

**HUNDRED AND NINETY-FOURTH
REPORT**

**PUBLIC ACCOUNTS COMMITTEE
(1983-84)**

(SEVENTH LOK SABHA)

**IRREGULAR ALLOWANCE OF RELIEF IN
RESPECT OF NEWLY ESTABLISHED UNDERTAKINGS**

**MINISTRY OF FINANCE
(DEPARTMENT OF REVENUE)**

[Action Taken on 75th Report (7th Lok Sabha)]



Presented to Lok Sabha on.....

Laid in Rajya Sabha on.....

**LOK SABHA SECRETARIAT
NEW DELHI**

March, 1984/Phalguna, 1905 (Saka)

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Corrigenda to the Hundred and Ninety-Fourth Report of the Public Accounts Committee (Seventh Lok Sabha) on Irregular allowance of relief in respect of newly established undertakings.

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PUBLIC ACCOUNTS COMMITTEE
(1983-84)

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(iv)

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INTRODUCTION

I, the Chairman of the Public Accounts Committee as authorised by the Committee, do present on their behalf this 194th Report on action taken by Government on the recommendations of the Public Accounts Committee contained in their 75th Report (Seventh Lok Sabha) relating to irregular allowance of relief in respect of newly established undertakings.

2. In their 75th Report, the Committee had pointed out that the coverage of cases by Internal Audit Wing in the Department was limited to 'priority' and 'immediate' cases. Even in this limited area, there was a perceptible fall in the cases checked by the Internal Audit. The Committee had desired that the Ministry should have taken an early decision in regard to the projected requirement of additional manpower in the Department. In their reply, the Ministry of Finance have stated that as the present strength of Departmental audit set up is very inadequate, the possibility of some 'priority/minimum' cases remaining undetected cannot be completely eliminated. In this Report, the Committee have expressed surprise that no specific measures have been taken by the Department to strengthen the Internal Audit Wing and the position remains unchanged. The Committee have strongly recommended that a decision on the projected requirement of additional manpower should be taken immediately and the Internal Audit Wing strengthened so as to reduce the chances of mistake in assessment to the barest minimum. The Committee have further emphasised that in addition to quantitative strengthening, there should be qualitative strengthening of the Internal Audit so as to make it more effective to better sub-serve the end in view.

3. The Committee considered and adopted this Report at their sitting held on 13 February, 1984. Minutes of the sitting form Part II of the Report.

4. For facility of reference and convenience, the recommendations and observations of the Committee have been printed in thick type in the body of the Report, and have also been reproduced in a consolidated form in the Appendix to the Report.

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6. The Committee place on record their appreciation or the assistance rendered to them in the matter by the Office of the Comptroller and Auditor General of India.

NEW DELHI;
March 26, 1984
Chaitra 6, 1906(S)

SUNIL MAITRA,
Chairman,
Public Accounts Committee.

CHAPTER I

REPORT

1.1 The Report of the Committee deals with the action taken by Government on the Committee's recommendations and observations contained in their 75th Report (Seventh Lok Sabha) on paragraphs 2.13 (i) & (ii) of the Report of the Comptroller and Auditor General of India for the year 1979-80—Union Government (Civil), Revenue Receipts, Vol. II, Direct Taxes regarding irregular allowance of relief in respect of newly established undertakings.

1.2 The 75th Report which was presented to Lok Sabha on 1 April, 1982 contained 22 recommendations. Action Taken Notes have been received in respect of all the recommendations/observations and these have been broadly categorised as follows :

- (i) Recommendations and observations that have been accepted by Government;

Sl. Nos. 1-4, 6-9, 11, 12, 19 and 20

- (ii) Recommendations and observations which the Committee do not desire to pursue in the light of the replies received from Government;

Sl. Nos. 13, 14, 15, 16, 18

- (iii) Recommendations and observations replies to which have not been accepted by the Committee and which require reiteration; Sl. Nos. Nil.

- (iv) Recommendations and observations in respect of which Government have furnished interim replies;

Sl. Nos. 5, 10, 17, 21 and 22.

1.3 The Committee observe that nearly two years have elapsed since the Seventy-fifth Report was presented to the House. But only interim replies to five of the recommendations have been received. The

Committee desire that final replies to these recommendations should be furnished to them expeditiously after getting the same vetted by Audit.

*Defective working of the Internal Audit Organisation of the Department
Sl. Nos. 14, 15 and 16 (Paragraph Nos. 1.105, 1.106 and 1.107).*

1.4 The committee in their 75th Report while bringing into focus the defective working of the Internal Audit Organisation of the Department had observed :

"The mistake [of the assessing I. T. O. in taking Rs. 2,98,511 as profit instead of loss as indicated by the assessee, and allowing a deduction under Section 80 J to this extent] in this case was attributable to the carelessness of the Income Tax Officer but it remained undetected and was brought to light only by the Receipt Audit. In terms of the existing procedure this case was required to be checked by the Special Audit party but it was not actually checked as the ITO who passed the order failed to include this case in the list of immediate and priority cases for audit to be sent to the IAC (Audit) every month. The officer concerned has been warned to be more careful in future".

1.5 The committee had further noted that "there is an elaborate system of checks by the Internal Audit obtaining in the Department. But the coverage is limited only to 'priority' and 'immediate' cases, with the result that majority of cases unchecked. Thus the mistakes committed at the level of ITOs are not likely to come to notice until the case falls in one of the two categories namely, 'priority' or 'immediate'. Even in this limited area, there is a perceptible fall in the percentage of priority and immediate cases already checked by internal audit. The figure has come down from 81.2% in 1975-76 to 77.1 per cent in 1976-77, 66.3 per cent in 1977-78, 67.5 per cent in 1978-79 and 64.1 per cent in 1979-80. This is obviously an unsatisfactory situation.

1.6 The Committee had desired that the Ministry should take an early decision in regard to the projected requirements of additional manpower.

