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Digital Leviathan or Efficient Governance? Navigating the AI Frontier in Indian Income Tax Administration

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Abstract:
AI in tax administration is a fundamental shift in the architecture of the modern state. In India, the 'Faceless Assessment Scheme', 'Insight Portal' and AI-based risk analytics are now a cornerstone of governance and a tool for revenue generation, reducing human arbitrariness, and detecting fraud. But such technological tools, while attractive, also raise fundamental legal and constitutional issues. In this paper, we assess the duality of AI in Indian income tax administration and its potential to become a "Digital Leviathan" (a huge digital entity which can be opaque, surveillance-based and coercive). Based on 'Technology Adoption Theory' and administrative law and the tenets of the Rule of Law, we explore the tension between AI efficiency against values of transparency and accountability, rational decision-making, privacy and natural justice. The article argues that the evaluation of AI in tax administration should not be based solely on revenue collection, compliance rates, and efficiency gains, but also on procedural fairness and taxpayer rights. It cites the risks as algorithmic bias, opaque "black-box" decision-making processes, a volume of data collection and a lack of human involvement in the quasi-judicial framework of tax administration. It should be clear that there is a need for a regulatory framework for AI-enabled tax administration in India, one that provides a "Human-in-the-Loop," or a framework that is technologically advanced and that is also legally sound in terms of data collection and accountability (i.e. auditable, accountable, explainable and responsible). This article has been a significant contribution to the discussion on digital governance, fiscal legitimacy, state power in the online era and state management with respect to digital governance and data.

Keywords: Algorithmic Accountability, Faceless Assessment, Tax Compliance, Predictive Analytics, Data Privacy.

1. Introduction:

The integration of artificial intelligence (AI) into public administration marks a watershed moment in the way modern states are organizing, redistributing power, controlling resources and risk, and exercising regulatory power. Across jurisdictions, it is becoming more common for public agencies to apply algorithms, machine learning, predictive analytics, data integration, and big data to make decisions that are now the domain of human bureaucrats. This transformation is often defended in terms of modernization: AI will be quicker, more consistent, more efficient, and able to better detect non-compliance in complex administrative systems.

Can algorithmic risk assessment be a rationale for and reviewable state action?

If large-scale data integration is implemented in the tax enforcement process, will the privacy and informational autonomy of taxpayers be safeguarded? Can a faceless and partly automated tax process preserve the principles of natural justice, especially the taxpayer's right to notice, hearing, and meaningful

opportunity to rebut adverse material? And, most importantly, who is responsible when algorithmic systems lead or shape coercive fiscal decisions that will impact citizens and businesses in a direct way? These are not merely small questions: they are also about the effect of digital governance on the rule of law (Citron 2008). There has been a lot of research into algorithmic governance and automated administrative systems and AI ethics, but the legal aspects of AI in tax administration have not been studied in India yet. There has been a lot of study about the technical potential of data analytics to avoid compliance and fraud detection, but very little on the normative criticisms of algorithmic decision-making in the field of public administration. The taxation sector is an area in which AI tools are interlinked with quasi-judicial functions, statutory obligations, and constitutional guarantees that can be seen as the basis of taxation in India. In India, the public has been more interested in digitization as a means of reform but little is being said to be done about the legal architecture around which automated state power can be managed. This article fills that gap in AI and AI in tax administration by analyzing AI and algorithmic systems in the Indian income tax administration on both a technology-driven and rule of law accountability level. AI in taxation needs to be evaluated not only in terms of efficiency gains, the impact of compliance, or reduction in corruption but also in terms of legal conditions that are required for legitimate public power to be upheld: transparency, explainability, contestability, proportionality, privacy protection, and meaningful human oversight, it says. It does not take a technophobic position. AI may indeed bring administrative benefits in a tax system of India's size and complexity. However, efficiency alone cannot be the basis for increasing automation of fiscal authority, as the book argues. So the central problem in this article is thus this: how can India reconcile the administrative efficiencies promised by AI-driven income tax governance with the constitutional and rule of law safeguards necessary to prevent opacity, arbitrariness, and rights erosion? This is not just an institutional problem for government design. It is also a manifestation of a larger question of state capacity and legal constraint that is not just about the digital age. And if left unresolved, algorithmic tax administration will eventually produce a system that is formally modern but substantively lacking in procedural justice.

To tackle this, the article proposes five goals

First, it describes the emerging architecture of AI-based income tax administration in India in terms of faceless assessment, data analytics, risk assessment, risk analysis and integrated compliance systems. Second, it analyses the governance justification behind these reforms, including efficiency, standardization and diminished human discretion. Third, it identifies the main legal and constitutional risks of algorithmic tax administration such as black-box decision-making, bias, privacy intrusion and the erosion of natural justice. It then puts these risks in the context of larger theoretical discussions about algorithmic governance, automated bureaucracy and the rule of law. Fourth, it proposes a human-in-the-loop regulatory framework for India that protects technological modernization without losing legal accountability and taxpayer protection.

The article is guided by the research questions:

- How AI is being utilized in the Indian income tax administration, particularly in risk assessment, faceless scrutiny and fraud detection?
- What are the risks to the transparency, privacy, natural justice, and accountability of AI tax systems?
- Is the current trend of adopting AI in Indian tax administration a sign of efficient governance, of a 'Digital Leviathan', or a combination of both?
- What legal and institutional reforms are required to ensure that AI tax administration is in line with the Rule of Law?

