

## CHAPTER-IV REVENUE RECEIPTS

### 4.1 Trend of revenue receipts

The tax and non-tax revenue raised by the Government of Sikkim during the year 2008-09, the State's share of divisible Union taxes and grants-in-aid received from the Government of India during the year 2008-09 and the corresponding figures for the preceding four years are mentioned below.

**Table – 4.1**

*(Rupees in crore)*

Sl. no.		2004-05	2005-06	2006-07	2007-08	2008-09
<b>I.</b>	<b>Revenue raised by the State Government</b>					
	• Tax revenue	116.95	147.23	173.18	197.86	199.19
	• Non-tax revenue	992.47	990.10	1,085.04	1,413.74	1,205.31
	<b>Total</b>	1,109.42	1,137.33	1,258.22	1,611.60	1,404.50
<b>II.</b>	<b>Receipts from the Government of India</b>					
	• State's share of divisible Union taxes	107.35	182.13	222.78	345.12	364.20
	• Grants-in-aid	675.63	644.90	635.54	742.71	902.55
	<b>Total</b>	782.98	827.03	858.32	1,087.83	1,266.75
<b>III.</b>	<b>Total receipts of the State</b>	1,892.40	1,964.36	2,116.54	2,699.43	2,671.25
<b>IV.</b>	<b>Percentage of I to III</b>	<b>59</b>	<b>58</b>	<b>59</b>	<b>60</b>	<b>53</b>

During the year 2008-09, the State Government raised 53 *per cent* of the total revenue receipts against 60 *per cent* in the preceding year. The balance 47 *per cent* of receipts during 2008-09 was from the Government of India.

#### 4.1.1 Tax revenue

The following table presents the details of tax revenue raised during the period from 2004-05 to 2008-09:

**Table – 4.2**

(Rupees in crore)

Sl. no.	Head of revenue	2004-05	2005-06	2006-07	2007-08	2008-09	Percentage of increase (+)/ decrease (-) in 2008-09 over 2007-08
1.	Sales tax/VAT	48.18	56.65	74.66	81.32	101.14	(+) 24.37
2.	Taxes on income other than corporation tax	29.09	47.82	46.71	49.10	16.16	(-) 67.00
3.	State excise	32.69	32.96	33.31	37.94	46.47	(+) 22.48
4.	Stamps and registration fees	1.43	2.27	2.52	4.26	4.35	(+) 2.11
5.	Taxes on vehicles	3.24	4.24	5.95	6.22	6.94	(+) 11.58
6.	Other taxes and duties on commodities and services	1.88	2.68	9.25	16.26	22.18	(+) 36.41
7.	Land revenue	0.44	0.61	0.78	2.75	1.95	(-) 29.09
	<b>Total</b>	<b>116.95</b>	<b>147.23</b>	<b>173.18</b>	<b>197.85</b>	<b>199.19</b>	(+) 0.68

The following reasons for variations were reported by the concerned departments.

**Sales Tax/VAT:** The increase was due to proper monitoring for collection of tax and more realisation under Trade Tax (VAT) and State Sales Tax Act.

**Taxes on vehicles:** The increase was due to introduction of luxury tourist vehicles from which tax & permit fee etc. were realised and registration of more commercial and private vehicles.

**Other taxes and duties on commodities and services:** The increase was due to more realisation receipts from cesses under other Acts and from fees on *Bazaar* Contract and Miscellaneous Receipts.

In respect of Stamps and Registration reasons for increase was not furnished by the Department (October 2009) though called for (August-September 2009).

#### 4.1.2 Non-tax revenue

The following table presents the details of non-tax revenue raised during the period from 2004-05 to 2008-09:

Table – 4.3

(Rupees in crore)

Sl. no.	Head of revenue	2004-05	2005-06	2006-07	2007-08	2008-09	Percentage of increase (+)/ decrease (-) in 2008-09 over 2007-08
1.	Interest receipts	8.03	6.31	5.34	15.10	25.94	(+) 71.79
2.	Road transport	21.52	13.67	14.86	15.62	17.64	(+) 12.93
3.	Plantations	1.63	2.01	1.95	2.10	2.35	(+) 11.90
4.	Dividends & profits	0.92	1.14	0.76	0.68	1.31	(+) 92.65
5.	Forestry and wild life	7.92	9.97	9.50	10.95	11.26	(+) 2.83
6.	Tourism	0.78	0.81	0.87	1.18	2.11	(+) 78.81
7.	Crop husbandry	0.31	0.36	0.50	1.64	0.71	(-) 56.71
8.	Power	21.41	28.00	58.16	97.66	154.74	(+) 58.45
9.	Printing & stationery	1.07	1.65	1.69	1.98	1.50	(-) 24.24
10.	Medical and public health	0.98	0.91	0.60	1.14	0.96	(-) 15.79
11.	Village & small industries	0.08	0.14	0.10	0.23	0.08	(-) 65.22
12.	Public works	2.46	3.09	3.74	4.32	4.97	(+) 15.05
13.	Police	4.38	14.14	13.90	14.64	11.68	(-) 20.22
14.	Animal husbandry	0.31	0.41	0.39	0.43	0.30	(-) 30.23
15.	Industries	0.01	0.19	0.02	0.01	0.25	(+) 2,400.00
16.	State lotteries <sup>1</sup>	912.27 (31.16)	898.35 (22.19)	963.30 (50.01)	1,232.55 (30.84)	957.00 (54.46)	(-) 22.36
17.	Others	8.39	8.95	9.36	13.51	12.51	(-) 7.40
	<b>Total</b>	<b>992.47</b>	<b>990.10</b>	<b>1,085.04</b>	<b>1,413.74</b>	<b>1,205.31</b>	(-) 14.74

The following reasons for variations were reported by the concerned departments.

**Interest receipts:** The increase was due to more realisation on investment of cash balances.

**Road transport:** The increase was due to increase in traffic flow at the later part of the year, as a result of which the collections of supervision charges rose up.

**Tourism:** The increase was due to more realisation under rent and catering charge.

**Crop husbandry:** The decrease was due to less realisation on seeds and other receipts.

**Medical and public health:** The decrease was due to less realisations on receipts from patients and other receipts etc.

**Village and small industries:** The decrease was due to less realisations on sale proceeds.

**Police:** The decrease was due to less realisations on other receipts and police check post.

<sup>1</sup>Figures in brackets represent net receipts.

**Animal husbandry:** The decrease was due to less realisations on receipts from sheep, wool and piggery and other receipts.

**State lotteries:** The decrease was due to sudden closure of two digit lotteries.

The Finance, Revenue & Expenditure Department did not inform (October 2009) the reasons for increase in dividends and profits despite being requested (August-September 2009).

#### 4.1.3 Variations between the budget estimates and actuals

The variations between the budget estimates (BE) and actuals of revenue receipts for the year 2008-09 in respect of the principal heads of tax and non-tax revenue are mentioned below.

**Table – 4.4**

(Rupees in crore)

Sl. no.	Head of revenue	BE	Actuals	Variations excess (+) or shortfall (-)	Percentage of variation
<b>A.</b>	<b>Tax revenue</b>				
1.	Sales Tax/VAT	56.00	101.14	(+) 45.14	(+) 80.61
2.	Taxes on income other than corporation tax	40.00	89.61	(+) 49.61	(+) 124.03
3.	State excise	42.50	46.46	(+) 3.96	(+) 9.32
4.	Other taxes and duties on commodities and services	14.86	22.18	(+) 7.32	(+) 49.26
5.	Taxes on vehicles	4.00	6.94	(+) 2.94	(+) 73.50
6.	Stamps and registration	2.33	4.35	(+) 2.02	(+) 86.70
7.	Other taxes on income and expenditure	42.30	16.16	(-) 26.14	(-) 61.80
8.	Land Revenue	1.11	1.95	(+) 0.84	(+) 75.68
<b>B.</b>	<b>Non-tax revenue</b>				
9.	Power	146.00	154.74	(+) 8.74	(+) 5.99
10.	Police	16.30	11.68	(-) 4.62	(-) 28.34
11.	Road transport	14.00	17.64	(+) 3.64	(+) 26.00
12.	Forestry and wildlife	8.00	11.26	(+) 3.26	(+) 40.75
13.	Interest receipts	3.07	25.94	(+) 22.87	(+) 744.95
14.	Public works	2.04	4.97	(+) 2.93	(+) 143.63
15.	Medical and Public Health	0.50	0.96	(+) 0.46	(+) 92.00
16.	Tourism	1.23	2.11	(+) 0.88	(+) 71.54
17.	Dividends and profits	0.75	1.31	(+) 0.56	(+) 74.67
18.	Crop Husbandry	0.34	0.71	(+) 0.37	(+) 108.82
19.	Animal Husbandry	0.40	0.30	(-) 0.1	(-) 25.00
20.	Plantations	2.20	2.35	(+) 0.15	(+) 6.82
21.	Village and Small Industries	0.15	0.08	(-) 0.07	(-) 46.67
22.	Industries	0.17	0.25	(+) 0.08	(+) 47.06

The following reasons for variations between BE and actuals were reported by the concerned departments.

