

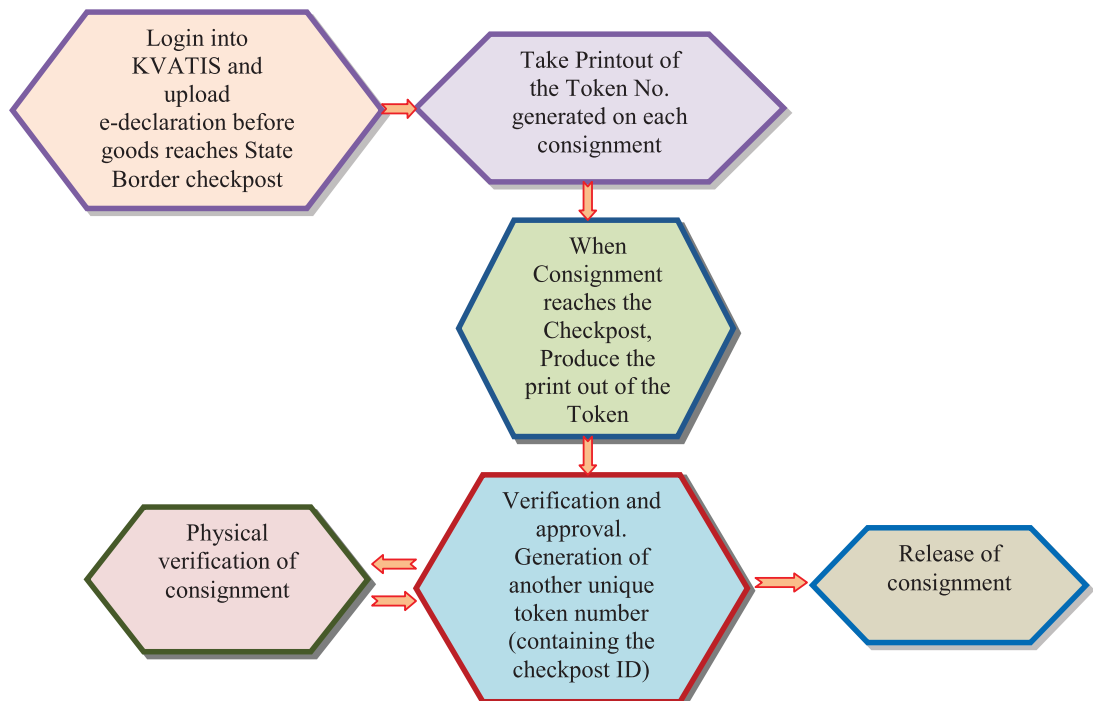
CHAPTER-III : CHECKPOST MANAGEMENT SYSTEM

3.1 Introduction

The Commercial Taxes Department has established checkposts along the borders of the State for monitoring the movement of goods into and outside the State. These are managed by Inspecting Assistant Commissioner/ Commercial Tax Officer/Commercial Tax Inspectors. The Checkpost Management System (CPMS) module in the KVATIS captures the details of goods purchased/sold and stock transferred into and outside the State by registered dealers, etc.

