CHAPTER II: TAXES ON SALES, TRADE ETC.

2.1 Results of audit

Test check of the records relating to sales tax/value added tax conducted during the year 2007-08 revealed underassessments of revenue amounting to Rs. 176.04 crore in 1,232 cases, which fall under the following categories:

(Rupees in crore)

Sr. No.	Category	Number of cases	Amount
1.	**Exemptions and concessions under Sales Tax/VAT Act (A review)**	1	56.01
2.	Non-levy of penalty	86	27.09
3.	Application of incorrect rates of tax	123	15.11
4.	Non-levy of interest	79	7.99
5.	Incorrect computation of turnover	62	3.35
6.	Underassessment of turnover under the CST Act	35	0.53
7.	Other irregularities	846	65.96
Total		**1,232**	**176.04**

During the year 2007-08, the department accepted underassessments and other deficiencies of Rs. 2.44 crore involved in 145 cases of which 138 cases involving Rs. 1.90 crore had been pointed out during 2007-08 and the remaining in the earlier years. The department recovered Rs. 1.44 crore in 77 cases during the year 2007-08, of which 71 cases involving Rs. 1.01 crore related to the year 2007-08 and the balance to the earlier years.

After the issue of the draft paragraphs, the department recovered Rs. 27.15 lakh in two cases.

A few illustrative cases involving Rs. 1.90 crore and a review of **"Exemptions and concessions under Sales Tax/VAT Act"** involving Rs. 56.01 crore are mentioned in the succeeding paragraphs.

2.2 Exemptions and concessions under Sales Tax/VAT Act

2.2.1 Highlights

- In the absence of details like bank draft/pay order/treasury challan number, amount and date of deposit of tax, particulars of goods sold etc., in form VAT C-4, genuineness of ITC of Rs. 270.16 crore allowed to 103 dealers in seven DETCs could not be verified.

(Paragraph 2.2.7)

- Assessments were finalised without cross verification of sales/purchases of 3,331 transactions having sales value of Rs. 1,969.14 crore involving tax effect of Rs. 163.01 crore.

(Paragraph 2.2.8.1)

- Due to failure of the AAs to scrutinise the claim and cross verify the transactions, tax and penalty for false declarations amounting to Rs. 9.26 crore was not imposed.

(Paragraph 2.2.8.2)

- In the absence of any prescribed mechanism, correctness of exemption of tax of Rs. 1.75 crore on sales of PVC pipes to agriculturists as component parts of agricultural pumping sets valued as Rs. 17.46 crore could not be verified.

(Paragraph 2.2.9)

- Eighteen dealers purchased goods valued as Rs. 363.92 crore at concessional rate of tax against declaration in forms STD-IV/VAT-D1 for use in the manufacture of goods for sale and transferred goods as such or to their branches outside the State resulting in undue tax benefit of Rs. 20.99 crore.

(Paragraph 2.2.11.1)

- Undue tax benefit of Rs. 4.87 crore (including maximum penalty of Rs. 2.92 crore) was allowed in the case of two dealers who had purchased goods at concessional rate for use in the manufacture and sale but utilised these goods for the purpose (telecommunication services) other than that mentioned in form C.

(Paragraph 2.2.11.2)

- Incorrect allowing of concessional rates/exemptions without production of prescribed statutory declarations or furnishing of duplicate/incomplete/invalid forms resulted in short levy of tax of Rs. 30.38 crore.

(Paragraph 2.2.12)

- Tax and penalty amounting to Rs. 19.27 crore was not levied.

(Paragraph 2.2.13)

2.2.2 Introduction

The assessment, levy and collection of sales tax in Haryana was governed under the Haryana General Sales Tax Act, 1973 (HGST Act) and the rules framed thereunder upto 31 March 2003 and thereafter under the Haryana Value Added Tax Act, 2003 (HVAT Act) and the rules framed thereunder. The State Government may, by notification and subject to such restrictions and conditions as may be specified therein, exempt any class of dealers or any goods or class of goods, in whole or in part from the payment of tax under the Act for such period as may be specified in the notification. The State Acts[1] also require that the registered dealer purchasing the goods exempted in whole or in part, from the payment of tax under the Act, shall furnish a declaration or certificate to the effect that the goods purchased were used by him for the purpose or in the manner and within the period specified in the notification granting such exemption/concession.

Under the Central Sales Tax Act, 1956 (CST Act) and the rules framed thereunder, the dealers are eligible for certain exemptions/concessions of tax on inter state sales/transactions to the registered dealers, Government departments, transfer of goods to branches/agents and on export/import of goods out of or into the territory of India on the strength of prescribed declarations in forms 'C[2]', 'D[3]', 'E-I' 'E-II[4]', 'F[5]' and 'H[6]' and supporting certificates and documents.

As per the departmental instructions issued in August 1988, the assessing authorities (AAs) are required to confirm genuineness of these transactions through cross verification of records of other dealers within the State before finalising the assessments.

It was decided by audit to review the mechanism for ensuring that the exemptions and concessions under Sales Tax/VAT Act were allowed correctly by the Excise and Taxation Department. The review revealed a number of system and compliance deficiencies which have been discussed in the subsequent paragraphs.