**Taxes on vehicles:** The increase was due to more registration of vehicles.

**Police:** The decrease was due to less realisations on other receipts and police check post.

**Road transport:** The increase was due to increased traffic flow in the later part of the year resulting in rise of supervision charges.

**Other administrative services:** The increase was due to the issue of duplicate identity cards on payment to voters and sale of election forms and documents after the announcement of general elections in the last quarter of the financial year.

**Urban development:** The increase was due to (i) better renewal initiative and new licences, (ii) regularisation of fee collection from Mobile Towers, (iii) enhanced collection through notices and (iv) increased lease rent from 5<sup>th</sup> year.

**Information and publicity:** The increase was due to realisation of outstanding advertisement cost from other Departments.

**Co-operation:** The increase was due to more receipts from cooperative societies.

**Other rural development programme:** The increase was due to sanction of new schemes.

**Non-ferrous, mining & metallurgical industries:** The increase was due to more number of applications received for the stability report from the public.

**Other general economic services:** The increase was from higher calibration fee on storage tanks which were verified in the interval of five years.

The other departments did not inform (October 2009) the reasons for variation despite being requested (August-September 2009).

The fact remains that the very large variations under most of the heads point to the need for framing of budget estimates on a realistic basis.

#### 4.1.4 Analysis of collection

The break-up of total collection at the pre-assessment stage and after regular assessment for the year 2008-09 and the corresponding figures for the preceding two years as furnished by the departments is as follows.

**Table – 4.5**

(Rupees in crore)

Head of revenue	Year	Amount collected at pre-assessment stage	Amount collected after regular assessment (additional demand)	Penalties for delay in payment of taxes and duties	Amount refunded	Net collection <sup>2</sup>	Percentage of column 3 to 7
1	2	3	4	5	6	7	8
Sales Tax/	2006-07	1.31 <sup>3</sup>	0.17	0.02	0.004	1.50	87.33
VAT	2007-08	1.63	1.72	1.25	Nil	4.60	35.43
	2008-09	1.91	1.99	1.35	1.24	4.01	47.63
Sikkim	2006-07	0.35	2.06	Nil	0.029	2.38	14.71
Income	2007-08	Nil	3.84	Nil	0.22	3.62	-
Tax	2008-09	Nil	Nil	Nil	Nil	Nil	Nil

#### 4.1.5 Cost of collection

The gross collection in respect of major revenue receipts, expenditure incurred on collection and the percentage of such expenditure to gross collection during the years 2006-07, 2007-08 and 2008-09 along with the relevant all India average percentage of expenditure on collection to gross collection for 2007-08 was as follows.

**Table – 4.6**

(Rupees in crore)

Sl. no.	Head of revenue	Year	Collection	Expenditure on collection of revenue	Percentage of expenditure on collection	All India average percentage for the year 2007-08
1.	Sales tax/VAT	2006-07	74.66	1.57	2.10	0.83
		2007-08	81.32	1.72	2.12	
		2008-09	101.14	1.95	1.93	
2.	State excise	2006-07	33.31	1.90	5.70	3.27
		2007-08	37.94	1.97	5.19	
		2008-09	46.46	2.36	5.08	
3.	Taxes on vehicles	2006-07	5.95	0.56	9.41	2.58
		2007-08	6.22	0.60	9.65	
		2008-09	6.94	0.77	11.10	

Thus, the percentage of expenditure on collection during 2008-09 as compared to the corresponding all India average percentage for 2007-08, was high in all the taxes which the Government needs to look into.

#### 4.1.6 Analysis of arrears of revenue

The arrears of revenue as on 31 March 2009 in respect of some principal heads of

<sup>2</sup>Net collection reported by departments does not tally with the Finance Accounts and needs reconciliation.

<sup>3</sup>The department did not inform the reasons for wide variation vis-à-vis the previous year despite being requested.

revenue as furnished by the departments amounted to Rs. 25.35 crore of which Rs. 10.33 crore was outstanding for more than five years as mentioned in the following table.

**Table – 4.7***(Rupees in crore)*

Sl. no.	Head of revenue	Amount outstanding as on 31 March 2009	Amount outstanding for more than five years as on 31 March 2009
1.	Road transport (SNT)	1.90	Nil
2.	Sales tax/VAT	0.65	0.20
3.	Income tax	8.23	7.58
4.	Police	11.27	Nil
5.	Non-ferrous mining & metallurgical industries	3.30	2.55
	<b>Total</b>	<b>25.35</b>	<b>10.33</b>

#### 4.1.7 Arrears in assessments

The details of pending assessment cases at the beginning of the year, cases becoming due for assessment during the year, cases disposed during the year and number of cases pending at the end of the year 2008-09 as furnished by the departments are mentioned below.

**Table – 4.8**

Name of tax	Opening balance	New cases due for assessment during 2008-09	Total assessments due	Cases disposed during 2008-09	Balance at the end of the year	Arrears in percentage against total cases
Sales tax/VAT	397	300	697	401	296	42.47
Sikkim Income Tax	Nil	Nil	Nil	Nil	Nil	Nil

Thus, percentage of assessment cases pending at the end of 2008-09 was 42.47 *per cent*. Immediate action needs to be taken to finalise the pending assessment cases within a definite time frame. The department informed (October 2009) that the pending assessment cases related to firms, companies and house property dealers only and that many of the firms were presently not in operation.

#### 4.1.8 Evasion of tax

There was no case of evasion of tax detected by the Finance, Revenue and Expenditure Department in respect of sales tax/VAT during the year as per information furnished by the department.

#### 4.1.9 Write off and waiver of revenue

There was no case of write off and waiver of revenue in respect of sales tax/VAT,

income tax and state excise as per information furnished by the respective departments.

#### 4.1.10 Refunds

The number of refund cases pending at the beginning of the year 2008-09, claims received during the year, refunds allowed during the year and cases pending at the close of the year 2008-09, as reported by the departments are mentioned below.

**Table – 4.9**

(Rupees in lakh)

Sl. no.	Particulars	State excise		Sales tax/VAT		Income tax	
		No. of cases	Amount	No. of cases	Amount	No. of cases	Amount
1.	Claims outstanding at the beginning of the year	Nil	Nil	Nil	Nil	Nil	Nil
2.	Claims received during the year	2	19.97	6	123.72	268	17.26
3.	Refunds made during the year	2	19.97	6	123.72	268	17.26
4.	Balance outstanding at the end of the year	Nil	Nil	Nil	Nil	Nil	Nil

#### 4.1.11 Compliance with the earlier Audit Reports

During the years from 2003-04 to 2007-08, the departments/Government accepted audit observations involving Rs. 107.97 crore of which only Rs. 50 lakh had been recovered till March 2009 as mentioned below.

**Table – 4.10**

(Rupees in crore)

Year of Audit Report	Total money value	Accepted money value	Recovery made
2003-04	9.75	9.75	—
2004-05	85.71	85.71	0.02
2005-06	9.95	6.80	0.48
2006-07	22.31	5.39	—
2007-08	1.33	0.32	—
<b>Total</b>	<b>129.05</b>	<b>107.97</b>	<b>0.50</b>

The fact that only 0.46 per cent of the accepted amount has been recovered, points to the need for the government to take concerted action in this regard.

#### 4.1.12 Failure to enforce accountability and protect interest of the Government

The Accountant General (Audit), Sikkim arranges to conduct periodical inspection of the various offices of the Government departments to test check the transactions of tax and non-tax revenue receipts and verify the maintenance of important accounting and other records as prescribed in the rules and procedures. These inspections are followed up with Inspection Reports (IRs) incorporating irregularities detected

during inspection and not settled on the spot, which are issued to the heads of the offices inspected with copies to the next higher authorities for taking prompt corrective action. The heads of offices/Government are required to comply with the observations contained in the IRs and rectify the defects and omissions promptly and report compliance through initial reply to the Accountant General within thirty days from the dates of issue of the IRs. Serious financial irregularities are reported to the heads of the departments and the Government.

Audit observations on the loss of revenue/short levy of demand and energy charges, irregular waiver etc., noticed during local audit are intimated through inspection reports (IRs) to the departmental officers, heads of departments and also to the Government, where necessary. The points mentioned in the IRs are to be settled as expeditiously as possible and first replies are to be sent within four weeks from the date of receipt of IRs by the departments.

The position of IRs (with money value) in respect of the following revenue heads that were issued upto the end of December 2008 but remained outstanding as of June 2009 is tabulated below.

**Table – 4.11**

*(Rupees in crore)*

Sl. no.	Head of revenue	No. of IRs	No. of audit objections	Amount
1.	State lotteries	05	08	137.43
2.	Mines, Minerals and Geology	02	02	3.31
3.	Urban development and housing	07	13	2.31
4.	Motor vehicles	03	07	0.20
5.	Sales tax/VAT	08	37	83.01
6.	Income tax	12	47	27.01
7.	Forest	30	50	46.99
8.	State excise	04	08	2.63
9.	Land revenue	15	16	0.58
10.	Energy and power	8	21	125.95
	<b>Total</b>	<b>94</b>	<b>209</b>	<b>429.42</b>

The outstanding audit observations indicate the failure of the departmental officers in initiating rectificatory action for defects, omissions and irregularities pointed out in the IRs by the Accountant General. The Principal Secretaries/Secretaries of the departments, who were informed of the position through half-yearly reports, also failed to ensure that the concerned officers took prompt and timely action.

