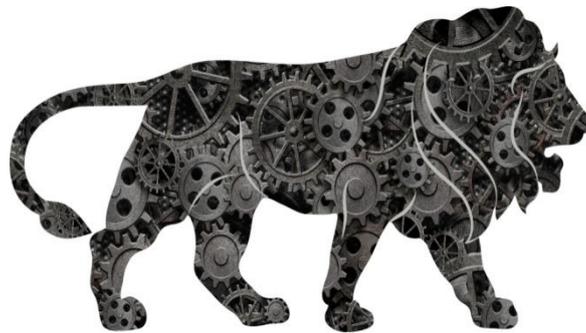


# PROJECT REPORT



**“NEED FOR BUSINESS PROCESS ENGINEERING IN CENTRAL EXCISE AND SERVICE TAX TO PROMOTE ‘MAKE IN INDIA’ CAMPAIGN AND LESSONS LEARNT OVERSEAS FOR IMPLEMENTATION IN INDIA”**

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# CHAPTER - I

## INTRODUCTION

**Make in India** is a key new initiative of the Government of India, to encourage companies to manufacture their products in India. It was launched by Prime Minister Narendra Modi on 25 September 2014.

Prime Minister had hinted towards this initiative in his Independence Day speech of 15 August 2014. It was launched on 25 September 2014 in a function at the Vigyan Bhawan. On 29 December 2014, a workshop was organized by Department of Industrial Policy and Promotion, which was attended by the PM, his Cabinet ministers, Chief Secretaries of States and various industry leaders, to explain the concept of “Make in India”.

### Overview

Its objective is to encourage foreign companies to set up manufacturing /service providing concerns in India to encourage job creation, and skill enhancement.

- This initiative aims to enhance GDP growth and increase tax revenues
- It also hopes to attract capital and technological investment in India.
- It also aims at establishing high quality standards
- *It aims at enhancing the global* competitiveness of the Indian manufacturing sector.
- It also aims at ensuring sustainability of growth, particularly with regard to environment.

The major objective behind the initiative is to focus on 25 sectors of the economy for job creation and skill enhancement. Some of these sectors are automobiles, chemicals, IT, pharmaceuticals, textiles, ports, aviation, leather, tourism and hospitality, wellness, railways, auto components, design manufacturing, renewable energy, mining bio-technology, and electronics.

In order to encourage the concept of 'Make in India' globally and to make it successful, many aspects of the current policies needs to be examined and finely at-tuned to provide the best of environment, which will allow this initiative flourish.

India is one of the fastest growing economies in the world. However, there is a need to focus on the business environment, as the World Bank's Doing Business Report 2014 that places India in a unflattering 134th position among 185 countries. India ranks lower than its BRICS counterparts and is a relatively poor performer even amongst the South Asian countries with very low rankings on most of the de-terminants of investment attractiveness.

	Doing Business		Change in rank
	Rank 2013	Rank 2014	
<b>Overall rank</b>	<b>131</b>	<b>134</b>	<b>-3</b>
Starting a business	177	179	-2
Dealing with construction permits	183	182	1
Getting electricity	110	111	-1
Registering a property	91	92	-1
Getting credit	24	28	-4
Protecting investor	32	34	-2
Paying taxes	159	158	1
Trading across borders	129	132	-3
Enforcing contracts	186	186	0
Resolving insolvency	119	121	-2

## Starting a business

### India vs BRIC Rank 2014

Brazil	123
Russia	88
India	179
China	158

### India Vs Southasia

	South Asia	India
Number of	7	12
procedures		
TimeTa- ken (in days)	16.2	27

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The main brochure prepared by the Dept of Industrial policy and promotion, highlights the advantages of each sector and what India has to offer. Despite all the advantages, there are huge problems as highlighted in this report. We also need to understand, that as a manufacturing destination we are not only competing with the developed countries but also our own neighbors and whole of south Asia.

It is no help to us that India fares miserably in International rankings in ease of doing business. However what is encouraging is that the new Govt. has taken the bull by its horns and is very seriously attempting to transform the Indian business landscape. We as a Major Tax Dept play a very important role in this. Collection of taxes is a sovereign right and a necessity but what is imperative is that the tax be collected fairly, correctly and judiciously.

In this report, we have looked at the macro issues plaguing India's development story and the specific issues relating to Central excise and Service Tax, as that is our brief. We have collectively obtained feedback from stakeholders, studied various reports etc, discussed amongst ourselves and have highlighted the problem areas. We have studied certain important processes closely and given our recommendations. We are not commenting on Tax Policy per se, but only on procedures that any business entity has to go through on a daily basis.

Over the last 20 years or so post liberalization, a lot of healthy tax policy initiatives have been put in place leading to a much better business friendly environment and fewer complications and simpler procedures. Merging of various tax rates into a smaller band of tax rates, doing away with statutory records and Filing of Classification list and Price list being a few examples. Enabling e-filing of returns, e-payment and specialized audit etc. However present high level of litigation and Industry perception, indicates that still a lot more needs to be done to improve Tax administration and Tax policy.

There is no doubt that the entire tax policy and tax administration need to take a deep hard look at themselves and see what kind of a tax administration we are running, and how it is not encouraging investment. It's a time to face facts when we are at the bottom of the world rankings, despite our tall claims of being a superpower etc. The Govt. had set up the Tax Administration Reforms Commission with the objective of identifying the problems in Tax Administration and how to make it more efficient and effective, but not much progress has been made on its recommendations.

We have no doubt that we as a nation have a huge potential but what is holding us back is lack of planning, clear conceptualization, initiative and inability to change our mindset. Now that the Govt. is taking the initiative, all arms of the Govt. must grab this opportunity and outdo themselves in providing a business friendly environment. We must remember that we exist because of the businesses, if they cease, whom will we tax !!!! Growth in businesses will spur the GDP, the per capita income, the employment and will increase the consumption, thus encouraging a further growth cycle.

In this report we have drawn data from specialized studies conducted by Industry bodies like CII and the Report of the Tax Administration Reforms Commission.

India is at a critical junction, we have to enhance our global competitiveness to attract investment. To achieve this we need high class infrastructure, investor / industry friendly policies, an enabling environment and most of all a will to work collectively to make this project of "Make in India" succeed.

## **CHAPTER - II**

### **PRESENT CONTEXT**

#### **Ref: Economic Survey of India 2014-15.**

“One of the redeeming features, while comparing economic performance across different countries for the year 2014-15, has been the emergence of India among the few large economies with propitious economic outlook, amidst the mood of pessimism and uncertainties, that engulf a number of advanced and emerging economies. Brighter prospects in India owe mainly to the fact that the economy stands largely relieved of the vulnerabilities associated with an economic slowdown, persistent inflation, elevated fiscal deficit, slackening domestic demand, external account imbalances, and oscillating value of the rupee in 2011-12 and 2012-13. From the macroeconomic perspective, the worst is clearly behind us.

#### **Key Indicators**

<b>Data categories</b>	<b>Unit</b>	<b>2011-12</b>	<b>2012-13</b>	<b>2013-14</b>	<b>2014-15</b>
Growth Rate	%	-	5.1	6.9	7.4
Index of Industrial Production	%	2.9	1.1	-0.1	2.1
Export growth(US\$)	%	21.8	-1.8	4.7	4.0
Import growth(US\$)	%	32.3	0.3	-8.3	3.6
Foreign Exchange Reserves	US\$ billion	294.4	292.0	304.2	328.7
Gross Fiscal Deficit	% of GDP	5.7	4.8	4.5	4.1
Revenue Deficit	% of GDP	4.4	3.6	3.2	2.9

**Source: Economic Survey of India Report 2014-15**

The manufacturing sector registered a growth of 6.2 percent and 5.3 percent respectively in 2012-13 and 2013-14 (6.1 percent and 5.3 percent) in terms of GVA at factor cost). As per the pre-revised series, this growth was 1.1 percent and -0.7 percent.

At the disaggregated level of the new series, the growth in manufacturing sector was chiefly on account of robust growth in textiles, apparels, and leather products, averaging 17.7 percent during 2012-13 and 2013-14, and the machinery and equipment sector averaging 9.3 percent.

The services sector triggered the growth momentum in 2013-14. Services like trade and repair services, rail transport, communication and broadcasting services and miscellaneous services achieved double-digits/close to double-digits growth during the year. However, sectors like water transport and storage services lagged behind.

### **International Trade**

After growing by 4.7 percent in 2013-14, India's merchandise exports growth moderated to 2.4 percent to reach US\$ 265 billion in 2014-15(April-January).

Capital goods imports declined continuously from 2011. Non-POL and non-gold and silver imports, which largely reflect the imports needed for industrial activity, grew by 7.8 percent in 2014-15(April-January), after registering a decline of 0.7 percent and 6.9 percent respectively in 2012-13 and 2013-14.

### **Outlook for 2015-16**

The macroeconomic situation in India has improved significantly during the current year. The release of the new series of national accounts revealed that the economy has been performing much better than what was being depicted earlier.

The steady acceleration in services and manufacturing growth in the face of subdued global demand conditions point to the strengthening of domestic demand. Most of the buoyancy in domestic demand can be traced to consumption. Investment activity, which is slowly picking up, needs to be grounded on a stronger footing. The savings-investment dynamics will be crucial for the growth to strengthen further in the coming years, in addition to reversal of the subdued export performance being currently witnessed. The key will be the response of savings to improved price and financial market stability, and of investment, particularly in the crucial infrastructure sector, to reform efforts of the Government that are underway.

### **Industrial, Corporate and Infrastructure Performance**

The industrial growth picture as per the IIP suggests that industrial production which has slowed down since 2011-12, reversed the trend in 2014-15. In terms of use-based classification of IIP, basic goods and capital goods witnessed marked improvement in growth during April-December 2014-15. While the growth in intermediate goods remained sluggish, consumer goods contracted in April-December 2014-15, particularly due to contraction in the consumer durable sector.

The performance of listed manufacturing companies the private sector in terms of growth of sales and net profit appeared to turn around in Q1 2014-15. However the performance Q2 2014-15 dampened expectations of sustained improvement.

### **Services Sector**

India's services sector remains the major driver of economic growth contributing 72.4 percent of GDP growth in 2014-15. Services-sector growth has increased from 8.0 percent in 2012-13 to 9.1 percent in 2013-14 and further to 10.6 percent in 2014-15. This is mainly due to growth acceleration in financial, real estate, and professional services to 13.7 percent from 7.9 percent and public administration, defence and other services to 9.0 percent from 7.9 percent in the previous year.

Growth in trade, hotels, transport, communication, and related services was 8.4 percent in 2014-15 compared to 11.1 percent in 2013-14. Data available for the beginning months of 2015 indicates pick-up in the services sector with expansion in business activity as indicated by services PMI data. This growth momentum is expected to continue in 2015-16.

The services sector is also the dominant sector in most of the states of India with a more than 40 percent share in the gross state domestic product (GSDP) in 2013-14 for almost all states. This sector has made substantial contribution to FDI inflows, exports and employment. During the last twelve years, with a compound annual growth average (CAGR) of 8.7 percent, India had the second fastest growing services sector, just below China's 10.7 percent. In commercial services exports, India had the highest CAGR of 20 percent during this period. India's share in global exports of commercial services increased to 3.2 percent in 2013 from 1.2 percent in 2000. Its ranking among the leading exporters in 2013 was sixth. In the first half of 2014-15, services exports grew by 3.7 percent to US\$75.9 billion and import of services grew by 5.0 percent to US\$ 39.9 billion, resulting in net services growth only 2.4 percent."

***The above details reflect the changing macroeconomic environment, where the mood is upbeat and positive. It is now for the reforms in tax administration to unleash the real growth. The tax administrators must remove all bottlenecks to facilitate industrial growth and enhance growth in services sector and export of services.***

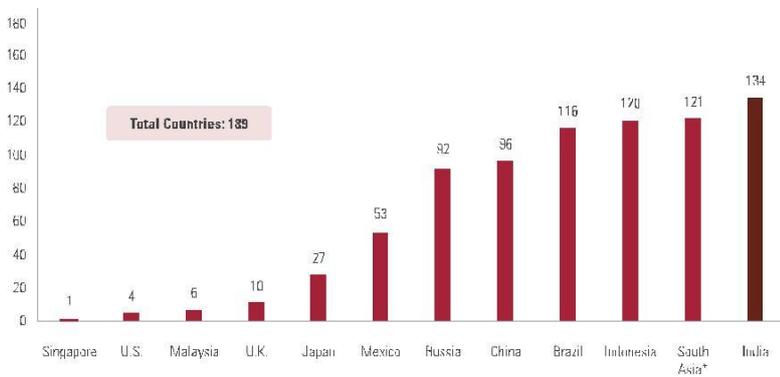
# CHAPTER - III

## CHALLENGES

### Ease of Doing Business

India is one of the fastest growing economies in the world, yet ranks among the lowest in the World Bank's rankings on the ease of doing business, 2014.