2.2.3 Organisational set up

At the Government level, the Financial Commissioner and Principal Secretary, Excise and Taxation Department is responsible for the administration of sales tax laws in the State. At the departmental level, the Excise and Taxation Commissioner (ETC) is responsible for the administration of the Sales Tax/VAT/CST Acts and rules in the Sales Tax Department. The ETC is

1 HGST Act and HVAT Act.
2 Form C for making inter state purchases/sales at concessional rate of tax.
3 Form D for making purchases by Government department at concessional rate of tax.
4 Form E-I and E-II for making transit sale during movement of goods from one State to another.
5 Form F for making transfer of goods (without payment of tax) to branch offices and agents in other States.
6 Form H for making purchases (without payment of tax) to comply with an order of export of goods outside the territory of India.

assisted by Additional Excise and Taxation Commissioners (AETCs), Joint Excise and Taxation Commissioners (JETCs), Deputy Excise and Taxation Commissioners (DETCs) and allied staff at headquarters. He is assisted by JETCs at range level (four ranges), 22 DETCs at district level and excise and taxation officers (ETOs), assistant excise and taxation officers (AETOs), taxation inspectors and other allied staff. The DETC is also responsible for receipt of declaration forms from the commissionerate and their distribution among circles/wards under his jurisdiction. The ETOs and AETOs are responsible for registration, assessment and distribution of declaration forms to the dealers.

2.2.4 Audit objectives

The review was conducted with a view to ascertain:

- efficiency and effectiveness of the State machinery in implementation of various provisions/instructions of the sales tax laws in the State;
- whether concessions and exemptions allowed by the AAs at the time of assessment had correctly been worked out in accordance with the provisions of the applicable Acts/Rules;
- whether cross verification of transactions of dealers was conducted by the AAs to verify the genuineness of the concessions/exemptions claimed on declarations produced by the dealers; and
- whether internal controls existed in the department to ensure proper use of declaration forms so as to prevent leakage of revenue.

2.2.5 Scope of audit and methodology

The review of the relevant records of registered dealers was conducted in 12[7] out of 22 DETCs and in the office of ETC relating to the assessment cases finalised during the period from 2003-04 to 2006-07 between April 2007 and March 2008. These 11 districts were sampled statistically after stratifying the districts on the basis of tax collection (six DETCs having tax collection exceeding Rs. 500 crore, three DETCs with tax collection ranging between Rs. 100 crore and Rs. 500 crore and two DETCs with tax collection less than Rs. 100 crore) to ensure a representative coverage. An additional district, Karnal, was included in the scope of the review on the suggestion of the department. Points of similar nature noticed in regular audit during 2003-04 to 2006-07 have also been included in the review.

2.2.6 Acknowledgement

The Indian Audit and Accounts Department acknowledges the co-operation of the Excise and Taxation Department in providing necessary information and records for audit. An entry conference was held and attended by the Financial Commissioner and Principal Secretary, Excise and Taxation Department,

[7] Ambala, Faridabad (East), Faridabad (West), Gurgaon (East), Gurgaon (West), Hisar, Jhajjar, Karnal, Panipat, Rohtak, Sirsa and Sonipat.

ETC, AETCs and JETCs. The audit objectives, methodology and selection of districts were discussed and agreed upon. The draft review report was forwarded to the Government and the department in May 2008 and was discussed in the Audit Review Committee meeting held in July 2008. The AETC represented the department. Views of the department have been incorporated in the relevant paragraphs.

Audit findings

System deficiencies

2.2.7 Absence of mechanism to verify the tax deposited before allowing input tax credit

Under the HGST Act, a dealer may deduct from his gross turnover the purchase and sale value of goods, forming part of the taxable turnover which have already been subjected to tax at the first stage of sale or purchase under section 17 or 18, provided the dealer produces, in respect of such goods, a declaration in form ST-14[8] duly authenticated by the AAs, filled in and signed by the selling registered dealer. The dealer is required to give detailed particulars like bank draft/pay order or treasury challan number and date of deposit of tax in the treasury by the selling dealer or previous selling dealer from whom he had purchased the goods. Under the HVAT Act, a registered dealer is entitled to claim benefit of input tax credit (ITC) if he produces proof in support of purchase of goods from VAT dealer in form VAT-C4[8] or original tax invoices. **But the form VAT-C4 does not contain column(s)/similar entries as existed in the form ST-14. The form VAT-C4 is also not required to be authenticated from the AA under the HVAT Act.**

During test check of the assessment records of seven[9] DETCs, it was noticed that 103 dealers purchased goods valued as Rs. 6,271.44 crore during the year 2003-04 and claimed ITC. While finalising the assessments between May 2006 and March 2007, the AAs allowed benefit of ITC amounting to Rs. 270.16 crore against the production of VAT-C4 forms. In the absence of these details, genuineness of ITC of Rs. 270.16 crore allowed to the dealers could not be verified in audit.

The Government may, therefore, consider providing additional column(s) for recording details like the particulars of goods sold, amount of tax deposited, date and number of treasury challan/bank draft/cheque etc. in the declaration form VAT C-4 on the lines of declaration in form ST-14 and authentication/issuance of these forms by the department to ensure genuineness and correctness of the tax deposited by the selling dealers while allowing ITC.

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[8]. Form ST-14 and VAT C-4 are used as a proof of payment of tax on the goods purchased to claim rebate or ITC under the State Acts.

