

## Chapter III

### Functioning of Director General of Audit and its zonal units

#### 3.1 Introduction

Internal audit is one of the main compliance verification mechanism in the department, which involves selection of assessee units on the basis of risk parameters and scrutiny of records of the assessee to ascertain the level of compliance with the prescribed rules and regulations. Internal Audit is empowered, under Central Excise and Service Tax Rules, to access the records of the assessees under rule 22 of Central Excise Rules, 2002. Every Commissionerate has an Audit cell, manned by an Assistant/Deputy Commissioner. The audit is done by a set of internal audit parties (IAP) consisting of Superintendents and Inspectors.

In order to monitor, co-ordinate and guide the effective implementation of the new audit system, the CBEC has set up Directorate General of Audit as the nodal agency. Directorate General of Audit and the field Commissionerates share the responsibility of administration and conduct of internal audit of units paying Central Excise duty and Service Tax. While the Directorate is responsible for collection, compilation and analysis of audit findings and its feedback to Central Board of Excise and Customs (CBEC) to improve tax compliance and to gauge levels of client satisfaction, audit parties from Commissionerates undertake audit in terms of internal audit protocol. In order to improve audit quality, CBEC took the assistance of Asian Development Bank in developing audit manuals, risk management manuals and manuals to train auditors in internal audit and Computer Aided Audit Tools (CAATs).

#### 3.2 Organization

The Directorate General of Audit (DGA) headed by Director General was created in July 2000 with headquarters at New Delhi. The Organization was expanded in November 2002 with the implementation of cadre restructuring when seven zonal units were created at Ahmedabad, Bangalore, Chennai, Delhi, Hyderabad, Kolkata and Mumbai each headed by an Additional Director General (ADG). Every zonal unit of DGA has area wise jurisdictional control over zonal units of Chief Commissioner and Commissionerates there under.

After restructuring in 2014, separate Audit Commissionerate have been assigned the work of Internal Audit by taking it out of purview of functional Commissionerates. However, functioning of DG (Audit) to monitor the internal audit function of the department has not been changed.

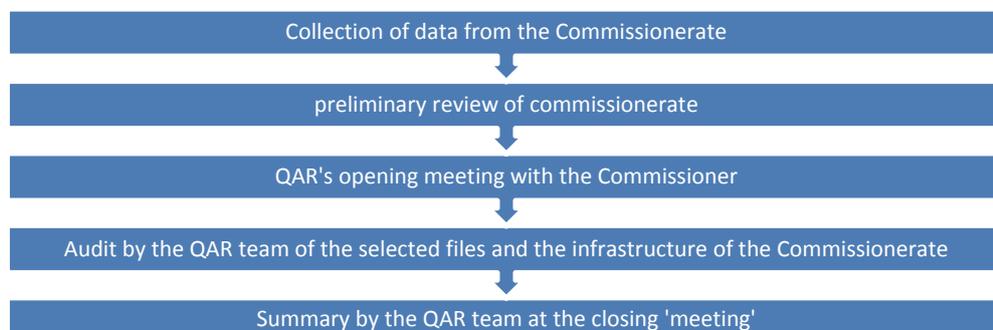
### 3.3 Functions and process:

The functional responsibilities of the Directorate have been delineated in the Charter of Functions approved by the Central Board of Excise and Customs (CBEC) through their letter F.No. 206/13/2000-CX.6 dated 30<sup>th</sup> January 2002. Directorate is to oversee the creation and institutionalization of a credible audit system. On one hand, it aids and advises the Board in policy formulation and on the other hand, it guides and provides functional direction in planning, co-ordination, supervision and conduct of audits to the field formations.

DG (Audit) is entrusted with assessment of quality of audits performed by Central excise and Service tax officers. Zonal Additional Director Generals (ADGs) are responsible for the actual conduct of Quality Assurance Review (QAR) in various Commissionerates in their respective zones. Detailed instructions to conduct QAR are prescribed in 'Manual for Quality Assurance Review' (Manual).

Information regarding audits carried out by Commissionerates by Chief Commissioners is collected from 104<sup>16</sup> Commissionerates across India through an annual proforma. Based on analysis of these proforma, DG (Audit) sends review teams to assess the quality of audit and to prepare Quality assurance report based on their assessment. Based on certain parameters such as selection of units for audit, evaluation of internal controls, audit verification, working papers, audit report preparation and timeliness and follow up, the Commissionerates are assigned grades from A to E (Excellent to Below average).

