CHAPTER II
COMMERCIAL TAXES

Audit of Commercial Taxes Department was conducted through a test check of the assessment files, refund records and other related records in 56 out of 120 offices (46.67 *per cent*) during 2019-21, to gain assurance that the taxes were assessed, levied, collected and accounted for in accordance with the relevant Acts, Codes and Manuals, and the interests of the Government are safeguarded. Audit brought out instances of deviations/ non-compliance with the relevant Acts/ Codes/ Manuals leading to under assessment of VAT/ GST in 700 cases involving an amount of ₹139.04 crore, due to reasons like under-declaration of tax, irregular exemption of tax, non-levy of penalty, Excess allowance of ITC, etc.

This Chapter contains eight paragraphs selected from the audit observations made during the local audit referred to above and during earlier years (which could not be included in earlier reports), including two subject specific compliance audits, involving financial effect of ₹153.47 crore.

The Department/ Government has accepted audit observations involving ₹35.49 crore, out of which ₹1.98 crore had been recovered. Significant audit findings having money value ₹153.47 crore are discussed in the succeeding paragraphs.

2.1 Subject specific compliance audit on 'Processing of refund claims' under GST

2.1.1 Introduction

Timely refund mechanism constitutes a crucial component of tax administration, as it facilitates trade through release of blocked funds for working capital, expansion and modernization of existing business. The provisions pertaining to refund contained in the Goods and Services Tax (GST) laws aim to streamline and standardise the refund procedures under GST regime. It was decided that the claim and sanctioning procedure would be completely online. Due to unavailability of electronic refund module on the common portal, a temporary mechanism was devised and implemented. In this connection, the State Tax Department had issued circulars No. 05 with CCT's Ref No. CCW/ GST/ 74/ 2015 dated 13 December 2017 and No. 07 with CCT's Ref No. CCW/ GST/ 74/ 2015 dated 10 January 2018 prescribing detailed procedures. In the electronic-cum-manual procedure, the applicants were required to file the refund applications in Form GST RFD-01A on the common portal, take a print out of the same and submit it physically to the jurisdictional tax officer along with all supporting documents.

Further, various stages like issuance of acknowledgement, issuance of deficiency memo, passing of provisional/ final refund orders, payment advice, etc., involved in processing of the refund applications were being done manually. In order to make the

process of submission of the refund application electronic, circular No. 04/ 2019 GST with CCT's Ref. in CCW/ GST/ 74/ 2015 dated 24 January 2019 was issued wherein it was specified that the refund applications in Form GST RFD-01A, along with all supporting documents, had to be submitted electronically. However, various post submission stages of processing of the refund applications continued to be manual.

For making the refund procedure fully electronic (wherein all the stages from submission of applications to processing thereof could be undertaken electronically), a common portal was deployed with effect from 26 September 2019 (also called Automation of Refund Process).

2.1.2 Audit Objectives

Subject specific compliance audit **(**SSCA) on 'Processing of refund claims' under GST was taken up to assess:

(i) the adequacy of Act, Rules, notifications, circulars, etc., issued in relation to grant of refund;
(ii) the compliance of extant provisions by the tax authorities and the efficacy of the systems in place to ensure compliance by taxpayers; and
(iii) whether effective internal control mechanism exists to check the performance of the departmental officials in disposing the refund applications.

2.1.3 Audit Universe, Scope and Extent of Audit

There were a total of 6,534 (pre-automation: 4,696 and post-automation: 1,838) refund claims involving claim amount of ₹3,064.86 crore processed till 31 July 2020 in the 103 circle[15] level offices under State Tax divisions in the State. Of these, 566 refund claims from 81 circle offices were sampled for scrutiny from the Pan India GST database. This sample comprised of 291 pre-automation claims (refund claims received from 1 July 2017 to 25 September 2019) and 275 post-automation claims (received from 26 September 2019 to 31 July 2020). Audit of post-automation refund claims was conducted online. Of the sampled 566 refund claims, relevant documents in six refund claims[16] in two circles were not made available to Audit and hence could not verify these claims. Thus, total 560 sampled refund claims involving money value of ₹672.19 crore were scrutinized during field audit. Entry Conference was held with the representatives of the State Government in November 2020, wherein audit objectives, scope, criteria and methodology of audit were explained. Exit Conference was held in February 2022 and discussed audit findings included in the draft report. Response of the Department has been incorporated suitably in the report.

[15] Circle, headed by Assistant Commissioner, is the first office of contact between the trade and industry and the Department
[16] Akividu (one case) and Gajuwaka (five cases)

2.1.4 Audit criteria

Audit observations were made with reference to:

(i) Sections 54 to 58 and Section 77 of Andhra Pradesh Goods and Services Tax Act, 2017 (APGST Act);

(ii) Rules 89 to 97 of Andhra Pradesh Goods and Services Tax Rules, 2017 (APGST Rules);

(iii) Sections 15, 16 and 19 of Integrated Goods and Services Tax Act, 2017 (IGST Act); and

(iv) Notifications/ circulars/ orders issued from time to time.

Audit findings

During scrutiny of the sampled 560 refund claims, which was less than 10 *per cent* of total claims, Audit observed deficiencies like delay in issue of acknowledgement, disposal of refund claims, sanction of provisional refund, non-conduct of post-audit of refund claims, excess/ irregular sanction of refund, etc., in 343 cases involving total money value of ₹66.53 crore. A statement showing the summary of the audit findings is given below:

Table 2.1: Summary of audit findings

(₹ in crore)

Nature of audit findings	Audit sample						Deficiencies noticed						Deficiencies as percentage of sample
	Number			Amount			Number			Amount			
	Pre-auto.	Post-auto.	Total	Pre-auto.	Post-auto.	Total	Pre-auto.	Post-auto.	Total	Pre-auto.	Post-auto.	Total	
Delay in issue of acknowledgement/ deficiency memo	285	275	560	332.91	339.28	672.19	58	26	84	--	--	--	15.00
Delay in disposal of refund claims	285	275	560	332.91	339.28	672.19	56	38	94	--	--	--	16.79
Non-payment of interest of delayed processing of refunds	285	275	560	332.91	339.28	672.19	41	38	79	0.04	0.29	0.33	14.11
Delay in sanction of provisional refund	160	131	291	137.06	94.57	231.63	9	13	22	--	--	--	7.56
Non-conduct of post-audit of refund claims	285	0	285	332.91	0	332.91	285	--	285	--	--	--	100
Irregular excess refund in claims relating to zero-rated supplies	160	131	291	137.06	94.57	231.63	9	1	10	1.77	0.01	1.78	3.44
Irregular excess refund in claims under inverted duty structure	50	72	122	123.74	209.51	333.25	1	4	5	0.34	0.14	0.48	4.10
Other observations	285	275	560	332.91	339.28	672.19	14	--	14	63.94	--	63.94	2.50

Audit findings are detailed in the subsequent paragraphs.

2.1.5 Delay in issue of acknowledgment/ deficiency memo

Rule 90(2) of APGST Rules, 2017, read with Section 54 of APGST Act, 2017, stipulates that after filing of refund application, the proper officer shall scrutinize the application for its completeness and issue acknowledgement in Form GST RFD-02 within a period of 15 days of filing of the said application. Further, as per sub-section (3) of Rule 90, where any deficiencies are noticed, the proper officer shall communicate the deficiencies to the applicant in Form GST RFD-03 requiring him to file a fresh refund application after rectification of such deficiencies.

During verification of 560 sampled refund claims, Audit noticed delay in issue of acknowledgement in 72 (12.86 *per cent*) refund claims and delay in issue of deficiency memo in 12 (2.14 *per cent*) refund claims pertaining to 30 circles[17] as detailed in ***Appendices – 2.1 and 2.1A***. Of these, 70 cases were delayed up to three months, 11 cases were delayed by three to six months and three cases were delayed by more than six months, respectively. This had resulted in non-observance of the provisions of the Act. Delay in issuing acknowledgement (RFD-02)/ deficiency memo (RFD-03) affects the disposal of refund claims (paragraph 2.1.6 refers).

On this being pointed out (between November 2020 and March 2021), Government in the reply (July 2022) stated that delay in 24 cases[18] was due to late submission of required documents by the taxpayers. Reply is not acceptable as in the cases of non-submission of required documents, deficiency memo is to be issued to the taxpayers.

Government further stated that in 36 cases[19] delay was due to technical/ systemic issues, in four cases[20] due to administrative reasons and in two cases (Chilakaluripet and Tirupati-II) due to involvement of large volume of records for verification. In 18 cases[21] specific reply for the delay in issue of acknowledgment (RFD-02)/ deficiency memo (RFD-03) was not furnished.

2.1.6 Delay in disposal of refund claims

As per Section 54(7) of the APGST Act, 2017, read with Rule 92 of the APGST Rules, 2017, the proper officer shall issue refund order under sub-section (5) within 60 days from the date of receipt of application which is complete in all respects.

During verification of 560 sampled refund claims, Audit noticed delay in disposal of the claims in 94 (16.79 *per cent*) refund claims, involving claims amount of

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[17] Addanki, Amalapuram, Anakapalli (3 cases), Ananthapuramu-II, Autonagar, Benz Circle, Bhavanipuram, Bhimavaram (3 cases), Chilakaluripet (4 cases), Chittoor-II (7 cases), Dwarakanagar, Gajuwaka (3 cases), Gudivada, Gudur, Hindupur, Ibrahimpatnam (12 cases), Jangareddygudem, Markapur (2 cases), Morrispet, Nellore-III, Ongole-I (3 cases), Ongole-II (6 cases), Patamata (3 cases), Puttur, Sattenapalli (2 cases), Sitharampuram (4 cases), Steel Plant (13 cases), Suryaraopet, Tirupati-II (3 cases) and Vuyyuru (2 cases)

[18] Amalapuram, Ananthapuramu-II, Autonagar, Bhavanipuram, Bhimavaram (3 cases), Chilakaluripet (2 cases), Chittoor-II (2 cases), Gudivada, Jangareddygudem, Ongole-II (6 cases), Patamata (2 cases), Sitharampuram and Vuyyuru (2 cases)

[19] Addanki, Anakapalli (3 cases), Benz Circle, Chittoor-II (3 cases), Dwarakanagar, Gajuwaka (3 cases), Gudur, Nellore-III, Ongole-I (3 cases), Patamata, Sitharampuram (3 cases), Steel Plant (13 cases), Suryaraopet and Tirupati-II

[20] Morrispet, Sattenapalli (2 cases) and Tirupati-II

[21] Chilakaluripet, Chittoor-II, Hindupur, Ibrahimpatnam (12 cases), Markapur (2 cases) and Puttur

₹111.39 crore, pertaining to 30 circles[22] as detailed in ***Appendices – 2.2 and 2.2A***. Of these, in 69 cases, the delay was up to three months, in 19 cases, the delay was three to six months and in six cases, the delay was more than six months. Of the 19 cases, one case relating to Vuyyuru circle was not finalised as on the date of audit due to non-furnishing of declaration by the dealer for the goods located in Special Economic Zone (SEZ) unit in support of non-availment of ITC on the corresponding purchases either electronically or manually.

On this being pointed out (between November 2020 and March 2021), Government stated (July 2022) similar replies[23] like late submission of required documents by the taxpayers (in 47 cases), systemic/ technical issues (in 35 cases), etc., as mentioned in paragraph 2.1.5 supra. Specific reply for the delay was not furnished in two cases of Chilakaluripet and Chittoor-I circles.

Further, as per Section 56 of APGST Act, 2017 if any tax ordered to be refunded under sub-section (5) of Section 54 to any applicant was not refunded within 60 days from the date of receipt of application, interest at such rate not exceeding six *per cent* as may be specified in the notification issued by the Government on the recommendations of the Council shall be payable in respect of such refund from the date immediately after the expiry of 60 days to the date of refund of such tax.

Despite delay in making refund to the taxpayers, interest under Section 56 amounting to ₹33.31 lakh in 79 cases (as detailed in ***Appendices - 2.2 and 2.2A***) was not paid to the claimants.

On this being pointed out (between December 2020 and April 2021), it was replied that interest was not paid as taxpayers did not claim the same. Reply is not acceptable as the provisions do not require interest to be paid only after being claimed by the taxpayer.

During Exit Conference (February 2022), Department stated that delay in most of the cases was due to late submission of requisite documents by the claimants. Payment of interest would arise only when the delay is on the part of proper officer. Further, assured that instructions would be issued to the authorities in the form of Standard Operating Procedure (SOP) for adhering to timelines and for payment of interest by ascertaining the reasons for such delays in disposal of claims on case to case basis.

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[22] Addanki, Amalapuram, Anakapalli (5 cases), Autonagar (3 cases), Benz Circle, Bhavanipuram, Bhimavaram (3 cases), Chilakaluripet (4 cases), Chittoor-I, Chittoor-II (2 cases), Dwarakanagar (2 cases), Gajuwaka, Ibrahimpatnam (13 cases), Jagannaikpur, Jangareddygudem, Kakinada (3 cases), Kavali, Nellore-I, Ongole-I (9 cases), Ongole-II (4 cases), Patamata, Puttur (2 cases), Samarangam Chowk (4 cases), Sattenapalli (2 cases), Sitharampuram (2 cases), Steel Plant (14 cases), Suryabagh (2 cases), Suryaraopet (2 cases), Vizianagaram West and Vuyyuru (6 cases)

[23] Late submission of required documents by the taxpayers (in 47 cases): Amalapuram, Autonagar (2 cases), Bhavanipuram (2 cases), Bhimavaram (2 cases), Chilakaluripet (2 cases), Chittoor-II, Dwarakanagar (2 cases), Jagannaikpur, Jangareddygudem, Ibrahimpatnam (13 cases), Ongole-II (4 cases), Patamata, Puttur, Samarangam Chowk (4 cases), Steel Plant (3 cases), Suryaraopet and Vuyyuru (6 cases)
Systemic/ technical issues (in 35 cases): Addanki, Anakapalli (5 cases), Benz Circle, Chittoor-II, Gajuwaka, Kakinada (3 cases), Kavali, Ongole-I (8 cases), Sitharampuram (2 cases), Steel Plant (8 cases), Suryabagh (2 cases), Suryaraopet and Vizianagaram West
Large volume of records (in seven cases): Autonagar, Chilakaluripet, Nellore-I, Puttur and Steel Plant (3 cases)
Administrative reasons (three cases): Ongole-I and Sattenaplli (2 cases)

2.1.7 Delay in sanction of Provisional Refund

Rule 91(2) of APGST Rules, 2017, read with Section 54 of APGST Act, 2017, provides for provisional refund against zero-rated supplies[24]. As per Rule 91(2) of APGST Rules, 2017 the proper officer, after scrutiny of the claim and the evidence submitted in support thereof and on being prima facie satisfied that the amount claimed as refund under sub-rule (1) is due to the applicant in accordance with the provisions of sub-section (6) of Section 54, shall make an order (in Form GST RFD-04), sanctioning the amount of refund due to the said applicant on a provisional basis within a period not exceeding seven days from the date of the acknowledgement under sub-rule (1) or sub-rule (2) of Rule 90.

