

CHAPTER I
TAX ADMINISTRATION

Chapter Summary

- ◆ The direct tax collection exceeded the budget estimates in all the years over the period 2006-07 to 2010-11 except 2008-09. The extent of actual collection exceeding the budget estimates ranged from 2.2 *per cent* in 2009-10 to 16.7 *per cent* in 2007-08.
(Paragraph 1.2.2)
- ◆ Direct tax collection increased by 94.2 *per cent* from ₹ 2,30,181 crore in 2006-07 to ₹ 4,46,934 crore in 2010-11 whereas total Gross Domestic Product (GDP) has increased by 90.0 *per cent* from ₹ 41,45,810 crore in 2006-07 to ₹ 78,75,627 crore in 2010-11 indicating a significantly higher growth rate of tax collection over five years period. During the period 2006-07 to 2010-11, the average rate of growth of direct tax collection was 23.6 *per cent*. The annual rate of growth ranged from 6.9 *per cent* in 2008-09 to 35.6 *per cent* in 2007-08.
(Paragraph 1.2.3)
- ◆ In the case of the corporate assesseees, net collection increased from ₹ 1,44,318 crore in 2006-07 to ₹ 2,98,687 crore in 2010-11 at an average annual rate of growth of 26.7 *per cent* and in the case of non-corporate assesseees, net collection increased from ₹ 75,079 crore in 2006-07 to ₹ 1,40,042 crore in 2010-11 at an average annual rate of growth of 21.6 *per cent*.
(Paragraph 1.3.1)
- ◆ Voluntary compliance by assesseees (pre-assessment stage) accounted for 81.4 *per cent* of the gross collections in 2010-11. The collection by way of voluntary compliance in 2010-11 was higher than 2006-07 but marginally lower as compared to 2007-08 to 2009-10.
(Paragraph 1.3.3)
- ◆ The assessee base grew over the last five years from 313 lakh taxpayers in 2006-07 to 335.8 lakh taxpayers in 2010-11 at average annual rate of growth of 1.8 *per cent*.
(Paragraph 1.3.5)
- ◆ The pendency of scrutiny assessments increased from 2.8 lakh in 2006-07 to 3.9 lakh in 2010-11.
(Paragraph 1.3.7)

- ◆ At the end of 2010-11, as much as ₹ 2,9 lakh crore remained uncollected. This comprised demand of ₹ 2.0 lakh crore of earlier years and current demand (2010-11) of ₹ 0,9 lakh crore.

(Paragraph 1.3.8)

- ◆ Cost of collection showed a uniform trend of about 0,6 *per cent* during 2006-07 to 2010-11 except 2008-09 and 2009-10, where it was 0,7 *per cent*.

(Paragraph 1.5.4)

- ◆ Internal Audit completed 66 *per cent* of the targeted audits. Only 14,9 *per cent* of major findings raised by Internal Audit were acted upon by the assessing officers in 2010-11. Departmental response to Internal Audit was clearly inadequate.

(Paragraph 1.6.1)

CHAPTER I

TAX ADMINISTRATION

1.1 INTRODUCTION

1.1.1 Direct taxes levied by the Parliament mainly comprise:

- **Corporation Tax** on companies which constitutes 66.8 per cent of direct tax collection¹. The corporates also pay **Wealth Tax** on the assets owned by them. In addition, tax is payable on **capital gains** made on the sale of assets.
- **Personal Income Tax** which is required to be paid if the income level reaches above ₹ 1.6 lakh².

1.1.2 Other direct taxes include **Fringe Benefit Tax**³, **Securities Transactions Tax**⁴ and **Wealth Tax**⁵ etc.

1.1.3 Table 1.1 provides a snapshot of tax administration.

	2006-07	2007-08	2008-09	2009-10	2010-11
1. Gross Collection	2,67,416	3,53,498	3,72,915	4,35,164	5,22,103
2. Refunds	37,235	41,285	39,097	57,101	75,169
3. Net Collection	2,30,181	3,12,213	3,33,818	3,78,063	4,46,934
4. Tax-GDP Ratio	5.6	6.6	6.3	6.1	5.7
5. Buoyancy ⁶	2.5	2.6	0.5	0.8	0.7
6. No. of effective assesseees (in lakh)	312.9	336.6	326.5	340.9	335.8
7. Pre-assessment collection	2,05,741	2,83,986	3,02,341	3,51,660	4,18,094
8. Post-assessment collection	50,891	52,865	56,188	73,053	95,804
9. No. of scrutiny assessments due for disposal	5,27,005	9,97,813	9,53,767	8,70,620	8,47,196
10. No. of scrutiny assessments completed	2,41,983	4,07,239	5,38,505	4,29,585	4,55,212
11. No. of officers deployed for assessment duty	3,954	3,218	3,106	3,605	3,687
12. Direct refund claims pending (in lakh)	4.4	8.3	15.5	19.4	19.5
13. Interest on refunds	3,693	4,444	5,778	6,8767	10,499
14. Demand pending	1,17,370	1,24,274	2,01,276	2,29,032	2,91,629
15. No. of appeals pending with CIT(A)	1,07,841	1,30,358	1,58,031	1,80,991	1,87,182
16. Certified demand recovered	8,521.4	8,612.6	4,035.8	3,322.3	4,074.6
17. Certified demand pending	26,703.9	27,444.9	27,461.0	95,122.4	106,990.8
18. Cost of collection	1,343	1,713	2,286	2,774	2,698

The details of tax administration are given in *Appendix-1*.

