

# **Leadership, Decision Making and Crisis Management in Indirect Taxation in India - Lessons learned overseas for implementation in India**

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## *Introduction*

1. In this era of globalisation, opening of borders leading to intense competition; uncertainty of predictability in geographical, economic, political arena, etc; the concepts of leadership, decision-making and crisis management have become the key to any country, organisation or system. Taxation has been the main pillar of every state/Kingdom since early years to ensure development and achieve social goals. Taxation and Expenditure policies follow economic and social principles. Taxation Administration plays a very important role in garnering revenue for the state and any crisis in its administration or collection can have very serious impact upon the economy of the State. India is on the threshold of introducing the biggest ever indirect tax reforms in the near future. Similar such tax reforms have already been implemented in Canada, Brazil, EU, etc. As such, understanding the complexity and underlying issues of such tax reform, the experience gained overseas would be useful to the leaders and others in India, so as to enable them to take appropriate decisions and manage crisis if so arise.

## *Leadership, decision-making and crisis management:*

2. Briefly, leadership can be defined as the ability to inspire confidence and support the people who are needed to achieve organizational goals. Leadership qualities are not only required among people at the higher levels, but at all levels in an organization. Some of the basic ingredients of effective leadership are awareness, ability, commitment, vision, integrity, passion, trust, Charisma, etc. Another important issue connected with leadership is decision-making. It is the ability of persons of any organisation to take appropriate decision at the right time keeping into consideration the best interest of the organisation or country. Inappropriate decisions or delayed decisions can seriously harm the prospects of any organisation; which may lead to creation of crisis, and hence its management becomes most important. Crisis situations threaten core values of the organisation and in such situations, organisational leaders often have an incomplete understanding of the origin and the risk and an understanding of the impact<sup>1</sup>. In a crisis, there is a finite time in which decision-makers are able to respond to the situation- “window of opportunity” to act. While some crisis cannot be avoided (like earthquake, tsunami, etc); yet, other type of crises arising out of delayed decision-making or faulty leadership can be avoided by taking preventive measures. The handling of crisis can be done in the following manner:

- a. Accurate risk assessment: by this process, the risk is assessed in a systematic manner, identifying and evaluating events that could affect the achievement of objectives. A standard risk assessment matrix may be prepared keeping into consideration likely impact of the consequences after doing requisite prioritization.
- b. Decision regarding investment on prevention or resiliency

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<sup>1</sup> Crisis Management, Bruce W Dayton, OUP, 2009

- c. Accurately framing the situation
  - d. Deploying right people at right places
  - e. Effective communication amongst all deployed to manage crisis
  - f. Learning to face similar issue in future. It could be cognitive shift or behavioural shift, or it may require an institutional framework.
3. The leadership and decision-making structure of indirect taxes in India is as under:

### **Leadership and Decision Making Structure of Indirect Tax**



*Scale of operations in India- Present situation*

4. Department of Revenue and CBEC are engaged in policy formulation relating to indirect taxation and border control. Field officers implement the policies formulated and their job can be broadly classified into two main categories, namely assessment and collection of revenue from Central Excise, Customs and Service tax, and border control. India has land border of 15,200 km and coastline of 7517 km. The role of Customs, falling under indirect Administration has also become important in view of the fact that the country is located between two largest narcotics drugs producing areas in the world, namely, *Golden Crescent* and *Golden Triangle*. Further, because of geopolitical reasons in the area, border controls have to be effectively exercised to ensure that anti-national elements do not enter into the country and carry out terrorist or any activities which can have serious impact upon the economy of the country. The country has witnessed nefarious act of the terrorists, trained in the neighbouring country and killing innocent civilians and causing damage on 26/11.