In their Action Taken Note the Ministry of Finance (Department of Revenue) have stated :

"The Income-tax Officers are under instruction to furnish along with their monthly progress report list of 'immediate' and 'priority'

cases' disposed of by them in a month, in a prescribed form to the Range IAC who is to send the lists to the concerned I.A.C. (Audit) by 15th of the succeeding month. For 'Immediate Audit' cases, as soon as the assessment is completed, the file is to be sent to the Internal Audit Party. While the primary responsibility for correct and timely reporting of priority and immediate audit cases rests with the Income-tax Officers, the audit parties are not to go entirely by the ITOs' lists and are required to verify the correctness of the lists with the references to the Demand and Collection Registers.

It has not been possible to call for explanation of the Officer Incharge of the relevant audit party for not locating this case as he has retired. Considering that the present strength of the Departmental Audit set-up is very inadequate, the possibility of some priority/immediate' cases remaining undetected cannot be completely eliminated."

1.7 Referring to a case in which the mistake committed by an Income Tax Officer had remained undetected in the Department till the same was pointed out by the Receipt Audit, the Committee in their 75th Report (1981-82) had pointed out that the coverage of cases by Internal Audit Wing in the Department was limited only to 'priority' and 'immediate' cases. Even in this limited area, there was a perceptible fall in the cases checked by the Internal Audit as the percentage covered had come down from 81.2% in 1975-76 to 64.1% in 1979-80. Expressing their dissatisfaction with this unsatisfactory situation, the Committee had desired that the Ministry should take an early decision in regard to the projected requirement of additional manpower in the Department. In their reply, the Ministry have simply pointed out that as the present strength of Departmental Audit set up was very inadequate, the possibility of some 'priority/immediate' cases remaining undetected could not be completely eliminated. The Committee are surprised that no specific measures have been taken by the Department to strengthen the Internal Audit Wing and the position remains unchanged even now. The Committee are strongly of the view that there is an urgent need to strengthen the Internal Audit Wing particularly in a revenue earning Department like Income Tax where any extra expenditure incurred in this behalf is certain to be more than compensated by increase in revenue as a result of detection of mistake by the Internal Audit Wing. The Committee, therefore, recommend that a

decision on the projected requirement of additional manpower for the Internal Audit Wing should be taken immediately and the Wing strengthened so as to reduce the chances of mistakes in assessment to the barest minimum.

It is hardly necessary to add that there should be in addition to quantitative strengthening, qualitative strengthening of internal audit so as to make it more effective and better subserve the end in view.

Sample study for devising measures for speedy settlement of audit objections—Sl. No. 19 (Paragraph No. 1.110)

1.8 The Committee in their 75th Report had recommended that the Board should undertake a sample study of the average time taken in disposal of major audit objections in certain selected/difficult charges for devising necessary remedial measures for speedy settlement of audit objections by individual Income Tax Officers/Commissioners.

1.9 The Ministry of Finance (Department of Revenue) in their Action Taken Note have stated :

“.....The sample study was carried out by the Directorate of Organisation and Management Services which has identified the reasons for the delay in settlement of major audit objections. The recommendations of the D. O. M. S. is under consideration and suitable action would be taken to implement the same where found feasible.”

1.10 While the Committee are happy to note that the sample study of the average time taken in disposal of major audit objection in the Income-Tax Department as recommended by the Committee has been carried out by the Directorate of Organisation and Management Services, they are surprised to find that the recommendations of the DOMS are still under consideration. The Committee feel that it should have been possible for the Ministry to take decisions on the recommendations of the DOMS and implement the same by now. The Committee desire that the matter should now be expedited and the Committee informed within a period of 3 months about the recommendations made by the Directorate of Organisation and Management Services and specific action taken by the Ministry on those recommendations.

CHAPTER II

RECOMMENDATIONS/OBSERVATIONS THAT HAVE BEEN ACCEPTED BY GOVERNMENT

Recommendation

Under the provisions of Section 80J of the Income-tax Act, 1961, where the gross total income of an assessee includes any profits and gains derived from a newly established industrial undertaking, the assessee becomes entitled to tax relief in respect of such profits and gains upto six percent per annum of the capital employed in the industrial undertaking in respect of the previous year relevant to the assessment year. The method of computation of capital employed for the purposes of Section 80J is prescribed in Rule 19A of the Income-tax Rules, 1962. According to this Rule, the capital employed in an industrial undertaking would be the value of assets (on the first day of the computation period) of the undertaking less the borrowed moneys and debts owed by the assessee on that day. Unfortunately, the language used in Rule 19A is such that it lends itself to an interpretation, not exactly in consonance with the sections.

The wordings used in Rule 19A suggest that for determining the "capital employed" in an industrial undertaking, the "aggregate of the amounts of borrowed moneys and debts owed by the assessee" has to be deducted from the "aggregate of the amount representing the value of the assetsof the undertaking." Thus, although the assets are relatable only to an undertaking, the borrowed moneys and debts, going strictly by the language of Rule 19A, can be interpreted to mean the entire debts of assessee. Therefore, in cases where an assessee has more than one undertaking, his total debts relatable to all the undertakings are liable for deduction from the assets of the newly established undertaking. Even though such an interpretation would lead to absurdity, the fact remains that the language used in Rule 19A, was susceptible of such interpretation and that plea was in fact raised by the Department before the Bombay High Court in *Indian Oil Corporation vs. ITO*. Apparently the distinctions between the concept of capital employed in an industrial undertaking in contradistinction to the capital

employed by an assessee—admitted by the Ministry to be two distinct concepts—had not been duly considered while framing the Rule.

The Bombay High Court, in the case of *Indian Oil Corporation Ltd. vs. S. Rajagoplan, ITO and others* (92 ITR 241) pointed out the absurd proposition inherent in the scheme of Rule 19A. The Court *inter alia* observed :

“At first look sub-rules (2) and (3) appear to provide that from the aggregate value of the assets of each undertaking the aggregate of the liabilities of assessee shall be deducted. The assessee in this case owns 4 industrial undertakings. The result of such interpretation would be that from the assets of each industrial undertaking the entire borrowings of the assessee in respect of all the industrial undertakings are to be deducted for arriving at the capital employed in an industrial undertaking. On the face of it, this is an absurd proposition. If you want to arrive at the capital employed by an assessee in a particular industrial undertaking, you cannot arrive at it by deducting from the assets of that particular undertaking the liabilities not only of that industrial undertaking, but also of three other industrial undertakings. This is mathematically absurd.

