

Chapter 1 – Introduction

1.1 Overview

Indian healthcare sector is one of the fastest growing service areas and has witnessed significant growth in terms of revenue and employment generation in recent years. With liberalization of the economy, the per capita income had increased manifolds, which in turn increased the demand for high value quality health services. The public infrastructure for providing health related services is not sufficient to cater to the increasing demands of quality health services in the country.

The healthcare sector in India comprises both private and public sectors. The private sector provides nearly 80 *per cent* of outpatient care and about 60 *per cent* of inpatient care. The private health care sector comprises organizations that operate both on profit and not-for-profit basis. The “not-for-profit” organizations include healthcare service providers such as Non-Government Organizations (NGO’s), charitable institutions, trusts, etc. The private sector in India has a dominant presence in medical education and training, hospital infrastructure and ancillary service areas such as medical technology and diagnostics. As per sector-wise data of the Department of Industrial Policy and Promotion¹, the share of foreign direct investment (FDI) inflows in “hospitals and diagnostic centres” has been increasing at an accelerating rate. This sector attracted FDI of ₹23,169.91 crore between April 2000 and September 2016 as indicated below.

Table 1.1: (FDI) inflows in “hospitals and diagnostic centres	
Year	Amount of FDI Inflows (₹ in crore)
From April 2000 to March 2013	7,437.93
From April 2013 to March 2014	3,994.60
From April 2004 to March 2015	4,072.59
From April 2015 to March 2016	4,278.09
From April 2016 to September 2016	3,386.70
Total	23,169.91

1.2 Healthcare infrastructure

The healthcare infrastructure is divided into the following segments:

➤ **Hospitals**, which include government hospitals and private hospitals. The government hospitals include primary healthcare centres, district hospitals and general hospitals. The private hospitals include nursing homes/medical clinics, mid-tier and top-tier private hospitals. It also includes hospitals run by trusts, charitable institutions and NGOs;

¹ Fact sheet on FDI from April 2000 to September 2016, source: dipp.nic.in

- **Medical Colleges/Research Institutes;**
- **Clinical Establishment** which include small clinics providing healthcare services without nursing aids and poly-clinic services;
- **Diagnostics Centres/Pathological Labs** which comprise businesses and laboratories that offer analytic or diagnostic and pathological laboratory services; and
- **Medical Equipment and Supplies** which include establishments primarily engaged in medical equipment management and supplies such as surgical, dental, orthopaedic, ophthalmologic, laboratory, consumables etc.

Among the professionals engaged in delivery of healthcare services, there are all types of surgeons, doctors (all disciplines), nurses and allied health professionals (AHPs) viz. technologists, radiologists etc.

1.3 Why we chose the topic

The grounds for selecting this topic for performance audit are:

- The health sector has witnessed a robust annual growth of 15 *per cent*². The sector is projected to grow from ₹ 684,000 crore in 2015 to ₹ 823,700 crore in 2018 with a CAGR of 12.1 *per cent*³.
- The fees charged by health professionals, private hospitals, nursing homes, medical clinics, medical colleges, diagnostic centres, pathological labs, medical supply stores etc. for their services are mostly received in cash, which is a high-risk area with potential for evasion of tax.
- As this sector is expanding very fast, the sources of investment for acquisition of assets require proper verification to plug the loopholes on any possible transfer of money from untaxed sources or unaccounted funds for such investments.

It was therefore felt necessary to verify whether the revenue department was satisfying itself that the income tax was duly being levied and collected based on all incomes generated from these services. Given the special nature of healthcare business, it was felt necessary to verify whether the Income Tax Department (ITD) was adequately equipped and vigilant while dealing with assessee engaged in the business of providing health related services.

² National Health Policy 2015

³ Industry Forecast -Healthcare -India -Q1 2015, Business Monitor International, 05 December 2014;

1.4 Audit objective

The audit was conducted to:

- ascertain whether the objectives of introduction of tax incentives specific to private hospitals, nursing homes/medical clinics, medical colleges/research institutes, diagnostic centres, pathological labs, medical supplies agencies/stores etc. have been achieved optimally and whether adequate monitoring mechanism is in place;
- derive an assurance that the existing systems and controls are adequate to promote compliance of provisions specific to the healthcare institutions and medical professionals under the Act as well as compliance to general provisions of the Income Tax Act;
- examine whether all the private hospitals, nursing homes/medical clinics, medical colleges/research institutes, diagnostic centres, pathological labs, medical supplies agencies/stores etc. were covered in the tax net of the Income Tax Department (ITD) and to ascertain whether the efforts made by ITD to strengthen the tax base were adequate.

