

Executive Summary

A taxpayer becomes eligible for a refund if the tax paid by him was higher than the tax due in the year. The refund process gets initiated with the claim contained in the annual tax returns submitted by the taxpayer, which is then examined by the assessing officer for eligibility. The claim is finally disposed when the refund voucher is prepared and issued to the assessee through the authorized banks.

Timely disposal of refund claims is a key measure of the operational efficiency of tax administration. Prompt refunds instill confidence among taxpayers and increase tax compliance. Automation was aimed to speed up the disposal and thus reduce the pendency of claims.

We conducted performance review of income tax refunds processed during 2005-06 to 2008-09 in order to seek an assurance that the systems and procedures were geared towards timely and accurate processing of refund claims and that internal controls provide for effective monitoring. While the department largely cooperated with our efforts, access to records was a major constraint with the department not producing 20 *per cent* of the records asked for by us.

In our review we found procedural irregularities in refunds aggregating Rs. 5803.5 crore; the tax effect of erroneous refunds being Rs. 135.8 crore.

Incidence of tax refunds measured by refunds as a percentage of gross tax collections, showed a declining trend during the period 2005-09, which reflects streamlining of the tax assessment process. Despite automation, the pendency rate of refund claims showed an upward trend. Our analysis showed that increase in interest outflows on refunds was mainly on account of delays in processing than due to increase in the volume of refunds. The recent initiative of the Department to establish the Central Processing Centre (CPC) at Bengaluru, is aimed to reduce the pendency.

Interest on belated refunds of excess tax is being incorrectly accounted as reduction of revenue instead of being correctly budgeted as an expenditure item. The incorrect accounting practice also leads to interest payments escaping legislative scrutiny despite being a charge on the Consolidated Fund of India and needs to be rectified.

We reviewed the checks and controls in the system for ensuring accuracy of the refund advice. The computerised systems are yet to stabilize. Although automation allows online verification of tax credits claimed by the assesseees, the high incidence of credits that could not be matched with the PAN of the assesseees (called OLTAS suspense) has rendered such verification difficult. The

Assessment Information Systems (AST) is being used mainly for summary assessment. Even so, the system controls do not ensure that refunds granted through summary assessments were adjusted while processing subsequent refunds. We also found cases of excess payment of interest on refunds.

Till such time that the computerised systems stabilise, continuance of manual systems of control become inevitable. We, however, noticed that maintenance of the manual registers was unsatisfactory and the supervisory controls were ineffective.

We have evaluated the timeliness in processing of refunds particularly of small taxpayers. The departmental target of settling refund claims within 4-6 months is much longer than international standards which range from 24 days to six weeks. Our analysis showed that the average time taken for processing of refund claims leading to issue of refund vouchers is 10 months. The average time taken for the assessee to receive the refund voucher after its issue is 40 days. In 2007-08 the taxpayer received the refund in 12 months after he submitted the claim. This inconveniences the taxpayer considerably, particularly the senior citizens whose refunds, the department claims, have been put on fast track with an assurance for on-the-spot settlement. We found that the average time taken for receipt of refund by a senior citizen was 12 months after filing of return.

The delays in processing of high value refunds were akin to that of low value refunds, with bottlenecks at various stages. The impact of delays in high value refunds is many fold: taxpayer inconvenience; both cost to the assessee and the monetary loss suffered by Government on account of interest payments is higher in high value refunds; the distortion of tax collections due to pending high value refunds, is also higher. The Refund Banker Scheme, which is in a pilot stage, has had a good impact on stemming delays in payment (i.e., stage after the refund voucher is issued).

During the exit conference, the Ministry accepted the audit recommendations and agreed to address the issues brought out in the report.