

CHAPTER II SALES TAX

2.1 Results of Audit

Test check of sales tax assessments, refund cases and connected documents of commercial tax offices conducted during the year 2007-08 revealed under assessment of turnover, non-levy of interest, grant of incorrect exemption, application of incorrect rate of tax etc. amounting to Rs. 334.37 crore in 1,055 cases which fall under the following cases:

(Rupees in crore)

Sl. No.	Category	Number of cases	Amount
1.	Claim for compensation of loss of revenue due to introduction of value added tax	4	227.83
2.	Grant of incorrect exemption	91	16.79
3.	Application of incorrect rate of tax	178	15.65
4.	Turnover escaping assessment	210	7.01
5.	Non/short levy of interest	147	5.83
6.	Incorrect grant of concessional rate of tax	15	1.17
7.	Grant of excess credit	15	0.10
8.	Other lapses	395	59.99
	Total	1,055	334.37

During the year 2007-08, the department accepted underassessments and other deficiencies of Rs. 5.22 crore involved in 289 cases of which 119 cases involving Rs. 3.49 crore were pointed out during 2007-08 and the remaining in earlier years. The department recovered Rs. 2.17 crore in 181 cases during the year 2007-08 of which 87 cases involving Rs. 1.20 crore related to the year 2007-08 and the balance to the remaining years.

After the issue of draft paragraphs, the department recovered Rs. 88.81 lakh in five cases.

A few illustrative cases involving Rs. 253.11 crore are mentioned in the succeeding paragraphs.

2.2 Claim for compensation of loss of revenue due to introduction of Value Added Tax

Introduction

The value added tax (VAT) was implemented in Kerala with effect from April, 2005. The Government of India (GOI) agreed to compensate the State Government for loss of revenue consequent to the implementation of VAT and issued guidelines in June 2006 on the modalities for calculation of compensation claims. As per the guidelines, VAT receipts were to be compared with the revenue of the pre-VAT period, suitably extrapolated on the basis of average growth rate of revenue of the previous five years. Further, tax receipts from petrol, diesel, aviation turbine fuel (ATF), liquor and input tax credit (ITC) under VAT adjusted against central sales tax (CST) were to be excluded while computing the receipts. These amounts were to be deducted from the total revenue collection for the year 2005-06. The resultant net revenue was to be compared with the projected tax revenue for 2005-06 to arrive at the loss due to the introduction of VAT. The compensation was allowed at 100 per cent and 75 per cent of such loss of revenue during the year 2005-06 and 2006-07 respectively. The State Government preferred compensation claim of Rs. 1,006.44 crore and Rs. 389.36 crore for the years 2005-06 and 2006-07 respectively against which the GOI sanctioned Rs. 882.70 crore for 2005-06 upto March 2007 and Rs. 110 crore for 2006-07 upto March 2008.

Test check of the records of offices of nine¹ Deputy Commissioners (DCs) and 14² Commercial Tax Offices, Special circle for the year 2005-06 and five³ DCs, seven⁴ Commercial Tax Offices, Special circle for the year 2006-07 was conducted between August 2007 and July 2008. The important audit findings are mentioned in the succeeding paragraphs.

2.2.1 Incorrect remittance of VAT

According to the guidelines of June 2006 issued by the GOI, the entire revenue realised under the Kerala Value Added Tax (KVAT) Act, 2003 (implemented from 1 April 2005), should be considered for working out the actual claim of compensation. Petroleum products other than petrol, diesel and ATF would fall under the KVAT Act.

Test check of the records, in special circle II, Ernakulam, revealed that tax paid under VAT on petroleum products other than petrol, diesel and ATF amounting to Rs. 10.57 crore by M/s. Indian Oil Corporation Limited was remitted under Kerala General Sales Tax (KGST) Act instead of the KVAT Act during 2005-06. This resulted in short accounting of receipts under the KVAT Act and thereby excess claim of compensation of Rs. 10.57 crore from the GOI.

¹ Alappuzha, Ernakulam, Idukki, Kollam, Kottayam, Kozhikode, Mattancherry, Palakkad and Thiruvananthapuram.

² Alappuzha, Ernakulam II & III, Kannur, Kattappana, Kollam, Kottayam, Kozhikode I & II, Mattancherry (HP), Palakkad, Pathanamthitta, Thiruvananthapuram and Thrissur.

³ Ernakulam, Kollam, Kottayam, Mattancherry and Thiruvananthapuram.

⁴ Aluva, Ernakulam II & III, Kollam, Kottayam, Mattancherry and Thiruvananthapuram.

2.2.2 Incorrect computation of projected VAT revenue

According to the guidelines of June 2006 issued by the GOI, for the purpose of computing projected revenue for the year 2005-06 and onwards, the tax revenue for the period from 1999-2000 to 2004-05 shall be taken into account. The calculations are required to be made on the basis of net tax revenue from VAT items. The tax revenue from non-VAT items like petrol, diesel, liquor etc. and CST receipts are to be excluded from the calculations. The annual growth rate would be worked out for each year, starting with the growth rate for the year 2000-01 over the year 1999-2000. Thereafter, three best growth rates shall be selected and simple arithmetic average of these rates shall be taken to arrive at the average annual growth rate.

