

37

**STANDING COMMITTEE
ON FINANCE
(2005-2006)**

FOURTEENTH LOK SABHA

**MINISTRY OF FINANCE
(DEPARTMENT OF REVENUE)**

**DEMANDS FOR GRANTS
(2006-07)**

THIRTY-SEVENTH REPORT



मयमेव जयते

**LOK SABHA SECRETARIAT
NEW DELHI**

May, 2006 / Jyaistha, 1928 (Saka)

THIRTY-SEVENTH REPORT
STANDING COMMITTEE ON FINANCE
(2005-2006)

(FOURTEENTH LOK SABHA)

MINISTRY OF FINANCE
(DEPARTMENT OF REVENUE)

DEMANDS FOR GRANTS
(2006-07)

Presented to Lok Sabha on 22.5.2006

Laid in Rajya Sabha on 22.5.2006



LOK SABHA SECRETARIAT
NEW DELHI

May, 2006/Jyaistha, 1928 (Saka)

COF No. 37

Price : Rs. 114.00

© 2006 BY LOK SABHA SECRETARIAT

Published under Rule 382 of the Rules of Procedure and Conduct of Business in Lok Sabha (Eleventh Edition) and printed by Jainco Art India, New Delhi.

CONTENTS

	PAGE
COMPOSITION OF THE COMMITTEE	(iii)
INTRODUCTION	(v)
REPORT	1—600
ANNEXURES	
Annexure I	61
Annexure II	63
Annexure III	81
Annexure IV	87
APPENDIX	
Minutes of the sittings of the Committee held on 18th April, 2006	93
Minutes of the sittings of the Committee held on 19th May, 2006	96
Statement of Conclusions/Recommendations	98

COMPOSITION OF STANDING COMMITTEE ON
FINANCE (2005-2006)

Maj. Gen. (Retd.) B.C. Khanduri — *Chairman*

MEMBERS

Lok Sabha

2. Shri Jaswant Singh Bishnoi
3. Shri Gurudas Dasgupta
4. Shri Bhartruhari Mahtab
5. Shri Shyama Charan Gupta
6. Shri Gurudas Kamat
7. Shri A. Krishnaswamy
8. Shri Bir Singh Mahato
9. Dr. Rajesh Kumar Mishra
10. Shri Madhusudan Mistry
11. Shri Rupchand Pal
12. Shri Danve Raosaheb Patil
13. Shri Shrinivas D. Patil
14. Shri K.S. Rao
15. Shri Jyotiraditya Madhavrao Scindia
16. Shri Lakshman Seth
17. Shri G.M. Siddeshwara
18. Shri Ajit Singh
19. Shri M.A. Kharabela Swain
20. Shri Vijoy Krishna
21. Shri Magunta Sreenivasulu Reddy

Rajya Sabha

22. Shri M. Venkaiah Naidu
23. Shri Yashwant Sinha
24. Shri Chittabrata Majumdar
25. Shri S.P.M. Syed Khan
26. Shri Amar Singh
27. Shri C. Ramachandraiah
28. Shri Mangani Lal Mandal
29. Shri Santosh Bagrodia
30. Smt. Shobhana Bhartia
31. Vacant

SECRETARIAT

- | | | |
|---------------------------|---|-----------------------------|
| 1. Dr. (Smt.) P.K. Sandhu | — | <i>Additional Secretary</i> |
| 2. Shri A. Mukhopadhyay | — | <i>Joint Secretary</i> |
| 3. Shri S.B. Arora | — | <i>Deputy Secretary</i> |
| 4. Smt. Anita B. Panda | — | <i>Under Secretary</i> |
| 5. Shri M.L.K. Raja | — | <i>Committee Officer</i> |

INTRODUCTION

I, Chairman, Standing Committee on Finance having been authorised by the Committee to submit the report on their behalf, present this Thirty-Seventh Report on the Demands for Grants (2006-07) of the Ministry of Finance (Department of Revenue).

2. The Demands for Grants of the Ministry of Finance (Department of Revenue) were laid on the Table of the House on the 11th March, 2006. Under Rule 331E of the Rules of Procedure and Conduct of Business in Lok Sabha, the Standing Committee on Finance are required to consider the Demands for Grants of the Ministries/Departments under their jurisdiction and make reports on the same to both the Houses of Parliament. Thereafter the Demands are considered by the House in the light of the reports of the Committee. However, this year, the Demands for Grants of the Ministry of Finance (Department of Revenue) were passed in Lok Sabha on the 17th March, 2006 prior to their consideration by the Standing Committee on Finance. Nonetheless, the Committee examined the Demands for Grants (2006-07) of the Ministry of Finance (Department of Revenue) and issues arising out of these.

3. The Committee took oral evidence of the representatives of the Ministry of Finance (Department of Revenue) at their sitting held on 18th April, 2006 in connection with Demands for Grants (2006-07) of the Ministry of Finance (Department of Revenue). The Committee considered and adopted the draft Report at their sitting held on 19th May, 2006.

4. The Committee wish to express their thanks to the officers of the Ministry of Finance (Department of Revenue) for the co-operation extended by them in furnishing written replies and for placing their considered views and perceptions before the Committee.

5. For facility of reference, the observations/recommendations of the Committee have been printed in thick type.

NEW DELHI;
19 May, 2006
29 Vaisakha, 1928 (Saka)

MAJ. GEN. (RETD.) B.C. KHANDURI,
Chairman,
Standing Committee on Finance.

REPORT

INTRODUCTORY

Ministry of Finance—Department of Revenue

The Department of Revenue functions under the overall direction and control of the Secretary (Revenue). It exercises control in respect of matters relating to all the Direct and Indirect Union Taxes through two statutory Boards namely, the Central Board of Direct Taxes (CBDT) and the Central Board of Customs and Central Excise (CBEC). Each Board is headed by a Chairman who is also *ex-officio* Special Secretary to the Government of India. Matters relating to the levy and collection of all Direct taxes are looked after by the CBDT whereas those relating to levy and collection of Customs and Central Excise duties and other Indirect taxes fall within the purview of the CBEC.

2. The Department of revenue administers the following Acts:—

1. Income Tax Act, 1961;
2. Wealth Tax Act, 1958;
3. Expenditure Tax Act, 1987;
4. Benami Transactions (Prohibition) Act, 1988;
5. Super Profits Act, 1963;
6. Companies (Profits) Sur-tax Act, 1964;
7. Compulsory Deposit (Income Tax Payers) Scheme Act, 1974;
8. Chapter VII of Finance (No.2) Act, 2004 (relating to Levy of Securities Transactions Tax);
9. Chapter VII of Finance (No. 2) Act, 2004 (Relating to Levy of Banking Cash Transaction Tax)
10. Chapter V of Finance Act, 1994 (relating to Service Tax);
11. Central Excise Act, 1944 and related matters;
12. Customs Act, 1962 and related matters;
13. Medicinal and Toilet Preparations (Excise Duties) Act, 1955;
14. Central Sales Tax Act, 1956;

15. Narcotic Drugs and Psychotropic Substances Act, 1985;
16. Prevention of Illicit Traffic in Narcotic Drugs and Psychotropic Substances Act, 1988;
17. Smugglers and Foreign Exchange Manipulators (Forfeiture of Property) Act, 1976;
18. Indian Stamp Act, 1899 (to the extent falling within jurisdiction of the Union);
19. Conservation of Foreign Exchange and Prevention of Smuggling Activities Act, 1974;
20. Foreign Exchange Management Act, 1999; and
21. Prevention of Money Laundering Act, 2002.

3. Department looks after the matters relating to the above-mentioned Acts through the following attached/subordinate offices:—

1. Commissionerates/Directorates under Central Board of Excise and Customs;
2. Commissionerates/Directorates under Central Board of Direct Taxes;
3. Central Economic Intelligence Bureau;
4. Directorate of Enforcement;
5. Central Bureau of Narcotics;
6. Chief Controller of Factories;
7. Appellate Tribunal for Forfeited Property;
8. Income Tax Settlement Commission;
9. Customs and Central Excise Settlement Commission;
10. Customs, Excise and Service Tax Appellate Tribunal;
11. Authority for Advance Rulings for Income Tax;
12. Authority for Advance Rulings for Customs and Central Excise;
13. National Committee for Promotion of Social and Economic Welfare;
14. Competent Authorities appointed under Smugglers and Foreign Exchange Manipulators (Forfeiture of Property) Act, 1976 and Narcotic Drugs and Psychotropic Substances Act, 1985; and
15. Financial Intelligence Unit, India (FIU-IND)

4. The detailed Demands for Grants of the Ministry of Finance were presented to Lok Sabha on March 11, 2006. The details of the demands of Department of Revenue, Central Board of Direct Taxes (CBDT) and Central Board of Excise & Customs (CBEC) are as under :-

(In thousands of Rupees)

Demand No.	Deptt. of Revenue	Revenue	Capital	Total
	Voted:	3,339,07,00	2,06,00	3,341,13,00
Demand No. 42:	Direct Taxes	Revenue	Capital	Total
	Voted:	1,305,98,00	28,00,00	1,333,98,00
Demand No. 43:	Indirect Taxes	Revenue	Capital	Total
	Voted:	1,614,89,00	98,93,00	1,713,82,00

5. The report reviews the performance of the Ministry of Finance (Department of Revenue) during the year 2005-2006.

6. In the present Report, the Committee have examined the following issues arising out of the Budget (2006-07) proposals:—

1. Refunds – Direct Taxes
2. Arrears of Revenue
3. Exemptions
4. Restructuring of Central Board of Direct Taxes and Central Board of Excise & Customs – Shortage of Manpower
5. Computerisation
6. Service Tax

CHAPTER I

7. The Committee, in their 17th report on Demands for Grants (2005-06), presented to Parliament on 20-4-2005, had examined two detailed Demands as well as seven issues relating to the overall performance of the Department of Revenue, which are as under:—

1. Demand No.43 – Information Technology
2. Demand No.44 – Investments
3. Revenue Targets
4. Vigilance Mechanism
5. Settlement Commissions
6. Computerisation
7. Arrears of Revenue
8. Appeals
9. Central Economic Intelligence Bureau and Financial Intelligence Unit - India

8. The Report contained 9 recommendations. The Finance Minister made a statement on the floor of the House on 20-12-2005 under Direction 73A of the Direction by the Speaker on the status of implementation of the recommendations. The Action Taken replies to three recommendations of the Committee were accepted by the Committee.

9. These recommendations pertained to the following issues:

- (i) Information Technology,
- (ii) Revenue Targets,
- (iii) Settlement Commissions.

10. In view of the reasons cited by the Government, the Committee did not desire to pursue two recommendations relating to Demand No. 44—Investment and Central Economic Intelligence Bureau and Financial Intelligence Unit – India.

11. Further, the Committee were not in acceptance of the replies furnished by the Government in respect of their four recommendations on which the Ministry have again furnished action taken notes. These recommendations pertain to the following issues:

1. Vigilance Mechanism,
2. Computerisation efforts,
3. Arrears of Revenue and
4. Remedial measures to bring down pendency of appeals.

CHAPTER II

1. Refund – Direct Taxes

12. The Committee note that while adequate procedures and safeguards have been laid down under Chapter XIX of the Income Tax, 1961 regarding issue of and proper accounting of refunds, these were not being adhered to by the Department resulting not only in delays but frauds too. During the course of examination the Committee took serious note of the large-scale refund frauds detected by the RBI in the Department of Income Tax and desired to have complete details on the same. In this connection, the Government, in their written reply, furnished the following details:

“The Income Tax Department found that bogus Income-tax returns claiming large refund on the basis of bogus TDS certificates were being filed in company circles. On basis of an exercise carried out, FIRs were filed by various officers with the Economic Offence Wing of Delhi Police. The Police arrested four persons including Shri Amit Chawla, Tax Assistant for alleged forgery in Income-tax Refund. Refunds were encashed by opening accounts with ABN Amro Bank-Barakhamba Road & Bank of India—Vikaspuri. These amounts were then transferred to various accounts maintained with the other banks such as Corporation bank, ICICI bank, Vaish Cooperative bank, Punjab National Bank etc. Shri Amit Chawla has since been placed under suspension. Details have been obtained from the Delhi Police recently and Disciplinary Action against the official is being taken shortly.

Following steps are being taken to prevent repetition of the scam in future:

- (i) Introduction of Electronic Clearing System (ECS) for credit of refund directly in the bank account of the taxpayer in respect of refunds of certain types. It is proposed to make ECS applicable for all refunds in future.
- (ii) It has been made mandatory for all taxpayers claiming refund of tax to mention their bank account details in the return of income. Necessary changes in the return form have been made. It is proposed that all refunds to be issued by the Income Tax Deptt. would carry the bank account details of the assessee.

- (iii) Letters have been issued to the Cadre Controlling Chief Commissioner to ensure that the books of Refund Orders should be kept in the personal custody of the Assessing Officer concerned. Any loss/theft of Refund Orders may be immediately notified to higher authorities, the clearing bank and the Police.
- (iv) Letters have been issued to the Cadre Controlling Chief Commissioner to ensure that for correct encashment of the Refund Order, the Advice Notes must be sent by the Assessing Officer direct to the clearing bank through authorized departmental personnel only.
- (v) Another letter has been issued to all Cadre Controlling Chief Commissioners by which Common Irregularities observed by Reserve Bank of India in the issue of Refund Orders were pointed out to prevent fraudulent issue and encashment of refund* ."

13. When enquired by the Committee on bogus claim of refunds on the basis of bogus TDS certificates, the Government, in their written reply, stated as follows:

"Some cases of bogus claim of refunds by filing fictitious returns of income with fictitious TDS certificates have come to the notice of the Government. The quantum of such refund is still under investigation. Criminal proceedings have been initiated by Police and based on the report further administrative action will also be taken."

14. In this connection, the Committee desired to know the *modus-operandi* used in such frauds. The Government, in their written reply, stated the following :

"Preliminary inquiry has indicated that bogus refunds have been issued in cases where assesseees are non-existent, TDS and tax payments certificates and challan appear to be fabricated. Further, the refunds have reached wrong persons and wrong bank accounts. It has also been noticed that stolen refund stationary has also been used for such purposes."

15. The Committee desired to be apprised of the procedure involved in the refund process and the steps taken to reduce the possibility of frauds, to which the Government in their written reply, responded as follows:

"The returns filed by assesseees are processed and refunds determined. Thereafter, refunds are issued by the Assessing Officers.

*Annexure I.

With the comprehensive computerization of the Income Tax Department, the whole process of issue of refunds is going to be streamlined. The following steps are going to make issue of refunds safe and quicker:—

- a) With introduction of Electronic Clearing System (ECS), the credit of refunds will directly be made in to the Bank account of the tax payer. It is proposed to make ECS applicable for all refunds cases in future.
- b) It has been made mandatory for all taxpayers claiming refunds of tax to mention their bank account details in the return of income. Necessary changes in the Income Tax Return form have already been made. It is also proposed that all refunds to be issued by the Department would carry the bank account details of the assesseees.
- c) It is also proposed to dematerialize TDS certificates so as to preclude possibility of claim of refund against fictitious TDS certificates.
- d) Administrative approval of Commissioner for issue of refunds. Instructions to the field officers to keep refund stationary in personal custody and to send Advice Notes of refunds to clearing banks through authorized Departmental personnel are some other measures taken for this purpose.”

16. Further delving into the matter the Committee asked whether any action has been taken on those who have not followed the procedure mentioned in the Circular issued by CBDT. The Government, in their written reply, stated as under:

“CBDT’s letter F.No. 385/40/2005-IT(B) dated 19.9.2005 was issued as a general guideline for avoiding common irregularities committed in the process of issue of refunds so as to safeguard refunds from any possible fraud . Wherever there would be a loss of revenue on account of non-observation of such guidelines, suitable administrative action would be taken against the erring officers.”

17. During the oral evidence of the representatives of the Ministry, the Committee noted with concern the laxity in the Department in granting refunds. In this connection, the Chairperson, Central Board of Direct Taxes (CBDT) clarified as follows:

“As far as procedure for granting refunds is concerned, the refunds can be granted only after return of income is filed in which the

claim for refund is made. After that, the return is processed. Then as a result of the processing, whatever amount is due as payable to the assessee is issued in the form of refund voucher. From 2006 onwards, we are making it mandatory for every person, who is claiming a refund, to give his or her bank account number also so that the refund can be credited directly in the bank account. This way lost vouchers or invalid vouchers being raised by taxpayers would be sorted out. Our effort is there to process the returns wherever refunds are due at the earliest and on priority basis. Of course, instructions are there, though not in the Statute. Administratively instructions are there to issue refunds within four months from the date of filing of the returns. In most of the cases, refunds are being issued within four months. In certain cases, yes, refunds do take a little time because either claims do not match with the interest certificate which the assessee has filed or the interest certificate pertains to a different year from what it is being claimed in the year under consideration. Duplicate interest certificates are filed on which we cannot allow the claim of refunds unless the original is produced. In the case of duplicates, an Indemnity bond is required to be filed by the taxpayer if he claims the amount. So we take these precautions. In certain cases, I do admit that refunds are delayed but there are valid reasons for that. Otherwise, by and large, they are being issued within four months."

18. The Committee are perturbed to find that bogus income-tax returns claiming large amounts of refunds on the basis of bogus TDS certificates were filed by some unscrupulous persons. The point of serious concern is the forgery committed by the tax officials themselves who connived with these persons, resulting in such fraudulent issue of refunds. The Committee feel that this is an ample proof of the extent of corruption in the tax machinery which could have been avoided, had the internal vigilance mechanism of the Department been more alert. In the Committee's view, lack of efficiency and integrity in the tax machinery leads not only to leakage of tax revenue but also to tax evasion. Although the Department has stated to have issued instructions/circulars to the field formations, yet the fact cannot be ignored that this has been done only after receiving Reserve Bank of India (RBI)'s communication pointing towards irregularities in the issue of refund orders. The Committee note that the system of issue of refunds is going to be streamlined by making ECS applicable for all refunds in future, making it mandatory to quote the assessee's bank account details in the refund orders and immediate reporting of any loss/theft of refund orders to

the higher authorities, the clearing bank and the police etc. However, the Committee are constrained to observe that corrupt officials succumbing to avarice has become bane of Income Tax Department. Further, there has been a systemic failure in the form of lack of proper checks and balances and a deficient supervision by the senior officials and the internal vigilance mechanism on such officials. The Committee take strong exception to such failures in the Department and desire the Government to furnish complete details of the extent of such fraud in terms of revenue loss and the penal action taken against the tax officials found to be involved. The Committee also recommend that the instructions of the Department on issue of refunds should be followed scrupulously and diligently with supervision at senior level in all their field formations.

19. Another disquieting feature about issue of refunds as noted by the Committee has been the inordinate delays in the issue of refunds. The Committee find that though there are administrative instructions to issue refunds within a period of four months, there have been several cases of delays. The Committee advise the Government to go into the discrepancies that have been stated to delay issue of refunds and take necessary action so that such instances do not recur.

2. ARREARS OF REVENUE

Direct Taxes:

20. The status of outstanding direct tax arrears in different zones, as on 1.1.2006, is as under:

Chief Commissioner Region	Amount of arrears of direct taxes outstanding (Rs. crore)
Mumbai	46,666
Delhi	13,938
Chandigarh	721
Kolkata	4,083
Lucknow	5,189
Kanpur	361
Patna	1,737
Guwahati	155
Bhubaneshwar	116
Ahmedabad	3,077
Bhopal	718
Jaipur	312
Pune	1,326
Nagpur	271
Bangalore	1,948
Kochi	318
Hyderabad	1,316
Chennai	1,479

21. When the Committee sought to know the reasons for mounting arrears year after year, the Government, in a written note, stated *inter alia* as follows:

“Recovery from arrear of direct taxes is a continuous process in which old demands are liquidated (by way of collection or reduction) and new demands are added. The amount of arrears outstanding cannot be recovered immediately as part of the arrears is contested in appeal before the Courts and other appellate authorities. Moreover, a part of the outstanding demand is also difficult to recover for various reasons including non-traceability

of the taxpayer, inadequacy of assets, liquidation of company, stay granted by Courts, etc. Thus, while the process of liquidation or collection of the arrears is long and disposal of appeals by the Courts, Tribunals and other authorities is slow, the demands are being continuously raised by the Department in various cases, leading thereby to net addition to the arrears year after year.

Moreover, there are certain other factors that cause accumulation of arrears, which are as follows:

- The arrears are required to be updated at the end of each year by adding the accrued interest on the outstanding amount of tax, thereby presenting an inflated and unrealistic position of the arrears.
- As per the provisions of Debt Recovery Tribunal Act the secured claims of banks and other creditors have a precedence over tax dues of the Government.
- No representation of Income Tax Department before Courts dealing with merger and acquisition of companies as a result of which, the recoverability of tax arrears of the companies involved is not examined before merger/acquisition is ordered by the Courts.”