The Bombay High Court had further stated that for a reasonable interpretation of sub-rule (3) the words “in respect of the industrial undertaking in which the capital employed is to be computed” should have been added after the words “borrowed moneys and debts due by the assessee.”

The Committee consider that the Bombay High Court had clearly brought out the drafting error in Rule 19A (3) and the after the judgement had been accepted by the Department as correct interpretation of the legislative intention, the rule should have been suitably amended. The Chairman, Central Board of Direct Taxes admitted in evidence that this was a lapse on the part of the Department and a clarificatory amendment should have been brought forward soon after the IOC case was decided by the Bombay High Court in 1973. In fact, the Committee find that even when Section 80J of the Indian Income tax Act, 1961, was amended in 1980 retrospectively with effect from 1 April, 1972, to incorporate the provisions of rule 19A in the Act itself, the Department

did not take the opportunity of making suitable changes in the wording of Rule 19A for making the meaning clear and unambiguous. Thus, the drafting lacuna in Rule 19(A), which had been adversely commented upon by the Bombay High Court in IOC case was allowed to creep in the amended section 80J as well. The Committee are anguished that the Board should take upon itself the task of implementing correct intent of Parliament through circulars/rules instead of bringing necessary amendments to the law in time before the Parliament. Clearly the attitude of the Board as far as framing of Rule 19A is concerned was negative in so far as the Board admitted that a part of the provision of the Rule was against the Section itself. The Committee disapprove the attitude of the Board and at this stage can only emphasise the need for more care in bringing forward necessary amendments in the main Act or the Rules, whenever authoritative pronouncements are handed down by the Courts in the country and in which it is felt that there have been drafting errors.

[Sl. Nos 1 to 4 (Paras 1.92 to 1.95) of the Appendix II to the 75th Report of the Public Accounts Committee (1981-82) (Seventh Lok Sabha)].

Action Taken

The observation and recommendation made by the Public Accounts Committee have been noted.

[Ministry of finance (Department of Revenue) OM No. 241/2/82-A & PAC II, dated the 31st March, 1983]

Further Information

*(Copy of the opinion of the Ministry of Law
obtained by the Ministry of Finance)*

The question for consideration is the objection raised by the Audit with reference to the amendment of Section 80J by the Finance Act, 1980.

2. Section 80J provides for tax holiday and the mode of computation for the purpose of relief under the said Section is provided by Rule 19A of the Rules framed under the Act. The Bombay High Court in *Indian Oil Corporation Vs. S. Rajagopalan* (92 ITR page 241) while construing Rules 19A (2) and (3) observed that the language employed

in the said rules "appears to provide that from the aggregate value of the assets of each undertaking the aggregate of the liabilities of the assessee shall be deducted". (The assessee in that case owned four industrial undertakings). It was, further observed "that the result of such interpretation would be that from each industrial undertaking the entire borrowings of the assessee in respect of all the industrial undertakings are to be deducted for arriving at the capital employed in an industrial undertaking. On the face of it, this is an absurd proposition." Therefore, the learned judges held that "on a true interpretation of rule 19A, in respect of each undertaking, the liabilities of the assessee in respect of that industrial undertaking only are to be deducted from the aggregate value of the assets from the same industrial undertaking."

3. The judgement of the Bombay High Court was accepted as a reasonable interpretation of the rule though the language of the rule reads otherwise.

Rule 19A (3) was declared as *ultra vires* of the rule making power by various High Courts, as "consequence of which Section 80J of the Act was amended by the Finance Act, 1980."

The relevant amended clauses are II and III of Section 80J. However, the language employed in clauses II and III is same as the language employed in Rules 19A (2) and (3). Since the same language is used while amending Section 80J and incorporating clauses II and III, the Audit raised an objection that while amending Section 80J, the Department should have taken the opportunity to clarify the intention having accepted the judgement of the Bombay High Court referred to above.

4. The objection raised by the Audit appears to be valid. The Department should have clarified the intention while amending section 80J by incorporating clauses II and III having accepted the decision of the Bombay High Court.

Since the matter relates to the Audit objection, JS & LA may kindly see.

Sd/-
(Miss S. V. Maruthi)
Deputy Legal Adviser
10-3-83

JS & LA (Shri P. K. Kartha)

Sd/-P. K. Kartha
14-3-1983

Recommendation

Section 80J bases the tax holiday relief on the "capital employed." In working out this capital employed, Rule 19A (3) provided in effect for the exclusion of borrowed capital. Since the Section itself did not make any distinction between the owned capital and/or the borrowed capital, the Calcutta High Court, in *Century Enka Ltd. Vs. ITO* decided on 29th April, 1976, held that Rule 19A (3) in so far as it directed exclusion of borrowed capital was *ultra-vires*, being beyond the power of the rule-making authority. This view was subsequently followed by Madras, Allahabad, Punjab and Haryana High Courts. The Andhra Pradesh and Madhya Pradesh High Court, however, took an opposite view and upheld Rule 19A (3). The decisions of the former group of High Courts were not accepted by the Board and the Board issued instructions in February 1979 stating that the "adverse decisions were being contested." The Department also directed the ITOs to continue to follow the existing departmental view till such time as an authoritative pronouncement on the subject was available from the Supreme Court, subject to the recovery of tax raised in assessment orders not being enforced within Calcutta, Madras and UP charges. In 1980 the relevant portion of Rule 19A (3) was incorporated in Section 80J itself retrospectively from 1-4-72.

The Calcutta High Court struck down the rule in 1976. The Madras High Court followed that decision in 1977. Apparently it was at that stage that the department had to decide between two courses—either to content these decisions in appeal or to amend the Act to get over the adverse decisions. The department opted for the former course and went in appeal before the Supreme Court. While, however, the matter was pending before the Supreme Court the department, in 1980, proposed a retrospective amendment to the Act to get over the adverse decisions. The Committee cannot but observe that having gone to the Supreme Court, it was not proper for the department to attempt to pre-empt the decision of the highest Court in this manner.