¹ Net direct tax collection for the financial year 2010-11.

² The base above which income tax is payable is revised from time to time. It is ₹ 1.6 lakh for the AY 2011-12 (₹ 1.9 lakh in case of resident women and ₹ 2.4 lakh in case of resident Sr. citizens).

³ Tax on the value of certain benefits offered by the employers to their employees. Fringe Benefit Tax is abolished from the assessment year 2010-11 onwards.

⁴ Tax on the value of taxable securities purchased and sold through a recognized stock exchange in India.

⁵ Tax chargeable on the net wealth comprises certain assets specified under section 2(ea) of the Wealth Tax Act.

⁶ Tax buoyancy is measured by the ratio of percentage change in tax revenues to percentage change in GDP.

⁷ The Department initially intimated the figure as ₹ 12,951 crore. Subsequently after the report was placed in the Parliament, the department intimated this figure as ₹ 6,876 crore.

1.2 POLICY

1.2.1 MAJOR POLICY INITIATIVES BY THE GOVERNMENT

In the Budget 2010-11, the Government sought to amend the provisions relating to direct taxes in order to : (i) lower the tax burden on individual taxpayers by widening the tax slabs; (ii) allow small companies to convert into Limited Liability Partnerships without attracting capital gains tax liability; (iii) reduce the compliance burden on small business enterprises by raising the turnover limits beyond which audit is compulsory; (iv) promote investment in Research and Development (R&D) to enhance the competitive ability of the economy; (v) encourage savings for funding infrastructure by providing a tax deduction on investment in long-term infrastructure bonds; and (vi) simplify and rationalize the provisions relating to Tax Deduction at Source (TDS).

The Government also introduced the Direct Taxes Code (DTC) with a view to revise, consolidate and simplify the language and structure of the Direct Taxes Laws. The DTC Bill, 2010 was presented in the Parliament in August 2010. The Bill is presently with the Standing Committee,

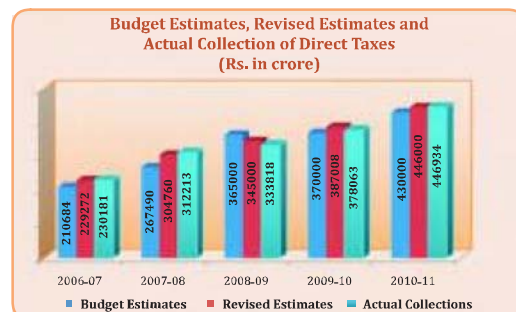
1.2.2 BUDGET VIS-À-VIS REVISED ESTIMATES OF DIRECT TAX COLLECTION

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) and the expenditure met from these revenues. Tax revenues comprise proceeds of taxes and other duties levied by the Government.

Comparison of budget estimates with the corresponding actuals is an indicator of quality of fiscal marksmanship. Actuals may differ from the estimates because of unanticipated and random external events or methodological inadequacies or at times it may be convenient to under project/over project some critical parameters,

The direct tax collection exceeded the budget estimates in all the years over the period 2006-07 to 2010-11 except 2008-09 (details in Chart 1.1). The extent of actual collection exceeding the budget estimates ranged from 2.2 per cent in 2009-10 to 16.7 per cent in 2007-08,

Chart 1.1 : Growth in Collection



The revised estimates were found realistic during 2006-07 to 2010-11

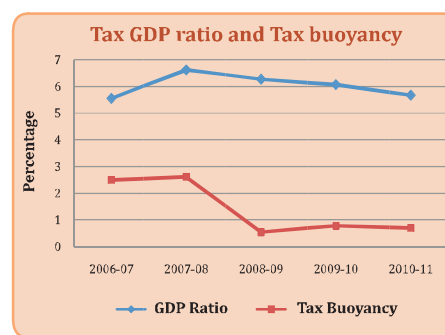
as the actual collection was within 3.2 *per cent* of the revised estimates.

1.2.3 TAX-GDP RATIO AND TAX BUOYANCY

The direct tax collection (net) has increased by 94.2 *per cent* from ₹ 2,30,181 crore in 2006-07 to ₹ 4,46,934 crore in 2010-11 whereas total Gross Domestic Product⁸ (GDP) has increased by 90.0 *per cent* from ₹ 41,45,810 crore in 2006-07 to ₹ 78,75,627 crore in 2010-11 indicating a significantly higher growth rate of tax collection over five years period. During the period 2006-07 to 2010-11, the average rate of growth of direct tax collection was 23.6 *per cent*. The annual rate of growth ranged from 6.9 *per cent* in 2008-09 to 35.6 *per cent* in 2007-08.