DG (Audit) then prepares an Annual report which also includes the grading of the assessed Commissionerates on audit performance. The review process is diagrammatically represented as follows:



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<sup>16</sup> 93 central excise, 07 service tax and 04 LTU Commissionerates

### **3.4 Audit Objectives**

This audit on “Functioning of Director General of Audit and its zonal units” was conducted to assess -

- i. Effectiveness of Directorate’s advice to CBEC in policy formation and to provide functional directions in conduct of audits to the field formations.
- ii. Effectiveness in following instructions and procedure framed under manual of QAR.
- iii. Improvements consequent to issue of QAR
- iv. Efficiency of human resources deployed for review of the Commissionerate.
- v. Existence of prompt and adequate follow-up of audit observation of internal audit.

### **3.5 Scope and Audit Coverage**

The scope of the audit was to evaluate the performance of the Directorate General of Audit (Headquarters office) and its seven zonal units in respect of the following two areas of its functions-

- (i) Quality Assurance Review of the Commissionerates, and
- (ii) Follow-up action on audit observations.

The office of DG (Audit), its seven zonal units and 57 Commissionerates falling under the jurisdiction of these ADGs were selected for study. The audit examined 25 sample files selected and verified for quality assurance exercise by ADG office. Sample files examined in seven zones were test checked in the selected Commissionerates to assess the authenticity of records maintained by DG audit and its subordinated offices. The period of coverage was from 2011-12 to 2013-14.

### **3.6 Audit findings**

The important audit findings under the two functions of DG Audit vis Quality Assurance Review of the Commissionerate and Follow-up action on audit observations are detailed below:

#### **3.6.1 Recommendation made by DG (Audit) to CBEC and field formation**

As per Board’s letter dated 30th January 2002, DG (Audit) is to oversee the creation and institutionalization of a credible audit system by giving advice to the Board and functional direction to field formations.

A test check of the files at DG (Audit) revealed that the recommendations were being sent to Board regarding audit norms to be followed by Commissionerate, suggestions for revision of CE and ST frequency norms, suggestions regarding improvement in final audit report format and minutes regarding formation of Audit Commissionerates. It was also seen that before finalizing the issues, suggestion/recommendation were also sought from Zonal Additional Director of Audit. After receipt of approval from CBEC the same were being circulated to all ADG office/Commissionerates.

The gist of recommendations was called for from DG (Audit). The department replied (May 2015) that the information will be compiled from the large number of files and will be provided as soon as possible.

Ministry stated (September 2015) that Directorate General is only meant to oversee the creation and institutionalisation of a credible audit system. It aids and advises the Board in policy formulation, guides and provides functional direction in planning, co-ordination, supervision and conduct of audits to the field formations. The gist of all recommendation submitted to the Board could not be prepared as there are voluminous records and there is no system to ascertain each and every letter sent to the Board and field formations. However, all live files were provided to Audit.

Audit is of opinion that Directorate should maintain records of important recommendations made to Board and field formations to evaluate proper follow up of such recommendations.

### **3.6.2 Discrepancies in the Part I of QAR report not pointed out by review teams**

The QAR process starts with collection of information from Commissionerates in Part I of proforma prescribed in Chapter-5 of QAR manual. This data is utilised as the base document to conduct a preliminary review by QAR team. The QAR team is required to verify the authenticity and correctness of the data in proforma provided by Commissionerates and recording the results in QAR report. Para 5.12 (3) of the manual states that data collected in part I of QAR is not only used to create and update national databank but is also used to identify trends of different aspect at national or zonal level.

Audit undertook scrutiny of proforma and compared the differences between Part 1 and the associated QAR reports. Audit observed instances where QAR teams have not pointed out the discrepancies in data submitted by Commissionerates in the QAR reports as detailed overleaf:

In Delhi ZU, in 11 cases there was difference in similar data i.e. number of paras raised and amount as depicted in statement D and statement G of part I of QAR for the period of three years 2011-12 to 2013-14.

Similarly, there was difference in number and amount of paras upheld in Bengaluru (10 cases) and Delhi Zones (5 cases) as depicted in statement G and statement H of part I of QAR during three years.

In Bengaluru zone, there was difference in 8 cases in number of units audited as depicted in statement D (column 8 to 12) and statement E (column 3) of part I of QAR during three years.

When we pointed this out (September 2014 and October 2014), Delhi ZU replied (October 2014) that the disparity was due to paragraphs upheld by Monitoring committee meeting (MCM). The reply is not acceptable as data element i.e. no. of para raised by audit or no. of paras upheld were same, having no relevance of MCMs.