During the scrutiny of 291 eligible refund claims for provisional refund in 49 circles, Audit noticed delay in sanctioning of provisional refund in 22 refund claims (7.56 *per cent*) pertaining to 12 circles[25] as detailed in ***Appendices – 2.3 and 2.3A***. This resulted in non-observance of stipulated provisions. In all the 22 cases delay was up to three months.

On this being pointed out (between December 2020 and March 2021), Government stated (July 2022) similar replies[26] like late submission of required documents by the taxpayers (in 10 cases), systemic/ technical issues (in two cases), etc., as mentioned in paragraph 2.1.5 supra.

In the case of Peddapuram circle, it was stated that the case was to be finalized by 19 March 2020. However, due to Covid pandemic time limit for completion of action was extended from 15 March 2020; Reply is not acceptable as the extension of time was granted from 20 March 2020 as per G.O. Ms. No. 264 of Revenue (Commercial Taxes-II Department, dated 11 September 2020.

Specific reply was not furnished in three cases relating to Steel Plant (two cases) and Kadapa-II circles.

The fact however, remains that timely sanction of provisional refund was not done resulting in delayed flow of working/ operating capital to the exporter.

2.1.8 Non-conducting of post-audit of refund claims

Andhra Pradesh State Tax Department in its circular No. 05 with CCT's Ref. No. CCW/ GST/ 74/ 2015 dated 13 December 2017 enunciated the procedure for manual processing of refunds of zero-rated supplies. The circular *inter alia,* stipulated that the pre-audit of manually processed refund applications is not required till issuance of

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[24] Zero-rated supplies: Goods or Services or both either (i) exported or (ii) supplied to SEZ unit/ SEZ developer as per Section 16 of the IGST Act, 2017

[25] Addanki, Anakapalli, Ananthapuramu-II (5 cases), Kadapa-II, Kakinada, Patamata (2 cases), Peddapuram, Puttur, Sattenapalli, Steel Plant (5 cases), Tanuku-I and Vuyyuru (2 cases)

[26] Late submission of required documents by the taxpayers (in 10 cases): Ananthapuramu-II (5 cases), Patamata (2 cases), Puttur and Vuyyuru (2 cases)
Systemic/ Technical issues (in two cases): Addanki and Kakinada
Large volume of records (in three cases): Steel Plant circle
Administrative reasons (in two cases): Anakapalli and Sattenapalli circles
Time lapse in conceptual understanding (in one case): Tanuku-I circle

separate guidelines by the Board, irrespective of amount involved. However, it was clarified that the post-audit of refund order shall be continued as per the extant guidelines.

Audit noticed that there was no mechanism in the department to monitor adherence to the post-audit instructions issued by the Board and none of the sampled 285 pre-automation refund claims, involving claim amount of ₹332.91 crore, were sent for post-audit. Thereby, instructions of the Board were not complied with. The Department, had thus forgone the opportunity of detecting cases of possible revenue loss in the cases detected by Audit (paragraphs 2.1.9 and 2.1.10 refers), due to non-adherence to Board's instructions regarding post-audit of refund claims.

On this being pointed out, the circles replied (between November 2020 and March 2021) that no specific guidelines were received by them with respect to post-audit. The reply is not acceptable as there were clear instructions to continue post-audit of refund orders as per the extant guidelines.

During Exit Conference (February 2022), regarding post-audit, the Department stated that there were no guidelines/ SOP under APVAT/ GST. Circulars were however, issued for conducting post-audit of 20 *per cent* of refund cases based on certain risk parameters.

2.1.9 Irregular/ excess refund in claims related to zero-rated supplies

Section 54(3)(i) of the APGST Act, 2017, provides for refund of unutilized Input Tax Credit (ITC) for zero-rated supplies made without payment of tax. Rule 89(2)(b) of APGST Rules provides for submission of (i) statement containing number and date of shipping bill/ bill of export and (ii) statement containing the number and date of relevant export invoices along with the refund application (RFD-01) as the documentary evidences, as applicable, to establish that a refund is due to the applicant and refund amount is required to be calculated as per the formula shown below specified under sub-rule (4) of Rule 89. In addition to the above provisions, as per instruction 42 of CCT's Ref. No. 03/2020 dated 10 January 2020, ITC of Compensation Cess may be availed for making zero-rated supplies.

Refund Amount = (Turnover of zero-rated supply of goods + Turnover of zero-rated supply of services) X Net ITC / Adjusted Total Turnover

Thus, excess declaration of zero-rated turnover of goods and services/ Net ITC or short declaration of adjusted total turnover by the dealers would result in claiming of excess refund.

Audit of 291 refund claims relating to export related claims showed that in 10 claims (deviation rate: 3.44 *per cent*) in six circles[27] excess amount of ₹1.78 crore was sanctioned to the dealers as detailed in the succeeding paragraphs.

[27] Chinawaltair, Daba Gardens, Nellore-III, Ongole-II, Tanuku-I (5 claims) and Vizianagaram East

2.1.9.1 Sanction of excess refund due to turnover variation

During scrutiny of refund claims, Audit observed in four claims pertaining to Tanuku-I circle, the value of zero-rated turnover mentioned in claim application was higher than that shown in statement of invoices enclosed. Non-considering the statement of invoices value resulted in the excess computation (₹8.10 lakh) of eligible refund claim in these cases as detailed in ***Appendix - 2.4***. One such case is illustrated below.

A taxpayer claimed refund (ARN No. AA370118010783C) for the period January 2018. In the refund application (RFD-01) the taxpayer had declared zero-rated turnover as ₹7.65 crore. However, as per the statement of invoices enclosed to the application the total value of zero-rated turnover was ₹7.22 crore. The proper officer had considered ₹7.65 crore instead of ₹7.22 crore while computing the eligible refund amount which resulted in excess claim of ₹3.52 lakh.

On this being pointed out (March 2020), Government in the reply (July 2022) stated that notices were issued to the taxpayer. Orders would be passed after verifying the objections filed by the taxpayer.

2.1.9.2 Sanction of excess refund due to net ITC variation

As per circular No. 04/ 2019 GST with CCT's Ref. in CCW/ GST/ 74/ 2015 dated 24 January 2019 read with Section 2(59) of APGST Act, inputs are goods other than capital goods used or intended to be used by a supplier in the course or furtherance of business. Thus, inputs do not include capital goods. ITC on capital goods can be availed towards adjustment of tax liability but not eligible for claiming as refund.

During scrutiny of the sampled refund claims, Audit observed (February 2021) in two claims in two circles[28] that the amount of ITC of ₹26.11 lakh on purchase of capital goods, *viz.,* purchase of motor car and construction equipment, was included in computation of 'Net ITC' to arrive at the refund amount. This had resulted in excess sanction and payment of refund of ₹18.83 lakh[29] as detailed in ***Appendix - 2.5***. One such case is illustrated below.

In a refund claim relating to Ongole-II circle, Audit observed (February 2021) that the proper officer had sanctioned (November 2018) refund of ₹27.35 lakh claimed by the taxpayer (ARN No. AA370318516198Y) for the tax period from July 2017 to March 2018. From the records, it was noticed that the taxpayer had included ITC on capital goods amounting to ₹23.10 lakh in the net ITC amount. The maximum eligible refund after excluding portion of 'capital goods' from net ITC worked out to ₹11.53 lakh. Thus, incorrect computation of eligible refund amount had resulted in excess refund of ₹15.82 lakh[30].

[28] Ongole-II and Nellore-III
[29] ₹3.01 lakh + ₹15.82 lakh
[30] ₹27.35 lakh - ₹11.53 lakh

The excess refund in these two claims was recoverable along with interest and penalty as per the terms of Section 73 of APGST Act.

On this being pointed out (February 2021), Government in the reply (July 2022) accepted audit observation and stated that notices, by raising demand for ₹50.62 lakh with penalty and interest, have been issued to the taxpayers.

2.1.9.3 Sanction of excess refund due to adjusted total turnover variation

In two refund claims pertaining to two circles[31], the value of adjustable total turnover (includes zero-rated and taxable supplies) of ₹159.29 crore mentioned in GSTR-3B was higher than that of ₹50.32 crore claimed in refund application (included only zero-rated supplies). This had resulted in excess refund of ₹1.49 crore in these two claims as detailed in ***Appendix - 2.6***. One such case is illustrated below.

In Vizianagaram East circle, the dealer (ARN no. AA370219378712U) had filed refund claim for the month of February 2019. In the application he had declared adjusted total turnover as ₹38.26 crore. This amount included only zero-rated turnover. However, from the monthly return (GSTR-3B) for the month of February 2019 it was observed that there was ₹24.05 crore turnover under 'other than zero-rated' and the total adjusted turnover thus worked out to ₹62.31 crore. Instead, the proper officer considered ₹38.26 crore as adjusted turnover while sanctioning the refund claim which resulted in excess refund of ₹75.22 lakh.

On this being pointed out (March 2020/ February 2021), in the case of Vizianagaram circle, Government stated (July 2022) that due to considering the amount of reversal of ITC by Audit, wrong adoption of exempt turnover in GSTR-3B and subsequent computation while arriving at eligible refund resulted in excess refund.

The reply is not acceptable. Audit computed eligible refund amount as per the details declared by the taxpayer in the GSTR-3B return by excluding the amount of reversal of ITC.

In the case of Tanuku-I circle, the turnover declared under outward taxable supplies (other than zero rated, nil rated and exempted) was considered as exempt supplies under Cess Compensation Act. This was not in order since the taxpayer had not declared the turnover as exempt supplies in the GSTR-3B return.

2.1.9.4 Other cases

(A) Excess refund due to incorrect consideration of tax period

In a claim relating to Chinawaltair circle it was observed that a taxpayer had filed refund application (ARN No. AA370520006873E) in May 2020 claiming refund of ₹1.49 lakh for the tax period August 2017 and the same was sanctioned (July 2020). However, as per provisions of Section 54 of the Act, refund is required to be claimed before the expiry of two-year period from the relevant date, *i.e.,* end of financial year to which refund claim was related. Thus, refund claim was to be submitted by March 2020.

[31] Tanuku-I and Vizianagaram East

Sanction of refund claim submitted after due date was thus irregular. The entire amount of ₹1.49 lakh is to be recovered with applicable interest.

AC, Chinawaltair circle replied (December 2020) that the claimant had wrongly filed one invoice while filing the GSTR-I and they were unable to claim the refund for the relevant period. The reply is not acceptable as a period of two years is provided for claiming refunds and sanctioning the claim for the time barred tax period is not permissible and hence not in order.

Government did not offer any remarks in their reply (July 2022).

(B) Refund sanctioned on ineligible exports

As per Para 4 of Notification No.26/ 2015-2020 dated 21 August 2018 issued by Ministry of Commerce & Industry, export of Beach Sand Minerals (BSM) was brought under State Trading Enterprise (STE). Beach sand minerals, permitted anywhere in the export policy, is to be regulated in terms of the notification with effect from 21 August 2018. As per the notification, export of BSM should be canalized through Indian Rare Earths Limited (IREL) as stipulated in the Export Policy.

Audit noticed (December 2020) in one refund claim (ARN No. AA37081834385X) relating to Daba Gardens circle that a taxpayer filed a refund claim of ₹1.10 lakh on 12 October 2018 on account of exports of Beach Sand Minerals for the tax period July - August 2018 and the claim was sanctioned in October 2019. Audit scrutiny of the invoices concerned and shipping bills revealed that turnover of ₹28.92 lakh mentioned in refund application included exports valuing ₹17.91 lakh made on 23 August 2018, *i.e.,* after issue of notification. These were, however, not canalized through IREL. Hence, this was not to be considered as export and ineligible for claiming as refund as the same violated the system devised through the notification for such exports. The eligible refund amount worked out to ₹0.17 lakh against the sanctioned amount of ₹1.10 lakh. The ineligible refund of ₹0.93 lakh was recoverable along with interest.

On this being pointed out (December 2020), it was replied (December 2020) that the audit observation would be verified and detailed reply submitted in due course.

Government did not offer any remarks in their reply (July 2022).

2.1.10 Irregular/ excess refund in claims relating to inverted duty structure

As per Section 54(3)(ii) of the APGST Act, 2017, a registered person may claim refund of any unutilized ITC at the end of any tax period where the credit has accumulated on account of rate of tax on inputs being higher than the rate of tax on output supplies (*i.e.,* inverted duty structure). Further, Rule 89(5) of the APGST Rules prescribes formula for maximum refund of unutilized ITC on account of inverted duty structure as given below.

Maximum Refund amount = {(Turnover of inverted-rated supply of goods and services) X Net ITC/ Adjusted Total Turnover) – tax payable on such inverted rated supply of goods and services}

Where –

"Net ITC" shall mean input tax credit availed on inputs during the relevant period other than the input tax credit availed for which refund is claimed under sub-rules (4A) or (4B) or both;

"Adjusted Total Turnover" means the sum total of the value of - (a) the turnover in a State or a Union Territory, as defined under clause (112) of Section 2, excluding the turnover of services; and (b) the turnover of zero-rated supply of services determined in terms of clause (D) and non-zero-rated supply of services, excluding-

(i) the value of exempt supplies other than zero-rated supplies; and

(ii) the turnover of supplies in respect of which refund is claimed under sub-rule (4A) or sub-rule (4B) or both, if any, during the relevant period.

"Relevant period" means the period for which the claim has been filed.

Thus, in addition to excess declaration of turnover/ net ITC or short declaration of adjusted turnover, non-declaration of tax payable on inverted rated supply of goods and services would also result in excess claiming of refund amount.

Further, in the case of inverted duty structure, as per Rule 89(2)(h), refund application shall be accompanied by a statement containing the number and date of invoices received and issued during a tax period where rate of tax on inputs being higher than the rate of tax on output supplies.

Audit scrutiny of 122 refund claims relating to inverted duty structure claims showed that in five claims (deviation rate: 4.10 *per cent*) in four circles[32] excess amount of ₹47.57 lakh was sanctioned to the dealers as detailed below.

2.1.10.1 Sanction of excess refund due to inflated turnover

As per Section 54(1) of APGST Act, 2017, any person claiming refund of tax and interest, if any, paid on such tax or any other amount paid by him, may make an application before the expiry of two years from the 'relevant date' (as per provisions of Section 54(14)(2) of APGST Act). In the cases of inverted duty structure, relevant date is the end of the financial year in which such claim for refund arises. However, this criteria was amended and the two-year period is to be reckoned from the due date for furnishing of return (under Section 39) for the period in which such claim for refund arises. The amendment came into force from 01 February 2019.

(A) Inflated turnover due to considering time-barred invoices

Audit observed that, in two claims in Sitharampuram circle, the taxpayers while claiming the refund included the invoices prior to the two-year period from the relevant date thereby inflated the turnovers. This had resulted in excess refund of ₹6.17 lakh as detailed in ***Appendix - 2.7***. One such case is illustrated below.