The main argument of this article is that AI-based income tax administration in India could enhance state capacity and reduce some kinds of human discretion; but unless it is embedded in a clear, auditable, privacy-preserving, and meaningful human review framework, it risks transforming tax administration

into an opaque and unbalanced form of digital state power. Algorithmic taxation cannot be legitimate just for better revenue return or speed of taxation. Tax administration is coercive and quasi-judicial, and AI needs to be based on rules that are fair, rational, and accountable. This article is theoretical, analytical, and policy-oriented. It covers four levels of inquiry. First, it traces the institutional and regulatory evolution of digital tax administration in India through policy documents, official frameworks, and administrative reforms. Also, it draws from the literature on AI in public administration, algorithmic governance, and digital bureaucracy. Second, based on constitutional and administrative laws, transparency, non-arbitrariness, privacy, and natural justice principles, it is able to assess the legitimacy of AI-based tax decision-making. Third, it contextualizes the Indian case in the context of state power change under the global context in comparison and international debate (e.g., from the OECD and international studies of automated administrative systems). This article can be seen as making three major contributions. First, it provides an intuitive view of India's tax digitization in terms of the tension that is inherent in efficient governance and the 'Digital Leviathan' (massive digital power). Second, by placing the debate in the context of coercive taxation, it allows us to move beyond an outdated vision of modernization and naive criticism of AI. And third, it connects to the growing literature on algorithm-driven governance, and it also places tax administration (a topic that has remained largely unexplored but is profoundly relevant) in the framework of the ‘rule of law’ and constitutional theory. It provides a normative model of 'human-in-the-loop’ tax administration: AI should be a helpful tool and not a decisive one in the context of taxation, and should help taxpayers in the issues of rights and responsibilities. In the era when states are increasingly governed by data, tax administration is one of the most important sites for assessing the future of lawful automation. India’s experience is particularly important not just because of the size of its digital public infrastructure but also because it illustrates a larger global challenge: whether the algorithmic state can honor the legal principles that underpin its authority. The answer to that question will not only shape the future of tax administration but also the constitutional nature of digital governance as a whole.

2. AI in Tax Administration:

A conceptual and global perspective: The rise of artificial intelligence in tax administration should be viewed in view of a wider change in the administrative state. In many sectors, governments are getting more and more reliant on data-driven technology to predict, classify, monitor compliance and enforcement. Tax administration is particularly important because it has three main characteristics that really make it a great target for algorithms: it is highly rule-structured, heavily data-dependent, and its learning from the way that compliance and deviation are done on a vast scale. As a result, tax authorities have been the first and most enthusiastic users of AI-based tools such as machine learning models, risk-scoring systems, automated case selection, anomaly detection engines, and integrated data analytics systems. But at the conceptual level, the concept of AI in tax administration is not simply a case study in how to implement advanced autonomous systems. In practice, we can use this term as a framework for a wide range of computational tools that process or structure administrative decisions. These include rule-based expert systems, machine learning models trained on historical tax and transaction data, predictive analytics for risk analysis of audit risk, graph analytics for identifying hidden connections between entities, natural language processing tools for document analysis and automated workflow systems that prioritize, flag or escalate cases for human review. In fact, in most cases, 'AI' is a combination of statistical modeling, data-matching technologies, and automated decision-making software that is embedded in layers of bureaucracy. But the difference is that legal and governance issues don’t take place only when machines make final decisions. They also arise when algorithms shape the way things are being represented, how people see things, what kind of suspicion there is in play and how people see things and also what they think of them (Citron 2008).

2.1 What does AI mean in tax administration?

In tax administration, AI means to put computers that can process vast amounts of structured and unstructured data. These systems are used for three main purposes: compliance management, enforcement and fraud detection. Instead of traditional tax administration in which tax authorities review the returns and audits conducted by human employees, AI-driven systems utilize data to identify underreporting, misclassification, tax evasion or suspicious financial activity patterns and the patterns that are detected through data analysis. This is not simply a general shift from a declaration-based to inference-based regime; it's a more profound transition. Tax authorities are no longer waiting for discrepancies to arise from data to be detected through a systematic review of existing data no longer, but rather they use algorithms to identify non-compliance according to deviations, correlations, behavioral trends and networked data relationships. This move to prediction-based approaches is key because tax liability is largely determined by statutory procedures, but it is also embedded in complex factual concepts associated with income streams and commercial arrangements, financial intermediaries and cross-border transactions. AI enables tax authorities to take a system-oriented approach to tax return reporting, and do not have to take a 'file-by-file' approach to tax return reporting but take a more comprehensive and system-wide view. Machine learning models can then be trained on past audit results and identify which returns have the most errors in terms of errors. Anomaly detection tools could detect unusual claims either in terms of claims, deductions or in terms of a mismatch between declared income and third-party data so that you can identify irregular filings. Network analytics can also reveal a group of related organizations where circular invoicing, fraud occurs, fraud occurs on a carousel basis. Natural Language Processing can help to interpret unstructured filings, correspondence, or legal documents. While final assessments are technically still done by humans, these systems are fundamentally transforming the way in which the bureaucracy conducts examinations, prioritizes interventions, and interprets risk.

It is therefore important to distinguish between three different layers of AI related to tax administration. The first is 'assistive AI', which helps administrative officers in making decisions, summarizing information, detecting patterns or issuing alerts. The second one is 'advisory AI', which helps in decision-making, in selecting cases based on risk assessment, or in recommending further study. The third type is 'determinative AI', where AI is directly involved in the decision-making process or the decision of what to do next (e.g. which data to report, which documents to be requested, and which tax liability to estimate). An 'assistive' AI will become 'determinative' if human officials increasingly rely on its results (Bullock 2019; Cobbe 2019) owing to institutional factors, technical complexity, or the perceived power of the machine to determine the outcome. It is why there is a need to study AI in tax administration, not only in terms of its technical level, but also in terms of bureaucratic need and in the greater decision-making environment. From this perspective, AI in taxation indicates that automation alone is not enough.

3. Predictive Analytics, Anomaly Detection, and Automated Scrutiny

Predictive Analytics, anomaly detection and automated scrutiny. The most important applications of AI in tax administration are predictive analytics, anomaly detection and automated scrutiny. Together, these are the backbone of digital tax enforcement today.

Predictive analytics is the use of historical and real-time data to estimate the probability of future events or behaviors relevant to tax compliance. Tax authorities use predictive models to answer questions such as:

- Which taxpayers are most likely to underreport income?
- Which refund claims are likely to be fraudulent?
- Which business entities are most likely to engage in false invoicing or abusive tax avoidance?
- Which cases are most likely to lead to high-value audit adjustments?