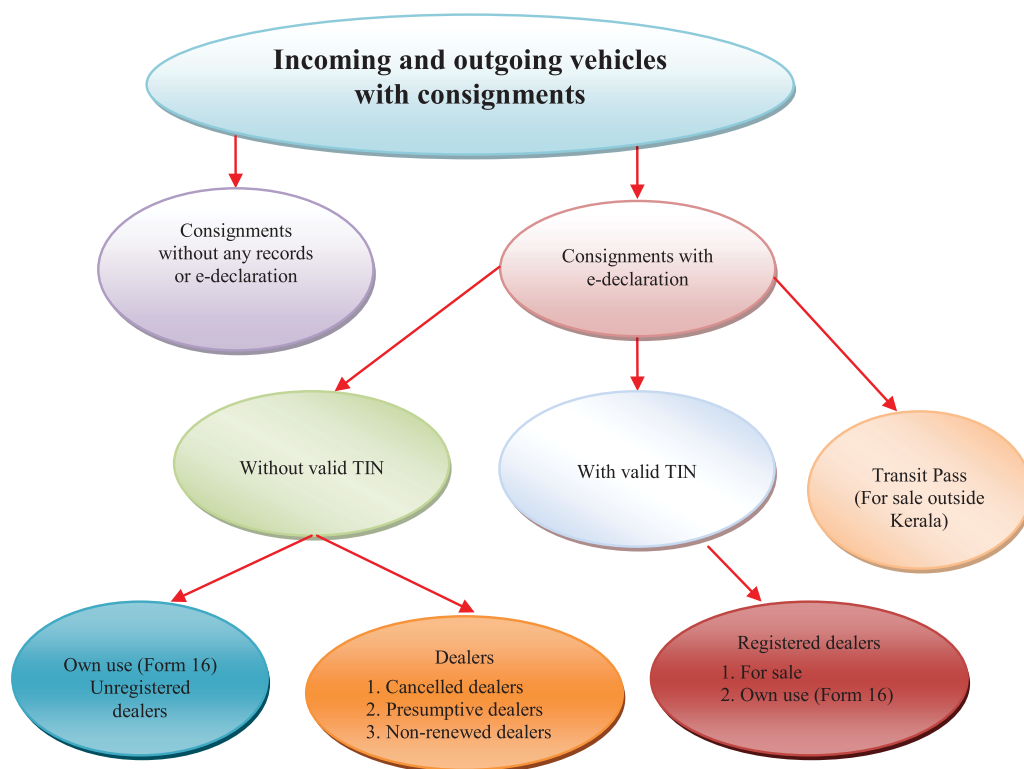
3.2 Process automation

There are 76 checkposts in the State, out of which only 36 are provided with online Wide Area Network (WAN) connectivity. The data regarding transactions through offline checkposts are uploaded to KVATIS from the nearest online office in the same week. Since 2010, the Department introduced a new system - 'e-declaration of consignments' (in Form No.8F), on interstate transfer of goods. This provides system information to the Department about the consignments arriving at the checkposts, enabling speedy clearance. The following diagram depicts the process of e-declaration.



The most important control in e-declaration is the 'second token system'; which identifies the person who transports the goods; the commodity transported in the vehicle and the checkpost. It helps the assessing officers spread all over the state to identify the dealer wise details of interstate transfers in VAT assessment.

The flow chart of the checkpost transactions are given below:



The year-wise details of token generated for inward and outward vehicles are as shown below:

Year	No. of tokens Generated (IN)	No. of tokens Generated (OUT)
2008-09	6, 07,979	1,85,862
2009-10	6,65,081	1,98,763
2010-11	7,07,916	4,49,401
2011-12	9,99,025	5,76,237
2012-13	18,33,802	7,56,351

3.3 Non-mapping of business rules for Token generation

As per Section 8 of CST Act, a registered dealer can purchase taxable goods from outside the State at concessional rate and transport it into the State for trading. If the dealer's principal place of business is outside the State or if he is acting as an agent of a principal dealer outside the State, then that dealer can also transfer the goods into the State for trading (Section 6A of CST Act).

Under Section 47(2) of the KVAT Act, if the goods under transport are not covered by proper and genuine documents or that any person transporting the goods is attempting to evade payment of tax, the same shall be allowed to be transported only on furnishing of security deposit at double the amount of tax likely to be evaded as estimated by the Officer.

As per Section 16(7), a certificate of TIN registration issued shall be valid for a year and shall be renewed from year to year on payment of the fee. If a

dealer fails to renew his registration in any year, he should be considered as an unregistered dealer and shall not be eligible for the concessional rate of tax for interstate transactions and transport of goods through checkpost without remitting security.

The KVATIS system is expected to map the above business rules. It should have an inbuilt control mechanism to give an alert to the authorities, on a non-renewed/cancelled dealer trying to generate a token for interstate transportation of goods. It should also generate a demand notice for collection of security deposit from the errant dealers.

The system deficiencies noticed in the CPMS module are discussed in the succeeding paragraphs.

