CHAPTER III : REVIEW ON PROVISIONAL ASSESSMENT

A review of provisional assessment system in 114 divisions of 73 commissionerates of Central Excise was conducted by audit, to evaluate whether the cases were finalised within the fixed time-frame and whether the existing internal control mechanism had been efficient in protecting the interest of revenue. Ten constructive and implementable recommendations have been given to remedy the systemic weaknesses identified by audit. Of these, nine recommendations have been accepted by the Ministry. Some of the major findings are abstracted below: -

3.1 Highlights

- **In 2087 pending provisional assessment cases, the differential duty was not quantified. The adequacy and sufficiency of the amount of bond/security required to be obtained in these cases could not, therefore, be evaluated in audit.**

(Paragraphs 3.5, 3.9 and 3.10.6.1)

- **Inspite of incorporation of normal time limit of six months in the Rules with effect from 1 July 2001, 2260 provisional assessment cases were pending for more than six months to more than 25 years.**

(Paragraph 3.6)

- **In three test checked cases, the blockage of revenue was to the extent of Rs.133.23 crore for want of administrative action for finalisation of pending cases.**

(Paragraph 3.8)

- **In 171 cases of provisional assessment in 36 commissionerates, the deficiency in bond value amounted to Rs.819.80 crore and deficiency in amount of bank guarantee amounted to Rs.212.29 crore, besides financial accommodation to the extent of Rs.16.05 crore by way of amount of bank commission saved by the assessees.**

(Paragraph 3.9)

3.2 Introduction

Rule 7 of the revised Central Excise Rules, 2002, provides that where the assessee is unable to determine the value of excisable goods or determine the rate of duty applicable thereto, he may request the competent authority for payment of duty on provisional basis. The competent authority may order allowing payment of duty on provisional basis, at such rate or on such value, as may be specified by him. The provisional assessment is allowed subject to execution of a bond by the assessee with such surety or security, as the competent authority deem fit, so as to bind the assessee for payment of difference between the amount of duty as may be finally assessed and the amount of duty provisionally assessed. As per the procedure devised by the Board, the assessee has to file a general bond 'B2' for an amount three times of the estimated amount of the differential duty, to be backed by security or bank guarantee of 25 per cent of the bond amount. For execution of bank guarantee, the assessee has to pay

'commission' to the bank which may vary depending upon the amount of bank guarantee, period of bank guarantee and the bank.

Pace of finalisation of provisional assessments was commented upon, by audit in the review on 'provisional assessment' in Audit Report 1994-95. The issue was examined by Public Accounts Committee, which recommended for a statutory time limit, for finalisation of provisional assessment cases. The Rules were amended on 1 July 2001, and under Rule 7 of revised Central Excise Rules, 2002, Assistant Commissioner or Deputy Commissioner, as the case may be, was required to finalise the case within a period not exceeding six months from the date of communication of the order for payment of duty on provisional basis. This time limit was, however, qualified by a clause that "on sufficient cause being shown and the reasons to be recorded in writing, the period could be extended for another six months by the commissioner of central excise and by the chief commissioner of central excise for such further period as he may deem fit". The adherence to the time limit of six months was, thus, left at the discretion of departmental officials.

3.3 Audit objectives

Review of provisional assessment cases was undertaken to assess: -

- the impact of the fixation of time limit on pace of clearance of provisional assessment cases;
- efficiency of internal controls and monitoring mechanism in protecting the interest of revenue; and
- the adequacy and effectiveness of rules, regulations and procedures governing disposal of provisional assessment cases.

3.4 Audit scope

Records of 114 divisions in 73 out of 93 commissionerates were test checked. The period covered under audit was from the year 2002-03 to 2004-05. The findings and recommendations are contained in succeeding paragraphs.

FINDINGS AND RECOMMENDATIONS

3.5 Macro issues

The overall position of provisional assessment cases, in respect of 93 commissionerates, is given in the table 1 below: -

Table No.1

	As on 31 March 2002	**As on 31 March 2003**	**As on 31 March 2004**	**As on 31 March 2005**
Number of provisional assessment cases pending finalisation	2374	2404	2344	2302
Estimated differential duty involved (in crore of rupees)	386.12	319.59	258.47	310.20

Figures furnished by commissionerates.

- As per information furnished by 73 commissionerates test checked in audit, differential duty was not even quantified in 2087 provisional cases as on 30 September 2005. The figures for the differential duty estimated by the department, therefore, relates to only 215 cases. Thus, the department is not even aware of the estimated differential duty involved in pending provisional assessment cases.
- The figures furnished by commissionerates do not appear to be reliable as under-reporting of the pendency both in terms of numbers and amount was noticed in audit, which has been commented upon in succeeding paragraphs.
- Differential amount of duty was not estimated/quantified, in any of the pending cases in D-Division of Hyderabad I (86 numbers), Chandigarh (3 numbers) and Jalandhar (5 numbers) commissionerates.
- Kolkata IV commissionerate depicted the highest pendency of provisional assessment cases in terms of amount (Rs.72.47 crore).