5. The scale of operations of CBEC and its offices in respect of assessment, collection of revenue; enforcement, etc have been collected from different sources and are tabulated below : ( Surprising, the official website [www.cbec.gov.in](http://www.cbec.gov.in) did not contain much of such information about mandate, jurisdiction, area of operations, collection of revenue in different years, volume of work undertaken, arrears of revenue, etc. This was incidentally demonstrated in US by Ms Inves )

Table 1: Technical Data ( 2014-15)

Total Indirect Tax	Rs 5,48,800 Cr
Central Excise Duty	Rs 1,88,000 Cr
Customs Duty	Rs 1,82,000 Cr
Service Tax	Rs 1,68,000 Cr
Central Excise Base	3.58 Lakhs
Service tax Base	22.12 Lakhs
Bills of Entries/ Shipping Bills	33.25lakhs/ 61.85 Lakhs
Arrears of Revenue and Cases	Rs 1,55, 300 Cr/ 12.2 Lakhs

Table 2: Border control Data

Land Border	15200 Kms
Coastal Line	7517 Kms

Table 3: Administrative data<sup>2</sup>

Sanctioned Posts	84875
Customs Zones	11
Central Excise Zones	23
ST Zones	4
Directorates	20
Customs Commissionerates	60
Central Excise Commissionerates	119
ST Commissionerates	22
Audit Commissionerates	45

<sup>2</sup> CBEC letter A11019/08/2013-AdIVdated 1.8.2014

LTU	8
Appeals	60
Cost of collection	.77%

6. Presently, Central Excise duties and Service Tax are collected separately. However, the facility of Cenvat Credit has been extended across both Central Excise and Service Tax as well as to the CVD component of Customs duty. There are significant number of taxpayers of Central Excise and Service Tax covering a very large proportion of the tax paying population in the large and medium sectors. Introduction of ACES for mandatory filing of *e-returns, e-payment of taxes, online registration* etc has minimised the interface between the department and the tax payer. However, their process is not yet comprehensive and an active interface exists where there are short/excess payments, demands, refunds etc. Audit is only partially computerised and significant work remains to be done; presumably put on hold to build in the GST interface simultaneously.

7. Majority of the customs duty is collected by Customs zone of Mumbai, Chennai, Ahmedabad, Delhi, etc. Though the dwell time attributed to customs has reduced in the recent times because of automation, PCRA and RMS, yet, methods of examination continued to remain obsolete because of lack of modern technology like scanners, analysers, etc. Further, significant number of land customs stations have been made operational along the land border where modern means of examination and assessment are grossly inadequate. These are areas prone for not only under assessment/evasion of duty, but also smuggling of drugs, arms, ammunitions, fake currency, etc.

8. Department has carried out large-scale cadre restructuring in 2014, creating new layers of officers and staff at different levels, with a view to meet the demand of increased workload and to have an effective border control. However, despite lapse of one year of approval of cadre restructuring, significant number of posts, especially at the top and the cutting edge levels have remained unfilled leading to the demoralization of the service.

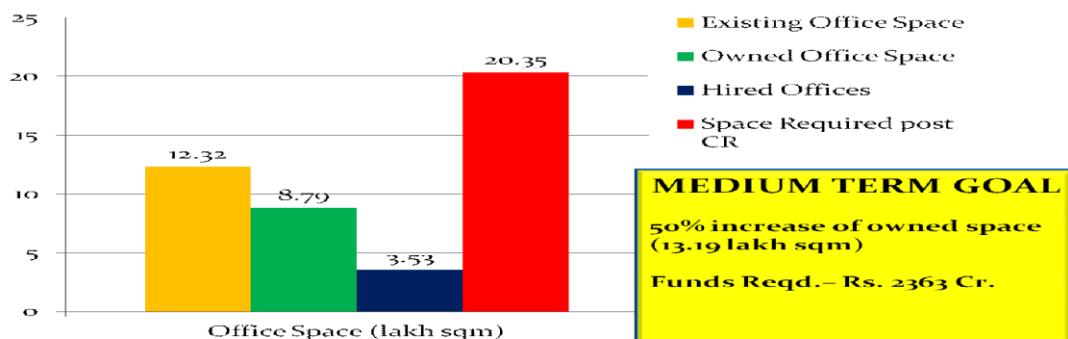
9. Cost of collection of .77% of the total revenue collection is one of the lowest for any organisation in the country. The cost of collection in the USA and Canada are 0.95 to 0.97%<sup>3</sup> respectively. Low cost of collection has severely restricted availability of funds with the Department, which in turn, has met the Department grossly lacking requisite infrastructure, not just in the form of buildings, vehicles, et cetera, but , in other important operational related infrastructures like scanners, non -intrusive methods of examination /inspection, surveillance, etc. This not only affects the efficiency and efficacy of the system and officers but morale of the officers and staff also. A large

