

## Highlights

The Comptroller and Auditor General of India conducts the audit of receipts of the Union Government under section 16 of the Comptroller and Auditor General of India (Duties, Powers and Conditions of Service) Act, 1971. This Report primarily discusses compliance to the provisions of the Income Tax Act, 1961 and the associated rules, procedures, directives etc. as applied to all aspects related to the administration of direct taxes. The report is organised into seven chapters, the highlights of which are described below:

### Chapter I: Direct Taxes Administration

Direct taxes receipts of Union Government in FY 2017-18 amounted to ₹ 10,02,738 crore grew by 18.0 *per cent* over the FY 2016-17 (₹ 8,49,801 crore). Direct Taxes represented 6.0 *per cent* of the GDP in FY 2017-18. Share of direct taxes in gross tax revenue increased to 52.2 *per cent* in FY 2017-18 from 49.5 *per cent* in FY 2016-17.

Of the two major components of direct taxes, collections from Corporation Tax increased by 17.8 *per cent*, from ₹ 4.85 lakh crore in FY 2016-17 to ₹ 5.71 lakh crore in FY 2017-18. Collections from Income Tax increased to 19.9 *per cent* from ₹ 3.41 lakh crore in FY 2016-17 to ₹ 4.08 lakh crore in FY 2017-18.

The number of non-corporate assesseees increased from 4.37 crore in FY 2016-17 to 5.38 crore in FY 2017-18, registering an increase of 23.1 *per cent*. The number of corporate assesseees increased from 7.13 lakh in FY 2016-17 to 7.99 lakh in FY 2017-18, registering an increase of 12.1 *per cent*.

The arrears of demand increased from ₹ 10.4 lakh crore in FY 2016-17 to ₹ 11.1 lakh crore in FY 2017-18. The Department indicated that more than 98.2 *per cent* of uncollected demand would be difficult to recover.

Number of appeals pending with CIT (Appeals) increased from 2.9 lakh in FY 2016-17 to 3.0 lakh in FY 2017-18. The amount locked up in these cases was ₹ 5.2 lakh crore in FY 2017-18. The amount locked up at higher levels (ITAT/High Court/Supreme Court) increased from ₹ 4.40 lakh crore (82,806 cases) in FY 2016-17 to ₹ 4.43 lakh crore (82,643 cases) in FY 2017-18.

## **Chapter II: Audit Mandate, Products and Impact**

During FY 2016-17, the ITD had completed 2.73 lakh scrutiny assessments in the units audited as per the audit plan of FY 2017-18, out of which we checked 2.64 lakh cases. Apart from this, we have also audited 0.47 lakh cases out of 1.07 lakh scrutiny assessments completed in the earlier financial years, during FY 2017-18. The incidence of errors in assessments checked in audit during FY 2017-18 was 0.20 lakh cases (6.45 *per cent*, as against 7.2 *per cent* last year).

There have been persistent and pervasive irregularities in respect of corporation tax and income tax assessments cases over the years. Recurrence of such irregularities, despite being pointed out repeatedly in the earlier Audit Reports points to structural weaknesses on the part of Department as well as the absence of appropriate institutional mechanisms to address this. Such irregularities were particularly noticeable in the assessment charges in Maharashtra and Delhi.

We have included 472 high value cases reported to the Ministry in Chapter III and IV of this Report. Of these, we received replies in respect of 325 cases as on 31 March 2019, of which, 302 cases (92.9 *per cent*) were accepted and 23 cases not accepted. In remaining cases the Ministry/ ITD did not furnish replies. In addition, two long draft paras viz. 'Follow up audit of exemptions to charitable trusts and institutions'; and 'Integrated audit of assessments of a group company' have been separately included in Chapter VI and VII of this Report respectively. Besides, the Report also discusses one subject specific compliance audit on 'Assessments relating to Agricultural Income' which has been included in Chapter V.