#### **4.1.13 Departmental Audit Committee Meetings**

During 2008-09, two Audit Committee meetings were held and 16 IRs and 38 paragraphs were discussed out of which three IRs and 16 paragraphs were settled.

#### **4.1.14 Response of the departments to draft audit paragraphs**

Draft audit paragraphs are issued to the concerned heads of the departments with a copy to the Finance, Revenue and Expenditure Department, the replies to which are to be communicated to the Accountant General within six weeks of the date of their receipt.

One review and seven draft paragraphs proposed for inclusion in the Report of the Comptroller and Auditor General of India for the year ended March 2009 were forwarded to the Secretaries of the respective departments between May 2009 and June 2009 through demi-official letters. The administrative secretaries responded to all the three paragraphs and the review featuring in this chapter.

#### **4.1.15 Follow up on Audit Reports – summarised position**

The administrative departments are required to submit explanatory notes on paragraphs and reviews included in the Audit Reports after its presentation in the State Legislature.

As at the end of 2008-09, Audit Reports for the period upto the year 2005-06 were discussed and recommendations made and selection of paras in respect of Audit Report 2006-07 done, which were taken up for discussion during 2009-10.

#### **4.1.16 Results of audit**

Test check of the records of income and commercial tax, state excise, transport, state lotteries, mines & geology, urban development and housing, forest department etc. conducted during the year 2008-09 indicated loss/non-collection of revenue/royalty/penalty, non/incorrect assessment, wrong imposition of rate, incorrect assessment of excise duties, irregular waiver etc. aggregating Rs. 97.92 crore in 24 cases. The department/Government accepted audit observations in all 24 cases and recovered Rs. 0.07 crore in three cases. In other cases, observations pointed out by audit are being considered for recovery/re-assessment etc.

This chapter contains one review involving Rs. 1.59 crore and three paragraphs involving Rs. 6.89 crore out of which Rs. 5.87 crore has been accepted by the departments as discussed in the succeeding paragraphs.

**FINANCE, REVENUE AND EXPENDITURE DEPARTMENT  
(COMMERCIAL TAX DIVISION)**

**4.2 Performance Audit on transition from sales tax to VAT**

**Highlights**

Though the revenue collection registered an increasing trend after implementation of VAT, the average and overall (except 2006-07) growth rate after implementation of VAT showed a negative trend.

(Paragraph 4.2.6)

The division did not prescribe the quantum of security deposit to be realised from the dealers. Consequently security deposit from the dealers was not realised despite the fact that 2,313 dealers out of 5,089 did not submit their returns. This also deprived the division from realising the arrear of Rs. 11.76 lakh due from eight dealers.

(Paragraph 4.2.8.4)

The division not only failed to persuade 2,378 dealers to file returns within the prescribed timeframe but also did not levy penalty of Rs. 72.92 crore and continued to issue way bills and C forms to these dealers for import of goods from neighbouring States.

(Paragraph 4.2.9.1)

Failure to initiate scrutiny of self assessed returns by the assessing authorities in accordance with Section 37 of SVAT Act led to non-detection of tax evasion of Rs. 2.15 crore by 19 dealers.

(Paragraph 4.2.9.2)

Failure of the assessing authorities to initiate assessment of tax on best judgment basis under Section 38 of SVAT Act not only led to delay in realisation of tax but also retention of Government dues with the dealers.

(Paragraph 4.2.9.3)

Absence of provision for cross verification of records of sub/principal contractors, led to non-detection of tax evasion of Rs. 54.83 lakh by two sub-contractors.

(Paragraph 4.2.11.2 & 4.2.11.3)

The division did not upload details of issue and utilisation of statutory declaration forms by the dealers of Sikkim in the TINXSYS website created by the Government of India to serve as a repository of information on declaration forms. This defeated the purpose of the website as far as information relating to Sikkim was concerned.

(Paragraph 4.2.11.4)

**The SVAT Act and Rules did not have any provision for maintenance of various records/registers by the division and for submission of report/return at any level. Despite existence of internal audit, no inspection was carried out during the period of review.**

**(Paragraph 4.2.14 & 4.2.15)**

**Mandatory VAT audit under SVAT Act was not initiated by the division even after four years of implementation to ensure correctness of the returns submitted by the dealers and assessments made by the assessing authorities.**

**(Paragraph 4.2.16.1 & 4.2.16.2)**

**Concealment of purchase and sales turnover by three dealers resulted in tax evasion of Rs. 79.84 lakh.**

**(Paragraph 4.2.17)**

**Non-deposit of VAT by one industry established under Sikkim Industrial Promotion and Incentive Act led to non-remittance of realised tax of Rs. 47.11 lakh.**

**(Paragraph 4.2.18)**

#### **4.2.1 Introduction**

In the existing sales tax structure, there were problems of double taxation of commodities and multiplicity of taxes, resulting in a cascading tax burden. For instance, before a commodity was produced, inputs were first taxed and then after the commodity was produced, output was taxed again. This caused an unfair double taxation with cascading effects. In several States the multiplicity of taxes, such as turnover tax, surcharge on sales tax, additional surcharge, etc. posed a problem.

With the introduction of Value Added Tax (VAT), these taxes were to be abolished. In VAT, a set-off was given for input tax as well as tax paid on previous purchases. In addition, Central sales tax was also going to be phased out. As a result, the overall tax burden was to be rationalised which would result in fall in prices in general. Moreover, VAT was to replace the existing system of inspection by a system of built-in-self-assessment by the dealers and auditing. The tax structure was to become simple and more transparent. That was to improve tax compliance and also augment revenue growth.

With the above objectives and on the recommendation of the Empowered Committee of State Finance Ministers on State-Level Value Added Tax, the Government of Sikkim repealed (except petrol, diesel and liquor) the Sales Tax (ST) Act, 1983 and enacted the Sikkim Value Added Tax Act, 2005 (SVAT Act) from 1 April 2005.

Some of the differences between the existing Sales Tax Act and VAT Act were as under:

- VAT is a multi point tax system while sales tax was single/double point tax system;
- VAT system relies more on the dealers to pay the tax willfully and submit the returns and deemed self assessment in VAT while supporting documents were required along with the returns in ST;
- Percentage check provided in VAT Act as against 100 *per cent* assessment in the existing Sales Tax Act;
- Reduced control of the executive on the dealers in VAT while many other taxes were there in ST.

SVAT Act had five schedules with 'nil' (exempted) *per cent*, one *per cent*, four *per cent*, four *per cent* and 12.5 *per cent* rate of tax respectively. Sections 26 to 29 of SVAT Act read with Rules 5 to 8 of SVAT Rules provide, detailed procedure for registration of dealers. Registered dealers were provided with a Taxpayer Identification Number (TIN). Section 16, 17 and 30 of SVAT Act have provision for dealers to pay tax at composite rate.

#### 4.2.2 Organisational set up

Commercial Tax division of Finance, Revenue and Expenditure Department (FRED), Government of Sikkim was responsible for implementation of VAT in the State. The FRED was headed by the Additional Chief Secretary and the division was headed by an Additional Commissioner who was assisted by three Joint Commissioners, three Deputy Commissioners, five Assistant Commissioners and other sub-ordinate staff who were posted at division headquarter at Gangtok, two Circle Offices at Gangtok and Jorethang, check post including charge office at Rangpo and check post at Melli.

#### 4.2.3 Audit objectives

The review was aimed to ascertain whether the

- planning for implementation and the transition from the ST Act to VAT Act was effected timely and efficiently;
- organisational structure was adequate and effective;
- provisions of the VAT Act and the Rules made there under were adequate and enforced properly to safeguard the revenues of the State;
- internal control mechanism existed in the Department and was adequate and effective to prevent leakage of revenue; and

- status of system which has been in place for four years, was adequate.

#### 4.2.4 Scope and methodology of audit

The performance audit on transition from Sales Tax to VAT in Sikkim for the period 2004-05 to 2008-09 was conducted between April and July 2009 with reference to the records maintained at Commercial Tax Division, FRED, Gangtok, both the circle offices (Gangtok and Jorethang) and both the check posts (Rangpo - including charge office and Melli).

Out of 2,776 registered dealers, who submitted their returns, assessments were completed in respect of 474 dealers, all of which were selected for detailed scrutiny. Of the remaining 2,302 un-assessed dealers, 149<sup>4</sup> dealers were selected. Thus, total 623 dealers (22.44 *per cent*) were taken up for detailed scrutiny. While selecting the 149 dealers, emphasis was given on industrial, automobiles dealers, works contractors and dealers having high turnover.

The performance audit was conducted through issue of requisitions for data and the records, analysis of data with reference to original records, scrutiny of files and other records maintained in the Commercial Tax Division, circle offices and check posts and framing of audit observations.