[32] Gajuwaka, Ongole-II, Patamata and Sitharampuram (2 claims)

A taxpayer in Sitharampuram circle had filed refund application (ARN No. AA370320010831U) in March 2020 for the tax period from July 2017 to March 2018. However, as per the amended provisions of the Act the taxpayer is required to claim refund before 20 August 2019, *i.e.,* two-year period from the due date of submission of return for the tax period (due date for filing return for the month of July 2017 was 20 August 2017). As the taxpayer applied for refund in March 2020, refund amount can be claimed for the months of February and March 2018 only. The eligible refund amount, as per the GSTR-3B returns of the two months, worked out to ₹1.20 lakh against the sanctioned amount of ₹5.15 lakh. Thus, sanctioning refund for the inadmissible tax period, *i.e.,* from July 2017 to January 2018 resulted in sanction of excess refund of ₹3.95 lakh.

On this being pointed out (March 2021), Government in the reply (July 2022) contested that the amendment to relevant date vide Act No. 31 of 2018 was effective from 01 February 2019 and not applicable for the cases pointed out by Audit.

The reply is not acceptable as the relevant period is to be reckoned from the due date for furnishing of return as per amended provisions of the Act. Further, in the instant cases, the taxpayers filed applications for refund in the months of December 2019/ March 2020 *i.e.,* after the effective date of amendment hence applicable to these cases.

(B) Claiming of excess refund by inflating turnover in comparison to GSTR-3B

In one case (ARN No. AA370420001497J) relating to Patamata circle, the taxpayer inflated the turnover (₹17.88 lakh) of inverted rated supply of goods and services in refund claimed for the month of October 2019 when compared to GSTR-3B return (₹11.29 lakh). Moreover, the turnover value of statement of invoices (₹14.39 lakh) also did not match with that mentioned in refund application and GSTR-3B return. Eligible refund amount as per GSTR-3B details worked out to ₹2.99 lakh. It was, however, observed that the proper officer had sanctioned refund of ₹3.48 lakh based on the details mentioned in the refund application. Thus, sanctioning refund claim without cross verification of available details had resulted in excess refund of ₹0.49 lakh.

We pointed out this in March 2021. Government did not offer any remarks in their reply (July 2022).

2.1.10.2 Sanction of excess refund due to net ITC variation

Audit observed in Ongole-II circle that the amount of refund claimed (ARN No. AA3709190030936) by a taxpayer included the ITC availed on input services amounting to ₹48.31 lakh (refund amount sanctioned: ₹75.20 lakh). The amount of ITC availed on input services should have been excluded while computing eligible amount of refund claim. Thus, eligible refund amount after excluding input services worked out to ₹40.81 lakh. The proper officer, however, considered net ITC of ₹1.07 crore without excluding the amount of input services which resulted in incorrect sanction of refund amount (₹75.20 lakh). The irregular sanction of excess refund of ₹34.39 lakh needs to be recovered along with applicable interest.

On this being pointed out (February 2021), AC, Ongole-II circle replied (November 2021) that an amount of ₹42.55 lakh towards excess refund along with interest has been recovered from the taxpayer.

2.1.10.3 Sanction of refund on ineligible goods

Central Government had notified[33] (June 2017) list of goods[34] in respect of which no refund of un-utilised ITC shall be allowed, where the credit had accumulated on account of rate of tax on inputs being higher than the rate of tax on the output supplies of such goods (other than nil rated or fully exempt supplies).

During test check of sampled refund claims, Audit observed (December 2020) in Gajuwaka circle that a refund of ₹6.51 lakh had been sanctioned (June 2020) to a taxpayer (ARN No. AA370520002326R) on account of refund of ITC accumulated due to inverted duty structure. The sanction was made for the commodity 'Indian Railway Wagon Parts' having Harmonized System of Nomenclature (HSN) Nos. 8602, 8607 (listed goods in Notification No.05/ 2017-Central Tax (Rate)) and for the commodity 'Indian Railway Services' having Service Accounting Code (SAC) No. 996739 having GST rate of 18 *per cent* which was not applicable for inverted rated structure in view of outputs also being taxed at 18 *per cent*. Thus, the entire refund of ₹6.51 lakh needs to be recovered along with applicable interest.

On this being pointed out (December 2020), Gajuwaka circle accepted (December 2020) the observation and intimated (September 2021) adjustment of the excess claim of refund through debit entry in the taxpayers ledger.

Thus, it is evident from the cases of irregular excess refund that in certain cases, the refund claims have been allowed based on details declared in refund application without cross checking it with the invoices/ monthly returns filed by the taxpayers which indicates a lapse in control procedure.

2.1.10.4 Other observations

(A) Irregular allowance of refund on account of balance in credit ledger

As per the provisions of Section 54(3) of APGST Act, 2017, no refund of unutilised input tax credit shall be allowed in cases other than (i) zero-rated supplies made without payment of tax; (ii) where the credit has accumulated on account of rate of tax on inputs being higher than the rate of tax on output supplies (other than nil rated or fully exempt supplies) *i.e.,* inverted duty structure.

During test check of 560 sampled refund claims, Audit observed in Anakapalli circle that a taxpayer filed a refund claim (ARN No. AA370518351574N) under the category 'any other', for the stated reason of 'unutilised SGST balance amount in the credit ledger after utilising IGST and CGST amounts towards set off in the transactions of

[33] No. 05/ 2017-Central Tax (Rate), dated 28 June 2017

[34] the description of which is specified in column (3) of the Table annexed and falling under the tariff item, heading, sub-heading or Chapter, as the case may be, as specified in the corresponding entry in column (2) of the said Table

interstate sales', for an amount of ₹13.76 lakh and the same was sanctioned in May 2019.

The refund was, however, irregular as the stated reason was not admissible as per the provisions of the Act. Hence, the ineligible refund of ₹13.76 lakh sanctioned needs to be recovered along with applicable interest.

On this being pointed out (January 2021), it was replied (January 2022) that the taxpayer had paid the entire amount of ₹13.76 lakh.

(B) Demand not adjusted while sanctioning refund order

As per Section 54(10) of APGST Act, 2017, read with Rule 92(1) of APGST Rules, 2017, in cases where any refund is due to a registered person who has defaulted in furnishing any return or who is required to pay any tax, interest or penalty, subject to conditions therein, the proper officer may withhold payment of refund until payment of dues or deduct the dues from the refund amount.

During scrutiny of 560 sampled refund claims, Audit noticed (January 2021) that a taxpayer in Kurupam Market circle filed a refund claim (ARN No. AA37061901367U) for the month of May 2019 for refund of cess amounting to ₹6.78 lakh paid erroneously instead of SGST. It was observed that a show cause notice was served (June 2019) on the taxpayer stating that there was a variation of ₹4.07 lakh on account of tax due for taxable supplies (₹2.04 lakh) and due for excess availed ITC (₹2.03 lakh). In response the taxpayer stated (July 2019) that he had adjusted the ITC of ₹1.26 lakh and also agreed to adjust/ deduct the remaining amounts towards differential tax and excess ITC. However, the Circle had sanctioned (August 2019) the refund for the whole amount of ₹6.78 lakh. Thus, sanction of refund without adjusting the pending tax liability of ₹2.81 lakh[35] was not justifiable. The same needs to be recovered along with the interest.

On this being pointed out (January 2021), it was replied (January 2021) that the observation would be examined and detailed reply submitted to Audit in due course.

Government did not offer any remarks in their reply (July 2022).

(C) Non-collection of interest on excess refund sanctioned

As per Section 50(1) of APGST Act, 2017, read with Section 73(1), every person who is liable to pay tax in accordance with the provisions of the Act or the rules made there under, but fails to pay the tax or any part thereof to the Government within the period prescribed, or erroneously availed/ utilised shall for the period for which the tax or any part thereof remains unpaid, pay on his own, interest at such rate, not exceeding 18 *per cent*, as may be notified by the Government on the recommendations of the Council.

During test check of 560 sampled claims, Audit observed (February 2021) in Vizianagaram East circle that in the process of finalization of refund claim (ARN No. AA370719065709R) for ₹27.32 lakh, provisional refund of ₹5.46 lakh was sanctioned (January 2020) to a taxpayer. Later, the entire claim was rejected (January 2020) and

[35] ₹4.07 lakh - ₹1.26 lakh

demand (Form DRC-07) for recovery of the amount of provisional refund was served in February 2020. However, the Circle office did not levy applicable interest of ₹0.14 lakh at 18 *per cent* on the amount of provisional refund as per the norms.

On this being pointed out (February 2021), Government replied (July 2022) that the taxpayer had paid the interest amount.

(D) Refund amount not credited within the stipulated time

As per Section 56 of APGST Act, 2017, if any tax to be refunded to any applicant is not refunded within 60 days from the date of receipt of application, interest at such rate not exceeding six *per cent* or as may be specified in the notification issued by the Government on the recommendations of the Council shall be payable in respect of such refund from the date immediately after the expiry of 60 days from the date of receipt of application till the date of refund of such tax.

During test check of 560 sampled claims, Audit noticed (March 2021) that in Jagannaikpur circle a taxpayer filed a refund claim (ARN No. AA370318000623I) for ₹44.60 lakh on account of accumulated ITC on export of goods without payment of tax. In this case, a provisional refund of ₹40.14 lakh was made on 28 January 2019. Further, the final refund order for the remaining amount of ₹4.46 lakh was issued on 25 March 2019 with a delay of 39 days and the same was credited to the claimant's account on 02 May 2019 with a delay of 75 days.

During scrutiny of refund file it was, however, observed that the SGST portion of ₹20.07 lakh against the total provisional refund amount of ₹40.14 lakh was not credited to the claimant account till the date of audit (*i.e.,* 06 March 2021). Thus, the audited circle did not comply with the said provisions of the Act. Due to non-crediting of the SGST portion of refund amount and delay in processing of refund claim, the Circle would be liable to pay applicable interest of ₹2.40 lakh as per Section 56 of APGST Act.

On this being pointed out (March 2021), it was replied (September 2021) that payment advice was rejected by Treasury office and no report has been received from the treasury authorities in the matter so far. It is evident from the reply that the issue was not settled as of September 2021, *i.e.,* even after a lapse of about 31 months.

Government did not offer any remarks in their reply (July 2022).

(E) Issue of GST refund amounts without evidence regarding the endorsement in the case of the supply of goods made to Special Economic Zone (SEZ) units

As per Rule 89(1)(a) of APGST Rules, 2017, a supplier can claim refund for the services/ goods provided to a Special Economic Zone (SEZ) unit or a SEZ developer after such goods have been admitted for authorised operations as endorsed by the specified officer[36] of the zone. Further, as per Rule 89(2), application for refund claim should be made along with documentary evidence (*viz.,* a statement containing the

[36] As per rule 2 (zd) of SEZ Rules 2006, 'Specified Officer' in relation to a Special Economic Zone means Joint or Deputy or Assistant Commissioner of Customs for the time being posted in the Special Economic Zone

number and date of invoices relating to the goods/ services provided and a declaration made by the specified officer to the effect that tax has not been collected from the SEZ unit/ developer) to establish that a refund is due to the applicant.

During test check of 71 sampled refund claims (claim amount: ₹158.74 crore) pertaining to deemed exports and supplies to SEZ, Audit noticed in three circles[37] that 10 (14.08 *per cent*) refund claims (as detailed in ***Appendix - 2.8***) were processed (refund sanctioned: ₹63.75 crore) for deemed export and the supplies of goods/ services made to SEZ unit without payment of tax. On scrutiny of these refund files, Audit noticed that these refund claims were sanctioned without the requisite endorsement/ evidence as mandated under the above provisions.

On this being pointed out (December 2020 and January 2021), Government in the reply (July 2022) stated that in nine (out of 10) cases notices were issued to the taxpayers for documentary proof of relevant declarations. In one case of Chittoor-II circle, it was replied that the taxpayer furnished endorsement issued by the Specified Officer, Ongole. However, Audit could not verify and confirm the details due to non-furnishing of copy of endorsement with the reply.

2.1.11 Conclusion

Scrutiny of a sample of 560 refund claims (out of 6,534) pertaining to the period 01 July 2017 to 31 July 2020 relating to the State of Andhra Pradesh revealed that there were delays in both disposal of claims and sanctioning of provisional refunds. The department needs to ensure that causes for these delays are addressed as they go against the intended provisions of the Act to make available entitled flow of funds to the taxpayer for working/ operating capital. Post-audit of refund claims must be ensured to protect revenue leakage, as this was not done despite specific instructions. While streamlining the existing procedures of grant of refund, compliance to laid down procedures in processing of refund claims is to be ensured to prevent loss of revenue to the exchequer.

2.1.12 Recommendations

- There is a need to evolve a mechanism to ensure compliance with post-audit of refund claims in accordance with the instructions issued by the Department.
- The Department should evolve a mechanism to ensure compliance with the instructions about verification of invoices submitted and returns filed by the taxpayers with those declared in the refund application while sanctioning refund claim.
- The Department may consider making a suitable provision in the GST module for payment of interest in the cases of delay in disposal of refund claims.
- Looking into the size of sampled case (560) test-checked and number of cases (343) having deficiencies, Department may rigorously examine cases not covered in the audit sample and take corrective action within a timeframe.

[37] Chittoor – II, Gajuwaka and Steel Plant

During Exit Conference (February 2022), the Department stated that suitable instructions would be issued to circle level offices duly considering the audit observations/ recommendations.

2.2 Subject specific compliance audit on 'Transitional Credits' under GST

2.2.1 Introduction

Goods and Services Tax (GST) is a significant reform in the field of indirect taxes in our country, which replaced multiple taxes levied and collected by the Centre and States. GST is a destination-based tax on supply of goods or services or both, which is levied at multi-stages wherein the taxes will move along with supply. The tax will accrue to the taxing authority which has the jurisdiction over the place of supply. Tax is levied simultaneously by the Centre and States on a common tax base. Central GST (CGST) and State GST (SGST)/ Union Territory GST (UTGST) is levied on intra state supplies and Integrated GST (IGST) is levied on inter-state supplies. Availability of input tax credit of taxes paid on inputs, input services and capital goods for set off against the output tax liability is one of the key features of GST. This will avoid cascading effect of taxes and ensures uninterrupted flow of credit from the seller to buyer. To ensure the seamless flow of input tax from the existing laws to GST regime, a 'transitional arrangement for input tax' was included in the GST Acts to provide for the entitlement and manner of claiming input tax in respect of appropriate taxes or duties paid under existing laws. Transitional credit provisions are important for both the Government and business. For business, the transitional credit provisions ensure transition of accumulated credits from the legacy returns, input tax in respect of raw materials, work in progress, finished goods held in stock as on the appointed day[38] as well as credit in respect of capital goods into the GST regime. The provisions enable the taxpayer to transfer such input credits only when they are used in the ordinary course of business or furtherance of business.