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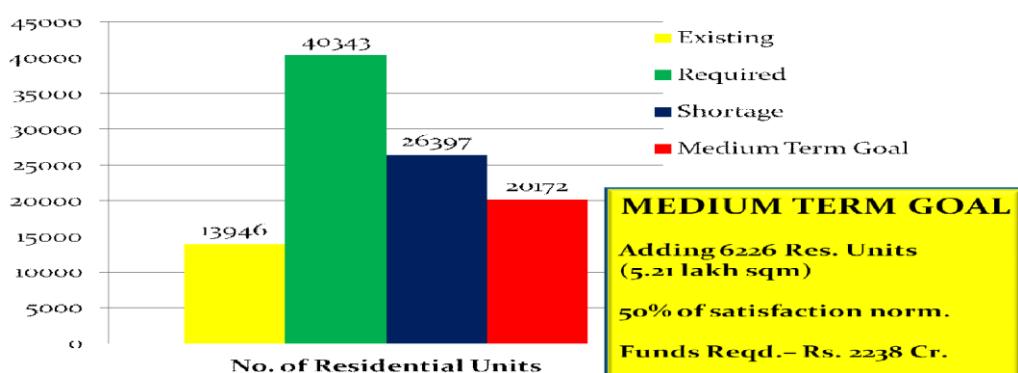
number of offices do not have requisite space and are grossly lacking in Modernisation and innovation. It is evident from the following graph;

#### Infrastructure- Office Space<sup>4</sup>



#### Infrastructure- Residential Space<sup>5</sup>

As against 22.4% in India



10. Though the cost of collection is among the lowest in the world, 0.77%, as against 0.95% and 0.97% respectively for US and Canada, the size of government is also much smaller ( India 01.89%, US 19.75%, Canada 19.82%) and the estimated size of the informal sector is consequently much larger (Between 7-13% for the developed world as against 22.5% of the GDP for India), clearly establishing the fact that cost cutting at this level is counterproductive insofar as the overall health of the economy is concerned.

11. Though, Department has gone for automation in assessment, filing of returns, document, etc, yet, the satisfaction of the customer is far from satisfactory, especially in excise and service tax arena. While the departmental IT system is working satisfactorily in Customs side, the taxpayers have to wait for inordinately long hours to file their returns and interact with the departmental computer system in the Central Excise and Service Tax area.

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<sup>4</sup> Presentation of DGHRD, August 2014

<sup>5</sup> DGHRD Presentation, August 2014

12. Litigation is another major concern of the Department. There is *revenue bias* in the mind of the officers and staff, which resulted into a large number of unsustainable cases being confirmed in favour of revenue. One of the reason for this *revenue bias* is the perceived fear from *vigilance and audit* for the possible vigilance action. It is perceived that once an independent decision is taken, likelihood of vigilance enquiry cannot be ruled out, which will go on for many years, affecting the career prospects of the officers and staff. Many a times, CBI have entered into *quasi-judicial* proceedings of the officers, doubting the adjudication orders passed in favour of the assessee. Although this is largely perceptual, this fear contributes to confirmation of significant number of cases, which otherwise could have been decided otherwise. The effect of recent circular attempting to allay these fears is yet to be seen<sup>6</sup>.

*Issues likely to convert into crisis:*

13. From the scale of the operations mentioned in the earlier paragraphs, several issues emerge, which may convert into crisis, if not handled effectively at appropriate time. These issues can be classified into two broad categories, namely, technical and human resource and infrastructural.