### Ranking of select countries on the overall ease of business, 2014



Source: Doing Business 2014, World Bank

#### The India Paradox

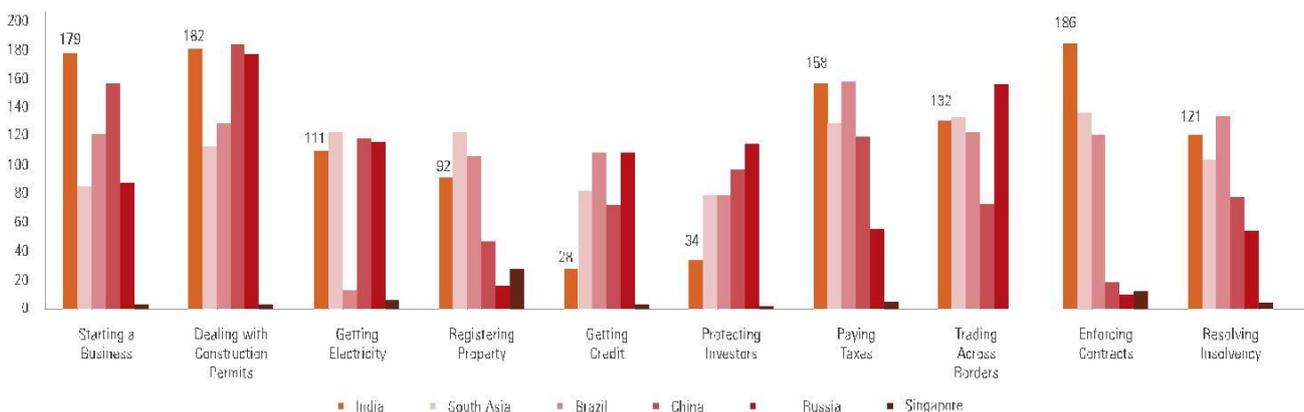
India is one of the fastest growing economies in the world. The high potential of the Indian market driven by an emerging middle class, cost competitiveness and a huge pool of talent makes it one of the most

attractive investment destinations. Yet, according to the World Bank's 'Doing Business 2014' report, India is ranked 134 out of 189 countries in the overall ease of doing business. This places India lower than the other BRICS (Brazil,

Russia, India, China and South Africa) members and highlights its relatively dismal performance among other South Asian countries.

#### Rankings on sub-indices on the ease of doing business

Source: Doing Business 2014, World Bank (Extracts from CII BCG REPORT on make in India )



In the World Bank survey, India ranks lowly on most of the determinants of investment attractiveness — especially starting a business, enforcing contracts, dealing with construction permits **and paying taxes**. Problems in securing permits, inadequate infrastructure, power shortages, stringent labour laws, **tax regulations**, **lack of** governance and **transparency** and approval processes are critical issues in the country that need to be addressed.

As part of the survey, corruption emerged as the **major obstacle** in doing business in India followed by cost of financing, **tax administration and high taxes**. **Economic and regulatory policy uncertainty** and macroeconomic instability create challenges in the operations and growth of business in India. Skill and education of workers, labour regulations, customs and trade regulations and access to land are some other major areas of concern in doing business in India. These are the challenges we need to address.

## Manufacturing Sector:

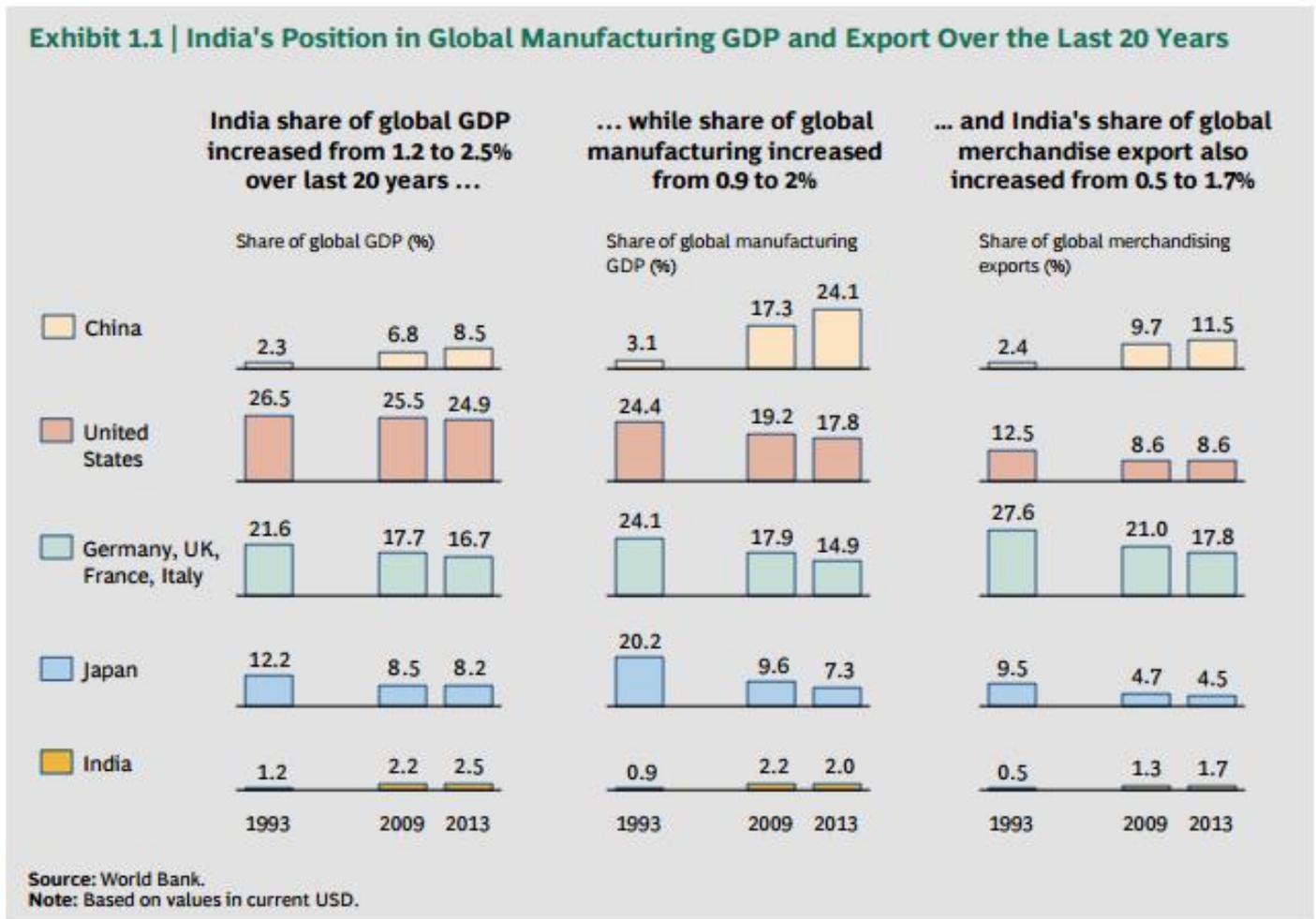
Over the last 20 years, Indian manufacturing has by and large grown at the same pace as our overall economy. Our share of global manufacturing has grown from 0.9 to 2.0 percent during this period while our GDP share has grown from 1.2 to 2.5 percent.

Over the last five years, there has been a reversal of sorts to this manufacturing trend, with Indian manufacturer's share of GDP falling from 2.2 to 2.0 percent between 2009 & 2013, even as the country's share of global GDP grew from 2.2 to 2.5 percent over the same period.

When seen against the performance of India's peers, the situation is bleaker still. China's share of global manufacturing increased by more than six percentage points (rising from 17.3 to 24.1 percent) during the same period, while the manufacturing share of several other countries (South Korea, Russia, Mexico, Malaysia, Thailand) has also significantly increased.

The same bleak picture characterizes the Indian export sector—and exports are, the best indicator of success for any manufacturing nation. Here, India's performance has improved with its share of global merchandise exports increasing from 0.5 to 1.7 percent over the past twenty years. However, this increase remains modest compared to China's performance, where manufacturing exports have risen from 2.4 to 11.5 percent of global exports.

While the NMP policy sets out plans for the sector to reach 25 percent of GDP and create 100 million additional jobs by 2022, the sector’s contribution to GDP has fallen from 16 to 15 percent, with fewer than five million incremental jobs having been added to the economy over the past five years (Exhibit 1.2).

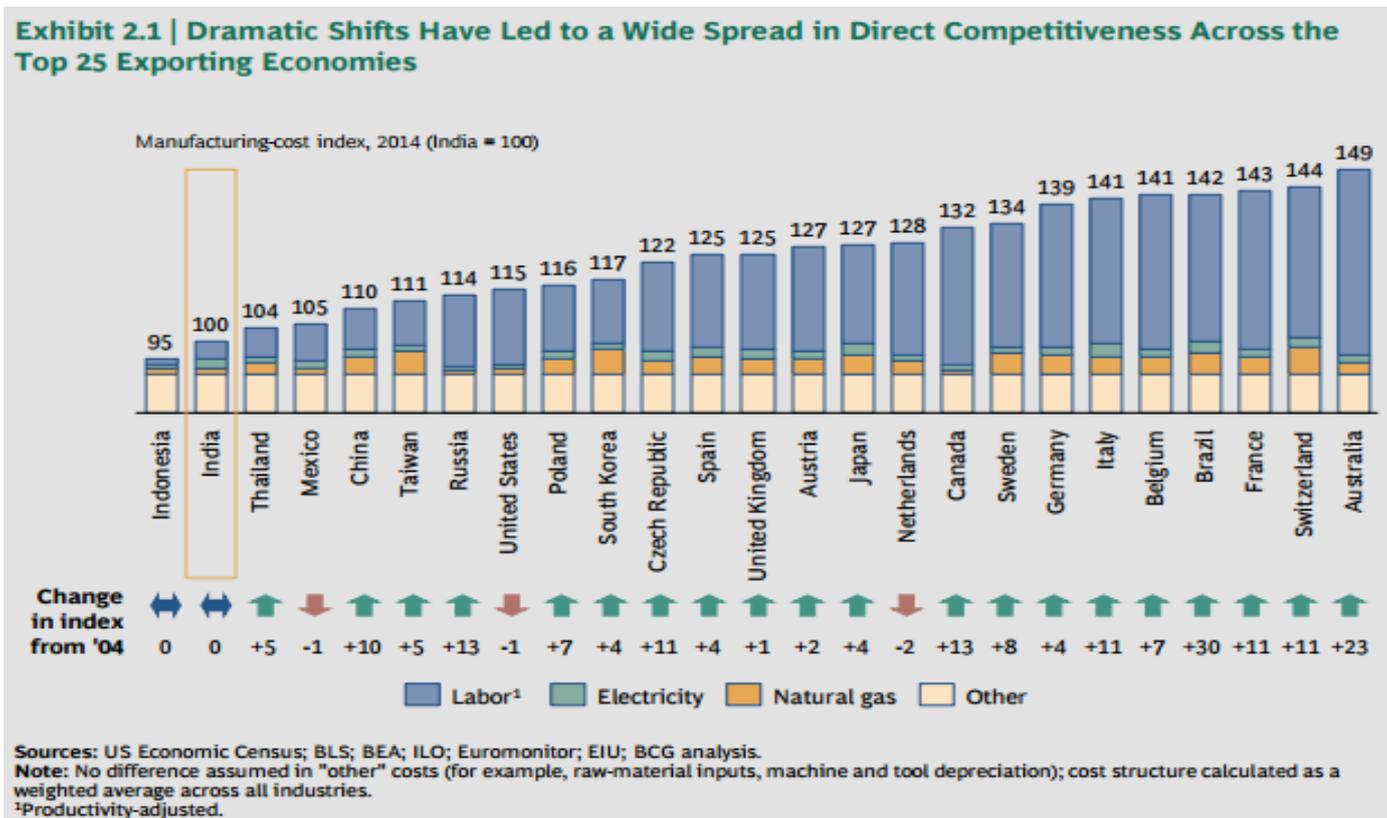


(Extracts from CII BCG report on Make in India 2014 )

The overall economic outlook across the world has been improving. Several countries, especially in the developed economies—where growth had slowed down or contracted significantly in the wake of the 2008 financial crisis—have started to show signs of revival. In the past year, the US, for instance, has experienced some good growth. And although questions remain over whether Europe as a whole can return to growth, several economies within Europe have started strengthening. China’s outlook has also improved.

Reforms have been announced to boost manufacturing growth to 10 percent per year by promoting “Make in India”, an initiative aimed at creating 100 million jobs over the next decade and bringing manufacturing up to 25 percent of Indian GDP.

(Extracts from CII BCG Report on Make in India turning Vision into Reality 2014 )



## India is challenged by Secondary Factors

One of the most important facts for any investor to decide on any manufacturing location **is cost**, while India has the 2<sup>nd</sup> lowest manufacturing cost. Indonesia has edged India out, China’s cost advantage is eroding, and even Russia’s cost competition has eroded over the last two decade. Mexico has regained its status as a low manufacturing base.

US is re-emerging as a preferred manufacturing destination. Their intensive focus on innovation & technology has led to high productivity. While China leads the

world overall in manufacturing, US tops the chart in technology intensive manufacturing.

What is important, is for us to look beyond the cost advantage and see how the other factors relating to a business environment actually drive us as an investment destination.

India is largely challenged by secondary factors.

**Exhibit 2.4 | India is Challenged by Secondary Factors**

Country	Direct cost relative to the India <sup>1</sup>	Overall business environment <sup>2</sup>	Ease of doing business <sup>3</sup>	Logistics performance <sup>4</sup>	Corruption perception <sup>5</sup>
	Delta	Rank	Rank	Rank	Rank
 India	-	57	142	54	94
 China	+10%	50	90	28	80
 Germany	+39%	12	14	1	12
 US	+15%	7	7	9	19
 Japan	+27%	27	29	10	18
 Thailand	+4%	34	26	35	102

Rank not among Top 50

Sources: US Economic Census; BLS; BEA; ILO; Euromonitor; EIU; BCG analysis.

<sup>1</sup>Includes a selection of economies ranked from 1 to 25 on total export size.

<sup>2</sup>EIU ranking based on ten separate criteria or categories covering the political environment, the macroeconomic environment, market opportunities, policy toward free enterprise and competition, policy toward foreign investment, foreign trade and exchange controls, taxes, financing, the labor market, and infrastructure.

<sup>3</sup>World Bank ease of doing business index.

<sup>4</sup>World Bank logistics performance index.

<sup>5</sup>Transparency International 2013 corruption perception index.