3.6 Time limit prescribed for finalisation of provisional assessment not adhered to – need for a realistic time limit

The extent to which normal time limit of six months was adhered to, for finalisation of provisional assessment cases was evaluated in audit by analysis of age-wise pendency.

Break-up of provisional assessments pending finalisation as on 30 September 2005 (after taking into account clearance between April 2005 and 30 September 2005) as furnished by 93 commissionerates is given in the table 2 below: -

Table No.2

(Amount in crore of rupees)

Age-wise pendency	**Number**	**Amount**
Cases upto six months	250	88.70
Cases more than six months but upto one year	90	11.21
Cases more than one year but upto five years	152	46.62
Cases more than five years old	1768	158.10
Total	**2260**	**304.63**

Figures furnished by commissionerates.

- Despite the time limit of six months, 2010 out of 2260 (89 per cent) provisional assessment cases were pending for period ranging between more than six months to more than 25 years.
- Cases pending finalisation beyond one year constituted 85 per cent of total cases.
- Provisional assessment cases pending for more than five years were 1768 in number.
- A provisional assessment in respect of M/s. Eicher Limited, in Chennai I commissionerate was pending finalisation for more than 22 years (from 30 December 1983 onwards). The case was shown as pending in the monthly technical report of the division with the remarks that 'certain records for the period from 1984 to 30 June 2000 were not available with the division and on instructions from commissioner search was being undertaken to locate the records'.

3.7 Slow pace of disposal

Number of cases pending finalisation beyond six months being high, an attempt was made by audit to assess the pace of disposal of cases after the fixation of time limit in the Rules. The position during the years 2002-03, 2003-04 and 2004-05 emerging from 103 divisions of 58 commissionerates test checked in audit, is given in the table 3 below: -

Table No.3

(Amount in crore of rupees)

Total number of cases including additions during the period from 2002-03 to 2004-05		**Overall clearance**						**Balance as on 30.09.2005**	
		Within six months		**Within one year**		**After one year**			
No.	**Amt.**	**No.**	**Amt.**	**No.**	**Amt.**	**No.**	**Amt.**	**No.**	**Amt.**
2985	488.97	261	127.80	194	43.07	310	146.43	2220	171.67

Figures furnished by commissionerates relating to 58 commissionerates.

Audit observed that: -

- The fixation of normal time limit of six months for finalisation of cases in the Rules has had little impact on the pace of disposal of pending cases, as only nine per cent of the cases in terms of number were cleared within six months, the clearance in terms of amount being 26 per cent.
- The clearance within one year was only seven per cent in terms of number and nine per cent in terms of amount.
- Cases cleared after one year were 10 per cent in terms of number and 30 per cent in terms of amount.
- The overall clearances were only 26 per cent of the total number of cases.
- The dichotomy in the percentages of clearances in terms of number and in terms of amount was due to the fact that the clearances were mainly in respect of those cases where the differential amount of duty had already been estimated at the time of issue of orders for provisional assessment.
- There was marked reluctance of the departmental officers to finalise those cases where amount of differential duty had not been quantified. This is borne out by the fact that out of 2220 cases pending as on 30 September 2005, there were 2087 cases where the differential amount of duty was not at all determined.
- Out of 2087 such cases, 1930 cases were pending finalisation for more than five years.

Recommendation No.1

Government may consider deleting the discretion of extending provisional assessment cases beyond six months; if felt necessary the time limit of six months could be extended to an appropriate period but with no exception. This would enable Government to finalise provisional assessment cases in a time bound manner and realise the differential duty in time, as at present interest is also not leviable on differential duty till the provisional assessment case is finalised.

While responding to the recommendation (September 2006), the Ministry expressed (January 2007), its inability to fix a rigid time limit for finalisation of provisional assessments in all cases as there could be legal issues/appeals pending with various authorities.

MICRO ISSUES

3.8 Cases involving substantial revenue were pending for want of administrative action

Some of the provisional assessment cases involving high amount and pending finalisation for more than two years were reviewed to ascertain the reasons for delay, despite the fixation of time limit of six months, in the rules. It was noticed that a large number of cases involving substantial revenue were pending mainly because of lack of initiative to finalise these cases. It was also noticed that quite a large number of cases related to multinational companies. Most of these cases could have been finalised, had the delays been addressed promptly by the department.