[9] Faridabad (East), Faridabad (West), Gurgaon (East), Gurgaon (West), Karnal, Rohtak and Sirsa.

In the Audit Review Committee meeting, the department stated (July 2008) that the suggestion for inserting similar provisions regarding tax deposited in form VAT-C4 as contained in form ST-14 was under consideration.

2.2.8 Absence of a monitoring mechanism to ensure cross verification of purchase transactions

Under the HVAT Act, if a dealer has maintained false or incorrect accounts or documents with a view to suppress his sales, purchases, imports into the State, exports out of the State or stocks of goods, or has furnished or produced any account, return, document or information which is false or incorrect in any material particular, such authority may direct him to pay by way of penalty, in addition to the tax to which he is assessed or is liable to be assessed, a sum thrice (twice under HGST Act) the amount of tax which would have been avoided. In order to ensure genuineness of the transactions and detect evasion of tax, the ETC in August 1988 emphasised the need for cross verification of sale and purchase transactions exceeding Rs. 10,000 in the case of ETO and Rs. 5,000 in the case of AETO.

With a view to detect evasion of VAT by claiming fraudulent ITC, the ETC issued instructions in March 2006 for cross verification of all purchase transactions totalling more than Rs. 1 lakh from a single VAT dealer in a year. **However, the department did not prescribe a system of periodical reporting by the AAs to the superior authorities about the position of conducting of the cross verification of transactions.**

2.2.8.1 Test check of the assessment records of 14[10] DETCs revealed that cross verification of 3,331 inter district transactions (each exceeding Rs. 1 lakh) in respect of 529 dealers aggregating sale value of Rs. 1,969.14 crore involving tax effect of Rs. 163.01 crore during the year 2003-04 was not done and assessments were finalised between April 2006 and March 2007.

After the cases were pointed out, the department stated in July 2008 that foolproof cross verification of transactions would be possible only after complete computerisation of the department. As such 100 *per cent* verification of purchases exceeding Rs. 1 lakh was not possible.

2.2.8.2 During test check of the assessment records of 10[11] DETCs, it was noticed that 55 dealers were allowed benefit of ITC on the strength of VAT-C4 forms and concessions against declaration in form C amounting to Rs. 2.43 crore on account of sales/purchases made during the years 2001-02 to 2004-05. Cross verification of records of these offices revealed that they had suppressed their sales or purchases and submitted false information/incorrect return. Failure on the part of AAs to scrutinise the claim and cross verify the transactions resulted in incorrect allowing of ITC and of concessional rate of

[10] Ambala, Faridabad (East), Faridabad (West), Gurgaon (East), Gurgaon (West), Hisar, Jagadhri, Jhajjar, Karnal, Panipat, Rewari, Rohtak, Sirsa and Sonipat.

[11] Faridabad (West), Gurgaon (West), Hisar, Jagadhri, Jhajjar, Jind, Karnal, Panchkula, Rewari and Sonipat.

tax on inter state sales (ISS) which consequently led to short levy of tax of Rs. 2.43 crore besides penalty of Rs. 6.83 crore.

After the cases were pointed out, the DETC Sonipat stated in March 2008 that the dealer in one case involving tax effect of Rs. 19.40 lakh had submitted two C forms for the same transaction i.e. one with the purchase order and second with the invoices issued by the purchasing dealers and had requested to withdraw one C form. The reply is not tenable as the dealer had not mentioned the particulars of sales transactions to which the said C forms pertained. Reply in the remaining cases has not been received (August 2008).

The Government may, therefore, consider prescribing a periodical return by the AAs to the superior authorities about the number of transactions required to be cross verified, actual number of transactions verified, shortfall, if any, to ensure compliance with departmental instructions.

2.2.9 PVC[12] pipes treated as tax free sales without submitting any proof of sale to agriculturists

As per the Government notification dated 3 February 1999 under the HGST Act, PVC pipes are exigible to tax at the rate of 12 *per cent* at the first stage of sale. Further, pipes and tubes made of any material other than iron and steel are exigible to tax at the rate of four *per cent* with effect from 1 April 2003 under the HVAT Act. In both the Acts, PVC pipes, couplet sockets are exempt from tax if sold as component parts of agricultural pumping sets of all kinds including submersible pumps and sprinkler system equipment and drip irrigation system but taxable if these are sold otherwise than as components of agricultural pumping sets including drip/sprinkler irrigation system. The Sales Tax Tribunal held[13] in April 2004 that PVC pipes are substitute of steel tubes/pipes which are used for deep tubewells as well as for other purposes. **The State Acts did not prescribe for submission of any document for supporting the claim of exemption from levy of tax being sale for agricultural purposes.**

During test check of the assessment records of six[14] DETCs, it was noticed that 14 dealers sold PVC pipes valued as Rs. 17.46 crore during the years 1999-2000 to 2004-05 and claimed deduction as tax free sales. In the absence of any prescribed mechanism, the AAs while finalising the assessments between November 2002 and September 2006, allowed deduction of Rs. 17.46 crore and did not levy tax of Rs. 1.75 crore treating the sale of PVC pipes as tax free.

After the cases were pointed out, DETC Sirsa stated in April 2008 that the case had been sent to DETC (Inspection), Sirsa for taking suo motu action for revision. A report on action taken in the remaining cases has not been received (August 2008).