From training models on prior enforcement results, authorities can find variables associated with non-compliance and use them to build risk scores for current taxpayers. The advantage of predictive analytics

is that it can be used strategically to allocate scarce enforcement resources. In a system with millions of returns and only a few audit staff, it is impossible to have universal scrutiny. We use predictive models to target those where we believe non-compliance is a high probability. This is why audit productivity, fraud detection, and revenue recovery are high from an efficiency perspective. It also helps reduce random or ad hoc selection methods that may not always work or be susceptible to bias or corruption. But predictive systems also raise important legal and normative problems. They depend on correlations rather than direct proof, so they could cause suspicion based on patterns that are statistically associated with misconduct but not necessarily causally correlated with wrongdoing in a particular case. Furthermore, past audit data may reflect earlier enforcement biases, and those biases can be reproduced or amplified by model training. Anomaly detection. Anomaly detection is the detection of data that goes beyond what is expected, peer groups, or patterns. For tax administration, anomalies could be unusually high deductions, poor turnover ratios, sudden filing behavior, a mismatch between income and transaction data, or refund claims out of the normal ranges of statistical statistics. Unlike predictive analytics where historical data are labeled and supervised learning is used, anomaly detection can be based on unsupervised or semi-supervised methods to find outliers that had not been classified. This makes anomaly detection particularly useful in identifying new evasion, fraud, and suspicious business cases that are unlikely to be recognized.

Anomaly detection is particularly important in an ever-changing tax environment where evasion strategies are evolving rapidly with regulatory as well as enforcement changes. Fraudsters will be able to adapt to audit criteria, but they will not be able to hide statistically unusual behavior on a vast dataset. This makes anomaly detection an interesting tool for new tax agencies looking to detect previously unknown schemes. At the same time, anomaly is not the same as illegality. Business variation, sector-specific features, one-off transactions, or unusual but legal tax positions may also appear as outliers. A significant reliance on anomaly signals for administrative purposes may result in a large number of false positives with taxpayers being subject to scrutiny based not on irregularity but on statistical rarity. Where anomaly detection is poorly understood or weakly governed, the line between atypicality and culpability may get very blurry.

3.1 Automated scrutiny and case selection

Automated scrutiny works with systems that identify, categorize, or prioritize taxpayer cases for further examination. This can be done through automated notifications to the taxpayer and pre-populated alerts about problems, high-risk returns and/or a hierarchy of audit streams according to risk categories. In some jurisdictions, these systems are integrated into an integrated compliance system that covers filing data, third-party records, payment histories, customs information, financial data and corporate registry records. Tax authorities are moving towards what is widely referred to as “continuous compliance monitoring” in which scrutiny is no longer an intermittent phenomenon but a part of digital processes.

Automated scrutiny is also attractive because of its scalability. No longer are authorities forced to sort through millions of records and weed them out of non-compliant returns manually; they can have millions of records in seconds to generate prioritized lists of cases that are in need of action. This also makes differential treatment of taxpayer cases more consistent and less likely that there will be inconsistencies or anomalies in the case handling process. This filtration process may not come through in the final notice or order itself, but it often determines the nature of a taxpayer’s interaction with the tax enforcement mechanisms. Thus AI in tax enforcement is not restricted to the final assessment and is involved in the first stages of administration. Global trends in digital tax enforcement. The rapid adoption of AI in tax administration, which is the current global trend towards digital taxation, has a global impact. With the availability of new data, increasing digital commerce and cross-border financial flows and increasing political pressure to strengthen compliance and bring in more people in the civil service, tax authorities in developed and emerging countries are rethinking their approach to tax administration. In particular, the OECD has been one of the key contributors to documenting and driving these changes, as evidenced in its reports on advanced analytics and comparative tax administration practices. These reports show that tax

administrations are already investing in real-time reporting systems, data warehouses, collaborative compliance frameworks, e-invoicing infrastructure, network analysis tools and risk segmentation models. There are structural factors driving this global transformation. One is the digitization of economic life and the amount of data that tax authorities are now able to access has been increased considerably and data-sharing and analysis tools are being developed. Electronic payments, online shopping, digital accounting systems, banking records, customs declarations, and platform-based business models, e.g., are all machine-readable data that can be readily integrated into compliance systems. Second, cross-border concerns about tax evasion, base erosion and profit shifting (BEPS), and the concealment of business models from tax authorities abroad have forced officials to use advanced tools for sharing data and analysis in order to make use of data and analysis. Third, pressure on public finances, especially at the moment of the global economic crisis and the COVID-19 pandemic, and the need to generate more money in terms of revenue has driven the need for more efficient revenue mobilization. Fourth, more and more people and companies expect government services to be digitally accessible and accountable which is making it increasingly incumbent on tax authorities to modernize not only the enforcement mechanisms but the services provided to taxpayers.

The global movement toward digital tax enforcement has manifested in many institutional forms. Some countries have focused on real-time data integration, e-invoicing, employer reporting and transaction-level information systems.

3.2 Tax administration is a prime platform for the use of AI

It meets the legal system at the center of the legal system with its multiple streams of data, rules, big data processing and huge data infrastructure and combines them in a way that few other areas of public administration can. Why are tax authorities so prone to adopting computational governance? How do algorithmic systems fit so well into fiscal administration, and why are there so few barriers to adopting them? Tax administration is a rule-bound and standardized process. Tax law is codified. And while it can be a bit complex to understand, the majority of tax administration involves formal rules for financial and transactional information. Tax returns are filed in standardized forms. Reporting requirements are defined. Payment dates, deduction categories, invoice trails, third-party disclosures are all machine-readable. This level of standardization sets tax administration up for automation and data analysis. When legal and factual elements are set up and structured, algorithms can process them in a fast and efficient manner. Even if the final legal assessment is done by humans, most initial tasks like matching, flagging, scoring, checking, sorting and categorization for the tax are fairly automated. The tax system generates a huge amount of data. Tax administration today is based on a huge and constantly expanding amount of data. This includes self-reported returns, withholding returns, employer reports, financial transaction records, customs information, property records, securities data, digital payment trails and much more from other public databases and private companies. Tax authorities have access to one of the largest administrative datasets in the entire government system. In this context, AI is able to thrive because the data and pattern recognition capabilities are available and integrated. In tax, there's never enough data and the problem is data processing, correlation and prioritization. The same with data processing and correlation. AI is the best for dealing with such massive datasets. Tax enforcement is in essence selective. Tax administrations cannot keep track of all returns or transactions at once and they need to constantly assess and determine where to focus their attention. Fundamentally, this is a large-scale triage problem. AI has its appeal as it has a more efficient way to handle administrative work. Algorithms can help determine which cases are most likely to result in success and which to go through the usual procedures of tax administration by producing risk scores or anomaly flags and/or other predictive scores. AI is not a peripheral component of tax administration, as it is a response to one of the key challenges that the organization has to address: how to know how much tax non-compliance is a problem given all the filings and data available and the ever-growing world of taxes. Tax non-compliance is pattern-based. Tax fraud and evasion have some well-known patterns: recurring invoice mismatches, clusters of related shell companies, irregular refund chains,