2.2.2 Transitional arrangements for input tax-Legal provisions

Section 140 of APGST Act 2017, enables the taxpayer to carry forward the input tax credit (ITC) earned under the existing laws to the new GST regime. The section, read with Rule 117 of APGST Rules 2017, prescribes elaborate procedures in this regard. All registered taxpayers, except those who are opting for payment of tax under the composition scheme (under Section 10 of the Act), are eligible to claim transitional credit by filing GST Tran-1 return within 90 days from the appointed day. The time limit for filing Tran-1 return was extended initially till 27 December 2017. However, many taxpayers could not file the return within the due date due to technical difficulties. Hence, sub-rule 1A was inserted under Rule 117 of APGST Rules, 2017 vide G.O. Ms. No. 489 dated 25 September 2018, to accommodate such taxpayers. The due date for filing Tran-1 was further extended up to 31 March 2020, vide CCT order

[38] Appointed day is the day from which GST Act, 2017 came into force *i.e.,* from 01 July 2017

No. 01.2020-GST dated 18 February 2020, for those taxpayers who could not file Tran-1 due to technical difficulties and for those cases recommended by the GST Council. Under transitional arrangements for input tax credit (ITC), the ITC of various taxes paid under the existing laws such as Central Value Added Tax (CENVAT credit), State Value Added Tax (VAT) etc., can be carried forward to the GST regime.

Instances where taxes can be carried forward to the GST regime are detailed below.

a) **Closing balance of the credit in the last returns**: The closing balance of the CENVAT credit/ VAT credit available in the returns filed under existing law for the month immediately preceding the appointed day can be taken as credit in electronic credit ledger (ECL).

b) **Un-availed credit on capital goods**: The balance installment of un-availed credit on capital goods can be taken by filing the requisite declaration in GST Tran-1.

c) **Credit on duty paid stock**: A registered taxable person, other than the manufacturer or service provider, may take the credit of the duty/ tax paid on goods held in stock based on the invoices.

d) **Credit on duty paid stock when registered person does not possess the document evidencing payment of excise duty/ VAT**: For traders who do not have excise or VAT invoice, there is a mechanism to allow credit to them on the duty paid stock.

e) **Credit relating to exempted goods under the existing law which is now taxable**: Input tax credit of CENVAT/ VAT in respect of input, semi-finished and finished goods in stock attributable to exempted goods or services which are now taxable in GST.

f) **Input or input services in transit**: The input or input services received on or after the appointed day but the duty or tax on the same was paid by the supplier under the existing law.

g) **Tax paid under the existing law under composition scheme**: The taxpayers who had paid tax at fixed rate or fixed amount in lieu of tax payable under existing law, now working under normal scheme under GST can claim credit on their input stock, semi-finished and finished stock on the appointed date.

h) **Credit in respect of tax paid on any supply both under VAT Act and under Finance Act, 1994**: Transitional credit in respect of supplies which attracted both VAT and Service Tax under existing laws, for which tax was paid before appointed date and supply of which is made after the appointed date.

i) **Credit in respect of goods or capital goods belong to principal lying at the premises of the agent**: The agent can claim credit on such goods or capital goods subject to fulfilment of certain conditions.

The transitional credit is a one-time flow of input credit from the earlier regime into the GST regime, which can be availed both by the taxpayers migrating from the previous regime as well as new registrants under the GST regime.

2.2.3 Audit objectives

Audit of transitional arrangements for input tax credit under GST is taken up with for seeking an assurance on:

i. whether the mechanism envisaged by the Department for selection and verification of transitional credit claims was adequate and effective (Systemic issues) and
ii. whether the transitional credits carried over by the assessees into GST regime were valid and admissible (Compliance issues).

2.2.4 Audit scope and methodology

The period of coverage for the subject specific compliance audit was from the appointed day, *i.e.,* 01 July 2017 to 31 March 2020. There were a total of 14,086 transitional credit claim cases amounting to ₹387.58 crore processed till 31 March 2020 in 103 Circle offices under GST divisions in the State. Of these, 1,592 transitional credit claims from 97 Circles were sampled for scrutiny from the Pan India GST database. Subsequently, due to second phase of COVID pandemic, the sample was reduced to 563 claims in the 97 circles. The transitional credit amount involved in the sampled 563 cases was ₹204.83 crore. Verification of individual transitional credit claims involved examination of ITC credit claimed in the last six months returns filed by the taxpayers under the existing laws immediately preceding the appointed date, along with the documentary evidence in support of such claims. Further, in respect of input tax claimed for materials held in stock, verification involved examination of necessary accounting details, documents or records evidencing purchase of such goods.

Entry Conference was held with the representatives of the State Government in April 2021 wherein audit objectives, scope, criteria and methodology of audit were explained. Exit Conference was held in February 2022 to discuss audit findings included in the draft report. Responses of the Department have been suitably incorporated in the report.

2.2.5 Audit Criteria

The criteria against which the audit objectives are to be verified comprise of:

(i) Sections 140, 141 and 142 of APGST Act 2017, which contained transitional arrangement for ITC, job work and miscellaneous provisions;
(ii) Rules 117 and 121 of APGST Rules 2017, which envisaged procedures for claiming transitional credit, recovery of credit wrongly availed; and
(iii) Notifications/ circulars issued by Central Board of Indirect Taxes and Customs (CBIC) and State Tax Department from time to time.

Audit findings

The audit areas are based on the provisions of law and the mechanism envisaged by the Department for verification of the transitional credit claims of taxpayers. Audit areas are categorised corresponding to the two audit objectives as systemic and compliance issues respectively.

During scrutiny of the sampled 563 transitional credit claims, Audit observed deficiencies like non-issue of guidelines for verification of claims, irregular/ inadmissible claims due to non-furnishing of supporting documents/ non-considering the arrears under debt management unit (DMU)/ without filing requisite returns, claiming of transitional credit twice, non-levy of penalty/ interest, etc. A summary of the audit findings is given in **Table-2.2**.

Table-2.2: Summary of audit findings

(₹ in crore)

Sl. No.	Nature of audit observation	Audit sample		No. of deficiencies noticed		Deficiencies as percentage of sample	
		Number	Amount	Number	Amount	Number	Amount
	Systemic issues						
1	Absence of verification mechanism	563	204.83	563	-	-	-
2	Excess credit/ Non-reversal of excess claimed amount	563	204.83	2	0.07	-	-
	Compliance issues						
3	Excess carry forward of input tax credit (NCCF)	563	204.83	58	11.80	33.21	28.13
4	Excess carry forward of input tax credit (28 NCCF)			28	2.95		
5	Irregular availment of transitional credit on works contract service (irregular availment of TDS)			29	21.98		
6	Irregular availment of transitional credit without filing all the preceding six months VAT returns			23	14.14		
7	Irregular claim of disputed/ inadmissible credit			3	0.98		
8	Claiming of transitional credit under two categories/ availing twice as transitional credit as well as refund in VAT regime			4	0.48		
9	Inadmissible claim of transitional credit due to non-disclosure of pending statutory forms			28	2.68		
10	Irregular claim due to non-consideration of VAT/ CST demands and DMU arrears			14	2.60		
11	Non-levy of interest and penalty on the excess transitional claim repaid/ reversed by the dealers	563	204.83	28	2.74	NA	NA
12	Irregular claim of transitional credit on goods in stock without duty paid documents	44	2.17	9	0.92	20.45	42.40
13	Irregular claim of transitional credit on capital goods	3	0.10	2	0.01	66.67	10
14	Irregular claim of transitional credit in respect of Goods held on behalf of Principal	1	0.09	1	0.09	100.00	100

Audit observations are detailed in the subsequent paragraphs.

2.2.6 Systemic issues

2.2.6.1 Absence of Verification mechanism for transitional credit claims

Securing compliance to the transitional credit provisions and regulating the transitional credit claims of taxpayers constitutes a control risk. Rule 121 of APGST Rules, 2017, specifies that the amount claimed under transitional credit may be verified and recovery proceedings under Section 73 or 74 of APGST Act shall be initiated in respect of any credit wrongly availed, whether wholly or partly. CBIC issued a Guidance Note (March 2018) envisaging the procedure of verification of transitional credit. However, no such guidelines were issued by the authorities of State Tax department for verification of transitional credit claims.

During field audit, the Circle offices stated that no verification was done by them. Department provided details of verification of claims carried out by the Department only in January 2022. The information provided by the Department indicated that verification of claims was carried out in 5,101 (out of 12,982) cases. However, details about procedure followed in verification of these cases were not provided. Hence, Audit could not assess the effectiveness of verification.

In the Exit Conference (February 2022), the Department stated that there was no mechanism in GSTN for verification of transitional credit claims and the amounts claimed by taxpayers in Tran-1 were auto populated into their electronic credit ledger.

The reply is not acceptable as verification of transitional credit claims is to be done manually by checking pre-GST regime data as instructed by CBIC in its guidance note.

Thus, due to non-issuance of guidelines on verification of claims and non-providing of procedure followed in verification of claims, Audit could not assess the extent of compliance of provisions of Act/ Rules.

2.2.6.2 Incorrect credit in ECL in comparison to transitional credit returns figures

As per Section 140(1) of APGST Act, 2017, read with Rule 117 of APGST Rules, 2017, a registered person, other than a person opting to pay tax under Section 10, shall be entitled to take, in his electronic credit ledger (ECL), credit of the amount of VAT carried forward in the return relating to the period ending with the day immediately preceding the appointed day, furnished by him under the existing law in such manner as may be prescribed *i.e.,* filing the transitional credit returns.

(i) During the scrutiny of 563 sampled transitional credit claims, Audit noticed in Vizianagaram South circle that a dealer claimed ₹6.81 crore as transitional credit. It was, however, seen that an amount of ₹6.86 crore was erroneously populated in the dealer's ECL. This discrepancy allowed the dealer an excess transitional credit of ₹4.74 lakh which needs to be recovered.

On this being pointed out (August 2021), it was replied (August 2021) that rectification report would be submitted to Audit.

(ii) In another case in Chittoor-I circle, Audit observed that the taxpayer claimed ₹2.10 lakh under CGST and SGST which was reflected in his ECL. Subsequently, the taxpayer filed the revised Tran-1 in December 2017 claiming CGST as NIL and only SGST amount of ₹1.05 lakh. However, only excess SGST amount of ₹1.05 lakh was debited in his ECL and CGST amount of ₹2.10 lakh was not debited thereby resulting in excess claim to that extent.

On this being pointed out (August 2021), AC, Chittoor-I replied (August 2021) that due to technical glitches of the GST portal, the system was not updated and it was not a mistake on the part of the taxpayer and the question of payment of CGST amount of ₹2.10 lakh along with interest and penalty did not arise.

The reply is not acceptable as the CGST amount, erroneously allowed by the system to the taxpayer was required to be debited and since the taxpayer utilized the credit, interest was also to be recovered.

2.2.7 Compliance issues

The compliance issues pertain to the validity and admissibility of the transitional credits carried over by the assessees into GST regime. Taxpayers were required to claim transitional credits in the various specified tables of Tran-1[39] and Tran-2[40]. Audit observations relating to compliance with the provisions envisaged in the APGST Act and Rules relating to transitional credit are detailed below.

2.2.7.1 Irregular claim of transitional credit due to carry forward of excess ITC/ 28 NCCF[41]/ TDS

As per Section 140(1) of the Act, a registered person, other than a person opting to pay tax under Section 10, shall be entitled to take, in his ECL, credit of the amount of VAT carried forward in the return relating to the period ending with the day immediately preceding the appointed day, furnished by him under the existing law, in such manner as may be prescribed:

Provided that the registered person shall not be allowed to take credit in the following circumstances, namely: –

(i) where the said amount of credit is not admissible as ITC under this Act; or

(ii) where he has not furnished all the returns required under the existing law for the period of six months immediately preceding the appointed date.

During scrutiny of 563 sampled transitional credit claims, Audit noticed that inadmissible credit amounting to ₹36.73 crore was availed in 115 claims pertaining to 45 circles involving cases of (i) carry forward of net credit in excess than available,

[39] Tran-1 is a return to be filed by taxpayers to claim the credit of tax paid under legacy rules

[40] Tran-2 is a return to be filed by taxpayers to claim the credit of tax paid under legacy rules, if tax paid documents are not available

[41] After bifurcation of Andhra Pradesh state into AP and Telangana from 2 June 2014, state codes were changed to 36 and 37 from 28. Credit pertaining to the period before 2 June 2014 is termed as 28 NCCF

(ii) availing 28 NCCF as GST transitional credit and (iii) availing tax deducted at source (TDS) as ITC in Tran-1 as detailed below:

a) Carry forward of net credit (NCCF) in excess than available: Audit noticed in 58 transitional credit claims (***Appendix - 2.9***) amounting to ₹11.80 crore relating to 34 circles[42], the dealers availed excess credit than that available under NCCF as per VAT 200[43] return/ dealer's ledger (DCB[44]) for the month of June 2017.

On this being pointed out (between July and September 2021), Government in the reply (July 2022) accepted audit observation in 35 cases[45] having money value of ₹3.46 crore and stated that notices/ demands have been issued/raised. Of these an amount of ₹35.81 lakh was collected/ partially collected. Further stated that:

- In four cases (Bhavanipuram, Kasibugga, Puttur and Rajam circles), the taxpayers filed appeals and were pending at appellate authority.
- In five cases (Dwarakanagar, Gajuwaka (three cases) and Patamata circles), the taxpayers claimed amount as per DCB registers. Further, the Hon'ble High Court of Telangana, in a similar case, has allowed writ petition.

The reply is not acceptable as the DCB will take care of credit in the cases of revised returns only and in other cases of change in ITC due to other reasons, without adjustment orders the DCB would not reflect accurate status. Further, audit observations were made duly verifying the DCB and Tran-1. Regarding Telangana High Court case, it was on different issue (*viz.,* availing credit under 28 NCCF) and not on credit of excess tax paid.

- In two cases of Nandyal-I and Parvathipuram, it was replied that the cases were referred to Central authorities as the taxpayers are under central jurisdiction.

The reply is not acceptable as SGST portion of Tran-1 has to be verified by the State authorities as Central authorities have no records relating to VAT credit.

- In one case of Daba Gardens circle, it was replied that due to different specifications in different situations of different acts, credit of last return for the month of June 2017 and ITC of Tran-1 are not correlated.

The reply is not acceptable since, details mentioned in Tran-1 are to be verified by the Department to ensure the correctness of credit transitioned.