#### 4.2.5 Acknowledgement

Indian Audit and Accounts Department acknowledges the co-operations of the division in providing necessary information and records for audit. Performance audit commenced with the letter of engagement (March 2009) followed by an entry conference (April 2009) with Additional Commissioner, Commercial Tax Division. Audit programme, scope, objectives and criteria were explained in the entry conference. The audit findings were communicated to the division on 11 August 2009 and discussed with the Additional Commissioner and other officers of the division in the exit conference held on 13 August 2009 and their replies obtained. The performance audit report was finalised after taking into consideration the replies received in the exit conference and at other times.

#### Audit findings

#### 4.2.6 Pre-VAT and post-VAT tax collection

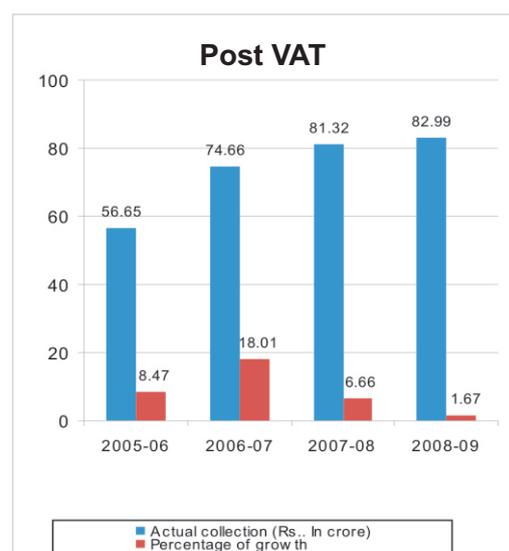
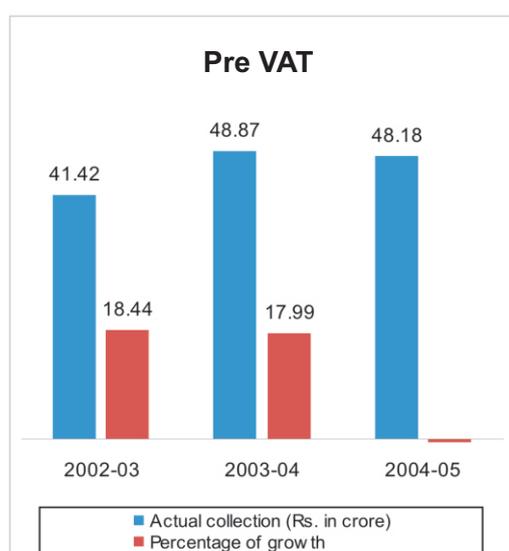
The comparative position of pre-VAT sales tax collection (2002-03 to 2004-05) and post-VAT (2005-06 to 2008-09) tax collection including VAT and the growth rate in each of the years is mentioned below.

---

<sup>4</sup>All 27 industrial dealers, all seven automobiles dealers, 16 works contractors and other 99 dealers based on probability proportionate relating to size.

Table – 4.12

Pre-VAT			Post VAT		
Year	Actual collection (Rs. in crore)	Percentage of growth	Year	Actual collection (Rs. in crore)	Percentage of growth
2002-03	41.42	18.44	2005-06	56.65	8.47
2003-04	48.87	17.99	2006-07	74.66	18.01
2004-05	48.18	(-) 0.69	2007-08	81.32	6.66
			2008-09	82.99	1.67
<b>Average</b>	<b>46.16</b>	<b>11.91</b>		<b>73.91</b>	<b>8.70</b>



It was seen that the collection of revenue which had become stagnant at the same level in 2003-04 and 2004-05, started growing post introduction of VAT. However, the growth rate which touched 18.01 *per cent* in 2006-07 has gradually come down to 1.67 *per cent* in 2008-09.

In the exit conference, the division stated that the above figures were also inclusive of CST and decrease in growth rate in the post VAT period was due to the reduction of CST rate in a phased manner from four *per cent* to two *per cent*.

#### 4.2.7 Preparedness and transitional process

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

As a follow up of White Paper on 'State-Level Value Added Tax' issued by the Empowered Committee of State Finance Ministers, the draft SVAT Act, 2005 was sent to the GOI through the Empowered Committee of the State Finance Ministers for vetting. Approval of the Sikkim Legislative Assembly was accorded to the Act on 9 March 2005. The State Government enacted Sikkim Value Added Tax Act, 2005 and also published Sikkim Value Added Rules, 2005 to implement VAT in the State.

The FRED also issued various notifications from time to time for effective implementation of VAT in the State. The division created awareness among the stake holders before implementation of VAT in the State through press releases in various news papers and awareness camps at various places apprising them about various benefits of implementation of VAT.

It was, however, noticed that though there was a provision detailing a time frame for bringing all dealers in the VAT net, submission of returns by all dealers within the stipulated period and scrutiny of returns and VAT audit, it could not be enforced properly. This would have further augmented the revenue generation on account of VAT. The various deficiencies in implementation have been pointed out in succeeding paragraphs.

#### **4.2.7.2 Computerisation of the Taxation Department/check gates and their interlinking**

Computerisation of VAT system was undertaken with the objectives of maintaining complete data of the registration of dealers/contractors, maintaining and processing of way bills and their issue/utilisation by the dealers, maintaining and processing of returns filed by the dealers, invoices declared and tax deducted at source, generation of defaulter list and blocking of defaulter through the system with interlinking the check gates.

Task of preparation of software for computerisation of the VAT system was given to the National Informatic Centre (NIC), Gangtok. Hardware were provided free of cost by the Government of India which had been installed at headquarter, circle offices as well as at check gates and are interlinked with each other.

Scrutiny indicated that out of five modules, the division was using only three modules (i) registration of dealers, (ii) way bills issue and endorsement at check post and (iii) returns and report. Another two vital areas *i.e.* (i) scrutiny and (ii) assessment modules had not been put to use till date (October 2009). Besides, the division had also not provided an audit trail. There was no disaster recovery plan in case of a major disaster like fire, earthquake, theft or continuous power failure etc.

Partial utilisation of computerisation and incomplete information in the system failed to facilitate the goal of fool proof system to avoid underassessment/ short assessment of the purchases/sales of the dealers.

#### **4.2.7.3 Creation of manuals and training of the staff**

The division has not created a manual on VAT so far but has prepared a Hand Book on Tax Deduction at Source for reference of drawing and disbursing officers. Officers of the division of various levels were imparted various trainings sponsored by the

Government of India and the State Government relating to implementation and other issues of VAT.

#### 4.2.7.4 Completion of assessments under the repealed Act

While switching over from Sales Tax to VAT on 1 April 2005, 1,533 assessments were due. The division neither fixed any time frame for completion of pending assessments of pre-VAT period nor declared any pending assessment as deemed assessment. Data on cases pending as on 1 April 2005, assessments done in subsequent years and the balance as on 31 March 2009 are mentioned below.

Table – 4.13

Year	No of cases pending for assessment under Sales Tax Act as on 1 April	No of cases assessed during the year	No of cases pending for assessment at the end of the year
2005-06	1,533	1,089	444
2006-07	435	113	322
2007-08	313	20	293
2008-09	284	72	212

Note: The variation between closing and opening figures of assessment was due to cancellation of registration certificates.

The division stated (October 2009) that due to insufficient man power and frequent transfer of the concerned officers, pending assessments could not be completed till date.

#### 4.2.7.5 Collection of arrears of taxes due under the repealed Act

The arrear of tax due under the repealed Act as on 1 April 2005 was Rs. 67.58 lakh. During the years 2005-06 to 2008-09, the division raised additional demand of Rs. 69.65 crore, of which arrears of Rs. 69.61 crore were recovered during these years. Thus, arrear of Rs. 71.29 lakh were due to be recovered as on 31 March 2009.

In reply, the division stated (October 2009) that they were preparing a comprehensive report on the outstanding dues for realisation of the full amount of tax and penalty with interest.

### System deficiencies

#### 4.2.8 Registration and database of dealers

##### 4.2.8.1 Creation of database of dealers and carrying forward of such database under the repealed Act

Though SVAT Act and Rules did not have any provision to prepare a database of dealers registered under the VAT Act, the division had computerised database of the

dealers registered under VAT. The division could not compare such database with the database of dealers registered in the existing Sales Tax Act as the existing database was kept in a manual register. **This constrained the division from detecting dealers who remained unregistered under the SVAT Act who were registered under the repealed Act. Besides, the division had also not prescribed any time frame/periodicity at which the database of dealers registered under the SVAT Act was required to be updated.**

The division stated (July 2009) that such comparison was not possible as the database of dealers registered under the existing Sales Tax Act was kept in a manual register.

#### 4.2.8.2 Registration of new dealers

Details of registered dealers under the SVAT Act for the last four years (2005-09) were as mentioned below:

**Table – 4.14**

Year	As on 1 April	Added	Cancelled	As on 31 March	percentage of increase over previous year
2005-06	Nil	1,811	Nil	1,811	-
2006-07	1,811	1,209	19	3,001	66
2007-08	3,001	865	101	3,765	25
2008-09	3,765	1,423	99	5,089	35

As would be seen, registration of dealers recorded an increase ranging between 25 and 66 *per cent* during 2005-06 and 2008-09.

