# CHAPTER II : SALES TAX

## 2.1 Results of audit

Test check of the records of the Sales Tax Department conducted during the year 2008-09, revealed underassessment/short levy/loss of revenue amounting to Rs. 1,862.78 crore in 734 cases as shown below :

**(Rupees in crore)**

| Sl. no. | Category | No. of cases | Amount |
|---|---|---|---|
| 1. | **Sales Tax incentives under Package Scheme of Incentives (A Review)** | 1 | 1,501.04 |
| 2. | **Transition from Sales Tax to VAT (A Review)** | 1 | 5.72 |
| 3. | Excess claim of compensation under VAT | 31 | 277.99 |
| 4. | Non/short levy of tax | 461 | 16.15 |
| 5. | Incorrect grant of set off/Input Tax Credit | 85 | 9.11 |
| 6. | Non/short levy of Interest/Penalty | 34 | 13.39 |
| 7. | Other Irregularities | 121 | 39.38 |
| **Total** | | **734** | **1,862.78** |

In response to the observations made in the local audit reports during the year 2008-09 as well as during earlier years, the department accepted underassessments/other deficiencies involving Rs. 20.62 crore in 242 cases. Out of this, 10 cases involving Rs. 6.04 lakh were pointed out during 2008-09 and the rest during earlier years. During the year 2008-09, the department recovered Rs. 52.33 lakh in 122 cases out of which Rs. 4.19 lakh in four cases were pointed out during 2008-09 and the rest in earlier years.

Two reviews, viz. "**Sales Tax incentives under Package Scheme of Incentives**" and "**Transition from Sales Tax to VAT**" involving a total financial effect of Rs. 1,506.76 crore and a few audit observations involving Rs. 307.46 crore are mentioned in the following paragraphs, against which an amount of Rs. 4.02 lakh had been recovered upto November 2009.

## 2.2 Review on Sales Tax incentives under "Package Scheme of Incentives"

### Highlights

Centralised database of incentives sanctioned, availed of by way of exemption and deferred tax was not available with the department.

**(Paragraph 2.2.6)**

Incentives of Rs. 11.32 crore were not recovered from 45 units which were closed during the operative period of the Eligibility Certificate.

**(Paragraph 2.2.7.2)**

In three of the five test checked divisions, the Sales Tax Department did not have the information of 66 closed units; in two of these divisions 20 units had availed incentives of Rs. 3.93 crore.

**(Paragraphs 2.2.7.3)**

In four divisions, 6,956 cases were pending for assessment of which 177 assessments were pending for more than 10 years.

**(Paragraph 2.2.9)**

In five divisions, instalments of deferred taxes amounting to Rs. 39.21 crore were not recovered in 74 cases.

**(Paragraph 2.2.10)**

Breach of conditions of production in one case resulted in non-recovery of incentives of Rs. 258.41 crore.

**(Paragraph 2.2.11)**

Incentives amounting to Rs. 1,034.47 crore were sanctioned to 30 units in excess of the prescribed norms.

**(Paragraphs 2.2.12 and 2.2.13)**

Incorrect allowance of exemption to one unit resulted in underassessment of tax of Rs. 174.10 crore including the interest of Rs. 46.08 crore.

**(Paragraph 2.2.15)**

In respect of four units, taxes of Rs. 13.48 crore on inter-State sale of goods not supported by declarations in form "C" was incorrectly considered for calculation of Cumulative Quantum of Benefits (CQB).

**(Paragraph 2.2.16)**

Incorrect levy of sales tax, surcharge and turnover tax in respect of five units resulted in short levy of tax of Rs. 3.17 crore and consequential short determination of CQB.

**(Paragraph 2.2.17)**

### 2.2.1 Introduction

A Package Scheme of Incentives (PSI) was introduced in 1964 to encourage dispersal of industries outside Bombay-Thane-Pune belt and attract industries to the developing and undeveloped areas of the State. The scheme was amended from time to time, the last amendment being in 2007. Under the scheme, sales tax incentives by way of exemption/deferral/interest free

unsecured loan, special capital incentives for Small Scale Industries units, refund of octroi/entry tax/electricity duty, concession in the capital cost of power supply and contribution towards the cost of feasibility study were given to new/pioneer/prestigious units as well as to the existing units undertaking expansion/diversification.

The Industries Department issues Eligibility Certificates (ECs) to the PSI units for sales tax incentives indicating quantum of benefits to be availed of, period of eligibility, finished products to be manufactured and other terms and conditions. On the basis of ECs, the Sales Tax Department issues Certificates of Entitlement (COEs) and monitors the quantum of benefits availed by the PSI units. The review mainly focused on the PSI schemes of 1988 and 1993. The salient features of the 1988 and 1993 Schemes relating to sales tax incentives are mentioned in the following table:

**Table: PSI Schemes 1988 and 1993**

| Scheme | Sales Tax incentives | Monetary ceiling | Period of eligibility | Remarks |
|---|---|---|---|---|
| PSI 1988 | Exemption or deferring of sales tax, turnover tax and additional tax on sale of finished products, purchase tax/additional tax on purchases of raw materials under BST[1] Act and tax payable under Central Sales Tax Act. | i) For original unit. 60 *per cent* to 100 *per cent* of Fixed Capital Investment.<br>ii) For expansion/ diversification. 50 *per cent* to 90 *per cent* of Fixed Capital Investment. | Five to 10 years or earlier if the ceilings are reached.<br>Four to nine years or earlier if the ceilings are reached. | i) Quantum of incentives and period linked with category of unit and location.<br>ii) Finished product includes scrap and byproducts.<br>iii) Deferring of tax for 10 years and the deferred amount thereafter payable in five equal annual instalments. |
| PSI 1993 | Same as above | i) For original unit 60 *per cent* to 160 *per cent* of Fixed Capital Investment.<br>ii) For expansion /diversification undertaken by the SSI/LSI/MSI[2] the percentage restricted to 75 *per cent* of amount admissible to new unit. | Five to 15 years or earlier if the ceilings are reached. | Same as above. |

### 2.2.2 Organisational set-up

The Industries Department is responsible for implementation of the PSI through the Development Commissioner (DC) (Industries), Mumbai, its Regional Offices and District Industries Centres (DIC).

[1] Bombay Sales Tax
[2] Small Scale Industry, Large Scale Industry and Medium Scale Industry

The Finance Department through the Commissioner of Sales Tax monitors the sales tax incentives availed of by the PSI units and effects the recovery in the deferral cases. Commissioner of Sales Tax is assisted by the Additional Commissioners, Joint Commissioners, Senior Deputy Commissioners, Deputy Commissioners, Assistant Commissioners and Sales Tax Officers. At functional level the sales tax divisions are headed by the Joint Commissioners.

### 2.2.3 Scope of audit

This review was limited to the PSI schemes of 1988 and 1993. The assessments finalised during the period 2003-04 to 2007-08 under the BST Act along with the records of the Development Commissioner and the DICs were test checked between December 2008 and June 2009 for the purpose of the review. Out of nine divisions[3] in which the schemes were implemented, five divisions[4] which covered 93 *per cent* of the incentives sanctioned were selected by adopting statistical sampling technique (Probability Proportional to Size method). The details of the statistical sampling technique is explained at **Annexure II.**

### 2.2.4 Audit objectives

The review was conducted with a view to ascertain whether:

- incentives sanctioned by the implementing agencies were as per norms;
- assessment of the units was taken up on priority to detect excess/ incorrect availing of incentives;
- repayment of instalments of incentives due from the deferral units were effected within the prescribed time period;
- prompt action was taken to recover the incentives from the units which were closed prematurely;
- quantum of incentives claimed by the eligible units were properly assessed;
- a system existed for sharing of information between implementing agencies and sales tax authorities; and
- an internal control mechanism existed to prevent the loss of revenue and misuse of the provisions of the schemes.

### 2.2.5 Acknowledgement

The Indian Audit and Accounts Department acknowledges the co-operation of Sales Tax Department and Offices of the Development Commissioner and DICs for providing necessary information and records for audit. An entry conference was held (February 2009) and the executives were informed about the selection of divisions and scope and methodology of audit. The Joint Commissioner of Sales Tax (Incentives), Deputy Commissioner of Sales Tax (Incentives) and other officers of the Sales Tax Department explained the

[3] Amravati, Aurangabad, Kolhapur, Nagpur, Nanded, Nashik, Pune, Solapur and Thane.
[4] Aurangabad, Nagpur, Nashik, Pune and Thane.

various aspects of the scheme viz. maintenance of records, determination of sales tax incentives, procedure for assessments and recovery. The draft review report was forwarded to the Government and to the department in July 2009 and the audit conclusions and recommendations were discussed in the exit conference held in October 2009. Principal Secretary, Finance Department and Under Secretary, Industries Department represented the Government while Commissioner of Sales Tax and Joint Director, Director of Industries represented the department. The replies given during the discussion and at other times have been appropriately included in the relevant paragraphs.

## Audit findings

## System deficiencies

### 2.2.6 Absence of database on incentives availed

Under the Package Scheme of Incentives, the Government of Maharashtra (GoM) allowed the manufacturing units to either defer or exempt the payment of Sales Tax, Central Sales Tax, Turnover Tax (TOT), Surcharge (SC) and the Purchase Tax (PT) including the SC on the purchase of raw materials. The details of incentives[5] for which ECs have been issued to large scale industries/medium scale industries under 1988 and 1993 schemes are as under:

**(Rupees in crore)**

| **1988 Scheme** | | | | **1993 Scheme** | | | |
|---|---|---|---|---|---|---|---|
| **Deferral** | | **Exemption** | | **Deferral** | | **Exemption** | |
| **No of ECs** | **Amount** | **No of ECs** | **Amount** | **No of ECs** | **Amount** | **No of ECs** | **Amount** |
| 556 | 3,992 | 752 | 7,531 | 697 | 12,954 | 628 | 21,683 |
| Incentive periods from 1992 to 2012 | | Incentive periods from 1992 to 2014 | | Incentive periods from 1996 to 2022 | | Incentive periods from 1999 to 2013 | |

In order to keep a proper watch on the implementation of the PSI schemes it is essential to have a database of unit-wise incentives sanctioned, progressive incentives availed of by the units, units closed prematurely, incentives availed of by the closed units, recoveries effected from these closed units and recoveries made from the deferral units after the moratorium period provided under the schemes.

Audit scrutiny indicated that neither the implementing agencies nor the Sales Tax Department had maintained a database in this regard. In the absence of any database, the departments could not monitor the performance of the PSI units effectively as brought out in the succeeding paragraphs.

After this was pointed out, the Development Commissioner stated (June 2009) that the information would be available with the Sales Tax Department. However, the Sales Tax Department also did not have the database of the above information. This revealed the lack of coordination between the Sales Tax Department and the Implementing Agency.

[5] Details of incentives in respect of small scale industries (SSI) are awaited from the department.

**The Government may consider maintaining a centralised database of incentives sanctioned, availed of etc., for proper evaluation and implementation of the PSI**.

### 2.2.7 Absence of recovery and monitoring mechanisms

As per the Package Scheme of Incentives and the eligibility certificates issued by the implementing agencies, if a unit is closed or continues to remain at below normal production during the operative period of the agreement or the eligibility certificate is cancelled, the amount of sales tax incentives availed of by the unit is recoverable forthwith with interest/penalty at the prescribed rates. Further, in respect of the exemption and deferral mode of incentives, the Sales Tax Department is required to intimate the date of closure as well as the quantum of incentives availed of by the unit upto the date of closure to the implementing agency for cancellation of the eligibility certificate. Under the deferral mode, Commissioner of Sales Tax may be moved by the implementing agency to recover the amount of sales tax liability deferred alongwith penal interest (at the rate of 22.5 *per cent*). In respect of the units under the exemption mode the implementing agency has to initiate recovery proceedings alongwith interest at the rate of 16.5 *per cent*, if not paid on demand, the Government shall be entitled to recover the same as arrears of land revenue.

**2.2.7.1** Audit scrutiny revealed that neither the Implementing Agency nor the Sales Tax Department has taken appropriate measures to ensure timely recovery of the incentives from closed units. The information furnished by the Development Commissioner (Industries) revealed that incentives aggregating Rs. 680 crore were recoverable from 85 closed units which had availed of incentives under 1993 scheme, but Revenue Recovery Certificates (RRCs) had been issued in seven cases only**.** This necessitates the creation of a suitable mechanism to ensure recovery of the Government revenue.

**2.2.7.2** Information obtained from five divisions[6] indicated that 45 eligible units which had availed incentives of Rs. 11.49 crore between March 1985 and April 2007 were closed during various periods between March 2004 and April 2007 as shown below:

**(Rupees in crore)**

| Division | Exemption | | | Deferral | | | Total | |
|---|---|---|---|---|---|---|---|---|
| | Period of scheme closure | No. of units | Amount | Period of scheme closure | No. of units | Amount | No. of units | Amount |
| Nashik | 10/00 to 9/06<br>9/06 | 1 | 0.13 | 1/96 to 12/06<br>10/05 | 1 | 0.15 | 2 | 0.28 |
| Thane | 1/90 to 4/06<br>4/04 to 4/06 | 8 | 3.01 | 3/85 to 4/07<br>9/04 to 4/07 | 6 | 1.35 | 14 | 4.36 |
| Pune | 12/91 to 4/05<br>4/04 to 4/05 | 13 | 1.95 | 10/97 to 4/06<br>4/04 to 4/06 | 2 | 0.68 | 15 | 2.63 |
| Nagpur | 5/95 to 7/06<br>4/04 to 7/06 | 10 | 0.37 | - | 0 | 0 | 10 | 0.37 |
| Auran-gabad | 4/94 to 3/04<br>3/04 | 1 | 1.23 | 11/88 to 6/05<br>3/04 to 6/05 | 3 | 2.62 | 4 | 3.85 |
| **Total** | **1/90 to 9/06** | **33** | **6.69** | **3/85 to 4/07** | **12** | **4.80** | **45** | **11.49** |

[6] Aurangabad, Nagpur, Nashik, Pune and Thane.