Chart 1.2: Tax GDP ratio and Tax buoyancy

Tax-GDP ratio increased marginally from 5.6 *per cent* in 2006-07 to 5.7 *per cent* in 2010-11 through 6.6 *per cent* in 2007-08 and 6.1 *per cent* in 2009-10. For every unit growth in GDP, though direct taxes grew by 2.6 *per cent* in 2007-08, the growth slowed down to



0.7 *per cent* in 2010-11 (details in Chart 1.2). Buoyancy value less than one is not a healthy indicator given the overall growth in the GDP. The decline in buoyancy is a matter of concern.

1.2.4 EFFECTIVE RATE OF TAXATION

The effective tax rate for companies⁹ was 23.5 *per cent*¹⁰ in 2009-10¹¹ which was substantially lower than the statutory tax rate of 33.9 *per cent*¹². We found that 216 companies with profits before taxes (PBT) of ₹ 500 crore and above accounted for 55.8 *per cent* of the total PBT and 53.4 *per cent* of the total corporate tax payable. However, their effective tax rate was only 22.6 *per cent* while the effective tax rate was 25.7 *per cent* for companies having PBT of upto ₹ one crore. This indicates that tax concessions are being availed of mainly by large companies.

⁸ At market prices (Source: Ministry of Statistics, National Statistical Organisation)

⁹ Source: Receipts Budget 2011-12

¹⁰ Effective tax rate in the case of companies is the ratio of total taxes paid (including surcharge and education cess but excluding Dividend Distribution Tax) to the total profits before taxes (PBT) and expressed as a percentage.

¹¹ The effective tax rate was 22.78 *per cent* in 2008-09.

¹² Corporation tax rate-30 *per cent*, Surcharge-10 *per cent* on tax, in case income exceeding ₹ 10 lakh, Education cess-two *per cent* on tax and surcharge and secondary & higher education cess-one *per cent* on tax and surcharge.

1.2.5 REVENUE FOREGONE

The main objective of any tax system is to raise revenues necessary to fund government expenditures. The amount of revenue raised is determined to a large extent by tax base and tax rates. It is also a function of a range of measures—special tax rates, exemptions, deductions, rebates, deferrals and credits—that affect the level and distribution of tax. These measures are sometimes called “tax preferences”.

The Income-tax Act, inter-alia, provides for tax preferences to promote savings by individuals; exports; balanced regional development; creation of infrastructure facilities; scientific research and development; cooperative sector, and accelerated depreciation for capital investment. Most of these tax benefits can be availed of by both corporate and non-corporate taxpayers.

The revenue foregone on account of tax exemptions has increased by 111.8 *per cent* from ₹ 65,587 crore in 2006-07 to ₹ 1,38,921 crore in 2010-11. Corporate sector accounted for 63.5 *per cent* of revenue foregone in 2010-11.

The revenue foregone on account of tax exemptions in respect of corporate taxpayers increased by 76.3 *per cent* as compared to 226.6 *per cent* in respect of non-corporate taxpayers during 2006-07 to 2010-11 as indicated in the following Table 1.2.

Table 1.2: Revenue Foregone# (₹ in crore)					
Sector	2006-07	2007-08	2008-09	2009-10	2010-11
1. Corporate	50,075	58,655	68,914	79,554	88,263
2. Non-corporate	15,512	42,161	39,553	40,929	50,658
3. Total	65,587	1,00,816	1,08,467	1,20,483	1,38,921

As per Receipts Budget of respective year.

Revenue foregone in case of corporate taxpayers in 2010-11 was mainly on account of accelerated depreciation under section 32 (₹ 35,494 crore) followed by section 80IA¹³/IB¹⁴/IC¹⁵ (₹ 28,315 crore) and 10A¹⁶/10B¹⁷ (₹ 20,559 crore). In the case of Non-corporate taxpayers, revenue foregone was mainly on account of section 80C¹⁸ applicable to individual taxpayers (₹ 37,424 crore).

¹³ Deduction to an undertaking providing infrastructure facility

¹⁴ Deduction to certain industrial undertakings other than infrastructure development undertakings

¹⁵ Deduction to certain undertakings in Himachal Pradesh, Sikkim, Uttarakhand and North-Eastern States

¹⁶ Deduction in respect of newly established undertakings in free trade zone, etc.

¹⁷ Deduction in respect of newly established hundred *per cent* export-oriented undertakings.

¹⁸ Deduction in respect of specified qualifying amounts paid or deposited by the assessee.