Test check of the records revealed that the department incorrectly computed the average growth rate as 17.94 *per cent* instead of 15.68 *per cent*. This was due to incorrect reduction of Rs. 700.36 crore against the correct figure of Rs. 406.93 crore as CST receipts for the year 2003-04 and Rs. 293.67 crore towards entry tax for the years 2000-01 to 2004-05 for computing the net tax revenue for the purpose of compensation claim. The incorrect computation resulted in short claim of Rs. 84.58 crore (Rs. 1,091.02 crore - Rs. 1,006.44 crore) for the year 2005-06 and Rs. 7.09 crore (Rs. 396.45 crore - Rs. 389.36 crore) for the year 2006-07.

2.2.3 Incorrect computation of input tax credit adjusted against CST

Test check of the records of six⁵ DCs revealed that there was variation between the figures of ITC adjusted against CST furnished by the respective Deputy Commissioners to the Commissioner of Commercial Taxes (CCT) and that was actually allowed in the assessment orders by these offices during the year 2005-06. This resulted in short claim of Rs. 12.04 crore from the GOI.

2.2.4 Delayed grant of refunds

As per instructions contained in circular issued (January 2006) by the Commissioner of Commercial Taxes (CCT), refund of input tax credit on account of inter state sale, branch/stock transfer outside the State and export contemplated in Section 13(2) of the KVAT Act for the year 2005-06 were to be allowed within a reasonable period of time, so as to ensure that as far as possible, all claims received upto February 2006 were processed and refunds allowed to dealers before 31 March 2006. The particulars of such refunds allowed were also required to be reported to the CCT by the 20th of every month.

Test check of the records revealed that refund of excess input tax of Rs. 91.07 crore in 11⁶ offices eligible for claiming compensation for the year 2005-06 was allowed during 2006-07 and 2007-08 and for the year 2006-07, refund of excess input tax of Rs. 22.73 crore in three offices⁷ was allowed during 2007-08 and 2008-09. Due to delay in scrutinising these claims of refund, Rs. 91.07 crore for the year 2005-06 and Rs.17.05 crore being 75 *per cent* of

⁵ Kollam, Kottayam, Kozhikode, Mattancherry, Palakkad, and Thiruvananthapuram.

⁶ Office of the DCs: Alappuzha, Ernakulam, Idukki, Kannur, Kasaragod, Kottayam, Kozhikode, Mattancherry, Palakkad, Pathanamthitta and Thrissur.

⁷ Office of the DCs: Ernakulam, Kottayam and Mattancherry.

Rs. 22.73 crore for the year 2006-07 could not be incorporated in the compensation claim preferred by the State Government to the GOI.

2.2.5 Refund of ITC without adjusting old arrears

Under Section 11(6) and 13(3) of the KVAT Act, excess input tax at credit shall be adjusted against any tax or any amount due from the dealer under this Act or under the provisions of the KGST Act, 1963 or the Central Sales Tax Act, 1956 or under the Tax on Entry of Goods into Local Areas Act, 1994.

Test check of the records of special circle II and III, Ernakulam revealed that while allowing refunds of Rs. 61.20 crore between March 2006 and September 2007 to three dealers, the arrears of Rs. 16 crore were not adjusted from the refunds allowed.

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

2.3 Short levy due to irregular exemption

2.3.1 Under Section 5(2) of the KGST Act, in respect of manufactured goods other than tea which are sold under a trade mark or brand name, the sale by the brand name holder shall be the first sale within the State for the purpose of the Act. By a notification issued in November 1993, the Government exempted small scale industrial (SSI) units from payment of tax due on their goods manufactured and sold by them for a period of seven years from the date of commencement of production. It has been judicially held⁸ that SSI exemption is not applicable if goods are manufactured with brand name or trade name of another manufacturer.

2.3.1.1 During scrutiny of the records in CTO, special circle, Mattancherry in November 2007, it was noticed that while finalising the assessment of a dealer for the years 2001-02 to 2004-05 between August 2006 and March 2007, turnover of Rs. 61.15 crore was exempted as second sales. As the assessee had sold the goods under their brand name, exemption allowed was not in order. This resulted in non-levy of tax Rs. 8.35 crore.

After the matter was reported to the department in November 2007 and the Government in February 2008, the Government stated in December 2008 that action had been initiated to revise the assessments.

2.3.1.2 During scrutiny of the records in CTO, Ponkunnam in December 2007, it was noticed that while finalising the assessments of an SSI unit for the years 1999-2000 to 2002-03 between December 2002 and September 2006, the assessing authority adjusted tax of Rs. 74.07 lakh, on the goods manufactured and sold by the assessee against the SSI exemption granted by the General Manager, District Industries Centre (GM, DIC), Kottayam. The assessee manufactured and sold goods under the brand name and got the right to use the brand name by virtue of an agreement with another unit and by paying royalty to them. The goods manufactured and sold by the assessee was in the brand name of another unit and hence not eligible for SSI exemption. This resulted in short levy of tax of Rs. 74.07 lakh.