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12 Poly vinyl chloride.

13 M/s Mittal Automobiles, Kaithal Vs. State of Haryana {(2004) 24 PHT 74}

14 Bhiwani, Faridabad (West), Gurgaon (East), Gurgaon (West), Rewari and Sirsa.

The Government may, therefore consider prescribing a periodical return from the AAs showing the list of cases and grounds on which the exemption has been granted.

2.2.10 Internal audit

Internal audit is generally defined as the control of all controls as it is a means for an organisation to assure itself that the prescribed systems are functioning reasonably well. The internal audit parties are required to conduct cent *per cent* audit of all the assessments finalised, examining inter alia assessment orders, issue of demand notices, amount of tax collected and verification of deposit of amount in the treasury.

It was noticed that an internal audit wing (IAW) had not been set up in the Excise and Taxation Department for conducting the audit of assessment of sales tax/VAT cases.

After this was pointed out, the department stated in July 2008 that internal audit system in respect of assessment of sales tax/VAT cases could not be set up as the Government had appointed DETC-cum-Revisional Authority (RA) who took care of the cases of underassessments by the AA and was competent to revise the assessment orders. The reply of the department is not tenable as internal audit is a management tool for ensuring efficient functioning of the department and plugging leakages of revenue. The role of internal audit is quite different from that of a RA. Thus, in the absence of internal audit, the department had no means of knowing the areas where systems were deficient and did not, therefore, have the opportunity of taking remedial action.

The Government may therefore consider setting up an IAW to ensure timely detection and correction of errors in assessment, levy, collection of sales tax revenue and refund cases.

Compliance deficiencies

2.2.11 Misuse of declaration forms STD-IV/VAT-DI and C

2.2.11.1 Under the State Acts, where goods taxable at first point of sale are sold by one dealer to another dealer, tax is leviable at a lower rate if the purchasing dealer furnishes a declaration in form STD-IV/VAT-D1 certifying that the goods are meant for use in the manufacture of goods for sale. As per the departmental inspections issued in September 1998 (applicable upto 31 March 2003), the manufacturers availing facility of concessional rate of tax are not allowed to transfer the goods to their branches in other states otherwise than by way of sale. Further, if the dealer availing the benefit of concessional rate violates any of the conditions/restrictions imposed, he is liable to pay penalty not exceeding one and a half times of the tax involved in addition to the additional tax payable.

During test check of the assessment records of five[15] DETCs, it was noticed that 18 dealers purchased goods valued as Rs. 363.92 crore at the concessional

[15] Faridabad (East), Faridabad (West), Gurgaon (West), Rewari and Sirsa.

rate of tax against declaration in forms STD-IV/VAT-D1, for use in the manufacture of goods. However, the goods purchased or manufactured were transferred to their branches outside the State otherwise than by way of sale during the period 2000-01 to 2004-05. The AAs, while finalising the assessments between June 2004 and March 2007, omitted to levy tax at the rates applicable to these goods. This resulted in non-levy of tax of Rs. 20.99 crore besides maximum penalty of Rs. 31.48 crore.

After the cases were pointed out, the department stated in July 2008 that if the concessional rate was restricted to the sale within the State or ISS of the manufactured goods, the State may lose even four *per cent* tax since the manufacturer would prefer to purchase goods from outside the State against C forms. The reply of the department is not tenable as it is not in conformity with the provisions of the State Acts.

2.2.11.2 Under the CST Act and the rules made thereunder, a dealer may purchase goods at concessional rate of tax for resale or use in the manufacture/processing of goods for sale, mining, generation/distribution of power, packing of goods for sale/resale against declaration in form C. If any registered dealer purchases goods on the strength of registration certificate against form C and does not use it for any of the purposes mentioned in form C, he shall be liable to pay by way of penalty, in addition to the tax leviable, a sum not exceeding one and a half times the tax which would have been levied.

During test check of the assessment records of DETC, Ambala, it was noticed that two dealers providing telecommunication services purchased machinery valued as Rs. 32.44 crore between April 2001 and 10 May 2002 at concessional rate of tax against form C and used them in providing telecommunication services i.e. for the purpose other than that mentioned in form C. The AAs, while finalising the assessments between September 2006 and March 2007, failed to levy additional tax/penalty. This resulted in underassessment of tax of Rs. 1.95 crore besides maximum penalty of Rs. 2.92 crore.

2.2.12 Incorrect allowing of exemption/concession without declarations/ documents or against incomplete declarations/documents

Under the State Acts and CST Act, certain exemptions and concessions have been allowed to dealers for selling/purchasing goods either without payment of tax or at concessional rate of tax on submission of statutory declarations in forms ST-15 A/VAT D-2[16], VAT D-1[17], C, F and H. One form F is to cover the transactions of only one calendar month. Similar exemption is allowed on account of sale during import of goods into the territory of India (high seas sale) and sale of goods to units availing benefit of exemption from payment of tax on production of proof of transfer of title to goods etc. and declaration duly

[16] ST 15A/VAT D-2: used for making purchases without payment of tax in pursuance of export of goods out of the territory of India.

[17] VAT D-1: used for making purchase of goods at concessional rate of tax for use in the manufacture of goods for sale.

supported with/list containing complete particulars of purchasing dealer availing exemptions from payment of tax respectively.