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[42] Addanki, Adoni-I, Anakapalli (2 cases), Bhavanipuram, Chilakaluripet, Chinawaltair (5 cases), Daba Gardens (7 cases), Dwarakanagar (2 cases), Eluru, Gajuwaka (3 cases), Gudur (2 cases), Indrakeeladri, Kasibugga, Kavali, Krishnalanka, Kurnool-I, Kurupam Market (2 cases), Madanapalli, Mandapeta, Mangalagiri, Nandyal-I, Nellore-III, Parvathipuram (2 cases), Patamata (4 cases), Peddapuram, Piduguralla, Puttur (2 cases), Rajam, Ramachandrapuram, Steel Plant (3 cases), Suryabagh, Tirupati-II (2 cases), Vizianagaram West and Vizianagaram South

[43] Monthly VAT return

[44] Demand collection balance register, a register showing input tax credit, output tax liability, payment particulars and balance credit

[45] Addanki, Adoni, Anakapalli (2 cases), Chinawaltair (5 cases), Dwarakanagar, Eluru, Gudur, Indrakeeladri, Kavali, Krishnalanka, Kurnool, Kurupam Market (2 cases), Madanapalli, Mandapeta, Mangalagiri, Nandyal-I, Nellore-III, Parvathipuram, Patamata (3 cases), Peddapuram, Piduguraalla, Puttur, Ramachandrapuram, Steel Plant (2 cases), Vizianagaram South and Vizianagaram West

- In one case of Tirupati-II circle, it was replied that verification for transitional credit was done electronically by the system.

The reply indicates that no verification of supporting documents was done to ensure the correctness of amount claimed by the taxpayer in Tran-1.

- In one case of Chilakapurpet circle, it was replied that the refund claimed by the taxpayer was allowed as transitional credit.

The reply is not acceptable. As per Section 142(8)(b) of APGST Act, the excess ITC due to the taxpayer as per assessment order pertaining to VAT regime is to be refunded in cash only.

Six cases of Daba Gardens (four cases), Steel Plant and Suryabagh circles were not finalised and in three cases of Daba Gardens (two cases) and Tirupati circles specific reply was not furnished.

b) **Availing 28 NCCF as GST transitional credit:** As per instructions issued by Commissioner of Commercial Taxes vide CCTs Ref. No. AI(1)/12/2014 dated 28 July 2015, if for any reason, 28 NCCF is not availed by the end of March 2016, then the same would be quantified and refunded as per the request of the dealer on conducting refund audit.

Though there were clear instructions of CCT regarding the utilisation and availment of 28 NCCF, Audit noticed in 28 transitional credit cases in 10 circles[46], the dealers claimed 28 NCCF amounting to ₹2.95 crore as transitional credit contrary to CCT instructions. This had resulted in irregular availment of transitional credit of ₹2.95 crore as detailed in ***Appendix - 2.10***.

On this being pointed out (between July and September 2021), Government in the reply (July 2022) accepted audit observations in 22 cases[47] having money value of ₹2.08 crore. In three cases of Brodipet and Rajam (two cases) circles, the taxpayers preferred appeal and were pending at appellate authority.

In two cases of Brodipet and Dwarakanagar circles, Government replied that as per DCB register the credit was allowed and further stated that Hon'ble High Court of Telangana, in a similar case, allowed writ petition. In the case of Chilakaluripet circle, it was stated that there was no excess claim in Tran-1.

The replies are not acceptable as per the CCT instructions above, after March 2016, 28 NCCF was allowed only as refund under VAT regime. Hence, availing the amounts as transitional credit is not in order.

During Exit Conference (February 2022), the Department agreed that claiming transitional credit on the basis of balance accrued due to 28 NCCF was against the

[46] Addanki (15 cases), Anakapalli (3 cases), Brodipet (2 cases), Chilakaluripet, Chinawaltair, Dwarakanagar, Ibrahimpatnam, Mangalagiri, Piduguralla and Rajam (2 cases)

[47] Addanki (15 cases), Anakapalli (3 cases), Chinawaltair, Ibrahimpatnam, Mangalagiri and Piduguralla

statutory provisions since the same could be claimed as refund or adjusted to the outward tax liability of the dealer.

c) Availing tax deducted at source (TDS) as ITC in Tran-1: As per Section 140(1) of the Act, a registered person, other than a person opting to pay tax under Section 10, shall be entitled to take, in his ECL, credit of the amount of VAT carried forward in the return relating to the period ending with the day immediately preceding the appointed day, furnished by him under the existing law, in such manner as may be prescribed.

As per Section 22(3) of APVAT Act, the Central Government or the State Government or an industrial, commercial or trading undertaking of the Central Government or of the State Government or a local authority or a statutory body or a company registered under the Companies Act, 1956 or any other person notified by the Commissioner, shall deduct from out of the amounts payable by them to a dealer in respect of works contract executed for them, an amount calculated at such rate as may be prescribed and such contractee deducting tax at source shall remit such amount in the manner prescribed.

Further, there is no procedure to claim TDS credit as no table is provided in transitional credit returns for claiming such credit.

During scrutiny of 563 sampled transitional claims, Audit observed in 29 claims pertaining to 17 circles[48] that the dealers had claimed TDS amounts of ₹21.98 crore (as detailed in ***Appendix-2.11***) under Tran-1 contrary to the above stipulations.

On this being pointed out (between July and September 2021), Government in the reply (July 2022) accepted the audit observations in 10 cases[49] having money value of ₹1.80 crore. Of this an amount of ₹8.81 lakh has been collected. Further stated that:

- In one case relating to Proddutur circle, the taxpayer filed appeal and was pending at appellate authority.
- In two cases of Gudur and Mangalagiri circles, it was replied that the cases were referred to Central authorities as the taxpayers are under central jurisdiction.

The reply is not acceptable as SGST portion of Tran-1 has to be verified by the State authorities as Central authorities have no records relating to VAT credit.

- In one case of Kadapa-I, it was stated that the AC (LTU), DC office, Kadapa conducted audit for the tax period from April 2015 to June 2017 and passed assessment orders vide AO No.196128, dated 11 February 2020 and allowed ITC in Tran-1 for ₹5.66 crore from the excess credit as on 30 June 2017.

The reply is not acceptable since, as per Section 142(8)(b) any excess credit due to the assessment order pertaining to VAT regime is to be refunded in cash only.

[48] Alcot Gardens, Anakapalli, Autonagar, Benz Circle, Bhavanipuram, Chinawaltair (4 cases), Daba Gardens (2 cases), Dwarakanagar (3 cases), Gajuwaka (2 cases), Gudur, Kadapa-I (3 cases), Mangalagiri, Nellore-I, Nuzividu, Proddutur-I, Sitharampuram and Steel Plant (4 cases)

[49] Benz Circle, Chinawaltair (3 cases), Kadpa-I, Nellore-I, Nuzividu and Steel Plant (3 cases)

- In the remaining 10 cases[50], Government justified their action on the reasons like claim was in order, allowed as per DCB register, the taxpayer had excess credit as per assessment, etc. Further stated that Hon'ble High Court of Telangana, in a similar case, allowed writ petition.

The reasons mentioned are not acceptable as Section 140 (1) of the APGST Act allowed the credit amount of VAT as carried forward in the return relating to the period ending with the day immediately preceding the appointed day. TDS credit is not included in the VAT return. Hence, allowing the credit is not in order. Regarding Telangana High Court case, it was on different issue (*viz.,* availing credit under 28 NCCF) and not on credit of TDS.

During the Exit Conference (February 2022), the Department stated that standard guidelines would be issued to field offices on interpretation of various judgements pertaining to transitional credit claims.

Four cases relating to Anakapalli, Daba Gardens, Dwarakanagar and Steel Plant circles were not finalised and in one case of Gajuwaka circle specific reply was not furnished.

2.2.7.2 Inadmissible claim of transitional credit due to non-disclosing of pending statutory forms

As per Section 140(1) of the Act, a registered person, other than a person opting to pay tax under Section 10, shall be entitled to take, in his ECL, credit of the amount of VAT carried forward in the return relating to the period ending with the day immediately preceding the appointed day, furnished by him under the existing law, in such manner as may be prescribed:

Provided that the registered person shall not be allowed to take credit in the following circumstances namely: –

(i) where the said amount of credit is not admissible as ITC under this Act; or

(ii) where he has not furnished all the returns required under the existing law for the period of six months immediately preceding the appointed date.

Provided further that so much of the said credit as is attributable to any claim related to Sections 3, 5, 6 and 8 of Central Sales Tax 1956, must be filed for the period 01 April 2015 to 30 June 2017. As per Table 5(c) of Form GST Tran-1, the dealer must declare turnover together with the applicable tax thereon voluntarily for which the statutory forms *viz.,* 'C' (for inter-state sales), 'E' (for transfer of documents of title of goods from one state to another), 'F' (for transfer of goods to other State other than by way of sale) and 'H' (for sale or purchase of goods taken place in the course of import/ export) are pending. The portion of ITC for which requisite declaration forms are not submitted shall not be eligible and such amount of ineligible credit shall not be credited to ECL.

[50] Alcot Gardens, Autonagar, Bhavanipuram, Chinawaltair, Daba Gardens, Dwarakanagar (2 cases), Gajuwaka, Kadapa-I and Sitharampuram

Further, as per Section 142(8)(b) of APGST Act, 2017 the credit should be refunded in cash only and not allowed as transitional credit.

During scrutiny of 563 sampled transitional credit claims, Audit observed in 28 claims of 16 circles[51] that the transitional credit amounting to ₹2.68 crore was credited in the ECLs of the respective dealers, despite pending submission of statutory forms. Claiming credit in Tran-1 despite non-submission of requisite forms was contrary to the provisions of the Act. Availing credit in these cases resulted in inadmissible transitional credit of ₹2.68 crore as detailed in ***Appendix - 2.12***.

On this being pointed out (between July and September 2021), Government in the reply (July 2022) accepted/ partially accepted audit observation in 16 cases[52] having money value of ₹1.08 crore. Further stated that:

- In three cases of Dwarakanagar, Lalapet and Rajam circles the taxpayers filed appeals and were pending at appellate authority.
- In two cases of Gajuwaka circle, it was stated that the taxpayers declared all the details in Tran-1/ paid the tax amount. In two cases of Puttur circle, Government stated that the taxpayers adjusted/ paid the amounts.

The reply is not acceptable as in the cases of Gajuwaka circle the taxpayers did not mention any amount relating to pending statutory forms in Tran-1. Further, though the taxpayers paid the tax, claiming credit without disclosing the details was contravention to Rule 140(1) of APGST Rules.

- In the case of Steel Plant circle, Government stated that the Assessing Authority finalised (March 2020) the assessment and levied tax of ₹3.31 lakh.

The reply is not acceptable as the taxpayer though declared pending tax (₹4.98 lakh) on 'C' forms, availed full ITC credit of ₹54.29 lakh without reducing pending tax amount which was not in order. Further, the reply is silent about adjustment of excess availed amount of ₹1.67 lakh (₹4.98 lakh - ₹3.31 lakh) by the taxpayer.

In three cases of Dwarakanagar, Gajuwaka and Patamata circles, relevant details/ specific reply was not furnished and one case of Daba Gardens was not finalised.

2.2.7.3 Irregular claim of transitional credit due to non-consideration of VAT/ CST demands and DMU arrears

As per Section 142(8)(b) of the APGST Act, 2017, where in pursuance of an assessment or adjudication proceedings instituted, whether before, on or after the appointed day under the existing law, any amount of tax, interest, fine or penalty becomes refundable

[51] Anakapalli (2 cases), Chinawaltair, Daba Gardens, Dwarakanagar (2 cases), Gajuwaka (3 cases), Kasibugga, Kurupam Market (2 cases), Lalapet, Narasannapeta (2 cases), Patamata (2 cases), Piduguralla, Puttur (2 cases), Rajam, Srikakulam, Steel Plant (3 cases) and Suryabagh (3 cases)

[52] Anakapalli (2 cases), Chinawaltair, Kasibugga, Kurupam Market (2 cases), Narasannapeta (2 cases), Patamata, Pidiguralla, Srikakulam, Steel Plant (2 cases) and Suryabagh (3 cases)

to the taxable person, the same shall be refunded to him in cash under the said law and the amount rejected, if any, shall not be admissible as input tax credit under this Act.

During scrutiny of 563 sampled transitional credit claims, Audit noticed in 14 claims (pertaining to the period from June 2014 to June 2017) relating to 12 circles[53] that the dealers had claimed the transitional credit amounting to ₹2.60 crore despite pendency of VAT/ CST assessment demands/ arrears accounted for under debt management unit (DMU) or adjudication proceedings. As per Section 142(8)(b) *ibid* the same should be claimed as refund. Non-compliance with the provisions had resulted in irregular claiming of transitional credit of ₹2.60 crore as detailed in ***Appendix - 2.13***.

On this being pointed out (between July and September 2021), Government in the reply (July 2022) accepted audit observation in 11 cases having money value of ₹78.50 lakh. Of this, an amount of ₹3.85 lakh has been collected. In two cases of Parvathipuram and Srikakulam circles, it was stated that the taxpayers filed appeals and were pending at appellate authority. In one case relating to Daba Gardens circle, specific reply for availing credit despite having arrears to be payable was not furnished.

2.2.7.4 Irregular claim of transitional credit without filing VAT 200A/ 200B returns by taxpayers selling exempted goods

As per the provision under Section 140(1) of APGST Act, 2017, the registered person shall not be allowed to take credit in the following circumstances namely: –

(i) where the said amount of credit is not admissible as input tax credit under this Act; or

(ii) where he has not furnished all the returns required under the existing law for the period of six months immediately preceding the appointed date.

Further, as per Rule 20(6) of APVAT Rules, where any VAT dealer making taxable as well as exempted sales, is able to establish that specific inputs are meant for specific output, the input tax credit can be claimed separately for taxable goods. For the common inputs, such VAT dealer can claim ITC by applying the formula A x B/C[54] for the common inputs used for taxable goods, exempt goods (goods specified in Schedule-I of APVAT Act) and exempt transactions.

Provided the VAT dealer furnishes an additional return in Form VAT 200A (monthly) for each tax period for adjustment of ITC and by filing a return in Form VAT 200B (Annual) by making an adjustment for the period of 12 months ending March every year.

During scrutiny of 563 sampled transitional credit claims, Audit noticed in 20 claims pertaining to 11 circles[55] (as detailed in ***Appendix-2.14***) that the VAT dealers had

[53] Anakapalli (2 cases), Benz Circle, Chinawaltair, Daba Gardens, Dwarakanagar, Kurupam Market, Ongole-II, Parvathipuram, Srikakulam, Steel Plant (2 cases), Suryabagh and Vizianagaram West

[54] A: Total amount of input tax for common inputs for each tax rate excluding the tax paid on the purchase of goods; B: Sales turnover of taxable goods including zero-rated sales; C: Total turnover including sales of exempt goods

[55] Benz Circle, Chinawaltair (2 cases), Daba Gardens (4 cases), Dwarakanagar (2 cases), Kurupam Market, Patamata, Puttur (2 cases), Rajam, Steel Plant (2 cases), Suryabagh (2 cases) and Tirupati-II (2 cases)

availed the transitional credit in spite of non-filing of the mandatory VAT 200A/ 200B returns. This has led to incorrect allowance of transitional credit of ₹13.94 crore.

On this being pointed out (between July and September 2021), Government in their reply (July 2022) accepted/ partially accepted audit observation in 10 cases[56] having money value of ₹4.12 crore.