A few illustrative cases are mentioned in the following paragraphs: -

(i) A test check of the records of Chandannagar division II, in Kolkata IV commissionerate, revealed that M/s. ITC Limited (Triveni Tissue division) had been clearing goods on provisional assessment since 1980. The action, if any, taken by the department by way of demanding differential amount of duty for the period from 1980 till February 1994 could not be ascertained by audit from the records made available. However, differential duty of Rs.40.20 crore was demanded from the assessee between March 1994 to August 2002. One case involving duty of Rs.18.56 crore was finalised on 31 July 2002. But on an appeal by the assessee, the CEGAT remanded the case back for fresh adjudication on 19 February 2003, which was still pending finalisation alongwith other cases (November 2005). Interestingly, as against the differential amount of duty of Rs.40.20 crore, the department had obtained bonds for Rs.3.10 crore and bank guarantee for Rs.78 lakh only, resulting in shortfall in the amount of bond to the extent of Rs.117.50 crore and of bank guarantee to the extent of Rs.29.37 crore. From the letter dated 9 May 2005 issued by the division to different ranges, it was also noticed that even the documents relating to the execution of bonds for Rs.3.10 crore alongwith bank guarantee for Rs.78 lakh were not available with the division.

The non-finalisation of these cases, even after a lapse of more than 25 years, has blocked a probable revenue of Rs.40.20 crore besides extending undue financial accommodation to the assessee by way of non-execution of bank guarantee for Rs.29.37 crore and minimum bank commission of Rs.8.08 crore which was required to be paid to the bank, for obtaining bank guarantee.

(ii) M/s. Sterlite industries (India) Limited, in Tirunelveli commissionerate, was allowed to clear the goods on provisional assessment, during the period from November 2002 to May 2003 on account of dispute over value for the clearances to their sister unit, on execution of a bond for Rs.19.15 crore and bank guarantee for merely Rs.10 lakh. Based on the amount of bond, bank guarantee of Rs.4.79 crore (25 per cent of bond amount) ought to have been obtained. Taking into consideration the estimated differential duty of Rs.90.92 crore approximately, even the bond for Rs.19.15 crore was inadequate. The assessee was required to execute a bond for Rs.272.76 crore and bank guarantee for Rs.68.19 crore. Bank guarantee

of Rs.10 lakh was valid till 10 October 2005 and from the records of the division it could not be ascertained whether bank guarantee had been renewed. The assistant commissioner vide his letter dated 22 May 2003 suggested to the commissioner that in the interest of revenue, cost audit under Section 14A of the Central Excise Act may be conducted for this purpose. There was, however, no response from the commissioner. The case was not finalised till the date of audit (November 2005), nor was the cost audit conducted as suggested by the assistant commissioner.

The lack of action to finalise the provisional assessment case has resulted in blockage of revenue to the extent of Rs.90.92 crore besides financial accommodation by way of non-execution of bank guarantee for Rs.68.09 crore and bank commission of Rs.5.11 crore.

(iii) M/s. TRF, in Jamshedpur commissionerate, was allowed to clear goods on provisional assessment on 16 June 1997, on account of despatch of machines in knock down condition, valuation and classification. The assessment was finalised by commissioner on 13 May 1999. On appeal by assessee, the CEGAT vide their orders dated 21 December 2001 remanded the case back to the commissioner for de-novo finalisation. At the time of issue of orders for provisional assessment, bond was executed for only Rs.50 lakh alongwith bank guarantee of Rs.12.50 lakh on 3 September 1997. The amount of bond and bank guarantee was not reviewed from time to time. On the estimated differential duty of Rs.2.11 crore, the amount of bond required to be executed was Rs.6.33 crore alongwith bank guarantee for Rs.1.58 crore. The case was not finalised till the date of audit (November 2005).

Non-finalisation of the case has resulted in blockage of estimated revenue of Rs.2.11 crore, besides financial accommodation to the assessee by way of non-execution of bank guarantee for Rs.1.45 crore and Rs.8.20 lakh as bank commission.

(iv) M/s. BHEL, Ramachandrapuram, in Hyderabad I commissionerate, was allowed to clear goods on provisional assessment on account of several factors such as price variation, escalation charges, change in design, foreign exchange fluctuation etc., for the period from 1985-86 to 2001-02. The assessee executed a consolidated bond for Rs.1 crore with a security/bank guarantee for Rs.25 lakh.

There were 84 provisional assessment cases involving contract value of Rs.1512.28 crore which had not been finalised till the date of audit (November 2005). Final accounts in these cases have already been furnished by the assessee to the department, during the period between May 2001 and August 2004. Verification at range level was, however, completed in only 18 cases involving contract value of Rs.138.26 crore. Even in these 18 cases, the final action to communicate the differential duty amounting to Rs.3.67 crore was awaited, although the assessment memoranda were already completed by division in March 2004. Acton to finalise the remaining 66 cases involving supplies valuing Rs.1374.02 crore was yet to be taken.

