

**CHAPTER – 3**  
**COMMERCIAL TAX**

## CHAPTER 3 COMMERCIAL TAX

### 3.1 Tax administration

The Principal Secretary, Commercial Tax Department (CTD) is the administrative head of the Department at the apex level. The Department functions under overall control of the Commissioner of Commercial Tax (CCT) assisted by a Director and Additional Commissioner. The Department is divided in five zones, each headed by a Zonal Additional Commissioner. These zones comprises 16 divisional offices headed by divisional Deputy Commissioners (DCs). Under these divisions, there are 84 circle offices and 19 Regional assistant commissioner offices headed by the Commercial Tax Officers/Assistant Commissioners (CTOs/ACs).

### 3.2 Trend of receipts

The trend of revenue receipts against budget estimates of Commercial Tax Department from revenue heads Taxes on sales, trade, etc. and Taxes on goods and passengers is mentioned in **Table 3.1**.

**Table 3.1**  
**Trend of receipts**

(₹ in crore)

Year	Budget estimates	Actual receipts	Percentage of variation
2012-13	16,150.00	17,251.33	(+) 6.82
2013-14	19,140.00	19,228.59	(+) 0.46
2014-15	22,400.00	20,822.35	(-) 7.04
2015-16	24,500.00	22,890.91	(-) 6.57
2016-17	26,200.00	26,366.16	(+) 0.63

*(Source: Finance Accounts and Budget Estimates of Government of Madhya Pradesh)*

Audit observed that the MP Power Generating Company did not pay entry tax on purchase of coal from April 2007 to March 2017 and the matter was under consideration with the High Court. Finally, a meeting was held on 25 August 2015 between the two ministries and it was decided that the MPPGCL would make payment of Entry tax of ₹ 875.13 crore. The company had paid arrears of ₹ 12.90 crore during 2013-14 and ₹ 590.09 crore during 2016-17. This was the main reason for increase in actual receipts of the Department over the budget estimates of 2016-17.

### 3.3 Internal Audit

The Public Accounts Committee (PAC) in its 65<sup>th</sup> Report directed (December 2015) the Department to establish Internal Audit Wing and make it function effectively. However, the Department is yet to comply with the PAC orders.

The Department accepted (July 2017) the audit observation, but stated that personnel from Finance/ Accounts services posted in the Department conduct internal audit as per roster. The reply is not acceptable for the following reasons: (i) the Department has not explained why it failed to comply with

PAC orders; (ii) the Department has not provided any evidence by way of details of units audited and audit observations to support its contention; (iii) as admitted by the Department, there is vacancy of Sr. Accounts Officer in the Department, and therefore there was no supervisory control for any internal audit activity stated to have been conducted.

**Recommendation:**

**The Department should immediately comply with the recommendations of the Public Accounts Committee and ensure the establishment of fully functioning Internal Audit Wing.**

**3.4 Results of audit**

During the year 2016-17, 113 units<sup>1</sup> (out of 132 auditable units) of the Commercial Tax Department (CTD) were covered for Audit. Revenue generated by the Department during the year 2016-17 aggregated to ₹ 26,366.16 crore of which audited units collected ₹ 20,590.54 crore. Audit of “Assessment of taxes on works contracts and builders under MPVAT Act” was done between December 2016 and November 2017. Audit noticed underassessment of tax and other irregularities involving ₹ 1,030.24 crore in 1,398 cases, which fall under the following categories as mentioned in Table 3.2.

**Table 3.2  
Results of Audit**

(₹ in crore)			
Sl. No.	Categories	No. of cases	Amount
1.	Audit on "Assessment of taxes on works contracts and builders under MPVAT Act"	1	667.02
2.	Tax short levied/not levied	291	49.41
3.	Application of incorrect rate of tax	137	43.81
4.	Incorrect determination of tax	381	132.85
5.	Incorrect grant of exemption/deduction	179	33.64
6.	Others	409	103.51
<b>Total</b>		<b>1,398</b>	<b>1,030.24</b>

The Department accepted underassessment of tax and other irregularities of ₹ 961.40 crore in 872 cases. In the remaining cases, it was replied that the cases would be reopened and Audit would be intimated accordingly. Further progress in this regard including recoveries would be watched in Audit.

During 2016-17, the Department reported revenue realisation of ₹ 2.68 crore in 24 cases pertaining to previous Audit Reports and Inspection Reports.

**3.5 Follow up of previous Audit Reports**

In the Audit Reports for the period from 2011-12 to 2015-16, Audit had pointed out various observations amounting to ₹ 542.10 crore in 116

<sup>1</sup> Office of Commissioner, Commercial Tax, 26 Divisional Offices, 21 Regional Offices and 65 Circle Offices.

paragraphs against which recovery of ₹ 1.11 crore only was effected by the Department. Further, audit recommended (Audit Report 2014-2015) that the Department should prepare a Manual to outline policy, general rules and procedures to be followed for VAT assessments. However, the Department has not prepared such a Manual.

The PAC has already given its recommendations and directions (65<sup>th</sup> Report, 2014-15 and 72<sup>nd</sup> Report, 2015-16) on similar paragraphs of ARs for the years 2004-05 and 2006-07. Some of the directions were as follows: (i) the Department should issue instructions so as to check repetition of same irregularities; (ii) action should be taken against defaulting officers.

The Department has however, failed to comply with these directions and the same type of irregularities persist.

#### **Recommendations:**

- **The Department should comply with the directions of the PAC and issue instructions and take action to ensure that similar irregularities do not occur;**
- **The Department should prepare a Manual on rules, procedures, guidelines etc., for use by its officers and staff.**

### **3.6 Audit on "Assessment of taxes on works contracts and builders under MPVAT Act"**

#### **3.6.1 Introduction**

The definition of "Sale" under the Madhya Pradesh Value Added Tax Act, 2002 (MPVAT Act) includes 'a transfer of property in goods involved in the execution of works contract'. Every works contractor whose turnover in a year exceeds ₹ five lakh shall get himself registered with the Commercial Tax Department (CTD) and shall pay tax under Section 9 on the value of goods transferred in execution of the works contract at specified rates<sup>2</sup>. Works contractors may, however, opt for composition facility<sup>3</sup> but will not be eligible to Input Tax Rebate (ITR) on purchase value of goods transferred.

The MPVAT Act was amended (April 2011) and Section 9-B 'Tax on buildings' was inserted to enable levy of tax on builders at the rate of five *per cent* on the capital value of the buildings constructed by them and sold or leased out. No tax under this section shall be levied in respect of transactions which are in the nature of works contract and on which tax is payable under Section 9 as a works contractor. Every builder liable to pay tax under Section 9-B and who is not liable to pay tax under Section 9, shall get himself enrolled with the CTD.

<sup>2</sup> Five *per cent* rate of tax as mentioned in part II of Schedule II and 13/14 *per cent* rate of tax as mentioned in part IV of Schedule II.

<sup>3</sup> Under composition facility, works contractors are allowed to pay lump sum tax at the rate of one or five *per cent*, under Section 11-A instead of paying tax under Section 9 of MPVAT Act.

In terms of Supreme Court decision<sup>4</sup>, if the building is constructed by the builder by entering into an agreement with the prospective purchaser taking advances, such transaction shall be treated as works contracts and tax should be assessed on value of goods transferred in execution of works contract under Section 9.

### **3.6.2 Audit Objectives**

Audit was conducted to ascertain whether:

- An effective mechanism exists in the Department to monitor the tax payable by works contractors and builders;
- The provisions of Acts/Rules, instruction/orders contained in circulars/notifications were followed to prevent leakages of revenue; and
- The correctness of declared turnover, Input Tax Rebate (ITR) availed and Tax Deducted at Source (TDS) claimed by the works contractors and builders were ensured.

### **3.6.3 Audit Criteria**

Audit criteria were derived from the following:

- Madhya Pradesh VAT Act, 2002,
- Madhya Pradesh VAT Rules, 2006,
- Madhya Pradesh Entry Tax Act 1976, and
- Rules, notifications, circulars and instructions issued by the State Government and Department.