22. The Government in their written response to a related query raised by the Committee on the reasons for the non-recovery of such arrears, stated as under:

“Out of the outstanding arrear demand of Rs. 84,662 crore outstanding as on 1.1.2006, only a sum of Rs. 4,890 crore is clearly collectible. The process of collection of balance demand is fraught with impediments for the following reasons:

1. The demand has been stayed by the Courts/Tribunal.
2. Demand pertains to persons notified under section 3 of Special Court (Torts) Act, 1992 and so no recovery can be made directly from such persons. (Demand in scam cases)
3. Assessee is not traceable and so cannot be proceeded against for recovery or has no assets from which recovery can be made.
4. Case is before B.I.F.R. and so recovery cannot be enforced.
5. Company is under liquidation and the claim of Revenue would be settled as per the orders of the High Court.

6. Case is before Settlement Commission and so the income-tax authorities can not proceed with recovery proceedings.
7. The demand is arising from protective assessment or the Department is in appeal on similar issues in earlier years.
8. The demand has been stayed by the income-tax authorities, as in earlier years the disputes were decided in favour of the assessee.
9. The demand is covered by installments for tax-payments granted by the income-tax authorities.
10. Demand is being processed for write-off as the demand has become irrecoverable beyond doubt

For the above reasons and prolonged litigation, the entire amount of demand that is created by the Income Tax Department does not get collected immediately. While the process of liquidation or collection of the arrears is long and disposal of appeals by the Courts, Tribunals and other authorities is slow, the demands are being continuously raised by the Department in various cases, leading thereby to net addition to the arrears year after year.”

23. The steps taken by the Government to recover the tax arrears have been stated as follows:

“Apart from the statutory steps being taken for recovery of outstanding tax dues as prescribed under the Income Tax Act (including attachment of bank account, debtors, etc, attachment and sale of immovable property, etc.) the following special measures are also being taken to expedite recovery of direct tax arrears:

- (a) Monitoring of recovery of arrears in large cases by a Task Force.
- (b) Identification of cases involving substantial amount of arrears pending before Commissioners (Appeals) and ITAT and requesting these authorities to dispose of such appeals early so that the demand can be collected during the current financial year itself.
- (c) Requesting the President of ITAT not to allow stay of demand beyond 180 days as prescribed in section 254(2A) of the Income-tax Act.
- (d) Requesting Settlement Commission to dispose of high-demand cases expeditiously.

24. When asked about the legal or administrative backup that are required by the department to recover such dues, the Government in their written reply stated the following:

“There are certain legal backups that would be helpful in effecting expeditious recovery of direct tax arrears, which are as follows:

- a. Provisions for allowing only the principal part of tax to be shown as arrears without adding the interest accrued on the principal tax. The present practice of adding accrued interest on the outstanding arrears at the end of the year presents an inflated and unrealistic position of the arrears.
- b. Enabling provisions under Debt Recovery Tribunal Act to establish the supremacy of sovereign dues like tax arrears over secured claims of banks and other creditors.
- c. Necessary provisions for representation of Income Tax Department before Courts dealing with merger and acquisition of companies so as to enable the Department to examine the recoverability of tax arrears of the companies involved after the merger/acquisition.”

25. The Revenue Secretary during the oral evidence stated the following on the trend in collection of revenue arrears:

“There has also been significant increase in the amount of recovery of arrears from Rs. 3,930 crore in 2001-02 to Rs. 5,470 crore, Rs. 5,540 crore and Rs. 7,084 crore in the next three years. During 2005-06, an amount of Rs. 5,996 crore has been recovered from arrears up to February 2006.”

26. The Revenue Secretary further added:

“In respect of arrears collections, we had set for ourselves a target of Rs. 2,700 crore to be recovered during the financial year 2005-06—Central Excise at Rs. 1,682 crore, Customs at Rs. 718 crore and Service Tax at Rs. 300 crore. As against this, the Department has collected total arrears of Rs. 3,140 crore. This also represents a growth of 19 per cent over the last year’s collection of Rs. 2,643 crore.”

27. The Committee also raised concern about the concentration of huge amount of arrears in the two metropolitan cities *i.e.* Mumbai and Delhi, to which the Chairperson of CBDT stated the following:

“As far as arrears are concerned, yes, you will find that the amount of arrears outstanding against Mumbai and Delhi are the highest

in the country. As far as Mumbai is concerned, more than Rs. 35,000 crores are standing against the scam-related cases only, for which the Department has no power to recover because those are persons notified under Section 3 of the Special Court Act, 1991. We can get the money of the tax only when released by that court. So, more than Rs. 35,000 crores are locked up in Mumbai alone on account of those scam-related cases.”

28. In a written note submitted subsequently, the Government stated as follows:

“As regards the concentration of arrears in Delhi and Mumbai, it is for the reasons that these two cities are the largest collection centers for direct taxes. Since almost 50% of the collections are made from these two centers, it is only natural that the arrears are also concentrated in these two stations. Moreover, arrears of Mumbai contain the arrears in the cases of Harshad Mehta Group and Ketan Parekh Group, where large amount of arrears are locked up.”

29. To a specific question as to the status of those cases, the Chairperson, in her oral submission, stated as under:

“So far, they are not before the Supreme Court. They are at the level of either the first appellate authority or the tribunal.”

30. The Committee expressed concern about the huge amount of tax arrears to which the Chairperson replied as follows:

“Rs. 35,000 crore is not the tax arrears. It also includes the interest component on the uncollected amount of this arrears which is added at the end of every year, on the 31st March as per the Statute. The interest component is also included in that amount and whatever begins like that at the end of 10 years, it can be like this. It includes the interest amount also.”

31. When the Committee desired to know as to how certain cases of arrears are concluded as non-recoverable, a representative of the CBDT during oral evidence, stated the following:

“...the total arrears which finally come and presented here, are collected case wise from the lowest rank. The ITO selects the cases where the recovery cannot be made. The major reasons for that are either the assessee is not traceable or he does not have the asset from which the recovery can be made. These are the two

major reasons we are finding where assets matching liability are not available with the assesseees. Then, it is compiled by the Additional Commissioner range-wise. Then, it is done by Commissioner wise and town-wise it is collected, and then the national data is collected. About the case, when we find that the assets are not available, then there is a Committee in all major towns at the commissioner level. We have distributed the cases according to the quantum of the arrears. Up to Rs. 10,000 level, it can be done at the range level. Then, if the figure goes up, the Commissioner can wind up and he can write-off. If the arrears is more than Rs. 25 lakh, then it is brought to the Board level.

32. The Revenue Secretary, during the oral evidence, informed the Committee about the steps taken by the Government to deal with delay in disposal of tax cases, as under:

“We have instituted a system of by-monthly kind of an institutional discussion between the Law Secretary and myself on all these issues. So, we will look at this aspect also and see what is possible to expedite it. If something can be done, we will bring it to the notice of the Government also.”

Indirect Taxes

33. The trend to fix targets for arrears realization by the Government has been started since the financial year 2004-05. The year-wise realization of arrears of revenue vis-à-vis targets for the financial years 2004-05, 2005-06 & 2006-07 are as under:

Head of duty	(Rs in Crore)					
	2004-05		2005-06		2006-07	
	Target	Realisation	Target	Realisation	Target	Realisation
Central Excise	2250	1799.38	1682.4	1657.94	1300	-
Customs	750	843.49	717.6	600.29	650	-
Service Tax	-	-	300	881.42	500	-
Total	3000	2642.87	2700	3139.65	2450	-

Separate reporting of Service Tax was started from December, 2004. Earlier, it was included as a part of Central Excise arrears collections.”

34. The Committee desired to know the reasons for non-recovery of arrears. The Government in their written reply stated the following:

“There are a total arrears of Rs. 21368 Crore as on 31.01.2006. Out of these, a sizable amount of arrears of Rs. 7132 Crore (Approx.) are stayed in various Courts, hence, not recoverable. There are also substantial unstayed arrears which are reportedly restrained and hence unrecoverable owing to the following reasons:

- The defaulting units were under BIFR and hence no recovery proceedings could be initiated;
- The assets of the defaulting units were taken over by official liquidator;
- Arrears were not recoverable owing to the proceedings initiated by Debt Recovery Tribunal;
- The sale proceeds of the available assets fell short of the arrears;
- Cases pending for COD clearance;
- Cases within appeal period.”

35. The strategy of the Government, as per the written note furnished to the Committee by them, to realise the arrears, are as follows:

“The Government has constituted the Task Force headed by a Chief Commissioner to expedite realization of arrears in indirect tax. Important measures taken in this regard are :—

- (a) Sensitization at the level of Commissioners/Chief Commissioners by holding meeting at Nodal/Zonal levels;
- (b) filing applications for vacation of stay orders;
- (c) filing early hearing applications in Courts/CESTAT;
- (d) targeting defaulters with coercive action; and
- (e) persuading major units to pay outstanding arrears.”

36. According to the Ministry of Finance, following is the action plan proposed for the said Task Force to expedite the realisation of such arrears:

“The Field Officers have been sensitized to effectively pursue the recovery cases and the following action plan has been decided :

(A) *Filing of Applications for Stay Vacation/Early Hearing in Courts/CESTAT*

A total arrears of Rs. 7132 Crores (approx.) is locked up in various Courts/CESTAT as stayed arrears. The field formations have been

sensitized to file applications for stay vacation/early hearing, particularly in the deserving cases. The Chief Departmental Representative, (CESTAT) has also been requested to take up all these matters on priority basis.

(B) Follow up cases pending in BIFR/DRT/OL/COD

The arrears of units ending up in BIFR/DRT proceedings is another area of concern. It has been decided that these cases may be closely monitored and properly defended, as substantial amount of revenue is locked up.

(C) Write-off of irrecoverable cases of arrears

As regards irrecoverable arrears which are being carried forward from year to year without any fruitful realization of arrears. All the Chief Commissioners have been directed to initiate action towards write-off in those cases where they were of the considered view that the arrears were not recoverable for valid reasons.

(D) Timely disposal of all adjudication cases pending at the level of Commissioners

Considerable revenue is locked up in adjudication cases at the level of Commissioners and they have been directed to expeditiously dispose of such cases, so that the connected amount of arrears can be recovered.

(E) Quick implementation of favourable orders of CESTAT/Courts

The Task Force is closely monitoring all the cases of favourable orders from CESTAT, High Courts and the Supreme Court. The list of cases collectively decided in favour of Revenue by CESTAT, are forwarded to all the Nodal officers for effective monitoring and realization of arrears in such cases.

(F) Defaulters on CBEC website

The list of defaulters against whom Sec. 142 notices have been issued, and those which have not been stayed by the courts have already been displayed on CBEC website. All Commissionerates have been directed to keep the Directorate of Systems updated in this regard but also browse the website in connection with the recovery action at their end."

37. Responding to query from the Committee, the Government furnished a note on the status of outstanding Indirect tax arrears in different Chief Commissionerates as on 31-1-2006, which is as under:

	Total arrears at the end of the month			Stayed arrears			Unstayed arrears									
							Restrained Arrears (BIFR/DRT /OL/COD/ cases within appeal period)			Unrestrained Arrears			Total			
	No. of cases	Revenue involved (Rs. in crs.)	(Total of col. 3 & 13)	No. of cases	Revenue involved (Rs. in crs.)	(Total of col. 4 & 14)	No. of cases	Revenue involved (Rs. in crs.)	Recoverable	No. of cases	Revenue involved (Rs. in crs.)	Non-Recoverable (fit for write-off cases)	No. of cases	Revenue involved (Rs. in crs.)	Total	
	1	2		3	4		5	6	7	8	9	10	11	12	13	14
	(Total of col. 3 & 13)	(Total of col. 4 & 14)											(Total of col. 7 & 9)	(Total of col. 8 & 10)	(Total of col. 5 & 11)	(Total of col. 6 & 12)
Central Excise	39877	15823.34		7933	5437.48		15108	7254.15	13615	2462.83	3221	668.88	16836	3131.71	31944	10385.86
Customs	19557	4869.84		1265	1366.21		1968	1818.7	12595	1078.5	3729	606.44	16324	1684.9	18292	3503.63
Service Tax	15818	674.93		355	327.82		1647	138.22	13624	197.59	192	11.3	13816	208.89	15463	347.11
Total	75252	21368.11		9553	7131.51		18723	9211.11	39834	3738.87	7142	1286.62	46976	5025.49	65699	14236.6

38. The Committee further raised a point pertaining to the proposed action for speedier disposal of cases pending before various appellate authorities, to which the Government, in their written reply, responded as follows:

“Adjudication of cases take time due to various reasons such as :

- Adjournments sought by the assesseees.
- Assesseees/parties have not submitted replies to Show-Cause Notices or subsequent submissions have not been given by the assesseees.
- Supply of relied upon documents to the assesseees.
- The request for cross-examination wherever appropriate, has to be accepted.
- SCNs issued following audit objections have to be kept pending till the closure of objection by C&AG
- Similar issue pending before a higher appellate authority for decision.

However, the Committee were further informed that taking note of the pendency in adjudication, the Central Board of Excise and Customs diverted posts of Commissioner and appointed Commissioner (Adjudication) in those zones, which had high pendency. Similarly the Board also directed all quasi-judicial authorities to expeditiously adjudicate cases pending before them in order to reduce the pendency in adjudication. In the same vein, the Ministry pointed out that while old cases are decided, new cases crop up adding to the pendency.

As far as realization of arrears is concerned, the Committee were informed that the amounts involved can not be immediately realized due to various factors such as :

- Stay orders by various Courts/Tribunal.
- The defaulting units are under BIFR and hence no recovery proceedings can be initiated;
- The assets of the defaulting units are taken over by official liquidator;
- Arrears are not recoverable owing to the proceedings initiated by Debt Recovery Tribunal;
- The sale proceeds of the available assets falls short of the arrears;
- Cases pending for COD clearance;
- Cases within appeal period.”

39. The Government's reply in response to the query regarding targets fixed for the actual recovery of arrears is as follows:

"No target for recovery of arrears was envisioned in the restructuring proposal. However, the Department has given internal targets to the field units for recovery of arrears in various years, including years before the restructuring. The target has generally been to collect 15% of the arrears outstanding at the beginning of the year. However, the actual realization of arrears has been in the range of 7%—9%, as shown below:

Financial Year	Arrear Demand outstanding at the beginning of year (Crore)	Cash Collection out of outstanding arrears (Crore)	%age of cash collection
□			
2004-05	94063	7084	7.53%
2003-04	74824	5540	7.40%
2002-03	76313	5470	7.17%
2001-02	57399	3930	6.85%
2000-01	53959	4970	9.21%
1999-2000	44862	2983	6.65%
1998-99	41828	3049	7.29%
1997-98	34806	2845	8.17%
1996-97	29261	2321	7.93%

40. Taking a serious view of the recurring trend of huge pendency of arrears, the Committee had, in their 33rd Report (14th Lok Sabha) desired the Government to take concerted efforts to reduce such arrears. Although the Government are stated to have taken measures to recover the arrears, there has been hardly any substantial increase in the collection of arrears over the years. It is evident from the fact that as on 31.1.2006 the outstanding arrears demand in direct taxes amounts to a whopping Rs. 84662 Crore (approx.) and in indirect taxes, it is around Rs. 21,368.11 crore. The Committee would also like to particularly point out that majority of the arrears are pending to be recovered from the two cities of Mumbai and Delhi. The Committee find that an amount of Rs. 35000/- crore in Mumbai alone is outstanding against stock-scram related cases of Harshad Mehta Group and Ketan Parekh Group, and are stated to be at the initial stages either at the first appellate authority or the Tribunal. No serious efforts seem to have been made to get the cases decided early. From this, the Committee are led to conclude that recovery of arrears is moving at a painfully slow pace. The Committee hope

that at last now the Government would make concerted efforts to realise the arrears with due despatch.

41. In so far as indirect taxes are concerned, the Committee note that as on 31.1.2006, out of the total outstanding arrears of Rs. 21,368.11 crore the unstayed arrears demand is around Rs. 14236.6 crore. From the information furnished to them, the Committee also note that the targets of recovery of arrears are being reduced over the years in both Central Excise and Customs. Moreover, the targets of recovery fixed for 2006-07 is even below than the recoverable amount. In this connection, the Committee have been given to understand that a task force has been constituted to expedite the realisation of arrears with certain specific measures e.g. sensitization at the level of Commissioners/Chief Commissioners etc., filing application for vacation of stay orders etc. Though the Committee feel that this is a step in the right direction, yet in their view, as the adjudication of cases attribute, to a great extent, to realise the arrears, they are of the opinion that the Government may examine fixing a time-limit to expedite the adjudication procedure.

42. The Committee note that one of the major reasons for concluding certain portion of arrears as 'non-recoverable' is that the assesseees are not traceable. In this backdrop, the Committee recommend the Government to further strengthen their institutional and procedural safeguards so that traceability of assesseees could be managed well and revenue due to the Government could be recovered.

43. The Committee are given to understand that a sizeable number of cases are either pending with IT authorities/Appellate Tribunals/Courts or the demands have been stayed by them. The Committee while expecting that cases pending before IT authorities would be disposed of expeditiously, desire to either get the stays vacated as early as possible or persuade the Tribunal not to allow stays beyond 180 days as provided under Section 254 (2A) of Income Tax Act, 1961. In so far as the huge pendency of recovery cases at the level of Tribunal/courts is concerned, the Committee note that there exists an institutional mechanism through which the Revenue Secretary can interact the Law Secretary on bi-monthly basis to discuss the matter. However, going by the past record of pendency, the Committee are of the opinion that this mechanism, perhaps, has not been utilised fully. The Committee urge the Government to optimally utilise this mechanism to expedite the disposal of cases and thereby increase the realisation of tax arrears. They desire to be apprised of the outcome of such meetings on a regular basis.

3. EXEMPTIONS

44. The Committee drew the attention of the Ministry of Finance during their oral evidence towards the fact that many exemptions have outlived their utility and are no longer justified. They were of the opinion that providing too many exemptions has resulted in substantial revenue foregone, which is detrimental to the country's economy.

Direct Taxes:

45. According to the Ministry, under the Income Tax Act 1961, provisions granting tax exemptions are contained in Chapter III titled INCOMES WHICH DO NOT FORM PART OF TOTAL INCOME. The relevant provisions are:—

- (i) Section 10 contains 78 clauses under which various type of income are exempted.
- (ii) Section 10A provides exemption to newly established undertakings in Free Trade Zones etc.
- (iii) Section 10AA provides exemption to newly established units in Special Economic Zones.
- (iv) Section 10B provides exemption to newly established hundred percent export oriented undertakings.
- (v) Section 10BA provides exemption in respect of export of certain articles or things.
- (vi) Section 10C deals with special provisions in respect of certain industrial undertakings in North-Eastern Region.
- (vii) Section 11 provides exemption to income from property held for charitable or religious purposes.
- (viii) Section 12 deals with the exemption of income of trusts or institutions from contribution.
- (ix) Section 13A deals with the provisions relating to incomes of political parties.

The Central Government issues notifications under the various provisions of the Income Tax Act 1961 including those under Chapter III mentioned above."

46. When enquired about the revenue foregone due to Income Tax exemptions for the year 2004-05, the Government, furnished the following details:

**Major tax expenditure on corporate tax payers
during financial year 2004-05**

Sl. No.	Nature of Incentive/ deduction	Revenue foregone (Rs. in crs.)
1.	Export profits of software producing units located in Software Technology Parks (section 10A)	7080
2.	Export profits of units located in Special Economic Zones, including Export Processing Zones and Free Trade Zones (section 10A)	1340
3.	Export profits of units located in Export Oriented Units (section 10B)	2320
4.	Profits derived from development of infrastructure facilities, SEZs and Industrial Parks, generation of power, providing telecommunication services (section 80-IA)	5832
5.	Profits derived from housing projects, production of mineral oil, development of scientific research, integrated business of handling, storage and transportation of foodgrains, industries set up in backward areas (section 80-IB)	11523
6.	Profits derived by units set up in Special category States like North-Eastern States, Uttaranchal, Himachal Pradesh and Jammu and Kashmir (Section 80-IC)	362
7.	Accelerated depreciation (section 32)	27077
8.	Weighted deduction for scientific research and development [section 35 (2AB)]	2318
Total		57852

Profile of sample companies across profit range

Sl. No.	Profits before tax	Number of companies	Share in total profits	Share in total taxes	Effective rate of tax
1	2	3	4	5	6
1.	Less than Zero	380	0	7.54	Infinity
2.	Zero	213	0	1.84	Infinity

1	2	3	4	5	6
3.	0-5 lakhs	52	0.001	0.09	13.32
4.	5 lakhs – 10 lakhs	33	0.002	0.003	24.90
5.	10 lakhs – 25 lakhs	68	0.01	0.01	16.90
6.	25 lakhs – 50 lakhs	74	0.03	0.05	40.62
7.	50 lakhs – 1 crore	90	0.06	0.14	41.44
8.	1 crore – 5 crore	269	0.644	0.78	23.39
9.	5 crore – 10 crore	104	0.73	0.90	24.06
10.	10 crore – 25 crore	148	2.34	2.66	22.04
11.	25 crore – 50 crore	88	3.10	4.14	25.86
12.	50 crore – 100 crore	66	4.70	4.34	17.89
13.	100 crore – 500 crore	65	14.87	16.79	21.86
14.	Above 500 crore	39	73.50	60.70	15.99
15.	All sample Companies	1689	100	100	19.37

47. In their written note, the Ministry further informed as follows:

“A comprehensive exercise to determine revenue foregone on account of some of the major exemptions and deductions was done for the first time for the financial year 2004-05 for Budget 2006. A statement of revenue foregone forms annexure 12* of the Receipts Budget 2006-07 and has been laid before the Parliament as part of the budget documents. One of the deductions for which such an estimate for the financial year 2004-05 is available is the deduction under section 80P available to cooperative banks other than primary agricultural credit societies for which the revenue foregone has been estimated to be Rs 1534 crores.”