The Committee consider that a retrospective amendment of a substantial nature gives rise to important questions of propriety in so far as it unsettles settled cases and defeats rights acquired in good faith. In this connection, the Committee would recall the observation made in para 10.10 of their 34th Report (1980-81) to the effect that while proposing retrospective legislation Government needs to bear in mind that

it is likely to cause hardship to honest and unsuspecting assesseees and is also apt to adversely affect the credibility of the Government.

The Committee have been given to understand that one of the reasons for proposing retrospective legislation in this case was that "the prospective application of the proposed amendment was estimated to result in substantial loss of revenue." This reasoning appears to be an after thought in so far as the representative of the Central Board of Direct Taxes had testified before the Committee that when the provisions of the Finance Bill, 1980, were being processed no estimate was actually made of the likely loss of revenue if the view taken by certain Courts was ultimately upheld. It is only in answer to the Committee's specific enquiries that the Ministry of Finance have now ascertained that a total amount of Rs. 45. 41 crores had been paid as tax by the assesseees who have been disputing their liability before the appellate authorities during the years 1970-71 to 1979-80. If the Calcutta High Court view were upheld by the Supreme Court only that part of aforementioned amount of tax related to this issue and only in respect of the assessment years 1972-73 to 1979-80 would become refundable. Parliament were not informed that the magnitude of the problem in terms of the revenue was not very substantial for which retrospective amendment was made. The Committee are distressed that for the failure to furnish full facts and figures to the Parliament relevant to a retrospective amendment of a fiscal statute a 'guesstimate' and not correct calculations, easily possible, were made. The Committee consider that Government should avoid proposing retrospective amendment to the Income-tax law unless the drafting error is manifest and the loss of revenue is substantial so as to justify retrospective amendment. Further, such amendment must be made at the earliest opportunity. The Committee urge that the revenue implications should invariably be gone into in such cases and clearly indicated to the Parliament in the legislative proposals in future."

[Sl. Nos. 6 to 9 (Paras 1.97 to 1.100) of Appendix-II to The 75th Report of the Public Accounts Committee (1981-82) (Seventh Lok Sabha)]

Action Taken

The observation made by the Public Accounts Committee have been noted.

[Ministry of Finance (Department of Revenue) OM No. F. No., 241/2/82-A & PAC-II, dated 31st March, 1983]

Recommendation

1.102 The Committee find that tax holiday provisions were introduced in 1965 when Chapter VI A, consisting then of four sections was added to the Income-tax Act and it gave reliefs not by way of rebate of tax at the average rate of tax but as straight deductions from total income. Many more reliefs have since been added and the Chapter now runs from Sections 80 A to 80 VV. The total relief of tax under all these section of Chapter VI A was of the order of Rs. 66 crores in 1977-78. In 1978-79 this figure came to Rs. 53 crores. On an overall view, the reliefs do not appear to be very substantial. A pertinent question that arises is whether the objective of the various tax relief measures aiming at accelerated socio-economic growth had been realised or these provisions have only cluttered the law book. The Committee consider that the need for simplifying the plethora of tax concessions/tax holiday provisions in the light of an extensive study of their precise impact on industrial development is overdue. The Committee therefore recommend that the Special Cell in the CBDT should be forthwith entrusted with this task so that the much needed simplification of the relevant provisions of the Act could be effected as quickly as possible. Such a study may usefully indicate the number of small sector companies and non-MIRP and non-FERA companies who have availed of the tax holiday under Section 80 J and their percentage to the total number of such companies. It would also be worthwhile to attempt a correlation of allowances for export market development and reduction under Section 80 J to see how far new export oriented undertakings are being set up.

[Sl. No. II (Para 1.102) of the Appendix II to the 75th Report of the PAC (1981-82) (7th Lok Sabha)].

Action Taken

- 1.102 (i) the impact of several reliefs in Chapter VIA have been considered and suitable amendments have been brought about by the Finance Act, 1983
- (ii) export market development allowance under section 35B has been drastically changed by Finance Act 1983; and
- (iii) recommendations regarding simplification will be kept in view when the Government implements the recommendations of the EARC.

[Ministry of Finance (Department of Revenue) OM No. F 241/2/82 A & PAC-II dated 4-10-83].

Recommendation

In this connection, the Committee are surprised to note that the statistical data given in the departmental publication entitled "All India Income-tax Statistics" has been found to be incorrect and unreliable. During the year 1979-80, 458 assesses are stated to have claimed a total deduction of Rs. 6.50 crores under Section 80J on which tax relief amounting to Rs. 3.70 crores was given. The Dandekar Committee which had collected information on the revenue cost of tax holiday, had however estimated that the loss of income-tax every year under Section 80J would be of the order of Rs. 20 crores. Explaining the wide variation between the two sets of statistics, it was stated that the Director of Inspection who was responsible for compiling the All India Income-tax Statistics, had to compile the statistics from the assessment forms, which were never checked whereas the Dandekar Committee statistics had been collected on a census basis. As it transpires on a recheck, both the figures have been found to be erroneous. It was admitted that the present system under which assessment forms numbering several lakhs are being received from a wide network of assessment officers, not only suffers from some inherent deficiencies but has also developed certain unavoidable delays and other shortcomings over the years. The fact stands out the methodology adopted for collection of statistical information needs to be rectified urgently not only in the interest of credibility of the Department itself but also for purposes of future planning and legislation. The Committee cannot, therefore, emphasise too strongly the need for devising a statistical system which fully takes into account the inherent features of tax administration and which simultaneously provides for expedition in collection, tabulation and publication of the statistical data. The Committee are doubtful if the new scheme of collection of income tax statistics based on "returned income" proposed to be introduced w.e.f. 1st April, 1982 would fully take care of these imperatives with the present paucity of staff. The Committee note that the Board have also agreed in principle to acquire an appropriate computer system for meeting the urgent demands for data processing. The Committee expect that the matter would be expedited and advance action also taken to provide training for the personnel needed for the purpose.

[Sl. No. 12 (Para 1.103 of Appendix II to the 75th Report of the Public Accounts Committee 1981-82)].