Inaction by the department, despite submission of accounts by the assessee, resulted in blockage of revenue of approximately Rs.25.67 crore, including revenue of Rs.3.67 crore already determined but yet to be communicated to the assessee.

Recommendation No.2

Board should issue instructions to its field formations for finalisation of provisional assessment cases involving substantial revenue, on a priority basis.

While accepting (January 2007) this recommendation, the Ministry informed us that instructions were being issued.

3.9 Bonds/bank security not adequate to cover differential duty involved

Rule 7 of the Central Excise Rules, 2002, provides for execution of a bond with security by the assessee, binding the assessee for payment of difference between the amount of duty as may be finally assessed and amount of duty provisionally assessed. Board vide their instructions dated 14 January 1997 stipulated that bond for proper amount (three times of the estimated differential duty) backed with proper security/bank guarantee (25 per cent of bond amount) should be executed by the assessee for safeguarding the revenue. Further, Board vide their letter dated 19 March 1998 instructed field offices to ensure that all the clearances under provisional assessments are covered by sufficient bond, backed by proper security and that securities are valid for the entire period for which extension was granted.

Test check in audit revealed that in 171 cases including provisional assessment cases already finalised, the deficiency in the bond value and bank guarantee was found to be Rs.819.80 crore and Rs.212.29 crore, respectively, as per the details given in table 4 below: -

Table No.4

(Amount in crore of rupees)

No. of commis-sionerate	Number of cases	Amount of differential duty to be covered	Amount for which bond executed	Shortfall in amount of bond	Shortfall in amount of bank security	Amount of bank commission saved by the assessees
36	171	349.43	234.66	819.80	212.29	16.05

Inadequate amount of bond and bank guarantee in these cases not only endangered the recovery of revenue in the event of units becoming defunct but also provided financial accommodation by way of bank guarantee not executed for Rs.212.29 crore and an amount of Rs.16.05 crore saved as bank commission by the assessees.

The amount of the general bond alongwith amount of security is determined on the basis of the difference between the duty being paid on provisional assessment and the probable duty payable. For want of estimation of differential duty in 2087 pending cases, as pointed in the foregoing paras, the adequacy and sufficiency of the amount of bond/security obtained in these cases could not be checked in audit. The interest of revenue was not fully protected in these cases, as the amount of bond/bank guarantee once fixed at the time of provisional assessment was also not reviewed from time to time, even though these cases were pending finalisation for periods ranging between 2 to 17 years.

A few illustrative cases are given below: -

(i) Orders for provisional assessment were issued in July 1999 for M/s. Danghee Vision Industrial Company Limited, in Chennai IV commissionerate. Bond for the amount of Rs.50 lakh and bank guarantee of Rs.12.50 lakh was obtained from the assessee. The provisional assessment was finalized in October 2003 and differential amount of duty was determined to be Rs.60 lakh. The unit closed down in November 1999. The bank guarantee for Rs.12.50 lakh was encashed. The balance amount of duty of Rs.47.50 lakh, however, could not be recovered due to fixation of inadequate amount of bond and insufficient amount of bank guarantee.

(ii) Provisional assessment case of M/s. Modi Vanaspati Manufacturing Company, in Ghaziabad commissionerate, was remanded to commissioner (appeals) for de novo adjudication by Delhi High Court in July 2001. The case was still pending finalisation till the date of audit (November 2005). The estimated differential duty worked out by the department was Rs.47.29 lakh, against which bank guarantee of Rs.10 lakh only was obtained by the department. The units had closed down in 1994 and the bank guarantee for Rs.10 lakh had expired on 8 October 2004.

Since the unit had closed and insufficient bank guarantee of Rs.10 lakh had expired, the possibility of recovery after the finalisation of the case was remote.

Similarly, the possibility of recovery of Rs.12.57 lakh from M/s. Travancore Electrochemical Limited, in Cochin commissionerate, in the pending provisional assessment case was remote, since the unit had closed in July 1999 and bank guarantee of insufficient amount of Rs.4.20 lakh had expired on 18 September 1999.

(iii) M/s. Hyundai Motors India Limited was instructed by the department on 2 June 1999 to execute a bond for Rs.20 crore with bank guarantee for Rs.2 crore (10 per cent of the bond amount in a provisional assessment case on account of valuation) instead of requirement of bank guarantee for Rs.5 crore (25 per cent of the bond amount). Again, the department instructed the assessee on 1 July 2003 to enhance the Bond amount to Rs.50 crore with bank guarantee for Rs.5 crore (10 per cent) instead of bank guarantee for Rs.12.50 crore.