14. The technical issues, which can acquire the proportion of a major crisis include imminent switching over to GST, trade facilitation and enforcement, litigation and automation. Honourable Finance Minister has announced that the country would switch over to GST from April 2016<sup>7</sup>. This is the first major indirect tax reform, which is being attempted in India after independence. GST proposes to subsume various Central and State indirect taxes to be collected by Centre (CGST) and State (SGST). Many other countries like Canada, Brazil, European Union, etc have switched over to GST in last two decades and have faced early problems in its implementation, despite the fact that those countries had very few provinces. India has 29 states and seven union Territory with huge regional disparities, not only in economic terms, but political and geographical terms also. Considering the fact that Centre-State relations have always been a matter of concern in the past, effective implementation of GST would be greatly dependent upon the coordination between Centre and States. It also requires robust and reliable GST IT network for seamless transfer of huge credit of taxes from originating state to destination state. Besides that, clear understanding of procedure and methodology of GST need to be informed to not only the trade and other stakeholders, including officers of State and Centre. Undoubtedly implementation is going to be a big challenge not only at the policy level but at the implementation level also.

15. More and more thrust is being put on trade facilitation under the WCO<sup>8</sup>. Trade facilitation enable movement of persons, goods and services with least possible time at the border of the countries, which allow goods and services to be available at the most competitive price. With the

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<sup>6</sup> DGVigilance letter V 500/39/2015; April 2015

<sup>7</sup> Union Budget, 2015-16

<sup>8</sup> WTO Agreement of Trade Facilitation, December 2013

signing of many bilateral and multilateral trade agreements, the physical boundaries of the countries have lost significance and trade facilitation is indispensable. However, considering the geopolitical location of the country and likelihood of smuggling of narcotics and arms and ammunitions, effective border control need to be put in place by deploying state of the art equipment at the border post.

16. Similarly, major issues in the human resource area include demoralised service and a poorly managed cadre, skill development and capacity development, acute lack of infrastructure, leading to inefficiency and fear factor leading to inaction.

17. Various steps of handling the crisis has been mentioned in the earlier paragraphs. Keeping in consideration those parameters, the Department has to prepare itself to handle it. Following broad principle can be kept in mind by the leaders and all other stakeholders to face the crisis:

- a. To have the mind-set to be ever ready to face any situation leading to crisis
- b. Infusion of Machine, Material, Money and Manpower. Use of modern machines and material would enable the Department to have robust infrastructure and minimise the problems and/or would enable ease of governance, monitoring and trade facilitation.
- c. Adequate manpower to be deployed and provided skilled through capacity building on continuous basis.
- d. Allocation of adequate fund/money would enable Department to procure machine material and manpower
- e. As far as possible, decision making power be clearly defined and delegated at appropriate levels, so that, the situation of crisis does not arise for want of decision taking.

#### *International best practices*

18. After the visit of USA and Canada, and interaction with the experts on the field, the international best practices can be summarised as under:

##### *18.1 GST in Canada:*

Canada has 10 provinces and has implemented GST in 1991. Initial response of the Taxpayer to VAT has been negative. At least two general elections have been fought in past over the VAT. The federal Conservative government that introduced the GST was reduced from a majority government to just two seats in Parliament in the general election of 1993.<sup>9</sup> Indeed, the GST in its early years was the most heartily disliked tax in Canada<sup>10</sup>. The gradual move of provinces to VAT came about in three stages – the Quebec Sales Tax in 1991, the ‘first generation’ HST adopted by several provinces in

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<sup>9</sup> A useful brief account of the politics of introducing the GST in Canada may be found in Eccleston (2007).