48. It was further informed:

“The following exemptions/deductions have been withdrawn *vide* the Finance Bill, 2006:

1. Exemption u/s 10(23G) to certain income of infrastructure capital companies and funds, and cooperative banks from investments in approved eligible businesses.
2. Tax benefits u/s 80P in cases of cooperative banks other than Primary Agricultural Credit Societies and Primary Cooperative Agricultural and Rural Development Banks.

*Annexure-II of this report.

3. Exemption for long-term capital gains u/s 54ED.
4. Exemption available to income of notified investor protection funds on income other than income by way of contributions received from recognised stock exchanges and the members thereof.
5. Exemption for long-term capital gains under section 10(38) for MAT companies.

49. The Committee also raised certain queries regarding the Government's proposal to review tax shelters extended, in the form of sectoral and area based exemptions, to which the Government in their written reply stated the following:

"Tax shelters to different sectors of the economy and to certain areas of the country have been on the statute for quite some time now. As a principle, no tax shelter can be provided in perpetuity. They are meant to support the assessee only in the initial stages. All existing tax shelters are being constantly reviewed to gauge their utility *vis-à-vis* the revenue loss caused by them. It is a continuous process and as and when the Government feels that a particular tax shelter has lost its relevance, the same would be withdrawn. A case in point is the deduction under section 80P available to co-operative banks. Since co-operative banks are no different from other commercial banks, the Finance Bill, 2006 proposes to withdraw this deduction to all co-operative banks other than Primary Agricultural Credit Societies and Primary Co-operative Agricultural and Rural Development Banks. Similarly, the Finance Bill, 2006 also proposes to withdraw the exemption available under section 10(23G), to income by way of dividends, interest or long-term capital gains of an infrastructure capital company or an infrastructure capital fund or a cooperative bank from investments made in approved eligible businesses.

A Committee of Secretaries was set up to review existing incentives for scientific research, including research and development in the pharmaceutical industry. The meeting of the Committee was held on January 30, 2006 and an interim report has been received subsequent to that meeting. The interim report is under examination. As regards the incentive in the form of weighted deduction to pharmaceutical industry, the deduction will continue to be allowed against expenditure incurred upto 31st March, 2007. The Finance Bill, 2006, presented in the Parliament on 28th February, 2006, will show that there is no proposal to

withdraw the deduction available in respect of expenditure incurred upto 31.3.2007.”

Indirect Taxes:

(i) The list of broad categories of exemptions (Customs and Central Excise) furnished by the Ministry is given below:

Broad categories of Customs duty Exemptions include:

Items having export links

Items covered under International Agreements (including FTA's, PTA's)

Inputs and intermediates for IT/Telecom sector

Items relating to health and family planning, rehabilitation aids

Machinery, equipment, parts for specified public transport projects, petroleum exploration, R&D etc.

Educational material, computer literacy, sports

Defence, security imports

Technical exemptions, say re-import

Miscellaneous exemptions.

Broad Categories of Excise duty exemptions include:

Area based exemptions

Export promotion

Small scale sector

Agro-based and food processing sector

Health and family welfare

Supplies to Diplomats, UN projects

Goods manufactured/sold by specified agencies like KVIC in rural areas

Goods for R&D

Defence sector

Environment protection

Power generation

Administrative necessity (like job-work, captive consumption, technical exemptions, unorganized sector)

Printed books, newsprint

Fertilisers.

50. The Committee were informed that for the year 2004-05, aggregate revenue foregone (in the case of Central Excise) and chapter-wise revenue foregone for Customs are already available in the Annexure-12 of the Receipts Budget for 2006-07. Amount of revenue foregone on the exemptions in 2005-06 is not yet available.

51. At the behest of the Committee, the Ministry furnished a list of exemptions pertaining to Customs, Central Excise and Service Tax, withdrawn after a comprehensive review, which is placed at Annexure-III.

52. When the Committee sought clarification from the Government on certain exemptions that had found mention in the Budget (2006-07) speech of the Finance Minister, the Government stated the following:

“Review of exemptions is assigned top priority by the Government. In this year’s budget a comprehensive review of customs, excise and service tax exemptions was done keeping in view the recommendations of Shri T.R. Rustagi (appointed by the Government for this purpose). As a result more than 12 customs duty exemptions, 64 excise duty exemptions and 12 service tax exemptions were withdrawn. However, there are some exemptions in which it was thought proper to consider the views of all concerned (Trade/Officers/Associations) before withdrawal of these exemptions. A list of such Customs and Central Excise exemptions is being put on the department’s website and comments are being invited on the same.

As regards the remaining exemptions, it is difficult to enumerate each separately. Reasons for their continuation are varied. However, all such notifications are reviewed periodically, and it is proposed to withdraw some of them.”

53. The amount of duty foregone as a percentage of Customs revenue during 2001-02 to 2005-06 (upto Nov. '05), as furnished by the Government, is as follows:

(a) *Duty Foregone under Various Export Promotion Schemes*

(Rs. in Crore)

Sl. No.	Scheme	2001-02	2002-03	2003-04	2004-05	2005-06 (upto Nov. '05)
1	2	3	4	5	6	7
1.	Advance Licence Scheme	7890.25	7461.88	10134.03	11740.85	9226.45
2.	EOU / EHTP / STP / EPZs	6282.95	5925.96	9421.95	8266.34	5076.18

1	2	3	4	5	6	7
3.	EPCG	2008.03	3025.47	3399.10	4680.90	3111.00
4.	DRAWBACK	2956.52	4520.40	4416.64	2811.52	2229.41
5.	DEPB SCHEME	5660.69	6830.82	11692.33	10075.75	3763.64
6.	SEZ			1320.02	2494.55	571.46
7.	DFRC			630.06	789.07	626.26
8.	DFCEC			48.08	173.58	245.72
	TOTAL	24798.44	27764.53	41062.21	41032.56	24850.12

(b) *Duty Foregone as a Percentage of Customs Revenue/Total Revenue*

(Rs. in Crore)

Sl. No.	Scheme	2001-02	2002-03	2003-04	2004-05	2005-06 (upto Nov. 05)
1.	Customs Revenue	40268	44852	48629	57611	42262
2.	% of duty foregone <i>vis-à-vis</i> customs revenue	61.6%	61.9%	84.4%	71.2%	58.8%
3.	Total Indirect Tax Revenue	117069	132339	148224	170391	119679
4.	% of duty foregone <i>vis-à-vis</i> total indirect tax revenue	21.2%	21.0%	27.7%	24.1%	20.8%

Note: Figures for 2004-05 & 2005-06 are provisional.

54. During the oral evidence the Revenue Secretary, while responding to the queries raised by the Committee on the issue of revenue foregone due to exemptions, stated as follows:

“The Hon. Members would be pleased to know that in the Union Budget of 2006-07, the Government has, for the first time, published a Statement indicating the Tax Expenditure under Central Tax System during the financial year 2004-05. The publication of this Statement is yet another milestone in our effort to impart transparency and accountability in the management of our public finances.

The tax laws provides for various tax exemptions, incentives, rebates, deferrals and credits, which are commonly referred to as ‘tax preferences’. The revenue foregone on the various ‘tax

preferences' is referred to as tax expenditure. It has been argued that tax expenditures are similar to subsidies and may be seen as a form of public expenditure. Tax expenditures are spending programme embedded in the tax statute which should generally appear as expenditure items for Parliament scrutiny and approval.

I would like to draw the attention of the Hon. Committee to Annexure 12 of the Receipt Budget 2006-07 (**Annexure II**) presented to the Parliament. It provides details of the revenue foregone during the financial year 2004-05 on account of various tax incentives, which form a part of the tax system of the Central Government along-with the assumptions and methodology for estimation. The revenue foregone during the financial year 2004-05 is estimated to be Rs. 71,081 crore under direct taxes and Rs. 87,580 crore under indirect taxes. The total revenue foregone is estimated to be Rs. 1,58,661 crore.

The main objective of the tax administration is to raise revenue necessary to fund Government expenditures. To the extent, tax laws also provide for tax expenditure in the form of exemptions and deduction, the tax administration also has the responsibility of managing such subsidy programmes. The performance of the tax administration, both CBDT and CBEC, should be evaluated in the context of the aggregate of revenue collected and revenue foregone."

55. The Revenue Secretary further added:

"There is another point also to which I would like to draw the attention of the hon. Members. When exemptions or concessions are given to one section of taxpayers, obviously another section of taxpayers would have to bear the burden. Revenue foregone like subsidies amounts to transfer of resources from one section of taxpayers to the other. Unlike budgeted subsidies where transfer of resources takes place through the expenditure route, revenue foregone implies transfer of resources through the revenue route. The scale of such transfers is evident from Annexure 12 of the budget. We believe that Parliamentary scrutiny is absolutely essential to assess whether such transfer of resources is necessary, whether it leads to increase in the aggregate welfare of the society, whether it has served its purpose and continues to serve its purpose. It is this conviction that has induced us to provide the statement for the first time. At present the estimate has been prepared on the basis of certain assumptions, as it is difficult

otherwise to gather details of revenue that has not been collected since returns from beneficiaries are not mandatory. It shall be our endeavour to improve our methods of estimation during the current year.”

56. The Revenue Secretary, while replying to a suggestion by the Committee on review of all exemptions, during the oral evidence, stated the following:

“...we did undertake an exercise last year. We appointed a consultant who has been working in this Department to look at all these concessions that we are giving on the indirect tax side. As far as I recall, I think, 73 exemptions have been removed in the current year’s Budget. Twelve customs duty exemptions, 64 excise duty exemptions and 12 service tax exemptions were withdrawn in the current year’s Budget.”

57. The Revenue Secretary further added on the issue during the oral evidence as under:

“...Something has been done on this, on removal of exemptions and we have also put up on the website all the remaining exemptions that we have. We have invited public opinion because these are sensitive issues where we would like to hear from the people as to what do they think about each of these exemptions and after that we can still take further view.”

58. To a specific opinion expressed by the Committee during the oral evidence that a cost-benefit analysis should be conducted on exemptions, the Revenue Secretary replied as under:

“...I think a cost benefit analysis needs to be done. It is very easy to give away a tax break; but we do not really know what are the consequences and whether it is necessary at all, giving up a lot of money. I would think that we need to look at it.”

59. The Committee raised their concerns during the oral evidence on the evasion of tax and ostentatious display of wealth to which the Revenue Secretary stated the following:

“...very often, we think that this ostentatious display has been facilitated by tax evasion. But, I think, the kind of figures that we have been able to produce on the question of exemptions, dropouts etc., if you look at it, I think tax avoidance through using the existing law, perhaps, is a more serious problem. If you look at

Annexure 12, where we have talked about revenue foregone, you will see that we have estimated that the sample of companies with profitability exceeding Rs. 500 crore, they are paying taxes, paying income-tax only to the extent of around 15 to 16 per cent whereas the corporate tax rate in that year, 2004-2005 was something like 35 per cent. So, you can see the extent of gap that is there between the two, between the nominal rate and the effective rate. This is all not done through illegitimate means. It is there embedded in the system. So, we need to tackle this problem both ways in which case we could have a more simple, rational tax structure applicable to all. I think that should be the ideal, which we aim at."

60. However, the Committee, during the oral evidence, expressed the public impression on such extravagant display of wealth that such lavish expenditure come from the money which is not accounted for and those are the people who flout the tax laws and flaunt the money often escape the tax net.

The Revenue Secretary replied to the concern of the Committee as under:

"I think it is a very major issue which we are trying to tackle in a limited way. As we have shown, we have tried to do certain things. Our annual information return is giving some information which we have been using. We have sent out letters to everybody, including myself. I also received a letter for some investment. I think, we are trying to make that. But the scale is substantial as you said and the effect will probably take some more time before we can really have any effective answer to that."

61. The matter concerning exemptions given both under direct and indirect taxes had engaged the attention of the Committee earlier also. The Committee, in their Thirty-Third Report (14th Lok Sabha) had recommended, *inter alia* that since prolonged continuance of exemptions may turn detrimental to the economy as they deplete considerable portion of tax base, leave tremendous scope for evading tax and prompt people to resort to unwarranted tax planning, there is a need for urgently withdrawing the exemption provision under the tax laws or reducing the list of exemptions and rationalising the same. The Committee are in total agreement with the observation made by the Rustogi Committee that exemptions cause distortions, are prone to misuse and not always easy to implement. The Committee appreciate that the Government have taken right steps in this direction by withdrawing quite a few exemptions which are no

longer justified. The Committee would further consider it to be a necessary and beneficial exercise to conduct a cost-benefit analysis on the tax exemptions, which would enhance the credibility of either extending or withdrawing an exemption. Therefore, the Committee recommend that a comprehensive exercise may be conducted by the Government to analyse the cost-benefit ratio on all the existing tax exemptions.

62. The Committee in their Thirty-Third report had also conveyed their apprehension on the possible misuse of exemptions provisions by research institutions. They note that the Government have now formed a Committee of Secretaries to review existing incentives for scientific research, including research and development in the pharmaceutical industry. The Committee hope that the review would be completed in a time bound manner and the Government would strive its best to consider and implement the recommendations at the earliest so as to prevent the misuse of exemption provisions to the extent possible. The Committee would like to be apprised of the position in this regard.

4. RESTRUCTURING

63. Reform of tax administration is an integral part of tax reform. The Committee note that with this background, a scheme of restructuring of the Department of Revenue was proposed in the year 2000 to tackle the exponential increase in their volume of work. Its components were to restructure the department, retrain and reorient its personnel through functionalisation, increase in the number of officers rationalising the span of control for better supervision, control and management of workload and reorientation, retraining and redeployment of surplus staff by increasing the level of existing work norms and providing appropriate incentives like promotions commensurate with increased productivity.

Direct Taxes

64. As per the Ministry the Restructuring of the Income Tax Department resulted in increase in the manpower in the executive cadre from the level of the Chief Commissioner down to the level of the Income Tax Inspector as shown in the table given below:—

Sl. No.	Name of the Post	Strength		Increase in Numbers	%age increase
		Prior to Restructuring	After Restructuring		
1.	Chief Commissioner of Income Tax	36	116	80	222.22
2.	Commissioner of Income Tax	402	698	296	73.63
3.	Addl. Commissioner of Income Tax	339	469	130	72.28
4.	Joint Commissioner of Income Tax	453	647	194	38.34
5.	Deputy Commissioner of Income Tax	1033	1240	207	20.03
6.	Assistant Commissioner of Income Tax	648	734	86	13.27
7.	Income Tax Officer	3261	4204	943	28.91
8.	Income Tax Inspector	8106	9490	1384	17.07
Total		14,317	17,598	3,281	22.91

65. Responding to a point raised by the Committee about the performance benchmarks and extent of achievement of such targets, the Government in their written reply stated:—

“The following performance benchmarks (tangible objectives) were envisioned in restructuring proposal:

- Rs. 2,800 crore of additional revenue to be generated through enhanced ability to deal with stop-filers.
- Rs. 6,000 crore of additional revenue to be mobilized through expeditious disposal of assessments.

- Rs. 7,500 crore of revenue to be realized as a result of increase in the number of Commissioners (Appeals) and Tax Recovery Officers.
- 200% increase in productivity at the organizational level.
- Downsizing of the size of the Income Tax Department by 4.75%.
- Release of Rs. 300 crore per annum on account of reduced claim of interest on refunds.

66. However, the Ministry contended:

“It is not feasible to measure the extent of the targets achieved in respect of various performance benchmarks for the reason that any growth and progress in an organization is a result of an intricate inter-play of several factors and it is not feasible to ascertain the disaggregated effect of each such factor. However, the growth of revenue and increase in the productivity of the Department has been more than benchmarks indicated in the restructuring proposal.

The progress made by the Income Tax Department towards the achievement of the defined objectives can be evaluated on the basis of various concrete parameters including growth rate of tax collections, quantum of recovery from arrears, tax GDP ratio, cost of collection etc. Judging by these parameters, the following has been the extent of progress made since the restructuring of the Department in 2001-02:

- (a) There has been an increase of 92% in the collection of direct taxes from 2001-02 to 2004-05 at an average annual growth of 24% as against average growth rate of 18% between 1990-91 to 2000-01. It has happened for the first time in last 35 years that direct tax collections have increased at a rate above 20% for three consecutive years.
- (b) The direct tax-GDP ratio has increased from 3.02% in 2001-02 to 4.24% in 2004-05 (three years' time) as compared to increase from 2.10% in 1990-91 to 3.23% in 2000-01 (in 11 years). This is for the first time in last 35 years that direct tax GDP ratio has surpassed 4%.
- (c) There has been a significant increase in the amount of recovery from arrears from Rs. 3,930 crore in 2001-02 to Rs. 5,470 crore, Rs. 5,540 crore and Rs. 7,084 crore in 2002-03, 2003-04 and 2004-05, respectively. During 2005-06, an amount of Rs. 5,996 crore has been recovered from arrears up to February 2006.

- (d) Collection out of current demand, which was Rs. 4,326 crore in 2001-02 has increased to Rs.7,300 in 2002-03, Rs. 10,610 in 2003-04 and Rs. 15,632 crore in 2004-05. During 2005-06, an amount of Rs. 6,911 crore has been recovered from current demand up to February 2006.
- (e) The cost of collection of direct taxes has drastically come down from 1.44 paise per rupee collected in 2001-02 to 0.86 paise per rupee collected in 2004-05.
- (f) Comprehensive computerization of the Income Tax Department has been undertaken with a view to facilitating electronic delivery of taxpayers services, augmenting Departmental computer infrastructure, and setting up of Tax Information Network (TIN). The Income Tax Department has recently received "The Golden Icon" for best e-delivery of services by any Government Department or Public Sector Undertaking.
- (g) There has also been progress in various areas including taxpayers service, level of use of technology in work, higher morale of the work-force, development of core-competence, etc, which have directly or indirectly resulted from restructuring of the Department."

67. When asked to furnish the details of revenue realization during the four years preceding and four years succeeding the restructuring, the Ministry provided the following information:—

Financial Year	Direct Tax Collections (Rs. in crore)
1997-98	48,280 [#]
1998-99	46,600
1999-2000	57,959
2000-01	68,305
2001-02 (Year of restructuring)	69,198
2002-03	83,088
2003-04	1,05,088
2004-05	1,32,771
2005-06 (Revised Estimates)	1,70,077

[#]Inclusive of VDIS collections of Rs. 9,803 crore.

Indirect Taxes

68. As desired by the Committee, the details regarding increase/decrease in the number of posts at all the levels (from the level of Inspector to Chief Commissioner) due to restructuring of the department were furnished as follows:—

Grade	Sanctioned Strength		
	Before Cadre Restructuring	After Cadre Restructuring	% increase/decrease
Chief Commissioner	21	47	123.80%
Commissioner	146	289	97.90%
Additional Commissioner	194	300	54.60%
Joint Commissioner	96	276	187.50%
Deputy Commissioner	808	601	(-) 25.62%
Assistant Commissioner	453	790	74.40%
Supdt. of Central Excise	6158	10515	70.80%
Supdt. of Customs (Prev.)	1021	1442	41.20%
Appraiser	722	809	12%
Inspector CE	18472	15826	(-) 14.32%
Examiner	456	376	(-) 17.54%
Preventive Officer	2294	1851	(-) 19.31%
CAO	41	155	278%
AO/ACAO/EA	584	972	66.40%
Sr. P.S.	21	47	123.80%
P.S.	103	290	181.60%

69. Asked to explain the performance benchmarks and the extent of their achievement, the Government, in their written reply, stated as follows:

“No specific targets or benchmarks were envisioned to be achieved due to restructuring of the department. Cadre Restructuring Plan 2001 basically aimed at creation of a tax administration, which is officer-oriented, assessee-friendly and positively responsive. The Cabinet Note for the Cadre Restructuring Plan 2001, presented before the Union Cabinet, envisaged the following broad objectives:

- (i) Creation of a tax administration, which is officer-oriented, technology-driven, positively responsive and assessee-friendly.

