorrect Computation of Income	35	253.11
d. Errors in implementing provisions of TDS/TCS	8	48.49
e. Unexplained investment/ cash credit	3	12.18
f. Incorrect estimation of Arm's Length Price	13	290.81
<b>D. Others</b>	<b>13</b>	<b>235.98</b>
Over charge of tax/interest	13	235.98
<b>Total</b>	<b>393</b>	<b>8,380.79</b>

**Appendix 2.4 (Reference: Paragraph 2.7.2)**

<b>Cases where remedial action has become time barred in FY 2018-19</b>		
<b>State</b>	<b>Audit observations where remedial action became time barred</b>	
	<b>Cases</b>	<b>Tax effect (₹ in crore)</b>
Andhra Pradesh & Telangana	0	0
Assam	0	0
Bihar	104	18.88
Chhattisgarh	19	140.06
Delhi	0	0
Goa	7	0.61
Gujarat	181	110.94
Haryana	173	68.17
Himachal Pradesh	28	2.32
UTs of Jammu & Kashmir; and Ladakh	18	4.12
Jharkhand	16	14.12
Karnataka	9	2.41
Kerala	15	12.98
Madhya Pradesh	49	25.13
Maharashtra	265	364.79
Odisha	144	646.81
Punjab	57	2.55
Rajasthan	21	2.23
Tamil Nadu	314	213.17
UT Chandigarh	15	0.95
Uttarakhand	0	0
Uttar Pradesh	50	18.71
West Bengal	476	588.09
<b>Total</b>	<b>1,961</b>	<b>2,237.04</b>

## Appendix 2.5 (Reference Paragraph 2.9.2)

Details of non-production of records during FY 2016-17 to FY 2018-19					
States	Records requisitioned in FY 2018-19	Records not produced in FY 2018-19	Percentage of records not produced in FY 2018-19	Percentage of records not produced in FY 2017-18	Percentage of records not produced in FY 2016-17
Andhra Pradesh & Telangana	21,087	1,065	5.05	5.26	5.10
Assam	3,618	78	2.16	0.59	0.03
Bihar	2,376	120	5.05	6.81	8.26
Chhattisgarh	3,747	0	0.00	0.30	1.12
Delhi	39,722	3,702	9.32	21.45	18.60
Goa	1,223	29	2.37	2.46	6.01
Gujarat	16,291	368	2.26	2.40	4.14
Haryana	10,008	68	0.68	4.77	0.86
Himachal Pradesh	1,280	20	1.56	5.24	0.00
UTs of Jammu & Kashmir; and Ladakh	722	77	10.66	1.26	0.16
Jharkhand	2,405	35	1.46	2.03	1.45
Karnataka	13,662	397	2.91	5.64	7.10
Kerala	11,446	368	3.22	5.01	3.11
Madhya Pradesh	22,410	840	3.75	11.67	13.85
Maharashtra	89,283	4,335	4.86	8.59	6.80
Odisha	4,940	296	5.99	6.94	9.44
Punjab	7,793	183	2.35	5.08	0.12
Rajasthan	15,971	770	4.82	9.74	7.96
Tamil Nadu	22,337	2,750	12.31	11.38	16.18
UT Chandigarh	3,968	44	1.11	0.06	3.01
Uttarakhand	916	5	0.55	1.56	0.63
Uttar Pradesh	26,808	429	1.60	1.67	3.47
West Bengal	39,417	2,013	5.11	6.49	7.43
<b>Total</b>	<b>3,61,430</b>	<b>17,992</b>	<b>4.98</b>	<b>8.27</b>	<b>8.29</b>

**Appendix 5.1**  
**Legal Provisions**  
**(Reference para 5.4)**

Legal Provisions relating to interest under sections 234A, 234B and 234C and interest on refunds under section 244A are given below:

Section of the Act	Provisions prescribed in the Act
234A(1)	Section 234A of the Act provides for levy of interest on account of default in furnishing return of income at specified rates and for specified time period. As per this section, where the return of income for any assessment year under sub-section (1) or sub-section (4) of section 139 or, in response to notice under sub-section (1) of section 142, is furnished after the due date or, is not furnished, the assessee shall be liable to pay simple interest at the rate of one <i>per cent</i> for every month or part of a month comprised in the period commencing on the date immediately following the due date, and ending on the date of furnishing of the return or, where no return has been furnished, ending on the date of completion of the assessment under section 144 on the amount of tax on the total income determined under section 143(1) and where a regular assessment is made, on the amount of tax on the total income determined under regular assessment as reduced by the amount of advance tax, TDS/TCS, relief of tax allowed under sections 90, 90A and 91 and tax credit available under section 115JAA or 115JD.
234A(3)	Section 234A(3) of the Income Tax Act, 1961, provides that, where the return of income for any assessment year, required by a notice under section 148 or 153A issued after the determination of income under sub-section (1) of section 143 or after the completion of an assessment under sub-section (3) of section 143, is furnished after the expiry of the time allowed under such notice, the assessee shall be liable to pay simple interest at the rate of one <i>per cent</i> for every month or part of a month comprised in the period commencing on the day immediately following the expiry of the time allowed and ending on the date of completion of the reassessment under section 153A on the amount by which the tax on the total income determined on the basis of such reassessment or re-computation exceeds the tax on the total income determined under section 143(1) or on the basis of earlier assessment.
234A(1) read with explanation 3	<i>Explanation 3</i> under sub section 1 provides that where, in relation to an assessment year, an assessment is made for the first time under section 147 or 153A the assessment so made shall be regarded as a regular assessment for the purpose of this section.
234B(1)	Section 234B of the Act provides for levy of interest on account of default in payment of advance tax at specified rates and for specified time period. As per this section, where in any financial year, an assessee who is liable to pay advance tax, has failed to pay such tax or, where the advance tax paid by such assessee is less than ninety <i>per cent</i> of the assessed tax, the assessee shall be liable to pay simple interest at the rate of one <i>per cent</i> for every month or part of a month comprised in the period from the 1 <sup>st</sup> day of April next following such financial year to the date of

determination of total income in regular assessment, on an amount equal to the assessed tax or, as the case may be, on the amount by which the advance tax paid as aforesaid falls short of the assessed tax.

234B(3)	Section 234B(3) of the Income Tax Act, 1961 provides that, where as a result of an order of reassessment under section 147 or 153A, the amount on which interest was payable in respect of shortfall in payment of advance tax for any financial year under sub-section (1) is increased, the assessee shall be liable to pay simple interest at the rate of one <i>per cent</i> for every month or part of a month comprised in the period commencing on the day 1 <sup>st</sup> day of April next following such financial year and ending on the date of the reassessment u/s 147 or 153A (as the case may be), on the amount by which the tax on the total income determined on the basis of the reassessment exceeds the tax on total income determined under regular assessment.
234B(1) read with explanation 2	Explanation 2 under sub section 1 provides that where, in relation to an assessment year, an assessment is made for the first time under section 153A, the assessment so made shall be regarded as a regular assessment for the purpose of this section.
234C	Section 234C of the Act provides for levy of interest on account of default in payment of instalments of advance tax at specified rates and for specified time period. As per this section, where in any financial year, the assessee who is liable to pay advance tax under section 208 of the Act, has failed to pay such tax or, where the instalments of advance tax paid by such assessee is less than the percentage fixed for specified months, then the company shall be liable to pay simple interest at the rate of one <i>per cent</i> for three months on the amount of shortfall.
Interest on refunds under section 244A:	<p>Section 244A of the Act provides for payment of interest on refunds arising due to excess payment of advance tax, Tax Deducted at Source (TDS) or Tax Collected at Source (TCS) at specified rates and for specified time period. Where refund of any amount becomes due to the assessee under this Act, he shall, subject to the provisions of this section, be entitled to receive, in addition to the said amount, simple interest thereon calculated in the following manner:</p> <p>(i) where the refund is out of any tax paid by way of advance tax or treated as paid under section 199, during the financial year immediately preceding the assessment year, such interest shall be calculated at the rate of one-half <i>per cent</i> for every month or part of a month comprised in the period from the 1st day of April of the assessment year to the date on which the refund is granted. Provided that no interest shall be payable if the amount of refund is less than 10 <i>per cent</i> of the tax as determined on regular assessment.</p> <p>(ii) in any other case, such interest shall be calculated at the rate of one-half <i>per cent</i> for every month or part of a month comprised in the period or periods from the date or, as the case may be, dates of payment of the tax or penalty to the date on which the refund is granted.</p>