<sup>10</sup> Richard Bird, 1994

1996, and the ‘*second generation*’ HST of the last few years.<sup>11</sup> Today, five provinces have their own VATs in the form of the federally administered Harmonized Sales Tax (HST) while Quebec administers its own VAT, the Quebec Sales Tax (QST). British Columbia became only the sixth jurisdiction in the world – and the first in the developed world-- to abolish a VAT once one was in place.<sup>12</sup> The Québec Sales Tax (QST) and the federal GST constitute an operational “*dual VAT*” system with essentially none of the problems usually associated with such systems.<sup>13</sup> The rates of the two taxes are set independently by the respective governments. The tax bases are also determined independently, although they are essentially the same. From the beginning, both taxes have been collected by a single administration -- that of the province. Taxes on interprovincial sales from one business to another are basically handled by a zero-rating deferred-payment) system similar to that now applied in the EU but under the protective umbrella of a uniform national VAT. Five provinces impose value added taxes HST on the same base as the federal GST. These provincial taxes are administered by the federal government and the revenues distributed to the provinces on the basis of estimated taxable consumption in each province. Interprovincial sales are in most cases taxed on a destination basis, with taxes collected by the federal government and allocated to provinces by a formula that mimics the destination basis. Three provinces continue to operate their RSTs alongside the federal GST. The two taxes are collected by separate administrations, and the existence of the federal GST has simply been ignored by these provinces.

### 18.2 *RST in USA*

USA is the only developed country in the world, which is collecting indirect tax through Retail Sale Tax and they are not planning to move to GST. The system of tax credit is also not adopted in the RST regime. USA collects majority of it's revenue from Income Tax, Corporate Tax, Pay Roll tax, Property Tax. These tax are collected at federal, state and county levels.

18.3 *Amalgamation of border control agencies in a single agency in USA:* After 9/11 incidence in USA, comprehensive review of various enforcement agencies was undertaken. All agencies entrusted with the task of border control like, Coast Guard, Immigration and Customs have been amalgamated to form *Department of Homeland Security*. With this, the lack of coordination amongst different agencies have been eliminated and there has not been, even a single case of terrorist attack.

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<sup>11</sup> The remainder of this section is based largely on Bird (2012) and Bird and Gendron (2010).

<sup>12</sup> Its predecessors in the retreat from the VAT were Belize, Ghana, Grenada, Malta, and Vietnam (Bird and Gendron 2007). All five countries have subsequently reintroduced the tax.

<sup>13</sup> For a brief comparison of alternative ways of imposing two-level VATs, see Bird (2013).

*18.4 Robust and reliable IT network, with user friendly software managed by professionals:*

IRS, USA and CRA (Canadian Revenue Authority) have placed great reliance upon their IT network in capturing various financial transaction in a comprehensive return to all stakeholders. It had enabled them to track the cases of evasion of tax and to take punitive action against offenders.

*18.5 Time bound disposal of disputes*

Certainty of finalisation of dispute within a reasonable time is one of the backbone of developing the faith of the taxpayer in the taxation system.

*18.6 Stability of taxation and rates*

This is one of the most important feature of any taxation system in the country. Stability of rates and taxation system strengthen the confidence of the taxpayers; which result in greater compliance and future planning. Frequent change in rates or revisiting the settled laws shaken the confidence of investors and taxpayers, seriously affecting the economic growth of the country.

*18.7 Deployment of modern technology at ports, border enforcement and trade facilitation*

Deployment of modern means of examination like container scanners, x-ray inspection systems, pallet scanners, mail scanners, body scanners, etc can facilitate faster movement of passengers and goods. Similarly, use of faster and reliable IT network for exchange of documents with all stakeholders would not only facilitate trade, but also ensure adequate border protection.

*18.8 Decentralise decision-making*

Decentralisation of decision-making with adequate safeguard would enabled faster decision-making at all level in IRS restructuring in USA.

*18.9 Adequacy of funds*

Revenue administration at both the USA and Canada have about 1% of revenue collected as funds allocated for modernisation and creation of infrastructure. This enable them to keep pace with the technology and also facilitate them to hire professionals with better perks to provide expertise in revenue collection mechanism.

*18.10 Periodic training and online skill development*

Continuous training, including online skill development is one of the important ingredient of capacity building of any organisation, including revenue.

### *18.11 Perform or perish*

IRS restructuring has successfully completed by retrenching deadwoods and non -performers<sup>14</sup>. Certainty of employment should be based upon certain performance based parameters. Any person found lacking in performing their duties to well-defined parameters should be retrenched, whereas the good performers need to be rewarded by way of promotion or better pay packets

### *18.12 Functional jurisdiction instead of territorial*

IRS, USA has reformed by resorting to jurisdictional based on functions rather than territory<sup>15</sup>. It has immensely helped them in curtailing various layers in the administration.