### **3.6.4 Scope of audit and methodology**

The audit was conducted between December 2016 and November 2017. The records pertaining to the period 2012-13 to 2014-15 on assessments done by the Assessing Authorities (AAs) between 1 April 2015 and 31 March 2017 were examined.

Audit selected all construction circles<sup>5</sup> which were established specifically to assess the cases of builders and contractors and their Divisional Offices<sup>6</sup>. Out of the remaining 45 circles, Audit selected nine circles<sup>7</sup> on random sampling basis.

There were 33,810 registered works contractors and 311 enrolled builders in the State (December 2016), out of which 16,176 works contractors and 236 builders were registered/enrolled in selected units. Audit examined records of 691 works contractors and 162 builders assessed in selected units during the period covered in audit. The Department may like to internally examine records of remaining works contractors and builders with a view to ensure that they have paid correct amount of tax.

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<sup>4</sup> Civil appeal No. 8672 of 2013 - M/s Larsen & Toubro Ltd. versus State of Karnataka 2013.

<sup>5</sup> CTO- Bhopal VI, Gwalior I, Indore III and Jabalpur II.

<sup>6</sup> DC- Bhopal I, Gwalior I, Indore II and Jabalpur I.

<sup>7</sup> CTO- Anuppur, Balaghat, Betul, Chhatarpur, Jhabua, Ratlam I, Rewa, Sendhwa and Waidhan.

Audit obtained the data<sup>8</sup> of Value Added Tax Information System (VATIS<sup>9</sup>) from the Department and analysed the e>Returns, option for composition of tax given by the works contractors, levy of tax by way of composition, deposit of tax, verification of ITR, scrutiny of issued statutory forms and assessment orders. Data from external sources like Municipal Corporation and Department of Registration and Stamps were also obtained and cross verified with database of the Commercial Tax Department.

An entry conference was held on 10 March 2017 with the Principal Secretary of the Department, in which the objectives, scope and methodology of Audit was discussed. An exit conference was held on 29 November 2017 with the Principal Secretary of the Department. The replies of the Department have been duly incorporated in the paragraphs.

### **Acknowledgement**

The cooperation of the Department in providing necessary information and records to audit is acknowledged.

### **Audit Findings**

Audit found system deficiencies and non-compliance of various provisions of the Act/ Rules involving financial effect of ₹ 667.02 crore as discussed in the following paragraphs:

### **System deficiencies**

#### **3.6.5 MPVAT Act did not define works contract and procedure to determine the taxable turnover**

**The MPVAT Act did not define works contract and procedure to determine taxable turnover of contractors. As a result, AAs did not apply uniform process for assessment of taxes on works contract.**

Clause 29-A of Article 366 of the Constitution of India empowers States to levy sales tax on the value of the material transferred in the execution of a works contract and this definition was also incorporated in the MPVAT Act.

Audit observed that works contract is not specifically defined under MPVAT Act; also, there is no format prescribed for return, nor any procedure adopted, for assessment of taxable turnover (value of materials transferred) of contractors. Therefore, AAs had adopted different methods to determine taxable turnover of contractors by either allowing deduction of direct expenses from gross receipt or adding profit in value of material purchased and other expenses relating to material transferred. This resulted in underassessment in 125 cases as discussed in paragraph 3.6.10.

In the exit conference, the Department stated (November 2017) that the issue was well taken but in the upcoming Goods and Service Tax regime the above discrepancy shall be rectified.

<sup>8</sup> VATIS data received (December 2016) from the Department for the year 2012-13 to 2015-16.

<sup>9</sup> Departmental work i.e. registration, submission of returns, issuance of statutory forms, submission of VAT audit report and assessment etc., done through application software "VATIS".

The reply is not acceptable because assessment/re-assessment of legacy cases of VAT regime has not been completed and therefore, works contract and related procedures need to be defined.

**Recommendation:**

**The Department may consider issuing specific guidelines/instructions for determination of taxable turnover of works contracts.**

**3.6.6 Cases of works contractors/builders were not included in construction circles**

**Even after the formation of four construction circles, cases of 1,947 works contractors/builders were assessed in other circles.**

The State Government notified (September 2012) formation of four new construction circles<sup>10</sup> for the purpose of effective monitoring of tax liability and verification of input tax rebate in the cases of contractors, builders and dealers dealing with construction material viz., cement, iron and steel, *gitti*, *murrum*<sup>11</sup>, bricks, marble and tiles. Such assesses were to be included in construction circles corresponding to the respective revenue districts<sup>12</sup>.

Audit analysis revealed, however, that cases of 1,947 out of 8,913 works contractors/builders of the four revenue districts were not included in the new construction circles, and these assesses continued filing returns in their erstwhile circles between September 2012 to November 2017. Consequently, the very purpose of formation of the four specialised construction circles was defeated.

Accepting the audit observation during the exit conference, the Department stated (November 2017) that the assessment of contractors continued in the revenue circles for administrative convenience, as the earmarked four circles were not capable of handling all such cases.

The reply is not acceptable, since it is for the Department to equip the construction circles to handle the additional work load, and not to continue with the existing system that does not meet the State Government's requirements.

**Recommendation:**

**Department may ensure that all cases of works contractors of the four revenue districts are transferred to the respective construction circles.**

**3.6.7 Non-monitoring of TDS certificate and related returns**

**The Department did not ensure submission of annual return in Form 35 by persons who had taken blank TDS certificate forms.**

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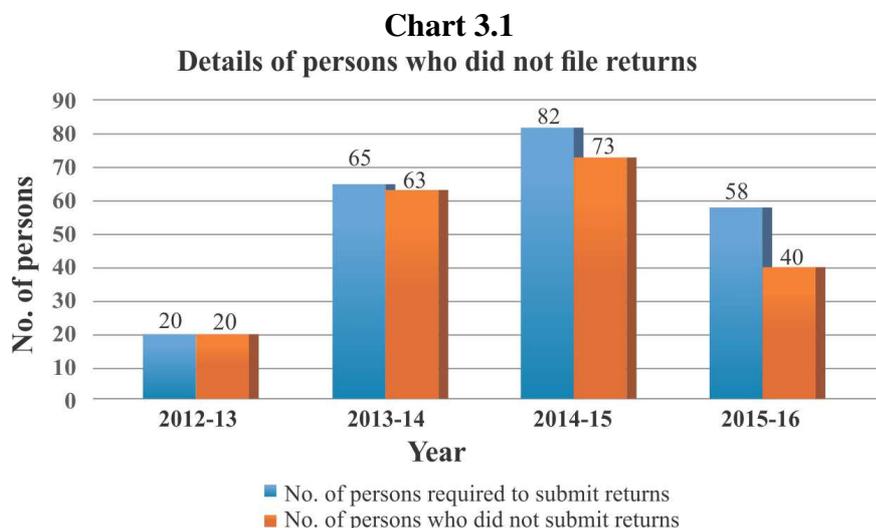
<sup>10</sup> CTO- Bhopal VI, Gwalior I, Indore III and Jabalpur II.

<sup>11</sup> A type of laterite used for road surfaces.

<sup>12</sup> Revenue Districts of Bhopal, Gwalior, Indore and Jabalpur.

The MPVAT Act and the MPVAT Rules prescribe that the person<sup>13</sup> shall deposit the amount of TDS deducted from the works contractors in Government Treasury before the 10<sup>th</sup> day of the next month. The persons shall obtain the blank TDS certificate (Form 32) from the Commercial Tax Department and give duly filled TDS certificate to the works contractors. They are also bound to file annual return of utilised TDS certificates in Form 35<sup>14</sup> within thirty days of expiry of the financial year to which the returns relate. The Commissioner, Commercial Tax (CCT) vide circulars<sup>15</sup> also reiterated the necessity of obtaining the details of TDS.

Audit test check in four circles<sup>16</sup> out of 13 circles, most of the persons who obtained blank TDS Certificate forms from the Commercial Tax Department for the period between 2012-13 and 2015-16 did not submit annual returns in Form 35 and shortfall ranged between 69 *per cent* and 100 *per cent*. The Department also did not initiate action for submission of returns by these persons. Details are given in **Chart 3.1**.