Test check of the records of 16[18] DETC offices revealed that the AAs allowed the concessions and exemptions to the dealers either without obtaining requisite declarations/documents or after obtaining incomplete/invalid declarations. This resulted in short levy of tax Rs. 30.38 crore as mentioned below:

(Rupees in crore)

Sr. No.	Number of districts	Number of dealers	Value of goods sold/ purchased	Amount of tax			Nature of irregularity
				leviable	levied	short levied	
1.	15	66	241.16	26.79	8.77	18.02	Concession/lower rate of tax was allowed/applied in cases not supported with declaration in form C or against duplicate C forms.
Remarks: After the cases were pointed out, the AA Faridabad (West) created an additional demand of Rs. 2.06 lakh in one case in August 2006. The department issued instructions (July 2008) in one case of dryer felts involving Rs. 2.88 lakh to the revisional authority (RA) to revise the assessment. Reply in the remaining cases has not been received (August 2008).							
2.	11	88	91.47	7.65	-	7.65	Exemption was allowed against incomplete/invalid forms H/ST-15A/ D-2.
Remarks: After the cases were pointed out, the department accepted (July 2008) the audit observations. A report on recovery has not been received (August 2008).							
3.	2	2	24.35	2.43	-	2.43	Exemption of tax on high seas sale was allowed without the requisite documents.
4.	10	23	17.03	1.60	-	1.60	Exemption was allowed without the production of F forms or one form covered transactions for more than one calendar month.
5.	2	4	3.32	0.37	-	0.37	Deduction of sale to units availing exemption from payment of tax was allowed without the requisite declaration/ complete particulars of purchasers.

[18] Faridabad (East), Faridabad (West), Gurgaon (East), Gurgaon (West), Hisar, Jagadhri, Jhajjar, Jind, Kaithal, Karnal, Panipat, Panchkula, Rewari, Rohtak, Sirsa and Sonipat.

Sr. No.	Number of districts	Number of dealers	Value of goods sold/ purchased	Amount of tax			Nature of irregularity
				leviable	levied	short levied	
6.	2	3	3.84	0.46	0.15	0.31	Benefit of concessional rate of tax was allowed without the requisite declaration forms.
Remarks: After the cases were pointed out, the AA raised additional demand of tax of Rs. 8.56 lakh in one case in September 2007. A report on recovery and action taken in the remaining cases has not been received (August 2008).							
Total		**186**	**381.17**	**39.30**	**8.92**	**30.38**	

2.2.13 Non-levy of penalty

Under the State Acts, if a dealer has maintained false or incorrect accounts or documents with a view to suppress his sales or purchases or has furnished or produced any account, return, document or information which is false or incorrect in any material particular, such authority may direct him to pay by way of penalty in addition to the tax to which he is assessed or liable to be assessed a sum thrice (twice under the HGST Act) the amount of tax which would have been avoided. Under the CST Act, if any dealer fails to prove to the satisfaction of the AA claim of transit sale from one state to another against form E-1, he would be liable to pay penalty not exceeding one and a half times of the tax leviable.

Further, section 14 (6) of the Act provides that if any dealer fails to pay tax as required, he shall be liable to pay simple interest at the rate of one and a half *per cent* per month, if the payment is made within 90 days from the last date specified for the payment of tax. If the default continues thereafter, simple interest is chargeable at the rate of three *per cent* per month for the whole period from the last date specified for payment of tax to the date he makes the payment.

2.2.13.1 Scrutiny of the records of four[19] DETCs revealed that 56 dealers had purchased iron and steel from dealers who had evaded payment of tax on that sale. While finalising the assessments, the AAs failed to disallow ITC and levy penalty or had kept penal action pending. In another case, the AA failed to levy penalty after disallowing deduction from sale against form E-1. This resulted in short levy of tax and penalty amounting to Rs. 19.14 crore as mentioned below:

(Rupees in crore)

Sr. No.	Number of districts	No. of dealers	Value of goods sold/ purchased	Tax levied/ ITC disallowed	Tax leviable/ ITC to be disallowed	Penalty leviable	Nature of irregularity
1.	1	48	146.30	5.85	-	17.56	The AAs disallowed the ITC but penal action for levy of minimum penalty kept pending at the time of assessment in February and

[19] Ambala, Faridabad (West), Gurgaon (East) and Gurgaon (West).

Sr. No.	Number of districts	No. of dealers	Value of goods sold/ purchased	Tax levied/ ITC disallowed	Tax leviable/ ITC to be disallowed	Penalty leviable	Nature of irregularity
							March 2007 has not been finalised/initiated even after the lapse of 16/17 months.
2.	1	1	17.46	0.70	-	1.05	Maximum penalty leviable was not levied on account of disallowing of dealer's wrong claim of E-1 sale.
3.	3	8	3.53	-	0.13	0.40	No action to disallow the benefit of ITC and levy minimum penalty was initiated on account of purchases made from dubious[20] dealers.
Total		**57**	**167.29**	**6.55**	**0.13**	**19.01**	

2.2.13.2 During test check of the records of DETC, Hisar in December 2006, it was noticed that a dealer purchased iron/scrap valued as Rs. 1.06 crore from five dealers (selling dealers) between December 2003 and March 2004 and claimed ITC of Rs. 4.24 lakh. The AA got the purchases made by the assessee verified from the offices of DETC Jind and Sonipat and found that the selling dealers did not exist and were bogus dealers. Therefore, the AA, while finalising the assessment for the year 2003-04 in April 2005, rejected ITC and raised additional demand of Rs. 4.24 lakh and stated that action to levy interest would be taken separately. The AA did not levy minimum penalty of Rs. 12.72 lakh for maintenance of false/incorrect account and submission of false/incorrect returns. This resulted in non-levy of minimum penalty of Rs. 12.72 lakh, besides interest for non-payment of tax.