3.3.1 Interstate transactions of dealers whose registrations were not renewed

Due to the absence of proper system for detection of transaction using non-renewed TIN; goods worth ₹ 2,029.57 crore were transported into the State by 3,979 dealers during 2010-11 to 2012-13, without collecting security deposit.

Audit analysed the risk in allowing non-renewed dealers effecting interstate transactions by cross verifying their transactions with the returns filed and cases of non-reporting of interstate purchases were noticed during analysis. Two illustrative cases are shown below:

TIN	Year to which the registration was not renewed	Token Number	Value of goods transported (₹)	Interstate purchase declared in returns
32070235994	2010-11	320310/2010-11/ 7629	12,12,695	Nil
32010805314	2012-13	320117/2012-13/ 4474	57,12,000	Nil

On this being pointed out, Government stated (April 2014) that assessing authorities are provided with Management Information System (MIS) reports to identify the defaulters in filing returns having checkpost transactions. Additional demands can be created by them using this data. Short-levy worked out by audit requires verification of individual cases and hence not sustainable.

The reply is not acceptable as audit found that self-assessments in respect of 59 assessment files¹ relating to 55 dealers who failed to renew their registration were not reopened though they failed to report their interstate transactions. Short levy of tax in this regard works out to ₹ 4.37 crore. Out of these, audit cross verified (May 2014) 16 cases with the live data available in KVATIS and found that in all the cases the dealers failed to file the return and pay tax on the sales turnover of goods purchased interstate. The resultant short-levy of tax in the 16 cases worked out to ₹ 1.67 crore. This shows that assessing authorities are not taking proper action based on MIS reports. Hence, the system should be modified to detect and generate notices on the

¹ Where tax effect is greater than rupees one lakh

interstate transactions effected by the dealers who have not renewed their registration.

Further, dealers who have not renewed their registration were effecting interstate transport of goods leading to evasion of tax. However, security deposit as stipulated in the Act had not been collected in the checkpost. Non-collection of security deposit from these 55 non-renewed dealers is worked out to ₹ 7.89 crore.

3.3.2 Interstate transactions of dealers whose registrations were cancelled

Absence of proper system for detection of transaction using cancelled TIN resulted in irregular release of 1,605 consignments of 184 dealers without collecting security deposit. Audit analysed the risk in allowing cancelled dealers effecting interstate transactions by cross verifying data on interstate transactions with information as per returns filed. Instances were noticed where dealers failed to report their interstate purchases. Two illustrative cases are shown below:

Sl. No	TIN	Name of the dealer	Date of cancellation	Reason for cancellation	Token Number	Date of transportation of goods	Value of goods (₹)
1	32070292143	JT.INTERNATIONAL (WHOLESALE) INDIA PVT LTD.	28.03.2011	Business stopped	320921/2011-12/65718	05.09.2011	3,41,198
2	32071739062	BIOTECH SCIENTIFIC	25.03.2010	Business stopped	320921/2012-13/303007	29.08.2012	1,32,487

On the risk being pointed out, Government stated (April 2014) that in cases of *suo motu* cancellation of registration by assessing authorities, the cancellation could be revoked later by appellate/revisional authorities on application by the dealers concerned, the process of filing appeal/revision and disposal of which were purely manual. Further, it was stated that in cases of transaction by cancelled dealers, checkpost authorities and data mining wing were given facility to view the checkpost transactions of cancelled dealers so that the authorities can initiate statutory measures.

The controls pointed out in the reply is not adequate since audit found that in spite of these precautions, there were 153 dealers (178 assessment files) who effected interstate transactions, even after cancellation of registrations. Even if the registration was restored by appellate authorities, the dealers had the liability to report and pay tax on their interstate transactions. On analysis audit found that no returns were filed by these assesseees. Short-levy of tax including interest would work out to ₹ 0.45 crore.

Since cancelled dealers were transporting goods interstate and evading payment of tax, in order to protect the revenue, the department should collect the security deposit at the checkpost for interstate transactions effected by dealers whose registrations were cancelled treating it as a transaction made by an unregistered dealer. Non-collection of security deposit from 153 cancelled

dealers, whose tax liability of goods transported into the state is above rupees one lakh, worked out to ₹ 0.69 crore.