On this being pointed out in audit (November 2005), the department replied that from the year 2005-06, the assessee has been instructed to furnish 25 per cent of the bond value as bank guarantee. It could not, however, be ascertained from the available records whether assessee had furnished bank security for Rs.12.50 crore for earlier period.

The obtaining of lesser amount of bank guarantee, in contravention of the instruction of the Board not only resulted in government revenue being left un-protected to the extent of Rs.7.50 crore but also gave financial accommodation to the assessee.

Recommendation No.3

The department should strengthen its internal control mechanism to ensure that (i) differential duty is estimated in each provisional assessment case as required; and (ii) bonds/bank guarantees of appropriate amount are obtained and the bonds/bank guarantees are reviewed from time to time in keeping with the increase in estimated differential amount of duty.

Responding to the recommendation, the Ministry accepted (January 2007) the recommendation.

3.10 Internal controls

3.10.1 Time limit for issue of orders for provisional assessment not fixed

Rule 7 of the Central Excise Rules, 2002, provides that assistant commissioner or deputy commissioner, may order allowing payment of duty on provisional basis. Central Board of Excise and Customs Excise Manual of Supplementary Instructions stipulate that competent authority must issue specific order in each case of provisional assessment, accepting or

rejecting the request of the assessee for provisional assessment. While it has been provided in the Rules that the provisional assessment case may be finalised within six months, no such time limit has been fixed for issue of order allowing or rejecting the request of the assessee.

A test check of the records revealed that in some cases either the orders for provisional assessment were not at all issued or there was considerable delay ranging from 3 to 53 months in issue of orders. Though the number of such cases may be very large, audit could identify a few cases only from the records made available, as per the details given in the table 5 below: -

Table No.5

No. of commissionerate	Number of cases where orders were not issued	Number of cases where orders were delayed
14	49	32

The Board vide instructions dated 24 November 1989 had emphasised the need for observance of all the conditions governing provisional assessment. The issue of specific order being one of the basic legal requirements prescribed in the Rules, non-observance of this provision could result in loss of government revenue by way of non-recovery of differential amount of duty.

An illustrative case is mentioned below: -

M/s. Mahavir Spinning Mills, Hoshiarpur in Jalandhar commissionerate, had been clearing goods on provisional assessment since the year 1994. His requests for provisional assessment for the years 2001-02 and 2002-03 were, however, neither properly accepted nor denied by the division in the sense that while not permitting the provisional assessments, the range office was at the same time directed to get the figures of sales on quarterly basis from the assessee and finalise assessment. Superintendent range office vide his orders dated 10 June 2003 and 19 June 2003 finalised the assessment, demanding a duty of Rs.38.13 lakh and Rs.37.05 lakh respectively. On an appeal by assessee, commissioner (appeals), quashed the order being 'void ab-initio' owing to ambiguous orders of the assistant commissioner in rejecting the requests of the assessee. The department has not appealed against the decision of commissioner (appeals). The non-issue of specific and clear orders by the division, thus, resulted in loss of revenue of Rs.75.18 lakh.

Recommendation No.4

The Government may consider prescribing a time limit of orders for provisional assessment by the competent authority so that the provisional assessment is effective soon after the request of the assessee and the probability of revenue loss on this account is avoided. Alternatively, deeming provisions making the provisional assessment effective from the date of request of assessee could be introduced.

The Ministry accepted (January 2007) the recommendation and informed that executive instructions prescribing an appropriate time limit will be issued.

3.10.2 Interest on finalisation of provisional assessment not levied

Rule 7(4) of the Central Excise Rules, 2002, provides that the assessee shall be liable to pay interest on any amount payable to central government, consequent to order of final assessment under Rule 7(3), at the rate specified by the central government by notification

under Section 11AA or Section 11AB of the Act, from the first day of the month succeeding the month for which such amount is determined, till the date of payment.

It was noticed in audit that in 11 cases, interest to the extent of Rs.47.41 lakh was not levied.

On this being pointed out in audit (25 January 2005), the department intimated the recovery of Rs.8.28 lakh from three units.

3.10.3 Provisional assessment cases transferred to call book

The Central Board of Excise and Customs' instruction dated 6 September 1990 specifies the circumstances under which a pending case can be transferred to 'call book'. The provisional assessment case cannot be transferred to call book unless the case is sub-judice and the specific approval of the commissioner is obtained.