## *19. Recommendations:*

Based on the international experience and the present situation in India, the group makes following recommendations:

- a. All indirect tax collecting authority in the country should be consolidated to constitute only one authority, which shall be responsible for implementation of GST throughout India. This authorities should have independence of taking decisions relating to implementation within the policy guidelines decided by the government and should be provided with adequate fund.
- b. Proper legislative timeframe need to be prescribed for resolutions of tax disputes in fair manner following the judicial discipline. Mind-set of adjudicating authorities towards *revenue bias* need to be addressed by eliminating fear of *vigilance and audit*.
- c. Only one border control agency be constituted by the merger of Customs, Coast Guard and Immigration. Trade facilitation should be achieved by deployment of modern non- intrusive system of examination at all ports, airports, land customs stations; round-the-clock and use of IT network for automation for documentation and RMS, post -Clearance audit.
- d. A transparent, empowered and performance-based HR system should be put in place with proper grievance mechanism. It is important that morale of the workforce is boosted by provided them with training, requisite infrastructure and skill development.

## *20. Challenges to implementation of recommendations*

The implementation of recommendations can face bottlenecks or hurdles on account of the following factors;

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<sup>14</sup> Leadership and Transformation-Charles Rossotti and the IRS- Rainey & Thompson

<sup>15</sup> Leadership and Transformation-Charles Rossotti and the IRS- Rainey & Thompson

- a. *Independence of indirect administration board:* Presently, CBEC works under Department of Revenue and is devoid of Administrative and Financial power. Many a time, it results in delay in decision-making affecting the efficiency of the Department. Similarly, cost of collection of .77%, is one of the lowest of any organisation and basic infrastructure like office buildings, mobility, IT network, etc are far from satisfactory, leading to lower morale of the officers and hardship to taxpayers. Tax Administration Reforms Committee, constituted by the Government has recommended for independence of Revenue Boards with sufficient powers.<sup>16</sup>
- b. *Multiplicity of states and agencies:* After introduction of GST, where the taxes are required to be collected at Central and State level, multiplicity of state and other agencies would pose innumerable problems unless proper coordination is achieved. This is likely to be a Herculean task considering 29 states and seven union Territories with wide regional disparities.
- c. *GST Network and its management:* GST proposed to have an elaborate GST IT network for seamless transfer of information and credit from originating states to the destination state. Creation of such IT network and its maintenance amongst 29 states, seven union Territory and Central government would be a stupendous task.
- d. *Paucity of funds and non-delegation of power:* Lack of adequate fund with the Department, and delegation of power has been one of the main factor for poor infrastructure. Until unless, adequate fund is provided with sufficient delegation of financial power, the problem is likely to aggravate.
- e. *Hiring a professional in IT and infrastructure:* While State and Central government are training its staff and officers in the taxation matters, they continued to be ill-equipped/trained in the IT and infrastructure related matters. Since IT and infrastructure will play a very dominant role in modernisation of taxation equipment system and related infrastructure, it is essential that professionals are hired with better pay and perks.
- f. *Procedural delays in promotions and appointments:* The experience of the officers/staff has been very frustrating in the matter relating to promotions and appointments. Many posts, including at the very top, have remained unfilled for years together leading to massive frustration and disappointment in the Department. The officers and the staff need to be motivated by providing adequate working opportunities and promotional avenues.

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<sup>16</sup> Report of TARC, 2015

- g. *Skill development and capacity building:* Introduction of GST and deployment of modern nonintrusive equipment would need training to all stakeholders. A time bound and continuous method of skill development and capacity building need to be properly planned.
- h. *Fear factor duty vigilance and audit:* The fear of vigilance and audit continue to haunt the officers and staff of the Department, even in the cases relating to adjudication, review. Vigilance enquiry opened on the frivolous ground remained non-finalised for years together leading to massive fear in the mind of officers and staff. They prefer to take decision in favour of revenue.