sector-specific underreporting, sudden turnover or discrepancies between declared income and spending patterns. AI can detect such patterns in large datasets, in which a human auditor's knowledge of tax law would not be able to detect complex relationships. Graph analytics, network analysis and machine learning are particularly useful in situations where non-compliance is organized, held back by intermediaries and distributed among multiple entities.

States have strong incentives to invest in tax technology. Tax systems need not be seen only as an administrative reform but also as a public finance strategy. AI may thus benefit from political and bureaucratic support in taxation more easily than in other fields— especially in dealing with anti-corruption, formalization, or tax evasion.

3.3 Tax administration is a bit of both service delivery and power

Another reason why tax administration is ideal for AI is that it is a combination of service and enforcement, and the job of tax administration is to audit and penalize people. Tax officials provide support to taxpayers, assist with filing the tax return, send reminders to taxpayers, process refunds, and guide them. This dual function can lead to more AI applications than ever before. Chatbots can help with taxpayer services, recommendation engines can assist with compliance filing, anomaly detection systems can assist with enforcement problems, and predictive analytics can help with enforcement. The result is a comprehensive digital ecosystem where AI can be seamlessly integrated into different stages of the taxpayer-state interface. But it is precisely that combination of functional richness and power that makes tax administration such a worry. The very qualities that make it the perfect environment for AI—formalization, data abundance, standardization, large-scale decision-making—also present opportunities for overreach. Since tax administration is information-intensive and legally authoritative, algorithmic systems are often embedded within it even before any serious scrutiny is made. The results may be objective because they are data-driven, but the underlying assumptions are not obvious because they are technical, and their impact is not uniform since they are not only within formal procedural models; they are, in effect, above the line of control, that of decision-making in selection and prioritization. Taxation is a fertile ground for AI deployment and a test ground for the usual boundaries of the algorithmic state.

4. From Digitization to Algorithmic Tax Governance

From the taxation perspective, it is important to distinguish between digitization and algorithmic governance. Digitization means that tax administration becomes a digital process with online filing and digital records, automated acknowledgements, electronic payment processes and centralized databases. Algorithmic governance is not simply that. It involves computers to make predictions, classify risks and decide enforcement priorities and indirectly structure administrative outcomes. Tax administration has been digitized for a long time in procedural terms but what is new now are AI-based prediction and predictive regulation. This change is significant on the epistemic level for administration. In a digitized tax office, computers store and transmit information. In an algorithmic tax office, systems assess, rank, predict and make recommendations. The tax authority is no longer merely recording economic activity; it is modeling taxpayer behavior. That transition from recording to predicting is where the old debates about automation come alive. Transparency, explainability, fairness, proportionality and due process are all raised not only because machines are there but also because the assessment is done from the beginning to inform the government's enforcement. AI in tax administration is an aspect of a larger shift in administrative power in the digital age. It is the state's move toward analytics and predictability, not retrospective judgment. For taxation, it is to treat tax with efficiency and compliance. But it is also new risks: opacity, over-classification, surveillance, bureaucracy, which are kept from us with technology. The question is not whether AI should be part of tax administration, it already is. The issue is how we conceptualize it, how we limit it, and how we manage it? Now we turn to the next section from a global and conceptual perspective to the Indian perspective and discuss how these trends are now a fact of income

tax administration today in an era of digitalization, faceless processes, data integration and analytics-driven scrutiny.

5. AI in Indian income tax administration

AI's penetration in India's income tax administration didn't happen overnight. It is the culmination of a long history of digitization, administrative centralization, and data-based governance that has slowly transformed the relationship between taxpayers and the fiscal state. Over the past few decades, India's tax administration has moved from paper-based filing and local assessments to a technology-oriented compliance architecture with electronic filing, centralized processing, platform-based interactions, faceless processes, and more advanced data analytics. While AI is often mentioned casually in official and public discourse, its use in India's income tax administration is being implemented in a whole new way: through risk-based case selection, data matching, predictive scrutiny tools, and digital workflows. It has implications for the taxation of India's state in digital times. The evolution of digitization in India's tax system. The digitization of Indian tax administration is part of a wider fiscal reform and administrative restructuring. As there has been a number of reform efforts in direct taxation, mainly in the form of tax evasion, voluntary non-compliance and bureaucratic inefficiency (Kelkar 2002), the focus was on tax simplification, tax compliance, tax coverage, tax accessibility and administrative efficiency. Over the years this has become more and more technology oriented and its policy goals are very much linked to technology. One of the early developments was the use of electronic filing and centralized processing that has enabled tax returns to be filed and processed digitally and at a large scale. The Centralized Processing Centre (CPC) was thus an effective means of changing data-driven and data-driven assessment processes from paper-based assessment to data-based. CPC significantly sped up the return processing, refund issuance and preliminary verification, as well as was the digital platform for further development in the field of data-driven analysis (Government of India 2021; CBDT 2023). In addition to these changes, PAN-based ID was also incorporated into tax administration with large volumes of annual information returns (AIR) and subsequently the Statement of Financial Transactions (SFT) system, third-party reporting channels and taxpayer-facing online portals introduced to the system. With a growing amount of money and transactions recorded electronically, tax administration moved away from verification of return and towards data-driven compliance. The government no longer only had to look at the declarations provided by the taxpayer and it was possible to look at these declarations together with other data points. The digitization process was fast in India due to the increased digital public infrastructure. With a well-organized administrative ecosystem (Aadhaar and digitized banking, electronic payments, GST data architecture and extensive public databases), tax administration became more integrated and data-rich. And although income tax administration is not completely separate from all these other systems, digitalization has provided the government with a much stronger means of collecting, analysing and cross-verifying tax data. In this way, the evolution of tax digitization in India is not just a departmental reform and digitalization but a part of the government's platform digitization and data integration programs. In addition, digitization in the Indian tax system has never been a zero-sum game. Publicly, it has been presented as a reform to curb corruption, arbitrariness, and harassment; in reality, it has been presented as a means to ensure compliance and to make it easier for businesses to do business. Digitization was not only a technological revolution; it was also a political and administrative response to the institutional problems that arise from face-to-face bureaucratic interactions. So, the transition from the physical to the digital system was managerial and only served to validate the legitimacy of the process. This is most clearly demonstrated in the introduction of the 'Faceless Assessment Scheme,' which is one of the most significant efforts undertaken in tax administration to integrate digital processes and intermediary institutions. The Faceless Assessment Scheme. The Faceless Assessment Scheme is one of the most important innovations to Indian income tax administration. It aims to transform the assessment process by reducing the interaction of taxpayers with assessors and centralizing decision making in the digital era. It was initially introduced as an e-assessment initiative and was then extended to a 'faceless' framework to