Test check of the records of selected divisions revealed that inspite of being pointed out in Audit Report No.11 of 2004 (chapter III) in the review on 'Call Book', eight provisional assessment cases continued to be retained in call book, contrary to the instructions of the Board, as per details given in the table 6 below: -

Table No.6

(Amount in lakh of rupees)

Commiss-ionerate	Assessee	Date of provisional assessment	Date of transfer to call book	Differential amount of duty estimated
Pune I	M/s. Bajaj Auto Akurdi	1988-89	July 1996	Not estimated
	M/s. Bajaj Auto Chakan	January 2001 to June 2001	January 2003	-do-
Ranchi	M/s. Waxpol India Limited Tatisiliwai, Ranchi	July 1970	13.01.1997	8.94
	M/s. HEC Limited, Ranchi	November 1981	13.01.1997	4110.00
Goa	M/s. Vicco Laboratories, Corlim, Goa	11.09.1997	01.11.1999	3778.00
Bolpur	M/s. IISCO, Burnpur	25.09.1990	Could not be ascertained	217.00
Kolkata III	M/s. Sika (I) Limited	28.08.1990	-do-	154.99
	M/s. Ramsarup Industrial Corporation	15.12.1992	-do-	217.00

Audit further noticed that: -

- The amount of differential duty has not been quantified till the date of audit (November 2005) in two cases in respect of M/s. Bajaj Auto in Pune Commisisonerate, which were transferred to call book in July 1996.
- In case of M/s. Waxpol India Limited, Ranchi commissionerate, the provisional assessment was ordered as early as in July 1970 and case was transferred to call book on 13 January 1997.
- A provisional assessment case in respect of M/s. Vicco Laboratories, Goa was transferred to call book on 1 November 1999. Even though the Supreme Court had, on 7 December 2004 decided a similar issue in the case of Nagpur unit of the same assessee, the case continued to be kept in call book till date (November 2005).

Recommendation No.5

Department should issue instructions to the field formations to review the call book expeditiously with a view to take these provisional assessment cases out of call book for finalisation.

The Ministry accepted (January 2007) and implemented the recommendation.

3.10.4 Differential amount of duty not quantified although provisional assessments were shown as finalised

Central Board of Excise and Customs, vide circular dated 19 March 1998 stipulated that on finalisation of assessments, necessary adjustments should be made within a period of 15 days and in case of any delay on the part of the assessee, the bond/securities must be enforced/encashed to safeguard the revenue.

It was noticed that some cases were shown as finalised between March 2003 to July 2005 in the records of the division, but the amount of differential duty to be paid by the assessee was not worked out till date (November 2005), as per details given in the table 7 below: -

Table No.7

Commissionerate	Assessee	Date of finalisation of case
Pune I	M/s. Cadbury India Limited	19.12.2003
	M/s. Venkey's India Limited	21.05.2004
Mumbai IV	M/s. Koch Rajes CD (India) Pvt. Ltd.	28.03.2003
Kolkata III	M/s. Saregama India Limited	27.07.2005

Audit observed that: -

- These cases could not be treated as finalised, unless the differential amount of duty was quantified.
- Since the differential amount of duty was not worked out in these cases, the question of encashment of bank guarantee in these cases also did not arise.
- This not only resulted in blockage of revenue and interest but also provided financial accommodation to the assessee.

Recommendation No.6

Department should issue instruction to its field formations to ensure that only those provisional assessment cases are shown as finalised where the differential duty has been finally determined.

The Ministry accepted (January 2007) the recommendation.

3.10.5 Extension for finalising the cases beyond six months not obtained from commissioner/chief commissioner

Rule 7 of the Central Excise Rules, 2002, provided for grant of extension of the period for finalisation of case beyond six months by commissioner and beyond one year by the chief commissioner. This extension was to be given on sufficient cause being shown and the

reasons to be recorded in writing, so that there was no un-necessary delay in finalisation of cases.

A test check of the records made available to audit revealed that during the period from 2002-03 to 2004-05, the requirement of extension by the commissioner in writing, was not fulfilled in 99 cases in seven commissionerates.

In 1645 cases in 18 commissionerates, the extension required to be granted by chief commissioner was also not obtained.

In Chennai III commissionerate, the extension of time was not even applied for in 23 cases which were pending for the period ranging from 1 year to 8 years.

In Chennai I commissionerate, a case relating to M/s. Eicher Limited was pending since 1983 without extension of the chief commissioner having been obtained.

No mechanism was devised by the Board, whereby the requirement of grant of extension by commissioner/chief commissioner on the merit of each case could be monitored by the commissioner/chief commissioner/Board.

Recommendation No.7

Department should consider devising a suitable internal control mechanism to ensure that the required extension at commissioner/chief commissioner level is obtained and that the extension by commissioner/chief commissioner is granted on the merit of each case.