The Sales Tax Department intimated closure in respect of 34 units to the implementing agencies after delays ranging from five to 58 months. An amount aggregating Rs. 17.16 lakh only, out of Rs. 9.66 crore recoverable from these units had been recovered upto March 2009. In the remaining 11 cases, no information was furnished by the department to the implementing agency to cancel the EC and to recover the amount. Sales tax incentives availed of by these units aggregated Rs. 1.83 crore till the date of closure. Non/delayed intimation on the part of the Sales Tax Department thus resulted in non-recovery of Rs. 11.32 crore and possibility of loss of this revenue due to passage of time.

**2.2.7.3** In order to ascertain the correctness of the information of closed units furnished by the department, audit called for information from the test checked divisions for carrying out independent cross-check of the data furnished by the Sales Tax Department in respect of the units covered under the 'Package Scheme of Incentives'. Information was received from three out of the five test checked divisions only which were cross-checked with the data obtained from the Industries Department and the Central Excise Department.

- Cross-check of the information received in respect of Nagpur and Pune divisions of the Sales Tax Department with the information furnished by the concerned DICs revealed that 41 units of Nagpur division and 10 units of Pune division which were closed during the operative period of the agreement did not feature in the list furnished by the Sales Tax Department. In respect of the 10 units of Pune division, the incentives availed of by the units was Rs. 2.43 crore. Details of incentives availed of by the closed units under Nagpur division have not been received so far.

- Cross-check of information pertaining to live units collected from the Sales Tax Department (Thane Division) with the data of live units furnished by the concerned Central Excise Department (CED) revealed that of the 94 units considered as live by the Sales Tax Department, 15 units did not feature in the list of live units furnished by the CED. On further verification with the records of Sales Tax Department it was noticed that actually six of these units were closed, three were filing 'nil' returns with effect from 1 April 2005 and one unit had not renewed its registration after the introduction of Value Added Tax. These 10 units had availed of incentives totalling Rs. 1.50 crore. The Sales Tax Department had not taken any action to get the ECs of these defaulting 10 units cancelled. Information in respect of the remaining five units was not available with the department.

This indicated lack of coordination between the Sales Tax Department and the implementing agencies and also absence of monitoring of the status of units for timely recovery of incentives from the closed units.

**The Government may institute an effective system in the implementing agencies for initiating action for prompt recovery and a system may be put in place by the Government for effective coordination between the implementing agencies and the Sales Tax Department for monitoring of recoveries in respect of closed units.**

**Compliance deficiencies**

### 2.2.8 Absence of monitoring of the units through prescribed returns

The Government resolution (GR) relating to PSIs stipulates that the PSI units have to submit the certified true copy of annual sales tax returns within one month from the date of its submission to the Sales Tax Department and audited annual statement of accounts and balance sheet within nine months from close of the year to the implementing agency. The PSI units are also required to furnish information regarding production and sales indicating the period of stoppage of production and /or closure, if any, with reasons thereof. Failure on the part of the eligible unit to submit any of the above information/ document within the specified time period shall tantamount to breach of the provision entailing cancellation of EC and recovery of incentives.

Test check of the records of the Development Commissioner, Mumbai indicated that 284 out of 1,325 units, were sanctioned sales tax incentives of Rs. 8,893.44 crore under 1993 scheme, did not submit the annual sales tax returns, report comprising details of production and sales, stoppage of production, closure of unit, addition to fixed capital investment, disposal of fixed assets, change in the constitution of the unit and certified true copies of audited annual accounts. Though there was breach of conditions prescribed in the G.R. by these units, the implementing agency did not initiate action to cancel the EC as per the provisions of the GR (July 2009).

### 2.2.9 Delay in assessment

As per the provisions of the BST Act, 1959 and the rules made thereunder, where a dealer files all the returns within six months of the end of the assessment year, the assessments are to be completed within three years and in other cases the assessments are to be completed within eight years. In respect of units covered under the PSI the Sales Tax Department is required to assess the returns of the eligible units on priority and take appropriate and timely steps to prevent availing of incentives in excess of admissible monetary ceiling.

Test check of the records in Aurangabad, Nagpur, Pune and Thane divisions indicated that 6,956 assessments of dealers covered by the PSI schemes (both under deferral and exemption modes) were pending as of March 2008, of which 177 assessments were pending for more than 10 years. Out of 30 units in Thane division assessments in 22 units were pending, returns in respect of seven dealers were not available with the department and one dealer had not filed any return. In the case of 22 units where assessments were pending, the sales tax incentives availed as per returns were Rs. 2.71 crore. Since in the case of deferral units, the maximum period upto which tax was allowed to be deferred was 4 to 15 years depending upon the schemes, non-assessment of these units not only resulted in non-fixation of instalments for recovery but there was also the possibility of the amount not being recovered due to closure of such units. Similarly, in respect of cases covered by the exemption mode, due to non-finalisation of assessment on time, the cumulative quantum of benefit availed by these units in excess of monitory ceiling was not available

with the department. Though the status of pending assessments with the assessing authority is watched by the department no effective steps were taken to liquidate the huge arrears in assessment. Thus, Sales Tax Department was not following its own directions to assess the eligible units on priority basis. Audit observed that no mechanism was evolved in the Sales Tax Department to monitor completion of assessments of exempted/deferred units on priority basis.

### 2.2.10 Non-payment of instalments

Under the PSI the tax allowed to be deferred is payable after 10 years in five equal annual instalments. After completion of the deferral period Sales Tax Department fixes the instalments after assessment of the dealer to recover the deferred taxes. As per the circular dated 4 December 1991 issued by the Commissioner of Sales Tax, the respective assessing officers are required to maintain a register in Form 78 and note the details of instalments fixed and the due date of payment of instalment.

Scrutiny of the register in Form 78 in five test checked divisions indicated that deferred instalments aggregating Rs. 39.21 crore were not recovered in 74 cases as shown below**:**

**(Rupees in crore)**

| Sl. no. | Division | No. of assessing officers | No. of dealers | Amount |
|---|---|---|---|---|
| 1. | Aurangabad | 2 | 9 | 7.03 |
| 2. | Nagpur | 4 | 7 | 1.53 |
| 3. | Nashik | 1 | 5 | 7.13 |
| 4. | Pune | 6 | 21 | 8.85 |
| 5. | Thane | 8 | 32 | 14.67 |
| **Total** | | **21** | **74** | **39.21** |

After the cases were pointed out by audit, between December 2008 and April 2009, the department stated that recovery of Rs. 6.34 crore was under progress in respect of 16 units. Incentives aggregating Rs. 6.10 crore recoverable from five units were referred to the Board of Industrial and Financial Reconstruction (BIFR) and Rs. 5.31 crore recoverable from six units were already closed. Reply is still awaited for remaining 47 units (October 2009).

This indicated that recovery from the dealers was not being monitored by the department effectively.

### 2.2.11 Non-recovery of incentives for breach of conditions of production

As per procedural rules of 1988, a pioneer unit was required to maintain normal level of production for a period of 25 years from the date of grant of EC. The incentives availed were liable to be recovered on breach of condition to maintain the normal level of production.

In Thane Division, M/s. Reliance Industries Limited (manufacturer) was granted three separate ECs under 1983, 1988 and 1993 schemes for expansion. The EC period under 1983 scheme was between 1988 and 1997 and the operative period was upto 2012 as the unit was a pioneer unit. Test check of the assessment records of the manufacturer, for the year 1999-2000 and

2000-01, finalised in September and October 2004 respectively, indicated that the manufacturer had bifurcated his entire production under the ECs granted for expansion of 1988 and 1993 Schemes. The manufacturer did not show production from expansion made under EC of 1983, though the operative period under that scheme was not over. Hence, the manufacturer had breached the condition of maintaining normal production as far as it relates to 1983 Scheme. Thus incentive of Rs. 258.41 crore availed of by the manufacturer in the form of exemption during October 1993 to June 1997 was liable to be recovered. No action was taken by the department to recover the amount (November 2009).

### 2.2.12 Excess sanction of incentives under PSI 1988

As per the provisions contained in paragraph 5.2(i) and 5.2(ii) of the GR dated 30 September 1988, the quantum of sales tax incentives admissible to a new unit/pioneer unit was 95 *per cent* of the fixed capital investment (FCI) and a pioneer unit undertaking expansion/diversification was 80 *per cent* of FCI under PSI 1988 scheme irrespective of the area in which the unit was located. Further, as per clause 5.9(d) of the said GR the implementing agency and the sales tax authorities shall independently examine the position to ensure that the sales tax incentives availed of are well within the ceilings specified, relates to the eligible product manufactured by the unit and the production capacity specified therein.

Test check of the records in Thane Division indicated that the erstwhile implementing agency namely State Industries and Investment Corporation of Maharashtra Limited (SICOM Ltd.) sanctioned (October 1995) sales tax incentives of Rs. 555.85 crore at 95 *per cent* of the fixed capital investment of Rs. 585.11 crore. However, being a pioneer unit seeking expansion/ diversification, the sales tax incentives were admissible at 80 *per cent* of Rs. 585.11 crore which worked out to Rs. 468.09 crore. This resulted in excess sanction of incentives of Rs. 87.76 crore.

After the case was pointed out, the Department stated (January 2009) that the EC for the said amount had been issued by the implementing agency and the case would be reported to them. The fact remains that Sales Tax Department was required to independently verify the correctness of the sales tax incentives sanctioned for granting certificate of entitlement. The reply from the Development Commissioner is awaited (November 2009).

### 2.2.13 Excess sanction of incentives under PSI 1993

As per the provisions contained in paragraph 5.1 (ii) of the GR dated 7 May 1993, regulating the PSI 1993, the quantum of sales tax incentives sanctioned to a new unit/pioneer unit in 'B' and 'C' area was 80 and 95 *per cent* of fixed capital investment respectively. The eligibility period was for a period of seven years or on reaching the ceiling, whichever was earlier. The resolution was amended (July 1994) whereby the period was extended upto 14 years if the investment made was Rs. 300 crore and above. Further, the quantum of incentives admissible to any unit seeking expansion was restricted to 75 *per cent* of that admissible to a new unit. As per clause 6.1(iv) of the said GR the implementing agency and the sales tax authorities shall independently

examine the position to ensure that the sales tax incentives drawn/availed of are well within the ceilings specified and relates to the eligible product and capacity.

**2.2.13.1** Test check of the records in Thane Division revealed that the erstwhile implementing agency SICOM Ltd. had sanctioned (December 1994) sales tax incentives of Rs. 651.83 crore at 95 *per cent* of the fixed capital investment of Rs. 686.13 crore to one unit. However, being a new pioneer unit in 'B' area, the sales tax incentive was admissible at 80 *per cent* of FCI (Rs. 683.13 crore) which worked out to Rs. 548.90 crore. This resulted in excess sanction of incentives of Rs. 102.93 crore.

After the case was pointed out, the Development Commissioner stated (June 2009) that the case was being examined in the light of the audit observation.

**2.2.13.2** Test check of the records of Development Commissioner, Mumbai revealed that in respect of 28 units seeking expansion, ECs were issued sanctioning sales tax incentives aggregating Rs. 3,375.10 crore. However, in these cases the dealers had sought sales tax incentives for expansion of existing pioneer units, hence the incentives admissible was aggregating Rs. 2,531.32 crore only. This resulted in excess sanction of incentives of Rs. 843.78 crore.

After these cases were pointed out, the Development Commissioner stated (June 2009) that the issue of granting incentives to pioneer units at the rate of 75 *per cent* was pending in the High Court at Mumbai in respect of the petition filed by M/s. ACC Ltd. and M/s. Jain Irrigation Ltd.

## 2.2.14 Non-maintenance of normal level of production

As per paragraph 11.16 of the procedural rules for regulating PSI, if the eligible unit to which an EC has been issued fails to maintain normal level of production during a year, the unit shall be liable to repay the sales tax incentives availed of upto the date of stoppage of the normal production in the manner and the extent prescribed in the rules.

Test check of the records in Pune division indicated that two units failed to maintain normal production during the operative period of the agreement after availing of incentives aggregating Rs. 52 lakh on which interest of Rs. 14 lakh was leviable as shown below:

**(Rupees in crore)**

| **Sl. no.** | **Division No. of dealers** | **EC Period Operative period** | **Period of availment** | **Tax/ Interest Total** | **Amount paid** | **Balance** |
|---|---|---|---|---|---|---|
| 1. | Pune 2 | March 1996 - December 2000 upto February 2011 | 1998-2001 | 0.38/Nil 0.38 | Nil | 0.38 |
| | | December 1997 - October 2004 upto November 2012 | 1998-2001 | 0.14/0.14 0.28 | Nil | 0.28 |
| **Total** | | | | **0.52/0.14 0.66** | | **0.66** |

After the cases were pointed out, the department stated (March 2009) that implementing agency would be intimated to cancel the EC and recover the incentive availed.

### 2.2.15 Incorrect allowance of CQB resulting in underassessment of tax

As per the PSI, a manufacturer in an eligible unit is entitled to avail of incentives under the exemption mode in respect of sales tax, purchase tax, Central Sales Tax and sales of finished goods, which are mentioned in the EC during the period covered in the eligibility and entitlement certificates within the admissible monetary ceiling. Further, as per the determination order[7] passed by the Commissioner of Sales Tax in September 2006 in the case of M/s.Bharat Petroleum Corporation Ltd. (BPCL), it was held that the return of kerosene purchased from BPCL after extraction of "N-Paraffin" therefrom is a 'goods return' as the physical and chemical characteristics of the returned kerosene remains the same. Thus, kerosene after extraction of "N-Paraffin" would not be a different product.

Test check of the records of Thane division revealed that M/s. Reliance Industries Limited, a dealer who was granted EC by the implementing agency for manufacturing purified teraphthalic acid (PTA), linear alkyl benzene (LAB), polyster filament yarn (PFY) and polyster staple fibre (PSF) had imported kerosene valued at Rs. 828.87 crore and also purchased kerosene for Rs. 826.57 crore from the BPCL during the years 1999-2000 and 2000-01. After extraction of "N-Paraffin" from the kerosene, the balance quantity valued at Rs. 697.27 crore was returned to BPCL without levy of tax as per the determination order passed by the Commissioner of Sales Tax, Mumbai. The remaining kerosene valued at Rs. 816.11 crore out of the imported purchases was sold locally as well as inter-State. Since the sales were first point sales in the State of Maharashtra, tax of Rs. 128.02 crore was levied on these sales in the assessment orders passed in September and October 2004 and was considered for calculating the CQB for exemption from payment of the tax. Since kerosene was not manufactured in the eligible unit and was not covered by EC, exemption of payment of tax on kerosene was incorrect and was liable to be recovered. Grant of incorrect exemption resulted in underassessment of tax of Rs. 174.10 crore including interest of Rs. 46.08 crore.