Action Taken

The views expressed by the Hon'ble Committee have been noted by the Ministry. As has been conceded, the present infra-structure of the organisation for collecting statistics would require review and removal of certain deficiencies. The Ministry is seized of the matter. While the Committee's apprehension that the new scheme of collection of Income-tax statistics based on returned income has not fully taken care of these imperatives with the present paucity of staff has been noted, it would be the Ministry's effort to try to improve the working of the Directorate within the limited man-power and resources available. As has been noted in the report, the computerisation of the information service has been accepted in principle, but the acquisition of computers for statistical work has been deferred pending the preparation of a feasibility report about an integrated computer system for the Income-tax Department as a whole, by Computer Management Corporation of Department of Electronics.

[Ministry of Finance (Department of Revenue) OM No. F 241/2/82
A & PAC-II dated 15th March, 1983].

Recommendation

The Committee consider that much more attention needs to be paid to the speedy settlement of audit objection by individual Income Tax Officers/Commissioners. The Board should, therefore, undertake a sample study of the average time taken in disposal of major audit objections in certain selected/difficult charges for devising necessary remedial measures.

[Sl. No. 19 (Para 1.110 of Appendix II to the 75th Report of P.A.C.
(1981-82)].

Action Taken

The sample study recommended by the Honourable Committee has been entrusted to the Directorate of O. & M. Services. The Committee would be informed as soon as the sample study is completed.

[Ministry of Finance (Department of Revenue) OM No. F.
241/2/82-A & PAC-II dated 18th June, 1982)].

Further Information

The sample study was carried out by the Directorate of Organisation and Management Services which has identified the reasons for the delay in settlement of major audit objections. The recommendations of the D. O. M. S. is under consideration and suitable action would be taken to implement the same where found feasible.

[Ministry of Finance (Department of Revenue) OM No. F. 241/2/82-A & PAC-II dated 14, Dec., 1982].

Recommendation

During evidence before the Committee the Chairman of the Central Board of Direct Taxes reiterated the plea of overall shortage of staff in the Income-tax department. In Para 8.27 of their 34th Report (1980-81) the Committee have already recommended that the complaint of the department about its being understaffed should be properly evaluated and that in a revenue earning department Government should not labour under a false sense of economy in not providing adequate manpower if it is needed to optimise speed and efficiency. The figures of requirements of additional staff quoted before the Committee, however, varied so widely, from 3,500 to 10,000, that the Committee could not but feel that the Income-tax departments computation of their needs were more in the nature of bargaining rather than being based on any scientific study of the requirements. As the Finance Secretary stated during evidence, one of the material factors for assessing the requirements of staff in the Income-tax department is the number of assessees. According to the budget speech of the Finance Minister (1981-82) the effect of the raising of the exemption limit of tax from 1981-82 would be that "about 14 lakhs of tax payers will go out of the tax net." This same figure has been mentioned against the para 6.20 of the Economic Survey, 1981-82 issued by the Government of India in February 1982. The Committee consider that it was patently wrong on the part of the Chairman, Central Board of Direct Taxes, to not only belittle the statement but also to say that the impression that 14 lakhs of assessees were going out of the tax net was, to his mind, a wrong impression. Apart from that, it is an admitted fact that the strength of the officers in the Income-tax department has been raised substantially in recent years. The cost of collection of direct taxes is almost 2% as against less than 1/2 percent for indirect taxes. Over 90 percent of the collections from income-tax and corporation tax

are paid directly by the assesseees by way of advance tax or deductions at source or payment on the basis of self-assessment and the collections on the basis of regular assessments made by the Income-tax department represent under 9 percent of the total collections. As may as 75 percent of the assessments were completed as summary assessments during the year 1979-80, and the scope of summary assessments has been enlarged still further thereafter. While, therefore, reiterating their recommendation that the justified requirements of additional manpower in the income-tax department should be met, the Committee would also like to sound a word of caution and suggest that the number of assesseees as well as the various other factors mentioned above, should be duly taken into account and a proper scientific study made of actual requirements of additional manpower for efficient functioning of the department.

[Sl. No. 20 (Para 1.111) of Appendix-II to the 75th Report of the P.A.C. (1981-82)].

Action Taken

The recommendation of the Public Accounts Committee that while the justified requirements of additional manpower in the Income-tax Department should be met, factors such as the number of assesseees etc. should be duly taken into account and a proper scientific study be made of actual requirement of additional manpower for efficient function of Department, has been noted. For the purpose of assessment of the requirement of officers and staff of the Department to ensure its functioning efficiently, Government have set up a separate organisation known as the Directorate of Organisation and Management Service (Income-tax). This Directorate has been regularly conducting work measurement studies to determine the functional requirements of manpower of the Department in various areas of cooperation and their recommendation are often subjected to further scrutiny by the Staff Inspection Unit of the Department of Expenditure. Invariably, in such studies, factors such as the number of assesseees, collection by way of advance tax self-assessment and tax deducted at source, the scope of summary assessment etc. are duly taken into account. Similarly, while sanctioning additional manpower, considerations of economy in expenditure are also kept in view.

[Ministry of Finance (Department of Revenue) OM No. F. No. 241/2/82—A & PAC-II dated 20th October 1982].

CHAPTER III

RECOMMENDATIONS/OBSERVATIONS WHICH THE COMMITTEE DO NOT DESIRE TO PURSUE IN VIEW OF THE REPLIES RECEIVED FROM GOVERNMENT.

Recommendation

The Committee recommend that the All India Income-tax Statistics published by the Department every year should be laid on the Table of both the Houses of Parliament.

[Sl. No. 13 (Para 1.104) of Appendix II to the 75th Report of the Public Account's Committee (1981-82) (7th Lok Sabha)].

Action Taken

The presentation of the statistics in the All India Income-tax Statistics has been fairly uniform for the last several years except for some marginal modifications. The latest issue relating to Financial Year 1979-80 carries the following tables :

Details of Tables

<i>Table No.</i>	<i>Description</i>
1.1	Demand, Collection and Arrears of Income-tax
1.2	Distribution of Arrears of Income-tax—By range of tax in arrears.
2.	Summary of Net collection of Income tax & Corporation Tax.
3.1	Number of assessments, gross income and gross tax—By source of income.
3.2	Deductions, rebates and reliefs—By nature deduction etc.
3.3	Double income-tax relief.
3.4	Tax deducted or otherwise paid at source—by source of income.