⁸ Commissioner of Central Excise, Raipur V/s. Hira cement in 145 STC 264 (SC)

The matter was reported to the department in December 2007 and the Government in April 2008. The Government stated in July 2008 that the assessee claimed SSI exemption after fulfilling the requirements mentioned in the notification granting SSI exemption to manufacturing units within the State. The reply is not tenable in view of the judicial pronouncement mentioned above. Further report has not been received (December 2008).

2.3.2 Under the KGST Act, if conversion of field latex into centrifuged latex does not involve any manufacturing process, purchase turnover of field latex in proportion to the centrifuged latex sold inter state is assessable to tax. It has been judicially held⁹ that there was no manufacture involved in the conversion of field latex into centrifuged latex. Rubber purchased within the State is taxable at 11 *per cent* at the point of last purchase.

2.3.2.1 During scrutiny of the records in three offices¹⁰ between June 2007 and October 2007, it was noticed that while finalising the assessments of four assessees for the assessment years 2000-01 and 2002-03, between October 2006 and February 2007 the assessing authorities exempted the purchase turnover of Rs. 26.30 crore in respect of field latex used in the conversion of centrifuged latex/crumb rubber/cream latex which was sold inter state. This resulted in non-levy of tax of Rs. 1.84 crore.

After the cases were pointed out between June 2007 and October 2007, the department stated between August 2007 and January 2008 that normal latex and centrifuged latex are different commodities and there involved manufacturing process when field latex is converted into centrifuged latex. The reply is not tenable in view of the judicial pronouncement mentioned above. Further report has not been received (December 2008).

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

2.3.2.2 During scrutiny of the records in CTO, special circle, Kottayam in August 2007, it was noticed that while finalising the assessments of a dealer engaged in the business of sale of rubber, gloves etc. for the years 2002-03 to 2004-05 between December 2006 and March 2007, the assessing authority allowed exemption of Rs. 3.04 crore being the value of processing loss and this resulted in short levy of tax of Rs. 42.47 lakh.

After the case was pointed out in August 2007, the department stated that processing loss upto four *per cent* was allowable in terms of quantity. This was incorrect as rubber was taxable at the point of last purchase. However, the reply given by the department is incorrect in terms of the provisions of the Act cited above. Further report has not been received (December 2008).

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

⁹ M/s Kurien Abraham V/s State of Kerala and others in 12 KTR 235.

¹⁰ Inspecting assistant commissioner, Idukki, CTO third circle Thrissur and CTO special circle Thrissur.

2.3.3 Under the CST Act, sale or purchase of goods shall be deemed to take place in the course of inter state trade or commerce if the sale or purchase occasions the movement of goods from one State to another. Every dealer shall be liable to pay tax on all such sales effected by him in the course of inter state trade or commerce.

During scrutiny of the records in CTO, special circle, Kottayam, in September 2007, it was noticed that while finalising the CST assessment in March 2007 for the year 2001-02 of a dealer engaged in the manufacture and sale of tread rubber, the assessing authority incorrectly exempted, inter state turnover of Rs. 1.71 crore. This resulted in non-levy of tax of Rs. 23.55 lakh.

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

2.3.4 Under the KGST Act, every contractor engaged in civil works, may at his option, pay tax at the rate of two *per cent* on the whole amount of contract which shall be deducted from the payments made by the awardee at every time including advance payment and shall remit it to the Government in such manner as may be prescribed.

During scrutiny of the records in CTO, WC & LT, Kannur in March 2007, it was noticed that a contractor engaged in civil works was running a metal crusher unit in the same registration number. The assessee had, however, opted to pay tax at compounded rates both for crusher unit and works contract. While finalising the assessments for the year 2000-01 to 2002-03 between December 2005 and February 2006, the assessing authority incorrectly exempted Rs. 10.42 crore being charges for supply of crushed ballast on the plea that tax was already paid on the turnover. Omission to assess the turnover at the rate of two *per cent* resulted in short levy of tax of Rs. 21.96 lakh.

After the case was pointed out to the department in March 2007 and reported to the Government in December 2007, the Government stated in June 2008 that the supply of crushed stone ballast was a sale and not works contract and hence the exemption granted was correct. The reply is not correct as the assessee opting for compounding was liable to pay tax on the gross turnover. Further report has not been received (December 2008).

2.3.5 Under the CST Act, branch transfer of goods, from one state to another, other than by way of sale, is to be proved by the dealer who effects branch transfer by furnishing declaration in form F¹¹ duly filled and signed by the principal or agent of the other place of business, along with the evidence of despatch of such goods.

During scrutiny of the records in CTO, special circle, Kollam in July 2007, it was noticed that while finalising the CST assessment of a dealer for the year 2004-05 in December 2006, turnover of Rs. 26 lakh was exempted as branch transfer on the basis of form F filed by the assessee, received from a consignee at Delhi who had no valid registration. This has been substantiated by the findings of Intelligence wing of the department in another assessment

¹¹ To prove that transfer of goods claimed is otherwise than by way of sale

(November 2006) in the same office. This resulted in short levy of tax of Rs. 2.60 lakh.

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

2.4 Short levy due to incorrect rate of tax

2.4.1 Under the KGST Act, rate of tax depends on the nature of sale, point of sale and also on the kind of commodity. Rubber purchased within the State was taxable at the rate of 12 *per cent* at the point of last purchase and subsequently the rate was reduced to 11 *per cent* with effect from 1 April 2000. By a notification issued in December 1999, the term 'manufacture' was defined. Treating raw rubber in any form with chemicals to form a compound of rubber by whatever name the same is called would not fall under the definition of manufacture.