## Global Competitiveness:

In the highly Globalized World today, countries are fighting to attract investment to boost their local economy and generate employment. They are all fighting for a share in the Global Value Pie. Global Competitiveness can be judged on basis of ability to simply “make” or ‘manufacture”. To manufacture you need something more than just make. Innovation and skills are required. How does India fare in that area is also interesting. The table below indicates that we need to do a lot more in that area too, to enhance our competitiveness.

## Global Competitiveness Index: R & D Innovation

Country	Capacity for innovation		Quality of scientific research institutions		Company spending on R&D		University – Industry collaboration on R&D		Availability of scientists and engineers		PCT patents granted / million population	
	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
USA	5.9	2	6.1	4	5.5	4	5.8	2	5.3	5	149.8	11
UK	5.3	10	6.3	2	4.8	14	5.7	4	4.8	22	89.1	18
South Korea	4.7	24	5.0	27	4.5	20	4.6	26	4.4	42	201.5	8
South Africa	4.3	35	4.7	34	3.4	48	4.5	31	3.5	102	6.5	45
China	4.2	40	4.3	39	4.3	23	4.4	32	4.4	43	11.7	34
Brazil	4.1	44	4.0	50	3.5	43	3.8	54	3.3	114	3.2	50
India	4.0	48	4.0	52	3.8	30	3.9	50	4.4	45	1.5	61
Russia	3.8	66	4.0	56	3.2	62	3.6	67	4.1	70	7.1	41

**Source:** Global Competitive Report 2014-15, World Economic Forum.

**Note:** PCT-Patent Cooperation Treaty

The present government has laid much stress on its “Make in India” campaign. After all, the election campaign promised jobs galore through rapid industrial growth. The NMP is projecting a growth of 15 % in the manufacturing sector and 25 % in a few years. Given our dismal performance in the last few years, as seen in the IIP index, a lot of work is required to be done.

While we may want to increase employment through industrialization, However, industrial jobs are not growing fast anywhere in the world. Modern technology is increasingly mechanizing industries, and manufacturing requires ever fewer workers per unit of output. Many US industries have moved to China seeking lower wages. Yet US companies overall are flourishing, brimful of innovation. Much of US innova-

tion is in services (as with Facebook, Google or Amazon). But it also includes Apple, the new manufacturing giant of the world. Virtually all its products are assembled in China, from components made in several countries. Obama, like Modi, would like Apple to do more manufacturing at home. One would say that Apple phones are made in the US, and merely manufactured in China. Historically, making and manufacturing meant the same thing but not anymore.

When Apple started selling smartphones for \$300, China's share from assembly was just \$7. Apple got \$150 of the value through innovation, marketing and profits. The remaining value was split among component suppliers, transporters, and other minor partners.

If Apple gets \$150 of a phone's value and China gets only \$7, is the phone really made in China? No, we would say it is made in the US, and merely manufactured in China. The key parts of making goods is shifting to innovation design and marketing, not manufacturing components or assembling them. What matters is value capture, not just manufacture. Even in India, companies have begun replicating Apple's approach. Micromax has ousted Samsung as India's top cellphone seller. Other Indian cellphone companies like Karbonn, Lava are using the same approach. They design their phones, which are then manufactured and imported from China. As in Apple's case, one could argue that Micromax's cellphones are really made in India, and merely manufactured in China. Similarly Flipkart, India's leading e-commerce company, has sales of \$3 billion and a market valuation of \$ 2 billion, more than the combined value of all Indian brick-and mortar retail chains. Others like Snapdeal are following suit. Hungama dominates the e-music space. Ola has come up in the cab-booking area. The sky-high valuations of these companies by investors may sink in due course: that happened to many companies during the dotcom boom and bust. But those that survived have the potential to grow into giants, just as Infosys and Wipro did in software. Such new companies will gradually dominate the 21st century.

Let's be clear, traditional manufacturing is not dying. It will grow in volume and employment for a long time. The newcomers occupy only a small part of the economic space today. In traditional industries, “make” and “manufacture” may remain synonymous. But let us prepare for a future where, increasingly, “manufacture” will be just a small part of “make”.

To put in other words, “to make” means capturing a definite portion of value of an ultimate final product which is proportionately fragmented and sourced from various countries, territories, jurisdictions and economies who has critical and core competency to manufacture such fragmented part or component with the given specifications, meeting with the strict quality and inspection standards, capable to deliver on committed schedule and having the best in class logistics, manpower, skill, transportation and other support services. This gives rise to new concept called the “Global Value Chain” & “Global Production Networks”, “International production and Supply Chain Hub”.

Ideally there can be three approaches for “Make in India” be a successful campaign:–

- (i) Continuation and Up gradation of existing Industries and Businesses in India.
- (ii) Attracting Foreign Direct Investment and new industries from International market, which will run parallel and complementary to the existing Indian Industry.
- (iii) Getting entry into Global Value Chains and Global Production Networks depending upon core competency areas and by improving infrastructure, logistics and service delivery. Generally speaking as of now, all over the world the trend is moving towards Global Value Chains and Global Production Networks which gives the synergy and comparative cost advantage regardless of the

country, geography, territory or jurisdiction and therefore most likely future of all industries barring few conventional industries, this appears to be the future of manufacture. Hence, it is extremely important for India.

There are several studies which shows similar Value Chains spread across the geography. The list is enclosed as **Annexure A**.

The table above indicates that while we may be ahead in the cost advantage our overall business environment and other infrastructure related issues are preventing this growth. Our own Asian neighbors are beating us and getting a share in the global value chain that we ought to have grabbed.

### **Extracts from CII KPMG Taskforce Report - Ease of Doing Business in India 2014.**

Concerned with India's dismal rankings in World Bank's 'Ease of Doing Business', where India has been placed consistently lower than its BRICS counterparts and even amongst other South Asian countries; a survey-based report on the prevailing business regulatory environment in the country was undertaken by CII with the support of KPMG. The study focused on few key parameters of 'Doing Business' such as starting a business, land acquisition, taxation and contract enforcement.

The objective was to underscore the areas of business regulation that need attention.

The report has highlighted that even after two decades of economic reforms, India continues to falter on various sub-indices such as starting a business, dealing

with construction permits, getting electricity, registering property, paying taxes, trading across border, enforcing contracts or resolving insolvency.

Enforcing contracts  
Resolving insolvency

Starting a business  
Employing workers



What ails the Indian economy is the business needs at various stages of doing business – at the startup, in getting a location and financing, daily operations and enforcing contracts.

To steer the economy back on the growth trajectory, India needs to become an attractive investment destination. The Government needs to undertake reforms that will help place the country on an equal footing amongst countries having favorable, flexible, liberalized and transparent business environment.

Some of the major observations of this study are:

- 1. Lack of an effective land acquisition process has made land acquisition complex & time-consuming**

- Average time taken to acquire the land is 14 months and has taken even longer in several occasions.
- 58% of the respondents feel number of visits made to each department to obtain the permission pose major obstacles in the approval process.
- 69% of the respondents feel that there is a lack of effective land acquisition process.
- 83% of the respondents feel that unsecured land titles generate uncertainty
- Land mutation process is considered complex and time-consuming.

## **2. Taxation still a challenge, not conducive to fostering growth.**

- 90% of the respondents are in favor of reduction in tax rates.
- 92% of the respondents feel that there are challenges in transfer pricing audit/assessment relating to distribution / agency.
- 90% of the respondents believe that the tax authorities are not proactive in promoting investments.
- 60% of the respondents feel that neutralization of tax decision by Supreme Court through retrospective amendment has damaging effect on investment sentiments

- More than half the respondents face delays in obtaining service tax refund.

### **3. Costs incurred in the process of starting a business are significantly high.**

- Approvals related to environment clearances, land procurement, construction permits, industrial safety permits and power connection are top five obstacles in starting a business.
- 85% of the respondents feel that the time required to obtain such clearances is not reasonable.
- 78% of the respondents, who feel the number of windows/ministries one has to visit, are not reasonable.

### **4. Contract Enforcement complicated and time consuming:**

- Time taken from filing to final judgment seems unreasonable to most of the respondents and poses major obstacles
- Costs involved (costs for engaging and retaining lawyers, miscellaneous costs, during the interim stage, enforcement costs) also pose significant obstacles.
- 84% of the respondents have indicated that a review of laws & regulations needs to be taken up urgently

In this project, we are not addressing all these issues but only those related to taxation.

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## The Road to Global Leadership - What we need to do:

		<b>Change in mindset</b>	<ul style="list-style-type: none"> <li>• Change business leader and consumer mindset – Think long term, think global</li> </ul>
	<b>Technology and innovation</b>	<ul style="list-style-type: none"> <li>• Facilitate tech capability and capacity building in SMEs</li> </ul>	<ul style="list-style-type: none"> <li>• Create R&amp;D and technology led global scale and competitive advantage</li> </ul>
<b>Government policy and reforms</b>	<ul style="list-style-type: none"> <li>• Initiate Labour reforms to improve productivity</li> </ul>	<ul style="list-style-type: none"> <li>• Apply policy levers to promote strategic depth in select sectors, develop clusters</li> </ul>	<ul style="list-style-type: none"> <li>• Promote global access and brand positioning of India inc</li> </ul>
<b>Ease of doing business</b>	<ul style="list-style-type: none"> <li>• Address key issues around set up cost, approval and clearances, access to credit</li> </ul>	<ul style="list-style-type: none"> <li>• Create measures to attract greater FDI and investments – administration, taxation</li> </ul>	<ul style="list-style-type: none"> <li>• Achieve best in class business ecosystem-move beyond 'companies'</li> </ul>
<b>Infrastructure</b>	<ul style="list-style-type: none"> <li>• Build basic transport, power and other infrastructure</li> </ul>	<ul style="list-style-type: none"> <li>• Drive investment led infrastructure creation – real estate, industrial corridors, export oriented infra</li> </ul>	<ul style="list-style-type: none"> <li>• Develop smart cities and global centres of industrial excellence</li> </ul>
	<b>Revive manufacturing</b>	<b>Gain global competitiveness</b>	<b>Claim global Leadership</b>

Source: BCG / CII Make in India Report 2014

# TAXATION

## Ease of paying taxes in select countries

India fares poorly on the 'Doing Business 2014' paying taxes indicators — total tax rate, the time to comply and the number of payments. Of the 189 countries studied, India ranks 158 in terms of overall ease in tax payment.

	Rank	Payments (number per year)	Time (hours per year)	Profit tax (%)	Labour tax and contributions (%)	Other taxes (%)	Total tax rate (% profit)
UAE	1	4	12	0	14.1	0.8	14.9
Qatar	2	4	41	0	11.3	0	11.3
Saudi Arabia	3	3	72	2.1	12.4	0	14.5
Hong Kong	4	3	78	17.5	5.3	0.1	22.9
Singapore	5	5	82	4.9	17.6	4.7	27.1
Russia	56	7	177	8	36.7	6.1	50.7
China	120	7	318	6.2	49.6	7.9	63.7
<b>India</b>	<b>158</b>	<b>33</b>	<b>243</b>	<b>24.4</b>	<b>20.7</b>	<b>17.8</b>	<b>62.8</b>
Brazil	159	9	2,600	24.9	39.6	3.8	68.3

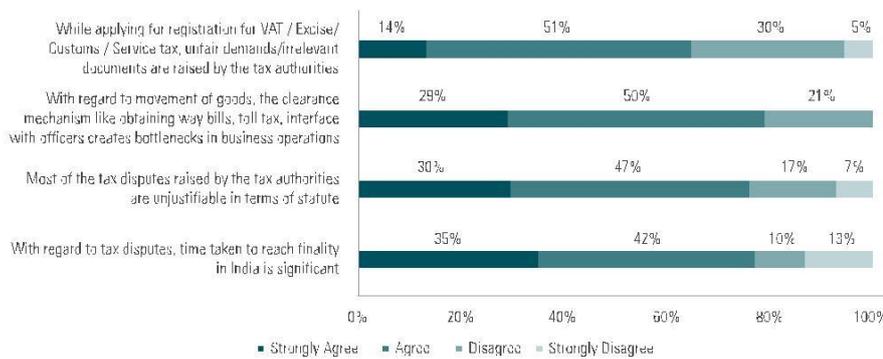
Source: Doing Business 2014, World Bank

High tax rates emerged as one of the major obstacles to operating and growing a business in India. The World Bank report is largely focused on the Direct taxes regime. It has no specific findings on central Excise and Service tax.

However, the Indian Industry i.e. CII carried out a survey to understand what ails the Indian Manufacturing sector and looked closely at taxation. Their findings are as given below.