1.5 Legal Framework

The assessee engaged in the business of Private Hospitals, Nursing Homes/Medical clinics, Medical Colleges/Research Institutes, Diagnostic Centres, Pathological labs, Medical supplies agencies/stores etc. are governed by all the provisions of the Income Tax Act that are generally applicable to the different class of assessee viz. Companies, Firms, Trusts, Charity firms, Association of Persons, Hindu Undivided families, Individuals etc. Further, the Income Tax Act provides specific tax incentives to hospitals. It provides a five-year tax holiday in respect of profits derived from the business of operating and maintaining hospitals located anywhere in India other than the excluded areas subject to certain conditions, besides deduction of capital expenditure incurred in connection with setting up of new hospitals, also subject to certain conditions. Further, it allows higher rate of depreciation on medical equipment to incentivize the hospitals to upgrade their healthcare infrastructure and to provide access to patients to the latest technology. The provisions specific to healthcare sector are given in **Annexure 1A**. Other important deductions and allowances admissible under the Income Tax Act which are also availed by the assessee in healthcare sector are given in **Annexure 1B**. There have been important judicial pronouncements, and circulars based on these, indicating that (i) there should be a direct nexus between the research activities undertaken and business of the assessee and that (ii) unlawful expenditure in form of commission paid to doctors to be disallowed as business expenditure. These are shown in **Annexure 2**.

1.6 Scope of audit and sample size

1.6.1 The audit covered assessment cases relating to Private Hospitals, Nursing Homes/Medical Clinics, Medical Colleges/Research Institutes, Diagnostic Centers, Pathological Labs, Medical Supplies Agencies/Stores etc., including those running on 'not-for-profit basis', and healthcare delivery professionals. The performance audit covered cases of scrutiny assessments, appeal and rectification cases completed during the period 2012-13 to 2015-16. Wherever necessary, assessment records of previous assessment years in respect of the selected assessees were also examined.

1.6.2 The Director General of Income Tax (Systems), New Delhi furnished only the Commissionerate-wise consolidated data in respect of health sector assessees (for three categories coded⁴ as '604' Medical Professionals, '605'-Nursing Home and '606'-Speciality Hospitals) with respect to assessments completed during the financial years from 2012-13 to 2015-16 for all the regions. The data contained PCIT/CIT wise and assessing officer-wise number of scrutiny assessments completed and aggregate amounts of income returned and assessed to tax.

The selection⁵ of Commissionerates and units within each Commissionerate was therefore based on risk analysis of consolidated data obtained from DGIT (Systems) and information available at regional levels specific to different jurisdictions and not based on granular level data pertaining to the assessees. Within the selected assessment units⁶ under different PCsIT/CsIT in 20 states⁷ (detailed in **Annexure 3**), a total of 3,210 assessees were identified for examination in audit based on the information available in the 'Demand and Collection Register' maintained by the selected assessment units and through discussions with the Department.

⁴ The codes for nature of business are extracted from Part-A of Income Tax Return – Nature of business. Code 6 is related to Service.

⁵ Sample selection of Commissionerates was made by applying filter on the aggregate data (Excel format) and subject to minimum requirements (2 Commissionerates) and resource availability. Further, 50 per cent circles and 10 per cent ITO wards for each selected PCIT/CIT were selected based on risk parameters like Number of scrutiny assessments, nature of assessees, their turnover, exemptions, deductions, issues relating to internal/ external audit findings etc.

⁶ 50 per cent circles and 10 per cent ITO wards for each selected PCIT/CIT based on risk parameters like Number of scrutiny assessments, nature of assessees, their turnover, exemptions, deductions, issues relating to internal/ external audit findings etc.

⁷ Number of assessees in the PCIT/CIT office in the States located in Tamil Nadu-267, Kerala-132, Karnataka-31, UP-110, Bihar-124, Jharkhand-76, Delhi-281, Madhya Pradesh-104, Chattisgarh-43, Uttarakhand-64, Haryana-80, Punjab-50, Gujarat-156, Rajasthan-203, Maharashtra-589, Andhra Pradesh & Telangana-267, Odisha-42, Assam-63 and West Bengal-528.