During scrutiny of the records in CTO, special circle, Kottayam, in September 2007, it was noticed that a medium and large scale industrial unit engaged in the manufacture and sale of tyre, tube, compound rubber etc., purchased rubber for Rs. 156.64 crore during the years 2003-04 and 2004-05, converted it into compound rubber and transferred to branches outside the State. While finalising the assessments for these years in October 2006, the assessing authority incorrectly applied concessional rate of six *per cent* instead of 11 *per cent* on the purchase turnover of Rs. 156.64 crore. This resulted in short levy of tax of Rs. 9.01 crore.

After the case was pointed out, the assessing authority stated in September 2007 that the Sales Tax Appellate Tribunal in September 2005 had held in the case of assessment years 1990-91 to 1996-97 that the compound rubber manufactured by the assessee and that specified in the notification are different. The reply is not correct as the decision of the Tribunal was based on the provisions of a notification prevailing during that period and the notification issued in December 1999, in supersession of all previous notifications, is relevant for the periods 2003-04 and 2004-05. Further report has not been received (December 2008).

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

2.4.2 By a notification issued in December 1999, the tax payable by SSI units was reduced to eight *per cent*. As per the norms fixed by the Government of India, an industrial unit would continue to enjoy the benefits of SSI status as long as the investment in plant and machinery does not exceed Rs. 3 crore.

During scrutiny of the records in CTO, special circle, Kottayam, in June 2006 it was noticed that while finalising the assessments in December 2005 of an industrial unit having SSI registration for the years 2002-03 and 2003-04, sales turnover of *hawai chappals* was subjected to tax at the concessional rate of eight *per cent* instead of the correct rate of 12 *per cent*, though the limit fixed by the Ministry of Industry, Government of India in respect of investment in plant and machinery had exceeded the limit prescribed. This resulted in short levy of tax of Rs. 1.44 crore.

After the case was pointed out in June 2006, the department stated in June 2006 that the unit was having SSI registration at the time of assessment and hence assessed to tax at the concessional rate. However, the fact remains that as per the profit and loss accounts of the assessee, the investment in plant and machinery was Rs. 3.43 crore and Rs. 3.91 crore for the assessment years 2002-03 and 2003-04 respectively and thus the assessee ceased to be an SSI unit from 2002-03.

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

2.4.3 The KGST Act, as amended by the Finance Act 2004, stipulates that any dealer in gold or silver ornaments or wares may at his option, pay tax at 130 *per cent* of the tax payable by him as conceded in the return or accounts or the tax paid for the previous consecutive three years whichever is higher. Further, if an assessee paying tax in accordance with the provision of section 7(1) (a) of the Act, opens a new branch during a year such branch shall be treated as an independent place of business and these provisions shall also apply to it.

During scrutiny of the records in CTO, special circle, Kasaragod, in June 2007, it was noticed that while finalising the assessments for the year 2004-05 between November and December 2006, of two dealers in gold who were paying tax under section 5 (1) of the KGST Act and had not opted for compounding, the assessing authority incorrectly allowed these assesses to pay compounded tax for their newly opened branches. This resulted in short levy of tax of Rs. 11.47 lakh.

After the cases were pointed out to the department in June 2007 and reported to the Government in December 2007, the Government stated in July 2008 that the amendment to the section enables a dealer to treat his branch as a separate unit and he can opt for paying tax under section 7(1) for the branch alone. The reply is not tenable as the proviso inserted below section 7(1) is applicable to a dealer paying tax in accordance with the provisions of the said section.

2.4.4 Under the CST Act, on inter state sale of goods made to registered dealers and supported by prescribed declaration in form C, central sales tax is leviable at the concessional rate of four *per cent* or at such lower rate as applicable to the sale or purchase of such goods within the State. Tax on goods not covered by such declaration, in the case of declared goods, shall be calculated at twice the rate applicable in the State and in respect of other goods at 10 *per cent* or at the rate applicable to the sale of such goods inside the State whichever is higher.

2.4.4.1 During scrutiny of the records in CTO, second circle, Thalassery, while finalising the assessment for the year 2003-04 of an assessee engaged in the manufacture and sale of furniture in March 2007, the assessing authority allowed concessional rate of tax at the rate of two *per cent* on sales turnover of Rs. 3.96 crore, though valid declaration in form C was available only for an amount of Rs. 3.09 crore. This resulted in short levy of tax of Rs. 10.19 lakh.

After the case was pointed out in June 2007, the department stated in September 2007 that action had already been initiated to rectify the assessment.

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

2.4.4.2 During scrutiny of the records in CTO, special circle, Thiruvananthapuram in August 2007, it was noticed that while finalising the assessment of an SSI unit for the year 2002-03 in March 2007, turnover of Rs. 28.37 lakh relating to inter state sale of electronic goods, not covered by form C, was taxed at four *per cent* instead of the correct rate of 10 *per cent*. This resulted in short levy of tax of Rs. 3.61 lakh.