Bengaluru ZU replied (October 2014) that barring few cases, the differences were not significant.

Audit is of the view that discrepancy in data not only affect the ranking of Commissionerates, but also affect the decision making of top management. Board may issue suitable instructions to maintain and monitoring accuracy of data.

Ministry stated (September 2015) that the zonal units were being sensitised to point out the discrepancies in part I of QAR to the field formations.

### **3.6.3 Faulty Selection of assessee files by QAR teams**

One of the most important steps in determining the efficiency of QAR is the selection of files at random from the slab-wise list of assessee units audited by the Commissionerate during the financial year being assessed. The number of files selected should be in line with the number as prescribed in the QAR manual. As per Notes part III (2) of annexure 5.1 of the manual, the QAR team is required to select a minimum of 25 files randomly from 5 slabs<sup>17</sup> with at least 5 files in each of the three revenue slabs.

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<sup>17</sup> (i) Paying total duty (in cash+Cenvat credit)above ₹ 3 crore per annum  
(ii) Paying total duty (in cash+ Cenvat credit)between ₹ 1 crore and ₹ 3 crore per annum  
(iii) Paying total duty (in cash+ Cenvat credit) between ₹ 1 crore to 50 lakh per annum  
(iv) Paying total duty (in cash+ Cenvat credit) less than 50 lakh per annum  
(v) EOU

Audit observed that the file selection norms were not adhered to in QAR process of Kolkata<sup>18</sup> Ahmedabad<sup>19</sup>, Delhi<sup>20</sup> and Mumbai<sup>21</sup> zones by selecting files less than 25 or not selecting minimum five files from three slab.

In Hyderabad zone, ADG asked the Commissionerates to keep 5 files in each category ready for audit before approaching the Commissionerates, thereby undermining the objective of selecting the files randomly giving the Commissionerates opportunity to select files with better work.

When we pointed this out (between October to December 2014), Ahmedabad ZU (December 2014), Hyderabad ZU (December 2014) and Mumbai ZU (February 2015) accepted the audit observations whereas Kolkata ZU replied (December 2014) that the situation depends on the availability of the files in respective Commissionerates.

Reply of Kolkata ZU indicate casual approach in selecting the files, thereby compromising the effectiveness of QAR process.

Ministry stated (September 2015) that the zonal ADsG are being sensitised to be careful in selecting the files for QAR.

### 3.6.4(a) Inordinate delay in issue of QAR Report

As per para 5.11 of chapter 5 of the manual, QAR report should be finalized and communicated to the jurisdictional commissioner and DG (audit) within a month of conduct of review.

Audit observed that there was delay in issuing of QAR for the year 2011-12 to 2013-14 in all zones ranging from 01 to 193 days. Few significant delays are given below:

**Table 3.1 : Delay in issue of QAR reports**

zone	Range of delay	No of QARs where delay was more than two months from scheduled time		
		2011-12	2012-13	2013-14
Delhi	11-177 days	-	6	-
Hyderabad	4-127 days	4	4	4
Chennai	2-155 days	1	-	-
Mumbai	1-87 days	-	-	2
Ahmedabad	5-193 days	4	-	-
Kolkata	24-86 days	1	-	-

In Delhi zone, there was delay ranging from 11 to 177 days in issue of QAR from the stipulated time for the year 2012-13. Further, in respect of six

<sup>18</sup> Kolkata–VI, Kolkata–VII and Kolkata Service Tax Commissionerates

<sup>19</sup> Ahmedabad service tax and Vadodara-I Commissionerates

<sup>20</sup> Chandigarh-I Commissionerate

<sup>21</sup> Pune-I, Belapur and Thane-I Commissionerates

Commissionerates,<sup>22</sup> delay was more than two months from the stipulated time.

In Hyderabad zone, delay was ranging from 4 to 127 days during the period of observation. Further, there was delay of more than two months in respect of 12<sup>23</sup> cases.

In Chennai zone, delay was ranging from 2 to 155 days. In Madurai Commissionerate delay was of 155 days for the year 2011-12.

In Mumbai zone, delay was ranging from 1 to 87 days during three years. QAR for Commissionerate Mumbai-III and Pune-I was issued with delay of more than two months from the stipulated time during the year 2013-14.

In Ahmedabad zone, delay was in the range of 5 to 193 days. QARs in respect of four Commissionerates<sup>24</sup> were issued with delay of more than two months from the stipulated time during the year 2011-12.