reduce regional arbitrariness, 'rent-seeking' (seeking to make a profit off of illegal activities) and bring into common hands the assessment process. Faceless assessment is one of the most important changes from individualized tax decision making in India to digital administrative modularity. Instead of a single assessing officer being responsible for all aspects of a case, the work is spread across many specialized units (Assessment Units, Verification Units, Technical Units and Review Units) connected via a central platform. Taxpayer responses are submitted online, notices are sent through the system and all interactions are done in digital terms. Nor is the aim to merely digitize existing paper-based procedures, but to completely redesign the entire structure of assessment.

And administrative-wise, "faceless" is an enormous advantage. It reduces the tax administration's dependence on personal contact and geographic jurisdiction and discretionary interactions with officials. The objective is to prevent 'local capture' and unfair targeting and informal bargaining by anonymizing the interface and standardizing communication. It also provides centralized oversight and performance monitoring with more institutional consistency. This reform has been framed in public discourse around transparency, taxpayer convenience and anti-corruption objectives. But faceless assessment is not just about reducing interactions with people; it's also a procedural framework in which AI-enabled and data-driven systems can work better. With platform-based assessment processes in place, cases are assigned more efficiently, documents are examined, discrepancies are detected and scrutiny prioritization is easier to apply. In other words, facelessness is not just a procedural change; it is an infrastructural requirement to scale automation. The faceless system provides the data conditions for predictive administration by standardizing processes and converting interactions into structured digital records. The legal and institutional challenges we face and the need for solutions are increased. Even if faceless assessment was introduced to avoid arbitrariness in the workplace, changing the context from the interpersonal to a system-based platform may not completely eliminate it; it might just make things less transparent. And decisions about case selection, issue identification, case escalation and internal review will ultimately be made with digital criteria that are not available to taxpayers. Facelessness may remove one form of subjectivity, while increasing another: systemic opacity. Taxpayers will not have to feel like they are subject to the arbitrary decisions of a single officer and will have to work with a system with triggers, rankings and internal logic and systems, which technology may be able to hide. AI-enabled tax administration in India is centered on a platform for large-scale data integration; in particular, the Insights Portal is a key component of AI-compliant tax administration. The Insights Platform is designed as a data analytics and compliance management environment in order to identify high-risk cases, to guide intelligence-driven enforcement, and to improve profiling of taxpayers across datasets. This is a move away from intrusive and targeted tax administration to a data-driven approach to taxation that goes beyond basic return reviews. The Insights Portal is not just a database. It is an administrative knowledge base; it is a platform to add and cross-reference data streams for tax enforcement. Such data streams can be tax return filings, statements of financial transactions, TDS/TCS data, records of high-value purchases, securities transaction records, banking information, property transactions and other third-party information that can be made available to the tax administration. The platform will help tax administration to identify discrepancies, suspicious behavior patterns, hidden income and non-filers whose financial activities do not appear to be in line with their declared tax behavior. It is a platform that changes the epistemic basis of tax administration. In a traditional filing system, tax authorities are only reacting to what is declared. In a data-driven system, tax authorities are using a data-driven approach to build a complete information profile of a taxpayer through external sources. This transition greatly increases enforcement by triangulation of data from multiple sources. A taxpayer's returns can be compared to third-party reports, expenditures, transaction history and sector-specific regulations. The result is a 360-degree compliance visibility where a taxpayer's behavior is evaluated on a wide range of informational levels.

Integrated data platforms also can bring India's tax administration closer to the advanced analytics practices of other countries. Recent OECD discussions on digital tax administration highlighted the need

for linked datasets, real-time information environments, and analytical tools which can spot inconsistencies in data and prioritize. India's adoption of such systems is evidence of both domestic administrative priorities and a global trend towards data-rich tax enforcement.

But such platforms also raise governance challenges. The bigger the data collection is, the more likely it is to be compliant and the more likely it will be watched. Data integration can help to expose undeclared income and improve the equity in tax administration by curbing tax evasion; but it may also reinforce the asymmetry of information between the citizen and the state. When the State aggregates large volumes of taxpayer data into opaque analytical processes, data accuracy, proportionality, privacy, purpose limitation and taxpayers' ability to question erroneous information in the collected data are all threatened. So 'Insight' is about both the promise and peril of modern AI-based tax administration: it is an advantage for the government but also the problem with the government's opaque decision making. At the heart of AI-based tax administration in India are risk profiling and automated scrutiny. Since the Income Tax Department cannot individually review each and every return, it is increasingly drawing on data-driven approaches to determine which cases are considered as important for investigation. Risk profiling is the identification of taxpayers or transactions based on the likelihood of non-compliance. Automated scrutiny then operationalizes these classifications by issuing notices or conducting more in-depth investigations or starting specific reviews. Risk profiling is a tool for identifying trends such as discrepancies between declared figures and third-party data, unusual deductions made by taxpayers, or tax returns made while income is being generated and not declared in the public domain, high-value transactions, or anomalies associated with a sector or past non-compliance. These indicators can be categorized into various risk profiles and then used to determine where administrative attention should be directed. Some of these functions can still be done using rule-based systems, but the increasing volume and complexity of data makes machine learning and analytics-based approaches very compelling.