The Department failed to monitor the mandatory requirement of submission of annual returns which would have facilitated the Department to detect short deduction of TDS, delay in deposit of revenue in Government treasury and identification of unregistered dealers.

In the exit conference (November 2017), the Department agreed with the fact and assured to take remedial action for submission of return by the persons.

#### **Recommendation:**

**The Department may ensure compliance of departmental instructions regarding submission of annual returns by the TDS deducting persons.**

<sup>13</sup> Person means-Department of Central or the State Government, Public Sector Undertaking, Municipal Corporation, Authority enacted under any law for the time being in force, Public Limited Company.

<sup>14</sup> Form 35 contains the complete details of payment to contractor and also details of deducted and deposited amount of TDS.

<sup>15</sup> Circular No.164/2012-13/30/15/diary/6, Indore dated 15 February 2013 and No.184/2012-13/30/15/22, Indore dated 31 March 2013.

<sup>16</sup> CTO- Indore III, Jhabua, Rewa and Sendhwa.

### 3.6.8 Non-registration of builders and contractors

**Failure of the Department to register 656 contractors with annual turnover of more than rupees five lakh resulted in contractors' receipts of ₹ 456.99 crore escaping assessment.**

The MPVAT Act stipulates that every contractor, whose turnover in a year exceeds rupees five lakh, shall get himself registered with the Commercial Tax Department. The Commissioner vide circulars<sup>17</sup> instructed the circles-in-charge of construction circles to obtain annual returns from Municipal Corporations on works executed within their jurisdictions to assess the tax liability of such works contractors.

Audit test check of records relating to four Municipal Corporations<sup>18</sup> revealed that the circles in-charge failed to ensure regular submission of returns by the Municipal Corporations and consequently, an amount of ₹ 456.99 crore received by 656 unregistered contractors was detected to have been unassessed.

In the exit conference (November 2017), the Department issued instructions to get the records of the Commercial Tax units reconciled with those of Municipal Corporations. Progress will be monitored in future audits.

#### **Recommendation:**

**The Department may put in place mechanisms to ensure that Commercial Tax units mandatorily reconcile their records with those of Municipal Corporations and Councils, so that all contractors who are required to be registered are so registered and their turnover is assessed to tax.**

### Compliance deficiencies

#### Short levy of tax on works contractors

### 3.6.9 Short levy of tax on notified goods in execution of works contracts

**AAs failed to cross check returns of works contractors with related records and royalty payments on the sand and *gitti* consumed by them, resulting in short levy of tax of ₹ 45.51 crore including penalty.**

The State Government notified<sup>19</sup> goods like sand and *gitti* (small pieces of stone) liable to tax at the rate of ₹ 20 per cubic meter (cu.m). Further, if underassessment of tax is attributable to the contractor, penalty between 3 to 3.5 times of the amount of assessed tax shall be imposed under the MPVAT Act.

Audit test check of records in eight circle offices<sup>20</sup> and Division-I, Bhopal revealed that in 30 cases, the AAs assessed the volume of sand and *gitti* as

<sup>17</sup> No/164/2012-13/30/fifteen/dairy/06 dated 15 February 2013 and No/164/2012-13/30/fifteen/dairy/365 dated 09 May 2014.

<sup>18</sup> Bhopal, Gwalior, Indore and Jabalpur.

<sup>19</sup> Government Notification no.35 dated 27 January 2010.

<sup>20</sup> CTO- Bhopal VI, Gwalior I, Indore III, Jabalpur II, Jhabua, Ratlam I, Rewa and Sendhwa.

12,83,535 cu.m against the aggregate volume of 70,92,014 cu.m, without verifying the volume of sand/ *gitti* on the basis of royalty paid as mentioned in their books of accounts and other relevant records. Failure to assess 58,08,479 cu.m sand and *gitti* resulted in short levy of tax amounting to ₹ 11.62 crore and penalty of ₹ 33.89 crore.

In the exit conference (November 2017), the Department agreed with the audit findings and assured that all these cases shall be reopened and appropriate action taken under intimation to Audit.

### 3.6.10 Short levy of tax due to failure to perform mandatory checks

**Failure of AAs to perform mandatory checks on records like audited accounts, details of material purchased, TDS certificates etc., at the time of assessment led to underassessed turnover of ₹ 872.97 crore resulting in short levy of tax of ₹ 226.13 crore including penalty.**

Audit test check of records in three Divisional offices<sup>21</sup> and 10 circle offices<sup>22</sup> revealed that in 125 cases of works contractors, some important documents relating to works contracts like agreements, work orders, running account bills were not found in case files. Without verifying the nature, value and quantity of material transferred in execution of works contracts, the AAs assessed the taxable turnover of ₹ 1,034.70 crore on the basis of tax proposals submitted by the contractors against the aggregate turnover of ₹ 1,907.67 crore which was determined on the basis of audited accounts, value of material purchased, TDS certificates etc., available with the Department. Thus, the AAs failed to perform mandatory checks on records at the time of assessment leading to underassessed turnover of ₹ 872.97 crore resulting in short levy of tax amounting to ₹ 58.04 crore and penalty of ₹ 168.09 crore.

In the exit conference (November 2017), the Department agreed with the audit findings and assured that all these cases shall be reopened and appropriate action taken under intimation to Audit.

#### Recommendation:

**The Department should introduce mechanisms to ensure that Assessing Authorities verify, at the time of assessment, all records relating to the value of goods transferred in execution of the works contracts.**

### Sub-contractor

#### 3.6.11 Deductions allowed to main contractors without confirmation of tax payment by sub-contractors

<sup>21</sup> DC- Bhopal I, Gwalior I and Indore II.

<sup>22</sup> CTO- Betul, Bhopal VI, Chhatarpur, Gwalior I, Indore III, Jabalpur II, Jhabua, Ratlam I, Rewa and Sendhwa.

**Failure of AAs of main contractors, when allowing deductions to the main contractor, to cross-verify from the AAs of the sub-contractors, whether sub-contractors had paid tax on these deductions, resulted in non-inclusion of contract receipts of ₹ 171.82 crore in the taxable turnover of the sub-contractors/ main contractors, and short levy of tax of ₹ 20.60 crore including penalty.**

The MPVAT Act prescribes that in case of works contracts executed through sub-contractors, the principal contractor and the sub-contractor shall be jointly and severally liable to pay tax in respect of such works contract. If the contractor proves in the prescribed manner<sup>23</sup> to the satisfaction of the Department that the tax has been paid by the sub-contractor on the turnover of the works contracts, the contractor shall not be liable to pay tax again on the said turnover. Audit scrutiny revealed failure of the AAs to include the taxable turnover of the sub-contractors at the time of assessment of tax in the following cases:

- M/s Sarla Mantena MP JV (main contractor) got two works contracts (May 2013 and July 2013 respectively) in Pench Diversion Project amounting to ₹ 145 crore and ₹ 100 crore on turnkey basis. The main contractor sublet the entire works to M/s Mantena Infra LLP and M/s Sarla Project Works Pvt. Ltd respectively. In the assessments pertaining to 2014-15, the AA allowed deductions to the main contractor amounting to ₹ 93.95 crore from the contract receipts on the basis of acceptance of the tax liability by the sub-contractors (Mantena Infra for ₹ 51.69 crore and Sarla Project Works for ₹ 42.26 crore), without verifying the fact that both sub-contractors did not include said receipts in determination of turnover in their returns.
- M/s HES Infra Pvt. Ltd. (main contractor) got two works contracts (both, in August 2013) in Pench Diversion Project amounting to ₹ 126 crore and ₹ 76.50 crore on turnkey basis. The main contractor sublet both the works entirely to M/s Mantena Infra LLP. In the assessments pertaining to 2014-15, the AA allowed deductions to the main contractor amounting to ₹ 10.23 crore from the contract receipts on the basis of acceptance of the tax liability by the sub-contractor, without verifying the fact that the sub-contractor did not include said receipts in determination of turnover in their return.
- M/s HES Mantena MP JV (main contractor) sublet the entire works in Mahi Dam Project to M/s Mantena Construction Pvt. Ltd. In the assessments pertaining to 2014-15, the AA allowed deductions of ₹ 67.34 crore from the contract receipts of the main contractor on the basis of acceptance of tax liability by sub-contractor for the above receipts. However, the sub-contractor did not include the contract receipts in its turnover and the same was not detected by the AA.