In the last three years, the ITD recovered ₹ 1,076.06 crore from demands raised to rectify the errors in assessments that we had pointed out. There are 52,417 cases involving revenue effect of ₹ 1.13 lakh crore pointed out in audit which are remaining unsettled as of 31 March 2018 for want of replies from the ITD.

During FY 2017-18, 2,739 cases with tax effect of ₹ 2,735.17 crore became time-barred for initiating any remedial action.

## **Chapter III: Corporation Tax**

We pointed out 340 high value cases pertaining to corporation tax with tax effect of ₹ 4,866.66 crore. We classified these cases in four broad categories viz. (1) quality of assessments involving tax effect of ₹ 1,121.78 crore (118 cases); (2) administration of tax concessions/exemptions/deductions involving tax effect of ₹ 3,149.58 crore (141 cases); (3) income escaping

assessment due to omissions involving tax effect of ₹ 359.47 crore (56 cases) and (4) over-charge of tax/interest involving ₹ 235.83 crore (25 cases).

#### **Chapter IV: Income Tax**

We pointed out 132 high value cases of income tax with tax effect of ₹ 331.06 crore. We classified these cases in four broad categories as follows: (1) quality of assessments involving tax effect of ₹ 276.53 crore (85 cases); (2) administration of tax concessions/exemptions/deductions involving tax effect of ₹ 39.23 crore (26 cases); (3) income escaping assessments due to omissions involving tax effect of ₹ 5.17 crore (12 cases); and (4) over charge of tax/interest involving ₹ 10.12 crore (9 cases).

#### **Chapter V: Assessments relating to Agricultural income**

i) We audited 6,778 cases and found that in 1,527 scrutiny assessments cases (22.5 *per cent*), claim of exemption on account of agricultural income was allowed without adequate documentation and verification of supporting documents. We noticed that out of 1,527 cases where documentation and verification by Assessing Officer was inadequate, land records were not available in 716 cases (10.6 *per cent*) and proof of agricultural income and expenditure such as ledger account, bills, invoices etc. were not available in 1,270 cases (18.7 *per cent*). As such, it was not possible to determine whether the system in place was robust enough to ensure that assesseees were being allowed exemption for agricultural income, only after adequate examination in the process of assessment.

While allowance of exemption of agricultural income claims based on inadequate verification or incomplete documentation has been pointed out in respect of selected sample of scrutiny assessments, ITD needs to re-examine not only the remaining scrutiny cases, but also all cases where income has been allowed as agricultural income above a certain threshold, say ₹ 10 lakh or more, to ensure that exemption has been allowed only to eligible assesseees, and is based on appropriate documents and their verification.

ii) We observed that out of 3,133 cases checked in audit across nine states, in 48 cases there was a mismatch between the exemptions allowed in the assessment order vis-à-vis that reflected in the ITD database. The agricultural income in the ITD database continued to reflect the agricultural income as returned by the assesseees or depicted irrelevant figures in cases where agricultural income allowed was different from that claimed by the assessee.

iii) DGIT(Systems) had sought status reports regarding data entry errors while filling up the return in respect of 2,746 cases, where returned agricultural income was more than ₹ one crore. Only 26 out of 136 Commissionerates provided the information in respect of 327 cases. Even in this small sample, data entry errors were seen in 36, i.e., 11 *per cent* of the cases. Out of these 36 cases of data entry errors, 12 cases still remained to be corrected (January 2019). Errors in the database imply a dual risk: of loss of tax on one hand, and of harassment of tax payer on the other hand. The Department, therefore, needs to attend to similar cases for all Commissionerates to ensure without exception that data entry errors are corrected in all cases.

Existence of such data entry errors would render the AST data unreliable. Reasons for such persistent data entry errors is a matter of inquiry. The Department also needs to examine why a manual system of assessment is allowed to co-exist with an electronic system of assessment. It should work towards elimination of actual interface with the taxpayers.

iv) Audit also noticed non-compliance to provisions of the Act, such as, incorrect exemption granted for income derived from agricultural land, incorrect allowance of exemption for partial agricultural income, excess allowance of replantation expenditure/due to adoption of incorrect export turnover and exemption granted to non-agricultural income on account of sale of fish, sale of goat, sale of dry grapes, sale of milk etc.