After this was pointed out, the department stated (April 2009) that the case was under revision.

### 2.2.16 Incorrect allowance of CQB on inter-State sales

Under the provisions of the Central Sales Tax Act, tax on sales in the course of inter-State trade or commerce, supported by valid declarations in form 'C', is leviable at the rate of four *per cent* of the sale price. In respect of declared goods, tax is leviable at twice the rate applicable on sales inside the State and in respect of goods other than declared goods, at 10 *per cent* or at the rate of tax applicable to the sale or purchase of such goods inside the State, whichever is higher. Further, the Commissioner of Sales Tax by a trade circular dated

[7] Determination Order No. DDQ-11/2005/Adm-5/Remand/86-87/B-2 dated: 11 September 2006 in the case of M/s. Bharat Petroleum Corporation Ltd. and Reliance Industries Ltd.

20 July 2002 clarified that inter-State sales by a registered dealer, which are supported with declarations in form 'C', of an eligible unit, will alone qualify for benefit of exemption from Central Sales Tax under the PSI with effect from June 2002. Due to this, inter-State sales which are not supported with declarations in form 'C' cannot be considered for calculation of CQB under PSI.

Test check of records in Thane and Pune divisions indicated that in the assessments of four cases, finalised between January 2006 and October 2007, inter-State sales of Rs. 106.69 crore effected during the periods 2002-03 and 2004-05 were incorrectly exempted from levy of tax though these sales were not supported by declarations in form 'C'. As a result, Central Sales Tax aggregating Rs. 13.48 crore was incorrectly considered for determining the CQB. Thus, Central Sales Tax aggregating Rs. 14.73 crore including interest of Rs. 1.25 crore was recoverable from these units.

After this was pointed out, the department intimated (January 2009), that action to revise the assessment in one case involving Rs. 10.87 crore of Thane division had been initiated. Replies in the remaining three cases are awaited (November 2009).

### 2.2.17 Short determination of CQB

Under the PSI an eligible unit is entitled for exemption from sales tax, TOT and SC payable on sales and PT and SC on tax payable on purchase of raw material used in the manufacture of finished goods mentioned in the EC. Rule 31AA(2)(e) of BST Rules, 1959 contains provision for the calculation of the quantum of incentives admissible to the unit. The rate of tax leviable on any commodity is determined with reference to the relevant entry in schedule B or C of the BST Act, 1959.

Test check of the records in Nashik, Nagpur and Thane divisions indicated that in the assessments of five dealers finalised between January 2006 and June 2007, for various periods between 2000-01 and 2004-05, there was underassessment of tax aggregating Rs. 3.17 crore due to non/short levy of sales tax, TOT, SC and PT, resulting in short determination of CQB.

After the cases were pointed out between December 2008 and April 2009, the department accepted the observations and stated (October 2009) that corrective action had been initiated.

### 2.2.18 Short deferment of tax

As per the BST Rules, an eligible industrial unit registered under the BST Act was allowed to defer the payment of sales tax and PT on the purchase of raw materials. Besides, TOT and SC leviable was also allowed to be deferred. Further, if a dealer purchased goods specified in Part-I of Schedule 'C' of the Act and used such goods in the manufacture of taxable goods and had dispatched the manufactured goods to his own place of business or to his agent's place of business situated outside the state but within India, then such a dealer was liable to pay PT at the rate of two *per cent* on the turnover of such purchases.

Test check of the records in Nagpur and Nashik divisions indicated that in the assessment of three dealers for various periods between 1999-00 and 2002-03 there was underassessment and consequential short deferring of taxes of Rs. 24.92 lakh due to incorrect levy of sales tax, PT, SC and TOT as mentioned below:

**(Rupees in lakh)**

| **Sl. no.** | **Division No. of dealers** | **Period** | **Name of Commodity** | **Nature of irregularity** | **Turnover of sales/ purchases** | **Tax leviable levied (*per cent*)** | **Under assessment Tax/ TOT/ SC** | **Total** |
|---|---|---|---|---|---|---|---|---|
| 1. | Nashik<br>1 | 1999-2000 | Paints | PT u/s 14(1) was not levied on purchases against Form 15EC, used in the manufacture of goods and sent to branches outside Maharashtra within India | 671.38 | 2<br>Nil | 13.43<br>4.03 | 17.46 |
| 2. | Nagpur<br>2 | 2002-2003 | Grinding wheels | - do - | 140.41 | 2<br>Nil | 2.80<br>0.84 | 3.64 |
| | | 2001-2003 | Chemicals | Sales of chemicals was incorrectly subjected to tax rate of 8 *per cent* instead of 13 *per cent* | 69.48 | 13<br>8 | 3.47<br>0.35 | 3.82 |
| **Total** | | | | | | | **19.70<br>5.22** | **24.92** |

After the cases were pointed out between January 2009 and April 2009, the department accepted the observation in two cases involving Rs. 7.46 lakh and initiated corrective action. Reply has not been received in the remaining case (November 2009).

## 2.2.19 Conclusion

The review revealed that no centralised database of incentives sanctioned, availed etc., was maintained either by the implementing agencies or by the Sales Tax Department for evaluation and proper implementation of the scheme. Action was not initiated for effecting timely recovery of the incentives availed. Co-ordination between the implementing agencies and Sales Tax Department was lacking. There was no mechanism in the implementing agencies to ascertain whether periodic returns were submitted regularly by the units. Due to large number of pending assessments in the Sales Tax Department it could not be ascertained whether monetary ceilings prescribed for incentives availed by the eligible units had been exceeded. The Sales Tax Department has failed to implement its own directives to assess the returns of eligible units on priority.

## 2.2.20 Summary of recommendations

**The Government may consider:**

- **maintaining a centralised database of incentives sanctioned, availed of etc., for proper evaluation and implementation of the PSI; and**

- **instituting an effective system in the implementing agencies for initiating action for prompt recovery and a system may be put in place by the Government for effective co-ordination between the implementing agencies and the Sales Tax Department for monitoring of recoveries in respect of closed units.**

## 2.3 Review on "Transition from Sales Tax to VAT"

### Highlights

Implementation of the Value Added Tax (VAT) was slow due to delay of 27 months in implementation of all the functional branches under the VAT and non-establishing of Border Check Post resulted in non-utilisation of posts for the purpose for which they were created.

**(Paragraph 2.3.7.2)**

Due to non-preparation of all the basic modules the automation process in the department could not keep pace with the changes for implementation of VAT.

**(Paragraph 2.3.7.3)**

Huge number of pending assessments under the repealed Acts resulted in non-realisation of amounts blocked in these cases.

**(Paragraph 2.3.7.4)**

In the absence of timely validation of the data the correctness of the database maintained by the department could not be ensured. Further, delay in validation of data and consequential delay in issue of RCs and holograms adversely affected the authentication of the dealers.

**(Paragraph 2.3.8.3)**

In respect of 43,48,342 returns received during the year 2007-08 and 2008-09 no defect notices were issued.

**(Paragraph 2.3.9.1)**

Non-inclusion of refund for computation of cumulative quantum of benefit (CQB) resulted in short determination of CQB of Rs. 60.81 lakh.

**(Paragraph 2.3.12.1)**

Non-assessment of cases relating to short payment of tax detected by the Business Audit/Refund Audit branches resulted in non-levy of penalty in cases relating to willful default.

**(Paragraph 2.3.14.1)**

Absence of internal audit under the VAT deprived department of the vital area of internal control.

**(Paragraph 2.3.16.1)**

Delay in grant of refund under VAT resulted in claim of less compensation of Rs. 5.72 crore for loss of revenue from the Government of India.

**(Paragraph 2.3.17)**

### 2.3.1 Introduction

The Empowered Committee of State Finance Ministers had in its meeting held on 23 January 2002 resolved to implement VAT in India. Accordingly, the President of India accorded approval to the Maharashtra VAT (MVAT) Act, 2002 in March 2005. Further, the Empowered Committee in its meeting held on 7 March 2005 decided to implement VAT from 1 April 2005 in various States. The Government of Maharashtra (GoM) repealed the Bombay Sales

Tax (BST) Act, 1959 and enacted the MVAT Act, 2002 with effect from 1 April 2005.

VAT in Maharashtra is levied as per MVAT Act, and the MVAT Rules, 2002 made thereunder. VAT is levied on sale of goods including intangible goods. VAT is a taxation system that avoids double taxation. In addition to granting set-off of tax paid on purchases to the dealers, VAT has various other advantages for both business and Government, such as, eliminating cascading effect of double taxation and promoting economic efficiency. It is primarily a self-assessment system with more trust put on the dealers. It also has the potential for a stronger manufacturing base and more competitive export pricing. It has an improved control mechanism resulting in better compliance.

**Difference between MVAT and BST**

- VAT is a multipoint taxation system unlike BST which was a single/double point taxation system.
- The independent Acts which were in existence upto 31 March 2005 such as Works Contract Tax (WCT) Act, Motor Spirit Taxation Act and Lease Act have been merged with VAT.
- VAT system relies more on self compliance of tax by the dealers. Assessment is not compulsory in all the cases unlike in the repealed Acts where returns filed by the dealers were subjected to cent *per cent* assessment.
- In VAT, supporting documents like statement of sales and purchases, copy of annual accounts, etc., are not required to be submitted by the dealers along with the returns. In the repealed BST Act, however all such documents were required to be produced at the time of assessment.
- VAT provides for selection of dealers on scientific basis for audit of records. Under the repealed Acts there was assessment in all the cases.

**Salient features of VAT**

In Maharashtra, registration of dealers is compulsory for importers whose gross turnover of sales or purchases exceeds rupees one lakh and for others whose turnover of sales or purchases exceeds rupees five lakh in a financial year. A new dealer has to get himself registered under the Act within 30 days from the date on which he is liable to get registered. There is also a provision for voluntary registration by the dealers. Under the VAT Act there are mainly two rates for levying tax on various goods viz. four *per cent* and 12.5 *per cent*. Under schedule 'A' certain goods are tax free. There is a special rate of one *per cent* on precious metals, stones and jewellery, and on liquor, petrol, diesel, etc. the rate is 20 *per cent*. Multiple rates as was in existence under the repealed BST Act has been significantly brought down under VAT. There is also a composition scheme for manufacturers and retailers whose turnover of sales/tax liability is within the limit specified in the concerned notification. Dealers opting for composition scheme are not entitled for grant of set-off.

### 2.3.2 Organisational set up

VAT is administered by the Sales Tax Department. The Commissioner of Sales Tax (CST) heads the Sales Tax Department and he is assisted by the Additional Commissioners/Joint Commissioners (JCs)/Deputy Commissioners (DCs)/Assistant Commissioners (ACs) and Sales Tax Officers (STOs) at various levels. There are nine sanctioned posts of Additional Commissioners as shown in **Annexure III**. Of this, eight posts are sanctioned for VAT and one post for administration of remaining items of work under the repealed Acts. Of the eight posts of Additional Commissioners under VAT, five are in Mumbai and remaining three are in the Zonal offices at Nagpur, Pune and Thane. VAT is being implemented in Maharashtra with functional jurisdiction unlike the repealed Act which was administered with territorial jurisdiction. In Mumbai, each functional branch is headed by a JC whereas in the divisions outside Mumbai the JC heads all the functional branches. The functional branches/units in the divisions are headed by DCs. The GoM has established 70 Large Taxpayer Units (LTUs) in the State in January 2007 with the objective that these units will function as single window system. These LTUs are headed by DCs. The dealers whose tax liability is rupees one crore and above are assigned to these LTUs.

### 2.3.3 Audit objectives

The review was conducted to ascertain whether:

- the planning for transition from BST to VAT as well as implementation of VAT was done in time and efficiently;
- the organisational structure was adequate and effective;
- the provisions of the VAT Act and Rules made thereunder were adequate and were enforced properly to safeguard the revenue of the State;
- an internal control mechanism is in place to ensure timely collection of revenue; and
- the system after being put in place was working efficiently.

### 2.3.4 Scope and methodology of audit

The review was conducted between April and August 2009 in four[8] out of 13 selected divisions[9]. Records pertaining to the period 2005-06 to 2008-09 were test checked during the review. The divisions were selected by applying statistical sampling technique (Simple Random Sampling Without Replacement). The details of the technique adopted is explained in **Annexure IV**.

[8] Mumbai, Nashik, Pune and Thane (Rural).

[9] Amravati, Aurangabad, Dhule, Kolhapur, Mumbai, Nagpur, Nanded, Nashik, Pune, Raigad, Solapur, Thane (City) and Thane (Rural).

## 2.3.5 Acknowledgement

The Indian Audit and Accounts Department acknowledges the cooperation of the Sales Tax Department for providing necessary information and records for the audit. An entry conference for the review was held on 23 July 2009 and the executive was informed about selection of divisions and scope and methodology of audit. The Additional Commissioner of Sales Tax (Headquarters), Officer on Special Duty (Finance Department), Joint Commissioners of the respective branches and Deputy Commissioners explained the various aspects of VAT administration and its implementation. The draft review report was forwarded to the Government and to the department in October 2009. No reply to the Review Report has been received. The exit conference to discuss the audit conclusions and recommendations could not be held despite request from audit (October 2009).

## Audit findings

Audit scrutiny revealed a number of deficiencies in the process of transition from sales tax to VAT which are discussed in the following paragraphs.

## 2.3.6 Pre-VAT and post-VAT revenue collection

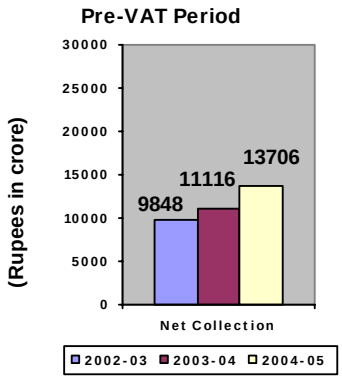
The Whitepaper by the empowered committee of State Finance Ministers while justifying the introduction of VAT envisaged that after introduction of VAT there will be growth in the revenue of the State.