1.7 Audit methodology

The audit included:

- i) the examination of data held by Income Tax Department and detailed examination of assessment cases of the assessee engaged in the business of Private Hospitals, Nursing Homes/Medical Clinics, Medical Colleges/Research Institutes, Diagnostic Centres, Pathological Labs, Medical Supplies Agencies/Stores etc., for ascertaining compliance to the provisions of the Income Tax Act, 1961.
- ii) Collection of data and information from other sources *viz.* registering bodies, Directorates of Investigation, Intelligence & Criminal Investigation etc., (discussed in para 2.2). The data so obtained from these sources were issued to the Commissioners of Income Tax to ascertain whether the entities were subject to tax assessment.
- iii) Survey through issue of questionnaire⁸ to:
 - a) the Controlling Officers of CGHS/DGHS/PSUs that empanel Private Hospitals, Nursing Homes/Medical Clinics, Medical Colleges/Research Institutes, Diagnostic Centres, Pathological labs, Medical supplies agencies/stores and Authorised Medical Attendants (AMAs) to ascertain whether such empanelled healthcare facilities/professionals were within the income tax net; and
 - b) other registering authorities and healthcare institutions (as discussed in para 2.4 and 2.5 of this report) to ascertain whether the conditions for registration as a healthcare facility/professional included reporting on the income tax registration status.

1.8 Constraints

The following constraints were faced by audit while conducting this performance audit:

- The assessment unit-wise detailed data of assessee related to health sector was not furnished by DGIT (Systems). Due to non-availability of case-wise detailed data of the selected units, attempts to select a representative sample through scientific sampling techniques was not possible.

⁸ To provide: (a) the list of private hospitals, nursing homes/medical clinics, medical colleges/research institutes, diagnostic centres, pathological labs and other Medical supplies agencies/stores and Authorised Medical Attendants which are empanelled with your organisation for providing health facility to Central Government/State Government/PSU employees, alongwith their complete address, phone numbers, email Ids;
 (b) While empanelling/registering a medical professional/health facility, it may please be stated whether PAN/TAN details and status of filing of income tax returns are sought and collected.
 (c) Please state the terms and conditions of empanelment of these institutions along with the list of documents which are a mandatory requirement for registration.
 (d) What are the criteria for de-registering/de-listing (black-listing) the medical facilities/professionals from empanelled/registered body?

- Further, out of total of 3,210 cases identified during this performance audit for which records were sought by audit, 230 assessment folders relating to 32 PCsIT/CsIT⁹ were not received (as detailed in **Annexure 4**), despite repeated requests, reminders and discussions at different levels. This had hindered the audit process.

CBDT stated (June 2017) that the Board had noted this.

1.9 Acknowledgement

We acknowledge the cooperation of ITD in facilitating the conduct of this performance audit. At the start of this performance audit, an Entry Conference was held with CBDT in August 2016 wherein audit objective, scope of audit, audit methodology etc., were explained.

We issued draft performance audit report to the Ministry on 3 May 2017 for their comments. Post receipt of the Ministry's response in May 2017, we held Exit Conference with CBDT on 26 May 2017 to discuss audit findings and audit recommendations vis-à-vis their comments. We have duly incorporated the Ministry's comments together with the audit comments in the report.

⁹ Kerala-2 (CIT-1, Kochi),UP-6 (PCIT-1, PCIT-Ghaziabad), Bihar-27 (PCIT-Patna, PCIT-Muzaffarpur, PCIT-Darbhanga), Delhi-14(PCIT-1,PCIT-3, PCIT-4, PCIT-6), Madhya Pradesh-17 (CIT-1, Indore) Chattisgarh-3 (PCIT-Raipur),Haryana-7 (PCIT Hisar, PCIT, Karnal, PCIT, Faridabad), Gujrat-13(PCIT-Baroda, PCIT-4, Ahmedabad, Rajasthan-11 (PCIT-III, Jaipur, PCIT-Udaipur), Maharashtra-97 (PCIT-16, Mumbai, CIT (Exemption), Mumbai), Andhra Pradesh & Telangana-11 (PCIT-2, Hyderabad, PCIT-3, Hyderabad, PCIT-4, Hyderabad,PCIT-1, Visakhapatnam), Odisha-4 (PCIT-Cuttack, PCIT-Bhubaneswar-1), and West Bengal-18 (PCIT-3, PCIT-4, PCIT-8, PCC-1, PCIT (Exemption))