When we pointed this out (between September 2014 and January 2015), Delhi ZU stated (October 2014) that there was no inordinate delay except in case of Chandigarh II which was due to inadvertently misplacing QAR file. The reply is not tenable as in other cases also there was inordinate delay.

ADG Mumbai (November 2014), Bengaluru (October 2014). Ahmedabad (November 2014) and Hyderabad (December 2014) replied that due to staff constraints and some additional information required from Commissionerates, there was delay in finalization of QAR. Reply from ADG Kolkata and Chennai was awaited (September 2015).

Audit is of the view that delay of two to six months is a matter of concern as late issuance of QAR further delays its compliance by the Commissionerates affecting the objectives of QAR process.

Ministry stated (September 2015) that due to inadequate manpower in the zonal units coupled with delay in response from the field formations in providing the information called for result in some delay in issuance of QAR report. However, the zonal units are being sensitised to issue the QAR without delay.

Ministry reply indicates that there were manpower constraints in zonal units even prior to restructuring of the department. After restructuring, 45

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<sup>22</sup> Chandigarh-I, II, Allahabad, Delhi-IV, Meerut-II and Ludhiana

<sup>23</sup> Hyderabad I(2012-13 and 2013-14), Hyderabad II (2011-12 and 2012-13), Hyderabad III (2012-13 and 2013-14), Hyderabad IV(2011-12), Viskhapatanam II (2013-14), Guntur(2011-12 and 2012-13), Tirupathi(2011-12 and 2013-14)

<sup>24</sup> Ahmedabad-III (CE), Ahmedabad-III (ST), Ahmedabad Service Tax and Jaipur-I (ST)

dedicated Audit Commissionerates have been formed and it is expected that in future, the QAR reports will be issued in time.

### **3.6.4 (b) Delayed communication of grading**

As per para 5.11 of the manual, quality assurance report along with grading, should be finalized and communicated to the jurisdictional commissioner, jurisdictional chief commissioner, and the Director General (Audit) within a month of conduct of the review. Grades are assigned to Commissionerates, based on audit performance.

Audit observed that in Delhi zone, QARs were finalized and forwarded to the concerned Commissionerate but the grades were forwarded to 19 Commissionerates with delay ranging between 13 days to 249 days for the years 2011-12 and 2012-13.

Though delay in 2013-14 was marginal and in few cases, however, there may be delay in other zones/Commissionerates also. Audit is of the view that grading should mandatorily be issued along with QAR report as a QAR report would not serve its purpose without the final result of the QAR process.

Ministry stated (September 2015) that due to inadequate manpower in the zonal units coupled with delay in response from the field formations in providing the information called for result in some delay in issuance of QAR gradings. However, the zonal units are being sensitised to issue the QAR without delay.

Ministry has not replied on issuing grading separately after QAR report, though as per Manual, it should be a part of QAR report.

### **3.6.5 Delay/non-submission of response to QAR by Commissionerates**

Paragraph 2.6B of the manual prescribes that the findings of QAR are summarized and presented to the commissioner at closing meeting. These are then drafted in the form of prescribed report and forwarded to the concerned commissioner, jurisdictional chief commissioner and the DG (audit). The commissioner is required to communicate his response within a month of receipt of QAR report.

Audit observed that in Delhi, Mumbai, Hyderabad, Bengaluru and Ahmedabad zones compliance reports were not received from many Commissionerates even after one to three years as detailed in table 3.2:

**Table 3.2 : No. of Commissionerates who did not submit compliance report**

Zone	2011-12	2012-13	2013-14
Delhi	9	11	11
Mumbai	13	10	11
Hyderabad	8	10	10
Bengaluru	-	-	2
Ahmedabad	10	10	9
Kolkata	-	-	1

In Delhi zone, out of 19 Commissionerates, 8 Commissionerates had not communicated their response to the findings in 2011-12, 12 Commissionerates failed to send their response in 2012-13 and 13 Commissionerates in the year 2013-14. No action was initiated by Delhi ZU to remind the defaulting Commissionerates of their failure to respond.

In Mumbai zone 13, 10 and 11 Commissionerates did not respond to QAR during the 2011-12 to 2013-14.

In Hyderabad ZU out of 10 Commissionerates, 8 Commissionerates did not respond to QAR Report and no reply on remedial action initiated was sent to ZU.

In Bengaluru zone, reply to QAR of 2012-13 Bengaluru ST Commissionerate had not been furnished and no action was initiated by the zone.