After the case was pointed out in December 2006, the AA admitted the facts and rectified the order in July 2007 and raised an additional demand of Rs. 17.86 lakh (including interest of Rs. 5.13 lakh upto July 2007). The department further stated in June 2008 that the action for recovery was in process. A report on recovery has not been received (August 2008).

2.2.14 Conclusion

Sales tax receipts contribute major tax revenue of the State. The review revealed a number of deficiencies in the system of allowing exemptions and concessions without obtaining statutory declarations/certificates in different forms or non-checking of genuineness and validity of declaration forms or acceptance of incomplete/invalid forms. Despite issue of departmental instructions, cross verification of transactions was not conducted from other circles/States before finalising the assessments by the AAs. The internal control mechanism of the department was abysmally weak as is evidenced by

[20] Dubious dealers means dealers engaged in nefarious activities of evasion of payment of tax.

the absence of an IAW which is the control of all controls and a management tool for plugging leakages of revenue.

2.2.15 Summary of recommendations

The Government may consider:

- inserting similar provisions regarding tax deposited in the declaration form VAT C-4 as contained in declaration form ST-14 and authentication/issuance of these forms by the department to ensure genuineness and correctness of tax deposited by the selling dealers while allowing ITC;
- ensuring cross verification of transactions against declaration forms with other circles/State before finalising the assessments and also prescribing reporting to the superior authorities of the results of such cross verification;
- prescribing submission of list of sales along with evidence/proof of sales of PVC pipes and related goods for claiming exemption/tax free sales; and
- setting up an internal audit wing in the Sales Tax Department to ensure timely detection and correction of errors in assessment, levy and collection of sales tax revenue and refund cases.

2.3 Non/short levy of purchase tax

Under the HGST Act, a dealer is liable to pay purchase tax on goods (other than goods specified in schedule B) purchased from within the State without payment of tax and used in the manufacture of tax free goods or taxable goods which are disposed of otherwise than by way of sales. In the event of default in payment, the dealer is liable to pay interest on the amount of tax remaining unpaid at one *per cent* per month for the first month and at one and a half *per cent* per month thereafter so long as the default continues. Further, if any dealer fails to pay the tax due, the Commissioner may impose a penalty not exceeding one and a half times the amount of tax to which he is assessed or is liable to be assessed.

During test check of the records of DETC, Panipat in July 2004, it was noticed that a dealer purchased goods (synthetic waste, chemicals, raw wools, shoddy waste and machinery parts etc.) valued as Rs. 4.62 crore from registered dealers within the State without payment of tax during the years 2001-02 (Rs. 3.12 crore) and 2002-03 (Rs. 1.50 crore). The dealer used these goods in the manufacture of blankets (tax free goods) and sold the blankets in the course of inter State trade or commerce. The AA, while finalising the assessments in March 2004, did not levy purchase tax treating the sale of blankets as tax free. This resulted in non-levy of purchase tax of Rs. 10.30 lakh. Additionally, interest and penalty for non-payment of tax due were also leviable.

After the case was pointed out in July 2004, the AA admitted (January 2007) the mistake and sent the case to DETC Panipat, RA for taking suo motu action. The RA raised an additional demand of Rs. 10.30 lakh in July 2007 and directed the AA to take action to levy interest and penalty under the Act. The department further intimated in June 2008 that a sum of Rs. 2.57 lakh had been recovered in February 2008. A report on recovery of the balance amount and action to levy interest and penalty has not been received (August 2008).

The matter was reported to the Government in August 2004; their reply has not been received (August 2008).

2.4 Short levy of tax due to incorrect classification

Under the HVAT Act, tax is leviable at the rates specified in Schedules 'A' to 'G' of the Act depending upon the classification of goods. Mosquito mats/coils and other mosquito repellents were taxable as specified commodity under Schedule 'C' at the rate of 10 *per cent* from 11 December 2002 to 31 March 2003 under the HGST Act. The State Government did not specify this commodity under any schedule of the HVAT Act with effect from 1 April 2003. It has judicially been held[21] in August 1998 that mosquito coil/mats cannot be treated as insecticides and is commonly known as repellent and taxable as such. Mosquito mats/coils and other mosquito repellents, being non-specified item in any schedule, is leviable to tax at the general rate of 10 *per cent*.

During test check of the records of DETC, Ambala Cantonment in November and December 2007, it was noticed that two dealers made sales of mosquito mats/coils valued as Rs. 19.63 crore during the years 2003-04 and 2004-05. The AA, while finalising the assessments between May 2006 and February 2007, levied tax at the rate of four *per cent* treating the goods as insecticides instead of the correct rate of 10 *per cent*. Incorrect classification resulted in short levy of tax of Rs. 1.17 crore.