**21. *Measures to implement recommendations:***

*GST:*

- a. CBEC to be reconstituted as an independent CGSTB (Customs, Goods and Service Tax Board) with mandate to implement GST throughout India with phase consolidation of all states and agencies into it. This recommendation has been suggested in view of the experience of Canada, where, there is only one tax collecting authority with adequate independence of implementation and financial support.
- b. The GST statute/rules/procedure/forms should be made simpler and should be made in consultation with all stakeholders in time bound manner. Complex statute/rules/procedure would result in substantial litigation locking revenue in the court matters.
- c. In the initial stages of implementation, the Canadian experience reveals that a very strong system of mandatory advance rulings and clarifications eases the transition to a substantial extent.
- d. The work of creation of GST IT network should be outsourced to professionals with clearly defined procedures. This network should be managed by them. The professionals should be allowed to be hired on compatible pay and perks.
- e. The dispute redressal mechanism should have a provision of time bound resolution, failing which, it should provide for penal provisions, including administrative.
- f. All stakeholders, including taxpayers and departmental officers/staff need to subject to intense training on GST laws, rules and procedures; which need to be updated on continuous basis online.
- g. The infrastructure requirement of all stakeholders need to be quantified and created with adequate allocation of funds for them.

*Trade facilitation and enforcement*

- a. Multiple agencies relating to the work of border control need to be merged in single agency. It will ensure proper coordination, planning, implementation, etc. Thus, all border control agencies like Customs, Coast Guard and immigration should be merged.
- b. Deployment of adequate state of art equipment for non-intrusive examination at ports, airports, in a time bound manner. Necessary funds in this regard may be provided. This would help in reducing not only dwell time, but also strengthen the border control in curbing smuggling of narcotics drugs, arms, ammunitions, etc.
- c. Use of IT network and communications system would reduce the interface of officers/staff with the public.
- d. Setting up of canine establishment would be very effective in curbing cases of smuggling of narcotics drugs and ammunitions.

#### *Litigation*

- a. There has to be certainty in taxation in the matter of policy and rates. The settle case laws should not be disturbed.
- b. *E-filing* of appeals would greatly enhance the transparency as well as accountability.
- c. Judicial indiscipline in adjudication can be curtailed by adopting *carrot and stick* policy. Adjudicating authorities not following settled case laws should be cautioned including appropriate disciplinary proceedings can be initiated. However, protection from vigilance and audit need to be provided for officers and staff maintaining judicial discipline.
- d. Professionals can be hired for arguing the cases of Department before tribunal. This will improve the success rate of departmental cases before tribunal.
- e. Reward policy should be amended to include collection of arrears more than five years. The policy for *shaming the defaulters* of arrears should also be prepared and made operational.

#### *HR and infrastructure*

- a. The jurisdiction of Department need to be reorganised on *functional basis* under the charge of Principal Chief Commissioners. This would enable expertise required to be effectively utilised in collection of revenue and other related activities.
- b. To motivate officers and staff, attractive transparent performance-based system be prepared in consultation with all office bearers of union/Association and put in place.
- c. Those not performing to the objectives and goals of the Department should be retrenched.
- d. Career planning, including promotion and appointment should be done without delay. Proper advance planning should be done in this regard.
- e. The officers and staff need to be protected from vindictive action of *audit, vigilance, and preventive*. In case, any vigilance enquiry have been initiated, the same should be completed in time bound manner, *say one year*.

- f. Adequate funds need to be made available for creation of infrastructure and its management. Separate Directorate can be constituted to look after creation and maintenance of infrastructure like building, vehicles, etc

### *Conclusion*

Emergence of difficult situation in any organisation, system, state or country cannot be ruled out completely. But before such situation turns into crisis, remedial actions can be taken by effective leaders and it's team by critically examining underlying issues and prioritising the threat parameters. Even if the crisis strike, a well prepared, equiped and trained manpower would be in a better position to handle and also to develop confidence to face crisis in future.

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