1.3 FUNCTIONS OF THE DEPARTMENT

1.3.1 COLLECTION OF TAXES

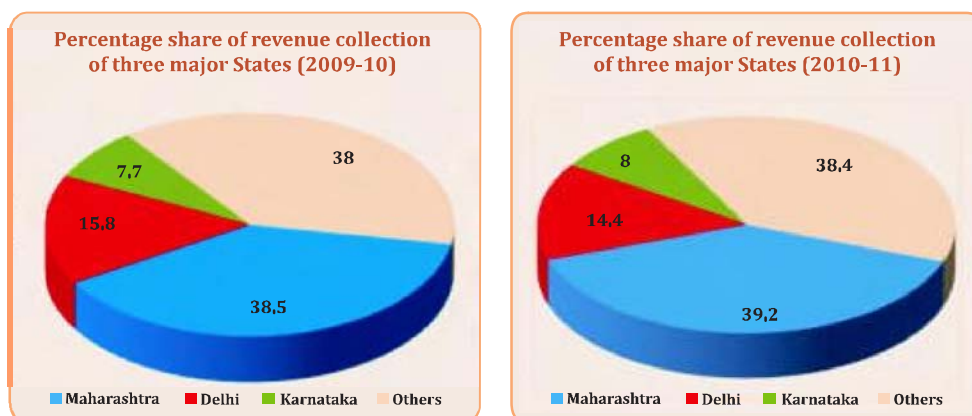
During the last five years direct tax collections (net) have increased from ₹ 2,30,181 crore in 2006-07 to ₹ 4,46,934 crore¹⁹ in 2010-11 at an average annual rate of growth of 23.6 per cent.

In the case of the corporate assesseees, net collection increased from ₹ 1,44,318 crore in 2006-07 to ₹ 2,98,687 crore in 2010-11 at an average annual rate of growth of 26.7 per cent and in the case of non-corporate assesseees, net collection increased from ₹ 75,079 crore in 2006-07 to ₹ 1,40,042 crore in 2010-11 at an average annual rate of growth of 21.6 per cent.

1.3.2 CONTRIBUTION OF STATES IN DIRECT TAX COLLECTION

The state-wise collection of direct tax has been compiled by Pr. CCA, CBDT, New Delhi. The collection in respect of each state/union territory has been correlated with the Permanent Account Number of the assessee/Tax Collection Account Number of the deductor²⁰. Three major States of Maharashtra, Delhi and Karnataka had contributed 61.6 per cent of direct tax collection in 2010-11 against 62.0 per cent in 2009-10 (Chart 1.3). Karnataka, Maharashtra and Delhi registered increase of 22.4 per cent, 20.2 per cent and 7.7 per cent respectively in collection over the previous year.

Chart 1.3: Relative-share in collection



Growth in direct tax collection was unevenly spread across the country. Positive growth was reported in all states/union territories

¹⁹ Head wise/State/UT wise break up of direct tax collection is given in *Appendix-2*.

²⁰ The state-wise collection shown in the Audit Report no. 26 of 2010-11 was based on collections reconciled by ZAO through nodal branches of banks wherein e-collection was reported. For e-collection only one Nodal Branch of each Bank in a particular state has been authorized for reporting collections. Nodal branches for e-collection for most of the banks are located in Mumbai, Delhi, Kolkata, Bengaluru and Nagpur. Therefore most of the e-collection got reported to those ZAOs showing higher collection for the States of Karnataka, Maharashtra and West Bengal as mentioned in the report *ibid*.

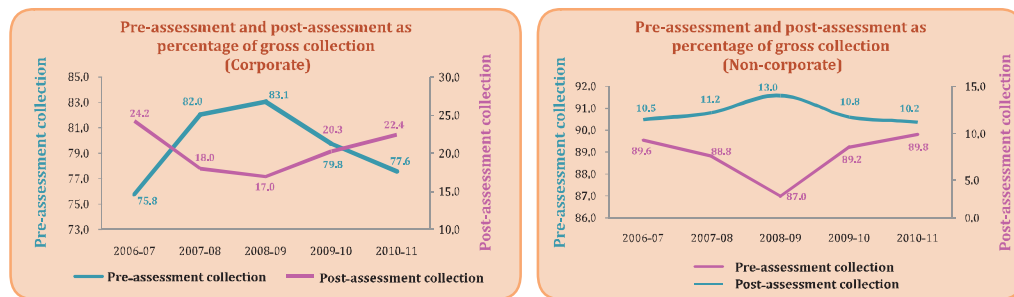
except Mizoram, Sikkim and Uttarakhand in 2010-11 vis-a-vis 2009-10 (Appendix 3).

1.3.3 TAX COLLECTION FOR CORPORATE AND NON-CORPORATE ASSESSEES AT PRE-ASSESSMENT AND POST-ASSESSMENT STAGES

The details of over-all tax collected at the pre-assessment and post-assessment level during last five years are given in Appendix-4,

Voluntary compliance by assessees (pre-assessment stage) accounted for 81.4 per cent of the gross collections in 2010-11. The collection by way of voluntary compliance was higher than 2006-07 but marginally lower as compared to 2007-08 to 2009-10,

Chart 1.4: Extent of voluntary compliance by Corporate and non-corporate assessees



During 2010-11 in the case of corporate assessees, 77.6 per cent of gross collection was made at the pre-assessment stage (Tax deducted at source, Advance tax, Self assessment tax) of which 51.9 per cent was by way of advance tax. Similarly, in the case of non-corporate assessees, 89.8 per cent of gross collection was made at the pre-assessment stage (Tax deducted at source, Advance tax, Self assessment tax) of which 63.3 per cent was by way of Tax deducted at source.