In all above cases, the AAs of the main contractors, when allowing deductions to the main contractors, did not cross-verify from the AAs of the sub-contractors, whether sub-contractors had paid tax on these deductions or not. As a result, neither the main contractors nor the sub-contractors included the

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<sup>23</sup> Deduction claims by a contractor shall be supported by a declaration in Form 3 by the sub-contractor.

contract receipts amounting to ₹ 171.82 crore in their taxable turnovers. This led to short levy of tax amounting to ₹ 5.15 crore and penalty of ₹ 15.45 crore.

In the exit conference (November 2017), the Department agreed with the audit findings. The Department further intimated (February, 2018) that all the cases had been reopened for reassessment under Section 21(1) of MPVAT Act.

**Recommendation:**

**The Department may evolve a mechanism whereby, deductions may be allowed to the main contractors only on receipt of evidence that the sub-contractors had actually remitted the tax, on whose turnover the main contractors claimed the deductions.**

**3.6.12 Irregular exclusion of sub contract value in the absence of requisite certificate Form 3**

**AAs determined taxable turnover without including sub-contract expenses resulted in short levy of tax and penalty amounting to ₹ 5.20 crore.**

The MPVAT Act and MPVAT Rules prescribe that deduction from the contract receipt claimed by a principal contractor shall be supported by a declaration in Form 3 to be issued by the sub-contractor to the principal contractor and the principal contractor shall not be liable to pay tax again on the said turnover.

Audit scrutiny of records (assessment orders, audited accounts, returns, VATIS report etc.) in seven circle offices<sup>24</sup> revealed that in 17 cases of works contractors assessed between April 2015 and March 2017 for the years 2012-13 to 2014-15, AAs determined taxable turnover by irregularly excluding the sub contract expenses even in the absence of Form 3. However, sub contractor's expenses aggregating to ₹ 70.96 crore were certified in their audited account which was required to be included in the turnover of the main contractors. Thus, injudicious exclusion of sub-contract expenses in determining taxable turnover of the main contractors led to underassessment of taxable turnover by ₹ 70.96 crore which resulted in short levy of tax amounting to ₹ 2.12 crore and penalty of ₹ 3.08 crore.

In the exit conference (November 2017), the Department agreed with the audit findings and assured that all these cases shall be reopened and appropriate action would be taken under intimation to audit.

**Deficiencies in administration of composition of tax**

Registered dealers involved in works contracts in MP may opt for composition facility in respect of the works executed by them. Under composition facility, works contractors are allowed to pay lump sum tax at the rate of one or five *per cent*<sup>25</sup> on gross contract receipts, instead of tax ranging between five and 14 *per cent* at the rate prescribed in Schedule-II of MPVAT Act on taxable turnover. Contractor shall pay composition of tax and submit their quarterly statement in Form 4-B within 30 days after end of the quarter enclosing

<sup>24</sup> CTO- Bhopal VI, Gwalior I, Indore III, Jabalpur II, Jhabua, Ratlam and Rewa.

<sup>25</sup> In terms of the MPVAT Rules, composition of tax shall be levied at the rate of one *per cent* (applicable to goods purchased within the State) otherwise five *per cent*.

therewith proof of the payment. Composition opted dealers are exempted from submission of returns (Section 18), maintenance of audited account (Section 39), liability of assessment of tax (Section 20) and interest cannot be charged in case of delay in payment of amount of tax [Section 18(4)(a)]. If dealers who opt for composition do not fulfill the restrictions and condition prescribed under Rule 8-A of MPVAT Rules, the CTO may revoke the permission granted to the registered dealer, who shall then be liable to be assessed under Section 20 and the provision of Section 18, 20 and 39 shall apply in relation to the works contract in respect of which such permission had been revoked.

### 3.6.13 Incorrect acceptance of option for composition facility

**Applications for option of composition of tax were required to be submitted within 60 days from commencement of work. However, the AAs allowed composition of tax without recording reasons in cases where applications were received with delays ranging between 10 and 3,296 days.**

The MPVAT Act and MPVAT Rules prescribe that option for composition of tax is to be submitted online in Form 4-A to the CTO concerned within 60 days of commencement of execution of the works contracts. In cases of any delay in filing Form 4-A, the CTO may reject the application. But, if there are sufficient and reasonable cause for such delay, the delay may be condoned.

Audit analysed the data provided by the Department pertaining to contractors who opted for composition of tax. Audit found that in all circle offices 3,618 composition applications were sanctioned by the CTO, out of which 310 composition applications with contract amount of ₹ 3,402.49 crore were submitted after prescribed time with delays ranging between 10 and 3,296 days. Details of delays are shown in **Table 3.3**.

**Table 3.3**  
**Incorrect grant of composition of tax**

(₹ in crore)

Year	No. of applications (composition granted)	No. of composition application submitted after prescribed time	Range of delay (in days)	Median value of delays	Amount of contract works
2013-14	1,091	5	10 to 228	108	105.95
2014-15	1,272	213	10 to 3,112	425	2,567.35
2015-16	1,255	92	10 to 3,296	265	729.19
<b>Total</b>	<b>3,618</b>	<b>310</b>	<b>10 to 3,296</b>		<b>3,402.49</b>

In these cases, instead of rejecting the applications, the CTOs condoned delayed submission of applications for composition of tax without recording reasons for the same. The CTOs incorrectly allowed these works contractors to pay lump sum tax under composition facility, and exempted from assessment and liability of submission of returns and accounts. However, they were liable to be assessed under section 20 of MPVAT Act.

In the exit conference (November 2017), the Department agreed with the audit findings.

### 3.6.14 Inadmissible allowance of composition of tax

Two hundred eighty eight contractors submitted their quarterly statement of composition of tax belatedly upto 877 days, 646 contractors did not deposit tax of composition amounting to ₹ 163.29 crore, and 698 contractors belatedly deposited composition of tax amounting to ₹ 38.78 crore.

#### 3.6.14.1 Delayed submission of quarterly statements

Audit analysed data provided by the Department and found in all circle offices that 288 out of 402 composition facility opted contractors submitted quarterly statement in Form 4-B after prescribed time with delay upto 877 days as shown in **Table 3.4**.

**Table 3.4**  
Delayed submission of quarterly statements

Year	No. of dealer who submitted quarterly statements	No. of dealer who submitted quarterly statements after prescribed time	Range of delay in days
2013-14	54	46	01 to 877
2014-15	150	131	01 to 807
2015-16	198	111	01 to 601
<b>Total</b>	<b>402</b>	<b>288</b>	

The Department did not revoke the permission of composition facility of such contractors and assess their cases under Section 20 of MPVAT Act.

In the exit conference (November 2017) the Department agreed with the audit findings and assured that all these cases shall be reopened and appropriate action would be taken under intimation to Audit.

#### 3.6.14.2 Composition of tax not deposited

Audit analysis of records relating to all circles revealed that there was no evidence that 646 works contractors who had composition facility for contract amount of ₹ 4,535.40 crore during the year 2013-14 to 2015-16, had actually paid the composition of tax amounting to ₹ 163.29 crore as shown in **Table 3.5**.

**Table 3.5**  
Composition of tax not deposited

(₹ in crore)

Year	No. of works contractors where there is no evidence of payment	Contract Amount	Amount of composition of tax due
2013-14	226	1,565.99	55.16
2014-15	106	287.66	8.72
2015-16	314	2,681.75	99.41
<b>Total</b>	<b>646</b>	<b>4,535.40</b>	<b>163.29</b>

In the exit conference (November 2017), the Department agreed with the audit findings and assured that all these cases shall be reopened and appropriate action would be taken under intimation to Audit.