After the cases were pointed out in November and December 2007, the AA stated in November and December 2007 that mosquito mats/coils were correctly classified and taxed as insecticides. The contention of the AA was not tenable in view of the provisions of the HGST/HVAT Act and the judicial pronouncement.

The matter was reported to the department and the Government in February 2008; their reply has not been received (August 2008).

2.5 Short recovery of lump sum tax on works contract

As per the Haryana Government notification dated 7 April 2003 issued under the HVAT Act, a contractee shall, deduct from the payment made to a contractor for execution of a works contract in the State involving transfer of goods (whether as goods or in some other form), tax in advance calculated at the rate of four *per cent* of the amount paid. Further, if a dealer fails to pay the

[21] M/s Sonic Electrochem and another Vs. Sales Tax Officer and others {(1998) 12 PHT 215 (Supreme Court)}.

whole or any part of the tax, he shall be liable to pay penalty, in addition to the amount of tax, a sum equal to the amount of tax so assessed.

2.5.1 During test check of the records of DETC, Karnal in August 2007, it was noticed that a contractor executed a works contract and the contractee paid Rs. 12.25 crore during the year 2003-04. The contractee (dealer) deducted tax at the rate of two *per cent* instead of four *per cent*. The AA, while finalising the assessment in March 2007, failed to detect the mistake. The omission resulted in short levy of tax of Rs. 24.49 lakh.

After the case was pointed out in August 2007, the AA stated in January and April 2008 that the case had been sent to the RA, Karnal for taking suo motu action in January 2008. Further report has not been received (August 2008).

2.5.2 During test check of the records of DETC, Faridabad (West) in September 2007, it was noticed that the dealer company (contractor) was engaged in building construction and paid tax in lumpsum. A firm of Faridabad (contractee) supplied cement and steel valued as Rs. 3.21 crore during the year 2003-04. The AA, while finalising the assessment in March 2007, allowed deduction of Rs. 3.21 crore from the gross turnover of Rs. 27.03 crore for the tax paid cement and steel supplied by the contractee to the contractor for use in the project. In the case of a dealer involved in the execution of works contract, no deductions except labour and service charges were admissible under the ambit of definition of sale price. Inadmissible allowing of deduction resulted in underassessment of tax of Rs. 12.84 lakh.

After the case was pointed out in September 2007, the AA stated in June 2008 that the case was sent to the RA Faridabad for taking suo motu action. Further report has not been received (August 2008).

2.5.3 During test check of the records of DETC, Faridabad (West) in September 2007, it was noticed that a works contractor received payment of Rs. 1.83 crore for execution of the works contract between April 2003 and March 2005. However, the contractee while allowing payment to the contractor incorrectly deducted tax at the rate of two *per cent*. The AA while finalising the assessments for the years 2003-04 and 2004-05 in November 2005 and August 2006, erroneously levied tax at the rate of two *per cent* instead of four *per cent*. This resulted in short levy of tax of Rs. 3.66 lakh, besides penalty.

After the case was pointed out in September 2007, the AA stated in January and June 2008 that a notice had been issued to the dealer for rectification of the order. Further report has not been received (August 2008).

The matter was reported to the department and the Government in November and December 2007; their reply has not been received (August 2008).

2.6 Excess allowing of input tax credit

Under the HVAT Act and the rules framed thereunder, claim of input tax can be allowed to the purchasing dealer only when the tax has been deposited by the selling dealer. With a view to detect evasion of VAT by claiming fraudulent ITC by issuing forged tax invoices or fictitious accounting of goods

neither purchased nor sold etc., the ETC issued instructions in March 2006 for cross verification of all purchase transactions totaling more than Rs. 1 lakh from a single VAT dealer in a year. As per direction issued by the JETC (Range), Faridabad in March 2007, claim of input VAT in respect of purchases made from dealer A and dealer B was admissible at nil and 35 *per cent* respectively during assessment year 2003-04.

During test check of the records of DETC, Faridabad (West) in August and September 2007, it was noticed that two dealers purchased cold rolled steel strips and iron and steel scrap valued as Rs. 2.74 crore (dealer A: Rs. 75 lakh; dealer B: Rs. 1.99 crore) during the year 2003-04 and claimed ITC of Rs. 10.98 lakh. The AAs, while finalising the assessments in January and March 2007, allowed the ITC of Rs. 10.98 lakh. Since JETC (Range) had issued direction on 1 March 2007 for allowing ITC at nil and 35 *per cent* of purchases made from dealer A and dealer B, the AAs were required to revise the assessment order of January 2007 and take into consideration the directions at the time of finalisation of assessment on 23 March 2007. Failure on the part of AAs to initiate action for allowing ITC as per direction of JETC (Range) in March 2007 resulted in non-raising of demand and excess allowing of ITC totalling Rs. 8.19 lakh.

After the cases were pointed out in August and September 2007, the AA disallowed ITC and raised demand of Rs. 3.69 lakh in August 2007. The department intimated in June 2008 that a sum of Rs. 2.68 lakh (out of Rs. 3.69 lakh) had been recovered in January 2008. A report on recovery of the balance amount and reply in the remaining case has not been received (August 2008).

The matter was reported to the Government in December 2007; their reply has not been received (August 2008).