6. The Digital Leviathan: Legal and Constitutional Risks

The Digital Leviathan: Legal and Constitutional risks. The benefits of AI-driven tax administration are efficiency, uniformity and fiscal capacity. Taxation is a coercive job in general but the move to an algorithm-driven system brings on a whole host of legal and constitutional issues. And the problem is not technology failing; it is that AI can change the way people exercise their power in ways that we can't even conceive of, challenge, or even legally regulate. So digitization of tax administration could create a 'Digital Leviathan' that has far more information, predictive capabilities and enforcement reach but little transparency on how suspicion is created, decisions are made and mistakes are acknowledged. Tax law is often framed in managerial or technical terms but tax administration is never a matter of simple bureaucratic efficiency. It has direct implications for rights to property, privacy, reputation and procedural fairness that are legally protected. If AI systems are used in assessment, audit selection, compliance monitoring and fraud detection, their design and operational processes may be subject to legal challenges based on constitutional guarantees and administrative law. Legal risks are particularly high in cases where AI shapes who is selected for an audit, which evidence is prioritized, which cases are allocated and whether taxpayers are given sufficient explanations for any adverse outcomes. The benefits of AI on tax administration are not just the ability of the system to deliver good governance to the state but also how well governance is established in terms of legitimacy, fairness and accountability.

6.1 Algorithmic opacity and black-box decision making

The biggest risk of AI in public administration is 'algorithmic opacity'. In the case of tax administration, opacity is particularly serious when taxpayers do not know why they are being asked to be examined, how their "risk scores" were built, what data was used to assess them or why specific disagreements were considered administratively significant. AI systems are "black boxes" as their internal logic is either too complex, institutionally concealed, or both. This opacity is particularly acute in tax administration when

decisions on tax administration such as audits, assessments, and enforcement are not advisory but can lead to intervention by the government. In tax administration, opacity occurs at several levels. At first sight, opacity may be inherent in the selection process: a taxpayer may be given a notice without justification, or be 'flagged' for more scrutiny. Second, opacity may arise during review: the taxpayer may not appreciate how a particular piece of information was interpreted, how it was considered, what weight it had to carry, or the reasons it was considered suspect. Third, opacity may be embedded in the decision process itself: even if the final decision is made by a person (an official) who gives the final order or who writes the final order, the algorithm that generated that decision might be opaque to the general public. This opacity is very harmful because it is in breach of the law that public power must be rational, understandable, and comprehensible. In the context of the Indian Constitution, opacity raises fundamental questions linked to the 'Rule of Law'. The Supreme Court has made it clear that government action should not be arbitrary and that decisions made by government that affect rights or obligations need to be justified by well-founded reasons in our country. Reasons are not just formalities; they are fundamental elements of accountability, fairness and judicial evaluation. The rationale behind government action allows affected parties to understand why we do so, to appeal and to review it and thus, to limit the use of arbitrary power. If tax authorities apply algorithms, and if the risk assessment and decision-making process is not transparent and understandable to the public, not to mention the risk analysis or selection, then tax authorities risk undermining this basic principle. This is the case for tax administration, as the very act of investigating itself is very important. Being picked for audit or under heavy scrutiny is an administrative task, and it comes with costs of compliance, damage to reputation, financial pain and financial misery. Taxpayers without full transparency—and entangled in these processes through opaque analytics—will get an administrative system that's at once arbitrary and coercive. In this case, in fact, the opacity of algorithms does not just erode fairness but also hinders judicial oversight. Only when courts are able to determine the reasons that led to the decision to make it happen and whether all valid considerations were taken into account in the process can judicial action be taken. As a result, a "black-box" (opaque) tax bureaucracy poses a major threat to taxpayer participation and the institution's accountability. The problem here is not that the government has to make every technical detail of every model it uses public. There may be some confidentiality of enforcement strategies. But a legal deficiency is when opacity is so deep that it would be difficult to know how a particular taxpayer had been targeted, who identified those things that were problematic for someone's interests, and how those decisions might have affected the legal process. When opacity goes beyond administrative convenience, it is a constitutional defect. Bias and discriminatory impacts. The second major risk of AI-driven tax administration is bias; the impact of biased decisions (not only in tax law enforcement but also in the generation of biased, incorrect or incomplete results) on the tax-gathering process. AI systems are presented as systems to replace human decision-making, but the bias isn't even a part of the process. As research has shown, instead of eliminating bias, AI can reproduce it, amplify it, and even hide it. This risk is present in tax administration if risk scoring or anomaly detection systems are based on historical data and institutional norms. The Constitution is not only a document on the basis of equality but also a law against arbitrariness in government actions. Indian constitutional jurisprudence has gradually recognized that arbitrariness is antithetical to equality (as long as executive action is not rational, fair, or proper). If algorithmic selection systems are unfair and with no reasonable criteria to use for selection, not only technical error is likely, but arbitrary state action can also be challenged. This concern is made even more worrying when you consider the way tax administration is categorized and differentiated. Not all taxpayers are examined, but some are selected for more serious research based on risk assessments. And that differentiation is not illegal. What is wrong is when the classificatory logic is hidden, weakly validated, or based on proxies that create unjustified burdens. A taxpayer targeted for years because of anomalous but still legal behavior, sector-specific data distortion, or inherited model biases can be subjected to selective over-scrutiny that cannot be justified. The threat is not only in blatant discrimination. AI systems can impose disproportionate procedural burdens on small taxpayers, informal firms transitioning to formal systems, or those whose financial records will have data

quality problems more than actual evasion. In this way, algorithmic systems can compound structural inequities by assuming irregularity in data to mean that the provider is responsible. If the state thinks that what is statistically unusual is suspicious, lawful variation can be legally penalized.
From a legal point of view, the question is not whether all differential enforcement is unconstitutional. Tax administration always involves prioritization. So, that such prioritization is based on just, rational and fair criteria and there is a system in place to identify and correct discriminatory or systematic biased outcomes. AI systems that are opaque and poorly audited or not adequately tested for disparate impact can fail to meet that standard.