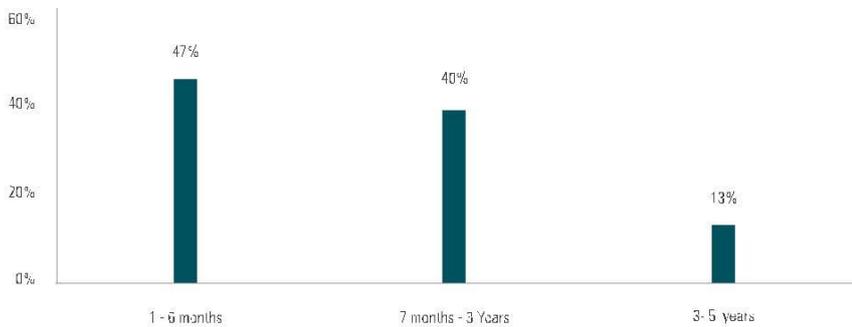
Companies face issues while dealing with tax authorities, settling tax disputes, availing tax incentives and obtaining timely service tax refund

### Issues/challenges in the Indian indirect tax regime (percentage of respondents)



Source: CII-KPMG Survey, 2014

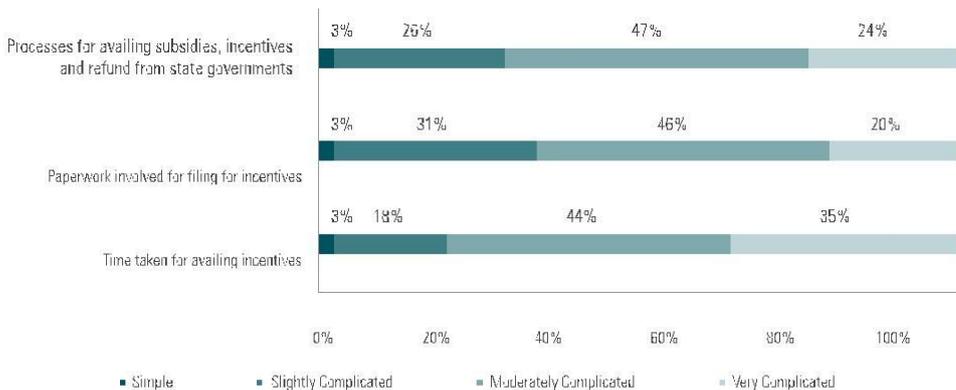
### Time taken in obtaining service tax incentives (percentage of respondents)



Source: CII-KPMG Survey, 2014

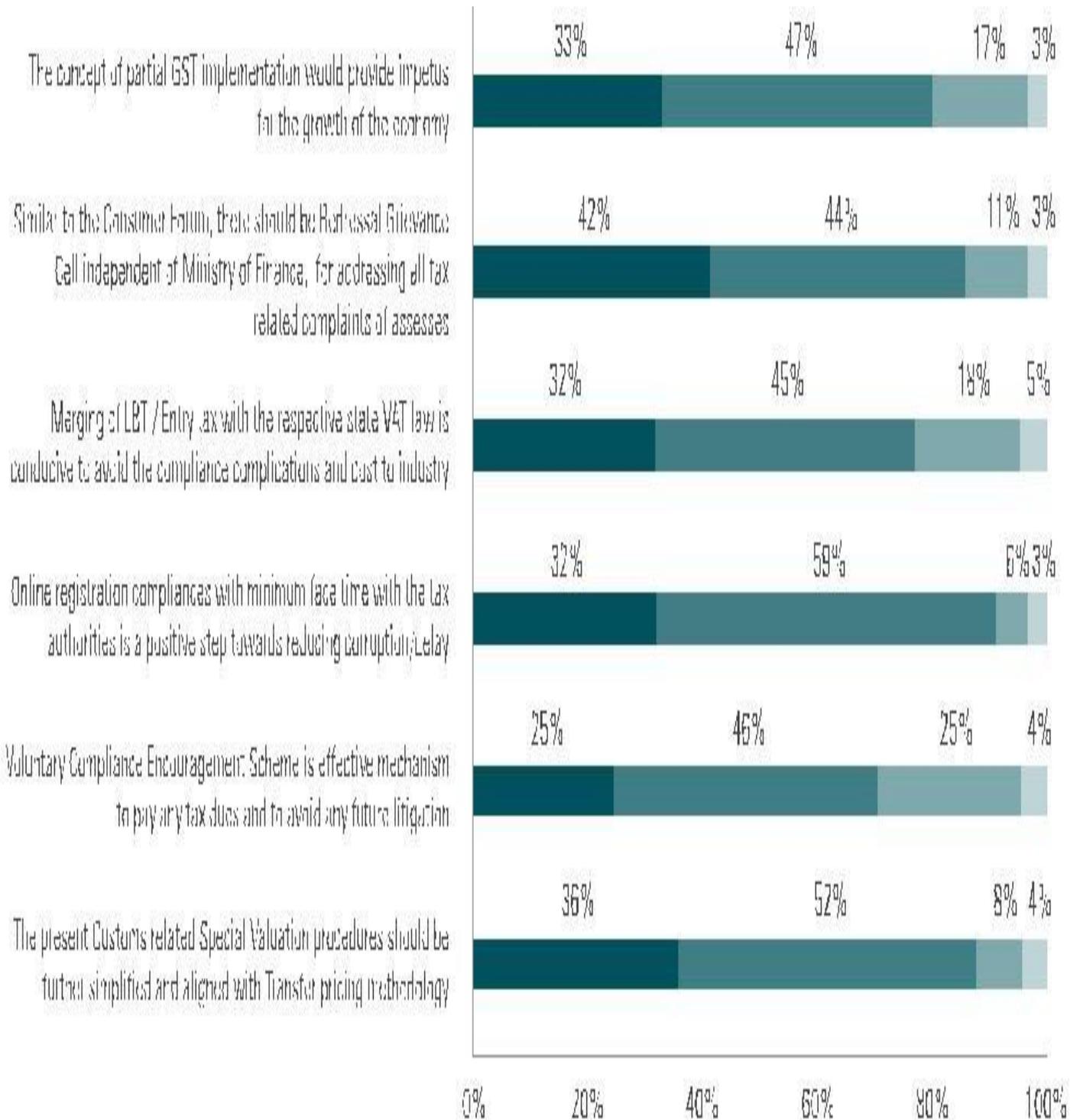
Around 2/3 of respondents find time taken for clearance and tax disputes resolution to be significant. More than half the respondents face delays in obtaining service tax refund.

### Complexities in Tax Incentives (percentage of respondents)



There is a need to simplify complex tax processes and reduce the time taken for availing incentives

**Indicated improvements to the indirect tax regime (percentage of respondents)**



As this survey indicates, Tax Administration needs to become more responsive and focus on resolving disputes.

Largely, all these papers have focused on enhancing transparency in processes, simplifying procedures, reducing disputes, encouraging voluntary tax compliance and increasing exchange of information.

At this juncture, India needs to strike the right balance between checking tax avoidance and making the tax environment more facilitative compared to other countries competing for investments.

More than low rates of tax or tax incentives, the investors will look for a responsive tax administration that provides certainty and consistency in tax treatment. The investors will look for a nation where dispute resolution is robust and engages stakeholders. There is an urgent need to foster trust between tax payer and tax administrator. An investor friendly climate alone will help India beat its neighbors who are competing for a share in the global value chain pie. The surest way to drive away investors is protracted unnecessary litigation, Lack of mechanism to engage in discussions and resolution of any difference of opinion. The standard refrain is that all lapses and mistakes are viewed as deliberate and tax avoidance measures. Even in disputes involving difference in interpretations there is no relief at the lower levels in tax administration. Penalties are imposed arbitrarily. Senior mgmt. is threatened, summoned, penalized for issues which are not in their purview. These are grievances that have to be addressed to enable this Make in India Project.

## Other Challenges to “Make in India”

(i) The success of GST regime in India is absolutely essential. Mahi-bubani, Dean of The Lee Kuan Yew School of Public Policy at National University Of Singapore, who is the author of The Great Conversions: Asia, The West and The Logic of One World, that national GST would make a massive difference and boost GDP growth by at least 1% a year. He further observes, now truck delivering goods in India take circuitous routes to maximise tax avoidance. With a unified GST, they may take the shortest possible route. The Indian economy would become vastly more efficient.

(ii) The difference of approach between Chief Economic Advisor and RBI Governor needs to be resolved in amicable manner. The larger case is CEA's making about slashing interest rate is valid. While RBI may no longer be tracking Wholesale Price Index (WPI) Inflation, it cannot ignore the fact that this rate is currently in negative territory. -2.6% of inflation for producers in a scenario where they are borrowing at an average 12%, translate into real rate of interest of nearly 15%. This is clearly unsustainable, when both consumption and investment demand is weak and companies are saddled with unutilised capacities across the sectors. Even if Consumer Price Index (CPI) Inflation is considered, the current level of 4.9% is well below the 6% threshold, the RBI has projected for January 2016. In short, there is a clear case of interest rate cut today to provide the level playing field to the Indian Business.

(Source: Editorial of Indian Express, Mumbai Edition, dated 29.05.2015)

(iii) **Power Crisis of India**: Currently, the country's power generation capacities are operating at lowest plant load factor(PLF) in 15 years i.e.

65%. The situation is more grim considering the fact that no new power generation project has been announced in the last two years and there are no takers for all the generation capacity that is in place. There is a demand but they do not have the money to pay for the power due to health of discoms(State Distribution Companies). As per the source of Economic Times, dated 29.05.2015, ailing the discoms across all the states had incurred the accumulated loss of 2.51 lakh Crores in 2012-13. India now has installed capacity of 1.58 Lakh MW with 31000 MW power in pipeline. Another 1 Lakh MW power would be added from solar power over the next five years. The root cause of this discoms health is the average gap between the power generation cost and the charge by the state discoms is now 82 paise per unit. The Coal India has around 8000 Crores in arrears from the discoms. As per the experts, the biggest worry is that no new power generation has been announced in past two years and low PLF as well as lack of clarity on bidding parameters for new UMPP has made investment unattractive for now.

(iv) As per the Editorial of Economics Times dated 29.05.2015, Mumbai Edition, there is no reason as to why there should be any cap on FDI as sectoral FDI caps of 26% or 49% or 74% have not till date achieved expected results. The country needs inflow of capital and overseas investors are also bullish on India's progress on long term growth. However rather than defining the areas where it will allow FDI, a better idea is for the government to have a negative list of few sensitive sectors where FDI would not be allowed and leave the rest open ended. It is a good idea to freely allow Foreign Investment in areas such as Retail. It will not only help retailers grow their operations but also encourage Foreign Investment in manufacturing by mid-size companies that are making good stuff but are too small to build their own distribution network. The remov-

ing caps alone is not enough to get fund flowing, we need better governance and proper regulation.

(v) In the progress of “Make In India” Campaign, vast number of bilateral and multilateral trade treaties between various trade blocks will find a difficult barrier to get entry into treaty bound trade blocks. Therefore, we need to have very strong and effective diplomatic initiatives to get entry into such regulated trade blocks.

(vi) Even after smooth sailing of “Make In India” Campaign and may look like apparently successful, there is already new trend started that developed countries are demanding “specially tailored trade pacts”. For example, Australian trade minister Andrew Robb will visit India for Indo-Australia CEO’s Forum next month for eight round in July 2015. Wherein Australia is insisting for “specially tailored trade pacts” for its dairy and wine sectors which are New Delhi sensitivities. According to the Australian sources, they want to enter in high end dairy product market, which India does not have expertise in. Australia is looking towards the fact that there may be cooperative activities in the dairy but there is no adequate storage systems.....may be particular areas in a dairy where Australia can contribute without being threatening. Canberra wants enhanced market access for auto components, textiles, financial services, pulses, wines, meat and dairy as against New Delhi wants market access for professional, textile, laser, auto components, pharma amongst other. However, while India is willing to cede the ground on some of the issues like auto components, high end wine and meat, it is unwilling to budge on issues including movement of natural person and agriculture.

## **CHAPTER - IV**

### **STUDY OF PROCESSES - RECOMMENDATIONS**

Make in India scheme has been launched to attract investment in India, mainly in the manufacturing sector. It requires streamlining of the tax processes and single window cum integrated clearance.

The main area of focus of this study report is the processes in Service Tax and Central Excise and how these need to be reengineered to create an enabling environment to promote “Make in India”.

This group has studied the following processes;

- **Registration**
- **Tax Payment**
- **Filing of Returns**
- **Audit**
- **Dispute Resolution**

#### **REGISTRATION:**

After any manufacturing facility is setup, registration process starts for commencement of actual production.

#### **PROCESS OF REGISTRATION:**

1. To transact business on ACES a user has to first register himself/herself with ACES through a process called “Registration with ACES”, This registration is not a statutory registration as envisaged in Acts/Rules governing Central Excise and Service Tax but helps the application in recognizing the bonafide users. This Registration can be done by furnishing a self-chosen user ID and e-mail ID. The system will then generate a password and send it to him by e-mail. The user then has to re-log in and proceed with the statutory registration with the Department by filing in forms A-1, A-2 or the case may be. Registration can be done for new assessee, existing assessee, LTU assessee and non-assessee through Registration Module.

### **1.1 Central Excise:**

After application of Registration, is filed by the applicant through ACES, the system instantaneously generates a Registration Certificate (RC) number after which the registration request goes to the AC/DC. AC/DC generates the RC and a message to this effect is sent to the assessee electronically. Depending on the option chosen by the assessee, the RC can be sent by mail or can be collected in person. The AC/DC then assigns it to the Range Officer (RO) for physical verification (PV) of the unit. The RO submits the PV report by choosing one of the three recommendations from the systems: (a) maintain status quo-verified, found OK, (b) re-issue the certificate based on amendment or (c) revoke the certificate. A message regarding physical verification is sent electronically. The assessee can view and take a print-out of this.

### **1.2 Service Tax:**

There are two kinds of Registration certificate for service tax

- (a) Registration for single premises
- (b) Registration for multiple premises

The registration of single premises is issued by the AC/DC of a division under whose jurisdiction it is covered. However, the registration of multiple premises is issued by the Commissioner.

### **Large Tax Payer Unit (LTU) Assessee/Client**

1. The consent form will have to be submitted manually by the New LTU assesseees to the jurisdictional LTU office which will be processed off line
2. The approved consent form will be uploaded by the competent officer of the Group LTU (GLTU) into ACES
3. Any new unit of an existing LTU, which applies for registration with ACES will be automatically attached with the LTU Commissionerate based upon PAN details in the registration form
4. As soon as the new or existing unit is attached with the LTU Commissionerate, a suitable intimation will be automatically sent by the ACES to the existing jurisdictional Commissionerate and the pending items of work will be transferred to the LTU Commissionerate
5. For existing LTU assesseees, the process of registration is same as in the case of existing assesseees.

### **SUGGESTIONS FOR IMPROVEMENTS:**

Registration process should be seen in light of chain of approvals required for starting a business in India. Quick disposal of registration request, which can be made only after FDI approval and setting up of factory/ service premise, will boost the confidence of the investor.