- (ii) Maximization of revenue productivity by having closer supervision over compact Commissionerates and Zones. Creation of smaller and compact Commissionerates & Zones will also provide better accessibility to trade and industry and rationalize the workload;
- (iii) Reinforcement of the Directorate of Anti-evasion and Revenue Intelligence to counter increased skills and capabilities of tax evasion and smuggling;
- (iv) Speeding up the process of disposal of Appellate cases pending at various levels, thereby unlocking nearly Rs. 11,000 crore;
- (v) Reorganizing Training Directorate to achieve the required level of capacity development, and reinforcement of the Directorates of Audit, Valuation, Drawback & Export Promotion, Systems etc. for increased efficiency in various areas of work;
- (vi) Achieving faster speed in decision-making by replacing manual processing of documents by greater use of computers and other tools of Information Technology;
- (vii) Reducing interface with the taxpayer especially at the lower level of staff by having more number of senior level officers in the field formations;
- (viii) Achieving the objective of zero-tolerance to corruption by strengthening the Vigilance Directorate and the grievance-redressal machinery;
- (ix) Downsizing of the Department by rationalizing various formations, grades and cadres into simpler and uniform structure by a reduction of staff strength from 68,761 to 65,161 (net reduction of 3600 posts, that is, 5.24% of the total staff strength);
- (x) Higher motivation through improved management of career prospects in all cadres of Group 'A', 'B', 'C' & 'D'.

70. It was further informed:

“Cadre restructuring also envisaged enhancement of productivity of the Department to achieve an estimated 5% per annum growth in revenue collection.

After implementation of the Cadre Restructuring Plan, the revenue realization has improved over the years despite reduction in duty

rates, removal of physical controls and various liberalization measures taken by the Government. Following Table indicates the growth of revenue since the year 2000-01:

(Rs. in crore)

Financial Year	Actual Collections				% growth over previous year
	Customs	Central Excise	Service Tax	Total	
2000-01	47542	68526	2613	118681	-
2001-02	40268	72555	3302	116125	-2.2
2003-04	48629	90774	7891	147294	12.2
2004-05	57611	99125	14200	170936	16.1
2005-06 (BE)	53182	121533	17500	192215	12.4

The above table indicates that the indirect tax revenue (Customs, Central Excise and Service Tax taken together) has grown by 12.2% and 16.1% during 2003-04 and 2004-05 respectively. The BE for the year 2005-06 envisages a growth of 12.4%, which is likely to be achieved.

As regards disposal of appeals cases, approximately 38,000 appeals cases were pending disposal in 2001. Most of these cases have been decided and as on 31.3.2005 there were only 8830 cases pending disposal. Most of these cases are new cases. As a result of declining pendency of Appeals cases, the Department could convert about 30 posts of Commissioner (Appeals) into other Commissioners posts.

The above factors indicate that the objectives of the Cadre Restructuring have been met."

71. Revenue collected from Indirect taxes over the years is as follows:—

Year	Revenue realised (in Rs. crore)				
	Customs	Excise	Service Tax	FTT/IATT	Total
1991-92	22257	28110	—	522	50889
1992-93	23776	30832	—	382	54990
1993-94	22193	31697	—	354	54244
1994-95	26789	37347	407	584	65127
1995-96	35757	40187	862	609	77415
1996-97	42851	45008	1059	675	89593
1997-98	40193	47962	1586	892	90633
1998-99	40668	53246	1957	1009	96880
1999-00	48420	61902	2128	982	113432
2000-01	47542	68526	2613	1133	119814
2001-02	40268	72555	3302	1193	117318

Shortage of Manpower

72. During the oral evidence the Committee referred to the fact that at almost every discussion involving Department of Revenue during their on-the-spot visits, the point regarding shortage of manpower and its effect on the efficient functioning of tax departments has always been raised. In this connection, the Secretary (Revenue) stated the following:

“We do believe that this is a serious problem which we need to address, particularly during the last few years our revenue collection has gone up enormously. It is almost doubled over the past five or six years and the number of taxpayers has increased. Our ability to look at the kind of returns that they are getting, the responsibility has increased. In fact, we are having a serious problem. The main difficulty that has arisen is that according to the DoPT norms, we have to bring down the total number, the total manpower by given percentage every year. So this has been affecting us for the last five or six years. We have not been recruiting effectively at the grass root level. I do not think that we can really progress much in this because ultimately whatever potential is there for collection has not been fully realised because of lack of manpower. So, we had taken up with the Cabinet the question of exempting us from this DoPT norm. The Cabinet referred it to the Committee of Secretaries. We had a meeting of the Committee of Secretaries. Two things were decided there that immediately for the CBEC, 1,400 new posts could be filled up. That can be immediately done and for the CBDT, 3,300 posts can be filled up. That will be basically at the lower level which you were referring to so that that problem to a certain extent can be sorted out. But it was also decided that both the Departments may work out their own what they consider to be the kind of structure that is required for maximum revenue collection and then it can be brought again to the Committee of Secretaries for a decision. Two or three weeks ago, we received a proposal from the CBEC which was considered by the Finance Secretary, myself and the Secretary DoPT. Certain queries were raised by Expenditure and DoPT and we now propose to hold a further meeting. Thereafter, we will collectively take it to the Committee of Secretaries and based on the decision taken by the Committee of Secretaries, it will go to the Cabinet. A similar exercise has been undertaken by the CBDT. They have just submitted their proposal. I think day after tomorrow; we are having a meeting with the Finance Secretary and the Secretary of DoPT where we will be looking at the structure. Meanwhile an action has already been initiated to fill these 1,400 posts in CBEC and 3,300 posts in the CBDT. Of course, we have to depend on the Staff Selection (SSC). I have written to the SSC Chairman requesting him to expedite the selections so that these people are in places as quickly as possible. But it is a problem and we are very conscious of it.”

73. To the specific point raised by the Committee during the oral evidence as to whether the Government have done anything to expedite the process of recruiting the sanctioned staff, the Chairperson of the Central Board of Direct Taxes stated as under:

“The posts on the CBDT side which have been sanctioned, as the Secretary just mentioned, are the ministerial staff level and they are all to be done by direct recruitment for which the SSC comes into the picture. They do this selection for us and they do the recruitment for us and then give us the manpower. So, that is likely to take a year’s time.”

74. Further raising the point the Committee during the oral evidence wanted to know whether the Government have taken up the issue with the recruiting agency to expedite the process of recruiting the staff, the Revenue Secretary stated the following:

“I have already done so in the case of CBEC. There has been a little bit of delay in submission of the proposals from the CBDT which we have corrected now. I will be writing to the SSC about the CBDT also.”

75. The Committee observe that restructuring of the department under the Central Board of Direct Taxes (CBDT) and Central Board of Excise & Customs (CBEC) had been undertaken resulting in perceptible difference in the performance of the departments. However, the Committee have been told on many occasions that shortage of manpower, particularly at the level of Inspectors etc is affecting the efficiency of the tax departments. In this regard, from the data submitted to them by the Government, the Committee note that the restructuring process in CBDT has resulted in an increase of 222.22% of the posts of Chief Commissioner but a rather poor 17.07% augmentation at the level of inspectors. In CBEC, the posts of Chief Commissioner have been increased by 123.80% and at the level of Inspector, there has been a decrease of 14.32%. This exercise, in the Committee’s view, has made the top slots heavy, and negligible or even negative growth in the number of posts at the cutting edge levels like that of Inspectors, Income Tax Officers, Superintendents and Custom Appraisers. This, the Committee feel, may further worsen the much-felt shortage of work force at these levels leading to serious problems in the overall functioning of the two departments. The Committee note that the Government have now started taking measures to fill up these gaps. Nevertheless, the Committee are led to the conclusion that the restructuring proposal was done in a manner, that chose to ignore the requirements at the middle and lower level of the functionaries, resulting in continuation of shortage of manpower. The Committee, therefore, recommend the Government to again assess the present structure of the department under both the Boards carefully and set right the anomalies that have crept up as a result of restructuring.

5. COMPUTERISATION

Direct Taxes

76. With regard to the efforts made so far by the Government to computerise their operations*, the Committee desired to know the status of establishment of Tax Information Network (TIN) and its utilisation in identification of tax evaders. In response, the Government, in their written reply, stated the following:

“Tax Information Network (TIN) has been set up by the Department. This is being hosted by National Securities Depository Limited (NSDL). TIN is a repository of information relating to—

- (i) Tax payments, coming online from banks collecting direct taxes.
- (ii) Tax deductions coming from TDS returns - filed electronically as well as on paper.
- (iii) High value financial transactions coming through Annual Information Returns. These have started being filed in electronic format with TIN using PAN as the key identifier from August 2005.

Information contained in TIN will be helpful in checking tax fraud, identifying non-filers and enabling deepening of tax base.”

77. The Committee further raised a point about the extent of utilisation of computerised processes in updating the assessee’s profile and speeding up assessment and adjudication processes. The Government, in their written reply to the point, stated the following:

“Direct Taxes:—

The computerisation project of the Income Tax Department under implementation for setting up single national database has following tracks-

- i. E-delivery of taxpayer services.
- ii. Augmentation of computer infrastructure in terms of—
 - PCs for all officers and one staff member of each officer

*A comprehensive status report on computerisation as submitted by the Government on 28.4.2006, is placed at Annexure IV.

- All India Network connecting Income Tax offices in 510 cities
- High End servers for National Computer Centre
- Upgradation of application Software
- Enterprise—wide Resource Management and security tools

The status of above project tracks for augmentation of computer infrastructure is as under:—

Project Track	Particulars	Status as on 20.02.2006	Remarks
Providing PCs to all users	Supply, installation of high end PCs to all users required to work on network.	Completed	More than 8,800 PCs have been provided to Departmental Users.
Migration of application software	Migration of application software to 3-tier architecture for consolidation of 36 regional databases into single national database.	Migration completed. Updated version under development.	Acceptance Testing in progress. Scheduled completion June 2006.
Linking Income tax offices in 510 cities to single national database	To set up an All India Virtual Private Network linking over 12000 users in 745 buildings in 510 cities to National Data Centre housing single national database.	Contract awarded.	Phase-I completed. Work on Phase-II in progress. Scheduled completion June 2006.
Setting up National Data Centre with Business Continuity/ Disaster Recovery sites	Providing computing, data storage, security facilities and related functionalities for enhanced requirement of 12000 departmental users working on single national database.	Bids received. Technical evaluation in progress.	Commissioning expected to be completed by July 2006.

The current status of various benchmark activities identified in the project, is stated to be as under:-

Benchmark activity	Current status
1	2
Allot PAN to applicants within 5 to7 days	Allotment time brought down to 5 days for Tatkal applications and 10 days for other applications

1	2
Electronic exchange of tax payment / refund data with Banks	On line transmission of tax payment information from Banks has started from 1.6.04
Expedition disposal of refund claims, thereby reducing interest burden & increasing taxpayer satisfaction;	All returns claiming refunds are being processed on computers within 4 months.
Process all returns of income in 6 to 12 months	All returns are being processed on computers within 4-6 months of filing.
Process all returns relating to Tax Deduction at Source (TDS) on computers, making it possible to verify claims for credit of TDS on-line across the country	e-filing of TDS returns has started. However, computerized processing and country-wide matching of TDS claims will start after single national database is set up
Process and match third party information with the returns of income across the country, for identifying non-filers/ stop-filers.	Filing of Annual Information Returns (AIR) of high value financial transactions in electronic format has started from August '05. Data matching will start after single national database is set up.

The Committee were informed that computerization effort of the Department has led to computerized processing of income tax returns which are now being completed in 4-6 months time. This has also enabled the Department to expedite issuance of refunds. A Tax Information Network has been established which acts as a repository of important tax related information coming from various sources. Information on taxes paid comes to the Department under the On-line Tax Accounting System (OLTAS) on T+3 basis. All corporate and government deductors are filing the TDS returns electronically. Further, gestation lag for allotment of PAN has considerably reduced and now PAN cards are being dispatched in just 15 working days of filing of valid PAN applications. Annual Information Returns are being filed in electronic format in respect of specified high value transactions with PAN as the key identifier. The information contained in these returns will be collated party-wise and subsequently used for identifying non-filers, for selection of cases for scrutiny and for other enquiries.

Indirect Taxes:

78. At the behest of the Committee, the Government, through a written note, furnished the following information with regard to computerisation in CBEC:

“The projects of CBEC are in line with the proposed vision of the National e-Governance plan and have targeted the business users such as importers and exporters, manufacturers and the service providers.

In these initiatives, the department is guided by the following principles:

- Citizen-centric delivery of services through “single window” interface.
- Providing services on “anytime, anywhere” basis.
- Ushering in Transparency and Accountability.
- Simplification of Procedures.
- Reduction in Transaction Costs.
- Minimization of manual interface.
- Encouraging voluntary compliance.”

79. It was further added:

“Central Board of Excise and Customs has already completed several projects which have augmented e-delivery of taxpayers services. Some of them are listed below :

- Indian Customs EDI systems (ICES) provides for online assessment of import and export documents through electronic data interchange (EDI), thereby eliminating the need for filing paper documents for customs clearance.
- Indian Customs and Excise Gateway (ICEGATE) provides e-filing facility and EDI messaging for trading partners such as importers, exporter, carriers and other agencies such DGFT, DGCIS and RBI.
- CBEC Website : This website provides information relating to Acts, Rules, Regulations, Notifications, Circulars and other information to the trade and the officers.

- PAN based electronic registration for Central Excise and Service Tax : This has quickened the process of registration.
- E-filing of returns for Central Excise and Service Tax: This facility has been created to enable the assesseees to file their return on the web site of the department electronically, for greater convenience of the taxpayers and reduced interface between the assesseees and the Departmental officers.”

80. About the on-going and future projects, the Committee were informed as under:

“A major project currently under implementation is the setting up of a Data center with consolidated servers and a Wide Area Network (WAN) linking over 20,000 users in 550 buildings in 245 cities. The WAN would provide quality connectivity from the Data Centre to Custom Houses, Air Cargo Units, ICD and Central Excise Commissionerates up to the divisional level with further connectivity up to the Ranges. Along with the setting up of a Data Centre, a Data Warehouse is proposed to be set-up which will provide data for assisting policy formulations and for generation of statistics.

In Central Excise, the Department maintains revenue profiles of assesseees paying revenue of more than Rupees one crore. The existing systems for Central Excise and Service Tax, however, are essentially modules for capturing data relating to registration of assesseees and the returns filed by them. There is a proposal for introducing a new system known as Automation of Central Excise and Service Tax (**ACES**) which is aimed at developing a workflow application to automate the entire business process relating to Central Excise & Service Tax including speeding up assessment and adjudication processes. The software is under development by the vendor and testing of the software is likely to commence in June, 2006.

Other on-going Initiatives:

Digital Certificates: iCert CA is the licensed Certifying Authority of CBEC, set up as part of the ICEGATE project which aims at enabling secure electronic transactions within the organization and with its trading partners through the optimal use of Public Key Infrastructure (PKI) technology, popularly known as Digital Signatures. These certificates are issued only after the identity and the antecedents of the applicant are verified by reference to records as well as by physically visiting the applicant’s premises.

Risk Management System (RMS) for Customs : Under the Risk Management System (RMS), documents filed in ICES would be subjected to a risk assessment by the system. The System determines whether the goods require examination and the nature of such examination, which may include documentary examination, and/or physical examination of goods by Customs according to the risk represented by the consignments. This system is meant to facilitate low risk and compliant trade for optimal use of CBEC resources by resorting to computer aided scrutiny of high risk consignments based on non-discretionary and objective criteria. RMS has started functioning at Air Cargo Sahar. The Pilot project of RMS has shown the desired results by way of faster clearance of imported goods. Phased roll out at other locations is dependent upon staff and other resource availability for Risk Management Division for which necessary action is being taken.

Automated Clearance of Courier Consignments : This project aims at bringing clearance operations for express consignments in line with international standards and WCO guidelines. Detailed designs of various modules have been worked out. The System Requirement Study is being finalized.

Advance Passenger Information System (APIS) : This project aims at passenger facilitation coupled with more effective control on passenger movement at International Airports. This is being jointly developed with the Ministry of Home Affairs. Consultations with MHA are in progress.

Electronic Accounting System in Excise and Service Tax (EASIEST) : This project aims at reconciling the duty paid in the banks with the data captured in the Central Excise returns. Pilot project is under implementation at Chennai.

E-Payment of Customs Duty: Facility for payment of Customs duties through internet. Pilot is being implemented in Delhi. Phased roll-out to other locations is to commence after successful run at Delhi.

The Customs EDI system has considerably speeded up the process of assessment and examination of goods and reduced the dwell time of cargo. It has also helped in increasing transparency and in the dissemination of information to the importers and exporters who can get to know the status of the document filed by them without any physical interface with the departmental officers. With a better database, assessee based information can be generated by the department.

On the Central Excise side, there is a practice of self assessment. Computerization has helped in the generation of assessee-specific and commodity-specific information. The new project for automation of Central Excise and Service Tax (ACES mentioned earlier) would also cover the area of adjudication.”

81. While responding to the Committee’s queries regarding computerisation of Income Tax Department during the oral evidence, the Revenue Secretary explained as follows:

“The computerisation programme of the Income Tax Department is scheduled to be completed during the current year. This will result in consolidation of 36 regional databases into a single national database and linking of all income tax offices at 510 cities to this database. Once this centralised IT infrastructure becomes operational it will be possible to extend the facilities for jurisdiction-free filing of returns, and electronic filing of returns to all taxpayers across the country. This will also enable countrywide data matching for identification of non-filers and stop filers and computerised selection of cases for scrutiny. The Income Tax Department has also committed itself to electronic delivery of taxpayer services as part of the National E-governance Action Plan with the objective of making it possible for all taxpayers to fulfil their basic tax related obligations without visiting income tax offices. Currently the Indian Customs’ EDI system operates in 34 customs locations covering all major ports, air cargo units and inland customs stations. Roughly 80 per cent of the country’s international trade is covered. Over 95 per cent of the documents are processed electronically in these Stations. In this year the Department is in the process of establishing a data centre with countrywide network which will enable the consolidation of IT infrastructure. This would help in increasing the cover of EDI to more locations. Risk Management System has already been introduced in four customs locations and it is showing quite significant results. The RMS is proposed to be introduced in all major customs locations in a phased manner. This would significantly increase the speed of clearance of cargo and drastically bring down the time. Some of the major initiatives that are proposed to be implemented during the year are automation of central excise and service tax, e-payment of duties, automation of imports by couriers, issuing digital certificates and improving help desk facilities.”

82. Providing further details on the matter, a representative of the Central Board of Direct Taxes explained as under:

“...the steps regarding taxpayer identification and accounting of taxes is fully computerised, countrywide. As far as dealing with returns of income, we have been able to set up a network in 60 cities only. So, all processing of returns in those 60 cities is taking place on computers. The remaining, about 450 cities are not in the income-tax network.

Our current project relates to bring all these 450 cities on the all India network and converting these databases into a single national database because the technology that we used in 1997, when the first and second phases were implemented, was on regionally distributed databases. Today, it is possible to set up a single national database. So, these are the projects that are under implementation and the committed date for completion of these projects is September, 2006. By September, 2006, it is expected that all income tax offices will be on the network and processing of all returns across the country will also be on the network. On the other side, there is information coming from third parties, that is, annual information returns and TDS returns. They have all been fully computerised countrywide. Hon. Member was asking about the gap. The gap is between the information coming from third parties, which is fully computerised, and the information coming from returns of income, which is partly computerised. By the end of this financial year, this gap will be filled and we will be able to complete all processing, all data matching and all selection of cases for scrutiny on computers.”

83. When asked about the statement made by the representative of the Ministry during an earlier meeting on the target date for completion, the representative stated the following:

“Last time, I said that it would be completed by June, 2006.”

84. The representative further explained about the date fixed for completion of computerisation stated as under:

“There are four major tracks within the computerisation programme which relate to network, application software, the data centre and the data centre space. Out of these four tracks, three are on time. One relating to system integration is running behind schedule by about three months. Our original committed date was June, 2006. Now, we are reporting that by September, 2006, the national data centre will be in place after which all the four tracks will converge into completion of the project.”

85. To a specific point raised by the Committee as to whether the computerisation programme has been given to a private party, the representative stated the following:

“The work relating to setting up of the network has already been awarded, which is one of the four tracks. The work relating to appointment of system integrator is still at the stage of evaluation of technical bids.”

86. When pointed out by the Committee that the process as stated above was supposed to have been finished in the last year itself, the Revenue Secretary stated the following:

“The sanction for this project came in June, 2005. It was supposed to be for one year. It is a Rs. 700 crore project which involves networking of all the 510 cities. It involves setting up a national data centre with centralised server and with all the related software technology. It is under strict monitoring and surveillance. Except for the system integration part, where they have slipped up, I think, for rest, they are on track at present.”