After the case was pointed out to the department in September 2007 and reported to the Government in April 2008, the Government stated in July 2008 that the turnover of Rs. 28.37 lakh not covered by valid form C was assessed at the higher rate demanding tax of Rs. 3.61 lakh and interest thereon. A report on recovery has not been received (December 2008).

2.4.4.3 During scrutiny of the records in CTO, special circle, Palakkad, in August 2006, it was noticed that while finalising the assessment of a dealer for the year 2002-03 in December 2005, inter state sales turnover of extra neutral alcohol (ENA), not covered by form C declaration was assessed to tax at 10 *per cent* instead of at the correct rate of 20 *per cent* plus additional sales tax (AST). This resulted in short levy of tax of Rs. 3.48 lakh.

After the case was pointed out to the department in August 2006 and reported to the Government in April 2008, the Government stated in September 2008 that the assessment had been revised creating an additional demand of Rs. 3.48 lakh. A report on recovery has not been received (December 2008)

2.4.4.4 During scrutiny of the records in CTO, special circle, Kottayam, in September 2007, it was noticed that while finalising the assessment of a dealer engaged in business of manufacture and sale of tyre, tube etc. for the year 2003-04 in January 2007, turnover of tread rubber for Rs. 72.29 lakh sold inter state not covered by declaration in form C was assessed to tax at the rate of 10 *per cent* instead of the correct rate of 12 *per cent* plus AST. This resulted in short levy of tax of Rs. 2.75 lakh.

After the case was pointed out in September 2007, the assessing officer stated in September 2007 that the assessee being a medium and large scale industry was eligible for reduced rate of two *per cent* upto 29 December 2003 and that in the absence of form C, tax was levied at higher rate of 10 *per cent*. The reply is not tenable, as the rate applicable was 12 *per cent* plus AST. Further report has not been received (December 2008).

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

2.4.5 Under the KGST Act, sales turnover of soda was taxable at 20 *per cent* at the point of first sale in the state by a dealer liable to pay tax.

During scrutiny of the records in three CTOs¹², in December 2007, it was noticed that while finalising the assessment of three dealers for the years 1997-98 to 2003-04 between April 2005 and February 2007, the assessing authorities exempted the turnover of soda valued at Rs. 31.76 lakh as second

¹² Attingal, Kodungallur and fourth circle, Thrissur.

sales, which was purchased from registered dealers in Kerala, whose turnover was below the taxable limit of Rs. 2 lakh and hence not liable to tax. This resulted in short levy of tax of Rs. 6.95 lakh.

After the cases were pointed out to the department in December 2007 and the Government in April 2008, the Government stated in July 2008 that if the second seller proves that the first seller is liable to tax, the second seller cannot be subjected to tax. The reply is not tenable as in the instant case the first seller is not liable to tax as his turnover was below the assessable limit and hence the second seller is liable to be taxed as per the provisions of the KGST Act which was upheld in a judicial decision¹³. Further reply has not been received (December 2008).

2.4.6 Under entry 106 (i) of 1st schedule to the KGST Act, the rate of tax on sale of paper was eight *per cent* at the point of first sale in the state, with effect from 31 December 2001.

During scrutiny of the records in CTO, third circle, Ernakulam in November 2007, it was noticed that while finalising the assessment of a dealer for the year 2001-02 in February 2007, the sales turnover of paper valued at Rs. 1.05 crore effected between 31 December 2001 and 31 March 2002 was incorrectly assessed at the rate of four *per cent* instead of eight *per cent*. This resulted in short levy of tax of Rs. 4.84 lakh.

After the case was pointed out to the department in November 2007 and reported to the Government in April 2008, the Government stated in July 2008 that the assessment was revised and tax amounting to Rs. 3.88 lakh with interest of Rs. 2.66 lakh was collected. However, the reasons for the difference in tax pointed out in audit and that demanded by the department have not been intimated despite being requested (December 2008).

2.4.7 Under the KGST Act, every contractor in civil works may opt to pay tax at two *per cent* of the whole amount of his contract and every other contractor may opt to pay tax at 70 *per cent* of the rates shown in the Fourth Schedule against such contract.

During scrutiny of the records in CTO, works contract and luxury tax, Thrissur in August 2007, it was noticed that while finalising the assessment of a dealer engaged in the work of collection, supply and stacking of crushed ballast and loading and unloading from railway wagon for the year 2004-05 in March 2007, the assessing authority treated the work as civil work and levied tax at the rate of two *per cent* instead of 70 *per cent* of the rate shown under entry 22 of schedule IV. This resulted in short levy of tax of Rs. 2.14 lakh.

After the case was pointed out to the department in August 2007 and reported to the Government in December 2007, the Government stated in August 2008 that the assessment was reopened in January 2008 and revenue recovery certificate (RRC) issued to collect the amount. A report on recovery has not been received (December 2008).

¹³ E M Purushothaman V/s State of Kerala in 134 STC 326

2.5 Non/short levy of interest

Under the KGST Act, where any dealer has failed to include any turnover in any return filed by him or any turnover has escaped assessment, interest shall accrue on the tax due on such turnover with effect from such date on which the tax would have fallen due for payment had the dealer included it in the return relating to the period to which such turnover related. The interest payable shall be at the rate of one *per cent* per month for the first three months and at the rate of two *per cent* per month for the subsequent months of delay upto 31 March 2005 and at the rate of one *per cent* per month thereafter. It has been judicially¹⁴ held that where the dealer has not filed the prescribed return of his turnover, the case is clearly one of “escaped assessment”.