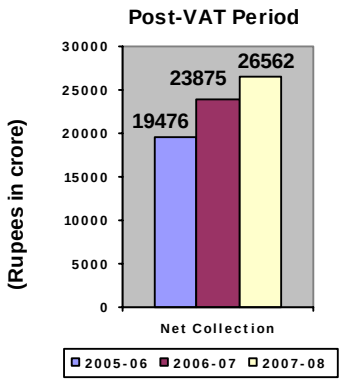
The revenue collections in the State during various periods between 2002-03 to 2007-08 are as under:

**Revenue collection**

**(Rupees in crore)**

| Pre-VAT | | | Post-VAT | | |
|---|---|---|---|---|---|
| **Year** | **Net Collection** | **Percentage of growth** | **Year** | **Net Collection** | **Percentage of growth** |
| 2002-03 | 9,847.61 | 6.60[10] | 2005-06 | 19,476.06 | 42.10 |
| 2003-04 | 11,116.18 | 12.88 | 2006-07 | 23,875.23 | 22.59 |
| 2004-05 | 13,705.93 | 23.30 | 2007-08 | 26,561.86 | 11.25 |




[10] Actual collection for the year 2001-02 was Rs. 9,237.59 crore.

As seen from the table, there was an increase in the growth of net revenue collection of 42.10 *per cent* after introduction of VAT during the year 2005-06.

### 2.3.7 Preparedness and transitional process

#### 2.3.7.1 Planning for implementation of VAT in the State

Empowered Committee through several rounds of discussions held between November 1999 and March 2005 finalised the design of State level MVAT Act, where various issues concerning the implementation of the VAT and common points of convergence among the states like returns, issue of tax invoice, grant of set-off, composition scheme for payment of tax, treatment of the exports, carrying forward of tax credit, procedure of self assessment under VAT liability, provision of the audit, grant of the incentives, abolition of taxes like turnover tax and surcharge, position of declaration forms, etc. were discussed.

In Maharashtra, the necessary draft bill styled as Maharashtra Value Added Sales Tax Act, 2002 L.A. Bill No. LX of 2002 was introduced in the state legislature in the year 2002 and was passed in the year 2003. The MVAT Act is implemented by the Sales Tax Department from April 2005.

Consequent upon the presentation of the draft bill on VAT in 2002, the department arranged a seminar in February 2003 to clear doubts of the departmental officers in respect of implementation of VAT. A Taxpayer's guide was also issued in July 2006 for the benefit of the dealers.

The department has prepared manuals for all the functional branches except for the LTU branch. All the departmental officers and staff were trained before introduction of VAT.

#### 2.3.7.2 Analysis of staff requirement and re-organisation of the Sales Tax department

The GoM issued a resolution in January 2007 for re-organisation of VAT administration on functional basis. However, all the branches were established in the year 2005. Out of this, the registration, refund, return and refund audit branches had become operational from the year 2005 itself. The remaining branches namely; business audit, survey, investigation, LTUs and recovery became operational from July 2007.

(i) GoM through Government Resolution dated 5 January 2007 created additional posts of 704 officers and 1,812 class-III posts for a period upto 31 March 2010 purely on temporary basis. These temporary posts were to be filled in by way of promotion, deputation, hiring retired employees or appointing new employees on contract basis only. However, the department had filled 1,195 posts only by promoting employees from lower posts as on 31 July 2009.

Hence, though the Act was drafted in 2002 and enacted in 2005, the department started the operation of all its functions 27 months after the date of its implementation.

After this was pointed out, the department stated (July 2009) that though VAT was implemented with effect from 1 April 2005, the department was not immediately ready with the functional branches/units and the total re-organisation has been completed only in April 2007.

(ii) Under Section 67 of the Act, if the state considers it necessary it may establish Border Check Posts (BCPs) and barriers to prevent or check the evasion of tax. The Government while issuing the order in January 2007 for reorganisation of the VAT administration also sanctioned various posts for establishing 30 BCPs in the state under the VAT as given below:

| Sl. no. | Designation | Sanctioned staff | Total filled | Used for BCP | Used in other branches | Shortfall |
|---|---|---|---|---|---|---|
| 1. | DC | 10 | 1 | 1 | 0 | 9 |
| 2. | AC | 50 | 3 | 0 | 3 | 47 |
| 3. | STO | 60 | 1 | 1 | 0 | 59 |
| 4. | STI | 30 | 0 | 0 | 0 | 30 |
| 5. | Clerk | 850 | 192 | 16 | 176 | 658 |
| **Total** | | **1,000** | **197** | **18** | **179** | **803** |

Information received from the department (July 2009) indicated that the BCPs were not established in the State even after a lapse of 30 months from the date of sanction of the posts. Due to this, out of the 197 posts filled by the department for this purpose, 179 posts were diverted to other branches on deputation basis and 18 posts were utilised for establishing of work relating to drawing and disbursement of pay and allowances of the staff on deputation work.

Non-establishing the BCPs resulted not only in non-utilisation of the posts for the purpose for which it was created but also in non-implementation of the process of collection of tax in respect of interstate movement of goods.

### 2.3.7.3 Computerisation of the Taxation Department and the check gates

The project of automation of Sales Tax Department is identified as Maharashtra Vikrikar Automation System (MAHAVIKAS). The contract for software development was awarded in 2001 to an agency M/s. Mastek Ltd. for Rs. 1.80 crore. Another agency M/s. Electronic Corporation of India Ltd. (ECIL) was awarded contract to provide hardware support.

Information received (July 2009) from the department revealed that in all, 22 software modules was developed (20 of which were ready by 2003 and two thereafter). Out of this, one module (Registration) is being used fully, three modules (Returns, Refund and Investigation) are being used partly and the remaining 18 modules have not been put to use till date.

Thus, the objective of automation of the VAT functions which has a vital role in effective implementation of the VAT remained largely unfulfilled.

The department stated (July 2009) that the business processes had not been crystallised. Therefore, some of the basic MODULES like the Audit MODULE were yet to be completed.

This indicated that the automation process did not keep pace with the changes taking place in the department for implementation of the VAT even after a lapse of six years from the commencement of the automation process.

**The Government may consider preparing modules in tune with the VAT functions for effective implementation of VAT**.

### 2.3.7.4 Completion of BST/Central Sales Tax assessments under the repealed Acts

As per the provisions of the repealed BST Act, each return filed by the dealer was to be assessed. As of 31 March 2005, 24,46,280 assessments of dealers under the BST and allied Acts were pending and the pendency during the period 2005-06 to 2007-08 was as under:

| Year | Opening Balance | Additions | Total assess-ment due | Disposal | | | Balance at the end of the year |
|---|---|---|---|---|---|---|---|
| | | | | Cases not to be assessed | Cases Assessed | Total | |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 |
| 2005-06 | 24,46,280 | 15,24,278 | 39,70,558 | 0 | 2,58,260 | 2,58,260 | 37,12,298 |
| 2006-07 | 37,12,298 | 1,640 | 37,13,938 | 16,78,584 | 9,38,462 | 26,17,046 | 10,96,892 |
| 2007-08 | 10,96,892 | 887 | 10,97,779 | 2,97,141 | 1,03,938 | 4,01,079 | 6,96,700 |
| **Total** | | **15,26,805** | | **19,75,725** | **13,00,660** | **32,76,385** | |

Out of the 24,46,280 pending assessments as on 1 April 2005, only 2,58,260, 9,38,462 and 1,03,938 assessments were completed during the periods 2005-06, 2006-07 and 2007-08, respectively. Considering the fact that VAT functional branches had become fully operational from July 2007 the staff could have been effectively deployed for clearing the pending assessments under the old acts.

**The Government may consider evolving a mechanism to complete the assessments early to realise any dues blocked in such pending assessments.**

### 2.3.7.5 Collection of arrears of taxes due under the repealed Acts

As on 31 March 2005, total arrears of revenue in the test checked divisions under the repealed Acts i.e. BST, Central Sales Tax, WCT Act, etc., was Rs. 8,446.89 crore in respect of 2,43,789 cases. The arrears had increased to Rs. 29,457.48 crore in respect of 2,90,798 cases as on 31 March 2009. These outstanding dues comprised recoverable dues of Rs. 8,995.62 crore, dues of Rs. 6,515.39 crore recoverable but in difficult zone, dues of Rs. 10,986.77 crore locked up in stay orders and Rs. 2,959.70 crore not really pursuable but need to be kept under watch.

Analysis of outstanding dues revealed that, though the recoverable dues were Rs. 2,296.23 crore as of 31 March 2005, same had increased to Rs. 8,995.62 crore. This indicated that efforts made by the Department to liquidate the arrears were not adequate.

### 2.3.8 Registration and database of dealers

#### 2.3.8.1 Creation of database of dealers

The database of Registered Dealers (RDs) maintained in the MAHAVIKAS system gets periodically updated by the registration branch in respect of new registration, cancellation, amendment of registration certificates (RCs) etc.

#### 2.3.8.2 Carrying forward of the database of dealers under the repealed Acts and confirmation of the securities provided by them

After implementation of VAT, a dealer, who was already registered under the repealed BST Act, was not required to apply for registration immediately. However, such dealers were required to apply by 31 December 2005 for registration in form 108 for obtaining a new RC, failing which the RC, issued under the repealed act was liable to be cancelled.

#### 2.3.8.3 Registration and monitoring process of dealers

Under the provisions of the MVAT Act dealers holding RCs under the other repealed Acts[11] as well as new dealers were required to apply for grant of registration and were liable to pay taxes. A 12 digit Tax payers Identification Number (TIN) was to be allotted first, followed by issue of RCs for this purpose. After allotment of TIN, the TIN forms were to be scanned and forwarded to an agency[12] appointed by the department for data entry, printing of TIN certificates and issuing of RCs. The data entry made by the agency was also required to be validated by the department. As per Rule 10(2) of the said act every registered dealer under VAT has to be issued a hologram for each place of their business for displaying in a prominent place of their business. The issue of RC to the dealer completes the process of registration.

- The details of dealers who had applied for TIN, number of TINs allotted and RCs issued, number of cases validated, shortfall in issue of RCs and number of cases not validated in the three test checked divisions, as of 31 March 2009 were as shown in the table under:

| Sl. no. | Year | Appli-cations received | Number of TIN allotted[13] | Number of RCs issued | Number of RCs not issued | Number of vali-dations done | Number of validations not done |
|---|---|---|---|---|---|---|---|
| 1. | 2005-06 | 42,247 | 39,409 | 28,391 | 11,018 | 3,907 | 35,502 |
| 2. | 2006-07 | 30,774 | 29,580 | 4,727 | 24,853 | 24,099 | 5,481 |
| 3. | 2007-08 | 22,315 | 20,816 | 11,142 | 9,674 | 19,240 | 1,576 |
| 4. | 2008-09 | 23,752 | 22,916 | 15,245 | 7,671 | 15,276 | 7,640 |
| | **Total** | **1,19,088** | **1,12,721** | **59,505** | **53,216** | **62,522** | **50,199** |

[11] Works Contract Tax Act, Motor Spirit Taxation Act and Lease Act.
[12] M/s. ECIL Ltd.
[13] Net of the TINs/RCs issued and cancelled subsequently during the period 2005-06 to 2008-09

From the above table it can be seen that as against 1,12,721 TINs allotted, 62,522 (55.47 *per cent*) cases were validated and in 59,505 (52.79 *per cent*) cases RCs were issued to the dealers upto 31 March 2009. Also holograms were not issued to the dealers in the test checked divisions, as was required.

- As per Section 16(6) of the Act, if any dealer discontinues the business or shifts the place of his business to a different area, then he has to apply to the concerned authority for cancellation or transfer of the registration within the prescribed period. After cancellation, the RC issued to the dealer had to be returned to the department. Further, if the turnover of sales/purchases of the dealer had gone below the prescribed limit in the preceding year, the dealer could apply for cancellation of registration.

In Mumbai division 1,028 applications were received upto March 2008 for cancellation of RCs for the years 2005-06, 2006-07 and 2007-08, out of which 894 RCs were cancelled. The remaining 134 RCs could not be cancelled either due to non-availability of signature of the applicants on the application form or due to shortage of staff in the department. Of the 894 cancelled RCs, 119 dealers had returned their RCs. The remaining 775 dealers had not returned the cancelled RCs as they had not received the RCs from the department at the time of registration. Similarly, in Nashik division out of 1,114 cancelled RCs, 887 dealers had not returned their RCs.

Audit also observed that in Mumbai division though 894 RCs were cancelled, neither the position of goods in stock nor the tax liability of the dealer was ascertained by the concerned officers as was required under Section 16(6) of the Act.

After this was pointed out, the department stated (August 2009) that the RCs were cancelled on receipt of application from the dealers. It was also stated that the stock of goods available with the dealer at the time of cancellation was not verified as this work was not assigned to the registration branch.

In the absence of timely validation of the data the correctness of the database maintained by the department could not be ensured. Further, delay in validation of data and consequential delay in issue of RCs and holograms adversely affected the authentication of the dealers.

**The Government may consider instituting a suitable mechanism for validating the work outsourced to the agency responsible for data entry, printing of TIN certificates and issuing of RCs. Further, a system should also be laid down for timely cancellation of RCs, only after completion of verification process as required under the Act/Rules and for timely return of the cancelled RCs to avoid its misuse.**

### 2.3.8.4 Periodic analysis of dealers below threshold limit

As per departmental instructions, the officials in the survey branch are required to visit selected dealers in respect of cases reported by the survey team as "not liable for registration". One *per cent* of such dealers who are randomly selected are to be revisited after a gap of three to six months.

Test check of the records indicated that in the Mumbai division though a list of the dealers was maintained in the Day Book Register, except the names of the

dealers no other details such as place of business, activity, etc., were available. In the Thane (Rural) division no such data was maintained.

After this was pointed out, the DC Survey, Thane (Rural) division stated (June 2009) that the branch does not keep track of dealers whose turnover of sales/purchases are less than rupees five lakh.

The fact remains that in the absence of this vital information, the effectiveness of the Survey Branch for conducting surveys of such dealers could not be ascertained.

#### 2.3.8.5 Detection of unregistered dealers

As per the provisions of Section 66 of the Act, the department was required to conduct surveys to identify the dealers who are liable to pay tax but have remained unregistered.