6.2 Privacy and Informational Overreach

The rise of AI in tax administration is in part a result of the huge amount of data collected, sharing the information on several platforms, and the rise of compliance analytics. It is not only about data use but about the privacy issues, and these are all more acute when tax authorities combine data from multiple sources to build up detailed profiles of the behavior of the taxpayer. AI logic is built on large data sets, while the constitutional right to privacy requires that the State's access to personal data be legitimate, correct and protected by data privacy laws. Indeed in taxation, data might be tax returns, banking records, capital market transactions, property records, employer reports, financial transactions and other third parties. Such integration will most certainly enhance the State's ability to detect undeclared income and improve tax compliance. But it also creates a very asymmetrical information environment, in which the State can discern patterns in an individual's economic life that go beyond what the taxpayer gives in his tax returns. In this opaque environment, privacy is connected to due process. In India, the constitutional importance of privacy was established in the seminal case of Justice K.S. Puttaswamy v. Union of India (2017), the Supreme Court made privacy a fundamental constitutional right and one of the fundamental values of individual liberty under Article 21. Any breach of privacy, in Puttaswamy's opinion, had to be done in line with a genuine state objective, proportionality and procedural protection. Tax administration is a legitimate government objective, but deep data extraction and algorithmic profiling should also be governed by the same constitutional framework. The pursuit of revenue does not mean that all data processing is good (and not so if the data will be used). A proportionality framework is in place for AI tax administration for a number of reasons

- Is there a legal basis for the collection and processing of these specific types of data?
- Do less intrusive alternatives exist?
- Are there safeguards in place to prevent misuse, data retention beyond necessity, secondary uses or unwarranted surveillance?
- Can taxpayers know which data is being used against them and challenge any inaccuracies?

These are not abstract problems. And if government agencies are using vast amounts of personal and financial data without full transparency, the risk goes beyond unauthorized disclosure to include excessive government profiling. Taxpayers do not lose all privacy rights just because they have financial obligations. Tax administration is surely an area where government agencies will be legally obligated to disclose and verify data. But constitutional privacy rights require that this kind of disclosure is legally limited and constrained. AI systems will pressure governments to collect data where they see it and analyze it. This is a classic example of informational overreach: government agencies are more interested in data, but not because every single data point is important for the future, but because aggregation provides a predictive advantage. In constitutional terms (in the context of data concentration), the mere fact that we have a predictive edge is insufficient to justify all data collection in the future. Natural Justice and Procedural Fairness. The most important legal issue to be addressed with AI-based tax administration is the compatibility of AI with natural justice and procedural fairness. Tax administration is often a quasi-judicial activity (issuing notices, interpreting facts, examining evidence, determining liability, and so forth). Natural justice (right to notice, right to be heard, the right to respond to adverse findings) is necessary to

make legally sound decisions. Algorithmic systems are not the end of these responsibilities; in fact, they make them more important.

The first point to be paid attention to is notice. A taxpayer needs to be informed not only of the imminent action but also of the specific issues to which they need to respond. If it is an algorithmic flag or data mismatch or risk indicator, fairness can be achieved only if the taxpayer is aware of the nature of the problem. Just a notice without any reason for such concern may not be sufficient to get an appropriate response, especially if the taxpayer has to explain differences due to third-party information or the inaccurate data that is detected by automated systems.

The second issue is the right to be heard. A hearing is important only if the taxpayer is given a genuine opportunity to hear the case against them and to come up with a response. Automated systems can even undermine this right (e.g. if risk classification is not clear; if the outcome of the model is an unknown to the taxpayer; or if procedural interactions are limited to a set of digital prompts that are not clear and do not allow for time for a proper response). In short, taxpayer participation is formal but lacks substance. This approach may satisfy the requirement for a hearing, but does not provide the taxpayer with the information needed to make a sensible response. The third issue is what one can do to respond to adverse material. Indian administrative law has long recognized that, in the interest of fairness, it is necessary to disclose any material used against an affected individual (except, of course, with these rarest cases). If tax officials use data integration, profiling tools, or anomaly analyses generated by AI systems, the taxpayer should have a meaningful chance to challenge such material. In short, algorithms can only produce unquestioned evidence in the form of technical validity. This raises a higher level of concern: do automated administrative systems undermine participation when there are no formal procedural lapses? A fully digitized process may meet notice and response requirements, but it will hollow out the real life of the taxpayer. And so if the taxpayer receives a notice, replies, and eventually gets an order, he will never really know why his case was chosen in the first place, what the risk assessment was like, or what the cause of the decision was. Such a system is not only inefficient but also antithetical to the essential principles of natural justice. Procedural fairness cannot be achieved by just using the digital world; it must be clear, it must be comprehensible, and it has to be capable of refutation. Danielle Citron's conception of "technological due process" is certainly applicable here. According to Citron, when procedural safeguards are not adapted to the realities of computational governance, automated administrative systems can do much harm (Citron 2008). The same principle applies to tax administration too: procedural rights must be extended in order to address not only allegations made by humans but also the conclusions that automated systems make. So if AI alters the basis for suspicion, then procedural law must allow taxpayers to challenge it. An Accountability Gap. The last major issue is accountability. As AI systems are increasingly integrated into tax administration, it is difficult to know who is responsible for errors, biases, mis-targeting, or data collection violations. The accountability gap is created when decisions are made in software systems, data pipelines, contractors, analysts, and administrative departments which mask or obscure responsibility. In such situations, harm may be real, but the chain of accountability is broken.

This is a serious issue because public law is at bottom a matter of identifiable responsibility. Administrative decisions need to be placed in the hands of the people who can justify, correct, and examine them. If a taxpayer is misclassified in a wrong way due to poor data integration, model drift, poor training data, or software design choices, who is responsible? Is it the official who signed the notice? The department that procured the system? The vendor who built it? Or the analysts who set the thresholds? AI without clear mechanisms of responsibility risks becoming a mechanism for splitting up blame.

Gaps in accountability also make judicial review more difficult. The courts have the power to review administrative decisions, but they may be unable to do so in the context of opaque technical systems that

are not fully reflected in the official record. If a taxpayer wants to challenge an audit or an adverse finding made on an algorithmic basis, the court will encounter a variety of difficulties: the lack of transparency, technical complexity, and confidentiality issues, or the absence of concrete evidence of how the system affected the outcome. And in such situations, judicial review would be very superficial.