1.3.4 IDENTIFICATION OF THE TAX PAYERS

The Department has different mechanism available to enhance the assessee base which includes survey, information sharing with other tax departments and third party information available in annual information returns. Automation also facilitates greater cross linking²¹. Most of these mechanisms are available at the level of the assessing officers.

1.3.5 GROWTH OF TAX PAYERS

Over the past few years, the Board in their Central Action Plans (CAPs) has been advocating for a 15 per cent increase in the addition of new

²¹ Information about non-filers of TDS returns from e-TDS, Annual comparative figures of TDS deposited by big corporate & non-corporate deductors, linking TAN data in order to ensure better compliance from them, linking tax returns with the PAN data base and linking return submitted by deductors on TDS deductions with the returns of the deductee.

assessee vis-à-vis the assessee added during the previous financial year,

The assessee base grew over the last five years from 313.0 lakh taxpayers in 2006-07 to 335.8 lakh taxpayers in 2010-11 (Chart 1.5) registering an increase of 7.3 per cent with an average annual rate of growth of 1.8 per cent. However, the assessee base declined from 340.9 lakh taxpayers in 2009-10 to 335.8 lakh taxpayers in 2010-11,

Chart 1.5: Widening of tax base



The total direct tax collection has increased by 94.2 per cent during the period 2006-07 to 2010-11. The increase in tax collection was around thirteen times as compared to increase in the taxpayers’ base. This indicates a very limited widening of tax base over the years.

1.3.6 CORPORATE ASSESSEES BASED ON ROC FIGURES

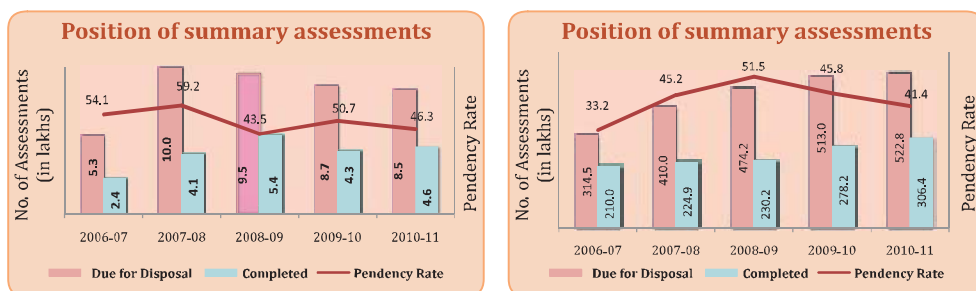
There were 7.2 lakh working companies²² in the country registered with Registrar of Companies (ROC) as on 31 March 2011. However, the corporate assesseees on the Income-Tax Department’s records are only 3.8 lakh, leaving an un-reconciled list of 3.4 lakh companies whereas all of them are legally obliged to file returns mandatorily. The difference was same as in 2005-06. It had been marginally reconciled in 2007-08 (2.8 lakh). The Board needs to reconcile the discrepancy for accurate assessment of the filing gap.

The Board in their Central Action Plan 2011-12 has instructed the field formations to issue notices to non-filers and take necessary action under the Act.

1.3.7 PROCESSING OF RETURNS AND SCRUTINY ASSESSMENTS

The number of summary and scrutiny assessments due and disposed off during 2006-07 to 2010-11 has been given in *Appendix-1*,

Chart 1.6: Position of Summary and Scrutiny assessments



²² Source: Ministry of Corporate Affairs (R&A Division).

High-risk tax returns are selected and examined with reference to collateral data by the assessing officers (AOs) in scrutiny assessments. Out of the total 8,5 lakh scrutiny assessment cases for disposal (Chart 1.6), the Department has disposed off 4,6 lakh (53.7 per cent) cases in 2010-11. This was higher than the scrutiny assessments completed in 2006-07 to 2009-10 except in 2008-09. The pendency of scrutiny assessments increased from 2.8 lakh in 2006-07 to 3,9 lakh in 2010-11.

Out of 5,2 crore summary assessment cases for disposal, the Department had disposed off 3,1 crore cases in 2010-11. As a result the pendency of summary assessments increased from 33,2 per cent in 2006-07 to 41,4 per cent in 2010-11. It may be mentioned that summary assessments are processed through Assessment Information System (AST).

The Department introduced e-filing of annual returns in 2007 for corporate and in 2008 for individuals. The Central Processing Centre at Bengaluru established by the Department to process e-filed returns is in operation since 2009.

It should be the constant endeavour of the Department to ensure that the entire assessee base, once correctly identified is duly meeting the entire tax liability. However, assurance could not be obtained that the tax liability on the assessees is being assessed and collected properly.