The survey work however commenced in January 2008. Information collected from the Survey branches of four test checked divisions revealed that as against 19,237 dealers (5,365 in 2007-08 and 13,872 in 2008-09) only 223 dealers (4.16 *per cent*) for the year 2007-08 and 6,518 dealers (46.99 *per cent*) for the year 2008-09 were registered upto 31 March 2009 leaving a balance of 12,496 (64.96 *per cent*) dealers unregistered.

After this was pointed out, the department stated (July 2009) that the dealers had failed to respond to the notices issued to them.

The fact remains that these unregistered dealers were to be assessed as per Section 23(4) of the Act. However, assessments of these dealers were pending. This not only resulted in delay of registration of dealers but also potential tax payers remaining outside the tax net.

**The Government may consider making it mandatory to conduct periodic survey to unearth unregistered dealers in the interest of revenue.**

### 2.3.9 Returns

#### 2.3.9.1 Scrutiny and verification of returns

As per Section 20 of the MVAT Act every RD has to file correct, complete and self-consistent returns. These returns are required to be examined by the return branch. In respect of incomplete and inconsistent returns, the department may serve a defect notice to the dealer within four months of the date of filing of the return. The dealer has to correct the defects as pointed out in the defect notice and submit a fresh, complete and self consistent return within one month.

Information received from the four test checked divisions revealed that out of 32,98,103 returns received during the years 2005-06 and 2006-07, 63,368 defect notices were issued. During the years 2007-08 and 2008-09, 43,48,342 returns were received but no defect notices were issued.

Since the time frame fixed for issue of defect notices is four months from receipt of returns, no action was possible in respect of returns received before November 2008.

In addition to issuing of defect notices to the erring dealers, the department has to conduct detailed scrutiny of all the returns to ascertain the date and amount of tax due, tax paid, interest payable, etc.

Test check of the records in two units of the Return branch in Mumbai division revealed that after scrutiny of returns, the department had raised demands for payment of interest of Rs. 5.47 crore in 33,867 cases during 2005-06. However, no such scrutiny of returns was conducted during the years 2006-07 to 2008-09 indicating that the returns filed by the dealers were accepted as complete and self consistent without ascertaining whether the dealers had paid taxes and interest correctly.

After this was pointed out, the department stated (June 2009) that from 2006-07 onwards the task of data entry of returns has been entrusted to a private agency and the defect notices were to be generated on MAHAVIKAS. Since the agency has not completed the data entry so far, the department could not generate and issue defect notices in the remaining cases.

The fact remains that the work entrusted to the agency was required to be periodically monitored by the Department to ensure that the data entry of returns is complete.

**The Government may consider evolving a system for monitoring the issue of defect notices and for scrutiny of returns in the interest of revenue**.

### 2.3.9.2 Inadequacy of the documentation to be given along with the returns

The Act does not provide for submission of any statement of sales/purchases along with the return. Further, there is no provision in the act for filing of annual return as was required under the repealed acts. However, the dealers whose turnover of sales/purchases are Rs. 40 lakh and above are required to furnish form 704 prepared by the chartered accountant (CA). Due to this, the details of sales/purchases, opening and closing stock is not available in respect of dealers whose turnover of sales/purchases is below Rs. 40 lakh. Hence, the scrutiny of returns cannot be said to have been complete without this vital information.

**Pending work towards scrutiny of chartered accountant's certificate in Form 704:**

Section 61 of the act provides for audit of accounts by the CAs of the dealers whose turnover of sales or purchases exceeds Rs. 40 lakh in a year or of the dealers who are dealing in country/foreign liquors or beer, etc. An audit report in form 704 prepared by CA has to be furnished by the dealer to the department within eight months (10 months with effect from 01 April 2007) as per Rule 66 of MVAT Rules. The Sales Tax Practitioners Association had challenged the validity of Section 61 of the Act in the Bombay High Court. On the basis of the decision of the High Court the period of submission of report in form 704, for the periods 2005-06 and 2006-07, was extended upto 31 July 2008. As per Section 61(2) of the Act, non-submission of audit report in the prescribed form attracts penalty equal to 0.1 *per cent* of the total sales. The exact number of dealers from whom form 704 is receivable was not available in the test checked divisions. In the absence of this information it

was not possible to ascertain in audit as to how many dealers were actually liable for penalty under Section 61(2) of the Act.

After this was pointed out, the department stated (July 2009) that the database in this regard is maintained by MAHAVIKAS. But the information called for by audit has not been furnished so far.

- Information furnished in form 704 is required to be checked in the Business Audit branch. This scrutiny is devised to see whether the dealer had paid the taxes and interest correctly. In Mumbai, Nashik and Thane (Rural) divisions, in respect of 2,22,383 (88.63 *per cent*) out of 2,75,795 forms (704) submitted by the dealers, scrutiny had not been conducted by the department till 31 March 2009. In Pune division after scrutiny of 53,412 forms (704) for the period 2005-06 to 2007-08, 284 cases were identified for levy of penalty under Section 61(2), of which, action was taken to levy penalty only in 46 cases.

- As per Rule 65 of MVAT Rules, 2002, the CA after conducting audit has to advise the dealer in form 704 with regards to any payment of additional tax liability, pay back of excess refund received, reduction in claim of refund, etc. However, as the role of the CA was advisory, it was not binding on the dealer to pay the differential dues or to file revised returns. Hence, such 704 forms should have been scrutinized on a priority basis.

### 2.3.10 Tax audit

#### 2.3.10.1 Process of selection of dealers for tax audit

As per Section 22 of the Act, the CST may arrange for audit of the business of any RD. Selection of dealers is done by MAHAVIKAS for this purpose by applying the following criteria:

- Dealers who have not filed the return;
- Who have claimed refund of tax;
- Who are selected by CST on the basis of application of any criteria or on a random selection basis;
- Where the CST is not prima facie satisfied with the correctness of any return of the dealer; and
- Where the CST has reason to believe that detailed scrutiny of the case is necessary.

The Additional Commissioners of the respective zones send the list of dealers as selected by MAHAVIKAS to the JCs of the divisions who in turn allot these cases to the branches/units headed by DCs for audit.

As scrutiny of transactions made by the dealer is predominantly return based, no records like statement of stock, declaration forms etc., are being kept in the audit file after completion of business/refund audit. However, as per the circular instructions issued by the Commissioner of Sales Tax in August 2008 documents relating to statement of sales and purchases and a list containing number and date of declaration forms issued in respect of interstate

transactions are to be kept and preserved in the audit files of cases selected for business/refund audit.

### 2.3.10.2 Time frame for completion of tax audit

As per the departmental instructions, business audit should be completed within three months from its commencement. Information received from the four test checked divisions revealed that during 2005-06 no audit was conducted in any of these divisions. During 2006-07 in the Mumbai division audit was completed in 118 out of 395 cases. In Nashik, Pune, and Thane (Rural) divisions no audit was conducted during 2006-07. In the four test checked divisions, in 7,626 out of 12,006 cases audit was completed in stipulated time during the periods 2007-08 and 2008-09.

After this was pointed out, the department stated (July 2009) that business audit was delayed due to want of documents from the dealers.

### 2.3.10.3 Percentage of dealers to be taken up for tax audit

- **Business Audit**

The Act does not prescribe any percentage or number of cases to be selected for business audit. However, as per the departmental instructions the dealers are to be selected for business audit in such a way that each dealer gets selected for audit once in five years.

In the four test checked divisions, the information regarding the year-wise registration granted to the dealers registered under the act was not made available to Audit, but number of fresh dealers registered after introduction of VAT was furnished by the department. Analysis of the data furnished by the department revealed that out of 83,571 dealers due for audit, during the period 2005-06 to 2008-09, only 12,124 (14.51 *per cent*) were audited and an additional demand of Rs. 127.58 crore including interest of Rs. 24.13 crore was raised. Thus there was a shortfall of 85.49 *per cent* in the number of cases to be audited by business audit branch. This indicated that the monitoring mechanism prescribed was not proper.

- **Refund Audit**

Section 51 of the MVAT Act deals with the grant of refund to the dealers. As per the amended provision of Section 51 of the Act and the Trade circulars issued by the CST from time to time, refunds were granted to the dealers during 2005-06 to 2007-08 without pre-audit or without obtaining bank guarantee. In all such cases, however, post-audit was to be taken up after March 2008.

Information received from the four test checked divisions revealed that post-audit in 798 cases involving Rs. 81.14 crore where the refunds were granted during 2005-06 to 2007-08 was still pending as on 31 March 2009.

The GoI in December 2006 had issued instructions to the GoM to complete internal audit of all cases where refunds were granted before submitting their claim for compensation for loss of revenue due to introduction of VAT.

Information received (July 2009) from the JC of Sales Tax, internal audit revealed that the audit of refunds by this wing had not been conducted upto March 2009. However, the department had issued circular instructions for commencement of refund audit in March 2008 only. This indicated that the instructions issued by the GoI for claiming compensation for loss of revenue due to introduction of VAT was not followed.

**The Government may consider devising a time bound programme for completion of refund audit to ensure that excess refunds were not granted.**

- **Scrutiny of returns and audit in LTU Branch**

In January 2007, the Government decided to establish 70 LTUs. Each unit consists of dealers with tax liability of rupees one crore and above. All the functions under VAT including audit in respect of each dealer are performed in this unit as a single window system. However, these units were established only in July 2007, except in Thane (Rural) division where it was established in the year 2008-09. As per departmental instructions, audit of each dealer of LTU is to be conducted every year. Information received from the department revealed that out of 2,695 cases due for the years 2007-08 and 2008-09, only 865 cases were scrutinised and additional demand of Rs. 87.72 crore was raised. Since bulk of the tax collection in the State is from LTU dealers, shortfall in audit of such dealers negated the very purpose of creating these units.

Reasons for shortfall are awaited from the department (November 2009).

### 2.3.11 Input Tax Credit

#### 2.3.11.1 Deficiencies in the provisions for set-off (Input Tax Credit)

Under the provisions of Rule 52 of MVAT Rules, 2002, a dealer is eligible for set-off of the taxes paid by him on purchases made from another registered dealer in respect of capital goods as well as in respect of purchases which are debited to the profit and loss account. Due to this provision in the Rules, dealers who are resellers or manufactures are eligible for set-off on any capital goods purchased irrespective of whether these goods are used in manufacture. Similarly, set-off is also admissible in respect of gift items, stationery goods, canteen expenses, office expenses if these purchases were debited to the profit and loss account.

As VAT envisages levy of tax on value addition along the supply chain and grant of set-off at each stage on the tax paid on purchases at the previous stage, the grant of set-off under the said rule was not consistent with the concepts under VAT. The White Paper prepared by the Empowered Committee of State Finance Ministries on 17 January 2005 finds mention in paragraph 2.2 as "The input tax credit in relation to any period means setting off the amount of input tax credit (set-off) by a RD against the amount of output tax". However, because of the provisions in the rule, dealers are eligible for set-off on purchases of both capital goods or otherwise. It leads to misuse of the provision of grant of set-off as in respect of purchases of

personal nature, gifts, helicopters, aeroplanes etc., the dealer could be eligible for set-off.

- As per Rule 51 of MVAT Rules, 2002 a dealer was eligible for set-off of taxes paid by him on the closing stock as on 31 March 2005, provided the dealer had produced a certificate in the prescribed form.

Scrutiny of records in the four test checked divisions, revealed that in respect of 12 dealers refund was allowed during the year 2005-06 on account of set-off of Rs. 30.15 lakh on the closing stock as on 31 March 2005, even though, the requisite certificates in the prescribed form were not furnished by them. In the absence of the prescribed certificate refunds of Rs. 30.15 lakh granted to the dealers was irregular.

After this was pointed out the department stated (July 2008 and June 2009) that the requisite certificates would be obtained from the dealers and kept on record.

The fact remains that furnishing of certificates by the dealers was a pre-requisite for grant of set-off. Moreover, the target date for furnishing the certificate was 28 February 2007.

- As per Section 48(2) of the MVAT Act no set-off or refund shall be granted to any dealer in respect of any purchase made from a RD unless the claimant dealer produces a tax invoice.

Test check of records of BA, LTU, Refund and Refund Audit branches in three test checked divisions viz. Mumbai, Pune and Thane (Rural) revealed that in five cases set-off of Rs. 2.46 crore was allowed during 2005-06 and 2006-07, even though the tax invoices were not furnished by the dealers.

After this was pointed out the department stated (between July 2008 and June 2009) that, the position varied from unit to unit such as i) the correctness of ITC claimed had been checked at the time of audit, ii) the claim was allowed as such after issue of cross check memos in pursuance of the departmental circular, etc..

The fact remains that set-off claimed by the dealer can be allowed only when it is supported with tax invoice.

### 2.3.11.2 Provisions for declaring details of the selling dealers in the returns

As per Rule 17 of the MVAT Rules, a dealer has to file returns in the prescribed form within the stipulated period. In the return column, number seven to nine are earmarked for computation of turnover of purchases eligible for set-off, breakup of purchases tax-rate wise and computation of set-off claimed in the return. The provisions in the act do not require the dealer to furnish details of the purchases such as, date of purchase, name and TIN of the dealer from whom the purchases were made and value of purchases in the return. In the absence of these details it was not possible for audit to verify correctness of set-off claimed by the dealer.

**The Government may consider making it mandatory to provide details of the selling dealers in the return alongwith the details of treasury challans.**

### 2.3.11.3 System of cross verification of the records of the selling dealers

As per the departmental instructions for grant of set-off to a dealer, the returns of the selling dealer who has issued tax invoice needs to be cross checked with the data maintained in MAHAVIKAS for the corresponding month. Further, while granting refunds, which has resulted due to claim of set-off in the returns filed by the dealer, a copy of the return for the succeeding month is to be invariably checked and kept on the record in order to ensure that the dealer has not carried forward the set-off claimed in the preceding month.

Test check of records of the Thane (Rural) division revealed that in respect of 11 dealers, for various periods between 2005-06 and 2008-09, set-off aggregating Rs. 70.73 lakh was allowed without cross-check of returns with MAHAVIKAS for the corresponding month. Set-off aggregating Rs. 2.22 crore was allowed in respect of 15 other dealers, for various periods between 2005-06 and 2006-07, without ensuring that the set-off was not carried forward in the returns for the succeeding month. Thus, the grant of set-off vis-a-vis refunds aggregating Rs. 2.93 crore was irregular.