### 3.6.14.3 Delayed deposit of composition of tax

Audit scrutiny revealed that 941 contractors deposited composition of tax amounting to ₹ 38.78 crore for the period 2013-14 and 2015-16, with delays ranging from 32 to 1,233 days as shown in Table 3.6.

**Table 3.6**

#### Delayed deposit of Composition of tax

(₹ in crore)

Year	No. of contractors who deposited composition of tax	Amount of tax deposited	No. of contractors who deposited composition of tax with delay	Amount of tax involved in delay deposit	Delay in days	Median value of delays
2013-14	108	12.26	52	1.95	32 to 473	67
2014-15	369	52.82	213	16.25	32 to 765	78
2015-16	464	65.00	433	20.58	32 to 1,233	70
<b>Total</b>	<b>941</b>	<b>130.08</b>	<b>698</b>	<b>38.78</b>	<b>32 to 1,233</b>	

The Department should have revoked the permission of composition facility under sub-rule 8 below Rule 8-A of MPVAT Rules and assessed these cases under Section 20 of MPVAT Act. However, the same was not done.

In the exit conference (November 2017), the Department agreed with the audit findings and assured that all these cases shall be reopened and appropriate action would be taken under intimation to Audit.

### 3.6.15 Application of incorrect rate of composition of tax

**Failure of AAs to apply the correct rate of composition of tax on contractors purchasing materials from outside the State resulted in short levy of tax of ₹ 119.04 crore including penalty.**

Audit scrutiny revealed that in two cases<sup>26</sup> of Division-II, Indore and CTO-VI, Bhopal, contractors were allowed composition of tax of ₹ 86.21 lakh at the rate of one *per cent* (applicable to goods purchased within the State) although these two contractors had purchased the materials from outside the State, for which the composition of tax rate was five *per cent*. Thus failure of the AAs to apply the correct rate resulted in short levy of tax amounting to ₹ 3.44 crore and penalty of ₹ 10.32 crore. Similarly, Audit analysed the data relating to all the circles and found that 218 contractors were allowed the composition of tax amounting to ₹ 26.32 crore at the rate of one *per cent* for the period between 2013-14 and 2015-16. However, these contractors had purchased the materials from outside the State which were transferred in works contract. Thus these contractors were liable to pay tax of ₹ 131.60 crore at the rate of five *per cent* instead of ₹ 26.32 crore. The AAs did not verify the fact that the contractors had purchased materials from outside the State which was available in Form

<sup>26</sup> M/s Highway Engineering Pvt. Ltd and M/s PS Construction.

4B and Form 49. This resulted in short levy of tax amounting to ₹ 105.28 crore. Thus the total short levy of tax worked out to ₹ 119.04 crore (₹ 13.76 crore + ₹ 105.28 crore) including penalty.

In the exit conference (November 2017), the Department agreed with the audit findings and assured that all these cases shall be reopened and appropriate action taken under intimation to Audit.

### 3.6.16 Short levy of composition of tax

**AAs incorrectly allowed composition facility in four cases, applied incorrect rate of tax in five cases and determined less taxable turnover in three cases against the contract receipt certified from payment details of works contracts. This resulted in short levy of tax amounting to ₹ 7.26 crore including penalty.**

The MPVAT Act prescribes that any registered dealer executing works contract may grant composition facility in respect of any one or more of the works contracts executed by him and the provisions of Sections 18 (returns), Section 20 (assessment) and Section 39 (audited accounts) shall not apply to these dealers. Contractors who have not opted this facility, shall be liable to be assessed under Section 20 of MPVAT Act.

Audit scrutiny of records of one Division<sup>27</sup> and six circle offices<sup>28</sup> revealed that AAs incorrectly allowed composition facility in four cases where the works were not covered under composition facility, applied incorrect rate of tax in five cases and determined less taxable turnover in three cases against the contract receipt certified from payment details of works contracts. This resulted in short levy of tax amounting to ₹ 3.35 crore and penalty of ₹ 3.91 crore.

In the exit conference (November 2017), the Department agreed with the audit findings and assured that all these cases shall be reopened and appropriate action would be taken under intimation to Audit.

#### **Recommendation:**

**The Department may develop an automated system in VATIS to reject applications received after prescribed time, to generate alert to contractors for submission of statements and to detect contractors purchasing materials from out of State and apply higher rate of composition of tax.**

### Short levy of tax on builders

#### 3.6.17 Assessments of builders without using VATIS

The Department instructed<sup>29</sup> (January, 2012) its circle offices that all the processes relating to registration, returns, tax assessment etc., would mandatorily be routed through VATIS modules from 1 February 2012.

<sup>27</sup> DC- Bhopal I

<sup>28</sup> CTO- Bhopal VI, Gwalior I, Indore III, Jabalpur II, Jhabua and Ratlam I.

<sup>29</sup> Vide Circular No.83/2011-12/30/Pandraha/120, Indore dated 31 January 2012.

Audit observed from records in all selected circle offices that in clear disregard to departmental instruction, all the cases of builders for the year 2012-13 to 2014-15 were assessed by the AAs between 2015-16 and 2016-17 under Section 9-B without using the VATIS. Moreover, the assessment orders were not uploaded in the VATIS. During further scrutiny it was found that requisite module for the assessment of enrolled builders was not developed in the VATIS by the Department. Thus, due to non-availability of data relating to the assessment of builders in VATIS module, the Department could not use the data (purchase and sales details, returns etc.,) to ascertain the correctness of assessments.

In the exit conference (November 2017), the Department agreed with the audit findings and stated that although the computerisation work in Department was complete, these issues continued to crop up.

The reply is not acceptable. The problems arose precisely because the Department failed to develop a module for assessment of builders in VATIS.

### **3.6.18 Incorrect determination of turnover in absence of returns**

**Due to lack of efforts by AAs in gathering requisite information from Registration Department or from VATIS before issuing *ex parte* assessment order, turnover was underassessed. This resulted in short levy of tax of ₹ 3.08 crore including penalty.**

The MPVAT Act prescribes that if a dealer has not furnished returns and statement as prescribed in the Act and failed to comply with any of the terms of the notice issued, then the cases of such dealers will be assessed by the taxing authority to the best of his judgement. Further, the MPVAT Rules prescribe that every registered/enrolled builder shall furnish to the appropriate Commercial Tax Officer or any other officer authorized by the Commissioner in this behalf for each quarter of a year a quarterly return in Form 10-B within thirty days from the date of expiry of the quarter to which the return relates.

In three<sup>30</sup> cases in CTO-VI, Bhopal, the builders had not filed any returns and the AAs had settled the cases on *ex parte* basis to the best of their judgement. The AAs did not record basis of determining tax liability of builders in their assessment orders. Audit found that the AAs had failed to verify the data of these builders with related records available in the Registration Department and with the VATIS database and found that, though the builders sold the buildings for ₹ 11.57 crore, the AAs determined their Gross Turnover (GTO) at ₹ 1.26 crore, resulting in failure to levy tax on Taxable Turnover (TTO) of ₹ 6.19 crore<sup>31</sup>. Similarly, in seven cases of builders in CTO-III, Indore, where also, the AAs assessed the cases *ex parte*, the builders purchased material of ₹ 8.38 crore during the period 2014-15 but the AAs determined their TTO and tax as Nil, resulting in failure to levy tax on TTO of ₹ 9.22 crore (material value ₹ 8.38 crore plus 10 *per cent* profit on material value).

Thus, failure of the AAs in verifying related information available with the Registration Department and in the VATIS database before issuing *ex parte*

<sup>30</sup> Ultimate construction (81329000173), Sai Construction (81459000257) and Pradhan Homes (81419000164).

<sup>31</sup> 60 *per cent* material value of GTO of ₹ 10.31 crore [₹ 11.57 crore (-) ₹ 1.26 crore]

assessment order, resulted in underassessment of turnover by ₹ 15.41 crore (₹ 6.19 crore + ₹ 9.22 crore), and short levy of tax (at the minimum rate of five *per cent*) amounting to ₹ 77.03 lakh and penalty of ₹ 2.31 crore.

In the exit conference (November 2017), the Department accepted the audit findings, and issued directions that AAs should coordinate with related departments and local bodies and with the VATIS database, before making *ex parte* determinations of tax.

