



CHAPTER 1

Introduction

1.1 Tax refund primarily arises when tax paid by an assessee at the pre-assessment stage¹ exceeds tax determined as payable at the time of assessment, whether in summary or in scrutiny².

1.2 Disposal of refund claims is a key indicator for measuring the operational performance of tax administration in providing quality services to the taxpayers; dimensions of quality being taxpayer satisfaction through accuracy of advice and timeliness in receipt of refund. Prompt issue of refunds reduces the interest liability of the government and by instilling confidence in the taxpayers, encourages them to greater tax compliance.

1.3 The Task Force on Direct Taxes (Kelkar Committee) had observed that “the failure of the tax administration to issue refunds continues to be a major source of public grievance.” One of its main recommendations to address the problem was replacement of the existing cumbersome and manually-operated procedures for issue of refunds with a more efficient automated system. The initiatives of the Department in automation were aimed to improve efficiency in management of refunds.

Legal provisions

1.4 Chapter XIX of the Income Tax Act, 1961 deals with the law and procedure regarding refunds. Sections 237 to 245 relate to refunds with particular reference to excess tax paid; persons entitled to claim refund in special cases; procedure and time limit for claim of refund; interest on refunds and set-off of refund against pending tax demands.

Why we chose the topic

1.5 We had conducted a performance evaluation of refunds in 2001-02. Our major findings highlighted taxpayer inconvenience because of delays in refunds, particularly those arising out of appeals³ and set-off of refunds against pending tax demands without intimating the tax payers; excess payment of refunds arising out of computation errors; and avoidable and excess payment of interest on refunds.

¹ Tax at pre-assessment stage is collected by way of tax deducted at source (TDS), advance tax and self assessment tax. While TDS is deducted by third party deductors from payments made to tax payers and remitted to government, advance tax and self-assessment form voluntary compliance by the tax payer.

² Annual tax return submitted by the tax payer is first summarily assessed by AOs without calling for additional documents or insisting on the presence of the tax payer. High risk returns are then selected for scrutiny assessments in which AOs subject the returns to detailed examination with reference to additional documents, if need be.

³ An aggrieved tax payer can avail of appellate mechanisms within the Department; if still aggrieved he can take legal recourse.

1.6 Public Accounts Committee (PAC) made several recommendations on the above audit report in its 55th Report (13th Lok Sabha) and 15th Report (14th Lok Sabha), in response to which the Department committed the following:

- ❑ To address the Committee's concern on inordinate delays, the Department assured that instructions had been issued to field formations to strengthen their internal procedures for prompt detection of delays, with their performance being monitored through monthly reports on refunds;
- ❑ PAC was informed that the Information Technology (IT) systems have been put in place to minimize errors in computation; and
- ❑ Section 244A was amended to reduce the interest rate on refunds to discourage taxpayers from paying excess tax. A new section was also introduced to charge interest on excess refunds granted in summary assessment.

1.7 The PAC desired that it may be apprised of the progress in implementation of IT systems as well as of the impact of the administrative measures to bring in timeliness in issue of refunds. We audited refunds this year to examine the extent to which the Department has been able to fulfill the above commitments.

1.8 The fact that efficiency in giving timely refunds forms the touchstone for evaluation of the Department's IT systems also prompted us to choose this audit. Our attempt was to focus on the grievances of the common taxpayer who is affected the most by the quality of services provided by tax administration in refunds.

Objectives of audit

1.9 The objectives of our audit were to seek an assurance that:

- ❑ The systems and procedures are geared to timely examination of refund claims and issue of refunds;
- ❑ Internal controls provide for effective monitoring of delays in issue of refunds and for timely corrective action;
- ❑ Automation in the Department has helped to improve efficiency in processing of the refunds. It also provides adequate safeguards to ensure accuracy in refund advices.

Scope of audit

1.10 Refunds due and paid during the financial years 2005-06 to 2008-09, were the subject of our study conducted during the period from January 2009 to August 2009. We divided refunds into two clusters notably high value refunds⁴ and low value refunds⁵:

- ❑ Two tier statistical sampling was employed while conducting the review. At level-1, the assessment units were selected using stratified random sampling. The universe was sub-divided into types of assessment units with specified percentage selection amongst them. Selection of the actual units was based on the risk analysis of each unit⁶. At level-2, assessment records having high value refunds were selected for audit within the assessment units using stratified random sampling. Low value refunds of individuals were sampled randomly⁷ as indicated in Appendix-I.
- ❑ 12423 high value refunds in 613 selected assessment circles/wards in 23 offices were selected for detailed examination with regard to compliance with laws and procedures and accuracy in advice. Of these, 9889 assessment records representing nearly 80 *per cent* of the selection were provided to audit. The remaining assessment records were not produced to audit.
- ❑ 12491 low value refund cases were selected to see if the small taxpayer is being served well by timely receipt of refunds. Delays, if any, were the only focus in examining low value refunds.

Acknowledgement

1.11 Indian Audit and Accounts Department acknowledges the cooperation of the Income Tax Department in providing the necessary records and information for audit. An entry conference was held on the review on refunds, with the Member (Audit) and other senior officers of the CBDT. The audit objectives, scope of audit and the main areas of audit examination were explained in the meeting. Audit was conducted on the assessment records in the respective field formations of the IT Department.

1.12 The exit conference was held (March 2010) with the CBDT wherein the report was discussed. The views expressed by the Board in the exit conference have been suitably incorporated in this report. Replies from the Ministry have not been received (March 2010).

⁴ Involving not less than Rs. 5.00 lakh;

⁵ Involving not more than Rs. 5.00 lakh and less than Rs. 500

⁶ Several factors such as materiality of assessments in a unit, assessee profile of a unit and previous audit observations in respect of a unit etc., form the risk matrix for evaluation of a unit.

⁷ Without following pre-defined criteria other than the value of refund and subjecting the total number of cases to be selected by any field formation to a ceiling.