In three cases of Puttur (two cases) and Tirupati-II circles, Government contested that there was no need to file VAT 200B returns since there were no exempt sale transactions.

The reply is not acceptable as there were exempt sales along with taxable sales as observed from monthly VAT 200A returns; hence it is requisite to file consolidated annual VAT 200B return as per Rule 20 of APVAT Rules.

In six cases[57] specific reply was not furnished and one case relating to Daba Gardens circle was not finalised.

2.2.7.5 Inadmissible transitional credit due to non-furnishing of supporting invoices/ documents

The credit of eligible duties paid in respect of inputs, semi-finished goods or finished goods held in stock on the appointed day is permissible under the following situations:

a) As per Section 140(3)(iii) of the APGST Act, 2017, a registered person, who was not liable to be registered under the existing law or who was engaged in the sale of exempted goods, or tax free goods or goods which have suffered tax at the first point of their sale in the State and the subsequent sales of which are not subject to tax in the State under the existing law but which are liable to tax under this Act or where the person was entitled to the credit of input tax at the time of sale of goods, if any, shall be entitled to take, in his ECL, credit of the VAT in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock on the appointed day subject to condition that the said registered person is in possession of invoice or other prescribed documents evidencing payment of tax under the existing law in respect of such inputs;

b) As per Section 140(4)(b) of the Act, a registered person who was engaged in the sale of taxable goods as well as exempted goods or tax-free goods under the existing law but which are liable to tax under this Act, shall be entitled to take, in his ECL the amount of credit of the VAT in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock on the appointed day.

[56] Chinawaltair (2 cases), Dwarakanagar, Kurupam Market, Patamata, Rajam, Steel Plant (2 cases) and Suryabagh (2 cases)

[57] Benz Circle, Daba Gardens (3 cases), Dwarakanagar and Tirupati-II

c) In the cases where a registered person either paying tax at fixed rate or paying a fixed amount in lieu of tax payable under the existing law as per Section 140(6) of the Act.

Further, Table 7(b)–eligible duties and taxes/ VAT in respect of inputs in transit and 7(c)-VAT paid on inputs in stock, of the Tran-1 return captures the transitional credit in respect of such goods held in stock as on the appointed day for which supporting documents are available with the taxpayers.

During scrutiny of 44 claims falling under 7b/ 7c category of transitional credit claims, out of 563 sample cases, Audit noticed in nine claims of seven circles[58] that the dealers had claimed ₹92.10 lakh (as detailed in ***Appendix - 2.15***) under Table 7(b)/ 7(c) of Tran-1 form and the same was credited in the ECL of the taxpayers. However, the relevant invoices/ documents for the stock/ inputs held/ in transit were not made available to audit for verification. Allowing the ITC on stock inputs without verification of supporting invoices by the departmental authorities is contrary to the provisions of the Act. This had resulted in irregular availment of transitional credit amounting to ₹92.10 lakh.

On this being pointed out (between July and September 2021), Government in the reply (July 2022) accepted audit observation in six cases[59] having money value of ₹69.43 lakh.

In one case of Tirupati-II circle, it was replied that verification for transitional credit was done electronically.

The reply indicates that no verification of supporting documents was done to ensure the correctness of amount claimed by the taxpayer in Tran-1.

Two cases pertaining to Daba Gardens circle were not finalized.

2.2.7.6 Irregular claim of transitional credit on capital goods

As per Section 140(2) of APGST Act, 2017, a registered person, other than a person opting to pay tax under Section 10, shall be entitled to take, in his ECL, credit of unavailed ITC in respect of capital goods, not carried forward in a return furnished under the existing law by him, for the period ending with the day immediately preceding the appointed day in such manner as may be prescribed.

Provided that the registered person shall not be allowed to take credit unless the said credit was admissible as ITC under the existing law and is also admissible as ITC under this Act.

Explanation contained in the Act to the above provision clarifies that the expression 'unavailed ITC' means the amount that remains after subtracting the amount of ITC already availed in respect of capital goods by the taxable person under the existing law

[58] Daba Gardens (2 cases), Dwarakanagar, Nellore-II, Patamata, Sattenapalli, Sitharampuram and Tirupati-II (2 cases)

[59] Dwarakanagar, Nellore, Patamata, Sattenapalli, Sitharampuram and Tirupati-II

from the aggregate amount of ITC to which the said person was entitled in respect of the said capital goods under the existing law.

Further as per Rule 117(2) of APGST Rules, 2017, a taxpayer claiming unavailed credit on capital goods shall submit separately the particulars of amount of tax availed or utilised and yet to be availed in respect of capital goods.

During the scrutiny of three transitional credit claims where taxpayers claimed the unavailed credit on capital goods, out of total 563 sample cases, Audit noticed in two claims of two circles[60] that the dealers had claimed the unavailed credit on capital goods amounting to ₹1.32 lakh in table 6(b) of Tran-1. However, the dealers did not submit the declaration of credit availed and yet to be availed which is contrary to the provisions of APGST Act 2017. In the absence of relevant details, Audit could not ensure that the claim was made in accordance with the provisions.

On this being pointed out (August 2021), AC, Steel Plant circle replied (August 2021) that the audit observation was verified with reference to Tran-1 claim and notice was issued to the taxpayer. Reply from AC, Puttur circle is awaited (August 2022). Government did not furnish any remarks in their reply (July 2022).

2.2.7.7 Non-levy of interest and penalty on the excess transitional claim repaid/ reversed by the dealers

As per Section 50(3) of the APGST Act, 2017, a taxable person who makes an undue or excess claim of input tax credit under sub-section (10) of Section 42 or undue or excess reduction in output tax liability under sub-section (10) of Section 43, shall pay interest on such undue or excess claim or on such undue or excess reduction, as the case may be, at such rate not exceeding 24 *per cent*, as may be notified by the Government on the recommendations of the Council.

Further, as per Section 73, penalty is leviable for any reason other than fraud or willful misstatement or suppression of facts to evade tax. Penalty equivalent to 10 *per cent* of tax or ₹10,000, whichever is higher, due from such person is to be levied subject to condition that if he had not paid the excess tax availed along with interest within 30 days from the issue of notice.

As per Section 74, penalty is leviable for the reason of fraud or willful misstatement or suppression of facts to evade tax; in the case of voluntary payment penalty equivalent to 15 *per cent* of such tax on the basis of his own ascertainment of such tax or the tax as ascertained by the proper officer; else the taxpayer pays the said tax along with interest and a penalty equivalent to 25 *per cent* of such tax within 30 days of issue of the notice, all proceedings in respect of the said notice shall be deemed to be concluded.

During scrutiny of 563 sampled transitional credit claims, Audit noticed in 23 claims relating to 17 circle[61] offices that the dealers have reversed the excess claimed amounts.

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[60] Puttur and Steel Plant

[61] Ananthapuramu-II, Benz Circle, Chittoor-I, Daba Gardens (2 cases), Gajuwaka (2 cases), Gandhi Chowk, Gudur, Krishnalanka, Nandyal-II, Nellore-I, Patamata (2 cases), Patnam Bazar, Puttur, Srikakulam, Steel Plant (4 cases), Suryabagh and Tirupati-II

In five cases relating to Ongole-I circle the authorities issued (April 2021) notices under Section 73 for reversal of excess claimed ITC of ₹11.98 lakh without levying penalty/ interest. Of these 28 claims (as detailed in ***Appendix - 2.16***), in 24 claims, applicable penalty of ₹2.74 crore was not levied/ paid under the relevant provisions 73 and 74 of APGST Act, 2017. In 16 claims, though dealers have already utilised the excess transitional amount claimed, the applicable interest has also not been levied on the taxpayers.

On this being pointed out (between July and September 2021), Government in the reply (July 2022) accepted audit observation in 14 cases[62] having money value of ₹25.18 lakh (excluding interest) and an amount of ₹27.91 lakh (including interest) has been recovered in three cases[63]. Further stated that:

- In four cases relating to Ongole-I circle, the taxpayers filed appeals and were pending at appellate authority.
- In two cases of Patamata and Srikakulam circles quoted the judgement of Hon'ble High Court of Patna and stated that interest cannot be recovered on mere availment of ITC. In two cases of Suryabagh and Tirupati-II circles, it was replied that the dealers have reversed the credit before utilisation and hence penalty and interest is not leviable.

The reply is not acceptable as in one case (Suryabagh circle) though the credit was not utilised, penalty at 10 *per cent* was leviable as the amount was not reversed within 30 days period as envisaged in the provisions and in the other three cases it was noticed from the ECL that the dealers had not only utilised the excess ITC claimed through Tran-1 but also reversed the amount after the stipulated period of 30 days. Hence, interest and penalty are to be levied as per the provisions of the Act.

In four cases of Benz Circle, Krishnalanka, Patamata and Steel Plant circles, specific reply was not furnished and two cases of Daba Gardens circle were not finalised.

2.2.7.8 Miscellaneous issues

(A) Claiming of transitional credit without filing of preceding six months returns

As per Section 140(1) of APGST Act, 2017, a registered person, other than a person opting to pay tax under Section 10, shall be entitled to take, in his ECL, credit of the amount of VAT carried forward in the return relating to the period ending with the day immediately preceding the appointed day, furnished by him under the existing law, in such manner as may be prescribed:

Provided that the registered person shall not be allowed to take credit in the following circumstances namely: –

[62] Ananthapuramu-II, Chittoor-I, Gajuwaka (2 cases), Gandhi Chowk, Gudur, Nandyal-II, Nellore-I, Patnam Bazar, Puttur, Ongole-I and Steel Plant (3 cases)

[63] Ananthapuramu-II: ₹24.04 lakh; Nandyal-II: ₹0.32 lakh and Nellore-I: ₹3.55 lakh

(i) where the said amount of credit is not admissible as input tax credit under this Act; or (ii) where he has not furnished all the returns required under the existing law for the period of six months immediately preceding the appointed date.

During the scrutiny of 563 sampled transitional credit claims, Audit noticed in three claims in three circles[64] (as detailed in ***Appendix - 2.17***) that the dealers had claimed the transitional credit without filing the monthly returns consecutively during the six months immediately preceding the appointed date. This had resulted in irregular allowance of transitional credit amounting to ₹20.12 lakh.

On this being pointed out (between July and September 2021), Government in the reply (July 2022) accepted the audit observation in all the cases. Of this, an amount of ₹6.36 lakh has been collected in one case (Patamata circle). In the case of Kakinada circle demand has been raised for ₹8.37 lakh and in the remaining case (Kurupam Market circle) notice was issued to the taxpayer.

(B) Irregular claim of disputed/ inadmissible credit

As per Section 142(8)(a) of APGST Act, 2017, where in pursuance of an assessment or adjudication proceedings instituted, whether before, on or after the appointed day under the existing law, any amount of tax, interest, fine or penalty becomes recoverable from the taxable person, the same shall be recoverable as an arrear of tax and the amount so recovered shall not be admissible as input tax credit under this Act.

During scrutiny of 563 sampled transitional credit claims, Audit observed in three cases pertaining to three circles[65] that though there were disputed cases involving tax amount of ₹98.20 lakh (as detailed in ***Appendix - 2.18***), the dealers had carried forward the same as transitional credit and utilised the amount which was contrary to the provisions of Act.

On this being pointed out (between July and August 2021), Government in the reply (July 2022) accepted the audit observation in all the three cases and stated that notices have been issued to the taxpayers. Of these, one case of Rajam circle was pending at appellate authority.

(C) Irregular claim of transitional credit due to non-disclosing details of goods held by agent on behalf of the principal

As per Section 142(14) of APGST Act, 2017, where any goods or capital goods belonging to the principal are lying at the premises of the agent on the appointed day, the agent shall be entitled to take credit of the tax paid on such goods or capital goods subject to fulfilment of the following conditions: -

(i) the agent is a registered taxable person under this Act

(ii) both the principal and the agent declare the details of stock of goods or capital goods lying with such agent on the day immediately preceding the appointed

[64] Kakinada, Kurupam Market and Patamata
[65] Daba Gardens, Kurupam Market and Rajam

day in such form and manner and within such time as may be prescribed in this behalf

(iii) the invoices for such goods or capital goods had been issued not earlier than 12 months immediately preceding the appointed day and

(iv) the principal has either reversed or not availed of the input tax credit in respect of such

(a) goods; or

(b) capital goods or, having availed of such credit, has reversed the said credit, to the extent availed of by him.

During scrutiny of one case pertaining to Anakapalli circle, where the taxpayer claimed the credit on goods held in stock on behalf of principal, Audit noticed that the dealer had claimed ₹9.26 lakh under 10(a) category of Tran-I. However, registration details of the principal were not disclosed. Further, declaration about non-availment of ITC by principal to the extent of claim amount was also not on record. In the absence of the declaration, Audit could not verify the correctness of the claim.

On this being pointed out (August 2021), AC, Anakapalli circle replied (August 2021) that the matter would be examined and detailed reply would be submitted in due course. Government did not furnish any remarks in their reply (July 2022).

(D) Claiming of transitional credit twice in Tran-1

As per Section 140(1) of APGST Act, 2017, read with Rule 117 of APGST Rules, 2017, a registered person, other than a person opting to pay tax under Section 10, shall be entitled to take, in his ECL, credit of the amount of VAT carried forward in the return relating to the period ending with the day immediately preceding the appointed day, furnished by him under the existing law in such manner as may be prescribed. Further, as a general principle, ITC should not be availed twice on the same documents.

During the scrutiny of 563 sampled transitional credit claims, Audit noticed in three claims of three circles[66] (as detailed in ***Appendix - 2.19***) that the ITC was claimed in Table-5(c) –'Amount of tax credit carried forward to electronic credit ledger as State/ UT tax' and the same amount was also claimed under Table-7(c) –'Amount of VAT and Entry Tax paid on inputs supported by invoices/ documents evidencing payment of tax carried forward to electronic credit ledger as SGST/ UTGST under sections 140(3), 140(4)(b) and 140(6)'. Thus, claiming of transitional credit in both Table-5(c) and Table-7(c) had resulted in excess credit of ₹28.35 lakh.

On this being pointed out (between August and September 2021), Government accepted (July 2022) audit observation in two cases of Chittoor-II and Suryabagh circles having money value of ₹26.78 lakh and stated that notices have been issued to the taxpayers. In the remaining case (Dwarakanagar), specific reply for availing the credit twice was not furnished.

[66] Chittoor-II, Dwarakanagar and Suryabagh

(E) Availing Input Tax Credit (ITC) twice through Tran-1 and by claiming as refund

As per Section 74(1) of APGST Act, 2017, where it appears to the proper officer that any tax has not been paid or short paid or erroneously refunded or where ITC has been wrongly availed or utilised by reason of fraud, or any willful - misstatement or suppression of facts to evade tax, he shall serve notice on the person chargeable with tax which has not been so paid or which has been so short paid or to whom the refund has erroneously been made, or who has wrongly availed or utilised ITC, requiring him to show cause as to why he should not pay the amount specified in the notice along with interest payable thereon under Section 50 and a penalty equivalent to the tax specified in the notice.