#### **Chapter VI: Follow up audit of Exemptions to Charitable Trusts and Institutions**

In a follow-up test check of Exemptions to Charitable Trusts and Institutions during FY 2017-18, Audit noticed instances of irregularities such as (i) diversion of income/property by trusts to related group trusts/institutions as application of income; (ii) exemptions to assessees whose activities were not 'charitable' in nature; (iii) allowance of expenditure and accumulation where exemption was denied; (iv) lack of monitoring the investment of accumulated money by the trusts in the forms or modes other than those specified in the Act; (v) exemptions granted to trust on application of funds given to foreign universities; (vi) exemption to assessee where voluntary contribution including foreign currency donation was considered as corpus fund without specific direction of donor; (vii) non-cancellation of registration where activities of the Trust and Institutions are not in accordance with the provisions of the Act; and (viii) Failure of the Assessment Information System to levy surcharge.

The PAC in their 104<sup>th</sup> Report on the Action Taken by the Government on the observations/recommendations of the Committee contained in their 27<sup>th</sup> Report (16<sup>th</sup> Lok Sabha) on 'Exemptions to Charitable Trusts and Institutions' had also desired C&AG to make recommendations on how to remedy the gaps and prevent recurrences in future. The major recommendations are given below:

(i) *CBDT may consider amending the provision to make prior approval a pre-condition for foreign donation by a charitable trust or institution. The CBDT may also specify a limit say, 5 to 10 per cent of income for such donations.*

(ii) *CBDT may consider including a provision to make the trustee also liable in case where the provisions of the Act are not complied with.*

(iii) *Some of the provisions for exemptions to charitable trusts and institutions viz. section 11(1)(c) from on or after 1.4.1952, section 13(1)(d)(iii) after 30 November 1983, proviso to section 13(1)(d)(iii) from 1.6.1973 are from specific dates and apply to different trusts differently thereby not providing a level playing field. CBDT may consider bringing in a level playing field by inserting a sunset clause for such provisions applicable to those Trusts that have retained the benefit on ground of actions, having been taken earlier though these are prohibited now. A sunset clause for such provisions would ensure that benefits not available now are not available to anyone, and thus that all types of Trusts and Institutions are treated on similar lines. This will reduce the difficulties in assessing Trusts, when different trusts have to be treated differently, and reduce the "errors" in assessments. CBDT may consider giving a period of say, three years to the affected trusts to comply with the new provisions.*

(iv) *Since the issues pointed out in the earlier Audit Report no. 20 of 2013 are continuing, ITD is advised to review all the trust cases without exception and ensure that exemptions and concessions allowed to them are as per the provisions of the Act and registration of trusts not fulfilling the prescribed conditions are reviewed.*

#### **Chapter VII: Integrated audit of assessments of a Group Company**

We observed that there was an absence of effort by the ITD in cross linking material transactions with related parties to ensure the correctness/genuineness during the assessment of related companies in a group. The ITD lacks a system of information sharing amongst its various charges leading to assessments of group companies getting completed in standalone manner thereby missing sight of important issues which have bearing on determination of taxable income.

### **General Recommendations**

*While the Ministry has initiated action in respect of cases pointed out by Audit, it may be noted that these are only a few illustrative cases. In the entire universe of all assessments, including non-scrutiny assessments, there is every likelihood of such errors, of omission or commission, in many more cases. The CBDT not only needs to revisit its assessments, but also put in place a fool proof IT System and internal control mechanism to eradicate, so-called “errors”.*

*The IT system for direct taxes needs to be designed in such a way that it should ensure zero or minimal physical interface between the assessee and the tax officers. Government may consider the IT System for direct taxes being placed at arms length from CBDT, with an independent governmental body or organisation.*

*CBDT may examine whether the instances of “mistakes” noticed are errors of omission or commission and if these are errors of commission, then ITD should ensure necessary action as per law.*