**Recommendation:**

**The Department should formalise a mechanism in VATIS whereby AAs mandatorily cross-verify details relating to their assesseees with related databases and records in other Government departments and local bodies.**

### 3.6.19 Works contractors incorrectly treated as builders

**The AAs failed to treat builders as works contractors even though the builders had entered into agreements with prospective purchasers by taking advances. This resulted in short levy of tax and penalty of ₹ 34.77 crore.**

Section 9-B of the MPVAT Act prescribes that every builder shall be liable to pay tax at the rate of five *per cent* on the capital value of the building, constructed by him and sold or leased out. Where transactions are in the nature of works contracts, tax is levied under Section 9 applicable to works contractors. Further, contractors entering in the works contract valued at ₹ five lakhs and above, shall get themselves registered with the Department.

In terms of Supreme Court decision<sup>32</sup>, if the building is constructed by the builder by entering into agreements with prospective purchasers taking advances, such transactions shall be treated as works contracts and taxes assessed under Section 9 of the MPVAT Act. Unregistered contractors are liable to pay two times penalty on assessed tax under Section 20(6) of the MPVAT Act and in case of contractors already registered, they are liable to pay penalty at three times of the short assessed tax under Section 21(2) of the MPVAT Act.

Audit test check of records in five circle<sup>33</sup> offices revealed that in 36 cases of builders the AAs assessed the tax amounting to ₹ 3.23 crore under Section 9-B of MPVAT Act though such builders took advances from the prospective purchasers and were liable to pay tax under section 9. It was also noticed that there were development agreements/ tripartite agreements between the land owners, builders/ developers and the purchasers for monetary consideration. This indicated the transactions should have been treated as works contracts, and tax levied on the value of the materials involved in execution of the works. Assessment of taxes of ₹ 3.23 crore against the tax liability of ₹ 26.46 crore resulted not only in short-levy of tax amounting to ₹ 23.22 crore but also indicated the failure of the AAs in making realistic assessment of taxes. This also attracts levy of penalty of ₹ 11.55 crore.

<sup>32</sup> Civil appeal No. 8672 of 2013 in case of M/s Larsen & Toubro Ltd. versus State of Karnataka 2013.

<sup>33</sup> CTO- Bhopal VI, Gwalior I, Jabalpur II, Ratlam I and Rewa.

In the exit conference (November 2017), the Department agreed with the audit findings and assured that all these cases shall be reopened and appropriate action taken under intimation to audit.

**Recommendation:**

**The Department may devise appropriate procedures to ensure that builders entering into composite contracts involving both works contract and transfer of immovable property are treated as works contractors for purposes of assessment of tax.**

**Inadmissible grant of input tax rebate (ITR)**

**3.6.20 Allowance of inadmissible ITR to works contractors**

**Allowance of inadmissible ITR to builders who should have been treated as unregistered works contractors, and to works contractors without verifying tax paid by the corresponding selling dealers, led to short levy of tax amounting to ₹ 36.67 crore including penalty.**

The MPVAT Act prescribes that input tax rebate (ITR) shall be allowed only where a registered dealer purchases any specified goods within the State, from another registered dealer, after payment of input tax. Further, the amount of input tax rebate on any purchase of goods shall not exceed the amount of tax in respect of such purchase of goods actually paid into the Government Treasury. If rebate of input tax has incorrectly been allowed, while making the assessment, and it is attributable to the dealer, penalty between 3 to 3.5 times of the amount of assessed tax shall be imposed under Section 21(2) of the Act.

Audit test check of records in Division-I, Bhopal and seven circle offices<sup>34</sup> revealed that in 20 cases, the AAs allowed ITR amounting to ₹ 2.76 crore to enrolled builders. Such builders took advances from the prospective purchasers and were liable to pay taxes under section 9. It was also noticed that there were development agreements/ tripartite agreements between the land owners, builders/ developers and the purchasers for monetary consideration. This indicated the transaction should have been treated as works contracts. Further, since these builders were not registered under the MPVAT Act, these builders should have been treated as unregistered works contractors instead of enrolled builder. Failure of the AAs to verify the above facts during assessments of builders resulted in allowance of inadmissible ITR of ₹ 2.76 crore.

Further in 18 cases, AAs allowed ITR of ₹ 22.63 crore to works contractors but the corresponding selling dealers had paid tax of ₹ 63.97 lakh only. As such, ITR should have been restricted to ₹ 63.97 lakh. Thus, AAs allowed inadmissible grant of ITR of ₹ 21.99 crore.

Thus, audit scrutiny revealed short levy of tax amounting to ₹ 24.74 crore and penalty of ₹ 11.93 crore.

In the exit conference (November 2017), the Department agreed with the audit findings and assured that all these cases shall be reopened and appropriate action taken under intimation to Audit.

<sup>34</sup> CTO- Bhopal VI, Gwalior I, Jabalpur II, Jhabua, Ratlam I, Rewa and Sendhwa.

## Entry Tax

### 3.6.21 Short levy of Entry Tax

**Entry Tax on goods like *gitti, murrām*, cement, iron and steel, furnace oil, bitumen etc., was either not levied or was levied at incorrect rates. This resulted in short levy of tax of ₹ 5.47 crore including penalty.**

The Madhya Pradesh Entry Tax Act, 1976 (ET Act) stipulates that where underassessment of entry tax (ET) is attributable to the contractor, penalty at not less than three times the assessed tax shall be imposed.

Audit scrutiny of records in two Divisional offices<sup>35</sup> and nine circle offices<sup>36</sup> revealed that in 48 cases of works contractors assessed between April 2015 and March 2017 for the years 2012-13 to 2014-15, the AAs short levied tax due to less determination of taxable turnover against the purchases certified in books of accounts and statutory forms<sup>37</sup>, wrong treatment of taxable goods purchased through un-registered dealers as tax paid goods, and application of incorrect rate of tax on goods like *gitti, murrām*, cement, iron and steel, furnace oil, bitumen etc. This resulted in short levy of tax amounting to ₹ 1.47 crore and penalty of ₹ 4.00 crore.

In the exit conference (November 2017), the Department agreed with the audit findings and assured that all these cases shall be reopened and appropriate action taken under intimation to Audit.

### 3.6.22 Conclusion

- The works contract is not specifically defined in MPVAT Act and no specific guidelines were issued by the Department to determine the taxable turnover in case of works contracts. This led to short levy of tax of ₹ 226.13 crore.
- The Department has not established any mechanism for cross verification of inter-departmental database of works contractors who had received more than rupees five lakh in a year and not registered themselves with the Department. Audit found that 656 unregistered works contractors who received more than rupees five lakh in a year from Municipal Corporations were not registered and contract receipts of ₹ 456.99 crore received by them escaped from assessment.
- While allowing deductions from contract receipts to the main contractor, the AAs of main contractors did not cross-verify from the AAs of the sub-contractors whether sub-contractors had paid tax on these deductions or not. As a result, neither the main contractors nor the sub-contractors included the contract receipts of ₹ 171.82 crore in their taxable turnover.
- The Department did not revoke the permission of composition of tax in cases where works contractors had violated restrictions and conditions under Section 11-A of MPVAT Act.

<sup>35</sup> DC- Bhopal I and Indore II.

<sup>36</sup> CTO- Balaghat, Bhopal VI, Chhatarpur, Gwalior I, Jabalpur II, Jhabua, Ratlam I, Rewa and Sendhwa.

<sup>37</sup> Dealer used Form-49 and Form-C to purchase the goods from outside the State.

- The Department did not issue instructions regarding treating builders as works contractors in cases where the builders enter into any agreement with the prospective purchasers and take advances for the work. This resulted in short levy of tax of ₹ 34.77 crore.

### Audit observations of Compliance Audit

#### 3.7 Incorrect determination of turnover

**Under determination of taxable turnover by ₹ 48.95 crore by AAs resulted in non-levy of tax of ₹ 3.98 crore, interest of ₹ 18.13 lakh and penalty of ₹ 5.41 crore.**

The MPVAT Act stipulates that if underassessment of tax is attributable to the assessee, penalty is to be imposed at between 3 to 3.5 times the amount of assessed tax.