The Ministry accepted (January 2007) the recommendation.

3.10.6 Provisional assessment monitoring system (PAMS) not fully functional

As a result of examination of Audit para 1.03 of the CAG's Report for the year ended 31 March 1995 (No.4 of 1996), the Public Accounts Committee, in its 14th Report of the 11th Lok Sabha, had recommended for development of appropriate computer programme so that uniformity could be maintained in all the commissionerates and consistency of data ensured. To implement this recommendation, a software namely Provisional Assessment Monitoring System (PAMS) for monitoring of provisional assessment cases was launched on 8 November 2002. The Board vide their circular dated 19 May 2003 instructed all the commissionerates to enter all new cases as well as pending cases into the system by 31 July 2003. The implementation of the instruction of the Board was reviewed in selected divisions.

Audit noticed the following deficiencies and inconsistencies.

3.10.6.1 Differential amount not worked out as per standard method

User guide for implementation of PAMS stipulated that 'for successful implementation it was necessary there should be a clear statement explaining how the differential duty was estimated for the purpose of obtaining B2 bond and security and that when the estimated duty difference for the goods cleared under provisional assessment went beyond security amount, action should be taken to bring in additional security'. It was noticed that even after entering new as well as old cases into system, differential duty was not at all worked out in as many as 2087 cases in accordance with standard method, in the absence of which, audit could not verify as to how did the department ensure that the security already obtained was revised from time to time to safeguard revenue.

3.10.6.2 Method adopted for the counting of the number of provisional assessment cases was incorrect

Provisional assessment monitoring system envisaged counting of number of pending provisional assessment assessee-wise and issue-wise.

It was noticed that the number of cases shown as pending in respect of M/s. BHEL, M/s. BHPV and M/s. BHEL. at Hyderabad I, Visakhapatnam I and Trichy commissionerates, were shown as one each, whereas the actual number of cases, contract-wise, were 84, 1816 and 35 respectively. Since the provisional cases were to be finalised contract-wise, the depiction of one case in PAMS as well as reporting of one case in the MTR was incorrect, which led to under-reporting of actual pendencies.

While acknowledging that the 'correct approach would be to have separate provisional assessments for clearances to different parties', the ADG (Systems), Chennai in his e-mail message dated 8 August 2003 to all the commissionerates, advised them to use an option of linked provisional assessment, thereby treating 100 contract as one case on PAMS site. The ADG (System), Chennai opted for use of linked provisional assessment system mainly because 'the correct approach may increase the number of cases pending in a commissionerate to a very high level'. Under this option, one basic number say 28 was to be allotted and each new provisional assessment was to be allotted linked number like 28.01, 28.02. Under this system, clearances to 100 parties were to be located as one case in PAMS.

PAMS, however, do not envisage use of linked provisional assessment other than when a change may occur in some important parameter like Central Excise Tariff Head (CETH) or the rate of duty.

Recommendation No.8

Board may consider to review the present method of numbering provisional assessment cases to correctly reflect the number of such cases, for its effective monitoring.

The Ministry accepted (January 2007) the recommendation.

3.10.6.3 Other deficiencies

While in 33 divisions no case was entered into system, in 61 other divisions, the entries into the system were partial. The annexures relating to provisional assessment cases to be attached to monthly technical report (MTR) were not being generated through PAMS in 82 divisions.

It was noticed that report for showing age-wise pendency was not yet developed on PAMS and the age-wise pendency was being worked out manually.

It was noticed that the software did not provide for capturing details of recovery of differential duty after realisation and refunds. When non-compliance of requirements by commissionerates and deficiencies in the functioning of system were brought to the notice of Directorate of System at Chennai on 25 November 2005, it was stated by ADG on 29 November 2005 that their office was in no way directly involved in data entry at the field level or monitoring of data or monitoring of any provisional assessments. He, however, acknowledged that PAMS software had not undergone any major changes based on the feedback from the field formations.

The introduction of PAMS has not brought about any tangible improvement either in monitoring the disposal of cases or correct estimation of differential amount of duty to protect revenue, by way of obtaining appropriate security.

Recommendation No.9

Board should continually develop PAMS software based on the feedback received from field formations so that the potential of PAMS is utilised for the intended objectives.

Responding to the recommendation, the Ministry accepted (January 2007) the recommendation.

3.10.7 Provisional assessment register not maintained properly

The board vide circular dated 14 January 1997 instructed the field offices to maintain provisional assessment register in prescribed format. In the absence of the orders of the Board to the contrary, commissionerates were required to maintain manual records, besides the maintenance of Provisional Assessment Monitoring System (PAMS).