87. With regard to the Committee’s queries on Computerisation of Central Board of Excise and Customs (CBEC), a representative of CBEC, during the oral evidence, stated the following:

“On the customs side, we have already got an ongoing computerisation system and about 34 major customs locations are already covered under the EDI. This represents roughly 80 per cent of the country’s international trade and in each of these places, about 95 per cent of the documents are processed electronically. The draw-backs of the exporters are credited automatically to their bank accounts. We have a work flow system and appraisalment is done on the system. What we have been noticing in the past one to one-and-a-half years is an increase in demand from the trade as well as from other administrative Ministries to extend the coverage of EDI to other locations. As I said, we have covered 34 locations so far, but we have so many other major ports and some of the minor ports to cover.

So, as in the case of income tax side, we have embarked on a major project of consolidation of our IT infrastructure. Instead of having one server at each of the locations as at present, we will be having a single data centre where the entire IT infrastructure will be located and this will be connected to the rest of the country through a Wide Area Network. That major project is on and once

that system is in place, which we expected to be in October-December—that is the phased manner of implementation—we will be in a position to cover most of the remaining places. What is 80 per cent today should become about 95 per cent in the next six months or so.

On the Central Excise side, we have a project which we have called System for Excise Revenue Monitoring (SRMON). That has been basically relating to offline data capturing and generating some MIS reports. What we are currently working on is to have an automated work flow system of central excise assessment as well as service tax assessment, which would be somewhat similar to customs EDI. Once this is in place, we would be able to give quality service to the tax-payers. They would be able to know the status of the documents, as it happens on the customs side. On the customs side today, an importer or exporter can know the status of the document filed by him. He will know whether it has been appraised, whether it has gone for audit or whether it is sent for duty payment and so on. Once the central excise system is in place, the automation of central excise and service tax project, similar information would be available to the tax-payer. He would be able to know the status of the return he has filed or the refund claim he has filed.

The other major project that we are working on is automation of courier imports, imports through couriers like the FEDEXpress, DHL and others. This is a public-private partnership. The investment has been done by the Express Industries Council of India. We are working closely with them. We expect that project to be ready by August/September, 2006 for test purpose.”

88. It was further added:

“The e-payment of duties is another major item on our agenda. On the customs side we have noticed that one of the major demands of the importers is that though the assessment and examination processes have been speeded up, yet they have to go to the bank for making the payment of duties. Typically, in a customs house what happens at times is that the assessment is completed by 4 o’clock, and there is a huge queue at the bank counters between 4 o’clock and 6 o’clock. Once e-payment is introduced in a big way covering more than one bank, then the queues at the bank counters would be considerably reduced. The importers would also be able to pay their duty sitting in their

office through the internet using the bank's electronic payment system.

We also expect that significant improvement can be made for the customers by way of helpdesk facilities with the augmentation of hardware and networking. We already have a helpdesk facility in the customs side, which works on a 24 hours 7 days a week and 365 days a year basis. We would be able to qualitatively improve the helpdesk functions, so that any importer, exporter or assessee — who has a genuine query — would be able to get quality assurance.

Another major initiative that we have introduced in the month of December 2005 was to implement a Risk Management System (RMS) on the customs side. So far, every single document filed by an importer was invariably subjected to assessment as well as the goods were examined subject to some minor exceptions like books, etc. In the Risk Management System we have built a system of risk assessment, which will be done by the system based on risk rules and our perception of risks — based on our experience so far — like country of origin or sensitive goods or goods prone to under-valuation, etc.

We have built this complex system of rules in the system by which the computer itself decides whether a consignment is to be examined and assessed or not based on the risk parameters. We started it as a pilot project at Mumbai Air Cargo in December 2005. Thereafter, we extended it to the JNPT, a major container port in the country, which handles roughly 50 per cent of the country's container traffic, and thereafter, we extended it to the Mumbai Customs Container Freight Station (CFS) in Mulund. Our experience so far has been very encouraging. Roughly 45 per cent to 50 per cent of the imported goods are no longer subjected to examination or assessment as a matter of routine. Once the Bill of Entry — which is our import document — is put into the system, the system itself pushes it on to the duty payment queue based on the risk parameters. So, all that the importer needs to do is to pay the duty and take clearance of the goods.

We have received feedback from the importers, and I would like to assure the hon. Members that these are not solicited responses. These are spontaneous responses from the major importers who have written to us saying that the time taken for both assessment and examination has significantly come down. Earlier the time

taken used to be roughly between 24 hours and 27 hours, but now it has come down to half-an-hour or 15 minutes in most of the cases. We also expect to roll out this Risk Management System (RMS) to other major ports like Chennai, Delhi, Kolkata, etc., and our aim is to cover all the major locations by June 2006. Therefore, we have to work very hard in the next three months to extend the RMS to other locations.

We have some other minor projects on hand on which we can send a detailed note as also on our other initiatives. These are our major initiatives.”

89. Following the above briefing, the Committee raised a point on the extension of coverage of computerisation, to which the representative has stated the following:

“...as regards your query about the extension of coverage.... On the customs side we have now covered 34 locations, which covers all the major ports, air cargo complexes and ICD stations. The hon. Members will appreciate that we have a vast coastline, we have a number of minor ports, we have many major ports, and we also have land custom stations. Therefore, the custom stations would exceed 400 in numbers, and we have to prioritise it when we extend coverage of EDI.

We have planned to start with 34 major locations, which have been covered so far. These are places where roughly 80 per cent of the international trade takes place. This is an approximation, and these figures sometime keep going up or coming down depending on the changing international trade pattern. For instance, on the western coast, Mumbai was the premier port for a long time till JNPT took over from it. Now some other ports like Mundra, Vadinar and others in the Gujarat coast have taken over from it. Our prioritisation would be to cover those ports, air cargo complexes in the first instance, which account for most of the international trade. As there are many land custom stations and minor ports, so it has to be done in a sequential manner. We expect to cover all the major locations once the major infrastructure like the data centre and the countrywide network are in place. We believe that it would cover about 90 percent or 95 per cent of the trade at the internal container depots, the internal stations and the container freight stations, and the rest would have to wait because we cannot do everything simultaneously.”

90. The Committee wanted to know whether the balance area left out of the computerisation programme will be taken up or not, the representative stated as under:

“We would be working on it. It is not that it is not on our radar, but we have to prioritise our projects accordingly.”

91. The Committee observe that so far as the computerization projects taken up by the Central Board of Direct Taxes are concerned, implementation of many small projects that would enhance the effective functioning of the department like computerized processing and country-wide matching of TDS claims, matching of data compiled in the Annual Information Returns (AIRs) with that of tax returns etc. depend to a large extent, on the completion of the creation of a single National database. They note that as per the original target, the database was to be completed by June, 2006. However, the target date for completion has now been shifted to September, 2006. The Committee are of the strong view that the Government should take all-out efforts to complete the project within the rescheduled target i.e, by September 2006 to reap the designated benefits that would accrue from the database. Further, the Committee feel that there exists a gap between the information obtained through Annual Information Report (AIR), which is fully computerized, and the information coming from returns of income, which is partly computerized. The Government have assured that the gap would be filled and they will be able to complete all processing, data matching and selection of cases for scrutiny on computers by the end of the current financial year i.e. 2006-07. The Committee expect that the whole process will be completed within the stated time at least now. Further, the Government have stated that the work relating to appointment of system integrator is still at the stage of evaluation of technical bids. The Committee urge the Government to expedite the process without further delay so that this should not adversely affect the project.

92. In so far as the overall computerisation of the Department is concerned, the Committee were given to understand that expenditure sanction for the third phase of Computerisation Plan of the Income Tax Department was approved by the Cabinet way back in December, 2002. The plan had included networking of I.T offices in remaining 440 cities out of the proposed 510 cities. The original target date for the same was 31.01.2006. The Committee further note that the Department sought fresh sanction for additional requirements from the Committee of Secretaries on Non-plan Expenditure on 11.5.2005. In the Committee's view, the pace of work with respect to

computerisation project has been slow. Despite urging the Government to expedite the various computerisation projects repeatedly in their earlier reports and the assurances given by them that it would be completed in time, the Committee are dismayed to note that certain components of the project like linking of cities under a single national database and setting up National Data Centre are yet to be completed. The Committee note that as per the revised schedule, the dates of completion of the above two components of Phase-III of the computerisation projects are 31.05.2006 and 30.09.2006 respectively. The Committee hope that the Government will not extend the date furthermore and take all out efforts to complete the project as per the revised schedule.

93. The Committee note that so far as the computerisation projects under the Central Board of Excise and Customs (CBEC) are concerned, the Government have taken the stand that some of those are under implementation and some others are in the proposal and testing stages—the important ones being the creation of a National level Data Center, Automation of Central Excise and Service Tax (ACES), Risk Management System (RMS) and Electronic Accounting system in Excise and Service Tax (EASIEST). The Committee recommend that all the projects under implementation as well as under consideration should be followed up by the Government in the right earnest so as to avoid avoidable delay in their implementation.

94. The Committee further note that roughly eighty per cent of the international trade is covered under the Customs' EDI system and over ninety per cent of the documents are processed electronically in these stations. The Committee urge the Government to increase this coverage to hundred per cent at the earliest. They observe that once the work relating to automated workflow system of central excise assessment as well as service tax assessment is completed, it would be possible for the Department to provide quality service to the tax-payers. Also, the Government are expected to roll out the Risk Management System (RMS) to major ports like Chennai, Delhi, Kolkata, etc., with the aim to cover all the major locations by June 2006. In this background, the Committee expect the Government to show tangible results in the near future.

95. The Committee note with concern that irrespective of the assurance given by the Government to furnish the White Paper on 'Information Technology in Tax Administration' the said 'White Paper' has not been furnished so far. They expect the Government to do the same immediately.

6. SERVICE TAX

96. The details of revenue collection, budget estimate and revised estimate of Service Tax for the last three years are tabulated below:

(Rs. in Crore)

Year	Budget Estimate	Revised Estimate	Revenue realized	% growth over previous year	% Achievement of	
					Budget Estimate	Revised Estimate
2002-03	6026	5000	4122	24.8	68.4	82.4
2003-04	8000	8300	7891	91.4	98.6	95.1
2004-05	14150	14150	14199	79.9	100.3	100.3

Revenue Collection for 2004-05 is provisional.

Source: Receipts Budget and Pr.CCA

97. To a point raised by the Committee whether the Service tax, collected from consumers eventually gets deposited in the Government exchequer, the Government in their written reply stated the following:

“As per Section 83 of the Finance Act, 1994, read with section 11D of the Central Excise Act 1944, every person who is liable to pay Service tax, and has collected any amount in excess of the tax payable from the receiver of such taxable services, in any manner as representing Service Tax, shall forthwith pay the amount so collected to the Central Government. Thus, in case any instance is noticed where a Service Taxpayer collects amounts as Service Tax but does not pay the same to the Government, action is taken to recover the same. The details of investigations undertaken in this regard would be gathered and placed before the Hon’ble Committee.”

98. The Committee desired to know the nature and extent of leakages in service tax collections by way of under-reporting by ‘Service Providers’, to which the Government, in their written reply, stated as under:

“Whereas individual instances of service tax evasion have been detected through Audit and Anti-evasion action, large-scale leakage in Service Tax collections by way of under-reporting by service providers has not been noticed. Moderate rates of tax, availability

of credit on inputs and inputs services, large-scale taxpayer awareness programme through advertisements, periodic survey of potential taxpayer are the measures adopted to curb leakage in Service Tax collections.”

99. During the oral evidence, the Committee raised serious concerns about the evasion of service tax, particularly that of under-reporting by service providers, to which the Revenue Secretary responded as follows:

“The growth rate, as I have mentioned, has been very good. Since it is a new tax, we have really not been pressing too hard on the collection. It is coming in its routine fashion because it could create a lot of backlash if we try to press too hard on this. So, as a policy, we will have to look at it in a year or two after it has stabilised.

There was also a question as to how do we link up with the State Governments because there is, of course, the need for allocation. Right now according to the 12th Finance Commission recommendations, we are sharing service tax revenue. But we have been already discussing with the State Governments on possible different ways of collecting the service tax including both the State and the Centre level. So, this is not an area where we have been pressing too hard at this stage, particularly, considering the fact that we are getting quite a lot of revenue.”

100. The Chairman, CBEC explained specifically on the issue as follows:

“...under Section 83 of the Finance Act, 1994 read with Section 11D of the Central Excise Act, any service provider, who collects service tax, is required to deposit that service tax into the Government treasury. Now, where he does not do so, the officers take measures to collect that service tax. As explained by the Revenue Secretary, the Government has not sanctioned any separate staff for service tax as such. The existing network of the Central Excise is being utilised for collection of service tax. As a pilot project we have established service tax commissionerates in the four metros, and we are looking at the working as to what will be the correct situation and the establishment that would be required. All these things are being looked into. We are going back to the Government and we are going to ask for specific staff for service tax. But what we do is that we hold the whole service

tax *melas*. We organise programmes to create awareness among the various service tax providers so that it is voluntarily given to the Department. But of course, we also have the Central Excise Intelligence Machinery where they collect specific intelligence for identifying those service providers who collect service tax but do not pay to the Government. There have been some cases but not many. But we are looking at it. We are strengthening our audit system of service tax providers.”

101. To a query raised by the Committee as how would the audit help the department check the leakage of revenue, the Chairman, CBEC stated as under:

“When the Audit party goes to the particular establishment, they look at the documents and then they would find out where they have collected a service tax. Then, they check back whether that much amount has been credited to the Government.”

102. Further probed by the Committee as to whether the department’s auditors check the statements submitted by the service providers, the Chairman, CBEC stated the following:

“On a selective basis we have a system. It is not that every service provider would be audited, nor is it possible. We have a selection basis. On that basis, we do that.”

103. The Director-General, Central Excise Intelligence, also explained further on the issue as under:

“Our unit has zonal units in all the major zones; in 2005-06, we have detected 546 cases of service tax evasion, amounting to Rs.498 crore, out of which we have recovered about Rs.330 crore on the spot, even before the show-cause notice was issue. For the remaining cases, show cause notices will be issued after we quantify the tax evasion. So, this is a major achievement in comparison with our total tax evasion.”

104. The Director-General, further elaborating on the strategy to detect leakage of service tax revenue, stated the following:

“By leakage, we mean that they are collecting service tax from the customers and not depositing. That is also covered by that. we do send decoy customers. We collect that type of intelligence also. But at the moment, I will not be able to quantify as to how much is the detection. We will send a note on that. but it includes both. But the break up, we are not able to give at the moment.”

105. When asked by the Committee on the penalty for collecting and not depositing the tax, the Director-General stated the following:

“it depends on adjudication. In any case, penalty has been made mandatory. It is the discretionary power of the adjudicator. After we issue show cause notice, we become *functus officio*. Then, it goes to the adjudicator.”

106. Further adding on the issue, the Director-General stated the following on the nature of punishment for such offences:

“Legal system does not provide any conviction. There is no conviction in service tax cases. There is only penalty.”

107. The Chairman, CBEC supplemented the reply stated by the Director General as follows:

“Immediate effort is to collect the tax which has not been paid, either by leakage or by way of evasion. The emphasis is on immediate collection on spot recoveries that he was highlighting. There are procedures under the law, if he deposits 25 per cent of the duty involved towards penalty, then there need not be any show cause notice and the matter rests there. But if he does not do it then the Department completes investigation, issues show cause notice, depending on the gravity of the case, the penalty may be imposed by the adjudicating authority. But in any case, it will not be less than 25 per cent. If it is a case of fraud, it will go up to 100 per cent of the duty evaded, as he explained; it depends on the process of adjudication.”

108. As the Committee were not satisfied with the severity of the punishment for the offenders involving higher revenue stake, the Revenue Secretary stated the following:

“Both on the excise and customs side, since you have studied the Direct Tax Law (Amendment) Bill and the Tax Law (Amendment) Bill of last year, we do have punitive measures but for Service Tax we have not yet introduced for the reasons that I have mentioned.”

109. The Chairman, CBEC supplemented the reply on the issue as under:

“The experience of the Department in the case of prosecution has not been very encouraging. So, keeping that in mind, in 2004 Budget an introduction was made into both the laws for compounding of the offences to avoid prosecution so that they will pay a fixed amount of penalty.”

110. The Committee take note of the fact that the extent of spot recovery of service tax- which works out to 66% of the total service tax evaded, as a result of detection of evasion of the tax by the Directorate General of Central Excise Intelligence (DGCEI) is a cause for serious concern, as it reveals the extent to which service tax evasion exists in the system. The trend shows that there is hardly any fear of detection and punishment in the minds of service providers, which the Committee feel, is the result of the lighter punishment that is meted out to the offenders. Even if the fact remains that the Government is being cautious, as Service Tax is a relatively new concept, the Committee feel that having no legal provision that provides for conviction for such evaders will prove to be detrimental at a later stage. The Committee also take note of the fact that on the contrary, the law provides for an escape route in the sense that if the evader deposits 25% of the tax evaded in addition to the total tax to be paid, he is let free without any further action against him.

111. Further still, the minimum penalty fixed, if such a case reaches the adjudication level, is also fixed at 25% of the tax due. The Committee, taking the above into consideration, recommend the Government to bring in the necessary legal changes early for enabling conviction of the tax offenders as well as increase the rate of survey and searches in order to inculcate a sense of fear among the tax evaders.

NEW DELHI;
19 May, 2006
29 Vaisakha, 1928 (Saka)

MAJ. GEN. (RETD.) B.C. KHANDURI,
Chairman,
Standing Committee on Finance.

ANNEXURE I

'COPY OF THE CENTRAL BOARD OF DIRECT TAXES' LETTER
F. NO. 385/40/2005-IT(B) DATED 19TH SEPTEMBER, 2005
ADDRESSED TO ALL CHIEF COMMISSIONERS OF
INCOME TAX (CADRE CONTROLLING)

Sub: Common Irregularities observed by Reserve Bank of India in the issue of Refund Orders - Remedial Action to be taken by Income Tax Department- regarding

I am directed to state that the Reserve Bank of India has pointed out the following common irregularities committed by the officers of Income Tax Department with regard to issue of Income Tax Refund Orders (ITROs):

1. The list of officers who are authorized to issue ITROs is not being updated regularly by the Income Tax Department. It is a pre-requirement that in the event of any change in the incumbency of the signing officers on account of transfer, retirement, termination of service, death, etc., duly attested specimen signature of the relieving officers should be furnished by the Income Tax Department and the signature of the previous incumbent should be deleted from the file. However, while the signatures of the newly posted/promoted officers are registered with RBI promptly, the signatures of the retired/transferred officers are not got cancelled by the Department.
2. The serial number of the ITRO books allotted to each Ward/ Circle and the distinct numbers of foils in each ITRO book are required to be invariably intimated to the concerned RBI office beforehand. However, this practice is not being followed presently by most of the Income Tax Offices. As a result, RBI is not aware of the number/series of the ITRO books used by each Ward/Circle or the distinct numbers of ITROs in each book.
3. Several ITRO books are in use simultaneously in each Ward/ Circle, which is against safe banking principles. Further, even though the ITRO books are required to be kept in the personal custody of the ITRO issuing officers, it appears that this not being ensured always.

4. The "list of lost/stolen/missing ITROs from their books" is not advised by the concerned Income Tax Officer to RBI, immediately after the loss is detected, for recording "stop payment" in their books. At times these are not reported at all or reported after 8-9 months, by which time the forged instrument might have been encashed. Availability of this information to RBI in time will go a long way in the prevention of such frauds.
5. The authorized officials have not been furnishing the complete 12-digit number of the missing ITROs (3 alpha suffixes, 3 numeral suffixes and the 6 digit number) while reporting the loss of the instruments to RBI for recording stop orders.
6. Instructions are in place in RBI for cross-verification of the high value ITRO advices with the concerned Income Tax Officer for its genuineness. For this, an up-to-date list of telephone numbers of contact persons in each Circle/Ward is required at each RBI office. Further, active cooperation from Income Tax Department is required for cross checking the genuineness of high value ITROs received for payment.

You are requested to kindly direct all assessing officers in your region to follow the above guidelines of RBI so that any fraudulent issue and encashment of refund is prevented.

Yours faithfully,

Sd/-
(Anand Jha)
Director (Budget)

ANNEXURE II

TAX EXPENDITURE UNDER THE CENTRAL TAX SYSTEM: FINANCIAL YEAR 2004-05

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 bases 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”. They have an impact on government revenue (i.e. they have a cost) and reflect the policy choices of the Government.

Tax preferences may be viewed as subsidy payments to preferred taxpayers. Such implicit payments are referred to as ‘tax expenditures’ and it is often argued that they should appear as expenditure items in the Budget. In this context, the basic issue is not one of tax policy but one of efficiency and transparency—programme planning requires that the policy objectives be faced explicitly; and programme budgeting calls for the inclusion of such outlays under their respective programme headings. Tax expenditures are spending programmes embedded in the tax statute.