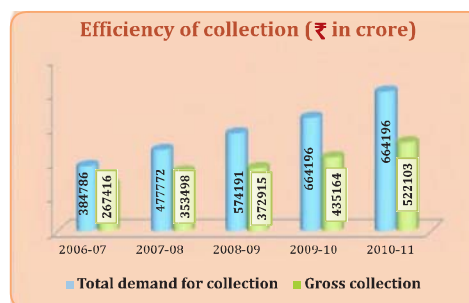
This comment is corroborated in para 2,3,1 of Chapter 2 of this report where we have mentioned about our detection of under/over charge of tax amounting to ₹ 14,475,4 crore in 20,130 cases audited during 2010-11. However, given the fact that ours is a test audit, Department needs to take firm steps towards strengthening the controls available in the existing statutes towards deriving an assurance on the tax collections and assessments.

1.3,8 UNCOLLECTED DEMAND

In 2010-11, only 64,1 per cent of the total demands cumulatively raised in assessments upto that year had been collected (Chart 1.7).

The performance was identical as in 2008-09 and 2009-10. However, there was a decline as compared to collection of 74 per cent for 2007-08. At the end of 2010-11, as much as ₹ 2,9 lakh crore remained uncollected. This comprised demand of ₹ 2,0 lakh crore of earlier years and current demand (2010-11) of

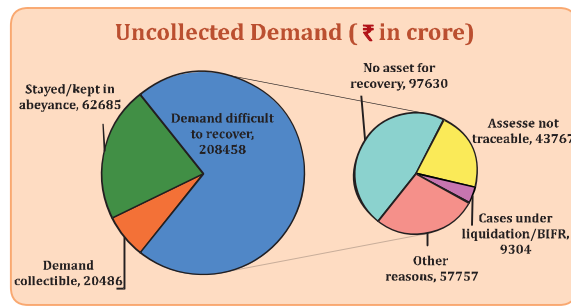
Chart 1,7: Efficiency of collection



₹ 0,9 lakh crore. However, in 2009-10, earlier years pending demand was ₹ 1,8 lakh crore and current demand was ₹ 0,5 lakh crore,

Chart 1,8: Details of uncollected demand

The Department intimated that various factors contributed to the uncollected demand (Chart 1,8). An amount of ₹ 1,06,934 crore (36,7 per cent) remained uncollected as there were no assets for recovery or the companies were under liquidation/BIFR,



The uncollected demand is rising despite clear provisions in the Act to enforce collection and recovery of outstanding demand viz, attachment and sale of assessee’s movable and immovable property, appointment of a receiver for the management of assessee’s properties and imprisonment, Tax demands remain irrecoverable for a long period in spite of exercise of the powers of recovery conferred under the Act. Write-off of such arrears may be considered as per the Departmental instructions laid down on the subject.

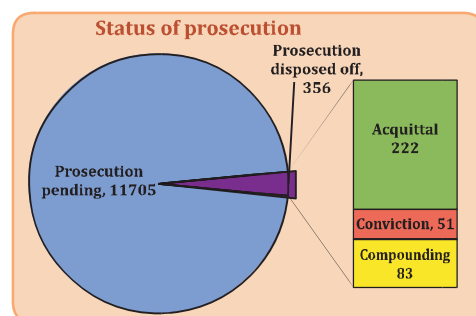
Defaults in payment of tax are referred to the Tax Recovery Officers (TROs) who draw up a certificate specifying the amount of arrears due from the assessee and proceed to recover the amount. The recovery mechanism is inefficient as certified demand remaining uncollected increased to ₹ 1,06,990,8 crore (96,3 per cent) in 2010-11 from ₹ 26,703,9 crore (75,8 per cent) in 2006-07.

Board may like to prepare a time bound action plan for recovery of current and arrear demands by fixing targets for each assessing officer. Recovery proceedings can be made effective by increasing the accountability of the TROs and incentivizing achievements,

1.3,9 STATUS OF PROSECUTION

The Department had launched prosecution in 11,705 cases of tax evasion upto 2010-11. Only 356 cases (3 per cent of the total cases) were disposed off, of which 222 cases resulted in acquittal (Chart 1,9). The Board needs to analyse the reasons for slow pace of disposal. The high rate of acquittal also needs to be analysed to ensure greater effectiveness of prosecution as a deterrent,

Chart 1,9: Status of prosecution



1.3.10 REFUND CASES AND INTEREST PAID ON REFUNDS

Where the amount of tax paid exceeds the amount of tax payable, the assesseees are entitled to a refund of the excess amount. Simple interest at the prescribed rate is payable on the amount of such refund. Refund is also admissible (alongwith interest) as a result of any order passed in appeal or other proceedings. Pendency of direct refund claims results in outflow of revenue from Government by way of interest.

Out of total 59,9 lakh direct refund claims, the Department had disposed off 40,4 lakh (67,4 *per cent*) claims in 2010-11. The pendency rate has increased to 32,6 *per cent* in 2010-11 from 24,1 *per cent* in 2006-07.

The Government has refunded ₹ 75,169 crore which includes interest of ₹ 10,499,4 crore (13,9 *per cent*) from gross collection of Corporation and Income tax of ₹ 5,13,898 crore in 2010-11. The interest paid on refunds in 2009-10 was ₹ 6,876 crore (12,0 *per cent* of ₹ 57,101 crore, the amount refunded) out of the gross collection of Corporation and Income tax of ₹ 4,24,713 crore. The interest on refunds also needs to be seen in the perspective of pendency of direct refund cases which increased from 4,4 lakh in 2006-07 to 19,5 lakh in 2010-11 registering an increase of 343 *per cent*.