Audit test check of records of five divisional offices<sup>38</sup>, 10 regional offices<sup>39</sup> and 33 circle offices<sup>40</sup> revealed that in 94 cases assessed between November 2014 and July 2016 for the period between 2011-12 and 2013-14, the AAs determined less turnover amounting to ₹ 48.95 crore due to non/short account of sale value, profit and other receipts in 55 cases, non-adoption of figures in audited accounts in 10 cases and adoption of lower rates of VAT and excise duty in 13 cases. In 15 cases excess deductions were given while in one case the views of the AAs were not taken by the Appellate Authority. As a result, tax of ₹ 9.57 crore including interest of ₹ 18.13 lakh and penalty of ₹ 5.41 crore could not be levied.

The Department intimated in November 2017 that the reassessment of cases was under process. Final recovery and action taken will be watched in Audit.

Similar observations were pointed out in previous Audit Reports from 2011-12 to 2015-16 but the Department has not evolved an effective mechanism to check the persistence of such irregularities. During the exit conference (October 2015) on Performance Audit on “System of Assessment under VAT in Madhya Pradesh” the Principal Secretary directed the Department to rectify the irregularities within a time frame, improve the internal check system and incorporate necessary modules in the VATIS to strengthen the system of assessment. However, the Department has not developed an effective mechanism to check the persistence of such irregularities.

#### Recommendation:

**The Department is required to incorporate necessary modules in VATIS and initiate other measures to ensure that the system of assessment is strengthened.**

<sup>38</sup> DCCT- Chhindwara, Gwalior (TAW), Indore (LTPU), Indore (TAW I) and Ratlam.

<sup>39</sup> ACCT- Bhopal III, Chhindwara, Gwalior I, Indore II, Jabalpur II, Katni I, Khandwa, Neemuch, Pithampur (Dhar) and Rewa.

<sup>40</sup> CTO- Anuppur, Balaghat, Betul, Bhopal I, Bhopal IV, Bhopal V, Chhindwara I, Damoh, Dewas, Gwalior II, Gwalior III, Gwalior IV, Harda I, Indore I, Indore II, Indore III, Indore VIII, Indore X, Indore XI, Indore XII, Indore XIV, Indore XV, Itarsi, Jabalpur I, Katni II, Khargone, Mandideep, Mandla, Neemuch, Sagar, Shahdol, Tikamgarh and Ujjain II.

### 3.8 Allowance of inadmissible input tax rebate

**The Assessing Authorities allowed input tax rebate of ₹ 120.97 crore against the admissible input tax rebate of ₹ 117.06 crore resulting in short realisation of tax of ₹ 9.41 crore including penalty of ₹ 5.50 crore.**

The MPVAT Act stipulates that input tax rebate (ITR) is allowed only in respect of specific goods purchased by a registered dealer from another registered dealer who has paid input tax, and further, the input tax rebate shall not exceed the input tax actually paid. If rebate of input tax has incorrectly been allowed, and is attributable to the dealer, penalty shall be imposed.

Audit test check of records in seven divisional offices<sup>41</sup>, 11 regional offices<sup>42</sup> and 25 circle offices<sup>43</sup> revealed that in 92 cases, assessed between April 2014 and December 2016 for the period between 2010-11 and 2013-14, the assessing authorities allowed higher ITR on the basis of returns submitted by the dealers without taking into consideration the purchase list and audited accounts. In 32 cases, the input tax paid by the dealer was less than what they had claimed in their returns for rebate, and in 31 cases ITR was granted though it was inadmissible. In other cases, either the ITR was given on tax-free goods or double ITR was given. As a result, inadmissible ITR of ₹ 3.91 crore and penalty of ₹ 5.50 crore is to be recovered.

In the exit conference (November 2017), the Department intimated that the reassessment of cases was under process. Further progress will be awaited in Audit.

Similar observations were pointed out in previous Audit Reports from 2011-12 to 2015-16. Audit in its recommendation on the Performance Audit on “System of assessment under Value Added Tax” of Audit Report for the year 2014-15 stated that purchase details should be properly authenticated/substantiated through the documents and in conformity with the audited accounts before accepting claims of ITR. In the exit conference held in October 2015 to discuss findings of this PA, the Department had intimated that all the ITR cases were being cross verified electronically after 2013-14 and a special cell for ITR verification was created. However, cases of inadmissible ITR have regularly been pointed out in audit. Despite existence of mechanism in the Department for monitoring the correctness of the ITR claimed/paid, intra departmental data/information were not taken into cognizance for ITR claims.

#### **Recommendation:**

**The Department may consider strengthening of ITR verification mechanism so that purchase details are verified with audited accounts,**

<sup>41</sup> DCCT- Bhopal II, Gwalior (TAW), Indore I, Indore I (TAW), Khandwa, Ratlam and Ujjain.

<sup>42</sup> ACCT- Bhopal I, Bhopal III, Gwalior II, Indore I, Indore II, Indore III, Khandwa, Pithampur (Dhar), Ratlam, Rewa and Sagar II.

<sup>43</sup> CTO- Anuppur, Betul, Bhopal I, Chhatarpur, Chhindwara I, Chhindwara II, Damoh, Dewas, Guna, Gwalior II, Gwalior III, Gwalior IV, Harda I, Indore I, Indore II, Indore III, Indore VII, Indore XI, Indore XII, Indore XIV, Indore XV, Jabalpur III, Jaora (Ratlam), Khargone and Mandla.

properly authenticated/substantiated by documents and cross-verified with corresponding selling dealers.

### 3.9 Entry tax not levied/short levied

**Entry Tax on goods was either not levied or levied at incorrect rates on their entry into local areas, resulting in non-realisation of entry tax amounting to ₹ 2.04 crore, penalty of ₹ 2.15 crore and interest of ₹ 10.23 lakh.**

The ET Act stipulates that if under-assessment of entry tax is attributable to the dealer, penalty at not less than three times of the assessed tax shall be imposed.

Audit test check of records of four divisional offices<sup>44</sup>, nine regional offices<sup>45</sup> and 19 circle offices<sup>46</sup> revealed that in 62 cases assessed /reassessed between April 2015 and January 2016 for the period 2012-13 to 2013-14, entry tax on goods like machinery, motor cycle, auto parts, oils, arms and ammunition, soyabean, HDPE fabrics, coal etc., was either not levied or was levied at incorrect rates on their entry into local area.

Of these 62 cases, in 32 cases entry tax was applied at the rates lower than the applicable rates; in 14 cases, the leviable entry tax was not levied, in six cases goods leviable to entry tax were not taken in the gross taxable turnover, and in other cases incorrect exemption or deduction was allowed without evidence. As a result, entry tax amounting to ₹ 4.29 crore including penalty of ₹ 2.15 crore and interest of ₹ 10.23 lakh could not be realised.

In the exit conference (November 2017), the Department intimated that the reassessment of cases was under process. Final action was awaited (May 2018).

Similar observations were pointed out in previous Audit Reports for the years 2011-12 to 2015-16. But the AAs continued to commit similar errors in the assessments ignoring clear provisions/tax rates of the Act/schedule which obviously reflect weaknesses in internal control.

#### **Recommendation:**

**The Department may ensure that claims for deduction of entry tax paid purchases from taxable turnover are properly authenticated by documents, and gross purchase are cross-verified with audited accounts of the dealers.**

### 3.10 Application of incorrect rate of tax

**Failure of AAs to apply the correct rates of tax resulted in short levy of tax of ₹ 3.98 crore including penalty of ₹ 2.44 crore.**

<sup>44</sup> DCCT - Indore (LTPU), Bhopal II, Khandwa and Ratlam.

<sup>45</sup> ACCT - Bhopal I, Bhopal III, Gwalior II, Gwalior (TAW), Indore III, Khandwa, Neemuch, Pithampur (Dhar) and Rewa.