## 2.3.12 Provisions for grant of exemption to certain class of dealers

### 2.3.12.1 Control mechanism to monitor the amount of revenue foregone due to grant of exemption to industrial units

A Package Scheme of Incentives (PSI) was introduced in 1964 to encourage dispersal of industries outside Bombay-Thane-Pune belt and to attract industries to the developing and undeveloped areas of the State. The Scheme was amended from time to time, the last amendment being in 2007. Under the scheme, sales tax incentives by way of exemption/deferral/interest-free unsecured loan, special capital incentives for SSI units, refund of octroi/entry tax/electricity duty, concession in the capital cost of power supply and contribution towards the cost of feasibility study were given to new/pioneer/ prestigious units as well as to the existing units undertaking expansion/ diversification.

**Short calculation of Cumulative Quantum of Benefits**

As per the PSI under the VAT Act and the rules made thereunder, a manufacturer in an eligible unit is entitled to avail tax incentives under the exemption mode in respect of sales tax, Central Sales Tax on sale of finished goods. The details are mentioned in the eligibility certificate issued by the department. After scrutiny of the returns, the Cumulative Quantum of Benefits (CQB) availed by the dealer during a year, is determined as per the provisions of the relevant MVAT Rules, 2002. The CQB is then reduced from the available monetary ceiling at the beginning of each year. Further, as per Rule 78 and 79 of the MVAT Rules, a dealer is entitled to claim refund of tax equal in amount to four *per cent* of purchase price of fuel, taxable goods used in manufacture of tax free goods and purchase price of goods used for manufacture which is dispatched to his own place of business or to his agent provided such amount is added to the CQB availed by the dealer during the said period.

During test check of the records of Pune division it was noticed that a dealer to whom eligibility certificate was granted under the exemption mode was allowed refund of Rs. 2.11 crore in January 2007, for the period April 2005 to December 2005, which was inclusive of refund of tax of Rs. 60.81 lakh. The refund claimed was equal in amount to four *per cent* of the purchase price. However, while computing the CQB availed by the dealer for this period, refund of Rs. 60.81 lakh was not considered as required under the rule. This resulted in short calculation of CQB to the extent of Rs. 60.81 lakh.

After the case was pointed out, the DC (Refund), Pune stated (February 2009) that the observation will be verified. Further reply is awaited (November 2009).

### 2.3.13 Acceptance and disposal of appeal cases

No time frame is prescribed in the repealed BST Act as well as in the MVAT Act for disposal of appeals filed by a dealer. Under the VAT regime however, the appellate authority has to give preference to the dealers whose age is more than 75 years.

Information received from four test checked divisions revealed that, 7,046 appeal cases involving revenue of Rs. 1,264.62 crore were pending as on 31 March 2009. Analysis of pending cases is given below:

**(Rupees in crore)**

| **Division** | **Number of cases pending** | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **upto 3 years** | | **> 3 years** | | **> 4 years** | | **> 5 years** | |
| | **No of cases** | **Amount involved** | **No of cases** | **Amount involved** | **No of cases** | **Amount involved** | **No of cases** | **Amount involved** |
| Mumbai | 2,174 | 551.32 | 489 | 103.32 | 218 | 27.45 | 566 | 51.92 |
| Nashik | 333 | 55.69 | 5 | 0.70 | 9 | 0.13 | 40 | 0.33 |
| Pune | 1,805 | 397.56 | 503 | 39.28 | 225 | 14.81 | 240 | 16.00 |
| Thane (Rural) | 193 | 1.97 | 12 | 0.29 | 24 | 0.96 | 210 | 2.89 |
| **Total** | **4,505** | **1,006.54** | **1,009** | **143.59** | **476** | **43.35** | **1,056** | **71.14** |

As no time frame was prescribed in the repealed BST Act as well as in the MVAT Act for disposal of appeal filed by a dealer, the department takes its own time to clear the cases.

After this was pointed out, the department stated that priority is given to cases involving tax dispute of more than rupees one lakh. The department further stated that, one of the reasons for large number of cases pending in appeal was due to vacancy in the post of appellate authorities.

The fact remains that inordinate delay in clearing of pending cases may lead to non-realisation of Government revenue due to passage of time.

## 2.3.14 Deterrent Measures

### 2.3.14.1 Absence of minimum penalty for offences

### Non-levy of Penalty under Section 29 (3) of the Act

As per Section 23(6) of the Act, if a dealer is found to have not disclosed the turnover of sales or of purchases in the return for any period or if tax had been paid at a lesser rate or set-off/deduction has been wrongly claimed, then the dealer may be assessed after serving a notice. Further, as per Section 29(3) of the act while passing an assessment order, the assessing officer can impose penalty equivalent to tax evaded or excess set-off claimed. However, as per departmental instructions, during the business audit, if any irregularity as specified in Section 23(6) of the act is noticed and the dealer agrees to pay the amount due with interest, no assessment order is required to be passed and the business audit is treated as complete.

During scrutiny of the records of the four test checked divisions, it was noticed that during various periods between 2005-06 and 2008-09, the business audit wing had noticed short payment of tax of Rs. 1.97 crore due to excess claim of set-off, application of incorrect rate of tax etc., and consequential levy of interest of Rs. 34 lakh in respect of 116 cases. However, in none of these cases notices were served by the department for carrying out assessment of these dealers. As a result, the department could not examine the aspect of levy of penalty in these cases.

After these cases were pointed out, the department stated that as per the departmental instructions assessment orders were required to be passed only if the dealer disagrees with the findings of the business audit.

Thus, the departmental instructions are not in conformity with the provisions of Section 29(3) of the act which was introduced with the intention of having a deterrent effect on the tax evaders.

**The Government may consider evolving a mechanism for carrying out assessment of dealers on a selective basis in cases where evasion of tax is noticed during the Business Audit/Refund Audit, so that the penalty could be levied where willful default have been noticed.**

## 2.3.15 Internal controls

### 2.3.15.1 Maintenance of registers in unit offices

- **Register of cross check memos**

As per the departmental instructions, before closure of audit, the concerned officer has to issue cross check memos to the dealer for ascertaining the correctness of ITC claimed by the dealer in his return. A register showing the names of the purchasing and selling dealer, their TINs, period of transaction, value of sales/purchases is to be maintained in each division for this purpose.

Scrutiny of the registers maintained in the four test checked divisions revealed that result of the cross check memos issued, the progressive figures of

outstanding memos, monthly abstracts, etc., were not recorded in these registers. It was also noticed that no follow up action was taken by the concerned branches for keeping the register upto date.

As the information required was neither kept on record nor the data updated in time the very purpose for which these registers was to be maintained was defeated.

- **Register number BAR 6 – selection criteria register**

As per departmental instructions, a register is to be maintained for selection of dealers for audit on the basis of the criteria prescribed under Section 22 of the MVAT Act. The register is to be maintained by the business audit branch until a computerised system for selecting the dealer in MAHAVIKAS is put in place.

It was noticed that in the four test checked divisions no such registers were maintained.

### 2.3.15.2 Reports and returns

The department has devised a system of calling for information from various functional branches/units of the field offices through a monthly statement known as key performance indicators (KPIs). The divisions in turn consolidate the KPIs under their jurisdiction in a form viz. key key performance indicator (KKPI) and send to the Commissioner's office for follow up action.

It was noticed that performance reports in form KKPI had been received in the office of the CST from the divisions only during the year 2007-08 and 2008-09.

No such reports were sent by the divisional offices for the years 2005-06 and 2006-07. The Department (August 2009) stated that the process of receiving KKPI reports in the Commissioner's office was initiated only in the month of December 2007.

Non-receipt of performance report from the field offices during 2005-06 and 2006-07 indicated that there was no control mechanism available with the department to monitor the performances of the various branches during these years.

## 2.3.16 Internal audit

### 2.3.16.1 Existence of Internal Audit

Under VAT administration there is no separate branch of internal audit (IA). The IA branch which was in existence under the repealed Acts along with its staff was allowed to continue for conducting internal audits of both BST Act and VAT Act.

Information received from the test checked divisions revealed that the IA branch was mainly engaged in conducting internal audit of assessments done under repealed Acts and not of VAT.

After being pointed out (July 2009), the department stated that since all the functional branches under VAT are headed by officers with full expertise in their respective fields, no internal audit under VAT was considered necessary.

The fact remains that the internal audit wing of any organisation is a vital component of the internal control mechanism and is defined as control of all controls to enable that the prescribed systems are functioning reasonably well. Absence of internal audit made the department vulnerable to the risk of control failure.

**The Government may consider taking up the internal audit of the functional branches of VAT to monitor the work done under these branches.**

### 2.3.17 Claim for compensation of loss due to introduction of VAT

As per the modalities prescribed under the GoI guidelines, compensation for loss of revenue due to implementation of VAT was available to the States at 100 *per cent*, 75 *per cent* and 50 *per cent* of such loss of revenue during the first three years, namely 2005-06, 2006-07 and 2007-08 respectively. The net revenue for the respective years was to be worked out after deducting the refunds granted under VAT from the gross receipts. The refunds were to be granted on receipt of application from the dealer for refunds in form 501.

During test check of the records of Mumbai and Pune divisions, it was noticed that though 112 dealers had applied for refund in time, during the years 2005-06, 2006-07 and 2007-08, the refunds were not granted in the same year but were granted during the subsequent years. Thus, due to delay in grant of refunds, the gross receipts could not be reduced by the refunds that would have been admissible during the year. This resulted in claim of less compensation from the GoI and consequent loss of revenue of Rs. 5.72 crore.

On this being pointed out, the department replied (March 2009) that this was the initial period of implementation of VAT. Being a new enactment, the trading community faced lots of problems in complying with the various requirements of the Act. Also the department faced several problems in administering the said Act. Under these circumstances it was impractical to implement the Act in totality right from the very beginning. Hence, the modalities as defined by the GoI for compensation were implemented and refunds granted to the dealers as per the circular instructions issued by the CST.

The fact remains that the department should have foreseen all these problems and taken steps to educate the traders and to gear the departmental machinery at all levels to expedite the grant of refund before the end of the respective financial years.

### 2.3.18 Conclusion

The review revealed that the administrative set up was not in place for smooth implementation of the VAT. The reorganisation of the department was done only after January 2007 and still the functional branches have not been fully streamlined. Further, the staff available with the department are not being fully utilised in assessing the pending cases under the repealed Acts. There

were delays in registration of unregistered dealers and their assessments resulting in potentially identified tax payers remaining out of the tax net.

Of the 22 modules included in MAHAVIKAS system only one module viz. that of Registration has been put to use so far. As the smooth functioning of VAT is based on effectiveness of data available on the system, its delay in implementation hampered the effective implementation of the Act. Also, returns were not scrutinised and defect notices were not issued from 2007-08 due to non-availability of data on MAHAVIKAS.

Internal control was not effective as the cases covered by Business Audit/Refund branch were not checked by the Internal Audit branch. Large refunds were granted without pre-audit or without taking bank guarantee from the claimant dealers. Non-imposition of penalty on dealers has resulted in loss of revenue to Government, besides sending wrong message to the dealers that the Department recovers only the tax evaded with interest in audit without any penalty as a deterrent measures.

### 2.3.19 Summary of recommendations

**The Government may consider:**

- **preparing modules in tune with the VAT functions for effective implementation of VAT;**
- **evolving a mechanism to complete the assessments early to realise any dues blocked in such pending assessments;**
- **instituting a suitable mechanism for validating the work outsourced to the agency responsible for data entry, printing of TIN certificates and issuing of RCs. Further, a system should also be laid down for timely cancellation of RCs, only after completion of verification process as required under the Act/Rules and for timely return of the cancelled RCs to avoid its misuse;**
- **making it mandatory to conduct periodic survey to unearth unregistered dealers in the interest of revenue;**
- **evolving a system for monitoring the issue of defect notices and for scrutiny of returns in the interest of revenue;**
- **devising a time bound programme for completion of refund audit to ensure that excess refunds were not granted;**
- **making it mandatory to provide details of the selling dealers in the return alongwith the details of treasury challans;**
- **evolving a mechanism for carrying out assessment of dealers on a selective basis in cases where evasion of tax is noticed during the Business Audit/Refund Audit so that the penalty could be levied where willful default have been noticed; and**
- **taking up the internal audit of the functional branches of VAT to monitor the work done under these branches.**

## 2.4 Other audit observations

*Scrutiny of the assessment records of Sales Tax/Value Added Tax (VAT), Central Sales Tax and Works Contract tax Act maintained in Sales Tax Department revealed several cases of non-observance of provisions of Acts/Rules, non/short levy of tax, irregular grant of exemptions and other cases as mentioned in the succeeding paragraphs in this Chapter. These cases are illustrative and are based on a test check carried out in audit. Such omissions on the part of Assessing Authorities (AAs) are pointed out in audit each year, but not only the irregularities do persist; these remain undetected till an audit was conducted. There is need for the Government to improve the internal control system including strengthening of internal audit.*

## 2.5 Excess claim for compensation of loss of revenue due to introduction of Value Added Tax in Maharashtra

The Value Added Tax (VAT) was implemented in Maharashtra with effect from 1 April 2005. The Government of India (GoI) agreed to compensate the Government of Maharashtra (GoM) for loss of revenue consequent to the implementation of VAT and issued guidelines in June 2006 on the modalities for calculation of compensation claim. As per the guidelines, the VAT receipts were to be compared with the revenue of the pre-VAT period and suitably extrapolated on the basis of the average growth of the rate of revenue of the previous five years. Further, motor spirit tax (MST) receipt, tax on liquor and credits on account of input tax credit (ITC) under the VAT adjusted against Central Sales Tax (CST) were to be excluded while computing the receipts. The resultant net revenue was to be compared with the projected tax revenue for 2006-07 to arrive at the loss due to the introduction of the VAT. The compensation was allowable at 75 *per cent* of such loss of revenue during the year 2006-07. The GoM preferred (January 2008) its final compensation claim of Rs. 3,061.23 crore for the year 2006-07, against which the GoI sanctioned Rs. 2,037.83 crore up to December 2008.