In Ahmedabad zone, 10, 10 and 9 Commissionerates did not responded to QAR during the years 2011-12 to 2013-14.

In Kolkata zone, Patna Commissionerate did not respond to QAR during 2013-14.

Audit also observed that in many cases where compliance reports were sent by the Commissionerates, there was delay in responding to QAR during the years 2011-12 to 2013-14 ranging 03 to 1051 days. Few significant delays are given below:

**Table 3.3 : No. of Commissionerates who submit compliance report with delay**

Zone	Range of delay	No of QARs where delay was more than two months from scheduled time		
		2011-12	2012-13	2013-14
Delhi	03-302 days	03	03	-
Chennai	65-300 days	-	04	09
Mumbai	38-1051 days	08	11	09
Bengaluru	30-569 days	02	02	02
Kolkata	107-285 days	01	01	-

When we pointed this out (between September 2014 and January 2015) Delhi ZU offered no comment on the issue (October 2014), which is indicative of a casual attitude to QAR process.

Chennai ZU (September 2014), Hyderabad ZU (December 2014) and Bengaluru ZU (January 2015) accepted the audit observations. Mumbai ZU replied (October 2014) that the Commissionerates have been repeatedly reminded to send the response. Kolkata ZU confirmed the facts of delayed compliance by the Commissionerate.

Lack of response to QAR reports by Commissionerates implies that remedial measures were not initiated in time to rectify the shortfalls in quality of audits pointed out in QAR, which defeats the objectives of the entire QAR exercise.

Ministry stated (September 2015) that zonal units issue reminders to the Commissionerates to provide response to QAR reports, but shortage of manpower in Commissionerates result in delay. However, the delay is likely to be reduced due to formation of separate Audit Commissionerates with dedicated staff.

### **3.6.6 Non-validation of data published in the Annual Report of DG audit**

As per chapter 1 of QAR manual, it is the primary function of the DG (Audit) to assess the quality of audits performed by central excise and service tax officers, report the findings so that best practices are disseminated and shortcomings come to attention for remedial action such as additional training etc. Based on QAR, DG audit compiles an annual report in which audit performance of the Commissionerates is published.

A test-check of data published in annual report for the years 2011-12 and 2012-13 revealed that there were discrepancies in figures between annual report published and QAR reports as detailed below:

There were differences in the number of mandatory units selected for audited and actually audited in Delhi and Hyderabad zones. For example, in Visakhapatnam Commissionerate, the figures of non-mandatory units selected for audit during 2012-13 and units actually audit had a difference of 587 units and 416 units respectively.

In Chennai Zone, annual reports for the year 2011-12 and 2012-13 with respect to LTU Chennai Commissionerates had difference in data i.e. no. of audits conducted, revenue impact and recovery. Also, in Annual report 2012-13, percentage of parameters of Trichy Commissionerate in respect of Central Excise and Service Tax both were recorded incorrectly and consequently grading of the Commissionerate was downgraded from to C from B in both the cases.

This shows that wrong figures were published in the annual report thereby doubting the correctness of published data.

Audit is of the view that DG Audit may get the draft of annual report verified by zonal ADGs to ensure authenticity of Annual report.

Ministry stated (September 2015) that the observation had been noted for future compliance.

### 3.6.7 Incorrect grading of Commissionerates in QARs

As per chapter 3 of QAR manual, the methodology and procedure of assigning grades to Commissionerates on the basis of QAR has specified 9 audit quality elements<sup>25</sup> for Central Excise and 5 for Service Tax.

Based on the QAR reports, audit performances of the Commissionerates are evaluated and grades based on parameters are assigned.

Audit test checked the grades awarded by ADGs in QARs and verified them with the relevant files in the Commissionerate. It was observed that percentage calculated for quality elements were arrived at incorrectly by ADGs, consequently lower/higher grades were awarded to Commissionerates as detailed below:

**Table 3.4 : Incorrect gradings to Commissionerates**

Zone	No. of Commissionerates	No. of cases where grades were wrongly assigned	Remarks
Chennai	4	9	Grades were downgraded in all cases
Bangaluru	5	18	Grades were upgraded in all cases
Hyderabad	3	18	Grading were upgraded in 12 cases and remained same in 6 cases

In Chennai ZU, in 9 cases QAR review teams had wrongly assigned lower marks against quality elements than was warranted thus downgrading the performance of Commissionerates of Coimbatore, Puducherry, Tirunelveli and Service Tax Commissionerate, Chennai.