This document seeks to list the revenue impact of tax incentives or tax subsidies that are a part of the tax system of the Central Government. In order to determine the tax expenditures, it is necessary to establish a “benchmark” tax structure that applies the relevant tax rates to a broadly defined tax base—e.g. personal income, business income, imports or production. Tax expenditures are then measured as deviations from this benchmark. Reasonable differences of opinion exist about what should be considered a normal part of the tax system and hence about what should be considered tax expenditure. This issue has been addressed by attempting to estimate the revenue loss only in respect of major items of tax preferences over which there is no ambiguity. The estimates are for financial year 2004-05, the last year for which the data are available.

In general, the estimates of tax expenditures have been made on the basis of the following assumptions:

- (a) The estimates and projections are intended to indicate the potential revenue gain that would be realised by removing

exemptions, incentives, weighted deductions and similar measures. The estimates are based on the short term impact analysis. They are developed assuming that the underlying tax base would not be affected by removal of such measures. To the extent the behaviour of economic agents, overall economic activity or other government policies could change along with the elimination of the specific tax preference, the revenue implications could be different.

- (b) The cost of each tax concession is determined separately, assuming that all other tax provisions remain unchanged. Many of the tax concessions do, however, interact with each other. Strictly, the interactive compounded impact of tax incentives could turn out to be different from the revenue forgone calculated by adding up the estimates and projections for each provision.

The assumptions and the methodology adopted to estimate each of the tax preferences are indicated in the relevant section.

Direct taxes

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, and co-operative sector and accelerated depreciation for capital investment. Most of these tax benefits can be availed of by both corporate and non-corporate taxpayers.

The last exhaustive list of incentives under the Income-tax Act appeared in the Report of the Advisory Group on Tax Policy and Tax Administration for the Tenth Plan, Planning Commission, May 2001, Appendix 4.1 While some of those incentives have since been rescinded, others have been enacted. Here it is attempted to estimate the tax expenditures on the major items.

a. Corporate Sector

Since large business is organized as companies, the tax expenditure on companies is large. For the purposes of estimating the tax expenditure, a list of about 9000 companies from the database of Centre for Monitoring the Indian Economy (CMIE) was sent to the field formations seeking tax-related information in respect of the financial year 2003-04 (assessment year 2004-05). Information was received in respect of about 2600 companies on random basis, from different tax

centres in Mumbai, Delhi, Ahmedabad, Chennai, Bangalore and Pune. This tax-related information was plotted against the financial results of these companies. After cleaning the data of inconsistencies, the sample size was reduced to 1689 companies from different sectors. These sample companies reported Rs. 1,02,325 crores as profits before taxes (excluding losses reported by companies) but declared a total income (hereafter referred to as "taxable income") of Rs. 50,735 crores only. These companies paid Rs. 19,816 crores as corporate tax during the financial year 2003-04. Therefore, the sample companies account for 30.14 percent of voluntary tax payment of Rs. 65,753 crores (i.e. aggregate of tax deduction at source and advance tax) during the year.

Table 1 profiles the sample companies across profit range. Companies with profits above Rs. 500 crores accounted for 73.5 per cent of the total profits of the sample companies but their share in the total taxes was only 60.70 per cent at an effective tax rate of 15.99 per cent. This was substantially lower than the effective tax rate of 19.37 per cent for the sample companies and the statutory tax rate of 35.875 per cent. Further, 593 companies with profits less than or equal to zero contributed 9.23 per cent of the total taxes.

Table 1: Profile of sample companies across profit range

Sl.No.	Profits before tax	Number of companies	Share in total profits	Share in total taxes	Effective rate of tax
1.	Less than Zero	380	0	7.54	Infinity
2.	Zero	213	0	1.84	Infinity
3.	0-5 lakhs	52	0.001	0.09	13.32
4.	5 lakhs-10 lakhs	33	0.002	0.003	24.90
5.	10 lakhs-25 lakhs	68	0.01	0.01	16.90
6.	25 lakhs-50 lakhs	74	0.03	0.05	40.62
7.	50 lakhs-1 crore	90	0.06	0.14	41.44
8.	1 crore-5 crore	269	0.644	0.78	23.39
9.	5 crore-10 crore	104	0.73	0.90	24.06
10.	10 crore-25 crore	148	2.34	2.66	22.04
11.	25 crore-50 crore	88	3.10	4.14	25.86
12.	50 crore-100 crore	66	4.70	4.34	17.89
13.	100 crore-500 crore	65	14.87	16.79	21.86
14.	Above 500 crores	39	73.50	60.70	15.99
15.	All Sample Companies	1689	100	100	19.37

Table 2 profiles the sample companies across effective tax rate. Companies within average effective rate of less than 20 per cent accounted for 55.8 per cent of the total income but only 19.95 per cent of the total taxes paid by all the sample companies. In other words, a large number of companies contributed disproportionately lower amount in taxes in relation to their profits. Further, 534 companies comprising 8.8 per cent of the total income contributed 30.77 per cent of the total taxes. Therefore, the tax liability across companies is unevenly distributed. This is primarily due to the various tax preferences in the statute.

Table 2: Profile of sample companies across effective tax rate

Sl.No.	Effective tax rate	Number of companies	Share in total income	Share in total taxes
1.	Less than or equal to 0	327	4.1	0.0
2.	0-5	145	16.2	2.26
3.	5-10	205	24.5	8.98
4.	10-15	78	6.7	4.61
5.	15-20	63	4.3	4.10
6.	20-25	77	16.0	17.99
7.	25-30	103	7.4	10.69
8.	30-35	113	8.2	13.66
9.	35-36.59	44	3.7	6.94
10.	>36.59	150	8.8	21.39
11.	Indeterminable	384	0.0	9.38
	Total	1689	100	100

The tax foregone on each tax concession/preference claimed by the sample companies has been estimated by applying the corporate tax rate of 36.59 per cent on the amount of deduction. The ratio of tax foregone to actual tax paid by the sample companies has been separately computed for each tax concession/preference and applied to the total voluntary tax payments by all corporate tax payers to estimate the total tax foregone on each such tax concession/preference.

The tax foregone in respect of export profits has been computed through an indirect method. The revenue foregone on exports from

Software Technology Parks, 100 per cent EOUs and Special Economic Zones is estimated in the manner detailed below:—

- (i) **Software Technology Parks**—The tax return data of sample companies have been used to estimate the profit margin on exports by units located in software technology parks. Such profits are estimated in the range of 27 per cent to 30 per cent. However, keeping in view the profit margin of the sample companies, the profit-margin on exports from this sector is assumed to be 25 per cent. This profit ratio has been applied to the total exports of software and information technology services during the financial year 2004-05 (figures for which have been obtained from NASSCOM sources) to estimate the aggregate profits from the total exports of software and IT services. The revenue foregone has been estimated by applying the tax rate of 36.59 per cent for the relevant year to such aggregate profits.
- (ii) **Special Economic Zones**—The estimate of revenue foregone on account of export profits derived by units located in Special Economic Zones is based on the same method as adopted in the case of Software Technology Parks. However, the profit from exports from the Special Economic Zones has been estimated to be 20%. The export figures for financial year 2004-05 have been taken from the website www.sezindia.nic.in.
- (iii) **Export Oriented Units**—The estimate of revenue foregone on account of export profits derived by 100% Export Oriented Units is based on the same method as adopted in the case of Special Economic Zones.

Section 80-IA of the Income-tax Act, 1961 provides for deduction in respect of profits derived from development of infrastructure facilities, SEZs and Industrial Parks, generation of power, and providing telecommunication services. Similarly, section 80-IB of the Income-tax Act, 1961 provides for deduction in respect of profits derived from housing projects, production of mineral oil, development of scientific research, integrated business of handling, storage and transportation of foodgrains, and industries set up in backward areas. The revenue foregone on account of these tax benefits has been estimated separately by adopting the proportionate assignment method described above. The same method has been adopted for estimating revenue foregone on account of section 80-IC.

The Income-tax Act, 1961 provides for depreciation calculated on the written down value at accelerated rates. These rates are substantially higher than what is permissible under the Companies Act, 1956. Consequently, in terms of the accounting standards prescribed by the Institute of Chartered Accountants of India, every company is required to report its deferred tax liability. The revenue foregone on account of accelerated depreciation has been computed by applying the ratio of the deferred tax liability to actual tax paid by the sample companies, to the total voluntary tax payments by all corporate taxpayers during 2004-05.

Section 35 (2AB) of the Income-tax Act, 1961 provides for a weighted deduction of 150 per cent for both capital and revenue expenditure incurred on scientific research and development in certain specified sectors. The expenditure on scientific research and development by the sample companies is Rs. 500 crores towards capital expenditure and Rs. 2183 crores towards revenue expenditure during the financial year 2004-05. The total deduction allowable under section 35 (2AB) in respect of such expenditure is Rs. 4025 crores. Ordinarily, depreciation at an estimated rate of 15 per cent of capital expenditure on scientific research and development and 100 per cent in respect of revenue expenditure would have been allowable. Therefore, the deduction under the Income-tax Act is higher by Rs. 1767 crores, thereby conferring a tax benefit of Rs. 634 crores to the sample companies. The ratio of this tax benefit to the actual taxes paid has been applied to the total voluntary payments made by the corporate sector in the year 2004-05 and further scaled back by 25 per cent to adjust for sample bias, if any, to determine the amount of revenue foregone.

Table 3 lists the major tax expenditure (in terms of revenue loss) on the corporate taxpayers during the financial year 2004-05.

Table 3: Major tax expenditure on corporate tax payers during financial year 2004-05

Sl.No.	Nature of Incentive/deduction	Revenue foregone (Rs. in crs.)
1	2	3
1.	Export profits of software producing units located in Software Technology Parks (section 10A)	7080
2.	Export profits of units located in Special Economic Zones, including Export Processing Zones and Free Trade Zones (section 10A)	1340

1	2	3
3.	Export profits of units located in Export Oriented Units (section 10B)	2320
4.	Profits derived from development of infrastructure facilities, SEZs and Industrial Parks, generation of power, providing telecommunication services (section 80-IA)	5832
5.	Profits derived from housing profits, production of mineral oil, development of scientific research, integrated business of handling, storage and transportation of foodgrains, industries set up in backward areas (section 80-IB)	11523
6.	Profits derived by units set up in Special category States like North-Eastern States, Uttaranchal, Himachal Pradesh and Jammu and Kashmir (section 80-IC)	362
7.	Accelerated depreciation (section 32)	27077
8.	Weighted deduction for scientific research and development [section 35 (2AB)]	2318
Total		57852

There are a number of other deductions available to the corporate sector. In particular, these deductions relate to:

- (i) donations to charitable trusts and institutions (section 80G)
- (ii) donations to institutions, universities or colleges, for the purposes of scientific or social science or statistical research [section 35 (1)]
- (iii) donations to political parties (section 80GGB);
- (iv) expenditure on project or schemes for promoting the social and economic welfare of, or the uplift of, the public, and recommended by the National Committee;
- (v) concessional tax regime for shipping industry.

The information relating to revenue foregone in respect of the aforesaid tax preferences is currently not available and, therefore, cannot be furnished in this report.

b. Co-operative Sector

Section 80P of the Income-tax Act allows a deduction of the whole of the amount of profits and gains of a co-operative society attributable to the activity of carrying on the business of banking or providing

credit facilities to its members. The three broad categories of co-operative banks availing of this deduction are:—

- Urban Co-operative Banks
- State Co-operative Banks
- Central Co-operative Banks

The Directorate of Income Tax (Research) carried out a study on the revenue implication of deduction under section 80P in the case of Urban Cooperative Banks and brought out its findings in a report in March 2002. The report concluded that the revenue loss on account of allowing this deduction to Urban Co-operative Banks amounted to Rs. 872 crore in F.Y. 1999-2000 and Rs. 982 crore in F.Y. 2000-01. The revenue loss calculated for all Urban Co-operative Banks is equivalent to 20 per cent of the gross income of Scheduled Urban Co-operative Banks (UCBs).

Assuming that the ratio of incomes of scheduled and unscheduled UCBs remained unchanged, the revenue loss on account of this deduction for all UCBs has been worked out at 20% of the income of Scheduled UCBs for F.Y. 2004-05.

In the case of State Co-operative Banks, the revenue loss has been worked out by calculating the revenue loss in the case of Scheduled UCBs as a percentage of the income of Scheduled UCBs and then applying the same percentage to the income of such State Co-operative Banks. For Central Co-operative Banks also the same methodology has been adopted.

The income of Scheduled UCBs for F.Y. 2004-05 has been taken from the Report of the Reserve Bank of India. For State and Central Cooperative Banks, the income for 2004-05 was not available. However, the incomes for 2002-03 and 2003-04 were available in the same report and the income for 2004-05 has been estimated by following the trend of the previous two years. Accordingly, the gross revenue loss in F.Y. 2004-05, on account of deduction under section 80P, has been estimated at Rs. 1534 crores (Table 4).

Table 4: Tax expenditure on co-operative taxpayers during financial year 2004-05

(Rs. in crs.)		
Sl.No.	Nature of Incentive/deduction	Revenue foregone
1	2	3
1.	Profits of cooperative banks other than primary agricultural credit societies, from banking activities	1534

1	2	3
2.	Profits of primary agricultural credit societies from banking activities.	N.A.
3.	Profits of other primary cooperative societies from milk, marketing of agricultural produce, etc.	N.A.
	Total	1534

c. Individual taxpayers

The task force on direct taxes set up by the Government on 6th September, 2002, had constructed a typical tax payer profile for different income groups based on income-tax return data of 9.25 lakh individual tax payers from the city of Mumbai, which accounts for 35 per cent of the country's direct tax collections. The data related to four assessment years: 1998-99, 1999-2000, 2000-01 and 2001-02. The sample data for the four years was segregated into two categories, *i.e.* salaried and non-salaried taxpayers. For every income group and category, a typical taxpayer profile for each of the four assessment years was separately obtained. Thereafter, the four-year average of such profiles for each income group was determined to obtain a typical taxpayer profile for all income group for the purposes of revenue estimation. The typical tax payer profile developed by the task force on direct taxes, has been adjusted to reflect subsequent changes in the tax legislation. The tax expenditure on the individual taxpayers during the financial year 2004-05, has been estimated on the basis of the adjusted profile during the relevant year. Table 5 lists the major tax expenditure (in terms of revenue loss) on the non-corporate tax payers during the financial year 2004-05.

Table 5: Major tax expenditure on non-corporate tax payers during the financial year 2004-05

(Rs. in crs.)		
Sl.No.	Nature of Incentive/deduction	Revenue foregone
1.	Tax rebate for investment in specified savings instruments.	6568
2.	Tax rebate for senior citizens.	1446
3.	Tax rebate for women.	2121
4.	Interest income on securities, deposits with banks, etc.	1560
	Total	11695

Indirect Taxes

a. Excise duty

Excise duty is levied as per the rates specified in the First and Second Schedules to the Central Excise Tariff Act, 1985. In many cases, the various Finance Acts, specify the rates at which excise duty should be levied. The rates specified in various enactments are known as the 'tariff rates' of excise duty. Government has been delegated powers under Section 5A (1) of the Central Excise Act, 1944 to issue notifications in public interest to prescribe duty rates lower than what are prescribed in the Schedule. These rates prescribed by notifications are known as the 'effective rates'.

Accordingly, the revenue foregone is the difference between duty that would have been payable but for the issue of the notification, and the actual duty paid in terms of the relevant notification. Therefore:

$$\text{Revenue foregone} = \text{Value} \times (\text{Tariff rate of duty} - \text{Effective rate of duty}).$$

Duty foregone is, thus, zero if the tariff rate is equal to the effective rate.

Information relating to the value of clearances has been obtained from periodic returns filed by the duty paying units in respect of clearances made by them, and the duty paid. However, the data are not comprehensive.

Units which make only exempted goods are not registered, and are not required to file any returns with the department. As such, no data are available in respect of clearances by such units. To this extent the revenue foregone is underestimated. However, units which make both dutiable and exempted goods file returns in respect of clearances of exempted goods also. In respect of such units, it has been possible to work out the revenue foregone even in respect of exempted items. Therefore, the data relating to duty foregone cover the following:

- Duty foregone on items which attract a non zero effective duty prescribed under a notification; and
- Duty foregone on a fully exempted good, if the unit manufacturing such goods also makes dutiable goods.

The data generated by the excise department are captured by SERMON, a system that compiles returns received from the

Commissionerates. In 2004-05, SERMON data captured gross revenue of Rs. 95,048 crore representing 93 per cent of the actual gross revenue collection of Rs. 104,427 crore. This has been blown up to 100 per cent by assuming that the same pattern of coverage also applies to the remaining 7 per cent. The duty-foregone statement, therefore, has been inflated proportionately to estimate the total revenue foregone. Subject to the limitations discussed above, excise duty foregone during 2004-05 on account of exemption notifications is estimated at Rs. 12,431 crore.

Obviously, the revenue foregone is understated for the reasons mentioned above. From other sources, information has been collected to estimate the revenue foregone in respect of certain major exemptions (Table 6).

Table 6: Estimate of major tax expenditure under the excise duty regime

Sl.No.	Details of Exemption	Estimated revenue foregone (Rs. in crores)
1.	Small Scale Industries Exemption ¹	11,316
2.	Fertilizers ²	4,000
3.	Area based exemptions applicable in North Eastern States, Jammu & Kashmir, Uttaranchal, Himachal Pradesh and Kuchchh District of Gujarat. ³	1,502
4.	50% exemption from all duties of excise for North East Oil refineries.	1,200
	Total	18,018

Notes:

¹ As per a Study conducted by the National Institute of Public Finance & Policy (NIPFP).

² Estimated on the basis on Crisil Research & Information Services Limited data bank. During 2004-05 sales turnover of 14 major fertilizer Companies was about Rs. 25,573 crore.

³ On the basis of Department records.

The estimates of revenue foregone presented in Table 6 do not include revenue foregone on account of *ad hoc* exemption orders issued under Section 5A (2) of the Central Excise Act, 1944, that tend to relate to circumstances of an exceptional nature.

b. Customs duty

Customs duty is levied as per the rates specified in the Schedule to the Customs Tariff Act, 1975. The Customs Tariff Act, 1975 also provides for levy of additional duty of customs (commonly referred to as countervailing duty or CV duty), which is levied at a rate equal to the duties of excise leviable on such goods if they were manufactured in India. As already indicated, these duties of excise are levied under various Finance Acts, which specify the rates at which they should be levied. The rates specified in various enactments are known as the 'tariff rates'. The Central Government has been delegated powers under Section 25A (1) of the Customs Act, 1952 to issue notification in public interest to prescribe duty rates lower than what are prescribed in the Schedule. These rates prescribed by notifications are known as the 'effective rates'.

$$\text{Revenue foregone} = \text{Value} \times (\text{Tariff rate of duty} - \text{Effective rate of duty}).$$

Duty foregone is, thus, zero if the tariff rate is equal to the effective rate.

The estimate of the revenue foregone for 2004-05 on account of issue of various exemption notifications, is based on the data generated from bills of entry filed in the Indian Customs Electronic Data Interchange System (ICES) at 20 Electronic Data Interchange (EDI) locations. The EDI data, however, are not complete, as certain ports fall outside EDI. Besides, the EDI data did not capture bills of entry in respect of imports by EOUs, warehouse bills of entry, and where manual bills of entry are filed in EDI locations.

The revenue of foregone takes into account exemptions from basic customs duty, CV duty and also exemption notifications issued under the Central Excise Tariff Act, 1985, which are relevant for levy of CV duty. Though, generally, the tariff rates should be taken into account for working out the revenue foregone, some exceptions have been made because of the software used by the ICES. In the case of industrial goods (non-agricultural goods), the peak effective rate was generally 20% upto 28.2.2005 and 15% from 1.3.2005 onwards. Though with effect from 1.3.2005, the peak rate was generally put as the tariff rate, this was not so during the period 1.4.2004 to 28.2.2005. For the purpose of revenue foregone for industrial tariff in general, this peak effective rate has been deemed to be the tariff rate. To illustrate,

Case 1: Tariff rate was 30 per cent. Notification No. 5/2004 prescribes a universal effective rate of 20 per cent for non-agricultural goods. Goods were imported at 20 per cent under this universal effective rate. The revenue foregone has been taken as Nil.

Case 2: Tariff rate was 30 per cent. A lower universal effective rate (5 per cent) has been prescribed for some industrial goods. Revenue foregone has been calculated as Value X (20 per cent=5 per cent) of Value X (15 per cent=5 per cent), depending on whether 20 per cent or 15 per cent was the prevailing peak rate.

However, for agricultural items, the revenue foregone has been calculated with reference to the tariff rate.

For 2004-05, gross customs revenue captured by EDI data is Rs. 35,364 crore as against actual gross revenue collection of Rs. 58,867 crore. EDI data thus represents about 60% of actual reported gross revenue collection for 2004-05. Therefore, the revenue foregone estimates are based on a fairly large sample.