#### 4.2.8.3 Periodic analysis of dealers below threshold limit and detection of unregistered dealers

**There was no provision in the SVAT Act and Rules for periodic verification of the dealers paying composite tax and for verification of the turnover of these dealers to pre-empt any scope of evasion of tax. The division had also not installed any mechanism/system of periodic scrutiny of books of accounts of dealers under the threshold limits. Besides, the SVAT Act and Rules did not have any provision for market survey/raids of the premises of the dealers to detect unregistered dealers.**

The division stated (September 2009) that periodic survey of market area was conducted to check the accounts of unregistered dealers to ensure that their sales turnover had not crossed the threshold limit and also to detect dealers of sales turnover above threshold limit operating without registration. However, audit scrutiny indicated that such survey was done only once during 2006 and further there was no documentary evidence to prove that division had taken any action on such survey report.

**The Government may prescribe a system of periodic review of the turnover of the dealers below threshold limit.**

#### ***4.2.8.4 Confirmation of the securities provided by the dealers***

Though Section 28 of SVAT Act prescribed for obtaining security deposit from the dealers during registration for securing proper and timely payment of tax, **the quantum of such security was neither prescribed in the Act/Rules nor notified by the division.**

Audit noticed that the security deposit was not realised from any of the 623 dealers covered in the audit sample. This was not only in contravention of the Act but also deprived the division from realising arrear of assessed tax of Rs. 11.76 lakh from eight dealers for the assessment years 2005-09 by forfeiting the securities.

It was also noticed that during 2005-06 to 2008-09, 2,313 out of 5,089 dealers did not submit their returns at all. Had the division insisted on obtaining security deposits from these dealers at the time of registration, it could have at least forfeited the security deposit in lieu of dues of these dealers.

Reply of the division (May 2009) that security deposit was not insisted upon to encourage registration during the initial years (2005-06 to 2008-09) is not tenable as the division did not analyse the credibility of the dealers, on a case-by-case basis before waiving their security deposit.

**The Government may prescribe the quantum of security deposit and its mandatory deposit by the dealers.**

#### ***4.2.8.5 Database of dubious/risky dealers***

**The SVAT Act and Rules did not have any provision for the preparation of database of dubious/risky dealers and upload it on the division's website/Tax Information Exchange System (TINXSYS).** This would have enabled the assessing officers to select dealers for tax audit based on risk analysis.

**The Government may consider preparation of a database of dubious/risky dealers in the interest of revenue.**

#### ***4.2.8.6 Periodic analysis of registration certificates to detect dormant registrations***

**There was no provision in the SVAT Act and Rules for periodic review of registration certificates to detect and cancel dormant TINs.**

The division stated (October 2009) that when a dealer obtains a TIN, it means that he had started a business or intended to start a business but a dormant TIN indicated that

the dealer was unable to start the business. There was no point in cancelling a dormant TIN as it did not cause loss of revenue.

Fact, however, remains that it could be seen from the paragraph 4.2.9.1 that 2,313 out of 5,089 dealers, i.e. almost 45 *per cent*, had never submitted returns. Besides, as there was no mechanism of conducting periodic survey as highlighted in paragraph 4.2.8.3, there was little scope for the division to monitor and cancel dormant registration(s). Further, instances of issuance of way bills and C forms to dealers who had never filed returns had also been noticed as discussed in paragraph 4.2.9.1.

**The Government may establish a system of reviewing the database of registered dealers at periodic intervals to detect dormant registrations for effective monitoring of the dealers in the State.**

### Deficiencies in the Act and the Rules

The review indicated a number of deficiencies in the provisions of the SVAT Act and the Rules which persisted during the period covered under the review. Some of the important deficiencies are discussed below.

## 4.2.9 Returns

### 4.2.9.1 Mechanism to monitor filing of returns

Section 30 (1) and 30 (2) read with 30 (8) of SVAT Act enjoins upon the registered dealers to furnish a true and complete return on quarterly basis to the prescribed authority in respect of all their transactions (sales, purchases, receipts and dispatches of goods), failing which penalty upto Rs. 500 per day of default would be imposed. **However, the division had not established any mechanism to monitor filing of returns by the dealers to guard against missing dealers or run-away dealers. The division also did not take any action on defaulters who did not submit returns as mentioned below.**

Audit noticed that during 2005-09 while 2,313 out of 5,089 registered dealers (45 *per cent*) had not submitted any returns, 65 dealers out of 623 checked submitted their quarterly returns belatedly – the delay ranged between 9 and 1,303 days. The division not only failed to persuade the dealers to file returns within the prescribed timeframe but also did not levy penalty. The maximum penalty leviable is Rs. 72.92 crore.

Scrutiny further revealed that in case of 50 out of 2,313 dealers, who had not submitted returns at all, the division continued to issue way bills and C forms to eight dealers to enable them to import goods from neighbouring States and run their businesses as usual.

The division stated (May 2009) that temporary suspension of registration number

was resorted to with a view to restrict the issue of statutory declaration forms to these dealers.

**The Government may ensure strict monitoring on submission of returns by the dealers and imposition of penalty in case of failure to submit returns or delay in doing so.**

#### **4.2.9.2 Scrutiny and verification of returns**

Section 37 of SVAT Act provides for scrutiny of returns by the prescribed authority to ascertain the correctness of computation of output tax, input tax, tax payable and application of tax rates besides evidence in support of payment of tax. **However, neither the SVAT Act and Rules nor the division had any provision prescribing cross verification of purchases to verify actual purchase and to reconcile the balance in the accounts of purchaser and seller. Besides, no record was prescribed for entering the details of returns received, returns scrutinised and balance thereof.** Due to these deficiencies, the division remained unaware about the overall position of receipt and scrutiny of returns.

Audit noticed that there was no scrutiny of returns by the assessing authorities to ascertain the correctness of the self-assessed returns submitted by the dealers. Failure to initiate scrutiny of returns was fraught with the risk of tax evasion by the dealers and consequent retention of Government dues. Audit scrutiny of 623 cases disclosed tax evasion of Rs. 2.15 crore by 19 dealers which have been discussed in some of the succeeding paragraphs.

The division stated (September 2009) that it has recently been decided to evolve a system by which concerned assessing authority shall endorse hard copy of the return to certify completion of scrutiny of the returns.

**The Government may prescribe a mechanism for monitoring the position of returns received, returns scrutinised by the division and results thereof.**

#### **4.2.9.3 Deficiencies in best judgment assessments**

Section 38 of SVAT Act envisaged that the assessing authority would assess the tax due from the dealer as per his best judgment in case no returns are furnished by the dealers within the prescribed date<sup>5</sup> or incorrect and incomplete returns are furnished by them.

**Scrutiny indicated that neither the SVAT Act/Rules nor any divisional order prescribed for maintaining information regarding non-receipt of returns, incorrect/incomplete returns etc. on which best judgment assessments were to**

---

<sup>5</sup> On or before the end of the month following the end of the quarter.

**be taken up.**

It was noticed that during the years 2005-06 to 2008-09, 'nil', 316, 153 and five assessments respectively were made under this Section on pick-and-choose basis from dealers who had submitted returns. But, none of the 1,119, 1,614, 1,706 and 3,258 dealers who did not submit the returns during the years from 2005-06 to 2008-09 respectively, were taken up for best judgment assessments to safeguard revenue interest. This not only resulted in delay in realisation of the non-assessed tax but also retention of Government dues with the erring dealers.

The division stated (September 2009) that it was provided under Section 42 that the assessment could be framed, if it was deemed necessary, within six years after expiry of the relevant period. The delay in framing assessment would not cause loss of revenue even in such cases where the self assessed tax paid by the dealer fell short of the actual tax assessed because the dealer could be charged with interest of two *per cent* per month on such due payment under Section 30 (10) of SVAT Act. Fact remains that accumulation of huge numbers of assessments year after year would put unnecessary burden on the divisional officers which would have dual impact of hampering day to day work and risk of cases becoming time barred.

**The Government may prescribe a mechanism for taking up all such cases for best judgment assessment without further delay.**

**4.2.10 Absence of system of cross verification of records of the selling dealers**

**The SVAT Act and Rules did not have any provision for cross verification of particulars of turnover disclosed by the dealers with those disclosed by other dealers from whom tax invoices were obtained. The division had also not installed any mechanism/system for cross verification of such transactions.**

**4.2.11 Provision for cross verification**

**4.2.11.1 Absence of provisions for cross verification of the records of other departments/source like, Central Excise & Income Tax Department, TINXSYS etc.**

**There was no provision in the SVAT Act and Rules and also no system installed by the division for cross verification of the records of other departments/sources like, Income Tax and Central Excise Departments, TINXSYS.**

A system of cross verification of sales turnovers returned under the SVAT Act with those in the Central Excise/Income Tax Departments and data of statutory forms available in the TINXSYS website would ensure veracity of the returns submitted by the dealers.

#### 4.2.11.2 Absence of provision for cross verification of the records of works/buying department in case of works contractors/suppliers

The SVAT Act and Rules did not have any provision for cross verification of the records of works/buying department in case of works contractors/suppliers. Besides, there was no provision for cross verification of records of sub/principal contractors while allowing exemption. The division had also not installed any mechanism/system for such cross verification. Also, no provision has been prescribed for submitting monthly report/return by the buying/works departments to the division. However, concerned suppliers/contractors had been obtaining TDS certificates from concerned buying/works departments and had been enclosing alongwith returns submitted by them. Cases of irregular allowance of exemption with cross verification of sub/principal contractors are pointed out in the succeeding paragraph.

