

# Executive Summary

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An aggrieved tax payer has the right to dispute a tax demand with the Income Tax Department through the Commissioner of Income Tax (Appeals). Second appeal against the orders of CIT (A) lies in the Income Tax Appellate Tribunal (ITAT) which functions under the Ministry of Law. On any question of law arising out of an order of ITAT, a taxpayer may appeal progressively to the High Court and the Supreme Court. Analogous right to appeal is also available to the Department against the orders of CIT (A) and onwards.

The dimensions of disputes in income tax are staggering. Rs 2.2 lakh crore is the amount locked up in appeals at various levels, which can almost wipe off the revenue deficit of the Union Government in 2008-09. On an average, 48 *per cent* of tax demands remain uncollected and disputes account for 45 *per cent* of uncollected demands. These factors, we felt, merited a performance evaluation of the appeal process. This is the first time we have attempted a holistic study of appeals. The topic was also suggested by the Central Board of Direct Taxes (Board) during our consultations on areas of concern in the Department.

In our study covering the period 2006-09, we sought an assurance that the processes ensure speedy resolution of disputes; they also identify litigious provisions in the Act for correction; the decisions for escalation of disputes to higher levels in the appellate hierarchy are based on a fair assessment of cost-benefit; the appeals are filed by the Department within the prescribed timeframe to avoid dismissal due to limitation; and the appellate orders are implemented accurately and timely to avoid inconvenience to the taxpayer as well as avoidable payment of interest.

We worked with several constraints. The absence of a centralised database on appeals at the State level, hampered the selection of the audit samples. We, therefore, had to examine individual assessment records for the selection, which considerably strained our audit plan. Poor maintenance of records across the assessment and judicial wings of the Department, is an area of concern. Non-production of records was a major constraint as well as concern. The Department produced only 49 *per cent* of the records we requisitioned for audit; it was as low as 5 *per cent* in the case of Delhi Office.

We found that despite a steady reduction in number of appeals preferred to CsIT (A), the inventory of appeals with CsIT (A) was building up because of low disposal of appeals. The disposal of appeals was 1/3<sup>rd</sup> of the targeted level and at the current levels of disposal, the CsIT(A) would take 2.4 years to clear the inventory. The average time taken for disposal of a case by CIT (A) is 14 months, which is substantially longer than the international standards. Low-end appeals (with demand of less than Rs. 1 lakh) constituted 66 *per cent* of the total appeals. The assessment process evidently is unable to satisfy the small taxpayer, the category of taxpayers which is least equipped

to bear the cost of litigation. This must be viewed with the fact that the success rate of the Department at various levels of appeals is low and appeals go decidedly in favour of the taxpayers.

There are some provisions in the Act (like imposition of penalty) that lead to disputes. Deviations from prescribed procedures by the assessing officers (AOs) have also contributed to disputes. We find that there is a tendency to escalate the disputes to higher levels even in cases where the Department is on a weak ground, which strains the system and the resources besides causing inconvenience to the taxpayer. On the other hand, we also found instances of inaction in such cases where a second appeal would have safeguarded revenue. There is lack of consistency while considering a case for second appeal; divergent actions weakening the departmental stand in appeals. The absence of independent evaluation of decisions for escalation creates unchecked avenues for arbitrary exercise of discretionary powers by the AOs.

One of our biggest concerns is the lack of credible and reliable data on the volume and impact of appeals. Widely divergent data is compiled by different sources which have not been subjected to reconciliation. Records to monitor filing of appeals and implementation of appellate orders were not maintained properly in the assessment units. Inadequate controls led to time barring of appeals and delays in implementation of appellate orders. AO's work on appeals is not subjected to internal audit, denying the process an independent appraisal.

We feel that implementation of appellate orders is placed low in the AOs' priorities. Inadequate attention on correctness in implementation of appellate orders, led to mistakes amounting to Rs. 1,456 crore in 385 cases. 97 *per cent* of these mistakes in implementation led to under-assessment of tax benefitting the tax payer, which raises doubts on the integrity of the process.