During scrutiny of the records in three CTOs¹⁵, between July and December 2007, it was noticed that while finalising the assessments for the years 1998-99 and 2001-02 to 2004-05 of three assesseees, the assessing authorities though levied tax on the suppressed turnover of Rs. 22.44 crore but did not levy interest on the tax due thereon. Non-levy of interest worked out to Rs. 82.13 lakh.

After the cases were pointed out to the department between July and December 2007 and reported to the Government in April 2008, the Government stated between July 2008 and August 2008 that in two cases interest of Rs. 23.54 lakh was demanded. Further report on the matter has not been received (December 2008).

2.6 Short levy of tax and interest due to non-appropriation of payment

2.6.1 Under the KGST Act, where any dealer has failed to include any turnover in the return filed by him, or any turnover has escaped assessment or if the tax is not paid by him within the time prescribed, the dealer shall pay interest at the rate of one *per cent* per month for the first three months and at the rate of two *per cent* per month for subsequent months of delay. Further any tax or any other amount due or demanded is paid by the dealer, the payment so made shall be appropriated first towards interest accrued on such tax or other amount under sub section 3 of Section 23 on such date of payment and the balance available shall be appropriated towards principal outstanding.

2.6.1.1 During scrutiny of the records in two CTOs¹⁶, in July 2007, it was noticed that while finalising the assessments of two dealers for the year 2000-01 to 2004-05 between February 2007 and June 2007 the assessing authorities appropriated the amount paid by the assesseees towards tax due instead of first appropriating it towards interest. This resulted in short demand of tax and interest of Rs. 49.86 lakh.

After the cases were pointed out to the department in July 2007 and reported to the Government between December 2007 and April 2008, the department

¹⁴ Malwa Vanaspati and Chemical Co. Ltd. V/s. Regional AC of Sales Tax, Indore in 21 STC 431 (Supreme Court)

¹⁵ Special circle, Kottayam, second circle, Perumbavoor and Ponkunnam

¹⁶ Special circle, Alappuzha and Special circle, Kottayam

stated in one case¹⁷ that the mistake would be rectified and in the other case¹⁸, the Government stated in July 2008 that the assessment was revised creating an additional demand of Rs. 13 lakh and interest of Rs. 2.77 lakh. However, the collection of arrears were stayed by Deputy Commissioner (Appeals) with a direction to pay 50 *per cent* of the balance. Accordingly the dealer had remitted Rs. 6.55 lakh. Further report has not been received (December 2008).

2.6.1.2 During scrutiny of the records in CTO, works contract and luxury tax, Malappuram in August 2007, it was noticed that in two cases while revising the assessments, the assessing authorities omitted to compute interest for the period upto the date of issue of demand notice and RRC. This resulted in short levy of tax and interest of Rs. 8.71 lakh.

After the cases were pointed out to the department in August 2007 and reported to the Government in April 2008, the Government stated in September 2008 that the amount due as interest as on date of payment has been appropriated from the payment made by the assesseees and the assesseees have been informed about the balance tax and interest due. A report on recovery has not been received (December 2008).

2.7 Short levy due to incorrect adjustment

By a notification issued under the KGST Act, the Government has exempted manufacturers of centrifuged latex and crumb rubber from payment of uncollected tax payable on the purchase turnover of rubber used in the manufacture of centrifuged latex and crumb rubber with a condition that tax, if any, already paid shall not be refunded.

During scrutiny of the records in two CTOs¹⁹, in October 2007, it was noticed that while finalising the assessments of three dealers in centrifuged latex for the years 2000-01 and 2002-03 between October 2006 and February 2007, the assessing authority erroneously adjusted tax paid on the purchase turnover of field latex, used in the conversion of centrifuged latex against the dues of CST assessments, resulting in incorrect adjustment of tax Rs. 52.33 lakh.

After the cases were pointed out to the department in September and October 2007 and reported to the Government in April 2008, the Government stated in October 2008 that in one²⁰ case action had been initiated to rectify the mistake. Report in the other case has not been received. (December 2008).

2.8 Short levy of tax due to incorrect computation of turnover

2.8.1 Under the KGST Act, taxable turnover means the turnover on which a dealer is liable to pay tax after making the prescribed deductions from the total turnover. As per section 59(4) of the KGST Act, goods which were liable to tax at the point of last purchase in the State and are held as closing stock on the date preceding the date of coming into force of the KVAT Act, shall be deemed to have acquired the quality of last purchase in the State on such date and tax is to be levied at the rate of four *per cent*.

¹⁷ CTO, Special circle, Kottayam

¹⁸ CTO, Special circle, Alappuzha

¹⁹ Third circle, Thrissur and Special circle Thrissur

²⁰ CTO, Special circle, Thrissur.