#### 4.2.11.3 Non-payment/Evasion of tax in absence of cross checking

Section 13 and 17 of SVAT Act exempted a dealer from payment of tax if his sub-contractor has paid VAT on the turnover. Similarly, the sub-contractor would not be liable to pay tax if it has been paid by the dealer (his principal contractor) on the goods supplied to him by the dealer in the course of execution of the works contract.

Scrutiny of the records of three<sup>6</sup> out of 16 dealers test checked, registered as works contractors, indicated that the entire turnover of two dealers for the period 2005-06 to 2008-09 were exempted on the plea that they were working as sub-contractors for principal contractors. Audit, however, noticed that the principal contractor (M/s Mitsui & Co) declared 'nil' turnover for the year 2005-06 to 2008-09 towards execution of works contract and accordingly did not pay any tax and thus a tax liability of Rs. 54.83 lakh escaped assessment as mentioned below.

**Table – 4.15**

(Rupees in lakh)

Name of the dealer	Year of assessment	Turnover for the year	Amount of lump sum tax at 2 per cent
M/s Tanrub Engineers, Balutar, Singtam	2005-06	145.01	2.90
	2006-07	165.70	3.31
	2007-08	112.26	2.25
	2008-09	NIL	NIL
M/s PES Engineers (P) Ltd, Singtam	2005-06	258.17	5.16
	2006-07	323.80	6.48
	2007-08	191.35	3.83
	2008-09	1,544.77	30.90
	<b>Total</b>	<b>2,741.06</b>	<b>54.83</b>

<sup>6</sup>(i) M/s Tanrub Engineers, Singtam; (ii) M/s PES Engineers (P) Ltd, Singtam and (iii) M/s Mitsui & Company, Singtam.

Non-scrutiny of returns coupled with the absence of a system of cross verification of the records of the principal/sub-contractors resulted in tax evasion of Rs. 54.82 lakh by these contractors.

In reply, the division stated (September 2009) that response would be furnished after verification of the issue raised in audit. Further development has not been intimated (October 2009).

#### **4.2.11.4 Deficiencies in uploading data in TINXSYS**

Tax Information Exchange System (TINXSYS) is a centralised repository for exchange of information of all interstate dealers spread across the various States and Union territories of India. The TINXSYS is intended to help the Commercial Tax Departments of various States and Union Territories to effectively monitor the interstate trade.

TINXSYS can be used by any dealer to verify the counter party dealer in any other State. Apart from dealer verification, Commercial Tax Department officials can use TINXSYS for verification of central statutory forms issued by other State Commercial Tax Department and submitted to them by the dealers in support of claim for concessions.

While verifying the data relating to the State of Sikkim available on the website, it was seen that **no dealer details were uploaded on the website for the year 2005 to 2009**. Only the numbers of dealers available in the State for the years from 2007 to 2009 ranging from 219 to 824 were uploaded in the website. **Other details like issue and utilisation of various statutory forms, periodic returns, commodity master, district master, office master etc. were not uploaded for any of the years. Non-uploading of data on the site deprived other states from accessing the database of declaration forms issued to the dealers of Sikkim which defeated the objective of creation of the website.**

The division stated (August 2009) that transfer of the main data was in the progress after the State Government accorded consent (14 May 2009) and the delay was in obtaining clearance from NIC.

#### **4.2.12 Disposal of appeal cases**

##### **4.2.12.1 Deficiencies in the provision for settlement of appeal cases**

The SVAT Act and Rules had provisions for disposal of appeal cases within a period of five years which was too long as the period of disposal of an appeal case in the VAT Act and Rules of West Bengal Government was three months only.

**The Government may consider amending the time limit for disposal of appeal cases to ensure speedier recovery of arrear dues and settlement of cases.**

### 4.2.13 Deterrent measures

#### 4.2.13.1 Deficiencies in deterrent measures

The SVAT Act provided for imposition of penalty for failure to get registered, interest and penalty on non/delayed submission of returns, interest on non-payment or delayed payment of tax before assessment and interest on non-payment of assessed tax respectively. **However, the division had not set up a system to adhere to the above provisions resulting in a range of deficiencies which has been pointed out in the various paragraphs of the report.**

#### 4.2.13.2 Absence of minimum penalty for offences

Section 81 of the SVAT Act stipulates various penalties for different types of offences ranging from simple imprisonment to two years imprisonment and/or a fine not exceeding from a maximum of Rs. 100 to a maximum of Rs. 10,000. **However, the Act did not specify either the period of simple imprisonment and the minimum amount of fine for any particular offence except in case of concealment of turnover in which minimum penalty of one and half times of the tax had been prescribed under Section 72. Further, Section 83 of the SVAT Act provides a maximum fine of Rs. 50,000 for compounding of offence. However, the Act did not specify a minimum amount of fine for compounding of any particular offence.**

#### 4.2.13.3 VAT fraud task force

Prevention and early detection of offence cases was of paramount importance to tax enforcement. In order to ensure prevention and early detection of dubious dealers there should be a “VAT Fraud Task Force” to act as an intelligence-cum-investigating unit, detect and list all fraud cases; to deal with such cases; to analyse anti-fraud policies and measures in place; and offer its views and suggestion for improving them. **However, it was seen that the SVAT Act and Rules did not have any provision to constitute such a task force. The division had also not made any mechanism/system to act on above lines.**

**The Government may fix responsibility for strict compliance with the codal provisions, consider fixing of the quantum of minimum penalty for every kind of offence and constitute a VAT fraud task force.**

### 4.2.14 Internal controls

Internal control measures are instituted by an organisation to enable it to function efficiently and to get timely warnings of irregularities and deficiencies in its various activities.

#### **4.2.14.1 Maintenance of registers in unit offices**

The SVAT Act and Rules provided various types of accounts and the records which were required to be maintained/kept by the registered dealers. **But the SVAT Act and Rules did not have any provision for the maintenance of various types of the records by the division.**

Audit scrutiny indicated that various registers like Register of Dealers, Register of Security Deposit, Register of Registration and Cancellation of Registration Certificate, Register of Surrender of Unused Statutory Forms etc. were not maintained.

#### **4.2.14.2 Reports and returns**

**The SVAT Act and Rules did not have any provision for the preparation/submission of any report/return at any level.** Such absence of reports/returns is indicative of weak management information system which in turn hampers monitoring of day-to-day functioning of the systems and the officers/staff by the division.

**The Government may take appropriate measures for the preparation and submission of periodic reports/returns by the field offices and monitoring by the higher authorities.**

### **4.2.15 Internal audit**

#### **4.2.15.1 Existence of internal audit**

Internal audit is an independent entity within or outside the department to examine and evaluate the level of compliance with the departmental rules and procedures so as to provide independent assurance to the senior management on the adequacy of the risk management and internal control framework in the department. The Directorate of Internal Audit was established in 1990 under the overall control of FRED to examine and evaluate the activities of all the departments including FRED, Public Sector Undertakings of the State Government, Pay and Accounts Office and Drawing and Disbursing Officers.

Despite existence of internal audit, it was seen that the Directorate of internal audit did not carry out even a single inspection during 2004-05 to 2008-09. Due to this, the risk of errors and irregularities resulting in leakage of revenue is high negating the purpose for which the directorate was established.

## Compliances deficiencies

### 4.2.16 Tax audit

#### 4.2.16.1 Process of selection of dealers for VAT audit

As per Section 39 (2) of SVAT Act read with Rule 47 of SVAT Rules, the Commissioner may select by 30<sup>th</sup> day of July every year, not less than 20 *per cent* of the registered dealers for detailed audit for any period or year ended on or before the 31<sup>st</sup> day of March, such selection being made by draw of lots either mechanically or with the use of computers.

Audit scrutiny indicated that only 20 dealers were selected for VAT audit during 2006-07 manually from various categories such as manufacturers, wholesalers, contractors, hoteliers and retailers. Further, during 2007-08 and 2008-09 no dealer was selected for VAT audit.

#### 4.2.16.2 Timeframe for completion of tax audit

As per the provisions under Section 39 (3) of SVAT Act, the audit of the returns and statements of a dealer selected under sub-section (2) shall be conducted in the manner prescribed, within a period of 24 months from the due date within the meaning of sub-section (3) of Section 30.

However, audit noticed that no VAT audit was carried out by the division even of the 20 dealers selected by the Commissioner for VAT audit during 2006-07 till date of review. Further, during 2007-08 and 2008-09 no dealer was selected for VAT audit.

The division stated (September 2009) that due to stagnation in the development of VAT software; the audit cell had not been able to conduct the audit.

### 4.2.17 Concealment of purchase and sales turnover leading to evasion of tax

Section 72 of SVAT Act provides for levy of penalty between one and half and thrice the amount of tax in case of concealment of turnover by dealers with the intent of reducing the tax liability.