1.3.11 INCORRECT ACCOUNTING OF INTEREST ON REFUNDS

We had earlier commented²³ that the Government was following an incorrect procedure of accounting for interest paid on refunds. Interest payment is a charge on the Consolidated Fund of India and is, therefore, payable through a proper budgetary mechanism. Accordingly, Minor Head “interest on refunds” is to be operated under the Major Head “2020-Collection of Taxes on Income and Expenditure”. However, no budget provision for ‘interest on refund’ was made in the Budget Estimates for 2010-11 and the expenditure on interest on refunds amounting to ₹ 10,499,4 crore was treated as reduction in revenue. Accounting of interest on refund as reduction in revenue is incorrect as this interest was never collected in the first instance. Interest on belated refunds of excess tax should be budgeted as an expenditure item which, in fact, was done in the Budget Estimates 2001-02 when ₹ 92 crore was provided in the demand of ‘Direct Taxes’ under the Major Head ‘2020 – Collection of taxes on Income & Expenditure’ towards interest on belated refund of excess tax. However, subsequently at the Revised Estimates stage the earlier practice of showing the interest on excess refund as deduct receipt was reverted to. This practice is still being followed. In response the

²³ in Audit Reports of 2004, 2005, 2006, 2007, 2008, 2009, 2009-10 and 2010-11

Department stated that this is a policy decision taken at the highest level,

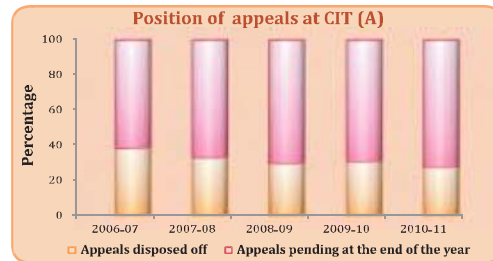
1.3.12 APPEAL CASES

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.

1.3.12.1 APPEALS PENDING AT CIT(A)

Chart 1.10: Appeals disposed off and pending

As per the instructions of the Board, each CIT(Appeal) is required to dispose off a minimum of 60 appeals per month, and a total of 720 appeals annually. Thus, 1,05,840 lakh appeals could have been disposed



off during the year on the basis of the working strength of 147 CIT(A). CIT(A) were required to dispose off 2,57,656 cases during 2010-11. Out of this, only 70,474 appeals (27.4 per cent) were disposed off (Chart 1.10) and the average annual disposal per CIT(A) during 2010-11 was only 479 appeals. The amount locked up in appeal cases with CIT(A) was ₹ 2.9 lakh crore in 2010-11 which is equivalent to 108.8 per cent of the revised revenue deficit of Government of India.

1.3.12.2 Further, the amount locked up in appeals at higher levels (ITAT/High Court/Supreme Court) was ₹ 2.1 lakh crore in 72,196 cases as on 31 March 2011.

1.4 IT INITIATIVES TAKEN BY THE INCOME TAX DEPARTMENT

The Task Force on Direct Taxes headed by Vijay Kelkar (December 2002) recommended that Tax Information Network (TIN) should be established to computerize vital arteries of the tax assessment and collection system. In pursuance of the Task Force recommendations, the Department had taken number of IT initiatives over the years.

ITD's current system is a result of several years' effort and it has been continually going through the process of modification. Comprehensive computerisation project of the ITD contains modules such as Assessee Information System (AIS), Assessment Information System (AST), On

line Tax Accounting System (OLTAS), Electronic Tax Deducted System (e-TDS), Individual Running Ledger Accounting System (IRLA), Computer Aided Scrutiny System (CASS) and Enforcement Information System (EFS) for functional areas of the ITD. Besides, several other internal management and house keeping modules such as pay roll System (PAS), Manpower Management System (MMS), Judicial Reference System (JRS), Financial Resource System (FRS), Management Information System (MIS) are also working.

Business Processing Re-engineering report submitted in April 2008 recommended functional segregation of the working of the Department across two broad lines; a Bulk Operations Division (BOD) handling routine, repetitive activities not requiring exercise of discretion in individual cases and a Compliance Operations Division (COD) to carry out specialized enforcement activities for a smaller number of taxpayers.

Based on the above recommendations ITD established a Central Processing Centre (CPC) at Bengaluru to process e-filed returns of All India and paper returns of Karnataka and Goa. This CPC became operational in October 2009.

We had earlier commented on IT initiatives taken by the Department in our Audit Reports {No. 10 of 2006 relating to performance audit of Assessment Information System (AST) and No. PA 25 of 2009 relating to IT audit of e-TDS system}.

Similarly, in our Audit Report No, 7 of 2009-10 relating to Income Tax Refunds, we had also commented on the CPC, verification of credits through OLTAS, AST and Refund Banker Scheme. Deficiencies in these modules were resulting in delayed refunds. The Department needs to address the deficiencies pointed out in these reports.