Audit rechecked (May 2014) 22 cases (12.23 *per cent*) with reference to the live data in KVATIS at the assessing offices and found that dealers did not file any return and thus sales turnover of goods purchased interstate was not assessed to tax. Thus, the controls stated by the Department were not effective.

3.4 Lack of processing/validation control against master files

3.4.1 System allows transport of consignments into the state by dealers without a valid TIN

TIN is used to track all the transactions of a registered dealer. TIN, the identification number allotted to a registered dealer is an eleven digit number, which is unique all over India. The first two digits identify the State. Thus, '32' is allotted to Kerala dealers.

The system should have the input controls to ensure that the data entered are valid, complete, accurate and properly authorised. Lack of input control by the system results in goods being transported, purchased/ stock transferred, into the State without declaring their TIN or declaring a defective TIN² at the Checkpost as detailed below:

Year	No. of entries made into the State without declaring a valid TIN	Value of goods transported (₹ in crore)
2010-11	14,328	496.70
2011-12	3,15,236	2,577.04
2012-13	5,17,118	3,332.59

Inability of the system to process/validate the data without a valid TIN resulted in non-payment of tax and interest of ₹ 171.51 crore³ on 2095 assessment files.

To curtail the evasion of tax, the system should alert and generate a demand for security deposit to be collected at the checkpost from the dealers who fail to declare their valid TIN. Non collection of security deposit on the above files worked out to ₹ 308.57 crore.

Government stated (April 2014) that in case the documents are defective, the checkpost officials detain the vehicle and demand security deposit. Since this is a manual process the short collection of revenue can be ascertained only after verifying the Offence Register (OR) maintained at checkpost. During the Exit Conference (April 2014) the Secretary, Taxes Department assured that necessary business rules will be built into the system to block the consignments brought into the state not for own use by unregistered dealers.

The effectiveness of manual controls pointed out in the reply is not adequate since audit analysed the details of consignments on which release order was

² TIN without mandatory eleven digits.

³ Dealers excluding Government departments and PSUs and those dealers having tax liability of more than rupees one lakh for the interstate transaction effected without a valid TIN.

issued without compounding⁴ any offence. Audit visited two major checkposts, CTCP Walayar and CTCP Amaravila that covered 69.70 per cent of the cases. It was found that the security deposit were collected for other offences like overload, difference in commodity transported etc and Token number which is the unique recognition number for transport of goods were not mentioned in the OR maintained. Moreover, the department admitted that the total security deposit collected for all the offences in the State for the above three years were ₹ 109.52 crore only whereas the security deposit to be collected for above said cases alone comes to ₹ 308.57 crore. Lack of proper controls in the system enabled transport of goods into the state without furnishing valid TIN.

3.4.2 System allows irregular claim of concession for Inter State sales effected to unregistered dealers

Section 3 of CST Act provides that a sale or purchase of goods shall be deemed to take place in the course of interstate trade if the sale or purchase occasions the movement of goods from one state to other or is effected by a transfer of documents of title to the goods during their movement from one state to another. Section 8(1) of the Act provides that, if the sale is to a registered dealer outside the state, a dealer can claim concessional rate of tax for that sale provided the dealer should produce valid C Form issued by that registered dealer. If movement of goods from one State to another occasioned as a result of an anterior contract of sale, then it is an interstate sale. There must be an inextricable link between movement of goods and prior order. As such, a dealer effecting interstate sale to a registered dealer outside the State would be aware of the details of the dealer.