EDI data have been blown up to work out the estimated revenue foregone for the year 2004-05, with appropriate adjustments where required. It has been seen that EDI data coverage is particularly low for edible oils and petroleum crude and products, as the major imports of these commodities were through ports, which were not under EDI at the relevant time. Data on actual revenue realized from petroleum and edible oils have been collected separately. When the actual revenue from these two commodities is added to EDI data, the coverage went up to Rs. 49655 crore or about 84% of the total revenue. This still leaves a shortfall of about 16% from the actual revenue. In the absence of any other data, it has been assumed that composition of import of goods giving the balance revenue was unchanged and was the same as per the EDI data. After suitable inflation of the data base, the duty foregone on account of all exemption notifications is estimated at Rs. 92,561 crore. The revenue foregone data for each of the chapters of Customs Tariff Act is presented in Table 7.

Table 7 : Estimates of major tax expenditure under the Customs duty

Chapter	Brief Description of Goods	Estimated revenue foregone (Rs. in crores)
1	2	3
1	Live animals	3
2	Meat and edible meat offal	0

1	2	3
3	Fish and crustaceans, other aquatic invertebrates	8
4	Dairy Products	16
5	Other products of animal origin	9
6	Live trees and other plants	2
7	Edible vegetables, certain roots and tubers	625
8	Edible fruit and nuts	1021
9	Coffee, tea, mate and spices	208
10	Cereals	1
11	Products of the milling industry	5
12	Oilseeds, grains, seeds, fruit	52
13	Lac, gums and resins	35
14	Vegetable plaiting materials	1
15	Animal or vegetable fats	7545
16	Preparations of meat or fish	0
17	Sugar	1096
18	Cocoa	8
19	Preparations of cereals	33
20	Preparations of vegetables	8
21	Misc. edible preparations	49
22	Beverages and spirits	54
23	Residues and waste from food industry	105
24	Tabacco	3
25	Salt, sulphur earths and stone	167
26	Ores	102
27	Mineral fuels and mineral oils	13725
28	Inorganic chemicals	814
29	Organic chemicals	3238
30	Pharmaceutical products	505

1	2	3
31	Fertilizers	627
32	Tanning and dyeing extracts, pigments	345
33	Essential oils	96
34	Soap and washing preparations	73
35	Albuminoidal substances	38
36	Explosives, matches	6
37	Photography goods	167
38	Miscellaneous chemical products	712
39	Plastics	1194
40	Rubber	458
41	Hide and skins and leather	277
42	Articles of leather	12
43	Furskins	3
44	Wood	101
45	Cork	0
46	Manufactures of straw	0
47	Wood Pulp	229
48	Paper	673
49	Printed books, newspapers	393
50	Silk	341
51	Wool	262
52	Cotton	1193
53	Other Vegetable fibres	63
54	Man made filaments	3023
55	Man made staple fibres	554
56	Wadding and non wovens	64
57	Carpets	18
58	Special woven fabrics	577

1	2	3
59	Coated textile fabrics	370
60	Knitted fabrics	139
61	Knitted ready made garments	10
62	Woven garments	25
63	Made ups	119
64	Footwear	38
65	Head gear	1
66	Umbrellas	8
67	Feathers/artificial flowers	1
68	Articles of stone, plaster	53
69	Ceramic products	128
70	Glass and glass ware	154
71	Precious stones, jewellery	15024
72	Iron and steel	6866
73	Articles of iron and steel	901
74	Copper and articles thereof	276
75	Nickel and articles thereof	150
76	Aluminium and articles thereof	409
78	Lead and articles thereof	83
79	Zinc and articles thereof	179
80	Tin and articles thereof	25
81	Other base metals	75
82	Tools and implements	201
83	Miscellaneous articles of base metals	78
84	Machinery	8660
85	Electrical machinery	12385
86	Railways or tramways, locomotives, rolling stocks etc.	145
87	Motor vehicles	1183
88	Aircrafts	219

1	2	3
89	Ships, boats and floating structures	452
90	Optical/photographic instruments	2435
91	Clocks and watches	26
92	Musical instruments	3
93	Arms and ammunitions	178
94	Furniture etc.	76
95	Toys and games	63
96	Miscellaneous manufactured articles	164
97	Works of art, antiques	0
98	Project imports, baggage	317
Total		92,561

The above figures of revenue foregone do not exclude all export-related input taxes. This information was calculated separately on the basis of returns received from the Commissionerates. The figures are as under (Table 8), and are included in the overall figure of Rs.92,561 crore. Most items in Table 8 may not, therefore, be termed incentive schemes, since they largely represent input tax credit that has to be allowed in order to offer a level playing field to our exporters in international markets. In this sense, the revenue foregone from customs duties—Rs. 92,561 crore—should be scaled down somewhat.

Table 8 : Export-linked Drawbacks

(Rs. in crores)		
Sl. No.	Scheme	Revenue foregone
1	2	3
1.	Duty entitlement Pass Book (DEPB)	9671
2.	Quantity Based Advance License (QBAL)	8851
3.	100 per cent Export Oriented Units (EOUs)	6826
4.	Export Promotion Capital Goods Scheme (EPCG)	4710
5.	Special Economic Zone (SEZs)	1314
6.	Value Based Advance License (VBAL)	1264
7.	Special Imprest Licence (SIL)	1152

1	2	3
8.	Export Processing Zones (EPZs)/ Software Technology Parks (STPs)	852
9.	Duty Free Replenishment Certificate (DFRC)	783
10.	Pass Book	5
Total		35430

The above does not include revenue foregone on account of exemption notifications issued under Section 25 (2) of the Customs Act, 1962.

Conclusion

In the absence of a well organized institutional mechanism and comprehensive computerisation, it has not been possible to estimate revenue loss associated with all tax preferences. However, an attempt has been made, in this first year of publication of this document, to take a broad approach and include estimates of the revenue loss associated only with the major tax preferences. As computerisation of the management systems of the income-tax department and customs and central excise department progress, it will significantly improve the government's ability to refine these estimates.

Given the above caveats, the estimated overall revenue foregone is as shown in Table 9.

**Table 9 : Revenue Foregone
(Financial Year 2004-05)**

	(Rs. in crores)
Corporate income tax	57852
Personal income tax	11695
Co-operative sector related	1534
Excise duty (i) Exemptions (other than through notifications)	18018
(ii) Exemption notifications	12431
Customs duty	92561
Total	194091
-Export credit related	-35430
Total	158661

WITHDRAWAL OF EXEMPTIONS PERTAINING
TO INDIRECT TAXES

A. Customs

- (1) Melting scrap of iron and steel. As against nil duty earlier, it will now attract 5% duty.
- (2) Saddle tree. It would now attract duty of 12.5%.
- (3) 5% concessional duty of customs on parts of outboard motors imported by specified agencies. They will now be at 12.5%.
- (4) Spare parts for maintenance of textile machinery. They will now attract duty of 10% or 12.5%.
- (5) Videocassettes and videotapes imported by Television Centre of All India Radio, or by M/s Electronic Trade and Technology Development Corporation Ltd. or by others. They will now attract duty of 10%.
- (6) Concessional rate of 5% on Nickel and articles of nickel (falling under Chapters 75, 85 and 90) is being restricted to goods falling under chapter 75 only.
- (7) Food preparations containing flour, meal, starch, etc. in a specified proportion meant for infant use and put up for retail sale. As against concessional rate of 5% earlier, such goods will now pay duty at 30%.
- (8) Food products (excluding alcoholic preparations) imported by hotels/tourism industry in terms of licenses issued under 1997-2002 Exim Policy. Such items will now pay merit rate of 30%, as against concessional rate of 25% earlier.
- (9) Concessional rate of 5% plus Nil CVD on plant, machinery and equipment imported for setting up of Currency Note/ Bank Note Press at Salbony, Mysore, Nasik and Dewas. Such imports will now attract duty of 12.5% plus full CVD.
- (10) Specified goods for manufacture of capital goods for setting up of a unit with an investment of Rs. 5 crore or more. As against concessional rate of 10% such imports will now attract duty at merit rates.

- (11) Specified parts of outboard motors. As against 5% concessional rate they will now attract duty of 12.5%.

B. Central Excise

1. Excise duty of 8% with CENVAT credit has been imposed on:

- (1) Goggles
- (2) Articles of wood
- (3) Registers, accounts books, order books, receipt books, letter pads, memorandum pads, dairies, binders, folders, file covers, etc. (excluding note books and exercise books)
- (4) Paper labels
- (5) Paper pulp moulded trays
- (6) Articles of mica
- (7) Goods containing at least 25% by weight of fly ash/ phospho gypsum
- (8) Roofing tiles
- (9) Raw, tanned or dressed fur skins
- (10) Portable receivers for calling, alerting or paging
- (11) Henna powder, not mixed with any other ingredient
- (12) 100% wood free plain or pre-laminated particle or fiberboard, made from sugarcane bagasse or other agro-waste
- (13) Parts of walking-sticks, seat-sticks, whips, riding-crops and the like
- (14) Parts of drawing and mathematical instruments
- (15) Frames and mountings for spectacles, goggles or the like, of value below Rs. 500 per piece.

2. Excise duty of 12% has been imposed on commuters.

3. Excise duty has been increased from 8% to 16% on:

- (1) Mosaic tiles
- (2) Glassware
- (3) Lay flat tubing
- (4) Cigarette filter rods

4. Excise duty exemption on following goods has been withdrawn. In general these goods will now attract excise duty of 16%:

- (1) Set Top Boxes
- (2) Railway track machines
- (3) Umbrellas and sun umbrellas, and their parts.
- (4) Soap manufactured under a scheme for sale of Janata soap.
- (5) Strips and tapes of polypropylene used in the factory of its production in the manufacture of polypropylene ropes.
- (6) Parts and components of motor vehicles transferred to a sister unit for manufacture of goods falling under chapter 87.
- (7) Goods (other than Electrical stampings and laminations; Bearings; and Winding wires) supplied for manufacture of PD pumps for handling water.
- (8) Specified Goods meant for display in any fair or exhibition in India. Merit rate would apply.
- (9) Parts of tableware, kitchenware and other household articles of—iron and steel, copper, aluminum.
- (10) Sulphur (2503 00 10). Sulphur falling under this tariff item for fertilizers will be exempt.
- (11) Mixture of graphite and clay for manufacture of pencils or pencil leads.
- (12) Aluminum ferrules for manufacture of pencils.
- (13) Tobacco used for smoking through 'hookah' or 'chilam', commonly known as 'hookah' tobacco or 'gudaku'.

5. Withdrawal of exemption on goods made without the aid of power

A number of excisable goods have been given exemption from excise duty if no power is used in the process of manufacture. There are disputes as to what constitutes use of power, and also whether use of power in a particular process can be considered as use of power in manufacture.

Since such units are small, they will anyway be eligible for SSI exemption scheme. Having regard to this, following exemptions to goods manufactured without the aid of power have been removed:

1. Essential oils, solutions of essential oils, other than sandalwood
 2. Perfumes and toilet waters
 3. Blocks, ceramic tiles and other ceramic goods
 4. Roofing tiles, chimney pots, chimney liners, Ceramic pipes and conduits etc.
 5. Unglazed ceramic flags and paving, vitrified tiles
 6. Padlocks, locks of base metal, clasps
 7. Signaling flares, rain rockets, fog signals and other pyrotechnic articles (excluding fireworks)
 8. Precious metals and metals clad with precious metals excluding silver of Chapter 71
 9. Other items of Chapter 71
 10. Metal containers of iron, steel and aluminium
 11. Lacs, gums resins, other vegetable saps and extracts
 12. Soap
 13. Turpentine oil, rosin oil
 14. Veneer sheets, and sheets for plywood and other wood sawn lengthwise, sliced or peeled, of a thickness not exceeding 6 mm
 15. Wood (including strips and friezes for parquet flooring, not assembled) continuously shaped along any of its edges or faces
 16. Biscuits
 17. Marble slabs and tiles
 18. Sugar
6. **Withdrawal of exemption on unbranded goods:**

Certain goods have been exempted from central excise duty if they are sold without a brand name. Since unbranded products are mainly made by smaller units, they will be eligible for exemption under the general SSI exemption

scheme. Larger units will pay excise duty but will be able to take input tax credit. Having regard to this, the exemption from excise duty has been withdrawn in the case of following unbranded goods:

- (1) Wadding, gauges.
- (2) Protein concentrates and textures protein substances.
- (3) Churan for paan.
- (4) Custard powder.
- (5) Food flavouring matter.
- (6) Sugar syrups containing added flavouring or colouring matter (excluding preparations for lemonades or other beverages intended for use in aerated waters).
- (7) Mineral water.
- (8) Waters other than aerated and mineral waters, ice and snow, not containing sugar or other sweetening matter or flavour (2201 90 90).
- (9) Waters other than aerated and mineral waters, ice and snow containing sugar or other sweetening matter or flavour other than aerated waters or lemonade (2202 10 90).
- (10) Beverages containing milk (2202 90 30).
- (11) Edible mixtures or preparations of animal vegetable or fats and oils (other than margarine and linoleum).

Service Tax

The following service tax exemptions have been withdrawn:

- (1) The exemptions in relation to general insurance where—
 - (i) Premium is received from re-insurance both domestic and overseas;
 - (ii) All business for which premium is booked outside India;
- (2) Exemption for services, other than accounting, auditing, and statutory certification services, provided by a practicing chartered accountant, company secretary or cost accountant in his professional capacity;

- (3) Exemption for taxable services provided by a Call Centre or a Medical Transcription Centre;
- (4) Exemption for taxable service provided in relation to Enterprise Resource Planning (ERP) software system provided by a management consultant in connection with the management of any organization;
- (5) Exemption for catering services provided on a railway train by an outdoor caterer;
- (6) Exemption for catering services provided within the premises of an academic institution or medical establishment by an outdoor caterer.

* * * *

ANNEXURE IV

STATUS OF FULL COMPUTERISATION OF
INCOME TAX DEPARTMENT

1. Cabinet Approval for Perspective Plan : Expenditure Sanction of Rs. 251.56 crore was accorded by the Cabinet in December, 2002 for third Phase of Computerisation Plan of the Income Tax Department with a view to ensure faster processing of returns and refund claims which could enhance taxpayer satisfaction; introduce higher transparency and free part of the manpower of ITD for investigation purposes; matching of financial information, collected from other sources across the country, with the information in returns of income.
2. Scope of Perspective Plan : Briefly stated, the Plan comprised of procurement, installation and commissioning of:
 - (a) High end Servers for National Computer Centre and 16 Regional Computer Centres proposed to be set up on consolidation of 36 existing Centres,
 - (b) Networking of Income Tax offices in remaining 440 cities as also additional points in the 60 cities covered in earlier two phases,
 - (c) Migration of application software, and
 - (d) Personal Computers for officers and staff.
3. Constitution of an Empowered Committee : For speedier implementation of the Perspective Plan for computerization (Phase III) in the Income-Tax Department and related activities, an Empowered Committee was constituted under the Chairmanship of Advisor to the Finance Minister on 31.7.03 with the approval of Finance Minister.
4. Enhanced functional requirements: The Empowered Committee took note of the additional functional requirements emanating from Budget Speech 2003, Finance Act 2003 and Finance (No. 2) Act 2004 relating to:
 - Compulsory e-filing of TDS returns by Corporate and Government deductors
 - Setting up of Tax Information Network (TIN) of following databases—

- On Line Tax Accounting System (OLTAS)
 - Dematerialisation of TDS certificates, and
 - Annual Information Return (AIR) of high value financial transactions
 - Processing of all returns of income within 4 months of filing
 - Direct credit of refunds through electronic clearance system
 - Computer assisted selection of cases for scrutiny
 - e-filing of returns of income
5. *Appointment of Project Consultants* : In its first meeting held on 04.08.2003, the Empowered Committee decided to appoint a Project Consultant for consultancy in implementation of Perspective Plan. Thereafter, in November, 2003, with the of Empowered Committee in its meeting of 19.10.2003, M/s Ernst & Young – NSE.iT Consortium were appointed as the Project Consultants for implementation of Perspective Plan.
6. *Change in technology architecture* : In the meeting of Empowered Committee held on 28.02.2004, the Committee discussed the reports on consolidation of RCCs (Regional Computer Centres) submitted by the Project Consultants. The Committee noted that country-wide matching of large volumes of data needed for widening and deepening of tax base will be very difficult in the regionally distributed database architecture. Instead a single national database with centralised architecture will be needed which will also give following functional advantages to the Department:
- “Anytime–anywhere” computing facilities enabling jurisdiction-free filing of returns of income and their centralised mass processing
 - All-India matching of data through Data Warehousing and Business Intelligence solution for computerised selection of cases and for detecting tax evasion
 - Centralised on-line availability of statistical reports

In view of the operational advantages, the Committee decided that instead of the 16 Regional Computer Centres proposed in the Original

Plan, a consolidated Single National Database should be set up with a National Data Centre (NDC) at Delhi, Business Continuity Planning (BCP) site at Mumbai, and Disaster Recovery (DR) site at Chennai with sufficient safeguards for data security. This impacted the technology architecture of Servers and Network proposed in the original approved Plan.

7. *Implementation methodology* : Considering the long term Information Technology infrastructure requirements of the department, limited availability of technical manpower and industry best practices for implementation of such large projects the Empowered Committee decided that—

- Network linking Income tax offices in all cities (number of such cities had increased from 488 to 510) should be set up on Build-Own-Operate (B-O-O) model
- NDC, BCP and DR sites should be set up in professional data centres hired for 5 years, through a System Integrator who should be responsible for their integration with the Network and the application software and management for 5 years
- Systems Integrator should also provide Facilities Management Services

8. *Cabinet approval for additional financial sanction*

8.1 In the Original Plan the network was based on old technology model of purchase of networking equipment by Department, hiring of leased data circuits from BSNL and their integration departmentally. While taking the expenditure approval of the Government for Networking, the Department was advised to seek fresh Cabinet approval of the revised Technology Model and consequential additional financial requirements.

8.2 The additional functional requirements of single national database and change in implementation methodology *viz.* outsourced service model for management of National Data Centre, BCP and DR facilities for 5 years and B-O-O model for setting up and running the Network for 5 years, had resulted in inclusion of running expenses (included in Original Plan on actual) in the overall cost.

8.3 The proposal for additional financial sanction was approved by the Committee of Secretaries on Non-Plan Expenditure (CNE) in its meeting on 11.05.2005.

8.4. Approval of the Cabinet, for additional expenditure sanction of Rs. 442.03 crore over 5 years in addition to the sanction of Rs.251.56 crore granted earlier, was accorded in June, 2005.

9. *Current status of implementation* – A chart showing current status of implementation is as follows:—

Comprehensive Computerisation of Income Tax System

List of Mile-Stones

Action Points	Objective to be achieved	Status as on 31.3.06	Remarks
1	2	3	4
1. E-delivery of taxpayer services			
1.1	Dissemination of tax information through web	Enabling taxpayers to obtain up to date information relating to taxation laws, forms, challans etc. through internet	Completed Department's website www.incometaxindia.gov.in setup and updated regularly. Average 4 lakh Visitors per day.
1.2	Dissemination of taxpayer specific information through web		
	Know your PAN	Facility to ascertain PAN on internet	Completed Facility provided on the website http://incometaxindiaefiling.gov.in
	Blank challans with preprinted PAN	Facility to download preprinted Challans with name address and PAN/TAN	Completed Facility provided on the website http://incometaxindiaefiling.gov.in
	View of tax paid in banks	Facility to verify tax payment on internet	Completed Facility provided on NSDL website http://tin-nsdl.co.in
	View of tax deducted at source	Facility to access ledger account of prepaid taxes on internet	Functional Dependent on demat of TDS certificates.
1.3	PAN and TAN related services	To ensure issue of PAN Cards within 15 days	Allotment during F.Y. 2005-06 PAN = 58,98,470 TAN = 4,64,745
	i/ Online filing of PAN application	Providing facility for online filing of PAN applications on internet	Completed PAN applications can be filed online at http://tin-nsdl.co.in or http://utiisl.co.in
	ii/ Web Tracking of status of PAN applications	Providing online access to taxpayers to ascertain status of PAN applications.	Completed Status of PAN applications can be tracked respectively at http://tin-nsdl.co.in or http://utiisl.co.in
	iii/ PAN grievance handling with Call centre support	E-filing of PAN grievances, their monitoring, tracking and redressal	Completed Call centre setup on pilot basis.