2.7 Underassessment of tax due to allowing of excess benefit of deferment

The HVAT Act, read with the HVAT Rules, 2003 provides that an industrial unit availing the benefit of deferment of payment of tax, may in lieu of making payment of the deferred tax after five years, pay half of the amount of the deferred tax upfront along with the returns and on making payment in this manner, the tax due according to the returns shall be deemed to have been paid in full. If the tax calculated is more than the input tax, the difference of the two shall be the tax payable.

During test check of the records of DETC, Panipat in August 2007, it was noticed that the assessee availing deferment from payment of tax for the period from 3 December 1998 to 2 December 2007 had opted to pay 50 *per cent* of the tax in lieu of deferment of payment of tax under the HVAT Rules. The assessee had made sale of goods valued as Rs. 6.52 crore involving tax of Rs. 26.06 lakh during the year 2004-05. After adjusting input tax of Rs. 14.55 lakh paid on purchases of goods (Rs. 3.64 crore) from tax of Rs. 26.06 lakh, the balance tax payable was Rs. 11.51 lakh. The dealer was entitled to exemption of 50 *per cent* of deferred tax amounting to

Rs. 5.76 lakh. The AA, while finalising the assessment in May 2006, allowed 50 *per cent* of total tax liability i.e. Rs. 13.03 lakh instead of admissible amount of Rs. 5.76 lakh. This resulted in excess exemption of tax of Rs. 7.27 lakh.

After the case was pointed out in August 2007, the ETO, Panipat intimated in June 2008 that the case had been sent to the RA for taking suo motu action in September 2007. The RA decided the case and created additional demand of Rs. 12.85 lakh including interest of Rs. 6.42 lakh in May 2008. A report on recovery has not been received (August 2008).

The matter was reported to the department and the Government in November 2007; their reply has not been received (August 2008).

2.8 Incorrect allowing of deduction from gross turnover

Under the HVAT Act, where a works contractor appoints a sub contractor, who executes the works contract, whether in whole or in part, the contractor and the sub contractor shall both be jointly and severally liable to pay tax in respect of the transfer of property in goods involved in the execution of the works contract executed by the sub contractor. As per clarification issued in March 2006 by the Government, the sub contractor is not absolved from tax liability as was the case under HGST Act, but liable to pay tax under the HVAT Act.

During test check of the records of DETC, Gurgaon (West) in August 2006, it was noticed that a contractor claimed deduction of Rs. 54.34 lakh from the gross turnover (GTO) on account of the work done as a sub contractor without submitting any proof of payment of tax on the entire amount of the main contract. The AA, while finalising the assessment for the year 2003-04 in March 2006, erroneously allowed deduction of Rs. 54.34 lakh from the GTO of the contractor on the basis of the affidavit relating to the execution of the works contract as sub contractor. The omission resulted in underassessment of tax of Rs. 2.17 lakh.

After the case was pointed out in August 2006, the AA sent the case to DETC, Gurgaon (RA) for taking suo motu action in February 2007 and the RA raised an additional demand of Rs. 2.17 lakh in June 2007. A report on recovery has not been received (August 2008).

The matter was reported to the department and the Government in September 2006; their reply has not been received (August 2008).

2.9 Underassessment of tax due to application of incorrect rate

As per the notification issued on 8 July 2003 under the HVAT Act, VAT on components, spare parts and accessories of motor vehicles including those of tractors is leviable at the rate of 12 *per cent* (at 10 *per cent* under general category upto 7 July 2003).

During test check of the records of DETC, Faridabad (West) in July 2007, it was noticed that a dealer sold components of tractors valued as Rs. 1.05 crore

between 8 July 2003 and 31 March 2004 and paid tax at the general rate of 10 *per cent*. The AA, while finalising the assessment for the year 2003-04 in March 2007, levied tax at the rate of 10 *per cent* instead of the correct rate of 12 *per cent* on the sales of Rs. 1.05 crore. Application of incorrect rate of tax resulted in underassessment of VAT of Rs. 2.09 lakh. Additionally, interest was also leviable.

After the case was pointed out in July 2007, the AA admitted the audit observation and raised (December 2007) additional demand of Rs. 4.03 lakh including interest. A report on recovery has not been received (August 2008).

The matter was reported to the department and the Government in December 2007, their reply has not been received (August 2008).

2.10 Inadmissible allowing of input tax credit

Under the HVAT Act, input tax in respect of any goods purchased by a VAT dealer shall be the amount of tax paid to the State on the sale of such goods to him.

During test check of the records of the DETC, Faridabad (West) in October 2007, it was noticed that the AA, while finalising the assessment for the year 2003-04 in December 2006, allowed ITC of Rs. 2.08 lakh on purchases of goods valued as Rs. 51.94 lakh from within the State. Audit scrutiny revealed that the invoices against which ITC was allowed actually pertained to the purchases of goods in May 2004. Thus, ITC of Rs. 2.08 lakh was not admissible during assessment year 2003-04. This resulted in inadmissible allowing of ITC of Rs. 2.08 lakh.

After the case was pointed out in October 2007, the AA admitted the audit observation and stated in October 2007 that rebate was wrongly allowed to the dealer during assessment year 2003-04 and necessary rectification order was being passed. A report on action taken has not been received (August 2008).

The matter was reported to the department and the Government in December 2007; their reply has not been received (August 2008).