Audit found that 977 dealers effected interstate sale to dealers having invalid TIN. This means that the dealers were not aware of the registration details of the purchasing dealers even at the time of transport of goods outside the State. As there was no inextricable link between movement of goods and prior order by a registered dealer outside the State in the aforesaid case, tax shall be levied at full rate for such interstate sale. Audit noted that self-assessments were not reopened in respect of 1,276 assessment files of the above 977 dealers, that tax to the tune of ₹ 192.57 crore was paid short by availing inadmissible concession. Penalty under Section 67 also should be imposed. Maximum penalty to be imposed would come to ₹ 316.52 crore. Two illustrative cases are shown below:

Token Number	Year	Consignor TIN	Consignee TIN	Value of goods transported Out of State (₹)
320921/2011-12/516576	2011-12	32071694602	Nil	2,05,221
320921/2011-12/161434	2011-12	32150304235	Nil	1,30,949

⁴ ‘Compounding of offence’: Section 74 of KVAT Act allows registered dealers to legalise their irregular transactions, paying an additional amount equal to the tax evaded as penalty. This process is termed as ‘compounding of offence’.

Lack of necessary input controls in the system, for detecting interstate sale to a consignee without TIN or to an unregistered dealer, enabled dealers to claim concessional rate for their interstate sale which was not due to them.

On this being pointed out, Government stated (April 2014) that at the time of assessment the assessing officer will allow the concessional rate only on production of statutory forms. Hence without verifying the details of assessment records the actual short levy could not be ascertained.

Audit verified (May 2014) 35 cases with the returns filed along with the checkpost transactions and found that in all the cases dealers effected interstate sale to unregistered dealers and availed concession for that sale resulting in short-levy of tax of ₹ 5.10 crore. Thus, the justification of the Department about manual controls is not acceptable.

3.5 Inadequate process control - Lack of integration between modules

3.5.1 Interstate purchase/stock transfer of goods short/non-reported

If a dealer purchases or stock transfers goods from outside the State and transports it into the State by declaring it at any of the checkposts, he should disclose that transaction through his periodical return and tax shall be paid on the sale of such goods within the State. He should also account it in his P&L Account and submit the copy of the certified Annual Accounts to the assessing authority.

Lack of application controls enabling cross-linkage of the checkpost transactions with information submitted in the returns allowed dealers to short report/short account interstate purchase/stock transfer in their returns filed.

Two illustrative cases noticed are shown below:

(₹ in lakh)

TIN	Year	Total value of goods transported (IN) to the State	Total Interstate transaction (IN) returned/ accounted	Short reporting of Interstate transaction (IN)
32070381682	2012	53,013.59	6,089.36	46,924.22
32151597344	2011	2,519.17	2,426.47	92.70

On analysis of electronic data audit could identify 1,581 cases involving a tax effect of ₹ 1,559.55 crore due to short reporting of interstate transactions.

Penalty under Section 67 should also have been imposed. Maximum penalty to be imposed works out to ₹ 2,572.44 crore.

On this being pointed out, Government stated (April 2014) that estimation of short levy based on assumption is not fair and reasonable. There is already a manual control in which short reporting of transactions can be detected during the process of scrutiny. At the time of return scrutiny the Assessing authority is provided with a number of options in the KVATIS to verify the veracity of the returns filed by the dealer. If any unaccounted transactions are detected by assessing authorities, assessment will be completed based on best judgement creating additional demand and it is a manual process.

The reply is not acceptable as the coverage of this manual control (scrutiny) in terms of percentage of assessments scrutinised may be low and a significant proportion of cases would remain undetected.

Further, Audit re-verified (May 2014) 46 cases with reference to returns and checkpost transactions available in KVATIS and found that in 11 cases invalid data was recorded in column concerned and in 35 cases dealers failed to report the entire interstate purchases effected by them resulting in short-levy of tax of ₹ 288.41 crore. Department/Government may take effective action to verify the remaining cases.

This indicates that the inherent risk of relying on manual scrutiny of returns instead of relying on the strength of an automated system where the information available across different modules of KVATIS will help prioritize files for scrutiny. Hence necessary controls needs to be built-in the system and to integrate the checkpost module with the return processing module.

3.5.2 Non-surrender of Transit Passes

Under Section 48 of the KVAT Act and Rules thereunder, transport of goods through the border checkposts that are not to be unloaded in Kerala should be accompanied by a transit pass in Form 7B. This pass should be issued by the entry checkpost and has to be surrendered at the exit checkpost. In case of failure to surrender the transit pass at the exit checkpost, the goods which are transported into the State through the entry checkpost should be treated as the goods delivered within the State for sale and are liable to tax under this Act.