2.8.1.1 During scrutiny of the records in CTO, special circle, Kollam between July 2007 and September 2007, it was noticed that while finalising the assessments of four dealers for the year 2004-05 between January 2007 and March 2007, the assessing authority did not include the closing stock as on 31 March 2005 of raw cashew nut/latex valued at Rs. 2.86 crore in the gross turnover. This resulted in short levy of tax of Rs. 11.44 lakh.

After the cases were pointed out between July 2007 and September 2007, the assessing authority stated in September 2007 that notice has been issued to revise the assessments.

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

2.8.1.2 During scrutiny of the records in CTO, Nedumkandam, in March 2007, it was noticed that while finalising the assessments of seven dealers for the year 2004-05 between May 2005 and March 2006, the assessing authority did not include the closing stock as on 31 March 2005 of pepper valued at Rs. 1.66 crore in the gross turnover. This resulted in short levy of tax of Rs. 6.65 lakh.

After the cases were pointed out in March 2007, the assessing authority stated (March 2007) that notice has been issued to revise the assessments.

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

2.8.2 Under Rule 9 of the KGST Rules, taxable turnover means the turnover on which a dealer shall be liable to pay tax as determined after making the prescribed deductions from the total turnover. It has been judicially held²¹ that freight or delivery charges incurred by selling dealer in making the goods available to purchaser at place of sale is includible in sale price.

During scrutiny of the records in two CTOs²², between January 2005 and June 2007, it was noticed that while finalising the assessments for the years 2000-01 to 2004-05 of two assesseees engaged in the business of manufacture and supply of concrete poles to KSEB²³ at their destination, the assessing authority did not assess Rs. 1.33 crore being transportation charges received by the assesseees during these years. This resulted in short levy of tax of Rs. 7.30 lakh.

After the cases were pointed out to the department between January 2005 and June 2007 and reported to the Government in April 2008, the Government stated between August 2008 and September 2008 that assessments were revised and outstanding dues were advised for revenue recovery. In one case²⁴ the dealer obtained stay order from Deputy Commissioner (Appeals) on condition to pay 50 *per cent* of the balance tax. Accordingly an amount of Rs. 2.72 lakh has been remitted by the assessee. A report on further recovery has not been received (December 2008).

²¹ Black diamond beverages and another V/s CTO, Central Section, Assessment wing Calcutta and others, in the honourable Supreme Court of India in 107 STC 219

²² Special circle, Kothamangalam and Kottayam.

²³ Kerala State Electricity Board.

²⁴ CTO special circle, Kottayam.

2.8.3 Under Section 17 (5A) of the KGST Act, where on re-opening of an assessment completed under Section 17(4) in respect of any dealer, it is found that the amount of tax, if any, paid by such dealer is less than the amount of tax which he is liable to pay on such fresh assessment, the assessing authority shall direct such dealer to pay the difference between the amount of tax already paid by him and that tax arrived at on such fresh assessment, together with thrice the amount of such difference as penalty.

During scrutiny of the records in CTO, second circle, Palakkad in January 2007, it was noticed that while finalising the assessment of a dealer for the year 2002-03 in June 2003 under Section 17 (4) of the Act, the dealer did not include the sales turnover of firewood valued at Rs. 7.30 lakh effected to another dealer of the same office. This resulted in non-levy of tax of Rs. 1.01 lakh and penalty of Rs. 3.02 lakh

After the matter was pointed out to the department in January 2007 and reported to the Government in April 2008, the Government stated in October 2008, that the assessment was set aside for rectifying the mistake.

2.8.4 Under the KGST Act²⁵, arecanut purchased within the State is taxable at the rate of four *per cent* at the point of last purchase in the State.

During scrutiny of the records in CTO, Mananthavady, in August 2007, it was noticed that while finalising the assessment of a dealer for the year 2004-05 in November 2006, the assessing authority did not assess the purchase turnover of arecanut valued at Rs. 72 lakh effected from within the State and sold out side the State. This resulted in short levy of tax of Rs. 3.31 lakh including AST.

After the case was pointed out to the department in August 2007 and reported to the Government in April 2008, the Government stated in July 2008 that the assessment was revised and RRC issued for collection of dues. A report on recovery has not been received (December 2008).

2.8.5 Under the KGST Act, taxable turnover means the turnover on which a dealer shall be liable to pay tax after making prescribed deductions from the total turnover. Under Section 45A of the KGST Act, if any dealer has filed an untrue or incorrect return, penalty not exceeding twice the amount of tax evaded or sought to be evaded may be imposed on such assessee.

During scrutiny of the records in CTO, Vatakara, in December 2006, it was noticed that while finalising the assessment for the year 2004-05 in December 2005, an assessee effected inter state purchase of cement for Rs. 5.74 lakh during the year and claimed the corresponding sales as second sales by filing incorrect return. This resulted in non-levy of tax of Rs. 1.06 lakh and penalty of Rs. 2.12 lakh.

After the case was pointed out to the department in December 2006 and to the Government in April 2008, the Government stated in August 2008, that the assessment had been revised creating an additional demand of Rs 1.59 lakh as tax and penalty of Rs. 3.17 lakh. A report on recovery has not been received (December 2008).

²⁵ Under entry 7(a) of the schedule 1 to the Act, read with SRO 127/2000.