- **STAKE HOLDERS VIEW**

**ASSESSEE**

*“M/s Honda Cars India Ltd have suggested that the Registration Certificate should be issued on receipt of application from the Assessee, within minimum number of days and should not be kept pending for want of physical verification. Physical verification can be done subsequent to issue of Registration Certificate.”*

This aspect has been taken care in recent budget vide Notification No. 7/2015-Central Excise (N.T.) dated 1 st March, 2015 wherein registration shall be granted with two days of receipt of online application only with no physical document required. Physical verification shall be done subsequently within seven days on submission of necessary documents. All registration is to be PAN based only.

Although the Government has introduced ACES for improving tax payer services, transparency, accountability and efficiency in the indirect tax administration in India, yet the objective could not be achieved due to the following reasons:

- There is no information regarding any cases/dues pending against the party with any statutory authority as the same can be retrieved from PAN or DIN (Directors Id Number).
- There is no method of verifying outstanding tax liability before accepting surrender applications
- Insufficient bandwidth/network availability for ACES which hampers the pace and timely disposal of work.

## **Suggestions:**

- There should be option to upload the required document along with the application online. These documents should be digitally signed and shall be used for physical verification. It will make the registration process paperless.
- Integration of registration in ACES with other statutory IT systems pertaining to Make in India scheme, under single window concept

**1. Payment of Tax:** Self-Assessment, Easy Calculation, Less Interpretations, fewer exemptions, benefit of advance ruling, tax payer education, on line help.

### **a) Self-assessment / Easy Calculations.**

The assessee's are now allowed to self assessee their duty/tax liability and the same is paid through CENVAT account or in Cash and the returns are uploaded into ACES network by the assessee.

The assessee can calculate the duty liability through the reports generated from his private records and based on this the duty liability is paid. This leads to greater ease for the assessee to cross verify the same and have proper internal control.

### **Problem Areas.**

The assessee can misdeclare the classification and can also quantify lesser duty suppressing the sales and can make calculations mistakes either intentionally/unintentionally.

## **Solutions.**

- The department has already got robust audit mechanism and preventive/anti evasion mechanism. However, the skill levels of the officers should be improved in dealing with the data of the assessee for tax compliance and to use modern audit techniques, i.e, CAAP (Computer Assisted Audit Programme)- audit methods, study of data / financial accounts, more often to plug revenue leakages.
- The returns format should be very simple, but still should consist the basic data of values, exemptions availed and duty paid, cenvat availed and utilized.
- There should be inbuilt mechanism for cross verification / validation of data between turnover/rates of taxes/tax calculated and paid.
- Since the assessee is self assessing the tax payment, there should be Master file back up in the ACES database, for most of the cells of data being entered, so that the assessee gets tips for entering or various options to select for each cell of data being entered. e.g. like HSN reference, duty rates, exemptions for those chapters being selected.

### **b. Less interpretations, fewer exemptions.**

With harmonised classification of products, classifying the products for ascertaining the rate of duty to be paid has become easy with same rate of tax/duty on all services and products, classification and calcula-

tions of duty / tax has become easy, with fewer exemptions and common rates of duty litigations have reduced giving no room for interpretations.

### **Problem Areas.**

There are still problems in interpretations in the Service tax areas and less in Central Excise areas.

### **Suggestions:**

- All the notifications and circulars that are being issued should be automatically sent to all the assessee's email so that they can easily access the same.
- An SMS alert should also be sent to the assessee's, the changes in law/process/forms, that are taking place to those of them who desire to want such service.
- A Call Centre should be opened where the queries of the assessee's can be answered and where ever a query takes time to answer the same can be replied through an E Mail or SMS in a time bound manner.

This will lead to less litigation and greater compliance from the part of the assessee and also save a lot of time to the department.

### **c) Benefit of Advance Ruling.**

Advance ruling generates a prospective non-resident investor into a joint venture with a resident or a non-resident of their Customs, Central

Excise or Service Tax liabilities in advance. It helps to avoid long drawn out and costly litigations.

**Areas covered:**

Issues such as (i) classification of goods and services, (ii) Principle of valuation, (iii) applicability of exemption notification or (iv) credit of input duty/services, on which Advance ruling can be sought.

- Benefits of advance ruling are (a) clarity and certainty of tax liability (b) finality and thereby avoidance of protracted litigation (c) speedy decisions (d) in expensive process (e) transparency. If transfer pricing is also brought under Advance Ruling it would be better.
- Legal enablement to the assessee as the same ruling is from the Department. There should be an option to appeal against the ruling.

**d) Tax payers Education.**

Better tax compliance is possible only when the tax payer is properly educated about the liability of his tax, how to easily calculate without much external help, easy filing of returns and periodical updating of changes in tax law that is taking place.

Further, to help taxpayer and educate him on online filing of returns, refund claim, tax payment, CBEC has opened online helpdesk with phone numbers and email address which can be accessed by assessee's in case of difficulties and queries. Besides Learning Management Software (LMS) has been provided in the ACES website for guid-

ing and training the assessee's step by step process. Downloadable version of LMS is also provided on website. Further user manuals, frequently asked questions and power point presentation with brochures have also been provided on the website to help the assessee's use ACES.

### **Solutions.**

- Robust education system to educate the taxpayer, if required a 24/7 call centre to guide the tax payer with basic information.
- The FAQ's should be periodically be updated in Department website whenever there are changes in law.
- Tax payer campaign to be organised with the help of various trade bodies or local industry associations frequently, in going one step further specific industry specific campaigns could be organised for example , auto part industry, steel, cement, SSI units, etc. which would go a long way in compliance by the assessee and also reduces the litigation.

**B. Filing of returns:** Easy to use format, decide on optimum frequency, online, provide a system for simple query and correction and not every mistake to be treated as mis-declaration.

**Online filing.** Online registration, online submission of refund, rebate and drawback claims with online filing returns is reducing the (a) physical interface with the department and banks, (b) saves assessee valuable time and additional costs (c) reduces paperwork (d) system gener-

ated acknowledgements and (e) online tracking and viewing the status of documents can be had.

Enhanced Computerisation is leading to the production of more meaningful statistics and Data Management so that data generated can be utilised for much better policy making, revenue monitoring and administration improvement.

**Difficulties faced.** The network get blocked and the filing gets delayed and that too after several attempts, also the departmental officers some time find it difficult to access the ACES network because of such problems of connectivity, etc .

### **Suggestions.**

#### **Marco Level solutions.**

- IT infrastructure is now facing severe constraints in terms of computing capacity, lack of infrastructure for new functionality, frequent break downs of the network etc.
  
- Also these old legacy systems do not lend themselves well for the kind of agility and quick response that is needed by a dynamic tax system which seeks to introduce new services for taxpayer facilitation and internal user empowerment.
  
- There is a urgent need for redesign of business applications after an appropriate Business Process Restructuring (BPR) to move to a modern Service Oriented Architecture which could accommodate changes necessitated by policy considerations of centre infrastructure is

such that it could support this change, provided it is also suitably augmented.

### **Mirco Level Solutions.**

- There should be a 24/7 facility to file the returns, so that the assessee's can access the network any time they are free and upload the same.
  
- All the returns should be electronically filed and a facility to file the returns through facilitation centres/authorised persons, like registered Chartered accounts, Cost accountants, etc.

**b. Other - Filing of returns.** Filing of returns online through ACES has been made easy and simple. The assessee's under Service Tax are required to file half yearly returns only and Central Excise assessee's have to file monthly returns showing value and quantity of clearances, duty payable and payment particulars. However, online feeding of purchase as well as sales invoices will go a long way in verifying correctness of availment of credit and genuineness decreasing verification problems for the officers, filing of revised returns in case of mistakes is also provided.

**Central Excise :** As of now the data collection is being done periodically (e.g. once in a month), by way of mandating the manufacturing units to file statutory returns. The return contains only macro details and does not contain invoice level details. It is a practice very often, the field formations, either for replying to Parliament Question or for the purpose of analysis by CBEC, need to contact the Assessee and collect the information over the phone. This can be avoided by collecting granular data,

at the invoice level, from the assessee, which may even obviate the need for filing of periodical returns. In an age of information revolution, where the technology, both in terms of hardware and software is available, it may not be difficult for the assesses to furnish such information; it will also not enhance the compliance costs as most of the companies will have some structured system of capturing data.

**Service Tax:** In respect of Service Tax, the service providers are expected to file the return only once in six months whereas they can pass on the credit to the receiver of Services along with each and every invoice raised by them. It is hence imperative to capture the details of the activities of a business, preferably on a real-time basis, rather than wait for an abstract of monthly activities, which is reported twice a year, in the form of statutory returns. As in the case of Customs, both on the Service Tax front and on the Central Excise front therefore, there is a need to capture data at the granular level (transaction based data) on Real Time basis.

Further improvements in the field of computerisation on the line of international norms is required for better monitoring and utilisation in policy making and administration in taxation.

### **Suggestions for improvement.**

#### **Department side.**

- There is a need to capture invoice based information, preferably on real-time basis as the invoice is being used as a document for claiming credit by the Receiver of goods/services.

- Once the taxpayer is comfortable with the delivery capability of a new system the resistance to change can be overcome. Wide circulation of updated, accurate manuals and instruction booklets and more responsive, augmented helpdesks/service desks can also help in overcoming this challenge.
- Implementing invoice-level CENVAT verification, as part of the existing EASIEST project, so that a comprehensive revenue reconciliation system (both cash and Cenvat credit) can be put in place to assist the departmental officers in detecting fraudulent availment of Cenvat credit and preventing misuse of large scale Cenvat credit facility.
- The viewing should be made available to more officers at the Division and range level so that revenue collection can be effectively monitored.
- These include inclusion of Inspector level officers in the workflow, mobility solutions (so that the officers can record their comments/observations during physical verification of premises of new registrants and examination and sealing of factory-stuffed containers).

**Assessee side.**

- All the discrepancies found in the Returns file with the department should also be communicated through an Email or SMS to the management of the company.

- The assessee should be given an opportunity to correct the returns, if any errors are occurred within a set time frame so that the litigation can be reduced.
  
- If there is problem of uploading due to non availability of network in ACES, it should through up a report for the assessee so that unnecessarily they should not be penalised.
  
- The concept of pre populated returns can be brought into the existence as discussed above, if the invoice level data is being captured, then the system should through up a return based on the period's data available and the assessee should be able to verify the same and if any corrections are required due to debit/ credit note/ JV passed to write off etc and the same can be uploaded.
  
- There should be rating of the assessee's with regard to filing of returns, i.e, correct returns, without any corrections, on time filing and on time payment of duty etc and can be given a status like the ACP status in customs.
  
- There should be simplified returns format for small assessee's and once in a year they can file a detailed returns for the financial period.
  
- The auto verification between returns should be available so that the opening balances of previous returns can be auto verified and if there is a difference then the error report for correction should be available.

- On the tax payment side, instead few banks, which accept the duty payment, all the banks should be allowed to collect the duties and also the facility of Net banking, RTGS, NGFT should be allowed.
- All the payment should be authenticated with the returns filed and errors should be intimated to Division/Range/Assessee.

### **Conclusion.**

In the long run the better understanding of law and procedures of tax compliance by the assessee will reduce the manpower required by the department and cost of tax collection will come down and also the assessee can concentrate on his business without much cost on tax compliance. In the present day dynamic Information Technology environment, the changes should be periodically reviewed and changes should keep pace of IT Changes.

The administration /collection of Central Excise Duty/Service Tax and in future GTS in going through a sea change in terms of use of technology, keeping in mind the need of future of Central Excise, Service Tax departments and with introduction of GST the computerisation should be on the lines of international norms. International Workshops to train officers as well as to convince the benefits of IT. Computerization will minimise moral hazards through minimising interface between officers and the assessee.

### **Audit Process.**

Audit process is one of the most important functions in Central excise and service tax as the department has over the last decade or so

has given very robust thrust to this particular process. Audit process is nothing but the reconciliation process aimed at aligning practices with given statute, rules and procedures. It plays major role in improving overall compliance management. Hence Audit by default is also one of the prime sources of litigation. Therefore it is very necessary to understand as to how audit objections arise.

As is commonly seen, audit objection basically arises from reasons enumerated below (in order of their severity):

01. Ignorance of law/rules on the part of the assessee as a result of frequent changes therein.
02. Human errors resulting into unlawful benefits accruing to the assessee.
03. Grey areas in law/rules arising out of less than perfect phrasing of the law/rules resulting into endless litigation, many a time needless and perfectly avoidable one.
04. Intention to escape compliance of law, sometimes due to paucity of funds and lastly
05. Outright fraud cases

As is stated earlier paras , in order to have a less strife full environment, some audit specific initiatives needs to be taken which will help a long way in curbing objections of the nature mentioned in point no. 1, 2 & 3 apart from making the audit process less painful for the assessee. These are as under:-

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01. Integrated Audit covering Central Excise and Service tax should be resorted to avoid burdening the assessee with frequent audit intervention.

02. Policy of posting only experienced officers or officers having accounting and computer background in Audit should be followed strictly.

03. Coordinated audit is needed for large tax payers spread across the length and breadth of the country to arrive at uniformity in approach on any given issue.

04. past compliance records of the assessee needs to be factored for future audit selection. Positive compliance should be seen as a ground for reducing the frequency of the audit. Sense of reliance needs to be placed on the assessee.

05. The audit report utility, recently developed, for digitally capturing the audit reports prepared by audit teams is a centralized repository of information. It would help in building a comprehensive audit database, analyze area of non-compliance. This would provide vital inputs to tax administrators and policy makers alike and also serve as a tool for uniformity of stand taken on any given issue. Any divergent position taken on any given issue needs to be brought to the higher forum for reconciliation of approach. Uniformity in governmental action is must as variation causes frustration in trade and industry.