The system should provide information about the non-surrendered transit pass to authorities including the intelligence wing of the department and alert them to track the vehicle.

An extraction and analysis of data for the period from 1 April 2012 to 22 May 2013 revealed that out of the 13,146 transit passes issued surrender details of 3,534 (27 *per cent*) cases were not available in KVATIS, which had a tax implication.

On this being pointed out, Government stated (April 2014) that out of 83 checkposts, only 29 have online access to KVATIS. Hence, if the vehicles entered into State through online checkposts and exit through offline checkposts, the details would be entered in the manual register maintained at the exit checkpost. Therefore, the short levy alleged is not correct. Government also stated that the system now generates alert messages to the checkposts, to detain vehicles which have not surrendered online transit pass on previous occasion.

The Department’s reply on existing manual controls exercised at checkposts was cross verified at four major checkposts⁵ where goods in respect of 2046 cases out of the 13146 transit passes referred to in the observation above should have exited. Verification of the manual registers showed that only 674 transit passes were recorded as surrendered. The reply of the department is therefore not acceptable and tax implication on non surrender of transit passes could not be ruled out.

3.6 Use of risk management system

3.6.1 Release of consignments brought by registered/unregistered dealers for own use without verification of genuineness

As per Section 46(3) of the KVAT Act, goods for own use can be transported through checkposts on the strength of certificate of ownership and Rule 58(18) of the KVAT Rules, 2005, stipulates that every person other than a registered dealer who brought in goods not in pursuance of a sale shall furnish a certificate of ownership in Form-16. The facility of transporting goods for own use except capital goods were extended to registered dealers also, vide Circular No.14/2007. The statute (Section 70B) provides for penalty (not exceeding three times of tax due on such goods) for commercial use of goods brought from outside the State declaring it as for own use.

The extraction of data relating to release of consignments for own use revealed that both registered and unregistered dealers brought substantial volume of taxable goods into the State by furnishing Form 16 at checkposts. An illustration of aggregating similar consignments each time as for own use is given below:

Consignee TIN	Name of the consignee	Frequency	Nature of goods	Value of Commodity (₹)
32130275782	New Western Saw Mill	114 times	Timber	4,99,70,720
Unregistered	Southern Batteries Private Limited	4 times	Bars - Lead	59,178,739

Audit extracted the details of transport of bulk quantities of taxable goods such as paint, toothpaste, medicines, medical and surgical equipments, cosmetics, computer peripherals, batteries, plastic granules etc. by registered dealers and found that 399⁶ registered dealers transported bulk quantity or transported same goods repeatedly (six times or more in a year) into the state, stating as for own use. The total value of such goods comes to ₹ 117.02 crore.

⁵ Walayar, Wellington Island, Aryankavu and Amaravila

⁶ Commodity value above ₹ Five lakh

Similarly, 178⁷ unregistered dealers transported goods of value above ₹ 10 lakh into the state for own use. The total value of these comes to ₹ 81.02 crore.

The system should be geared up to gather the details of bulk quantity or repeated transactions into the state and generate over a period, a report on the type of commodity and type of persons transporting such goods to alert the authorities against the misuse of this facility. The system should also have been designed to use a risk management system to block/scrutinise such consignments before release.

Based on the scrutiny, the system should generate a demand notice for security deposit from the dealers/persons misusing this facility.

On this being pointed out, Government stated (April 2014) that the physical verification of the consignment with the transporting document is the routine function of the checkpost. After verification only genuine consignments brought for own use will be permitted to proceed. Government also stated that the system data contains token details of both approved and unapproved transactions. The data set given to audit would also contain information related to unapproved, test tokens. The reply is not acceptable. The Audit observation is based on analysis of data relating to approved transactions. The reply itself validates the observation as it has been pointed out that the physical verification is a routine manual control, with minimal data driven intelligence built into the procedure. Each consignment is treated independently. The benefit of having computerised information on similar and related transactions is not taken care of by the Department.

The system should be redesigned to use such information for preventing misuse of the facility.