	1	2	3	4
	iv/ "Tatkal" allotment of PAN	On line filing of PAN applications, payment by credit card, and intimation on e-mail in 5 days	Completed	Facility provided on the website at http://tin-nsdl.co.in
1.4	i/ Simplification of return of income	To simplify and reduce the form of returns of income to one page	Completed	Returns form for salaried and other non-corporate taxpayers simplified. Naya Saral (Form 2E) is a simple one page return form for salaried taxpayers.
	ii/ Preparation of returns of income	Return Preparation Software enabling preparation of return of income through a simple question-answer based software	Completed	Sampark software released.
1.5	Electronic filing of returns	Simplifying and reducing the interface between taxpayer and the Department at the stage of filing of return of income.	Functional on pilot basis in 60 cities	About 42000 Returns for Assessment Years 2005-06 filed from July, 2005 onwards.
1.6	e-payment of taxes	Facility for payment of taxes through internet	Completed	Tax can be paid through internet banking.
1.7	Faster processing of returns of income/ refunds on computers	Computerised processing of returns of income within four months	Functional in 60 cities on network. In remaining cities being done on stand alone computers	Over 2.03 crore returns processed on computers in F.Y.05-06.
1.8	Issue of refunds through electronic clearance scheme	Direct credit of refunds to the bank account of taxpayers opting for this scheme.	Pilot scheme launched in 12 cities	Scheme available to salaried taxpayers for refund upto Rs. 25,000.
1.9	Computer assisted selection of cases for scrutiny	Computerised selection of cases for scrutiny on non-discretionary, transparency, intelligent criteria.	Completed	Facility for computerized selection provided to Assessing Officers in 60 cities on network.
1.10	Redesigning of TDS returns	To simplify and integrate 16 TDS return forms for lowering cost of compliance.	Completed	New TDS return Forms No. 24, 26 & 27 have been notified.
	Electronic filing of TDS returns	Computerisation of TDS returns of corporate deductors	Completed	TDS returns of corporate and Government deductors being filed on electronic medium only.
1.11	Grievance filing mechanism	Facility for e-filing of grievances	Software completed, testing in progress.	

	1	2	3	4
2. Augmentation of computer infrastructure within Department				
2.1	Providing PCs to all users	Supply, installation of high end PCs to all users required to work on network	Completed	More than 8,800 PCs have been provided to Departmental Users.
2.2	Migration of application software	Migration of application software to 3-tier architecture for consolidation of 36 regional databases into single national database	Target date- 31.12.05 Migration completed Acceptance testing in progress.	Dependent upon setting up of National Data Centre.
2.3	Linking Income tax offices in 510 cities to single national database	To set up an All India Virtual Private Network linking over 12000 users in 745 buildings in 510 cities to National data centre housing single national database	Target date- 31.1.06 Work awarded. Networking completed in 430 of 510 cities; work in remaining cities in progress	Expected to be completed by 31.05.06.
2.4	Setting up National Data Centre with Business Continuity/ Disaster Recovery sites	Providing computing, data storage, security facilities and related functionalities for enhanced requirement of 12000 departmental users working on single national database	Target date- 30.6.06 Technology solution finalised. Bids received. Technical evaluation under progress	Delayed Expected to be completed by 30.09.06 .

MINUTES OF THE TWENTY-FIRST SITTING OF STANDING
COMMITTEE ON FINANCE

The Committee sat on Tuesday, 18th April, 2006 from 1030 to
1315 hrs. and 1430 to 1630 hrs.

PRESENT

Maj. Gen. (Retd.) B.C. Khanduri - *Chairman*

MEMBERS

Lok Sabha

2. Shri Bhartruhari Mehtab
3. Shri Madhusudan Mistry
4. Shri Shriniwas D. Patil
5. Shri M.A. Kharabela Swain
6. Shri Vijoy Krishna

Rajya Sabha

7. Shri Chittabrata Majumdar
8. Shri Mangani Lal Mandal
9. Shri Santosh Bagrodia

SECRETARIAT

1. Dr. Smt. P.K. Sandhu — *Additional Secretary*
2. Shri A. Mukhopadhyay — *Joint Secretary*
3. Shri S.B. Arora — *Deputy Secretary*
4. Shri T.G. Chandrasekhar — *Under Secretary*
5. Smt. Anita B. Panda — *Under Secretary*

Part – I
(1030 to 1315 hrs.)

WITNESSES

Ministry of Finance

Department of Revenue

1. Shri K.M. Chandrasekhar, Secretary (Revenue)
2. Shri K. Mohandas, Additional Secretary (Revenue)

3. Shri M.C. Singhi, Economic Adviser
4. Shri K.L. Prasad, Additional Economic Adviser

Central Board of Excise and Customs (CBEC)

1. Shri M. Jayaraman, Chairman (EC)
2. Shri V.P. Singh, Member (CX)
3. Shri Kailash Sethi, Member (L&J/ST)
4. Ms. Chitra Saha, Member (P&V/Budget)
5. Shri A.P. Sudhir, Member (Cus)
6. Shri S.P.S. Pundhir, DG(Audit)
7. Shri V. Sridhar, DG (Systems)
8. Shri A.K. Raha, DG (Central Excise Intelligence)
9. Shri A.P. Kala, DG (Revenue Intelligence)
10. Shri K.N. Gupta, Chief Commissioner (TAR)
11. Shri Gautam Ray, Joint Secretary (TRU-I)
12. Shri R. Sekar, Joint Secretary (TRU-II)
13. Ms. Sheila Sangwan, Joint Secretary (Review)
14. Shri P.K. Mohanty, Joint Secretary (Drawback)
15. Ms. Kameswari Subramanian, Joint Secretary (Customs)
16. Shri Deepak Khandekar, Joint Secretary (Admn.)
17. Shri P.S. Pruthi, Commissioner (Customs)
18. Shri Gautam Bhattacharya, Commissioner (ST)
19. Shri Praveen Jain, Commissioner (DOPM)
20. Shri N.K. Bhujabal, Commissioner (RI&I)
21. Shri M. Deena Dayalan, JS&FA (F)

Central Board of Direct Taxes (CBDT)

1. Ms. M.H. Kherawala, Chairperson
2. Ms. Baljeet Matiyani, Member
3. Shri Arun Bhargava, Member (R)
4. Shri J.G. Pendse, Member (Inv.)
5. Shri S.S. Gandhi, DG (Systems)
6. Ms. Anita Kapur, JS(TPL-I)
7. Shri Arbid Modi, JS(TPL-II)
8. Shri S.S. Khan, DIT (Systems)

2. At the outset, the Chairman welcomed the representatives of the Ministry of Finance (Department of Revenue) to the sitting of the Committee and invited their attention to the provisions contained in direction 55 of the Directions by the Speaker.

3. The Committee then took oral evidence of representatives of the Ministry of Finance (Department of Revenue) on issues arising out of Budget Proposals (2006-07) of the Ministry of Finance (Department of Revenue) and other related matters.

4. Thereafter, the Chairman requested the representatives of Ministry of Finance (Department of Revenue) to furnish notes on certain points raised by the Members to which replies were not readily available with them during the discussion.

5. The evidence was concluded.

6. A verbatim record of proceedings has been kept.

The witnesses then withdrew.

The Committee then adjourned.

MINUTES OF THE TWENTY-SIXTH SITTING OF STANDING
COMMITTEE ON FINANCE

The Committee sat on Wednesday, 19 May, 2006 from 0930 to
1030 hrs.

PRESENT

Maj. Gen (Retd.) B.C. Khanduri - *Chairman*

MEMBERS

Lok Sabha

2. Shri Bhartruhari Mahtab
3. Dr. Rajesh Kumar Mishra
4. Shri Madhusudan Mistry
5. Shri Rupchand Pal
6. Shri Jyotiraditya Madhavrao Scindia
7. Shri M.A. Kharabela Swain
8. Shri Vijoy Krishna

Rajya Sabha

9. Shri S.P.M. Syed Khan
10. Shri Santosh Bagrodia

SECRETARIAT

1. Dr.(Smt.) P.K. Sandhu — *Additional Secretary*
2. Shri A. Mukhopadhyay — *Joint Secretary*
3. Shri S.B. Arora — *Deputy Secretary*
4. Shri T.G. Chandrasekhar — *Under Secretary*
5. Smt. Anita B. Panda — *Under Secretary*

2. At the outset, the Chairman welcomed the Members to the
sitting of the Committee.

3. ** ** ** **

4. The Committee then took for consideration draft Reports on the Demands for Grants (2006-07) of the following Ministries/Departments and adopted the same subject to the modification as shown in Annexure-I in respect of the draft Report at Sl. No. (v) :—

(i)	Ministry of Finance (Department of Revenue)			
(ii)	**	**	**	**
(iii)	**	**	**	**
(iv)	**	**	**	**
(v)	**	**	**	**

5. The Committee authorised the Chairman to finalise the Reports in the light of modification as also to make verbal and other consequential changes arising out of the factual verification and present the same to both the Houses of Parliament.

The Committee then adjourned.

STATEMENT OF CONCLUSIONS/RECOMMENDATIONS OF
THE STANDING COMMITTEE ON FINANCE IN THE
THIRTY-SEVENTH REPORT

Sl.No.	Para No.	Conclusions/Recommendations
1	2	3
1.	18 & 19	<p>The Committee are perturbed to find that bogus income-tax returns claiming large amounts of refunds on the basis of bogus TDS certificates were filed by some unscrupulous persons. The point of serious concern is the forgery committed by the tax officials themselves who connived with these persons, resulting in such fraudulent issue of refunds. The Committee feel that this is an ample proof of the extent of corruption in the tax machinery which could have been avoided, had the internal vigilance mechanism of the Department been more alert. In the Committee's view, lack of efficiency and integrity in the tax machinery leads not only to leakage of tax revenue but also to tax evasion. Although the Department has stated to have issued instructions/circulars to the field formations, yet the fact cannot be ignored that this has been done only after receiving Reserve Bank of India (RBI)'s communication pointing towards irregularities in the issue of refund orders. The Committee note that the system of issue of refunds is going to be streamlined by making ECS applicable for all refunds in future, making it mandatory to quote the assessee's bank account details in the refund orders and immediate reporting of any loss/theft of refund orders to the higher authorities, the clearing bank and the police etc. However, the Committee are constrained to observe that corrupt officials succumbing to avarice has become bane of Income Tax Department. Further, there has been a systemic failure in</p>

the form of lack of proper checks and balances and a deficient supervision by the senior officials and the internal vigilance mechanism on such officials. The Committee take strong exception to such failures in the Department and desire the Government to furnish complete details of the extent of such fraud in terms of revenue loss and the penal action taken against the tax officials found to be involved. The Committee also recommend that the instructions of the Department on issue of refunds should be followed scrupulously and diligently with supervision at senior level in all their field formations.

Another disquieting feature about issue of refunds as noted by the Committee has been the inordinate delays in the issue of refunds. The Committee find that though there are administrative instructions to issue refunds within a period of four months, there have been several cases of delays. The Committee advise the Government to go into the discrepancies that have been stated to delay issue of refunds and take necessary action so that such instances do not recur.

2. 40, 41, 42 & 43 Taking a serious view of the recurring trend of huge pendency of arrears, the Committee had, in their 33rd Report (14th Lok Sabha) desired the Government to take concerted efforts to reduce such arrears. Although the Government are stated to have taken measures to recover the arrears, there has been hardly any substantial increase in the collection of arrears over the years. It is evident from the fact that as on 31.1.2006 the outstanding arrears demand in direct taxes amounts to a whopping Rs. 84662 Crore (approx.) and in indirect taxes, it is around Rs. 21,368.11 crore. The Committee would also like to particularly point out that majority of the arrears are pending to be

recovered from the two cities of Mumbai and Delhi. The Committee find that an amount of Rs. 35000/- crore in Mumbai alone is outstanding against stock-scam related cases of Harshad Mehta Group and Ketan Parekh Group, and are stated to be at the initial stages either at the first appellate authority or the Tribunal. No serious efforts seem to have been made to get the cases decided early. From this, the Committee are led to conclude that recovery of arrears is moving at a painfully low pace. The Committee hope that at last now the Government would make concerted efforts to realise the arrears with due despatch.

In so far as indirect taxes are concerned, the Committee note that as on 31.1.2006, out of the total outstanding arrears of Rs. 21,368.11 crore the unstayed arrears demand is around Rs. 14236.6 crore. From the information furnished to them, the Committee also note that the targets of recovery of arrears are being reduced over the years in both Central Excise and Customs. Moreover, the targets of recovery fixed for 2006-07 is even below than the recoverable amount. In this connection, the Committee have been given to understand that a task force has been constituted to expedite the realisation of arrears with certain specific measures e.g. sensitization at the level of Commissioners/Chief Commissioners etc., filing application for vacation of stay orders etc. Though the Committee feel that this is a step in the right direction, yet in their view, as the adjudication of cases attribute, to a great extent, to realise the arrears, they are of the opinion that the Government may examine fixing a time-limit to expedite the adjudication procedure.

The Committee note that one of the major reasons for concluding certain portion of arrears

as 'non-recoverable' is that the assesseees are not traceable. In this backdrop, the Committee recommend the Government to further strengthen their institutional and procedural safeguards so that traceability of assesseees could be managed well and revenue due to the Government could be recovered.

The Committee are given to understand that a sizeable number of cases are either pending with IT authorities/Appellate Tribunals/Courts or the demands have been stayed by them. The Committee while expecting that cases pending before IT authorities would be disposed of expeditiously, desire to either get the stays vacated as early as possible or persuade the Tribunal not to allow stays beyond 180 days as provided under Section 254 (2A) of Income Tax Act, 1961. In so far as the huge pendency of recovery cases at the level of Tribunal/courts is concerned, the Committee note that there exists an institutional mechanism through which the Revenue Secretary can interact the Law Secretary on bi-monthly basis to discuss the matter. However, going by the past record of pendency, the Committee are of the opinion that this mechanism, perhaps, has not been utilised fully. The Committee urge the Government to optimally utilise this mechanism to expedite the disposal of cases and thereby increase the realisation of tax arrears. They desire to be apprised of the outcome of such meetings on a regular basis.

3. 61 & 62

The matter concerning exemptions given both under direct and indirect taxes had engaged the attention of the Committee earlier also. The Committee, in their Thirty-Third Report (14th Lok Sabha) had recommended, *inter alia* that since prolonged continuance of exemptions may turn detrimental to the economy as they deplete

considerable portion of tax base, leave tremendous scope for evading tax and prompt people to resort to unwarranted tax planning, there is a need for urgently withdrawing the exemption provision under the tax laws or reducing the list of exemptions and rationalising the same. The Committee are in total agreement with the observation made by the Rustogi Committee that exemptions cause distortions, are prone to misuse and not always easy to implement. The Committee appreciate that the Government have taken right steps in this direction by withdrawing quite a few exemptions which are no longer justified. The Committee would further consider it to be a necessary and beneficial exercise to conduct a cost-benefit analysis on the tax exemptions, which would enhance the credibility of either extending or withdrawing an exemption. Therefore, the Committee recommend that a comprehensive exercise may be conducted by the Government to analyse the cost-benefit ratio on all the existing tax exemptions.

The Committee in their Thirty-Third report had also conveyed their apprehension on the possible misuse of exemptions provisions by research institutions. They note that the Government have now formed a Committee of Secretaries to review existing incentives for scientific research, including research and development in the pharmaceutical industry. The Committee hope that the review would be completed in a time bound manner and the Government would strive its best to consider and implement the recommendations at the earliest so as to prevent the misuse of exemption provisions to the extent possible. The Committee would like to be apprised of the position in this regard.

1	2	3
4.	75	<p>The Committee observe that restructuring of the department under the Central Board of Direct Taxes (CBDT) and Central Board of Excise & Customs (CBEC) had been undertaken resulting in perceptible difference in the performance of the departments. However, the Committee have been told on many occasions that shortage of manpower, particularly at the level of Inspectors etc. is affecting the efficiency of the tax departments. In this regard, from the data submitted to them by the Government, the Committee note that the restructuring process in CBDT has resulted in an increase of 222.22% of the posts of Chief Commissioner but a rather poor 17.07% augmentation at the level of inspectors. In CBEC, the posts of Chief Commissioner have been increased by 123.80% and at the level of Inspector, there has been a decrease of 14.32%. This exercise, in the Committee's view, has made the top slots heavy, and negligible or even negative growth in the number of posts at the cutting edge levels like that of Inspectors, Income Tax Officers, Superintendents and Custom Appraisers. This, the Committee feel, may further worsen the much-felt shortage of work force at these levels leading to serious problems in the overall functioning of the two departments. The Committee note that the Government have now started taking measures to fill up these gaps. Nevertheless, the Committee are led to the conclusion that the restructuring proposal was done in a manner, that chose to ignore the requirements at the middle and lower level of the functionaries, resulting in continuation of shortage of manpower. The Committee, therefore, recommend the Government to again assess the present structure of the department under both the Boards carefully and set right the anomalies that have crept up as a result of restructuring.</p>

1	2	3
5.	91, 92, 93, 94 & 95	<p>The Committee observe that so far as the computerization projects taken up by the Central Board of Direct Taxes are concerned, implementation of many small projects that would enhance the effective functioning of the department like computerized processing and country-wide matching of TDS claims, matching of data compiled in the Annual Information Returns (AIRs) with that of tax returns etc. depend to a large extent, on the completion of the creation of a single National database. They note that as per the original target, the database was to be completed by June, 2006. However, the target date for completion has now been shifted to September, 2006. The Committee are of the strong view that the Government should take all-out efforts to complete the project within the rescheduled target i.e, by September 2006 to reap the designated benefits that would accrue from the database. Further, the Committee feel that there exists a gap between the information obtained through Annual Information Report (AIR), which is fully computerized, and the information coming from returns of income, which is partly computerized. The Government have assured that the gap would be filled and they will be able to complete all processing, data matching and selection of cases for scrutiny on computers by the end of the current financial year i.e. 2006-07. The Committee expect that the whole process will be completed within the stated time at least now. Further, the Government have stated that the work relating to appointment of system integrator is still at the stage of evaluation of technical bids. The Committee urge the Government to expedite the process without further delay so that this should not adversely affect the project.</p> <p>In so far as the overall computerisation of the Department is concerned, the Committee were</p>

given to understand that expenditure sanction for the third phase of Computerisation Plan of the Income Tax Department was approved by the Cabinet way back in December, 2002. The plan had included networking of I.T offices in remaining 440 cities out of the proposed 510 cities. The original target date for the same was 31.01.2006. The Committee further note that the Department sought fresh sanction for additional requirements from the Committee of Secretaries on Non-plan Expenditure on 11.5.2005. In the Committee's view, the pace of work with respect to computerisation project has been slow. Despite urging the Government to expedite the various computerisation projects repeatedly in their earlier reports and the assurances given by them that it would be completed in time, the Committee are dismayed to note that certain components of the project like linking of cities under a single national database and setting up National Data Centre are yet to be completed. The Committee note that as per the revised schedule, the dates of completion of the above two components of Phase-III of the computerisation projects are 31.05.2006 and 30.09.2006 respectively. The Committee hope that the Government will not extend the date furthermore and take all out efforts to complete the project as per the revised schedule.

The Committee note that so far as the computerisation projects under the Central Board of Excise and Customs (CBEC) are concerned, the Government have taken the stand that some of those are under implementation and some others are in the proposal and testing stages—the important ones being the creation of a National Level Data Centre, Automation of Central Excise and Service Tax (ACES), Risk Management System

(RMS) and Electronic Accounting system in Excise and Service Tax (EASIEST). The Committee recommend that all the projects under implementation as well as under consideration should be followed up by the Government in the right earnest so as to avoid avoidable delay in their implementation.

The Committee further note that roughly eighty per cent of the international trade is covered under the Customs' EDI system and over ninety per cent of the documents are processed electronically in these stations. The Committee urge the Government to increase this coverage to hundred percent at the earliest. They observe that once the work relating to automated workflow system of central excise assessment as well as service tax assessment is completed, it would be possible for the Department to provide quality service to the tax-payers. Also, the Government are expected to roll out the Risk Management System (RMS) to major ports like Chennai, Delhi, Kolkata, etc., with the aim to cover all the major locations by June 2006. In this background, the Committee expect the Government to show tangible results in the near future.

The Committee note with concern that irrespective of the assurance given by the Government to furnish the White Paper on 'Information Technology in Tax Administration' the said 'White Paper' has not been furnished so far. They expect the Government to do the same immediately.

6. 110 & 111

The Committee take note of the fact that the extent of spot recovery of service tax—which works out to 66% of the total service tax evaded, as a result of detection of evasion of the tax by the Directorate General of Central Excise Intelligence (DGCEI) is a cause for

serious concern, as it reveals the extent to which service tax evasion exists in the system. The trend shows that there is hardly any fear of detection and punishment in the minds of service providers, which the Committee feel, is the result of the lighter punishment that is meted out to the offenders. Even if the fact remains that the Government is being cautious, as Service Tax is a relatively new concept, the Committee feel that having no legal provision that provides for conviction for such evaders will prove to be detrimental at a later stage. The Committee also take note of the fact that on the contrary, the law provides for an escape route in the sense that if the evader deposits 25% of the tax evaded in addition to the total tax to be paid, he is let free without any further action against him.

Further still, the minimum penalty fixed, if such a case reaches the adjudication level, is also fixed at 25% of the tax due. The Committee, taking the above into consideration, recommend the Government to bring in the necessary legal changes early for enabling conviction of the tax offenders as well as increase the rate of survey and searches in order to inculcate a sense of fear among the tax evaders.