06. A comprehensive and simple and easy to operate software meant especially for the audit objective is the need of the hour. It should be programmed in such a way that audit could be done sitting in office without going to the assessee premises. Audit Plan containing the thrust areas of audit should be factored into while programming the said software. It should be such that the information needed for audit could collect directly into the portal of the audit thereby obviate the need for an intrusive audit and physical interaction between the department and assessee. Suitable training

be given to taxman to keep them abreast of the latest software to be handled by them. Minimum interference from taxman should be the essence of new policy initiative

07. A well-integrated IT system having template covering the parameters contained in the present Audit Manual with a system of ticking suitable options for every situations, enshrined in the statute, should be developed with active guidance and inputs from the audit field staff and representative from the manufacturing and service industry. The template is to be filled by the assessee as and whenever there is a new option to tick for. The template can have columns for the audit department to validate the entries made by the assessee. Once the validation process, which should be visible to the assessee, is over, the assessee can be rest assured of the line of action he has to adopt on any particular issue. It will ensure a certain level of stability and assurance to the assessee and prevent him from getting into unwanted financial distress because of future litigation and will help him remained focus on his business.

08. The department needs to shed its basic image of enforcement agency and actively pursue itself as a facilitating agent to cater the needs of the assessee to help them comply with the statute. A distinct organizational set up within the audit wing needs to be put in place to assist the assessee to make them acquaint with the law and procedures so that the foreign companies investing in the country do not feel lost in the newly entered tax regime. For this officers of suitable and sufficient experience, with supervisory structure, should be assigned to a group of units, to be designated suitably .He will serve as the single point of contact for all aspect of audit between the audit parties and the assesses.

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09. Propensity to litigate should be curbed. It can be achieved by effective legislation with greater explanations of the provisions and added provisos in Sections to cater to various specific situations found in commercial world. A clear and well drafted and articulated situations will greatly help in easing of litigative tendencies both in the field formation and from the assessee. Combined with this a non-intrusive and well enabled IT platform should be developed to conduct audit in a very transparent, transformed and uniform manner across the country.

10. Institutional mechanism should be put in place wherein after every budget or major changes; assessee should be suitably apprised of the changes in the law/procedures. Field staff should be properly trained to guide the assessee within an institutional framework.

By adopting these measures, objections of the nature stated in 1 ,2& 3 above can be reduced to a large extent.

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**Grounds for preparation of a Audit Specific Software for Distant Auditing (already explained in brief above):**

Minimum interference from the department in terms of Audit process should be achieved in such a way so as to minimize interaction of the assessee with the department. In this regard a well IT enabled audit platform should be developed to conduct audit in a very transparent, transformed and uniform manner across the country. A comprehensive and simple and easy to operate software is required to be prepared, which could collect the information needed for audit directly into the portal of the audit thereby obviate the need for intrusive audit and physical interface between the department and assessee for e.g. in the Audit

Plan of Central Excise assessee, the method of valuation adopted by the assessee is checked for its correct compliance. In this regard in the software a template containing all methods of valuation could be mentioned covering all the situations ranging from transaction value to various types of transactions visualized in the Central Excise (Determination of Value) Rules, 2000. Each provision should contain adequate number of examples analogous to that provision for added clarity. The software should operate in such a manner that the assessee can fill in his part of the information first time or thereafter whenever there is a change in the method of valuation arising out any fresh contract of sale or arrangement of clearances. The information so filled needs to be seen by the jurisdictional range authorities as well as the audit sections of the Audit Commissionerate for validation. If the method of valuation pursued by the assessee is found to be in sync with the law, a validating entry needs to be made by the respective RO/Audit section. This validation process can be done in a short period. Once this is done, the chances of audit objection coming up in the valuation will go down significantly and the requirement of an audit can be determined based on the information fed by the assessee. This method of filling up the information and its validation by the respective RO/Audit can be replicated in the case of all other aspects of the Audit Plan, namely Classification & Cenvat to name a few. A team of officers conversant with the excise and service tax valuation and representatives from the trade and industries can be empanelled to help the IT firm in formation of the software as their field experience will be helpful in making out a workable and practical software. This will obviate the need for an intrusive audit and physical interaction between the department and the assessee to a large extent.

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## **DISPUTE RESOLUTION IN THE CONTEXT OF MAKE IN INDIA**

To make the mega project “Make in India” a grand success, there is an absolute need for time bound, quick, inexpensive, certain, objective, dispute resolution system. In these directions following steps are suggested:

(i) A single window system should be introduced for all the projects operating under or coming under “Make in India” scheme. All such projects should be allowed to approach to advance ruling authorities i.e. already established or will be established having jurisdiction over issues and relating to Customs, Central Excise and Service Tax may be established. The ruling of advance ruling authority should be final and there should not be any appeal against it before any authority or court, save as only constitutional remedies.

(ii) In any other dispute involving property matters or taxation matters or consumer grievances etc., a fast track route with competent forum/court may be introduced where under daily hearings of the case may be conducted unless and until the case is concluded. In such scenario, only one adjournment should be allowed and only one appeal against such orders should be allowed. For this purpose, all necessary and relevant Acts may be amended to that extent.

(iii) As far as review is concerned, normally departmental orders are reviewed by the officers in a routine way, in interest of revenue and not justice often failing to maintain judicial discipline. Therefore, this existing system of review needs a review!!! Therefore, there is time to take a hard look at the situation in the context of “Make In India” and a new more judicious system needs to be designed. The CBEC has tried to re-

duce litigation levels by imposing monetary limits etc but the revenue centric and vigilance fear driven approach often leads to unnecessary appeals. The Dept must insist on judicial discipline at least of the CESTAT and High Court Orders. Considering that there are different orders by different benches of the CESTAT and HIGH COURTS, a centralized section in the CBEC HQRS should look at these cases and take one consolidated view. This will prevent different treatments in different jurisdictions.

(iv) On study of dispute resolution and tax matter; An India-UK Comparative Perspective, it is noticed that Her Majesty's Revenue and Customs (HMRC) in United Kingdom (UK) has put in place several mechanisms by which the confrontational approach to tax disputes has been rationalized through efficient case management, avoidance of procedural formalities and increasing opportunities for settlements and alternative dispute resolution. India can learn from this experience of UK so as to aim towards more efficient dispute resolution systems involving reconciliatory, consensual and informal processes. In light of the fact that the Government has recently set up a Tax Administration Reform Commission ("TAR Commission") to review the tax administration and dispute resolution systems in India. Its recommendations can be implemented by amending relevant statutes to give due effect to its recommendations.

(v) The Law Commission of India, in its 115th Report on Tax Courts, back in 1986, had stressfully cited the inordinate delay involved in the tax litigation process in India and had suggested several measures for the enhancement of the process so as to reduce erosion of the tax base.

(vi) Alternative Dispute Resolution Initiatives :

Although the Indian system has not yet completely embraced alternative dispute resolution for tax matters, there are a few initiatives taken by the Government to reduce the volume of pending tax disputes. Some of the initiatives have been listed below:

- (i) Advance Ruling Authority.
- (ii) Setting up a Settlement Commission.

Both these institutions need to be strengthened to discharge their functions so as to reduce down the burden of regular dispute settlement forums.

(vii) Certain other mechanisms which are not yet developed in India can be efficiently introduced and put into practice in effective manner by way of suitable enactment or amendments in the existing law. The processes can be :

- (i) Court mediated negotiations.
- (ii) Court mediated multilateral negotiations.
- (iii) Court mediated mediation to resolve the dispute out of Court.

## **CHAPTER - V**

### **STAKEHOLDERS FEEDBACK AND RECOMMENDATIONS**

#### **Stakeholders Feedback: E & Y**

#### **Reasons why people are not investing in the manufacturing sector from an excise and service tax perspective:**

- ▶ **Inverted duty structure across the supply chain is a dampener**
- ▶ The inverted structure arises due to the following factors:
  - ▶ Output Excise duty on finished goods lower than Excise duty on inputs and Service Tax on input services;
  - ▶ Inability to fully utilise Cenvat credit of Additional Duty in lieu of Excise ('AD') and Special Additional Duty of Customs ('SAD') against output Excise duty.
  - ▶ While certain measures have been taken in Union Budget 2015-16 to address the above issues, for example in IT sector, the inverted duty structure still continues in many sectors.
  - ▶ The second issue arises from the fact that for a company to offset 12% AD and 4% SAD, it requires substantial value addition. AD and SAD together with cesses form an effective duty of 18% plus.
  - ▶ This leads to significant accumulation of credits besides accumulation on account of capital goods and input services, resulting in increased costs;
  - ▶ This needs close examination and resolution either in the form of refunds or exemptions from SAD. In case of traders such SAD paid on

imports are refunded, for manufacturers the assumption is that credit is available but it is far from the truth.

▶ **Need to simplify Cenvat credits**

▶ The procedure to avail Cenvat credits requires simplification. Currently, too many restrictions and complexities in availing credits across capital goods, inputs and input services.

▶ There is an urgent need to simplify and allow credits in the chain without restrictions in view of GST being implemented soon.

▶ Simplification will avoid unnecessary disputes and cascading for the industry.

**Onerous process of realising export-led incentives**

▶ India is emerging as a key manufacturing hub for many sectors, for instance the automotive market and global small car hub. The manufacturing in India generates direct/ indirect employment and requires considerable investments.

▶ Duty drawback and Excise duty rebate arises on exports, both of which are significant. The process of realising both these export-led incentives is extremely onerous and time consuming, leading to significant cash flow issues for these sectors, which then affects the competitiveness of exported products.

▶ It is important that such processes/ documentation for claiming these benefits are simple and time bound to ensure no taxes/ duties are embedded in the export products.

**Fast track disposal of refund claims**

▶ There are various scheme / instances wherein industry is required to claim refund of taxes/ duties from the Government. This includes:

- ▶ Input tax refund on export of goods / services;
- ▶ Special Additional Duty (SAD)
- ▶ Extra Duty Deposit (EDD) in case of SVB
- ▶ In the absence of a strict stipulation within which the refund claims are to be cleared/ granted, the tax payers face great difficulty and harassment in obtaining service tax refunds from the field formation.
- ▶ It is recommended that the refund mechanism is streamlined to timely grant the benefit of refund to the tax payers.

### **Incentive to Manufacture/ Contrary judgments by the judiciary**

- ▶ Supreme Court passed a judgment earlier this year extending the benefit available to a manufacturer under excise to importers while importing a similar product from outside India.
- ▶ Basis this judgment, importers of mobile phones may pay CVD at the lower rate which was available only to a manufacturer under Excise.
- ▶ This challenges the whole idea behind “Make in India” to promote manufacture of mobile handsets in India.
- ▶ There are similar issues for other products where the incentive to manufacture has been diluted.
- ▶ Post this judgement, the Government needs to come up with a clear plan to incentivise manufacture by giving Cenvat benefits.

### **Control litigation**

- ▶ The recently tabled Tax Administration and Reform Commission (‘TARC’) reports have several valuable suggestions, which will go a long way to create the right administrative tax environment to incentivise investment and manufacturing. It is important that the implementation of these suggestions is quick and sincere.

- ▶ To put this in perspective, almost 90,000 cases were pending before various benches of the Customs, Excise and Service Tax Appellate Tribunals (CESTAT) across the country as on April 2014. Furthermore, according to the TARC report, amounts for which cases were pending as on March 2013 were INR 185.76 billion in Excise, INR 218.8 billion in Customs and INR 577 billion in Service tax, cumulatively adding to approximately INR 980 billion locked in litigation.
- ▶ Going forward, there is a serious need to control unnecessary litigation at low levels and also dispose cases at an increased pace at appellate levels including CESTAT.
- ▶ In future, issues should be raised purely on merits of law instead of routine challenges for revenue considerations. The recently introduced mandatory pre-deposits with automatic stay will in some way reduce the pendency at appellate levels to the extent of stay matters.

## **SEZ**

- ▶ The incentive to manufacture in an SEZ has been diluted on account of various restrictions placed on the supplies to an SEZ. The supply of goods to a SEZ no longer amounts to export as per the definition of export. This reduces the benefit of rebate/ refund of credits for supply of goods to SEZ.
- ▶ The supply of service to SEZ is also not considered export. The exemption works through a refund mechanism and subject to number of restrictions and dilutes the benefit, especially where an entity has both SEZ and DTA units.

## **Implementation of GST**

- ▶ The much awaited introduction of Goods and Services Tax (GST) is another key indirect tax reform that would go a long way in promoting the “Make in India” vision. This reform will incentivise Indian manufacturing through removal of cascading and simplifying the current complex indirect tax structure.
  - ▶ “Make in India” is an important initiative to promote manufacturing and generate employment, but its successful implementation will require a stable fiscal setup both at the Centre and State besides an industry friendly environment.
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## **State Holder Feedback (AIAM)**

### **India Tax Environment**

- More Revenue Driven – issue notices for achieving revenue targets
- Long drawn legal battle – Tax Court takes three years ; High Court – seven years ; Supreme Court – Ten years
- Extensive Open Audit years due to lengthy litigative process
- Loss making MNEs’ targeted for tax evasion – Valuation Issues in Excise & Service Tax with too much interpretations made available due to lack of Clear Governmental guidance

- The field formation sit in ivory tower and handle the tax assessments / audit without connecting with the business and without proper understanding of the way the business is conducted. Also, a pre-conceived notion prevail across the field formation that the tax payer is all for evasion and not in proper form
- Retrospective Amendments create uncertainty and makes tax policies very fragile

### **Specific Issues – Prosecution & Penalties**

- Statutory provisions in Customs, Central Excise and Service Tax enable the officers to launch criminal prosecution against the Company and also its officers responsible for the day-to-day affairs of the Company for tax evasion and the involvement of the officer concerned in the alleged evasion. However, it is used as a threatening mechanism initiated by way of Show Cause Notice. Investigative agencies like DRI and DGCEI misuse this provision during investigation against the Corporates (particularly MNEs and its officers).
- Penalties imposed on the individual officers holding responsible positions in the corporate office who do not handle day-to-day excise matters at the plant. It is more on account of purely interpretational issues for Revenue targets on paper.
- the words – “Attempt to evade” borrowed from Customs Act to be removed or clarified for prosecution & penalties , not below the rank of Principal Chief Commissioner.