3.7 Input data quality issues

3.7.1 Release of consignments brought by registered dealers without verification of the genuineness of the details entered by them

Checkpost Module System (CPMS) Module is an important unit of KVATIS in assisting the administration of tax. As the assessing officers had to rely heavily on the details of this module for assessment purpose, it is important that the data fed into this module is accurate. Audit observed that the system accepts any numerical in the value field due to weak validation controls. As a result, certain registered dealers had entered irrelevant figures like their TIN etc as the value of commodity transported into the state for trading. Illustrations of abnormal value entered into the CPMS module are as shown below:

⁷ Commodity value above ₹ 10 lakh

Sl. No.	Token no	Tin	Consignee name	Commodity value	Commodity name
1	321409/2012-13/88008	32101075708	Energy Papers	59929710019	Paper, Rolls - Uncoated (Other)
2	321310/2011-12/75759	32080750492	Gemco Rubber Pvt. Ltd	32080750492	Carbon Black
3	320921/2010-11/193513	32070482684	Geeyem Motors (P) Ltd	355700911062371	Motor Cars
4	320924/2010-11/10954	32090900174	J.M.P Traders	32090900174	Day Old Chicks
5	321310/2010-11/87485	32100252794	KVR Automobiles	1675261675261	Motor Cars

On this being pointed out, Government stated (April 2014) that errors crept into the database mainly due to data entry mistakes made by daily wage employees who entered the data into the system prior to the introduction of the system of e-consignment declaration in January 2010.

The reply is not acceptable as the data entry errors persisted during 2011-12 and 2012-13, after the introduction of e-declaration indicating absence of appropriate input controls. Integrating the data in CPMS module with that of the Return Processing Module for validation of data would enhance data integrity.

3.8 Data on physical verification of consignments

The main duty of the checkpost authorities is physical verification of consignment of goods in a vehicle and ensuring the correctness of the details entered in the e-declaration or invoices. They issue notices to the transporters in case of variation in quantity or commodity. An extraction and analysis of the data revealed that out of 1,91,43,413 vehicles with consignments released during the period from 1 April 2010 to 31 March 2013 details of physical verification were not seen entered in the field records for such verification in 99 *per cent* cases. Hence audit could not ensure/ascertain whether the consignments were physically verified or not.

The department may equip the system to capture data of physical verification using techniques such as hand held devices, x-ray scanners, uploading photographs etc. based on process and feasibility study.

On this being pointed out, Government stated (April 2014) that KVATIS is facilitated to capture the relevant details. However, due to slow performance of the application, at present, it is not practical to operate these modules as it would affect the vehicle movement. The recommendation can be incorporated once the system is upgraded by replacing the existing servers.

3.9 Conclusion

The checkposts were established to prevent the evasion of tax on interstate transport of goods. We found that the CPMS Module fell short of being an effective instrument in preventing or detecting tax evasion for the reasons stated below:

- Entering of registration numbers in the e-declaration was not made mandatory for generation of token in the case of registered dealers. Many consignments with e-declaration were released without insisting on Registration number.
- KVATIS has no provision to identify and raise alert on transport of consignments using cancelled registration numbers and transport of consignments by dealers who had not renewed their registration.
- System is not alerting the authorities concerned, though significant proportion of transit passes issued were not surrendered at the exit checkposts.
- Large quantity of goods are being transported into and outside the State 'for own use'. These include bulk quantities of medicines, surgical equipments etc. The system generates no alert to Checkpost authorities on the basis of information in KVATIS relating to the frequency and nature of these items brought in by certain dealers.

3.10 Recommendations

- ❖ The department may provide adequate controls in the software to detect and alert the interstate transactions by cancelled dealers and the dealers who have not renewed their registration.
- ❖ Entering of valid registration numbers in the field for Consignee TIN/Consignor TIN in the e-declaration format for generating e-token may be made mandatory.
- ❖ System generated alerts needs to be devised for tracking consignment of goods in bulk quantity to prevent misuse of the facility for transporting consignments 'for own use' without payment of tax
- ❖ The system should be enabled to provide information about the non-surrendered transit passes to authorities including the intelligence wing of the department so as to track such vehicle.