7. Comparative perspectives

From a comparative perspective, India's case is even more important. Countries around the world are using data analytics, intelligent decision making, and AI-based enforcement systems for taxation and other administrative functions. All these examples demonstrate the importance of algorithmic governance, as well as the obstacles that come with not having the capacity to build a strong system.

7.1 HMRC and Data-Based Compliance

As a government agency, HMRC as well as the UK's HM Revenue and Customs (HMRC) has also started to embrace digital compliance solutions such as advanced data analytics and risk-based targeting. The "Connect" system is frequently cited as a prime example of big data analytics in the UK, which is used to detect hidden income and undeclared assets, as well as to identify suspicious taxpayers and transactions. This underscores the administrative importance of combining different data sources as the basis for building up enforcement capabilities in the UK. But it also raises familiar concerns of transparency, the extent of surveillance, and how taxpayers can view—or challenge—the assessment made by those algorithms. The Childcare Benefits Scandal—or, in fact, the Dutch Childcare Benefits Scandal—is one of the most alarming public policy nightmares of algorithmic governance in public administration. These anti-fraud systems were unfair and discriminatory; they hurt and killed many people. And although the case is about welfare management rather than income tax, the lessons are still relevant today: opaque risk profiling, automated suspicion, and lack of recourse to redressal mechanisms can breed institutional injustice in the name of administrative efficiency. And what the Dutch experience has taught us is just how punitive and discriminatory data-driven public administration can become when accountability and fairness are not embedded within the system.

7.2 Australia: Robodebt.

Australia's Robodebt scheme is a good example and a cautionary tale for us. Robodebt used automated debt calculation and recovery systems in welfare administration and resulted in many unlawful claims, procedural injustices, and both judicial and political opprobrium. Robodebt exposed the perils of assuming automated determinations, which do not have a legal basis, clear verification, and no human intervention, are administrative authority. In tax administration, the message is plain to see: if the government is not to make legally sound, individualized assessments of taxpayers, but to accept system-generated suspicions or liabilities as fact, large-scale automation can result in large-scale legal lapses.

7.3 OECD Guidance

The OECD's work on advanced analytics and tax administration is evidence of the worldwide popularity of digital tax enforcement. Analytics serves as a tool not just to control compliance and to detect fraud but also for administrative efficiency. The OECD is also more and more aware that trust, governance, high quality data and responsible implementation are at the heart of this effort. These are crucial because they demonstrate that the question is not whether digital tax enforcement has gained global acceptance but rather, under what governance conditions it is legally valid.

7.4 EU AI Act

The EU AI Act provides a risk-based regulatory framework for AI systems, which is an essential element for tax administration in the public sector. Depending on the design and context that is used, the strategy may differ, but this Act is a historic step forward in regulatory evolution: AI in public administration

(especially rights and access to public services) will require new obligations in terms of transparency, documentation, human oversight and risk management. For India, this EU perspective is a useful reference point not just as a model for blind imitation, but also as concrete evidence that the use of AI in the public sector is coming to be viewed in the legal arena and is not simply administrative experimentation. It is of great relevance to India to compare these scenarios. But since this transition is global in nature the legal problems involved are more than theoretical and regional. It will be India's experience at the very center of the global discussion about how democratic nations can modernize their administrative governance without allowing opaque and less accountable forms of digital power to occur without any kind of oversight or control. The above analysis shows that AI in tax administration cannot only be evaluated in terms of its performance. It must be based on the rule of law, public power must be administered in a manner which is not biased, intelligible, and transparent. And this is especially true in taxation where the state exercises coercive power and where decisions taken by the state affect property, livelihood, privacy and legal status. In our perspective, there are at least five dimensions of rule of law. First, there is legality: AI systems that coerce and affect rights should be governed by a legal basis, not just by administrative convenience or by obscure internal systems. Second, there should be no arbitrariness: tax compliance algorithms should be founded on rational, relevant and consistent criteria. Thirdly, there should be a kind of procedural fairness: taxpayers should be given notice, a reason, and an opportunity to contest what is said to them. Fourth, there is accountability and oversight: decision making by AI systems needs to be transparent and subject to effective administrative and judicial scrutiny. Fifth, "proportionality" should be taken into account— especially where data collection and profiling are a threat to privacy and informational autonomy (Fuller 1969; Solum 2004). The point is that tax administration is not a managerial domain but a kind of state coercion under the law. To collect taxes the state can demand information, audit operations, impose penalties and even sanctions. These are a lot of ordinary public authority. AI does not change the legal nature of these powers; it changes the method through which they are used. No matter how technologically advanced it is, coercive public authority does not turn into a legal process with no legal legitimacy. So the main point of this article is that technical efficiency can't be taken as a substitute for legal legitimacy. A tax system— fast, standardized, or data-driven— is not going to be 'Rule of Law' if taxpayers are not able to see the decisions that affect them, to challenge them, to point out mistakes in the decision making and to find out who is actually responsible for the error. Efficiency is, of course, a very important administrative tool but in any constitutional framework it must be done in the context of legal legitimacy and fairness.

A legally sound AI tax regime has to satisfy a standard checklist such as:

- ~ Lawfulness: Can AI be used for a specific tax function, as outlined by statute or through a publicly articulated administrative framework?
- ~ Explainability: Can the taxpayer explain why a specific choice, assessment or decision was made?
- ~ Contestability: Does the citizen have the right to challenge any bad information from algorithms or data?
- ~ Human Accountability: Is there a government official or entity responsible for the outcome?
- ~ Proportionality and privacy: Are data collection, aggregation and profiling appropriate, proportionate and accompanied by adequate safeguards?
- ~ Auditability: Can the system's operation be reviewed for errors, biases and unlawful discrimination independently?
- ~ Judicial Reviewability: Can courts and appellate bodies have sufficient data and reasoning to rule the case for the validity of the action?

Without these conditions the AI is likely to expand administrative power at the expense of constitutional legitimacy. Where both conditions are met technology can combine with the rule of law. The difficulty isn't banning AI in tax matters but bringing it under constitutional control.

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