4. Number of assessments, gross income and gross tax from Business and Profession for Companies and Non-companies—By nature of industry.
5. Number of assessments, income assessed and tax demand—By status and range of net income.
6. Number of assessments and net income—By status and range of net income.
7. Number of assessments, gross income and gross tax—By source, range of income and status.
8. Number of assessments of individuals break-up of income assessed and tax payable—By range of income assessed and status.
9. Number of assessments, income assessed and tax demand by Companies—By range of income assessed and Nature of Company.
10. Number of assessments, income from Capital Gains and gross tax thereon—By range of Capital Gains Income.
11. Number of assessments, gross income, losses set off, deductions and net income—by range of income assessed.

The All India Income Tax Statistics is an annual publication compiled from the assessment forms ITNS-150 and 150-A relating to original assessment made during a financial year and received by the Director of Inspection (Research, statistics and Public Relations) for data processing except that the data relating to Tables 1.1 and 1.2 are based on the original quarterly statements of income-tax demand in arrears as received from the Commissioners of Income-tax by the Managerial Statistics Division of the Director of Inspection (Research, Statistics and Public Relations). The data for table 2 is received from the Chief Controller of Accounts, Central Board of Direct Taxes.

2. The Director of Inspection (Research, Statistics and Public Relations) who compiles the statistical data for the Income-tax Department has stated that the commitment to place the All India Income-Tax Statistics on the Table of the House would perhaps mean a great restriction for the following reasons :—

- (a) The statistics cannot be released till they have been placed on the Table of the House.

- (b) It would also mean that till the statistics are placed on the Table of the House the data cannot be used even within the Department or the Ministry for considering any changes in fiscal policy.

As it is, the statistical publications are already being sent to the Parliament's Library. They can in future be sent to the library immediately following the publication.

3. This issues with the approval of the Minister.

[Ministry of Finance (Department of Revenue) OM No. F. 241/2/82
A & PAC-II, dated 15th March, 1983].

Recommendations

1.105 In paragraph 2.13 (ii) of the Audit Report, the Audit had brought out a case where in the statement claiming relief under Section 80 J, the assessee (M/s. Brooke Bond India Ltd.) had indicated a loss of Rs. 2,98,511 in a new unit but the assessing ITO had taken this figure as profit and allowed a deduction under Section 80 J to this extent. In this particular case although there was no loss of revenue, it nevertheless brings into focus the defective working of the Internal Audit organisation of the Department.

1.106 The mistake in this case was attributable to the carelessness of the Income Tax Officer but it remained undetected and was brought to light only by the Receipt Audit. In terms of the existing procedure this case was required to be checked by the Special Audit party but it was not actually checked as the ITO who passed the order failed to include this case in the list of immediate and priority cases for audit to be sent to the IAC (Audit) every month. The officer concerned has been warned to be more careful in future.

1.107 The Committee find that there is an elaborate system of checks by the Internal Audit obtaining in the Department. But the coverage is limited only to 'priority' and 'immediate' cases, with the result that majority of cases go unchecked. Thus the mistakes committed at the level of ITOs are not likely to come to notice until the case falls in one of the two categories namely, "priority" or 'immediate'. Even in this limited area, there is a perceptible fall in the percentage of priority and immediate cases already checked by internal audit. The figure has

come down from 81.2% in 1975-76 to 77.1 percent in 1976-77, 66.3 percent in 1977-78, 67.5 percent in 1978-79 and 64.1 percent in 1979-80. This is obviously an unsatisfactory situation.

1.109 The Committee note that a new post of Director of Inspection (Audit) has been created to look after audit work exclusively to enable him to concentrate on audit work only. All IACs (Audit) ITOs (Internal Audit) and Chief Auditors will be placed under his direct control. The Committee trust that unification of control of the internal audit department under an officer responsible directly to the Board would help to tone up the efficiency of the system and provide the much needed concurrent check over of recurring cases of loss of huge amounts of revenue due to the Government.

[Sl. Nos. 14, 15, 16 and 18 (Paras 1.105, 1.106, 1.107, and 1.109) of the Appendix II to the 75th Report of the Public Accounts Committee (1981-82) (Seventh Lok Sabha)].

Action Taken

The Income-tax Officers are under instruction to furnish along with their monthly process report list of 'immediate' and 'priority cases' disposed of by them in a month, in a prescribed form to the range IAC who is to send the lists to the concerned I. A. C. (Audit) by 15th of the succeeding month. For 'Immediate Audit' cases, as soon as the assessment is completed, the file is to be sent to the Internal Audit Party.

2. While the primary responsibility for correct and timely reporting of priority and immediate audit cases rests with the Income-tax Officers, the audit parties are not to go entirely by the ITOs' lists and are required to verify the correctness of the lists with reference to the Demand and Collection Registers.

3. It has not been possible to call for explanation of the Officer Incharge of the relevant audit party for not locating this case as he has retired. Considering that the present strength of the Departmental Audit set-up is very inadequate, the possibility of some 'priority/immediate' cases remaining undetected cannot be completely eliminated.

4. Kind attention of the Hon'ble Committee is invited to this Ministry's reply dated 6-11-82 to para 1.108 of this Report. Various steps to reorganise and strengthen the Internal Audit Organisation are being taken. As soon as the reorganisation is complete, the Committee will be informed of the details thereof.

[Ministry of Finance (Deptt of Revenue) OM No. F 241/2/82—
A & PAC-II dated 28-1-83].

CHAPTER IV
RECOMMENDATIONS/OBSERVATION REPLIES TO
WHICH HAVE NOT BEEN ACCEPTED BY THE
COMMITTEE AND WHICH REQUIRE
REITERATION

NIL

CHAPTER V

RECOMMENDATIONS/OBSERVATIONS IN RESPECT OF WHICH GOVERNMENT HAVE FURNISHED INTERIM REPLIES

Recommendation

1·96 The interpretation placed by the Bombay High Court on the provisions of Rule 19A (3) to the effect that what was to be deducted in the computation of capital employed in the industrial undertaking was the aggregate amount on the borrowed moneys and debts owed by the assessee, was accepted by the Board and an instruction to that effect was issued on 25th March, 1976. The Committee would recommend that when such instructions are issued by the Board to the field staff following the judgement of a Court given a particular interpretation, the instructions should be suitably embodied in a public notice for the information and guidance of the general public. The wordings of Rule 19A (3) have been embodied in Section 80J without making any change and without explicitly adding the words "in respect of the industrial undertaking in which the capital employed is to be computed" implied by the Bombay High Court and the Ministry of Finance have expressed an opinion during evidence that the Bombay High Court decision "would be very much applicable" to the provision made in the Section also. The Committee would therefore, recommend that a suitable public notice bringing out this position should be issued even now.