On the other hand, in Bangaluru zone, in 18 cases, grades assigned by ADG were unwarrantedly higher because of more marks against quality elements.

<sup>25</sup> **Central Excise** - 1. Selection of units for audit 2.Preliminary/Desk Review 3.Evaluation of Internal Controls 4.Preparation of Audit Plan 5. Audit Verification 6. Technical Issues 7.Working Papers, Audit Reports and Follow up 8. Professional Conduct 9.Timeliness

**Service Tax** - 1. Planning of Audit 2.Conducting of Audit 3.Documentation of Working Papers 4. Finalisation and follow up of audit 5. Other functions

Thus, grades of Bengaluru-I, Belagavi, Thiruvananthapuram, Kochi and Kozhikode Commissionerates were pushed up elevating the performance of these Commissionerates.

In Hyderabad zone, in 12 cases higher grades were awarded while in 6 cases, grades were same though percentage marks awarded were higher.

When we pointed this out (December 2014), Hyderabad ZU replied (December 2014) that-(a) marks are not being awarded for some questions which may not be applicable (b) if detailed process and techniques used in detecting the paragraph were spelt out clearly, then weightage was being given. (c) Most of the queries are subjective in nature; hence interpretation of each officer scrutinizing the file may differ marginally, which in turn affected the marks awarded/grading eventually.

Reply of Hyderabad ZU is not acceptable as the parameters adopted by us as well as the DG(Audit) were the same.

Reply of Chennai and Bengaluru ZUs was awaited (September 2015).

Audit analysis of Commissionerates' performance against the same parameters and incorrect assessment of performance by ADGs indicate casual approach of the DG (Audit) to the whole QAR exercise.

Ministry re-iterated the reply of Hyderabad ZU (September 2015) stating that the main reason for difference in grading could be due to the fact that most of the queries for calculating the gradings are subjective in nature and hence interpretation of each officer scrutinizing the file may differ, which in turn affected the marks awarded/grading eventually. However, the zonal units are being sensitised to be careful/objective in calculating the gradings.

### **3.6.8 Non- publishing of grades of LTU Commissionerates in Annual Reports**

Audit also observed that the grades allotted to LTUs were not being reflected in annual reports, though they were being awarded by respective zones and thus not intimating the same to Board for performance evaluation and rectificatory action. In absence of depiction of grading in annual reports, performance of LTUs could not be commented upon. Analysis of QAR of Delhi LTU for the period 2011-12 and 2012-13 revealed that grading were 4.5 per cent and 7.2 per cent below the conformity level of 60 per cent which may be the reason that grade are not being reflected in annual reports due to poor performance of LTUs.

Ministry stated (September 2015) that LTU Commissionerates did not provide the details of audits conducted and hence same were not reflected in the

report. Two Audit Commissionerates for LTU audits have started functioning from 15.10.2015 and their audit results will be reflected in the annual report.

Ministry reply indicate casual approach of Board in respect of LTU audits despite the fact that LTU Commissionerates are meant for Large Tax Payer units keeping audit of high revenue units out of performance review.

### **3.6.9 Not attending of opening meeting by Additional Directors General of Audit**

As per para 5.4 of the QAR Manual, the review party should fix an opening meeting with the Jurisdictional commissioner at the beginning of the review, and discuss the scope and the expected time frame of the review. It is essential that the Additional Director General attends the opening meeting with the Jurisdictional commissioner.

Examination of relevant records revealed that there was no evidence on record showing that opening meetings had been attended by the Addl. Directors General of Audit of Chennai, Mumbai and Hyderabad zonal units during the period of review covered in audit.

When we pointed this out (between September to December 2014), Ministry stated (September 2015) that in routine course, ADG and in absence of them, the next senior officer attend the opening and closing meetings but no records of meeting are maintained as the same is not instructed in QAR manuals. However, the zonal ADsG are being sensitised in this regard.

Audit is of opinion that opening and closing meeting of QAR process is an important and integral part of the process and the same should be documented.

