

Chapter 1: Introduction

1.1 Introduction

Entertainment sector consists of different segments under its fold such as television, radio, music, event management, films, animation and visual effects, broadcasting, sports and amusement etc. This sector has witnessed a strong growth in the last five years making it one of the fastest growing sectors in India.

1.2 Significance of the Sector

India had 168 million TV households in 2014, which makes it the third largest television market in the world. The number of TV households will reach 196 million by 2019 along with 175 million Cable & Satellite subscriber base, indicating 90 *per cent* penetration of TV in households. The size of the television industry, estimated at Indian Rupee (INR) 542 billion in 2015, will reach INR 1098 billion by 2020. Animation and visual effects is new emerging area in India which offers opportunity in both domestic and foreign market. The broadcast segment in India has around 800 satellite television channels and 242 FM channels. In the film segment, India maintained its position as a top film producer and has produced 1827 digital films in 2015. The Indian film industry is expected to reach INR 204 billion by 2019, up from INR 126.4 billion in 2014¹. The organized event management industry in India has grown at 15 *per cent* annually from INR 28 billion in 2011-12 to INR 43 billion in 2014-15. The Indian sports sector is experiencing a sea change with all-around developments initiated by the government such as 'Khelo India' and involvement of private sector by organizing tournaments through various leagues. The estimated value of the sports infrastructure market was INR 800 billion in 2016. Additionally, the sports sponsorship market in India grew approximately at 12.5 *per cent* on year to year basis in 2015 to reach INR 52 billion².

1.3 Why we chose the topic

The grounds for selecting this topic for performance audit were:

- As this sector is expanding very fast and is a significant source of revenue to the Government as pointed out above, we felt it was necessary to focus on this sector and see that the income tax is duly levied and collected from the business in this area.
- In the year 2010-11, we had conducted performance audit on "Taxation of assessee engaged in the Film and Television Industry"

1 Source: Achievements report (Media and Entertainment), Ministry of Information & Broadcasting

2 Source: EY report on -The Indian events Industry and KPMG-CII report on the business of sports.

wherein we had focussed only on Film and Television Industry. We, therefore, decided to broaden the scope by covering all the segments of the entertainment sector and conduct a comprehensive audit.

- This office conducted a performance audit on Entertainment Sector in Indirect Taxes Wing (Service Tax) during the year 2016-17 wherein we had highlighted that the Central Board of Excise and Customs (CBEC) needs to utilise the already available data optimally and evolve a system of using third party data to identify potential assesseees for broadening the tax base. Accordingly, we decided to cover these aspects from direct taxes side as well.

1.4 Objectives of the performance audit

The objectives of conducting the performance audit were:

- a. to study the effectiveness of the department's efforts to coordinate within the department and with other central/state government departments to identify the probable assesseees and to widen the tax base in the entertainment sector and check evasion of Income tax;
- b. to ascertain whether the systems, internal controls and processes are sufficient and robust to ensure effective assessment of assesseees of Entertainment Sector and to check loopholes/ambiguity in the existing provisions applicable to entertainment sector;
- c. to assess the efficiency and effectiveness of the Assessing Officers (AOs) in ensuring compliance with the provisions of the Income Tax Act/Rules in relation to entertainment sector.

1.5 Legal Frame Work

The assesseees engaged in the business of entertainment sector are governed by all the provisions of the Income Tax Act that are generally applicable to the different class of assesseees viz. Companies, Firms, Trusts, Individuals etc. Further, the Income Tax Act/rules provide specific tax incentives to the assesseees of entertainment sector. It provides deduction in respect of professional income from foreign sources in case of author, playwright, artist, musician and actor; being a resident in India. It also allows deduction in respect of expenditure on production and on acquisition of distribution rights of feature films.

Legal provisions relating to the taxation of assesseees falling under Entertainment Sector with relevant latest judicial decisions and circulars of the CBDT are given in **Appendix-1**.

1.6 Audit Scope and Sample Selection

The audit covered assessment cases relating to assessees engaged in key sub-sectors of entertainment sector viz. television, radio, music, event management, films, animation and visual effects, broadcasting, sports and amusement etc. The performance audit covered the cases of scrutiny assessment, appeal and rectification completed during the period 2013-14 to 2016-17. Wherever necessary, assessment records of previous assessment years in respect of the selected assessees were also examined.

The Director General of Income Tax (Systems), New Delhi furnished the Commissionerate-wise consolidated data of assessees associated with cable TV Production (code 901), film distribution (code 902), film laboratories (code 903), motion picture producers (code 904), television channels (code 905), others (code 906) and advertisement agencies (code 701) in respect of scrutiny assessments completed during the financial years 2013-14 to 2016-17. The selection of Commissionerates and units³ within each Commissionerate was based on risk analysis of consolidated data obtained from DGIT(Systems) and information available at regional levels specific to different jurisdictions. We compulsorily selected dedicated film circles/wards created in four states⁴ for selection of assessment cases. Within the selected assessment units under PCsIT/CsIT in 21 states (**Appendix-2**), a total of 6,691 assessment cases comprising all the segments of entertainment sector were identified for examination in audit based on the information available in the 'Demand and Collection Registers' maintained by the selected assessment units. Besides, we conducted detailed analysis in 24 cases to cross verify the correctness of the related party transactions.

1.7 Audit Methodology

- a. An entry conference with CBDT was held on 25 October 2017 wherein we explained the audit objectives, scope of audit and main focus areas of the performance audit.
- b. Collection of data and information relating to assessees engaged in entertainment sector was also sought from other sources to study the department's effort to make the assessment effectively.
- c. Results of the audit examination were conveyed to the concerned AOs for their comments and draft review reports containing audit observations (conveyed during the period August 2017 to

3 100 per cent corporate circles and 25 per cent non-corporate circles for each selected PCIT/CIT were selected by field offices except Mumbai office and 50 per cent corporate circles, 25 per cent central circles and 10 per cent non-corporate circles for each selected PCIT/CIT were selected by Mumbai office based on risk parameters and resource availability.

4 Andhra Pradesh & Telangana, Karnataka, Maharashtra and Tamil Nadu

February 2018) were issued to the respective CCIT/CIT by the field audit offices for comments of the Income Tax Department (ITD).

- d. We issued draft performance audit report to the CBDT on 07 May 2018 for their comments. Post receipt of the CBDT's response 04 June 2018, we held Exit Conference with CBDT on 20 June 2018 to discuss audit findings and audit recommendations vis-à-vis their comments.
- e. Considering the high percentage of non-production of records for the performance audit and the fact that non-production of records in certain PCsIT/CsIT charges was very high, the audit was carried out in two phases. Out of total of 6,691 cases identified during this performance for which records was sought for audit, 175 cases (**Appendix-3**) were not received from the ITD.
- f. We have duly incorporated the CBDT's comments together with the audit comments in the report.

1.8 Audit Findings

Out of total of 13,031 assessments made in the period by the ITD, we checked 6,516 assessment records (approx. 50 *per cent*) with assessed income of ₹ 47,979.44 crore during this performance audit. We noticed 726 instances (approx. 11 *per cent* of the audited sample) concerning systemic and compliance issues involving tax effect of ₹ 2,267.82 crore. Since a sample of 50 *per cent* has yielded errors of ₹ 2,267.82 crore, the ITD needs to have the remaining 6,515 cases audited internally. The ITD also needs to try to pin down the reasons for why there are such substantial proportion of errors and fix the identified systematic faults and responsibility where the errors have happened as an act of commission. Audit findings are discussed in subsequent chapters.