1·101 The Committee find that 987 assesseees in the corporate sector and 355 assesseees in the non-corporate sector have claimed relief under section 80J but have paid the disputed tax amounting to Rs. 44·49 crores and Rs. 0·92 crore respectively during the period 1970—80. The number of assesseees who have not paid the disputed tax since 1970 is 748 in the corporate sector and 177 in the non-corporate sector and the amount of disputed tax is Rs. 65·52 crores and Rs. 1·08 crores respectively. The matter being sub-judice, the Committee would not like to express any opinion on the issues involved in the cases before the Supreme Court. The Committee would however like to be informed of

the decision of the Supreme Court and its implications in regard to the relief admissible under section 80J.

[Sl. No. 5, 10 (Paras 1·96 & 1·101) of the Appendix II to the 75th Report of the PAC (1981-82) (7th Lok Sabha)]

Action Taken

The matter is under consideration.

Under section 80 (J) of the Income-tax Act, 1961, a deduction is allowed in computing the taxable income at the rate of 6% per annum on the capital employed in the industrial undertaking or ship or business of the hotel. The manner of computation of the capital for this purpose was given in Rule 19A of the Income-tax Rules. Clause (3) of Rule 19A provided that borrowed money and debts owed by the assessee shall be deducted from the capital computed for this purpose.

Some of the High Courts have held that this Rule is ultra vires of the section in the Act. Section 80 (J) was, therefore, amended by Finance Act, 1980 (No. 2) with retrospective effect from 1.4.72, incorporating into the section the provisions that were contained in the Rule.

Some assesseees have challenged that :—

- (1) the Rule 19A (3) is beyond the scope of section 80 (J) of the I.T. Act; and
- (2) the amendment of section 80(J) incorporating the provisions of the Rule in the section with retrospective effect from 1.4.72 is constitutionally not valid.

The Supreme Court has heard the case on the issue whether Rule 19A (3) is beyond the scope of Section 80(J) of the Act or not. The judgment of the court is awaited.

Perhaps the Court would like to hear also on the question of validity of the retrospective amendment of Section 80(J). The Department has been reminding the Central Government Advocate in the Supreme Court to have the proceedings before the Supreme Court expedited.

[Ministry of Finance (Deptt. of Revenue) OM No. of F 241/2/82
A & PAC II dated 4/10/83]

Recommendation

The Committee have been informed that the Department is fully aware of the need for strengthening of the internal audit organisation but the Department's efforts to secure additional manpower have not yet fruited. The Committee desire that keeping in view the importance of a streamlined system of internal audit, the Ministry of Finance should take an early decision in regard to the projected requirements of additional manpower. The results of the steps taken in this direction may be communicated to the Committee.

[S. No. 17 (Para 1.108 of Appendix-II to the 75th Report of P.A.C. (1981-82) (7th Lak Sabha)]

Action Taken

The observations of the Committee have been noted. The proposal for augmenting the strength of officers and staff for Internal Audit Work is under active consideration of the Government.

[Ministry of Finance (Dept. of Revenue) OM No. F 241/2/82 A & PAC II dated 6th November 1982]

Recommendation

The Committee are surprised to find that a comprehensive census of assets and liabilities of foreign companies has not been carried out since December 1961 and Government have had to rely only on the annual reports filed by enterprises having foreign investment. It has been realised that "with the coming into force of the Foreign Exchange Regulations Act, 1974 (FERA) prescribing maximum foreign shareholding for different kinds of enterprises, the annual reporting by enterprises has become increasingly unsatisfactory with the result that reasonably reliable data on outstanding foreign investment have not become available for the period subsequent to 1976."

The Committee have been informed that since the FERA marks a watershed in the area of our foreign investment policy, a full census of the country's foreign assets and liabilities which would provide benchmark data for preparation of annual estimates for subsequent years, would now be undertaken by the Economic Department of the Reserve Bank of India with March 31, 1981 as the reference data. The

statement given in Appendix I gives the names of 172 Companies which applied under action 29 of the Foreign Exchange Regulations Act, 1973 and in which non-resident interest is presently more than 40 percent. The Committee observe that the total paid-up capital of such companies amounted to Rs. 552.50 crores of which the capital held by non-resident's amounted to Rs. 313.04 crores. 13 of these Companies still have 90 to 100 percent non-resident holding while as many as 21 have non-resident holding between 70 percent and 90 percent. The Committee have been further, informed that the Reserve Bank is presently engaged in a study of FERA companies with a view to ascertaining the impact of FERA process, impact on the capital market and on the inward and outward flow of remittances. The Committee would suggest that Parliament be apprised of the findings of the above study, the measures taken to improve the data base with regard to the operations of FERA companies and the efforts made to dilute the extent of share holding there in by non-residents in keeping with the objectives of the statute.

[Sl. Nos. 21 & 22 (Paras 1.112 and 1.113 of Appendix-II to the 75th Report of the PAC (1981-82)]

Action Taken

The Reserve Bank of India has informed the Department of Economic Affairs that the FERA study will take some more time for finalisation.

Further Information

Department of Economic Affairs have further informed that the Reserve Bank of India has commenced work relating to collection of data etc. They are making every effort to complete the study as early as possible. However, they will require quite some time to collect and analyse the massive data in respect of more than 700 companies and to finalise their report.

[Ministry of Finance (Deptt. of Revenue) O'M No. F 241/2/82 A & PAC-II dt 20th Oct. 1982]

NEW DELHI ;
March 26, 1984.
Chaitra 6, 1906 (S)

SUNIL MAITRA,
Chairman,
Public Accounts Committee.