**Appendix 5.2**  
**State wise Sample Selection<sup>106</sup>**  
**(Reference: paragraph 5.6)**

State/Region	FY 2016-17 (No. of cases)	FY 2017-18 (No. of cases)	FY 2018-19 (No. of cases)	Total (No. of cases)
1	2	3	4	5
Andhra Pradesh & Telangana	226	92	17	335
Bihar	41	20	18	79
Delhi	518	224	79	821
Gujarat	219	142	59	420
Karnataka	470	285	108	863
Kerala	182	92	30	304
Maharashtra	804	572	41	1417
Madhya Pradesh & Chhattisgarh	110	54	55	219
NER <sup>107</sup>	119	33	4	156
Odisha	16	19	10	45
NWR <sup>108</sup>	238	281	33	552
Rajasthan	108	117	17	242
Tamil Nadu	497	440	21	958
Uttar Pradesh	103	81	4	188
West Bengal	263	178		441
<b>Total</b>	<b>3,914</b>	<b>2630</b>	<b>496</b>	<b>7,040</b>

106 For FY 2016-17 & FY 2017-18, the cases processed/completed through AST was selected. For FY 2018-19, the cases processed/completed through ITBA was selected.

107 North Eastern Region

108 North Western Region (comprises Punjab, Haryana, UT-Chandigarh, Jammu & Kashmir & Himachal Pradesh)

### Abbreviations

ACIT	Assistant Commissioner of Income Tax
Act	Income Tax Act, 1961
ALP	Arm's Length Price
AO	Assessing Officer
AOP	Association of Person
AST	Assessment Information System
AY	Assessment Year
CASS	Computer Aided Scrutiny Selection
CBDT	Central Board of Direct Taxes
CCIT	Chief Commissioner of Income Tax
CIT	Commissioner of Income Tax
CIT(A)	Commissioner of Income Tax (Appeals)
CPC	Centralized Processing Centre
CPGRAMS	Centralized Public Grievance Redress and Monitoring System
CSO	Central Statistical Office
CT	Corporation Tax
CVC	Central Vigilance Commission
DGIT (Systems)	Director General of Income Tax (Systems)
DOR	Department of Revenue
DSIR	Department of Scientific and Industrial Research
DT	Direct Taxes
FIR	First Information Report
FY	Financial Year
GDP	Gross Domestic Product
GTR	Gross Tax Receipts
IRLA	Individual Running Ledger Account
IT	Income Tax
ITAT	Income Tax Appellate Tribunal
ITBA	Income Tax Business Application
ITD	Income Tax Department
ITO	Income Tax Officer
ITR/Return	Income Tax Return
JCIT	Joint Commissioner of Income Tax
LTCG	Long term capital Gain
LTCL	Long term capital loss
PAC	Public Accounts Committee
PAN	Permanent Account Number
Pr. CCA	Principal Chief Controller of Accounts
Pr. CCIT	Principal Chief Commissioner of Income Tax
MAT	Minimum Alternate Tax
MOP	Manual of Office Procedure
NMS	Non-filers Monitoring System
ROC	Registrar of Companies
Rules	Income Tax Rules, 1962
TCS	Tax Collected at Source
TDS	Tax Deducted at Source
TP	Transfer Pricing
TPO	Transfer Pricing Officer





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