<sup>46</sup> CTO - Anuppur, Bhopal V, Chhindwara I, Chhindwara II, Damoh, Dewas, Gwalior III, Indore I, Indore II, Indore VII, Indore VIII, Indore XI, Indore XII, Indore XIV, Jabalpur I, Jabalpur III, Katni II, Mandideep and Sagar.

As per the MPVAT Act, plant and machinery, scrap packing material, emulsion tractor accessories etc., are taxable at the rate of 13 *per cent*.

Audit test check of records in one divisional office<sup>47</sup>, one regional office<sup>48</sup> and eight circle offices<sup>49</sup> revealed that in 20 cases of 17 dealers assessed between September 2013 and January 2016 for the period between 2010-11 and 2013-14, the AAs levied five *per cent* or four *per cent* tax on the sale of tractor accessories, sanitary goods, furniture, kitchen panels, metal crash barrier system and machinery parts which were taxable at the rate of 13 *per cent*. This resulted in short levy of VAT of ₹ 1.54 crore and penalty of ₹ 2.44 crore thereon.

In the exit conference (November 2017), the Department agreed with the audit observations and intimated that reassessment of cases was under process. Final action was awaited (May 2018).

Similar observations were pointed out in previous Audit Reports from 2011-12 to 2015-16. The Department accepted (October 2015) that incorrect rates could have been applied due to difference of opinion with regard to the rate of tax for a commodity and in the absence of Harmonised System of Nomenclature (HSN) Code<sup>50</sup> there was possibility of such error. The PAC also recommended (2015-16), on similar irregularity pointed out in Audit Report for 2006-07, that, besides recovery of tax with interest the Department should avoid reoccurrence of such irregularities. The PAC held the departmental officers responsible for not initiating appropriate action on accepted cases.

The Department had not adopted the HSN code and there was no monitoring measure in the Department which could have a deterrent effect on the AAs to strictly follow the provisions of the Acts, Rules and departmental Circulars in order to classify the commodity correctly and apply the appropriate rate of tax.

#### **Recommendation:**

**The Department should adopt the Harmonised System of Nomenclature Code expeditiously, and also implement the recommendations/ directions of the Public Accounts Committee to initiate measures that will ensure non-recurrence of such irregularities in future.**

### **3.11 Short levy of tax/grant of irregular concession under CST Act**

**Failure of AAs to apply provisions relating to inter-state sales resulted in short realisation of tax of ₹ 2.52 crore and non-levy of penalty of ₹ 4.45 lakh.**

The Central Sales Tax (CST) Act stipulates that if a dealer claiming tax on inter-state sales (entitling him to pay tax at two *per cent* of turnover) fails to furnish the required declaration in Form 'C' signed by the purchasing dealer, he shall be liable to pay tax at the rate applicable to the sale or purchase of

<sup>47</sup> DCCT- Ujjain

<sup>48</sup> ACCT- Jabalpur II

<sup>49</sup> CTO- Bhopal I, Bhopal V, Chhindwara I, Chhindwara II, Gwalior IV, Harda I, Khargone and Katni II.

<sup>50</sup> Harmonised System of Nomenclature is an internationally adopted commodity description and coding system.

such goods inside the appropriate State, and in addition, pay penalty at three times of the tax so assessed.

Audit test check (between October 2016 and February 2017) of records of two divisional offices<sup>51</sup>, five circle offices<sup>52</sup> and office of the Assistant Commissioner, Neemuch revealed that in nine cases of nine dealers assessed between April 2015 and December 2015 for the assessment years between 2012-13 and 2014-15, the AAs allowed incorrect concession under CST Act.

Audit observed that in seven cases the AAs incorrectly allowed concessional rate of tax on interstate sales not supported with declaration in Form 'C'. The AAs applied two *per cent* tax in three cases where five *per cent* tax was applicable and five *per cent* or two *per cent* tax in four cases where 13 *per cent* tax was applicable. In one case AA did not include interstate sale which was not supported by Form 'C' in GTO. Further, in one case there was calculation mistake (two *per cent* CST was leviable, however less than 0.2 *per cent* was levied). This resulted in short realisation of tax of ₹ 2.52 crore and non-levy of penalty of ₹ 4.45 lakh.

In the exit conference (November 2017), the Department assured that reassessment would be done. Final action was awaited (May 2018).

Similar observations were pointed out in previous Audit Reports from 2011-12 to 2015-16. Audit observed that the AAs committed errors in the assessments ignoring clear provisions in the Act regarding applicability of the appropriate rate of tax.

### 3.12 Irregular grant of deduction

**Incorrect allowance of deductions by AAs resulted in short levy of tax of ₹ 1.92 crore including penalty of ₹ 72.80 lakh.**

The MPVAT Act provides a formula to arrive at the amount of taxable turnover and states that no deduction on the basis of formula shall be made if the amount by way of tax collected by registered dealer had been otherwise deducted from the aggregate of sale prices or not included in the sale prices. Sales returns beyond six months are not admissible. Further, deduction is not allowed if the transaction is not supported by prescribed declaration forms.

Audit test check of records in two regional offices<sup>53</sup> and 10 circle offices<sup>54</sup> and revealed that in 19 cases of 12 dealers, assessed between July 2014 and January 2016 for the years 2011-12 to 2013-14, the Assessing Authorities (AA) allowed irregular deductions as follows: in 10 cases, the AAs allowed deduction of tax from the aggregate of sale price though the same was not included in it; in two cases incorrect deduction of freight from the Gross Turnover (GTO) was allowed; and in the seven remaining cases incorrect deduction of sales return beyond six months, discount and interstate sales not supported by declaration forms was given. These irregular allowance of

<sup>51</sup> DCCT- Indore III and Ratlam.

<sup>52</sup> CTO- Bhopal IV, Bhopal V, Chhindwara I, Indore II and Indore VII.

<sup>53</sup> ACCT- Bhopal III and Katni I.

<sup>54</sup> CTO- Bhopal I, Bhopal V, Bina, Damoh, Dewas, Gwalior III, Harda I, Indore VII, Indore XI and Mandla.

deductions resulted in short levy of tax of ₹ 1.92 crore including penalty of ₹ 72.80 lakh.

Similar observations were pointed out in previous Audit Reports from 2011-12 to 2015-16. Audit observed that despite clear provisions in the Act and instructions of the Department, AAs did not adopt uniform approach to deal with the assessment cases. While determining taxable turnover, AAs were allowing deductions arbitrarily and data/information available with the Department was also not taken into cognizance in some of the cases.

In the exit conference (November 2017), the Department intimated that reassessment of cases was under process. Final action was awaited (May 2018).

### **3.13 Tax short/ not levied under Luxury, Entertainment, Amusement and Advertisement Tax Act**

**Underassessment by AAs of luxury tax in seven cases, entertainment tax in one case and advertisement tax in one case, resulted in short-levy of tax of ₹ 37.75 lakh and penalty of ₹ 1.13 crore.**

Luxury, entertainment and advertisement tax are leviable in terms of the Madhya Pradesh Luxury, Entertainment, Amusement and Advertisement Tax Act (MP LEAT Act), 2011.

Audit test check of records of three circle offices<sup>55</sup> for the period from 2012-13 and 2013-14 revealed that the AAs under-assessed the tax in nine cases, as follows. In five cases rent receipts from rooms attached to marriage/ banquet halls, and in two cases hotel facilities and banquet sales were not taken in gross turnover (GTO), resulting in short levy of luxury tax of ₹ 32.93 lakh. In one case income from advertisement was not included in GTO resulting in short levy of ₹ 2.54 lakh. In one case the dealer was allowed 10 *per cent* entertainment tax on guest charges, which was allowable only for regular members, resulting in short levy of ₹ 2.29 lakh. In all, tax amounting to ₹ 1.51 crore including penalty of ₹ 1.13 crore was short levied.

The Department did not adopt a uniform approach to deal with the assessment cases. AAs were allowing or disallowing amounts pertaining to transactions arbitrarily despite clear provisions.

In the exit conference (November 2017), the Department intimated that reassessment of cases was under process. Final action was awaited (May 2018).

<sup>55</sup> CTO- Indore, Jabalpur and Gwalior (Amod Vilas).