1.5 RESOURCE GAP

The overall responsibility for the administration of direct taxes lies with the Department of Revenue which functions through the Income Tax Department (ITD). The ITD has staff strength of 61,463. The organizational structure of the Income Tax Department is at *Appendix-5*.

1.5.1 SANCTIONED AND WORKING STRENGTH OF OFFICERS

Table 1.3 below shows the sanctioned and working strength of the officers of the ITD as on 31 March 2011,

Post	Sanctioned strength	Working strength	Short fall
CCIT/DGIT	116	104	12
CIT/DIT	729	693	36
ADDL CIT/JCIT	1,253	893	360
ACIT/DCIT	2,092	1,397	695
ITOs	4,448	4,247	201
Total	8,638	7,334	1,304

1.5.2 DEPLOYMENT OF OFFICERS ON ASSESSMENT AND NON-ASSESSMENT CHARGE

The deployment of officers on assessment duty in 2010-11 decreased to 3,687 from 3,954 in 2006-07. This could be one of the reasons for backlog in assessments referred to in para 1.3.7.

1.5.3 EXPENDITURE BUDGET

The revenue and capital expenditure (budgeted and revised) of the Department as per Expenditure Budget²⁴ for the last five years vis-à-vis actual are shown in the following Table 1.4:

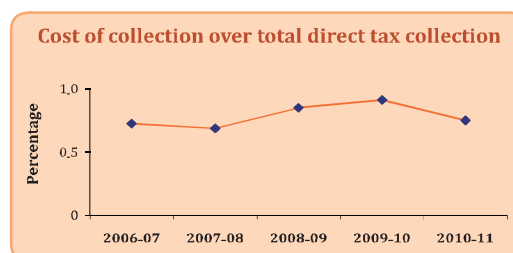
Financial Year	Revenue expenditure			Capital expenditure		
	Budgeted	Revised	Actual	Budgeted	Revised	Actual
2006-07	1,306.0	1,371.0	1,348.5	28.0	10.3	4.9
2007-08	1,521.5	1,742.2	1,687.3	10.5	10.2	35.7
2008-09	1,772.0	2,327.1	2,248.4	203.0	190.5	83.5
2009-10	2,884.0	2,819.4	2,725.9	618.0	21.0	9.3
2010-11	2,845.0	2,735.3	NA	1,679.0	1,610.0	NA

It is observed that savings on the revenue expenditure were marginal. However, there were huge deviations between budget estimates, revised estimates and actuals in case of capital expenditure.

1.5.4 COST OF COLLECTION OF TAXES

Total cost of direct tax collection (Chart 1.11) showed a uniform trend from 0.58 per cent in 2006-07 to 0.60 per cent in 2010-11 except 2008-09 and 2009-10,

Chart 1.11: Cost of collection of taxes



²⁴ Demand no. 42 of the Expenditure budget

1.6 MISCELLANEOUS

1.6.1 INTERNAL AUDIT

Internal audit is an important part of the Departmental control that provides the assurance that demands/refunds are processed accurately by correct application of the provisions of the Act.

The Department introduced a new Internal Audit System w.e.f. June 2007 to have an effective and objective set up of Internal Audit wherein the assessment functions and audit functions are assigned to separate specialized wings. Under each CIT(Audit) there shall be one Addl. CIT who would be responsible for internal audit of high value cases and supervision of the audit work of special audit party (SAP) headed by Dy./Asstt. CsIT and the internal audit party (IAP) headed by ITOs. The minimum number of cases to be audited by each Addl. CIT, SAP and IAP in a year shall be 50, 300 and 1,300 (600 corporate cases & 700 non-corporate cases) respectively.

Internal audit wing had planned 2,62,000 cases for audit during 2010-11 based on the working strength of wing. Out of which, 1,73,040 cases were completed thereby achieving 66 *per cent* of the target.

Internal audit had raised 13,494 observations in the audited assessments with money value of ₹ 5,466.9 crore during the year 2010-11. Based on the reply from assessment units, the internal audit had settled 7,996 cases with money value of ₹ 921.9 crore.

However, we detected numerous observations in the assessments previously audited by Internal Audit. We noticed that internal audit had audited 2,999 assessments in 2010-11, where we pointed out the mistakes but the same were not detected by them. This indicates a need for improvement in the quality of Internal Audit.

Out of 464 draft paragraphs included in this report, only 29 cases (6.3 *per cent*) were seen by internal audit and no mistakes were detected by them, which indicates need for improvement in quality of internal audit.

Departmental response to internal audit needs improvement. Only 1905 cases (14.9 *per cent*) having tax effect of ₹ 904.6 crore out of 12,792 cases having tax effect of ₹ 9,335.1 crore of the major findings²⁵ raised by internal audit were acted upon by the assessing officers in 2010-11. The total pendency increased from 6,688 cases having tax effect of ₹ 412.9 crore in 2006-07 to 34,940 cases having tax effect of ₹ 8,516.4 crore in 2010-11.

²⁵ Audit objection above ₹ 1 lakh in Income tax and above ₹ 30,000 in other taxes