2.9 Short levy due to incorrect computation

2.9.1 Under the KGST Rules, after making final assessment, the assessing authority shall, examine whether any and if so, what amount is due from the dealer towards the final assessment after deducting any tax already paid. Instructions in this regard have been issued by the erstwhile Board of Revenue (Taxes) laying down departmental procedures for verifying and checking all calculations and credits given in an assessment order.

During scrutiny of the records in CTO, special circle, Kottayam, in August 2007, it was noticed that while finalising the assessment of a dealer engaged in manufacture and sale of news print for the year 2001-02 in April 2006, the assessing authority incorrectly credited remittance made by the assessee for Rs. 9 lakh, against CST dues for 2001-02, out of which an amount of Rs. 8.62 lakh actually pertained to entry tax for the years 1997-98 to 2000-01. This resulted in inadmissible credit of Rs. 8.62 lakh.

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

2.9.2 During scrutiny of the records in CTO, special circle, Thrissur, in August 2007, it was noticed that while revising the assessment of a dealer for the year 1999-2000 in August 2006, the interest worked out in the original order was incorrectly reckoned as Rs. 81.71 lakh instead of Rs. 89.71 lakh. This resulted in short levy of interest of Rs. 8 lakh.

After the case was pointed out in August 2007, the assessing authority rectified the assessment in October 2007. A report on recovery has not been received (December 2008).

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

2.9.3 During scrutiny of the records in CTO, special circle, Thiruvananthapuram, in September 2007, it was noticed that while finalising the assessment of a dealer for the year 2001-02 in December 2006, the assessing authority correctly assessed the turnover liable to be taxed, but incorrectly adjusted it against exemption available to the assessee. The assessing authority computed Rs. 1.01 lakh as excess payment made by the assessee though Rs. 4.60 lakh was actually due from him. This resulted in short demand of Rs. 5.61 lakh.

After the case was pointed out in September 2007, the department stated in December 2007 that action is being taken to revise the assessments. Further report has not been received (December 2008).

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

2.10 Non-levy of penalty

2.10.1 Under the KGST Act, any dealer who had submitted an untrue or incorrect return is liable to pay penalty not exceeding twice the amount of tax sought to be evaded. By a notification issued by Government in December 1999, poultry farmers in the State were exempted from payment of tax on the turnover of sale of poultry reared by them in their own farm within the State.

During scrutiny of the records in CTO, special circle III, Ernakulam, in July 2007, it was noticed that a dealer in broiler chicken claimed exemption on a turnover of Rs. 42.77 crore for the year 2000-01, which related to the turnover of poultry reared in some contract farms and not in their own farms. The assessing authority while finalising the assessment for the year 2000-01 in January 2007, though disallowed the claim for exemption and levied tax on the turnover, but did not impose penalty for filing incorrect return. Maximum penalty leviable in this case worked out to Rs. 6.84 crore.

After the matter was reported to the department in July 2007 and to the Government in April 2008, the Government stated in September 2008, that the assessee had conceded the turnover of chicks as exempted. The reply furnished is not correct as the High Court has decided the case in favour of revenue on 13 March 2001 and the assessee had filed the return on 31 March 2001 claiming exemption on the turnover. Further report has not been received (December 2008).

2.10.2 During scrutiny of the records in CTO, special circle, Kollam, in August 2007, it was noticed that while finalising the assessments of 12 dealers for the years 2002-03 to 2004-05 between July 2006 and March 2007, the assessing officer disallowed exemption claimed on consignment sale/concessional rate of tax on inter state sales, stating that the form F/C furnished were bogus as per the report of intelligence wing. Even though the higher rate of tax was demanded in such cases, the assessing authority did not levy penalty. The maximum penalty leviable in these cases worked out to Rs. 3.27 crore.

After the cases were pointed out in August 2007, the assessing authority stated that penalty under Section 9 (2A) of the Act was not leviable on offences committed under Section 10 (a) and (e) of the CST Act. Further, the Government has announced to waive the penalty and all amounts in excess of four *per cent* and interest thereon for all transactions up to 31 March 2006. The reply is not tenable as the Government announcement was with the condition that the dealers remit the dues before 30 June 2007. As the above assessee failed to meet this condition, they were not eligible for the concession announced by the Government.

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

2.10.3 During scrutiny of the records in CTO, special circle, Thrissur in July 2007, it was noticed that while finalising the assessments of a dealer in automobile and spares for the years 2002-03 and 2003-04 between October 2006 and February 2007, the assessing authority did not impose penalty of Rs. 29.36 lakh on the suppressed turnover of Rs. 74.50 lakh.

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

2.10.4 During scrutiny of the records in CTO, Kundara in November 2007, it was noticed that the assessments of two dealers for the year 2004-05 were completed under Section 7 (1)(b) of the Act in February 2007 and March 2007. The assessments were subsequently revised under Section 19(1) of the Act creating additional demand of Rs. 1.04 lakh in each case. The re-assessment was due to non-disclosure of the actual size of the crushing machines by the assesseees. Maximum penalty that could be levied under Section 45A of the Act comes to Rs. 4.14 lakh.

After the cases were pointed out in November 2007, the department issued orders in November 2007 and December 2007 imposing penalty of Rs. 1.04 lakh in one case and Rs. 2.07 lakh in the other. A report on recovery has not been received (December 2008).

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