Audit of the assessment records and self assessed returns of three<sup>7</sup> registered dealers indicated that the dealers had reduced their turnover and that the figures were not tallying with their declared turnover. This was not detected due to non-scrutiny of the returns leading to concealment of turnover of Rs. 2.69 crore and consequent evasion of tax of Rs. 31.94 lakh. Penalty of Rs. 47.90 lakh as applicable in such cases calculated at the minimum rate of one and half times the tax were also not levied on these dealers for concealment.

<sup>7</sup>(i) M/s Tiwari Enterprises, (ii) M/s Tripti (P) Ltd and (iii) M/s Tirumala Enterprises.

Thus, concealment of purchase and sales turnover by the dealers resulted in evasion of tax of Rs. 79.84 lakh including penalty.

#### **4.2.18 Non-payment of VAT and penalty**

Sikkim Industrial Promotion and Incentive Act, 2003 exempted all industries established in the State from the payment of State Sales Tax for ten years. Consequent upon implementation (April 2005) of VAT in the State and there being no provision for exemption under SVAT Act, Department notified (May 2007), with immediate effect, under the provisions of Section 30A of SVAT Act for deferring of VAT payment for a period of ten years.

Audit scrutiny indicated that one industry<sup>8</sup> out of 27 industrial dealers checked transacted intrastate sales turnover of Rs. 3.77 crore and realised VAT of Rs. 47.11 lakh from the other dealers during the period April 2006 to April 2007 (before the notification of deferred payment scheme) but did not deposit the VAT in the Government account. Instead, he intimated (May 2006) the division about the realisation of VAT and enquired whether the amount should be deposited into the Government account. The division did not clarify this matter to the dealer despite the fact that the industry was neither exempted for payment of VAT nor was granted deferred payment. The division also failed to initiate any action for recovery of the realised tax of Rs. 47.11 lakh.

#### **4.2.19 Incorrect determination of the sale rate of items and consequent short payment of tax**

As per the established business practice, expenditure on account of transportation, storage, handling, establishment, taxes etc. on the cost price should be added on each item while selling it subsequently to the dealers/customers.

The dealers registered under the SVAT Act had regularly been obtaining C forms and import way bill forms from the division for import of various material from outside the State for resale in the State. Scrutiny of the records of twelve out of 623 dealers indicated that the actual cost price of purchases was shown as annual sales turnover without adding the basic elements<sup>9</sup> to the cost price. This had resulted in concealment of turnover of Rs. 2.29 crore and evasion of tax liability of Rs. 24.17 lakh.

In reply, the division stated (September 2009) that action would be taken in such cases where value additions were declared unreasonably low.

---

<sup>8</sup> Ms C.G. Foods India Pvt. Ltd., Rangpo.

<sup>9</sup> Calculated by adding 20 per cent i.e. five per cent transportation and supervision, five per cent storage and handling, three per cent income tax, two per cent losses on stock, two per cent interest on capital and three per cent establishment cost incurred in the business.

#### 4.2.20 Non-levy of penalty for non-remittance of tax deducted

Section 17 (4) of SVAT Act provides for the levy of penalty upto twice the amount deductible for failure to deduct the tax due or non-remittance of tax deducted within the stipulated time of 15 days.

Audit scrutiny indicated that one dealer (M/s Cipla Ltd.) had remitted the tax deducted from three dealers belatedly- the delay ranging between 30 to 94 days and was thus, liable for penalty of Rs. 9.60 lakh, which was not levied.

While accepting the fact, the division stated (October 2009) that the dealer had been issued show cause notice. Further development has not been reported (October 2009).

#### Other deficiencies

#### 4.2.21 Deficiencies in registration forms

Rules 5 to 7 of SVAT Rules require every dealer to make application in Form 1 for registration under Section 26 or 27 of SVAT Act to the appropriate registering authority duly accompanying declaration in Form 1A and 1B.

Audit scrutiny of 125 out of 623 dealers indicated a number of deficiencies such as (i) application forms for registrations were not available in case of 23 dealers (18 *per cent*), (ii) address of the 2<sup>nd</sup> contact person(s) was not filled in 55 cases (44 *per cent*), (iii) details of bank account not mentioned in 34 cases (27 *per cent*), (iv) details of loan account not filled in case of 57 dealers (46 *per cent*), (v) date of commencement of purchase and sale not filled in case of 106 dealers (85 *per cent*), (vi) telephone/contact numbers not filled in case of 28 dealers (22 *per cent*), (vii) seal of the dealers were not affixed in 76 cases (61 *per cent*), (viii) personal immovable assets were not filled in 77 cases (62 *per cent*), (ix) declaration stating name of the manager/officer in charge of the business were not filled in 80 cases (64 *per cent*), (x) acceptance of nomination not filled in 86 cases (69 *per cent*), etc.

The division accepted the audit observation (September 2009) and ensured that such oversight would be rectified and would not be repeated in future.

#### 4.2.22 Delay in crediting of revenue into Government account

According to Rule 50 (1) of Sikkim Financial Rules, head of the department/ office shall be responsible to ensure that all revenue, receipts or other sums due to Government are regularly and promptly assessed, realised and credited to the Government account under the relevant head of account.

Audit scrutiny indicated that the division had been receiving cheques from dealers dealing with automobiles trade and from works contractors/ wholesalers on quarterly

basis towards collection of VAT by them from various customers. However, test check of receipts of three major automobiles dealers<sup>10</sup> and six work contractors/wholesalers<sup>11</sup> for last four years, indicated that such cheques towards VAT receipts were credited into Government account with delays ranging between 11 and 175 days by the division which was indicative of lack of monitoring timely depositing of revenue into Government account.

While accepting the observation, the division stated (September 2009) that since April 2009, the division has devised prototype system of crediting revenue promptly into Government account.

#### **4.2.23 Claim for compensation of loss due to introduction of VAT**

Consequent upon the implementation of VAT in Sikkim with effect from April 2005, the Government of India agreed to compensate the State Government for the loss of revenue consequent to the implementation of VAT and issued guidelines in June 2005 on the modalities for calculation of compensation claims.

Accordingly, the Government of Sikkim claimed reimbursement of Rs. 8.07 crore (2005-06), Rs. 1.73 crore (2006-07) and Rs. 7.73 crore (2007-08). Against these, the Government of India released Rs. 5.87<sup>12</sup> crore for the year 2005-06 to the Government of Sikkim.

However, from the scrutiny of the records and information available with the division, it was seen that the reimbursement of Rs. 1.89 crore (2005-06), Rs. 'nil' (2006-07) and Rs. 3.73 crore (2007-08) only were admissible to the State Government. Thus, the State Government was entitled to the reimbursement of Rs. 5.62 crore only on account of loss due to implementation of VAT for the period from 2005-06 to 2007-08 instead of Rs. 17.53 crore claimed by the State. The difference was due to inclusion of cess while calculating average growth rate for the preceding block years. Out of which, the Government of India released Rs. 5.87 crore for 2005-06.

The division stated (August 2009) that average annual growth rate calculation was based on the bifurcation made by their office based on the records of tax paid by the dealers dealing in non-VAT items and requested to provide the base of their bifurcation made by Audit. Though the details of calculation made by the audit were forwarded to the division in August 2009, their further reply has not been received (October 2009).

<sup>10</sup> M/s Entel Motors, M/s Sikkim Motors and M/s Bajla Motors.

<sup>11</sup> M/s Garison Engineers, M/s Krishna & company, M/s NBCC, M/s Top in Town, NHPC and CRH.

<sup>12</sup> December 2005 Rs. 1.84 crore and June 2006 Rs. 4.03 crore.

#### 4.2.24 Conclusion

While after implementation of VAT, the registration of dealers recorded a growth of 25 to 66 *per cent* during the years from 2005-06 to 2008-09, the division failed to prescribe the quantum of security deposit to be realised from the dealers and consequently it could not be realised. The division also failed to carry out assessment of returns, levy penalty for delayed submission of returns, etc. leading to evasion of tax. The computerisation of VAT system was only partially utilised and internal control was not robust enough to check the leakages in revenue. Immediate attention of the division was necessary towards registration of all the dealers under VAT, timely submission of returns by the dealers, scrutiny and assessment of the returns and initiation of VAT audit of selective dealers. There were many loop holes/deficiencies in the SVAT Act and Rules in making provisions for market survey/raids of the premises of the dealers, database of dubious/risky dealers, periodic review of registration certificates, cross verification of transaction, VAT Fraud Task Force, uploading data in TINXSYS, deterrent measures etc. The internal controls within the division were weak as evidenced by absence of provisions for maintenance of records/registers in the division and submission of reports/returns at any levels. Also, despite existence of an internal audit wing, the division failed to utilise its services.

#### 4.2.25 Summary of recommendations

The Government may consider implementation of the following recommendations for rectifying the system and compliance issues:

- implement computerisation of VAT system completely and effectively in all areas;
- establish effective mechanism to review database at periodic interval and to prepare database of dubious/risky dealers;
- establish effective mechanism to ensure submission of regular and timely returns by all the dealers;
- establish effective mechanism for scrutiny of every returns submitted by the dealers, assessment of the dealers and VAT audit of selective dealers;
- fix responsibility at various levels in the Department for strict compliance of codal provisions to avoid tax evasion by any dealer;
- ensure fixing the quantum of minimum penalty for each and every kind of offences and to constitute VAT Fraud Task Force;
- strengthen internal control mechanism including internal audit; and
- review and rectify various loop holes/deficiencies of SVAT Act and Rules.