During scrutiny of 563 sampled transitional credit claims, Audit noticed in one claim pertaining to Ramachandrapuram circle that the dealer had claimed (December 2017) and availed credit of ₹20.26 lakh through Tran-1 for the available balance of ITC to the end of June 2017. Further, the dealer had claimed an amount of ₹21.55 lakh as refund for the period April 2017 to June 2017 and an amount of ₹20.12 lakh was sanctioned (August 2020) by the circle and paid (April 2021) to the dealer. However, as the credit availed through Tran-1 covered the period April 2017 to June 2017 sanctioning the refund claim was irregular. This had resulted in availing of ITC twice through Tran-1 and by claiming as refund. The excess paid amount of ₹20.12 lakh is to be recovered along with applicable penalty and interest.

On this being pointed out (August 2021), AC, Ramachandrapuram circle replied (February 2022) that notice was issued to the dealer for payment of amount pointed out by Audit. Government did not furnish any remarks in their reply (July 2022).

2.2.8 Conclusion

The State Tax Department had not issued any guidelines to verify transitional credit claims for ascertaining correctness of claims preferred by the taxpayers. Audit scrutiny showed instances of excess availment of ITC due to non-verification of transitional credit claims thereby giving scope for passing undue benefit to the taxpayers while claiming transitional credit. Non-compliance issues like availing credit in excess than available balance, claiming of credit without supporting invoices, non-disclosing details of goods held by agent on behalf of the principal, irregular claim of credit due to non-consideration of VAT/ CST demands, claiming of transitional credit twice, etc., were also observed during audit of sampled claims. Penalty and applicable interest were not levied/ paid in certain cases of excess credit availed by the taxpayers.

2.2.9 Recommendations

- Government should evolve a mechanism and issue suitable instructions to verify all the transitional credits availed by the dealers in the State for ensuring correctness of the credit availed.
- Government should take suitable action as per the provisions of the Act in the cases of availment and utilisation of excess credit by the dealers.

- Looking into the size of sampled claim (563) test-checked and number of excess/ incorrect claims noticed (227), Department may rigorously examine cases not covered in audit sample and take corrective action within a timeframe. A database of such cases may also be maintained to monitor/ rectify the same.
- Initiate remedial measures for the compliance deviations pointed out during this audit before the claims become time barred.

During Exit Conference (February 2022), the Department stated that suitable instructions would be issued to circle level offices duly considering the audit observations/ recommendations made in the report.

2.3 Value Added Tax

2.3.1 Under-declaration of tax due to application of incorrect rate of tax

Declaration of tax at the rate of five *per cent* by the dealers on the commodities taxable at the rate of 14.5 *per cent* had resulted in under-declaration of tax leading to short levy of VAT of ₹3.59 crore.

As per Section 4(1) of Andhra Pradesh Value Added Tax (APVAT) Act, 2005, VAT is leviable at the rates prescribed in Schedules II to IV and VI to the Act. The rate of tax for goods falling under Schedule-IV to the Act, was enhanced from four to five *per cent* from 14 September 2011. Commodities not specified in any of the Schedules fall under Schedule-V and are liable to VAT at 14.5 *per cent* from 15 January 2010. Further, Section 20(3)(a) of the Act stipulates that every monthly return submitted by a dealer shall be scrutinised by AC/ CTO to verify the correctness of calculation, rate of tax, input tax credit (ITC) claimed and full payment of tax payable for such tax period.

Commodities like 'Mobile phones and Mobile spares', 'Photo frames', 'Cranes', 'Plastic water bubbles', 'Plastic water tanks', 'Adhesives', 'Explosives', 'Fitness equipment', 'Poly vinyl acetate', 'H.R. Build up sectors, Purlins, H.R. Purlins, MS Plates', 'Cable tray ladders' are not specified in any of the Schedules II to IV and VI to the Act and therefore, these items would fall under Schedule-V attracting tax at the rate of 14.5 *per cent*.

During test check of VAT records of seven circles[67], we observed[68] that in 13 cases, dealers dealing in above mentioned commodities had declared tax at the rate of five *per cent* instead of 14.5 *per cent* on the taxable turnover of ₹37.79 crore. This resulted in total short levy of tax of ₹3.59 crore.

Government in the reply (July 2022) accepted/partially accepted the audit observation in nine cases[69] having money value of ₹2.82 crore and stated that notices were issued to the dealers/ amounts were taken to debt management unit (DMU). In one case of Ananthapuramu-II circle, the dealer filed appeal and was pending at appellate authority.

[67] Alcot Gardens, Ananthapuramu-II (5 cases), Autonagar, Dwarakanagar, Ongole-II, Suryabagh (2 cases) and Tirupati-I (2 cases)
[68] between May 2019 and January 2020 for the assessment period from January 2014 to June 2017
[69] Alcot Gardens, Ananthapuramu-II (4 cases), Autonagar, Dwarakanagar and Tirupati-I (2 cases)

In two cases of Suryabagh circle, specific reply was not furnished about action taken on the audit observation relating to VAT turnovers for the period 2016-17 to 2017-18 based on CST assessment orders.

In the remaining one case relating to Ongole-II circle, it was replied that water bubbles can be considered as plastic material and liable for tax at five *per cent* as it falls under items No. 90 and 130 of Schedule-IV of APVAT Act. The reply is not acceptable as the entry No. 90 and entry No. 130 were relating to 'packing material' and 'Plastic Moulded Furniture' respectively. Further entry No. 90 specifically excluded storage tanks made of any materials.

2.3.2 Irregular exemption from payment of tax on sales turnover of Set-top boxes

Irregular exemption from payment of tax on Set-top boxes in contrary to provisions resulted in non-levy of tax of ₹3.09 crore.

As per Section 4(8) of APVAT Act, 2005, every VAT dealer who transfers the right to use goods taxable under the Act for any purpose, whether or not for a specified period, shall pay tax on the total amount realised or realisable by him on such transfer of right to use goods.

During test check of VAT records of Gajuwaka circle, we observed[70] that, AA allowed exemption (by dropping the proposed levy) on the sales turnover of Set-top boxes which was in contrary to the provisions of the Act. This resulted irregular exemption of tax of ₹3.09 crore at applicable rate of 14.5 *per cent* on the sales turnover of ₹21.29 crore made during the period 2015-16 and 2016-17.

In response, Government accepted (July 2022) the audit observation and stated that the amount was taken to DMU.

2.3.3 Non-levy of interest and penalty for belated payment of tax

Assessing Authorities did not levy interest and penalty of ₹1.48 crore on belated payments of tax.

As per Section 22(2) of APVAT Act, 2005, if any dealer fails to pay the tax due within prescribed time, interest at the rate of 1.25 *per cent* per month for the period of delay was liable to be paid in addition to such tax or penalty. Under Section 51(1) of the Act, if a dealer fails to pay tax due by the last day of the month in which it was due, penalty at the rate of 10 *per cent* of the amount of tax due is to be paid, in addition to such tax.

During test check of the VAT returns and payment records in 11 circles[71], it was observed[72] that in 42 cases, the dealers paid tax after the due dates with delays ranging from 1 to 584 days. The AAs, however, did not levy any interest and penalty for belated

[70] in June 2019 for the years 2015-16 and 2016-17

[71] Aryapuram, Autonagar, Benz Circle (2 cases), Brodipet (5 cases), Dwarakanagar (2 cases), Nandigama (2 cases), Park Road (2 cases), Sitharampuram (7 cases), Tirupati-II (2 cases), Vizianagaram East (13 cases) and Vuyyuru (5 cases)

[72] between May 2019 and January 2020 for the period from 2014-15 to 2017-18 (up to June 2017)

payment of tax which was in contrary to the provisions. This resulted in non-levy of interest (₹0.41 crore) and penalty (₹1.07 crore) amounting to ₹1.48 crore.

In response, Government accepted (July 2022) the audit observation in all the 42 cases. In 16 cases[73] an amount of ₹25.25 lakh has been recovered/partially recovered. In 24 cases[74] amounts were taken DMU. In two cases of Park Road circle, the dealers filed appeals; hence not finalized.

2.3.4 Short payment of tax and non-levy of penalty due to non-registration of Turnover Tax (TOT) dealer as VAT dealer

Assessing Authorities did not comply with the provisions relating to conversion of Turnover Tax dealer as VAT dealer which resulted in short payment of tax of ₹31.87 lakh and non-levy of penalty of ₹7.97 lakh.

As per Section 17(3) of the APVAT Act, 2005, every dealer, whose taxable turnover in the 12 preceding months exceeds ₹50 lakh, shall be registered as a VAT dealer, and pay tax at applicable VAT rates from thereon, under Section 4(1) of the Act. As per Section 17(5)(h) of the Act, every dealer engaged in sale of food items including sweets etc., whose total annual turnover is more than ₹7.50 lakh, is liable for VAT registration and payment of tax as per provisions of the Act. Further Section 49(2) of the VAT Act provides that any dealer who fails to apply for registration shall be liable to pay a penalty of 25 *per cent* of the tax due prior to the date of registration.

During test check of TOT records of five circles, it was observed[75] in 15 cases[76] that the dealers did not register themselves as VAT dealer on crossing the taxable turnover of threshold limit. Omission to do so resulted in short levy of tax of ₹31.87 lakh and made them liable for levy of penalty of ₹7.97 lakh.

In response, Government accepted (July 2022) the audit observation in all the 15 cases. In three cases[77] an amount of ₹5.14 lakh was recovered/partially recovered. In remaining 12 cases amounts were taken to DMU.

2.3.5 Under-declaration of tax on food sales

A dealer involved in restaurant business had declared tax at the rate of five *per cent* instead of 14.5 *per cent,* resulting in under-declaration of tax of ₹20.18 lakh.

Under Section 4(9)(c) of the APVAT Act, 2005, every dealer, whose annual total turnover is ₹1.50 crore and above, shall pay tax at the rate of 14.5 *per cent* on the taxable turnover representing sale or supply of food or drink served in restaurants, sweet stalls, clubs or any other eating houses.

[73] Autonagar, Benz Circle, Dwarakanagar, Nandigama, Sitharampuram (2 cases) and Vizianagaram East (10 cases)
[74] Aryapuram, Benz Circle, Brodipet (5 cases), Dwarakanagar, Nandigama, Sitharampuram (5 cases), Tirupati-II (2 cases), Vizianagaram East (3 cases) and Vuyyuru (5 cases)
[75] between May 2019 and March 2020 for the period from 2013-14 to 2017-18 (up to June 2017)
[76] Kurnool-II (2 cases), Kurupam Market, Sitharampuram (7 cases), Vizianagaram East (4 cases) and Vuyyuru
[77] Sithrampuram (2 cases) and Vuyyuru

During test check of VAT records of CTO, Vizianagaram East circle, it was observed (November 2019) that for the assessment period 2015-16 and 2016-17 (up to June 2016), one dealer involved in restaurant business had exceeded the turnover limit of ₹1.50 crore. The dealer, however, declared tax at the rate of five *per cent* (instead of 14.5 *per cent*) in contravention of the provisions. This had resulted in under-declaration of tax of ₹20.18 lakh on the turnover of ₹2.12 crore.

In response, Government accepted (July 2022) the audit observation and stated that the amount was taken to DMU.

2.4 Non-levy/ short levy of penalty

Assessing Authorities did not levy penalty or levied penalty at lower rate on account of under-declaration of tax, excess claim of input tax credit (ITC) by the dealers for reasons of either of fraud/ willful neglect or other than fraud/ willful neglect, which resulted in non-levy/ short levy of penalty of ₹7.82 crore.

According to APVAT Act[78], 2005, a dealer who has under declared tax, is liable for payment of penalty depending upon the quantum of tax under declared. Further, penalty leviable will be equal (100 *per cent*) to the tax under declared if it is proved that dealer committed fraud or willful neglect while declaring tax payable and if any dealer issues/ uses fake/ false tax invoice to take ITC, the penalty leviable would be 200 *per cent* of the tax involved.

During test check of VAT assessments records, we noticed that in 35 cases, dealers had committed non-compliance/ omissions as detailed in the **Table-2.3** below. Assessing authorities have short levied/ not levied penalties on the dealers correctly.

Table-2.3: Short/ Non-levy of penalty

(₹ in crore)

Nature of omission	Quantum of penalty leviable	Jurisdiction of Commercial Tax Officer	No. of cases	Amount of non-levy/short levy of penalty
Willful under-declaration of output tax/ excess ITC	100 *per cent* under Section 53(3)	Ananthapuramu-II, Aryapuram, Benz Circle, Dwarakanagar, Gajuwaka, Kurupam Market, Ongole-1, Suryabagh, Tirupati-I and Vizianagaram South	19	6.12
False/ fabricated declaration	200 *per cent* under Section 55(4)(b)	Kurupam Market, Park Road and Vuyyuru	3	1.04
Short payment of tax/ excess claim of input tax credit (ITC)	10/ 25 *per cent* under Section 53(1)	Alcot Gardens, Aryapuram, Kurupam Market, Nuzividu, Suryabagh and Vizianagaram South	10	0.49
Wrong claim of ITC on the basis of fake tax invoices	200 *per cent* under Section 55(2)	Rajam	2	0.12

[78] Sections 50, 53(1), 53(3), 55(2), 55(4)(b) of APVAT Act, 2005

Nature of omission	Quantum of penalty leviable	Jurisdiction of Commercial Tax Officer	No. of cases	Amount of non-levy/short levy of penalty
Late filing of tax returns	15 *per cent* under Section 50	Ananthapuramu-II	1	0.05
Total			**35**	**7.82**

In response, Government accepted/partially accepted (July 2022) the audit observation in 27 cases[79] having money value of ₹6.39 crore and stated that notices were issued to the taxpayers duly taking amounts to DMU. Of this an amount of ₹9.61 lakh was recovered. In three cases[80] taxpayers filed appeals and were pending at appellate authority. In one case of Suryabagh circle, Government contested that since the assessing authority not imposed penalty, revision could not be taken up. The reply is not acceptable. Revision can be taken up under Section 32 of APVAT Act though the penalty was not imposed by the AA at the time of assessment.

In three cases of Kurupam Market circle relevant documentary evidence (viz., orders of Appellate authority/revision orders) in support of Government's contention was not provided along with the reply; hence Audit could not verify the details. In the remaining one case of Vuyyuru circle specific reply was not furnished.

2.5 Short levy of tax due to application of incorrect rate of tax under CST Act

Incorrect allowance of concessional rate/ application of incorrect rate of tax on interstate sales resulted in short levy of tax of ₹4.90 crore.

As per Section 8(2) of the Central Sales Tax (CST) Act, 1956 read with Rule 12(1) of CST (Registration and Turnover) Rules, 1957, interstate sales not supported by 'C' declaration forms are liable to tax at the rate applicable to sale of such goods inside the appropriate State. Taxes on interstate sales supported by 'C' declaration forms are liable to tax at the rate of two *per cent* as per Section 8(1) of the Act. Under Section 4(3) of the APVAT Act, 2005, every VAT dealer shall pay tax on sale of taxable goods at the rates specified in the schedules to the Act.