The refunds granted, receipts on account of the MST (non-VAT revenue),tax on liquor and input tax credit adjusted against the CST allowed as per the returns relating to the period April 2006 to March 2007 in Mumbai and Pune divisions were scrutinised between November 2008 and February 2009. The total amount of refund, MST, tax on liquor and input tax credit involved in the compensation claim under the VAT and amounts test checked for the period 2006-07 in the selected divisions were as under :

**(Rupees in crore)**

| Description | Total amount involved in compensation claim | Mumbai division | Pune division |
|---|---|---|---|
| Refund | 2,032.38 | 582.35 | 486.25 |
| MST | 6,496.98 | 6,496.98 | NIL |
| Tax on liquor | 954.24 | 362.95 | 134.81 |
| ITC | 1,058.87 | 375.45 | 428.64 |

Test check of the records in respect of Mumbai and Pune divisions indicated that there was excess compensation claim of Rs. 277.99 crore as discussed in the paragraphs below:

### 2.5.1 Inclusion of inadmissible refunds in the claim

According to the modalities prescribed by the GoI, tax refund allowed by the department relating to VAT items only are to be taken into consideration for claiming compensation.

**2.5.1.1** The GoM considered the total refund of Rs. 2,032.38 crore allowed during 2006-07 for compensation. Of this, Rs. 582.35 crore related to Mumbai division and Rs. 486.25 crore related to Pune division. However, as per the information furnished to Audit by the Sales Tax department, the refund relating to VAT amounted to Rs. 304.96 crore for Mumbai division and Rs. 434.37 crore for Pune division. This resulted in excess claim of compensation of Rs. 246.95 crore[14].

After this was pointed out (February 2009) the Department accepted (May and July 2009) the inclusion of refunds pertaining to old Acts amounting to Rs. 329.27 crore in respect of Mumbai and Pune Division resulting in excess claim of compensation of Rs. 246.95 crore.

**2.5.1.2** As per the letter sent to the Principal Secretary, Finance Department, GoM by the Commissioner of Sales Tax in January 2008, in final compensation claim the department had enhanced the amount of net revenue for the year 2006-07 by Rs. 1.07 crore[15] considering the grant of excess refund of Rs. 1.07 crore noticed by the refund audit section of the department. Scrutiny of the records indicated that the refunds actually disallowed by the refund audit sections in Mumbai and Pune was Rs. 96.79 lakh and Rs. 45.69 lakh respectively (totalling Rs. 1.42 crore). Thus, the net revenue was required to be enhanced by Rs. 1.99 crore[16] instead of Rs. 1.07 crore. This resulted in excess compensation claim of Rs. 69 lakh {(1.99 - 1.07) crore = 92 lakh x 75 *per cent}*.

The matter was reported to the department and the Government in March 2009; their reply is awaited (November 2009).

### 2.5.2 Inclusion of excess receipts on account of tax on liquor

According to the guidelines of the GoI, receipts on account of tax on liquor were to be excluded while computing the compensation claim. In the compensation claim preferred by the GoM for the year 2006-07, an amount of Rs. 954.24 crore was deducted on account of receipts from tax on liquor, out of which Rs. 362.95 crore related to Mumbai division.

During test check of the records of Mumbai division, it was noticed that in 20 cases, receipts on account of tax on liquor was considered at Rs. 69.50 crore. In these cases scrutiny of the audit reports in form 704 submitted by the chartered accountants indicated that actual receipts on account of tax on liquor was only Rs. 30.15 crore. The excess amount of Rs. 39.35 (69.50 – 30.15) crore was due to inclusion of tax on sale of food and non-exclusion of input tax credit on local sales. This resulted in excess deduction of Rs. 39.35 crore

[14] Inadmissible amount={(Rs. 582.35-Rs. 304.96) crore + (Rs. 486.25-Rs. 434.37) crore} = Rs. 329.27 crore, 75 *per cent* of Rs. 329.27 crore is Rs. 246.95 crore.

[15] Includes Rs. 50 lakh in Mumbai, Rs. 54 lakh in Raigad and Rs. 3 lakh in Thane (City) divisions.

[16] Includes Rs. 96.79 lakh in Mumbai, Rs. 45.69 lakh in Pune, Rs. 54 lakh in Raigad and Rs. 3 lakh in Thane (City) divisions.

and excess claim of compensation of Rs. 29.51 crore (75 *per cent* of Rs. 39.35 crore).

After the cases were pointed out (March 2009) the department accepted (June 2009) the observations in 19 cases amounting to Rs. 27.82 crore. Reply in the remaining case is awaited.

The matter was reported to the Government in March 2009; their reply has not been received (November 2009).

### 2.5.3 Incorrect deduction of ITC in compensation claim

The guidelines issued by the GoI prescribed that input tax credit adjusted against CST were to be excluded while computing compensation claim. During test check of the records of Mumbai division, it was noticed that in eight cases input tax credit was considered as per the returns filed by the dealers at Rs. 4.78 crore. However, as per the audit report in form 704 submitted by the chartered accountant, ITC adjusted against CST in respect of these dealers was only Rs. 3.66 crore. This resulted in excess deduction of Rs. 1.12 crore (Rs. 4.78 crore – Rs. 3.66 crore) and consequential excess claim of Rs. 84.33 lakh (75 *per cent* of Rs. 1.12 crore).

The matter was reported to the department and the government between January and March 2009; their reply has not been received (November 2009).

## 2.6 Non-observance of the provisions of Acts/Rules

*The BST/MVAT/CST/WCT Acts and Rules empowers/provide for :*

*(i) levy of tax/turnover tax/surcharge/interest at the prescribed rate;*

*(ii) registration of dealers liable for payment of tax under the VAT Act;*

*(iii) payment of refund of excess tax paid by the dealer either in cash or by adjustment against dues in respect of any other period;*

*(iv) exemption of tax on deemed export/branch transfers/inter-State sales subject to submission of the prescribed declarations/certificates;*

*(v) deferring tax under BST to eligible units either full or at a fixed percentage on the fulfillment of prescribed conditions; and*

*(vi) allowance of set-off as admissible.*

*The AAs, while finalising the assessments, did not observe some of the rules in cases mentioned in the paragraph 2.6.1 to 2.6.10. This resulted in non/short levy/non-realisation of tax/interest of Rs. 29.47 crore.*

### 2.6.1 Short levy of tax

Under the provisions of the BST Act, the rate of tax applicable on any commodity is determined with reference to the relevant entry in schedule 'B' or 'C' of the Act. Further, the Government, by notification from time to time, exempts certain sales or purchases from payment of tax in full or any part thereof, which are payable under the provisions of the Act, subject to such conditions as are prescribed. Besides, turnover tax (TOT), surcharge (SC) and interest are also leviable as per the provisions of the Act.

**2.6.1.1** During test check of the records of eight[17] divisions between December 2004 and September 2008, it was noticed in the assessments of 14 dealers finalised between July 2002 and October 2007, for the periods between 1999-2000 and 2004-05, that due to application of incorrect rates of tax, incorrect grant of exemptions, non-levy of tax, incorrect computation of turnover of taxable sales and error in computation of tax, there was underassessment of tax of Rs. 10.30 crore, including interest of Rs. 4.51 crore. A few illustrative cases are mentioned below:

**(Rupees in lakh)**

| **Sl. no.** | **Division** **No. of dealer** | **Period** **Month of assessment** | **Name of com-modity** | **Nature of irregularity** | **Taxable turnover** | **Tax leviable levied** *(per cent )* | **Under assess-ment** **Tax/ TOT/ SC/ Interest** | **Total** |
|---|---|---|---|---|---|---|---|---|
| 1. | Borivali 1 | 1999-2000 March 2005 | Kerosene and Superwhite Kerosene Oil | Resales of taxable goods were incorrectly allowed from the gross turnover of sales | 3,245.56 | 8 Nil | 259.64 32.46 25.96 352.26 | 670.32 |
| 2. | Thane 1 | 2001-02 March 2007 | Superior Kerosene Oil | Reduction of sales price was incorrectly allowed from the gross turnover of sales resulting in short levy of tax | 258.69 | 20 Nil | 51.74 2.59 5.17 NIL | 59.50 |
| 3. | Ghatkopar 1 | 2000-01 to 2002-03 July 2002 to May 2005 | Food | Incorrect benefit of notification was allowed to a contractor running canteen in a company | 307 | 4 Nil | 12.28 3.07 1.22 19.59 | 36.16 |
| 4. | Nariman Point 1 | 2002-03 April 2003 | Food | Incorrect rate/ exemption from tax was allowed on the goods served in five star hotel | 120.65 | 20 Nil | 24.13 1.81 2.41 8.77 | 42.50 |
| | | | Mineral Water | | 69.79 | 20 13 | 4.89 Nil 0.49 Nil | |
| 5 | Nariman Point 1 | 2004-05 July 2005 | Food | Incorrect exemption was allowed on food served to diplomatic missions though condition for exemption was not fulfilled | 126.90 | 20 Nil | 25.38 1.90 2.54 Nil | 29.82 |
| **Total** | | | | | | | **378.06 41.83 37.79 380.62** | **838.30** |

[17] Andheri(1), Borivali(3), Dhule(1), Ghatkopar (2), Nariman Point (3), Nashik (1), Thane (1) and Worli (2).

After the cases were pointed out between January 2005 and October 2008, the department rectified/revised the assessment or re-assessed 13 cases, between April 2006 and January 2009, raising additional demands of Rs. 9.43 crore including interest of Rs. 4.51 crore and penalty of Rs. 60.04 lakh. This includes one case where rectification of assessment of Rs. 87 lakh was awaited. In another case involving Rs. 60 lakh no action has been taken by the department (November 2009). In one case Rs. 4.02 lakh out of Rs. 6.22 lakh has been recovered and in respect of interest of Rs. 2.22 lakh the dealer is in appeal. A report on recovery in the remaining cases has not been received (November 2009).

The matter was reported to the Government between February 2009 and April 2009; their reply has not been received (November 2009).

**2.6.1.2** During scrutiny of records of Sales Tax Officer, C-959, Nagpur, it was noticed (April 2005) that the Sales Tax Officer allowed sales of branded milk aggregating Rs 22.07 crore as tax free under Section 5 of erstwhile BST Act while finalising assessment for the period from 1997-98 to 1998-99. However, the sale of branded milk was covered under schedule entry C-II-1 and was taxable at the rate of eight *per cent.* Incorrect assessment resulted in short levy of tax of Rs 3.85 crore including interest of Rs. 2.08 crore.

On this being pointed out in June 2005, the Deputy Commissioner of Sales Tax (Admn), M-95, Nagpur revised (August 2008) the assessment and raised the additional demand of Rs. 3.89 crore including interest and penalty. The dealer has filed an appeal against the revision orders. The decision in appeal is awaited (November 2009).

### 2.6.2 Non/Short levy of turnover tax and surcharge

Under Section 9 of the Bombay Sales Tax Act, 1959, as amended on 31 March 1999, Turnover tax was leviable at the rate of one *per cent* on the turnover of sales of goods specified in Schedule 'C', after deducting resales of goods from such turnover. Further, under Section 15A-I surcharge at the rate of 10 *per cent* of the tax payable where the aggregate of taxes payable by a dealer exceeded Rs. one lakh in a year was also leviable. From 1 April 2001, surcharge at the rate of 10 *per cent* of the taxes payable was leviable in all cases. Turnover tax was also leviable on the turnover of sales supported by declarations, subject to such conditions as prescribed by the Government from time to time.

**2.6.2.1** During test check of the records of Pune-II division in May 2007, it was noticed that in the assessment of a dealer, for the period 2001-02, finalised in January 2007, turnover tax on the turnover of sales of Rs. 10.54 crore and surcharge on sales tax of Rs. 1.37 crore were not levied. This resulted in underassessment of tax of Rs. 32.98 lakh including interest of Rs. 8.73 lakh.

After the case was pointed out (May 2007), the assessing officer accepted the observations in May 2007 and stated that action would be taken.

**2.6.2.2** During test check of the records of Nariman Point division in January 2008, it was noticed in the assessment of a dealer, finalised in March 2007, for the period 2001-02, that sales on declaration in Form-14 valued at

Rs. 9.14 crore were exempted from payment of turnover tax and surcharge. However, as per conditions of the notification sales on declaration in Form-14 were not exempted from turnover tax and surcharge. This resulted in underassessment of tax of Rs. 12.80 lakh.

After the case was pointed out in January 2008, the assessing authority accepted the observation and stated that the case had been forwarded in October 2008 to the appellate authority before whom the dealer has filed an appeal over the assessment order. The action taken in appeal is awaited (November 2009).

The matter was reported to the department and the Government in February and April 2009; their reply has not been received (November 2009).

### 2.6.3 Non/Short levy of tax under Works Contracts Tax Act

Under Section 6 of the Works Contract Tax (Re-enacted) Act, 1989 and the Rules made thereunder, a registered dealer is liable to pay tax on the turnover of sales involving transfer of property in goods in the execution of works contracts at the rates specified in the schedule to the Act. In case the dealer opted for the composition scheme, under Section 6A the amount of composition payable in lieu of tax on the total contract value, for the period May 1998 to 31 March 2000, was two *per cent* in respect of construction contracts and four *per cent* for other than construction contracts. The composition tax in respect of all types of contracts was three *per cent* for 2000-01 and four *per cent* thereafter. Besides, interest and penalty was leviable as per the provisions of the BST Act.

During test check of the records of Bandra division in September 2004 and March 2008, it was noticed in the assessments of two dealers, finalised in January 2004 and July 2006, that in one case sales valued at Rs. 9.90 crore for the periods 1999-2000 and 2000-2001 for construction and supply of heaters was incorrectly treated as a construction contract and taxed at the rate of two *per cent* instead of four *per cent*, resulting in underassessment of tax of Rs. 26.11 lakh including interest of Rs. 6.31 lakh. In the other case, for the period 2002-03, receipts on account of sales of Rs. 35.13 lakh on account of photo copy charges were deducted from turnover of sales under the BST Act. No tax was levied on these sales. As these receipts involved transfer of property of goods in the execution of works contract, tax was leviable under Works Contract Tax Act. This resulted in under assessment of tax of Rs. 2.76 lakh including interest of Rs. 1.35 lakh.