APPENDIX

Recommendations/Observations

Sr. No.	Para No.	Ministry/Deptt. Concerned	Recommendations/Observations
1	2	3	4
1.	1.3	Ministry of Finance (Deptt. of Revenue)	1.3 The Committee observe that nearly two years have elapsed since the Seventy-fifth Report was presented to the House. But only interium replies to five of the recommendations have been received. The Committee desire that final replies to these recommendations should be furnished to them expeditiously after getting the same vetted by Audit.
2.	1.7	—do—	1.7 Referring to a case in which the mistake committed by an Income Tax Officer had remained undetected in the Department till the same was pointed out by the Receipt Audit, the Committee in their 75th Report (1981-82) had pointed out that the coverage of cases by Internal Audit Wing in the Department was limited only to 'priority' and 'immediate' cases. Even in this limited area, there was a perceptible fall in the cases checked by the Internal Audit as the percentage covered had come down from 81.2% in 1975-76 to 64.1% in 1979-80. Expressing their

dissatisfaction with this unsatisfactory situation, the Committee had desired that the Ministry should take an early decision in regard to the projected requirement of additional man power in the Department. In their reply, the Ministry have simply pointed out that as the present strength of Departmental Audit set up was very inadequate, the possibility of some 'priority/immediate' cases remaining undetected could not be completely eliminated. The Committee are surprised that no specific measures have been taken by the Department to strengthen the Internal Audit Wing and the position remains unchanged even now. The Committee are strongly of the view that there is an urgent need to strengthen the Internal Audit Wing particularly in a revenue earning Department like Income Tax where any extra expenditure incurred in this behalf is certain to be more than compensated by increase in revenue as a result of detection of mistakes by the Internal Audit Wing. The Committee, therefore, recommend that a decision on the projected requirement of additional man power for the Internal Audit Wing should be taken immediately and the Wing strengthened so as to reduce the chances of mistakes in assessment to the barest minimum.

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It is hardly necessary to add that there should be, in addition to quantitative strengthening, qualitative strengthening of internal audit so as to make it more effective and better subserve the end in view.

**3. 1.10 Ministry of Finance
(Deptt. of Revenue)**

1.10 While the Committee are happy to note that the sample study of the average time taken in disposal of major audit objection in the Income-Tax Department as recommended by the Committee has been carried out by the Directorate of Organisation and Management Services, they are

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surprised to find that the recommendations of the DOMS are still under consideration. The Committee feel that it should have been possible for the Ministry to take decisions on the recommendations of the DOMS and implement the same by now. The Committee desire that the matter should now be expedited and the Committee informed within a period of 3 months about the recommendations made by the Directorate of Organisation and Management Services and specific action taken by the Ministry on those recommendations.

PART II

MINUTES OF THE SIXTY-SIXTH SITTING OF THE PUBLIC ACCOUNTS COMMITTEE HELD ON 20 MARCH, 1984 (AN)

The Public Accounts Committee sat from 1500 hrs. to 17 20 hrs.

PRESENT

Lok Sabha

1. Shri Bhiku Ram Jain *In the Chair*
2. Shri Chitta Basu
3. Smt. Vidyavati Chaturvedi
4. Shri G. L. Dogra
5. Shri Jamilur Rahman

Rajya Sabha

6. Shri Syed Rahmat Ali
7. Smt. Pratibha Singh

REPRESENTATIVES OF THE OFFICE OF THE C & AG

1. Shri R. K. Chandrasekharan *Addl. Dy. C & AB of India
(Reports)*
2. Shri S. R. Mukerjee *Addl. Dy. C & AB of India
(Railways)*
3. Shri K. N. Row *Director of Audit, Defence
Services*
4. Shri A. N. Biswas *Director of Audit P & T*
5. Shri V. Sundaresan *Director of Receipt Audit-I*
6. Shri N. Shivasubramanian *Director of Receipt Audit-II*

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|-----------------------------|--|
| 7. Shri A. N. Mukhopadhyay | <i>Jt. Director
(Report-Central)</i> |
| 8. Shri K. H. Chaya | <i>Jt. Director
(Railways)</i> |
| 9. Shri S. K. Gupta | <i>Jt. Director
(Receipt-Audit)</i> |
| 10. Shri N. R. Rayalu | <i>Jt. Director
(Defence)</i> |
| 11. Shri T. G. Srinivasan | <i>Jt. Director of Audit, P & T</i> |
| 12. Shri N. Balasubramaniam | <i>Jt. Director
(Receipt Audit)</i> |
| 13. Shri R. S. Gupta | <i>Jt. Director of Audit, Defence
Services</i> |

SECRETARIAT

- | | |
|----------------------|---|
| 1. Shri H. S. Kohli | <i>Chief Financial committee
Officer</i> |
| 2. Shri K. K. Sharma | <i>Senior Financial Committee
Officer</i> |
| 3. Shri K. P. Singh | <i>Senior Financial Committee
Officer</i> |
| 4. Shri R. C. Anand | <i>Senior Financial Committee
Officer</i> |
| 5. Shri K. Sahai | <i>Senior Financial Committee
Officer</i> |

2. In the absence of the Chairman, PAC, Shri Bhiku Ram Jain, was chosen to act as Chairman for the sitting.

3. The Committee considered the following draft Report and adopted the same with certain modifications/amendments as shown in Annexure.

1 * * * * *

Action Taken on 75th Report of PAC (7th Lok Sabha) on Direct Taxes—Irregular allowance of relief in respect of newly established undertakings.

* * *

The Committee also authorised the Chairman to finalise the Reports in the light of modifications/amendments suggested by Audit as a result of factual verification and present the same to the House.

The Committee then adjourned.

ANNEXURE

Amendment/modification made by the Public Accounts Committee in the Draft Report on Action Taken on the recommendations contained in 75th Report (7th Lok Sabha) relating to irregular allowance of relief in respect of newly established undertakings.

<i>Page</i>	<i>Para</i>	<i>Amendment/Modification</i>
5	1.7	<i>Add at the end :</i> "It is hardly necessary to add that there should be, in addition to quantitative strengthening, qualitative strengthening of internal audit so as to it make more effective and better subserve the end in view."