## FINANCE, REVENUE & EXPENDITURE DEPARTMENT (INCOME TAX AND COMMERCIAL TAX DIVISION)

### 4.3 Non-realisation of revenue

#### **Non-assessment of tax resulted in non-realisation of revenue amounting to Rs. 2.70 crore.**

With a view to promote speedy industrial development, the Government introduced a scheme for exemption from payment of the State income tax to the new industrial establishments in Sikkim from 16 February 1974.

According to the Sikkim Income Tax Manual 1948, income tax on the gross sale proceeds at the prescribed rate is required to be charged from all persons engaged in business. Rule 4 (II) of the Manual prescribes that 'every person doing business is expected to keep proper accounts and produce them on demand before the Income Tax Officer, who in case of default or unsatisfactory account will assess the tax according to his discretion'.

**4.3.1** Test check of the records (November 2008) of the office of the Special Secretary, Income Tax and Commercial Tax Division, Gangtok indicated that M/s Mount Distilleries (P) Limited, Mazitar, Rangpo availed of exemption from paying the State income tax for a period of five years from the date of their commercial production i.e., 11 March 1999 to 10 March 2004. After completion of the exemption period, the distillery did not file any return to the Income Tax Department for the accounting years 2004-05 to 2006-07. The Department also did not assess the tax on the basis of best judgment as per the provisions of Sikkim Income Tax Manual 1948. Verification of the records of the distillery in the commercial tax division indicated gross sale proceeds of Rs. 50.30 crore<sup>13</sup> for the above period on which Rs. 1.51 crore income tax was due.

After this was pointed out, the division stated (October 2009) that the company had been assessed and demand notice had been issued (October 2009). However, the assessee was claiming exemption for the assessment period. The case had been forwarded to the Commerce and Industries Department for their comments regarding the exemption of income tax. Reply of the division is not in consonance with the exemption scheme which allowed exemption to the firm for a period of five years from the date of commercial production, which had already expired in March 2004.

**4.3.2** Test check of the records (November 2008) of the office of the Special Secretary, Income Tax and Commercial Tax Divisions, Gangtok indicated that in

<sup>13</sup>Figures for 11-03-2004 to 31-03-2004 were not available in the records.

respect of three dealers, income tax for the respective periods falling between April 2001 and March 2007 was not assessed. Cross verification with the assessment records of these dealers maintained by the commercial tax division disclosed their gross sales turnover as Rs. 39.89 crore for the above period on which the income tax due worked out to Rs. 1.19 crore. Failure of the division either to obtain the books of accounts from the dealers or to ascertain the turnover from the records maintained by the commercial tax division and to demand the tax after assessment resulted in non-assessment of tax amounting to Rs. 1.19 crore.

After the case was pointed out, the income tax division stated (September 2009) that STP Pharmaceutical (Pvt.) Limited was served notices (November 2008 and June 2009) for submission of the accounts for the period upto 2006-07, failing which *ex-parte* decision would be initiated against the company. M/s Sarda Boiron Sikkim (Pvt.) Limited had contested the legality of the demand notice issued (February 2009) for the years upto 2004-05 by the department under the Sikkim Income Tax Manual 1948 in the event of Indian Income Tax having been imposed in Sikkim since 16 June 2008. The issue was pending with the higher authorities for a decision. M/s Denzong Laboratories (Pvt.) Limited had been assessed for the years upto 2005-06 and demand notice issued in September 2009 and the assessment procedure for the year 2006-07 was in progress.

While the final reply is awaited (October 2009), the inordinate delay in assessment/issue of demand notice since 2001 has resulted in delay in realisation of the Government revenue with consequential undue benefit to the assesseees. Further, the plea of non-submission of accounts by the assesseees is not tenable as the information were already available with the commercial tax division which could have been obtained for completion of the assessments.

#### 4.4 Non-realisation of revenue

**The Department failed to realise the sales tax and State income tax aggregating Rs. 2.25 crore including interest and penal interest.**

##### 4.4.1 Non-realisation of sales tax

According to section 14 (3) of Sikkim Sales Tax Act 1983, if a dealer fails, without reasonable cause, to make the payment of tax together with the penalty, if any, by the date specified in the notice or by the date extended, interest at 10 *per cent* per annum would be charged on such amount from such dates.

Test check (October-November 2008) of the assessment records of the commercial tax/Sales Tax/Value Added Tax (CT/ST/VAT) division indicated that the sales tax<sup>14</sup>

<sup>14</sup> Tax due Rs. 10,000 and above cases.

amounting to Rs. 1.69 crore assessed upto 2006-07 for the assessment years 1982-83 to 2004-05 has not been paid by 52 dealers within the due dates. It was further noticed that out of 52 dealers, 17 paid the tax amounting to Rs. 7.73 lakh after the due dates on which interest of Rs. 1.09 lakh has not been levied and realised by the Department. The remaining 35 dealers have not paid assessed tax of Rs. 1.61 crore alongwith interest of Rs. 1.06 crore for the delays ranging from 190 to 3,215 days till 31 March 2009.

#### 4.4.2 Non-realisation of State income tax

As per notification issued by the Income Tax Department in December 1973, any amount specified as payable in the notice of demand shall be paid within 45 days from the date of issue of the notice failing which simple interest at 12 *per cent* per annum shall be charged from the date of notice of the demand. The notification further provides that if the payment is not made even after three months of its demand, the assessee shall, in addition to the simple interest, be liable to pay penal interest at the rate of 20 *per cent* on the defaulted amount.

Scrutiny of the records (November 2008) of the State Income Tax (SIT) Division at Gangtok indicated that in the case of three assesseees<sup>15</sup> who defaulted in payment of the tax amounting to Rs. 25.31 lakh for the period 2001-02 to 2004-05, the division neither initiated any recovery proceedings against the defaulting dealers nor levied the mandatory simple interest and penal interest amounting to Rs. 24.12 lakh. This resulted in non-realisation of tax alongwith interest and penal interest aggregating to Rs. 49.43 lakh over a period of 105 to 1,160 days, as of March 2009.

Thus, laxity of the divisions in enforcing the statutory provision resulted in non-realisation of tax aggregating to Rs. 1.94 crore relating to the periods

1982-83 to 2004-05 and penalty thereon aggregating to Rs. 1.30 crore with consequential deferment of payment of tax.

After this was pointed out, the SIT Division stated (September 2009) that notices have been served on the dealers for paying the interest and penal interest. It was also stated that notices have been served to the defaulters and in the event of the failure of the assesseees to make payments, recovery proceedings would be initiated.

#### 4.5 Short realisation of Central Sales Tax

**Central Sales Tax on a turnover of Rs. 61.83 crore was not assessed resulting in short realisation of tax of Rs. 1.02 crore including interest.**

According to the Rule 11 of Central Sales Tax (Sikkim) Rules 1983, every registered

<sup>15</sup> (i) M/s Rajib Electronics for the period 2001-05, (ii) M/s Ramkumar Kedarnath for the period 2001-04, (iii) STP Pharmaceuticals (Pvt.) Ltd. for the period March 2004 & 2004-05.

dealer is required to furnish a quarterly return within fifteen days from the expiry of each quarter together with proof of the payment of tax and tax due. Further, as per the provision 9(2B) of Central Sales Tax (CST) Act, if the dealer fails to pay the tax in time, he is liable to pay the interest according to the sales tax law of the State. As per the Sikkim Value Added Tax Act 2005, simple interest at the rate of *per cent* for each calendar month of the default was leviable towards interest for delay.

Scrutiny of the records of commercial tax division in October-November 2008 indicated that one assessee<sup>16</sup> was exempted from paying the tax from 1st March 1999 for a period of five years under the industrial policy of Sikkim 1996. As per the exemption order of the Government issued in May 2001, he was liable to pay tax from 1<sup>st</sup> March 2004. It was noticed that though the turnover of Rs. 61.83 crore for the period from March 2004 to March 2007 was assessable under the CST Act, no assessment was made till November 2008. However, against the tax dues of Rs. 2.47 crore on the above turnover, the assessee remitted Rs. 1.67 crore between December 2004 and December 2007. This resulted in non-realisation of tax of Rs. 80 lakh on which interest of Rs. 21.75 lakh was also leviable. Besides, the non-realisation also led to undue financial benefit to that extent to the company.

After this was pointed out, the division stated (September 2009) that the assessment for the period from March 2004 to March 2007 could not be done as the representations (June 2006, February 2007 and March 2008) of the company for exemption of tax beyond five years under the industrial policy of Sikkim 1996 was pending with the Department of Commerce and Industries. Also, the requisite notification under section 8(5) of CST Act 1956 and section 5(2) of SST Act 1983 for exemption has not yet been issued. Notwithstanding the representations for exemption beyond five years remaining pending over more than three years, according to the existing Government order of May 2001, the company was liable for payment of CST from March 2004 onwards.

---

<sup>16</sup> STP Pharmaceuticals Pvt. Ltd.