## **Specific Issues – Settlement Commission / AAR**

- The Alternative Disputes Resolution Forums like the Settlement Commission etc. should be given more powers to waive the penalty and to waive either fully or partially the interest payable in cases where the Assessee come up with clean hands and seeks the settlement of the matter.
- Forums like Authority for Advanced Ruling to be expanded, should be made more powerful and hold more sittings to decide the issues raised by the corporates.
- A consortium of Commissioners should examine the orders passed by the AAR to make it final, instead of challenging every order before the High Court's /Supreme Court.
- A DRP like a body (of Direct Taxes / TP) be introduced in Excise & Service Tax to have faster disposal of the appeal matters in 8-10 months timeframe apart from Commissioner – Appeals where the matter is stuck for more than 2 years.

## **Specific Issues – Valuation Issues**

- Guidance Note with Illustrative examples on valuation issues for Excise and Service Tax matters would help the industry follow the same.
- Timely issue of circulars and notifications by the Board and its binding nature on the field formation should be in place, irrespective of difference of opinion.
- Connect with business fraternity to understand the business will iron out many of these long drawn litigations to an end easily and on a cordial note.

## **Specific Issues – Service Tax Refunds – SEZ / EOUs**

- All EOUs / SEZ were to receive refund of service tax input credit for their export of services. All the refund files are pending from 2006-07, particularly Bangalore Jurisdiction to be specific
- Refund , by itself is a big portfolio for the corporate tax team deputing many people to handle
- If we develop a model of input tax credit in line with Form 26AS of Income Tax for TDS deductions, it is easy for the department to validate and sanction automatically, except for the funds availability and release on FIFO basis.

## **A tax friendly environment – To do**

- Audit process should be once in three years on a computerized selection basis rather than visiting every year and seeking data for 5 years
- Litigation process should be separated from the jurisdictional commissionerate
- Once a quarter meeting at the taxpayer's place – Top 100 not below the rank of Assistant Commissioner to understand the issues and resolution / advise
- Routine clearances should be self-certified and not subject to inspection (like export containers)

## **What India needs to do/concluding thoughts:**

**(Ref. CII 2<sup>nd</sup> Global Tax Summit 2014: Enabling Make in India through effective Tax Reforms)**

The importance of equity, certainty and fairness are essential attributes for an effective and efficient tax system and they should be given due consideration in the making, administration and enforcement of tax laws. Unfortunately though, in recent years, a perception has been formed that India is not a very friendly place to do business. What startled people the most was retrospective amendment in 2012 to virtually negate SC judgment in the Vodafone case. There is an urgent need to change this image and the current Government appears to be committed to act towards this to usher in non-adversarial tax regime.

India has set up a Tax Administration Reform Commission (TARC) comprising senior government officials and private sector tax professionals under the chairmanship of Dr. Parthasarathi Shome, with an objective of bringing in credibility among tax payers and streamlining income tax procedures. The first report of the TARC that was made available to the public in June 2014 expresses an overwhelming need for fundamental reform in tax administration and contains various recommendations to achieve desired tax reforms. The report contains refreshingly significant recommendations for a “comprehensive” transformation of tax administration founded on accountability and recognition of the taxpayer as a “customer”. The recently released guidelines direct field officers to implement a series of taxpayer-friendly measures. These guidelines consolidate some earlier instructions and are aimed to boost

efforts in achieving the objective of furthering a non-adversarial and customer-friendly tax regime.

Moreover, in terms of TP assessment, Indian audits are perceived to be aggressive and have made various adjustments, which were seen to be inconsistent with the basic tenets of taxation. Introduction of APA and pragmatic response to the applicants will go a long way in controlling proliferation of tax litigation in the field of TP.

While there may be no objection to plugging the weakness created by e-commerce trading and while tax evasion and artifice can be dealt with sternly, discretion should be exercised in so implementing the law that there is no disincentive to invest in India. The growth of business brings many other economic advantages to the country. It becomes important to sustain the climate of confidence, clean environment and equitable approach in matters of tax administration.

## **CHAPTER – VI**

### **EXTRACT FROM TAX ADMINISTRATION REFORMS COMMISSION REPORT**

#### **Problems as identified by TARC:**

The Tax Administration Reforms Commission was set up with the single objective of recommend reforms exclusively in tax administration to enhance its efficiency and effectiveness, in context of global best practices. The Commission submitted its first report in May 2014 and since then has submitted its final report too. It undertook extensive dialogue with officers, industry stakeholders, experts etc. They have looked into almost each and every process of both direct and indirect tax including the organizational structure the human resource angle, the training and capacity building requirements. It's a very detailed and comprehensive report. Our Group looked at the recommendations of the TARC as contained in its Executive Summary viz :

- The current Indian tax administration is functioning in a vacuum; it has lost its purpose as revealed in its behavior, for its stated vision and mission are scarcely observed in its operational style.
- Its singular objective of protecting revenue without accountability for the quality of tax demands made is commonly believed to have severely affected the investment climate in India and in investment itself. This view reflects strongly the pleas, complaints and anger expressed by high and low taxpayers alike during the

TARC's stakeholder consultations. Thus, overall, the Indian tax administration is at its nadir.

- A fundamental and deep reform is urgently called for. There is no time to lose if investment is to be revived and its full potential reached, and an eventual tax revolt through capital flight or other direct protests is to be averted.
- A crucial deficiency is a fundamental lack of customer focus in the Indian tax administration, which is in stark contrast to modernizing and reforming tax administrations. The randomness and uncertainty in tax demands, the rudeness and abrasiveness in tax officer's behavior towards taxpayers, totally obviating the latter's stakeholder role, the inconsistency in demands made on similar tax matters without accountability, and the often poor quality of show cause notices have combined to project the tax administration in its poorest light in the eyes not only of the taxpayer but of society at large.
- The present structure of the tax administration system into the Boards— has led to a management functioning at a suboptimal quality and below its potential capacity.
- The risk averse behaviour of the tax administration has routinely led to infructuous tax demands on the taxpayer, often with the full knowledge that eventually such demands would not be able to withstand or pass the judicial process. In addition, a contrary view from the CAG on an AO's assessment is directed by the Boards to be assimilated through a 'protective demand' on the taxpayer, despite knowing that it is likely to lead to a dispute. The resultant number of disputes and the time taken to resolve these have surpassed heights that are globally incomparable. While raising a demand is praised, there is no punishment for infructuous

demands. The loser is the taxpayer in terms of time lost, advance payment required of the disputed amount resulting in deleterious effects on the cash flow of business, and the length of staff time and expenses associated with a long drawn-out dispute resolution process.

- The HRD or people function, or the approach to handling staff, is grossly inadequate. First, the pressure to meet exogenously imposed revenue targets, irrespective of the condition or prospects of the macro economy, has not only made it tough for making for taxpayers to make business decisions, it has also led to significant worsening in the officers' work environment. Second, the tax administration subjects its staff to an irrational practice of vigilance in which anonymous complaints against them are given equal status to direct evidence. Vigilance emanates also from external agencies, which is not common practice in many other tax administrations. The outcome of the vigilance process can linger for years, truncating the possibilities of success in many careers. This fear starts from entry to termination of a career. The result is extreme risk aversion.

- The TARC concluded that rapid rationalization of key internal processes is called for whether they be in the case of PAN – its generation and termination, or its wider rationalized use for more taxes – consolidated filing of returns for different taxes, harmonization of computerized processing at the CPC with that of the AO, making refunds of direct tax and indirect tax credit, risk-based selection scrutiny using ICT, or consistency checks across direct and indirect taxes in the case of search and seizure, and intelligence and criminal investigation.

- In the case of ICT, the TARC concluded that the Boards must commit themselves to full digitization and work towards building comprehensive systems, covering all key processes, in which everyone, from the top leaders to the frontline employees, works in a digital environment. In other words, ICT must get embedded in the DNA of the organization.

## **Recommendations of TARC.**

### **Customer focus**

- There should be a dedicated organisation for delivery of taxpayer services with customer focus for each of the Boards. There should be an exclusive Member in each Board for the taxpayer services.
- Officers and staff at all levels of tax administration should be trained for customer orientation. Further for people posted in this vertical, the training in customer focus need to be more specialized and intensive. This training should be appropriate to the areas in which such officers are deployed such as customer relationship, measurement of customer satisfaction, taxpayer education, etc. (Section II.6.a)
- In line with the international practice of spending 10-15 per cent of the administration's budget, a minimum of 10 per cent of the tax administration's budget must be spent on taxpayer services.
- Sufficient funds must be allocated to conduct customer research including, in particular, on customer surveys. (Section II.6.b)
- In redressing taxpayer grievances, the decision of the Ombudsman should be binding on tax officers. To bring independence and effectiveness to the office of the Ombudsman, nongovernment professionals should also be inducted in the post. (Section II.6.b)

- There should be regular stakeholder consultations on the issues of tax disagreements and tax law changes. The Commission recommends a permanent body for stakeholder engagement. The recent experience of the Forum through which many issues were resolved between stakeholders and the tax departments should become a continuing activity. (Section II.6.b)
- There should be a system for online tracking of dak/grievances/applications for refund etc.
- Continuous benchmarking of the tax administration, particularly in relation to delivery of taxpayer services, with that of other tax administrations should be done to highlight the area of focus. (Section II.6.c)

### **Dispute Management.**

The lack of accountability in the system is represented by infructuous demands raised by the tax administration with impunity as well as massive escalation, non-resolution and non recovery of such demands by global standards. Getting a handle on dispute management is crucial for retrieving stakeholder confidence and for saving much needed staff and financial resources of the tax administration.

The TARC recommends that:

- For clarity in law and procedures, a process based on best practices outlined in Section V.4.b should be followed. (Section V.4.b)
- Retrospective amendment should be avoided as a principle. (Section V.3.e)
- Fundamental approach should be collaborative and solution oriented. (Section V.3.d)
- Both the Boards must immediately launch a special drive for review and liquidation of cases currently clogging the system by setting up ded-

icated task forces for that purpose. The review and liquidation should be completed within one year and the objective should be to decide all cases pending in departmental channels for longer than a year as on the start date of the action plan. (Section V.6)

- To minimize the potential for disputes, clear and lucid interpretative statements on contentious issues should be issued regularly. These would be binding on the tax department. (Section V.4.b)
- The process of pre-dispute consultation before issuing a tax demand notice should be put into practice. (Section V.4.b)
- Disputes must get resolved in time as the times lines as mentioned for decisions in the respective enactments. The law should also prescribe the consequences of not adhering to the time lines, which would be that the case in question would lapse in favour of the taxpayer. (Section V.5)
- ADR processes, Arbitration and Conciliation should be statutorily introduced in both direct and indirect taxes legislations (Section V.4.f)
- The jurisdiction of AAR should be made available for domestic cases also. More benches of AAR should be established at Mumbai, Bangalore, Chennai and Kolkata, with the principal bench at Delhi. (Section V.4.c)
- The Settlement Commission should act as part of taxpayer services, and be made available to the taxpayer to settle disputes at any stage. There should also be an increase in the number of benches of the Settlement Commission. It should be manned by serving officers to enhance its accountability. (Section V.5)

### **The TARC recommends that:**

- The present permanent account number (PAN) should be developed as a common business identification number (CBIN), to be used by

other government departments also such as customs, central excise, service tax, DGFT and EPFO. A better regulatory system should be put in place to enhance its robustness and reliability.

- Both central excise and service tax should be covered under a single registration as both the taxes are administered by the same department and cross utilization of credit is permitted between central excise and service tax under the CENVAT credit rules.
- It is necessary to provide for de-registration, cancellation or surrender of registration numbers and PAN.

### **Tax payments.**

- Banks should be left to authorize their branches to collect taxes, and the present process of selection of banks needs to be purely standards-based and transparent.
- Payment gateways should be increased for better customer convenience.
- There should be specialization in scrutiny/audit work as recommended in Chapters III and IV of the report. Capability should be developed through training and re-training. The two Boards should also develop a standard audit protocol, with clear emphasis that the AOs must follow the principles of natural justice and respect the taxpayer rights to privacy and dignity.

### **Refunds.**

- Refunds should be issued within a strict time frame. There should be a separate budgetary head for refund of direct tax and indirect taxes in the annual budget out of which refunds should be issued so that there

is transparency. Adequate allocation should be made by the government under this head.

- Refunds sanctioned should be paid along with the applicable interest automatically as is done in the case of income tax and not on demand by the taxpayers. As in the case of direct taxes and customs duty drawback, the refund and interest payment should be directly credited to the bank account of the taxpayer.
- An easier and simplified scheme should be introduced for service exporters. The entire refund filing and processing mechanism should be online.