After the cases were pointed out in October 2004 and March 2008, the department revised/assessed the dealers in April 2006 and November 2008, raising additional demands totaling Rs. 28.92 lakh including interest of Rs. 7.64 lakh and penalty of Rs. 7,000. One dealer has filed appeal against the demand raised, results of appeal is awaited. Report on recovery in the other case is awaited (November 2009).

The matter was reported to the Government in April 2009; their reply has not been received. (November 2009).

### 2.6.4 Non-realisation of Value Added Tax

Under Section 3 of the Maharashtra Value Added Tax (MVAT) Act, 2002, every dealer is required to obtain a certificate of registration if the turnover of sales[18] during the year is Rs. 5 lakh and above, Value Added Tax (VAT) at the rate specified in the schedule to the act is leviable on the turnover of sales. Besides, interest and penalty is leviable as per provisions of the act.

In respect of licences issued by the district collectors for extraction of minor minerals including sand, the Commissioner of Sales Tax in his letter dated 28 March 2007 addressed to the Principal Secretary, Revenue and Forest Department had called for information in respect of these licences regarding name, address, quantity of sand extracted and amount of royalty paid. This was done as most of the licensees were found to be either unregistered or defaulters/evaders in payment of tax. In order to ascertain whether dealers liable to be covered were registered under the act and were paying taxes, details were independently collected by audit between January and March 2009 from the offices of five district collectors[19]. As per information received, 291 licences were issued by the collectorates for extraction of sand during the period 2005-06 to 2007-08. Out of this, only two licensees were registered under the MVAT Act and remaining 289 licensees were unregistered. These licensees had extracted sand aggregating 21.75 lakh brass[20]. Based on the district schedule of rates, the cost of sand extracted and sold excluding transportation charges worked out to Rs. 166.52 crore. The Department has not taken any follow-up action to get these dealers registered as per the provisions of the VAT Act though more than two years have elapsed after calling for the said information from the Collectorates. This resulted in non-realisation of VAT of Rs. 6.66 crore.

The matter was reported to the department in April 2009; their reply is awaited (November 2009).

### 2.6.5 Non-withdrawal of adjustment of refund

Under Section 43 of the Bombay Sales Tax Act, 1959, and rules made thereunder, the excess tax paid by a dealer is refundable by refund payment order or, at the option of the dealer, by adjustment against the amount due in respect of any other period.

During test check of the records of Nariman Point division in October 2006, it was noticed in the assessment of a dealer for the period 2001-02, finalised in January 2006, that the excess amount of Rs. 4.47 crore paid by the dealer, as per the assessment order passed in March 2001, for the period 1997-98 was adjusted against the dues payable by the dealer for the year 2001-02.

Scrutiny of records revealed that in March 2006, the Joint Commissioner of Sales Tax (Admn), Nariman Point Division, Mumbai had revised the assessment order for the period 1997-98 disallowing the excess amount and created a demand of Rs. 4.47 crore. This necessitated withdrawal of the credit

[18] substitued for the word "turnover" by Maharashtra Act 32 of 2006 with effect from June 2006.
[19] Ahmednagar, Aurangabad, Nashik, Pune, Raigad.
[20] Brass is 2.83 cubic meter.

of Rs. 4.47 crore incorrectly allowed in the assessment for the year 2001-02. However, no action was taken by the assessing officer to withdraw the incorrect adjustment of credit of Rs. 4.47 crore. This resulted in non-withdrawal of adjustment of credit of Rs. 4.47 crore.

After the case was pointed out in November 2006, the department rectified the error by issuing a corrigendum in November 2006, withdrawing the credit incorrectly allowed and enhancing the amount due for the year 2001-02 by Rs. 4.47 crore. The case is pending in second appeal. Decision of appeal is awaited. (November 2009).

The matter was reported to the Government in February 2009; their reply has not been received. (November 2009 ).

### 2.6.6 Irregular grant of exemption from payment of tax against form '14B'

Under the provisions of sub-section 3 of section 5 of the Central Sales Tax Act, 1956 read with Rule 21A of the Bombay Sales Tax Rules, 1959, sale in the course of export is exempt from tax provided the sale or purchase is preceded by an agreement or order from the foreign buyer for or in relation to such export. The selling dealer is required to produce a certificate in Form 14B duly filled in and signed by the exporter along with evidence of export of goods for claiming exemption of tax on sales.

**2.6.6.1** During test check of the records of Ghatkopar Division in December 2007, it was noticed that in respect of a dealer selling batteries, sales valued at Rs. 11.12 crore, for the period 2004-05, assessed during May 2006, was exempted from tax, as sales in the course of exports on certificates in Form 14B which were issued by the purchasing dealers. Scrutiny revealed that the purchase order placed by the exporter with the seller was prior to the order received from the foreign buyer. This indicated that the purchases made by the exporter was not preceded by an agreement with the foreign buyer resulting in irregular grant of the exemption and underassessment of tax of Rs. 2.06 crore including interest of tax of Rs. 30.75 lakh.

After the case was pointed out in January 2008, the department rectified the error in May 2008, raising additional demand of Rs. 1.79 crore including interest of Rs. 26.92 lakh and penalty of Rs. 10,000.

The rectification order was defective to the extent of incorrect reduction of sale price of Rs. 1.48 crore from the turnover sales of Rs. 11.12 crore. Under Rule 46A of the Bombay Sales Tax Rules, 1959, reduction of sale price was admissible only if the dealer had collected tax separately or had reimbursed himself to the extent of tax liability payable by him in the sale price itself. In this case since the dealer had claimed sales of Rs. 11.12 crore as exempt, no reduction from sale price was admissible. This resulted in short computation of tax of Rs. 27 lakh in the rectification order and total underassessment of Rs. 2.06 crore.

**2.6.6.2** During test check of the records of three divisions[21] between July 2004 and July 2008, it was noticed in the assessments of four dealers finalised

[21] Andheri (1), Ghatkopar (2) and Nariman Point (1).

between March 2004 and January 2008, for the periods 1995-96, 1996-97 and 2001-02 to 2003-04, that sales valued at Rs. 86.02 lakh were exempted from payment of tax on certificates in Form 14B. Scrutiny revealed that in respect of sales of Rs. 82.87 lakh, Form 14B furnished by three purchasing dealers were incomplete and regarding sales of Rs. 3.15 lakh one purchasing dealer had made purchases prior to the date of agreement orders of the foreign buyers. This resulted in irregular grant of exemption from tax and underassessment of Rs. 16.87 lakh including interest of Rs. 5.24 lakh.

After the cases were pointed out between August 2004 and August 2008, the department rectified the mistake/revised the assessment/reassessed the case between August 2008 and January 2009 raising additional demands totalling Rs. 26.69 lakh including interest of Rs. 5.24 lakh and penalty of Rs. 9.82 lakh. A report on recovery has not been received (November 2009).

The matter was reported to the department and to the Government in April 2009; their reply has not been received (November 2009).

### 2.6.7 Acceptance of invalid declarations for stock transfer

Under Section 6A(1) of the Central Sales Tax Act, 1956 no tax is payable by a dealer on movement of goods to other states which is not by way of sale but by reason of transfer of stock to other places of his business or to his agent or principal. For claiming exemption, the dealer may furnish to the assessing authority a declaration in Form 'F' duly filled in and signed by the Principal officer of the other place of business or his agent as the case may be alongwith evidence of despatch of the goods. Further, as per the CST (Registration and Transfer) Rules, 1957, a single declaration in Form 'F' is required for transfer of goods effected during a period of one calender month.

**2.6.7.1** During test check of the records of Churchgate division in August 2005, it was noticed in the assessment of a dealer finalised in June 2004, for the period 2002-03, that in the returns filed by the dealer, claims relating to transfer of the goods of Rs. 2.11 crore to its branches/consignment agents were exempted from payment of tax. Scrutiny indicated that out of the claims relating to Rs. 2.11 crore, the branches/agents had not furnished Form 'F' to the extent of Rs. 1.83 crore. Further, in respect of the claims relating to Rs. 12.45 lakh, Form 'F' kept on records were incomplete with respect to description of the goods, transfer documents etc.. This resulted in irregular grant of exemption from tax of Rs. 26.13 lakh including interest of Rs. 6.59 lakh.

After the case was pointed out in September 2005, the department revised the assessment in February 2008, raising additional demand of Rs. 26.13 lakh including interest of Rs. 6.59 lakh. A report on recovery has not been received (November 2009).

**2.6.7.2** Scrutiny of assessment records for the assessment year 2007-08 of two dealers in Aurangabad and Nashik divisions revealed that they had transferred goods (Brakes items and Travel Bags) valued at Rs. 41.12 lakh during the period between April 2002 and December 2003 to their branches in Karnataka and claimed exemption from tax by submitting three declarations in Form 'F'. However, cross verification of these forms with the assessment records of the issuing authority of Sales Tax Department of Karnataka revealed that the said

forms had not been issued by them. Thus incorrect allowance of sales against Form 'F' resulted in underassessment of tax of Rs. 11.42 lakh including interest of Rs. 1.50 lakh and penalty of Rs. 4.96 lakh.

The matter was reported to the department in May 2009; their reply has not been received (November 2009).

**2.6.7.3** During test check of the records of Andheri division in November 2006, it was noticed in the assessment of a dealer finalised in March 2006, for the period 2002-03, that transfer of the goods to the agents in other States valued at Rs. 31.16 lakh were exempted from tax on production of the declarations in Form 'F'. Scrutiny revealed that all the declarations, in Form 'F' kept on record covered transactions of three months. As such, these declarations were invalid and the turnover was liable to tax under the local Act. This resulted in underassessment of Rs. 5.89 lakh including interest of Rs. 2.77 lakh.

After the case was pointed out, the department rectified the assessment in March 2008, raising additional demand of Rs. 5.89 lakh including interest of Rs. 2.77 lakh. A report on recovery has not been received (November 2009).

The matter was reported to the Government between February and May 2009; their reply has not been received (November 2009).

### 2.6.8 Short levy of Central Sales Tax

Under Section 8 of the Central Sales Tax Act, 1956 and the rules made thereunder, tax on sales in the course of inter-State trade or commerce, supported by valid declarations in Form 'C', is leviable at the rate of four *per cent* of the sale price. Otherwise, in respect of declared goods, tax is leviable at twice the rate applicable on sales and in respect of goods other than declared goods, at 10 *per cent* or at the rate applicable to the sale or purchase of goods, inside the State, whichever is higher. Besides, interest and penalty is also leviable as per the provisions of the BST Act.

During test check of the records of Kolhapur division (Satara district) in September 2006, it was noticed in the assessment of two dealers finalised in February and March 2006, for the period 2000-01, that inter-State sales valued at Rs. 19.93 lakh were taxed at concessional rate of tax though the declaration forms were invalid either due to absence of registration details or due to the date of registration not being valid for the period of transaction. This resulted in underassessment of tax of Rs. 6.11 lakh including interest of Rs. 3.85 lakh.

After the cases were pointed out in September 2006, the department revised the assessments in February 2008 raising additional demands of Rs. 6.31 lakh including interest of Rs. 3.85 lakh and penalty of Rs. 20,000. A report on recovery has not been received (November 2009).

The matter was reported to the Government in April 2009; their reply has not been received (November 2009).

### 2.6.9 Incorrect deferment of tax under package scheme of incentives

As per the package scheme of incentives of 1993, an eligible unit is entitled to incentives in the form of local sales tax and Central Sales Tax on the sale of

finished goods and purchase tax on the purchase of raw materials during the period covered by the eligibility and entitlement certificates subject to terms and conditions specified in the schemes. An existing unit which creates additional manufacturing capacity for manufacture of the same product is eligible for tax benefits on the product manufactured out of the expanded capacity only. Further, taxes are required to be deferred either in full or at the specified percentage mentioned in the eligibility certificate.

During scrutiny of records in Ghatkopar division in July 2005, it was noticed in the assessments of a dealer engaged in the manufacture of Yeast, for the periods 2001-02 and 2002-03 finalised in September 2004 and October 2004, that eligibility/entitlement certificates for deferment of sales tax incentives was granted from October 2000 to September 2008 for expansion of production capacity. The entitlement certificate prescribed that deferment of taxes in the eligible unit was only to the extent of 37.58 *per cent* of the production. However, while computing taxes to be deferred the amount was not restricted to the percentage prescribed in the entitlement certificate and set-off was also not reduced from the tax collected. This resulted in excess deferment and consequential underassessment of tax totaling Rs. 64.74 lakh including withdrawal of interest of Rs. 6.24 lakh on the refund incorrectly granted in the assessment orders.

After the case was pointed out in August 2005, the department revised the assessments in April 2008, raising additional demands of Rs. 1.37 crore including interest of Rs. 19 lakh. A report on recovery has not been received (November 2009).

The matter was reported to the department and the Government in April 2009; their replies have not been received (November 2009).

### 2.6.10 Incorrect grant of set-off

According to the Bombay Sales Tax Act and Rule 41D of BST Rules, a manufacturer who had paid tax on purchase of goods specified in entry 6 of Schedule 'B' and 'C' to the Act and used those goods within the state in the manufacture of taxable goods for sale or export or in packing of goods so manufactured was allowed set-off of tax paid on the purchases after reducing four *per cent* of the purchase price in respect of capital goods and three *per cent* in respect of raw materials. In case the claimant dealer was running a 100 *per cent* export oriented unit (EOU), certified, as such, by the Government of India (GoI), full set-off on the purchase price of raw materials was admissible without reducing any amount from the purchase price.

During test check of records in the office of the Assistant Commissioner of Sales Tax, B-225, Ahmednagar in December 2004, it was noticed in the assessment for the year 2000-01, finalised in November 2003, that in the case of a dealer, the assessing officer had allowed full set-off on tax paid on purchase valued at Rs. 160.56 lakh without reducing three *per cent* of purchase price treating the unit as a 100 *per cent* EOU. However, the unit was not certified by GoI as a 100 *per cent* EOU. This resulted in incorrect grant of set-off of Rs. 6.51 lakh including interest of Rs. 1.69 lakh.

After the case was pointed out in January 2005, the department accepted the error and revised the assessment in February 2008 raising additional demand of Rs. 6.51 lakh including interest of Rs. 1.69 lakh. A report on recovery had not been received (November 2009).

The matter was reported to the Government in February 2009; their reply has not been received (November 2009).