Further, as per Rule 12(4) of CST (R&T) Rules 1957, dealers are required to submit a certificate in form 'E' for claiming exemption relating to interstate transfer of goods referred under Section 6(2) of CST Act.

During test check of CST records of 14 circles[81], we observed[82] that 24 dealers had cleared commodities at concessional rate of tax on interstate sales on invalid

[79] Alcot Gardens, Ananthapuramu-II (2 cases), Aryapuram (3 cases), Benz Circle, Dwarakanagar (4 cases), Gajuwaka (2 cases), Kurupam Market (5 cases), Nuzividu, Ongole-I, Rajam (2 cases), Suryabagh (2 cases) and Vizianagaram South (3 cases)

[80] Dwarakanagar, Park Road and Tirupati-I

[81] Ananthapuramu-II, Aryapuram, Autonagar (4 cases), Chirala, Chittoor-II (2 cases), Gajuwaka, Kurupam Market, Ongole-I, Ongole-II, Park Road, Sitharampuram (3 cases), Suryabagh (4 cases), Vizianagaram East and Vuyyuru (2 cases)

[82] between May 2019 and March 2020 for the period 2012-13 to 2017-18 (up to June 2017)

forms/ without supporting declaration forms. The AAs, however, levied tax at lesser rate of tax at two/ five/ 14.5 *per cent* instead of effective rate of five/ 14.5/ 70 *per cent*. This resulted in short levy of tax of ₹4.90 crore on interstate turnover of ₹46.51 crore.

Government in the reply (July 2022) accepted/ partially accepted the audit observation in 11 cases[83] having money value of ₹1.95 crore. Of this, an amount of ₹5.50 lakh was recovered in one case (Sitharampuram circle). In four cases[84] the taxpayers filed appeals and were pending at appellate authority. In another four cases[85], relevant documentary evidence in support of Government's contention was not provided along with the reply; hence Audit could not verify the details.

In one case of Ongole-II circle, Government replied that the dealer, as per objection filed, was liable to pay tax at five *per cent* for the goods machinery spares and tools for tapping and drifting as per entries 102 (29), 103 (6) and 103 (19) of Schedule IV of APVAT Act. The reply is not acceptable as the earth moving equipment and spares dealt by the dealer are not fall under the above entries.

In one case of Sitharampuram circle, Government replied that the dealer was dealing with Machinery for Photography and chemical preparation for photographic uses which fall under entries 102(49) and 100(134) respectively and taxable at five *per cent*. It was also stated that the AA verified the purchase invoices and concluded that the dealer did business in the above said goods. The contention of the Government is not acceptable. The purchased goods can be used as inputs and the AA is to verify sale invoices to ascertain the taxability on outputs. Further, no documentary evidence in support of reply was furnished for verification along with reply.

In one case of Chirala specific reply was not furnished. The remaining two cases[86] were not finalized.

2.6 Works Contracts

2.6.1 Short levy of tax on works contracts in the cases of non-maintenance of detailed accounts

Incorrect assessment of turnover in works contracts where detailed accounts were not maintained by contractors resulted in short levy of tax of ₹1.47 crore.

As per Rule 17(1)(g) of APVAT Rules, 2005, if any works contractor did not maintain the detailed accounts to determine the correct value of the goods at the time of their incorporation, tax shall be levied at the rate of 14.5 *per cent* on the total consideration received, after allowing permissible deductions on percentage basis on the category of work executed. In such cases, the works contractor shall not be eligible to claim ITC.

[83] Ananthapuramu-II, Aryapuram, Autonagar (4 cases), Ongole-I, Sitharampuram, Suryabagh and Vuyyuru (2 cases)
[84] Park Road, Sitharampuram, Suryabagh and Vizianagaram East
[85] Chittoor-II, Kurupam Market and Suryabagh (2 cases)
[86] Chittoor-II and Gajuwaka

During test check of VAT assessment records in two circles[87], we noticed that the turnover in two cases was assessed[88] according to the method prescribed for those who maintain detailed work accounts despite non-maintenance of the same by the dealers. Since the dealers did not maintain detailed work accounts, tax of ₹1.59 crore was leviable at 14.5 *per cent* on the turnover after allowing permissible deduction[89], whereas the tax of ₹0.26 crore only was levied. This resulted in short levy of tax of ₹1.33 crore in two cases. Besides, ITC of ₹13.54 lakh was allowed to these dealers which was contrary to VAT rules.

In response, in one case relating to Dwarakanagar circle, Government accepted (July 2022) the audit observation and stated that demand has been raised for ₹1.34 crore. In the remaining one case of Kurupam Market circle, Government contested that the dealer had maintained all the books of accounts to ascertain the various items of expenditure deductible under Rule 17(1)(e) of APVAT Rules. The reply is not acceptable. As noticed from the assessment order, the AA allowed deduction based on the ratio of pure labour and work involving material component. Had the contractor maintained detailed accounts respective amounts would have been considered for deduction instead of ratios.

2.6.2 Non-payment of taxes by works contractors

Contractors/ dealers had not paid tax of ₹43.52 lakh despite declaration of the same in their monthly returns.

As per Section 4(7)(a) of APVAT Act, 2005 every dealer executing works contracts shall pay tax on the value of goods at the time of incorporation of such goods in the works executed at the rates applicable to the goods under the Act.

During test check of records in two circles[90], we observed[91] from verification of records of tax paid particulars that three works contractors declared their turnover and tax thereon in the monthly returns. However, they have not paid the tax due of ₹43.52 lakh.

In response, Government accepted (July 2022) the audit observation in all the three cases and stated that the amounts were taken to DMU.

2.6.3 Short levy of tax due to incorrect determination of taxable turnover under works contract

Incorrect determination of taxable turnover under works contract resulted in short levy of tax of ₹8.99 lakh.

As per Section 4(7)(a) of the APVAT Act, 2005 every dealer executing works contract shall pay tax on the value of goods incorporated in the work, at the rates applicable to the goods under the Act. To arrive at the value of goods at the time of incorporation,

87 Dwarakanagar and Kurupam Market
88 assessment period October 2012 to June 2017
89 by allowing deduction at 30 *per cent* on gross receipts
90 Alcot Gardens (2 cases) and Kadapa-II
91 between May and August 2019 for the period 2017-18 (up to June 2017)

the deductions prescribed under Rule 17(1)(e) of APVAT Rules, 2005, such as expenditure towards labour charges, hire charges etc., incurred by the contractor, are to be allowed as deductions from the total consideration and on the balance turnover, tax is to be levied at the same rates at which purchase of goods were made and in the same proportions.

During test check of the VAT assessment files of a dealer in the office of Gajuwaka circle, it was observed[92] that the AA, while finalising the assessment, had incorrectly determined the taxable turnover by allowing certain inadmissible deductions from the gross turnover. Besides this, expenditure and profit relating to labour was also incorrectly computed. This resulted in short levy of tax of ₹8.99 lakh.

In response, Government accepted (July 2022) the audit observation and stated that the amount was taken to DMU.

2.7 Input Tax Credit (ITC)

2.7.1 Incorrect allowance of ITC and non-forfeiture of excess tax collected by dealers

Assessing Authorities had allowed ITC amounting to ₹1.25 crore to the dealers running eating houses who were not eligible to claim ITC as per the provisions of the Act. Further, excess tax of ₹88.38 lakh collected by the dealers was also not forfeited to Government.

As per Section 4(9)(d) of APVAT Act, 2005 every dealer, other than those mentioned in clause (a) and clause (b) and whose annual total turnover is more than ₹7.50 lakh and less than ₹1.50 crore shall pay tax at the rate of five *per cent* of the taxable turnover of the sale or supply of goods, being food or any other article for human consumption or drink served in restaurants, sweet-stalls, clubs, any other eating houses or anywhere whether indoor or outdoor or by caterer. Section 4(9) has been replaced with new sub-section (9)[93] to levy uniform rate of tax at five *per cent* which came into force from July 2016. As per Section 13(5)(h) of the Act, such dealers are not entitled to claim ITC.

Further, as per Section 57(2) and (4) of the Act, no dealer shall collect tax exceeding the rate at which tax was liable to be paid under the provisions of the Act. Any such excess amount collected shall be forfeited to the Government.

During test check of VAT records in three circles[94], we observed[95] that the AAs had allowed ITC of ₹1.25 crore against the provisions of Act to five dealers whose annual turnover ranged between ₹7.5 lakh and ₹1.50 crore. We also noticed that the dealers had collected tax at higher rate of 14.5 *per cent* instead of five *per cent* from the

[92] in June 2019 for the period from 2013-14 to 2016-17
[93] Act No.6 of 2017 AP Gazette Part IV-B Extraordinary
[94] Kurupam Market, Rajam and Suryabagh (3 cases)
[95] between June 2019 and March 2020 for the period 2013-14 to 2017-18 (up to June 2017)

customers. This resulted in excess collection of tax of ₹88.38 lakh and it required forfeiture to Government account.

In response, Government accepted (July 2022) the audit observation in one case of Rajam circle and collected part amount of ₹2.97 lakh.

In the case of Suryabagh circle, Government stated that the dealer purchased raw material from the VAT dealers for preparation of eatables and not claimed ITC. Further stated that the dealer claimed ITC on the items sold across the counter. In the remaining two cases of Suryabagh circle also Government contended that the assesses did not run hotel or clubs or other eating business with sitting provision and they did sales across the counter only. Hence, the charging Section in respect of the dealer does not fall under any clause of the Section 4(9) of the APVAT Act.

The replies are not acceptable, as the Act stipulated that the sale or supply of goods, being food or any other article for human consumption anywhere whether indoor or outdoor or by caterer liable to tax under Section 4(9)(d) of the Act and as per Section13(5)(h) the dealers were not eligible for ITC.

In one case of Kurupam Market circle relevant documentary evidence relating to revision orders (June 2020) passed by Deputy Commissioner, (CT) Visakhapatnam was not provided along with the reply for verification.

2.7.2 Excess allowance of ITC due to incorrect/ non-restriction of exempt transactions

ITC was not restricted/ restricted incorrectly by the Assessing Authorities on sale of exempt goods and exempt transactions resulted in excess allowance of ITC of ₹35.75 lakh.

As per Section 13(5) of the APVAT Act, 2005, no ITC shall be allowed to any VAT dealer on sale of exempted goods (except in the course of export) and exempt sales. As per Section 13(6) of the Act, ITC for transfer of taxable goods outside the State (otherwise than by way of sale) shall be allowed for the amount of tax in excess of five *per cent*. Further, as per sub-rules (7) and (8) of Rule 20 of APVAT Rules, 2005 a dealer making taxable sales and exempt sales by using common inputs, shall restrict ITC as per the prescribed formula[96].

During test check of records of four circles[97], Audit observed[98] from the VAT records of four dealers that the dealers had dealt with sale of exempted goods/ exempt transactions of taxable goods along with sale of taxable goods by utilising common inputs. However, the ITC was not restricted by the AAs as per the relevant provisions, resulting in excess allowance of ITC of ₹35.75 lakh.

[96] A x B/C, where A is the ITC for common inputs for each tax rate, B is the taxable turnover and C is the total turnover

[97] Alcot Gardens, Ananthapuramu-II, Nuzividu and Tirupati-I

[98] between May 2019 and September 2019 for the period from 2014-15 to 2017-18 (up to June 2017)

In response, Government accepted (July 2022) the audit observation in one case of Ananthapuramu-II circle and partly collected an amount of ₹3.00 lakh against ₹28.94 lakh. In two cases[99] dealers filed appeals and were pending at appellate authority.

In remining one case of Nuzividu circle Government replied that the dealer neither involved in manufacturing of taxable and exempted goods nor did he dispatch goods to outside the State other than by way of sale using common inputs. Hence, in this case there is no need to restrict ITC.

The reply is not acceptable. It was observed from the turnover ledger that the dealer had purchased five/ 14.5 *per cent* taxable goods and claimed ITC. However, the dealer had made exempt sales of ₹77.48 lakh along with five/ 14.5 *per cent* taxable sales. Thus, ITC is to be restricted as per the provisions of 20(7) of APVAT Rules 2005, as the dealer has made exempt and taxable sales from the purchases of taxable goods on which ITC was claimed.

2.7.3 Incorrect allowance of ITC

Allowing ITC based on records available without verifying the possession of tax invoice with the dealers resulted in excess allowance of ITC of ₹22.43 lakh.

Sections 13(1) and 13(3)(a) of APVAT Act, 2005, stipulated that ITC shall be allowed to the VAT dealer for the tax charged on all purchases of taxable goods made by that dealer during the tax period, provided the dealer is in possession of valid tax invoice.

During test check of VAT records of two circles[100], Audit observed[101] that the AAs had made assessments in three cases based on the records available with them citing that the dealers had not responded to the notices served/ whereabouts of the dealers not known. Scrutiny showed that the AAs, instead of disallowing, had allowed ITC without verifying possession of tax invoices with the dealers in these cases in contravention to the above provisions. The incorrect allowance of ITC in these cases amounted to ₹22.43 lakh.

In response, Government accepted (July 2022) the audit observation in all the three cases and stated that the amounts were taken to DMU. Of this, in one case of Sitharampuram circle, part amount of ₹1.35 lakh has been recovered from the dealer.

2.7.4 Excess allowance of ITC/ short levy of tax due to incorrect determination of turnover

Adoption of excess turnover than the turnover in annual returns resulted in excess allowance of ITC of ₹18.78 lakh.

Under Section 13(1) of APVAT Act, 2005, ITC shall be allowed to the VAT dealer for the tax charged in respect of all purchases of taxable goods, made by that dealer during

[99] Alcot Gardens and Tirupati-I
[100] Park Road (2 cases) and Sitharampuram
[101] between May and June 2019 for the period from 2014-15 to 2015-16

the tax period for use in the business of the VAT dealer. Further, Para 5.12 of VAT Audit Manual 2012 prescribed that the Audit Officer is required to verify the details declared by the dealer in VAT returns and to reconcile with those reported in certified annual accounts for that period.

During test check of VAT records of two circles[102] we noticed[103] that in one case in Tirupati-II circle, the AA had adopted excess purchase turnover of ₹2.27 crore for ITC than what was reported in relevant annual accounts. In other case AA, Alcot Gardens had not considered the receipts (job work and other income) included in the annual accounts while making assessment. This resulted in excess allowance of ITC/ short levy of tax of ₹18.78 lakh.

In response, Government accepted (July 2022) the audit observation in both the cases and stated that in one case of Alcot Gardens circle amount was taken to DMU. In the other case of Tirupati-II circle revision was pending.

[102] Alcot Gardens and Tirupati-II
[103] between May 2019 and January 2020 covering the period from 2013-14 to 2016-17