### **3.6.10 Insignificant improvement consequent to QAR**

Quality Assurance Reviews (QARs) are conducted to ensure full compliance with the standards set for the internal audit process. Based on the extent of the conformity to the process, Commissionerates are graded from A to E categories.<sup>26</sup>

In the comparative scrutiny of QAR gradings reflected in annual reports of DG (Audit) for the years 2010-11 to 2012-13 in respect of the 93 Commissionerates of Central Excise and 73 Commissionerates of Service Tax including composite Commissionerates, Audit observed the following:

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<sup>26</sup> A = Excellent (> 90%), B = Very Good (>80.01 – <90.00%), C = Good (>70.01 – <80.00%), D = Average (>60.01 – <70.00%), E = Below Average <60%

**Table 3.5 : Comparison of grades with previous years**

Duty/ Tax	Year of annual report	Number of Comm. which were downgraded	Number of Comm. whose grade stayed the same	Number of Comm. which showed improvement
Central Excise	2011-12 (comparing with 2010-11)	22	35	36
	2012-13(comparing with 2011-12)	29	39	25
Service Tax	2011-12 (comparing with 2010-11)	18	25	29
	2012-13(comparing with 2011-12)	21	27	25

From the above table, it is clear that during 2011-12 and 2012-13, 22 and 29 Commissionerates in respect of Central Excise and 18 and 21 Commissionerates in respect of Service Tax were downgraded vis-a-vis previous year grading, showing drop in performance of internal audit.

Ministry stated (September 2015) that Directorate General evaluates the qualitative as well as quantitative performance of audits conducted by the field formations. The field formations are not under the administrative control of the Directorate and the results of audit depend on various factors on quarterly basis as well as yearly basis.

Ministry's reply is indicative of casual approach in respect of the whole process. The main function of a performance evaluation is to find shortcomings in the process and suggesting improvement. Non-improvement or down-grading of performance indicates the ineffectiveness of performance evaluation process.

### **3.6.11 Shortfall in achievement of quantitative performance growth**

Effectiveness of internal audit is also reflected in terms of revenue recovered at the instance of internal audit. Audit observed that in many test checked Commissionerates recovery of revenue decreased in comparison of previous year. The details of some of Commissionerate where drastic reductions were noticed are tabled overleaf:

Table 3.6 : Shortfall in recovery

Zone	CX / ST	Year	No. of comm. where recovery increased	Range of increase	No. of comm. where recovery decreased	Range of decrease
Chennai	CX	2011-12	7	5% to 384%	4	18% to 73%
		2012-13	8	23% to 122%	3	6% to 76%
		2013-14	5	7% to 124%	-	-
	ST	2011-12	6	11% to 87%	3	35% to 41%
		2012-13	5	32% to 164%	4	12% to 28%
		2013-14	2	50% to 70%	2	10% to 31%
Hyderabad	CX	2011-12	8	22% to 309%	2	31% to 88%
		2012-13	5	9% to 792%	5	18% to 98%
		2013-14	8	4% to 308%	2	0.4% to 62%
	ST	2011-12	8	5% to 1633%	2	66% to 75%
		2012-13	8	51% to 113%	2	11% to 22%
		2013-14	6	3% to 161%	4	5% to 73%
Ahmedabad	CX	2012-13	2	27% to 35%	1	31%
		2013-14	3	14% to 35%	2	10% to 41%
	ST	2012-13	1	12%	4	26% to 63%
		2013-14	4	47% to 170%	1	40%
Delhi		2012-13	-	-	1	22%
Mumbai	CX	2011-12	3	18% to 135%	4	29% to 86%
		2012-13	5	22% to 740%	2	6% to 22%
		2013-14	5	22% to 1220%	2	1% to 56%
	ST	2011-12	2	73% to 143%	3	4% to 48%
		2012-13	3	18% to 110%	3	23% to 99%
		2013-14	4	37% to 13745%	2	10% to 16%

In 8 Commissionerates, i.e. Chennai III, Puduchery, Vishakhapatnam II, Bhubaneswar I, Hyderabad IV, Guntur and Vadodara, negative growth was more than 50 per cent. Though recovery was being mentioned in QARs, the reasons for decrease in recovery against the amount of the audit objection detected were not analyzed and recorded in QARs.

When we pointed this out (September 2014 to January 2015), Chennai ZU accepted (September 2014) the facts, while Ahmedabad ZU (January 2015) and Hyderabad ZU (December 2014) replied that QAR is assessing the qualitative aspect of audit and not the quantitative performance. The recovery aspect is not at all reflected in grading exercise. Even if, a Commissionerate makes a huge recovery or otherwise, the grading of the Commissionerate will not get affected. Reply from Delhi ZU was awaited (September 2015).

Audit is of the opinion that recovery based on audit observations is an important criteria as it reflect correctness and sustainability of audit

objections. In fact, large number of observations reported in CAG Audit Reports, wherein either the scheduled Internal Audit has not been carried out or if carried out then the lapse is not pointed out by Internal Audit wing of department. Most of such lapses detected by CAG Audit are very general in nature which can be easily identified by Internal Audit. So there is a need of including recovery as a performance evaluation criteria.