**The reason why we have chosen to highlight some of the major recommendation of TARC in this report is because, the report has dealt minutely with each process and function in both CEX and ST and come up with very valuable suggestions. These need to be looked into with sincerity. These are based on extensive feedback and research.**

## **CHAPTER - VII**

### **INTERNATIONAL PERSPECTIVE AND LESSONS LEARNT**

- Economies around the world have made paying taxes faster and easier for businesses by consolidating filings, reducing the frequency of payments or offering electronic filing and payment options. Some economies that have simplified tax payments and reduced rates have witnessed a rise in tax revenues. We visited USA and Canada during the MCTP. We studied their tax systems, particularly the GST in Canada. The USA does not have any indirect tax like CEX and ST at federal level, Only some form of sales tax at local levels.. However the reforms undertaken by the Govt in the IRS in USA was a huge lesson in change management and the need to transform. The way they did it was an amazing learning experience. I think the entire Indian IRS is ready for the same kind of radical reform. We learnt some basic lessons in improving Tax Administration, e.g
- 180\* Transformation from being Tax Centric to being Taxpayer centric.
- Simplifying taxes, tax structures, tax calculations.
- Making all the processes facile, electronic, and online.
- Ensuring fairness and equity in treatment.
- Educating the tax payer and treating him as a partner in national growth
- Encouraging voluntary compliance, by creating effective deterrents but also keeping cost of compliance low and keeping the process simple.
- Changing the mindset of the officers from suspicion to trust based
- Having a robust system of redressal of grievances

- Govt acting pro-actively in issuing clarifications and rulings etc to resolve disputes, areas of confusion
- Taking continuous feedback from tax payers about the quality and efficacy of the Tax services
- Officers' performance appraisal to include a rating on his/her ability to provide optimal services.
- Continuous capacity building of officers to enable them to perform well, phasing out the non- performers
- Inducting specialists, wherever required
- Focus being not on revenue target but on taxpayer service.
- Encouraging dispute resolution through constructive means to avoid litigation
- Having a proper mechanism to measure tax payer satisfaction or feedback about a particular jurisdiction, officer.
- Provide a single window solution

These were some of the key learnings from the US and Canada Tax systems.

## **Singapore**

Singapore, is ranked number 1 on the World Bank's 2014EDB index. Singapore does not have any natural resources and hence, its economy is heavily reliant on foreign investment. As such, Singapore's tax environment is generally friendlier to taxpayers, with a comparatively competitive corporate income tax rate, and a plethora of tax incentives for operations/activities in Singapore.

In addition to tax practices being relatively straightforward, to provide an even increased level of tax certainty, Singapore tax authorities are proactive in

issuing technical guidance on the interpretation of tax legislation. For example, when many countries struggle on the subject of taxation of “royalties” and resultant withholding tax in the hands of the payer, Singapore authorities have issued detailed guidance on how to interpret what a “royalty” is for the purposes of Singapore withholding tax, as well as guidance on the application of the foreign-sourced income exemption. These initiatives help to avoid protracted litigation, and make the tax process smooth and easy to comply with.

However, in the context of today’s globalised world and particularly in view of the Singapore economy’s dependence on foreign investment, Singapore is also careful to ensure that its tax policies are in compliance with generally accepted international tax practices to avoid being viewed/ and/or alleged as a “tax haven”.

(Source: Enabling 'Make in India' through effective tax reforms, CII Global Tax Summit 2014)

However, India’s tax regime has been traditionally viewed as extremely aggressive with fairly unreasonable positions adopted by tax authorities. It’s now time to change that.....

We as tax administrators have to spearhead these changes and bring about the transformation. The Govt will do its bit to make the process simple and ICT system efficient etc but our challenge is to change our mindset and that of our juniors. We have to stop seeing all tax payers as tax evaders. We have to recognize that many of them are sincere and genuine and believe in voluntary tax compliance.

In order to ensure this, we feel that our tax compliance processes should be re-engineered as follows:

- Registration of taxpayers: simple, common, fast online.
- Payment of tax ; online, self-assessment, easy calculation, less interpretations, fewer exemptions, benefit of advance ruling, taxpayer education, online helpline.
- Filing of returns: easy to use format, decide on optimum frequency, online, provide a system for simple query and correction. Not every mistake to be treated as mis-declaration.
- Provide clear circulars and clarifications on any contentious issue in a quick time bound manner.
- Reduce classification disputes, arbitrary change in settled classifications,
- Have a Fast, judicious dispute resolution system.
- Have consistency in tax laws
- Stability in tax administration, e.g. don't change classifications on a frequent basis.

## **CHAPTER - VIII**

### **CONCLUSION**

#### **Taxation – Recommendations.**

Taxation in India needs structural, operational and administrative reforms; the burden of tax compliance needs be reduced besides enabling e-filing of all taxes. Make Taxpaying easy and encourage voluntary tax compliance. Given the vast numbers, this would be more effective. In the previous chapters we have already seen the recommendations given by TARC, by various stakeholders, by CII etc. In the processes chapter we have already given process specific recommendations. To summarize, the following recommendations are being made, which are definitely capable of being implemented.

- Enable e-filing of all tax returns, ensure e-payment of taxes, simplify tax calculations, provide uninterrupted access 24#7, to online services especially in rural areas
- Give Tax Incentives to encourage manufacturing.
- The Goods and Services Tax (GST) proposes to subsume all indirect taxes levied in the country but is yet to be implemented. It could help address the shortcomings in the existing indirect tax system like tax cascading complexity and poor technological infrastructure along with high cost of compliance.
- Refund of all taxes should occur automatically and in a time-bound manner. The entire process should be online, somewhat like drawback. Interest payment should be automatic and not such as to create a fear factor in officers.

- Introduce a structured feedback mechanism to obtain input from taxpayers on the tax payers' services at every jurisdictional level. Make this as an important input in the performance appraisal of each officer.
- Introduce continuous capacity building measures in Tax administration, to ensure that the officers do not create bottlenecks due to wrong interpretations, lack of knowledge of settled case laws, settled positions.
- Advance Ruling authority should be strengthened and branches created in all major zones.

## **Taxation in India needs structural, operational and administrative reforms**

**Structural reforms** — reduce the number of levies and simplify their nature

**Structural reform** calls for:

- Clarity in policy and precision in drafting to help decrease the number of disputes.
- Clarity and precision in policy by aligning it to macroeconomic objectives.
- Stability and predictability to avoid frequent amendments.
- Emphasis on restricting practice of retrospective amendments.
- GST needs to be implemented urgently to meet the goals of consolidation and simplification while generating more revenues.
- Move away from the revenue bias, create a trust based approach. Make room for genuine errors to be overlooked.
- Elimination of 'dual levies' – e.g. software and IPRs.

**Operational Reforms** - Focus on getting the tax base right and ushering in certainty and stability:

- Ease restriction on the availability of Cenvat credits.
- Revisit issues like the Fiat India issue, which change established practices, give clear directives.
- Create a Classification Rulings Directorate in CBEC. Avoid frequent changes in classification at lower levels, across jurisdictions. Ensure uniformity in assessments. Divergent CESTAT decisions should be studied in the Board and a final view taken on which a binding circular should be issued. Waiting for a Supreme Court decision at times is very time consuming and leads to innumerable show cause notices.
- Implement – ADR's. Create norms, for negotiated settlement after any appeal stage, perhaps enhance the penalty proportionately.
- Encourage officers to close disputes under given provisions and avoid issuing show cause notices unless absolutely necessary. Adjudications must be minimized.
- Educate Taxpayers to ensure that they pay taxes correctly and promptly. Introduce institutionalized guidance, duty calculators, helpline, e-helpline etc.
- Build trust based relationships. Encourage field officers to have a 360 degree and continuous engagement with major taxpayers in their jurisdictions.

- Allow genuine errors to be pardoned and not unnecessarily penalized. Create a system of slab based penalties for encouraging voluntary tax compliance.
- All existing SCN's pending at various forums – call assesses, negotiate and settle.
- Delay in adjudication is a huge problem. Delay leads to lack of clarity and certainty of tax treatment. In such a scenario, Board must intervene pro-actively and resolve the dispute by way of clarifications and circulars. Then at least all the tax payers will be bound to follow the same practice. They can all collectively approach Supreme Court if they so wish.
- Board should actively issue clear directives for any new levy, new interpretation, new case law to prevent snowballing of issues.
- Despite number of judgments in the favour of assesses, officers still tend to invoke charges of mis-declaration, suppression in cases of pure interpretation, difference in classification etc. Differences of opinion cannot be termed as a deliberate attempt to evade taxes. In the first place the scope for such differences should be eliminated, this arises when multiple tax rates exist for similar items. This stems from a pure revenue bias and the fear of vigilance. This must be eliminated. Judicious officers must be rewarded. Officers who are pernicious and arbitrary should be marginalized in the system. Perhaps the Dept should look at segregating the adjudication powers from that of executive. E,g Placing a Commr Adjn under the DGDR to adjudicate the DRI SCNs, is not really fair. The bias will remain. The officer deciding the case should be truly independent. Likewise, as said in the earlier chapter, the activity of review should be meaningful and should be done with a

view to close the matter and not review simply because the order is against revenue.

## **Administrative Reforms**

- There is a need for consistency in approach — uniform interpretation and application of the law and judicial pronouncements.
- There is a need to adopt a trust-based approach — avoid not well-defined and onerous information requests during assessments.
- Equal incentives for the services sector — to bring them at par with manufacturing incentives.
- Greater consistency and accountability in tax administration.
- Increase stability in reporting — Avoid frequent changes in the return format/other forms
- Development of a strong IT backbone. IT infrastructure has to state of the art, capable of handling the large volumes. It should address all basic functions only, eg payment, registration, filing of return, refund rebate and drawback. These can all be carried out by auto validation on the system itself, eliminating the need for face to face interaction and hugely reducing the scope for corruption. It should leave complicated processes such as adjudication etc, to be done back end.

- Officers operating the IT infrastructure, at any level, should be well trained to carry out these operations.
- Provide certainty and clarity on interpretation of notifications, sections rules etc. Now that each zone is expected to have a Pr Chief Commr, a committee of three Chief Commrs, should be empowered to give rulings on any dispute which is placed before it and settle it. Any assessee should be able to approach this committee and seek clear guidance on any law, procedure, interpretation, including proposed show cause notices and seek clarity and finality.
- Considering the huge volume of show cause notices pending for adjudication, Govt has to take a one-time measure to reduce these. All the assesses should be called, cases discussed and a judicious view taken and case settled. This could be done by creating a team of dedicated officers in each zone or under the principal chief commrs. Composition can always be worked out. This would shortcut the other lengthy procedure. It should be completed in one year. Board can create a one-time fast track court for disposing all tax cases. Retired Officers and Judges could be involved.
- Taxpayers grievance redressal should be accorded Top Priority.
- To ensure timely disposal, staff augmentation is imperative. Given the huge shortage of staff in all grades esp. lower grades, day to day work is suffering. If you have 282 Units to audit and have only 20 officers to do so, how can you achieve your objective? This too leads to corruption and delay.
- Vexatious Preventive checks and searches etc should be resorted to in rare cases, not cases involving difference of opinion in assessments.

The 3 **C**'s imperative for any country to create a favourable, friendly and welcoming tax environment are – **C**larity in tax laws; **C**onsistency in their application and above all **C**ertainty of treatment.

***For all this to happen there is an urgent need to sensitise the entire tax administration about the 'Make in India' initiative. The tax administrators are required to change their mindset and approach, from enforcement to Tax payer facilitation.***

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## BRIGHTER SIDE OF MAKE IN INDIA

Astral Poly Technik Ltd, a pioneer in CPVC pipes in India and East Africa(Kenya), in collaboration with a US Company Specialty Process LLC has developed a product to replace galvanised iron pipes with new polymer having many advantages such as corrosion free, leaching free and can withstand the

temperature up to 93 Celsius degree so people can use the product for hot and cold water applications.

Astral entered in licensing agreement with Mr. Warren Buffett owned company Lubrizol Corporation having turnover of approx. 8 Billion US \$ and the company is world leader in CPVC product. Astral is the only company with whom Lubrizol has signed four product licenses with Indian Market – (i) Flowguard (ii) Corzan (iii) Bendable (iv) Blazemaster.

Not only that, Astral has one more collaboration with IPS Corporation USA under Royalty Sharing Agreement to manufacture solvent cement for CPVC & PVC pipe applications and is working very well in Indian Market and today “Weldon” is one of the most trusted brand in solvent cement in India. Such innovative product development or marketing arrangements will definitely success the “Make In India” Campaign.

Other initiative towards the “Make In India” Campaign are:-

(i) MPEDA is keen on producing “Make In India” Shrimps seed for supply to the farmers in the Andhra Pradesh, Kerala, Orissa and other states, thereby enhancing export revenue.

(i) Hitachi is investing 17 Billion Yen in areas of Information Technology, water, energy, transportation and health care as announced by the President & CEO of Hitachi on 26 February,2015. Now they have 31 businesses in India and number of employees is thirteen thousand. They are already focussing on selling of check up diagnostic equipments and advanced medical devices and also focus on elevators and escalators to cater to ur-

ban planning. They have an order of 58 elevators including 46 high speed elevators in Mumbai alone.

(ii) MSME and Samsung technical school is to promote the “Make In India” Campaign and is opening joint technical schools at fifty locations in India. Similarly, the Samsung new President and CEO for India announced that they will launch new 4G phones in India.

(iii) Huawei India opens new Research campus in Bangalore to give further boost to the India focused activities. The Chinese telecom gearmaker on 05 February,2015 unveiled its R&D Campus in Bangalore, its biggest outside China with investment of 170 million US \$.

## **CHAPTER - IX**

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## **ANNEXURE - A**

- (i) Value Chain and Competitive Advantage of McDonald's.
- (ii) The Value Distribution of Global Value Chain of most expensive inputs in the Lenovo Think Pad T43 Notebook PC,2005.
- (iii) The Value Distribution of key input in the 30 GB 5th Generation iPod,2005.
- (iv) The Value Distribution of key input in the 30 GB 3<sup>rd</sup> Generation iPod, 2003.
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- (viii) The diagram showing six Central Asian Regional Economic Cooperation Corridors. This corridor is extremely important for future growth of "Make In India". It will be like historical silk route but in appearance it would look like multipronged wheel.

- (ix) Share of Foreign Value added in Exports in selected Countries 2010.
- (x) The FDI by SWF,Commodity value by Region & by Sector /Industry - 2012.
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- (xviii) Examples of international standards for responsible investments in Global value Chain's.

- (xix) Development impact of Global value Chain, highlights of findings.
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