Ministry stated (September 2015) that QAR is designed to monitor the maintenance of quality standards and is not aimed at monitoring of amount by Commissionerates. However, the parameters for quantitative and qualitative evaluation of Audit performance are being revised and more weightage will be given to recovery.

### 3.6.12 Outstanding objections not settled

As per item 7 of para 5.8 of chapter 5 of QAR manual, QAR team has to examine the follow up of audit reports as corrective action can be ensured by prompt and adequate follow-up of audit observations. Mere issue of audit report without adequate and periodical follow-up would not serve any purpose.

Audit observed that in 27 Commissionerates, 1,553 paras were outstanding from one to three years as listed below :

**Table 3.7 : Paras outstanding for settlement**

Zone	Commissionerate	No. of paragraphs outstanding	Money value(₹ in lakh)
Hyderabad	Bhubaneswar-I CE	73	1,166.05
	Bhubaneswar-I ST	93	1,952.64
	Visakhapatnam ST	28	492.00
	Guntur ST	2	NA
Ahmedabad	Ahmedabad III CE	10	NA
	Ahmedabad III ST	7	NA
Delhi	Allahabad, Lucknow, Kanpur, Meerut I and II (CE)	534	13,903.06
	Allahabad, Lucknow, Kanpur, Meerut I and II (ST)	521	1,724.40
Kolkata	Patna ST	31	1,287.00
Bengaluru	Bengaluru-I	28	1,390.88
	Bengaluru-III	25	109.54
	Bengaluru ST	7	218.48
	Belagavi-CE	48	3,257.67
	Belagavi-ST	40	693.19
	LTU, Bengaluru-CE	1	-
	LTU, Bengaluru-ST	7	530.46
	Thiruvananthapuram (CE)	3	22.77
	Thiruvananthapuram (ST)	71	1,886.73
	Kochi (CE)	24	139.13
<b>Total</b>		<b>1,553</b>	<b>28,774.00</b>

Table 3.7 indicates that 1,553 paras are pending involving revenue of 287.74 crore.

When we pointed this out (between September 2014 to December 2014). Hyderabad ZU replied (December 2014) that it is not mandated to judge the process of liquidation of pending paras in the Commissionerate, it was impressed upon/advised to do so in general interest. Further, purpose of QAR is to assess as to whether the system are in place or not and nothing else.

The reply is not acceptable as without prompt and adequate follow-up, audit observations does not serve any purpose.

Ahmedabad Zone (September 2014) admitted the observation. The reply of Delhi, Kolkata and Bengaluru ZU was awaited (September 2015).

Ministry stated (September 2015) that details of outstanding objections noticed during QAR are brought to the notice of the field formations. Field formation would be suitably instructed.

### 3.6.13 Non-production of records to Audit

QAR is based on the review of Internal Audit files maintained by the Commissionerates. However, 15 Commissionerates in three zones failed to produced files, reviewed by the QAR teams during the three years, to audit as detailed below:

**Table 3.8 : Non-production of records to Audit**

Zone	Total no. of files demanded by audit	No. of files produced	No. of files not produced to audit
Delhi	597	143	454
Hyderabad	210	63	147
Ahmedabad	706	392	314

Thus, audit could not examine and comment on the efficiency of the QAR process.

Further, Service Tax Delhi Commissionerate failed to provide any record to audit stating that records were not available due to restructuring in the department. Besides the above Cochin (2011-12) Kozhikode (2013-14), Ranchi and Jamshedpur (2011-13) also failed to provide any records to audit.

Ministry stated (September 2015) that Directorate has no role to play in the matter as the Commissionerates are not under its administrative control. However, the observation of Audit will be conveyed to all field formations to produce records to Audit.

### **3.7 Conclusion**

QAR exercise is expected to monitor the performance of Internal Audit and to take necessary action for improvement of performance. Despite the fact that dedicated staff have been deployed for the process under DG (Audit) ,the intended objectives are not being met.

#### ***Recommendation No. 1***

Accuracy of data provided by the Commissionerates need to be ensured as same is utilised by top management for performance evaluation and policy formulation.

Ministry stated (September 2015) that the observation has been noted for future compliance.

#### ***Recommendation No. 2***

Time adherence for the issue of QAR report and compliance report from the Commissionerates should be ensured to avoid delay.

Ministry stated (September 2015) that the observation has been noted for future compliance.