A test check of records of 63 commissionerates revealed that in 11 divisions of Kolkata I, Kolkata III, Kolkata VI, Bolpur, Mumbai III, Vapi, Bhubaneshwar I and Ghaziabad commissionerates, the registers were not at all maintained.

The registers being maintained in 50 test checked divisions were incomplete and lacked information relevant for final assessment like differential duty involved, whether bonds/bank guarantees were furnished, validity period of bond/bank guarantee, etc.

Recommendation No.10

Board may consider issuing orders to discontinue maintenance of manual registers, once PAMS is fully functional to avoid duplication of work.

Responding to the recommendation, the Ministry accepted (January 2007) the recommendation.

3.10.8 Under-reporting in monthly technical report

In the course of test check of the records of selected divisions, it was noticed that there was under-reporting in terms of number as well as amount in the monthly technical reports sent to commissionerates/Board as per details given in table 8 below: -

Table No.8

(Amount in crore of rupees)

No. of commissionerate	No. of divisions	Pendency as per division records		Pendency as shown in MTR		Difference	
		No.	Amt.	No.	Amt.	No.	Amt.
18	18	250	104.60	128	35.63	122	68.97

Audit further noticed that: -

- In Balasore division of Bhubaneshwar I commissionerate, 12 cases involving differential duty of Rs.15.37 crore were pending in respect of M/s. Birla Tyres. But in the monthly technical report submitted to the commissionerate only one case involving differential duty of Rs.30 lakh was shown as pending.

- There was under-reporting to the extent of Rs.51.18 crore in terms of the differential duty amount in Kolkata IV, Kolkata VI and Bolpur commissionerates.
- The data furnished by the commissionerate to the Board regarding provisional assessment cases was, accordingly, not reliable.

CHAPTER IV : REVIEW ON EXCISE DUTY ON PLASTIC AND ARTICLES THEREOF

A review of 235 units manufacturing plastic and articles thereof was conducted in audit to evaluate whether the duty was paid in accordance with the Valuation Rules, cenvat credit taken in accordance with the Cenvat Rules and service tax on services provided/received by these manufacturers paid in accordance with existing provisions. Audit review has noticed a few cases of undervaluation, irregular availment of cenvat credit and non-payment of service tax. Two constructive and implementable recommendations have been given to remedy the weaknesses noticed by audit. The total additional revenue which could have come to the government, as a result of this audit intervention (review) is Rs.18.24 crore. Some of the major findings are abstracted below: -

4.1 Highlights

- **The percentage of Cenvat to duty paid in cash was exceptionally high in plastic industry.**

(Paragraph 4.5)

- **Undervaluation of goods consumed captively resulted in revenue loss of Rs.64.88 lakh.**

(Paragraph 4.7.3)

- **Irregular availment of Cenvat credit resulted in revenue loss of Rs.9.07 crore.**

(Paragraph 4.8)

- **Non-payment of service tax on the services rendered by foreign consultants resulted in revenue loss of Rs.2.98 crore. Non-payment of service tax on various services rendered by manufacturers of plastic and articles thereof, resulted in revenue loss of Rs.1.24 crore.**

(Paragraphs 4.9.1 to 4.9.6)

- **Non adjudication of demands resulted in blockage of potential revenue of Rs.52.99 crore.**

(Paragraph 4.10.3)

4.2 Introduction

'Plastics and articles thereof', is one of the twenty commodities yielding major revenue to the Government, the percentage share in total collection (central excise receipts) being 2.55 per cent during the year 2004-05. Plastic of all sorts became a subject of duty of excise with effect from 1 March 1961 and was classifiable as item 15A to the First Schedule of Central Excise and Salt Act, 1944. With the adoption of the harmonised system of coding and classification with effect from 28 February 1986, the goods stand included in Chapter 39 of the schedule to the Central Excise Tariff Act, 1985 (Act No.5 of 1986). From the budget for 2000-01, duty at the rate of 16 per cent was levied on plastic articles uniformly. There has

been no change in the rate of duty till 2004-05. The excise duty on lay flat tubing (heading 39.17) was reduced to eight per cent ad valorem from 1 March 2003.

4.3 Audit objectives

Records of selected manufacturing units and departmental offices were scrutinised in audit to examine: -

- at macro level, adequacy of provisions of the Act, Rules, and instructions issued by the Ministry of Finance/Central Board of Excise and Customs (Board), in maximizing revenue collection and
- at micro level, to seek assurance that

(i) valuation of goods was done in accordance with provisions of Section 4 of the Act and Central Excise Valuation Rules (as amended from time to time);

(ii) credit of duty paid on inputs/capital goods under Modvat/Cenvat was taken correctly;

(iii) service tax on services provided/received by manufacturers was paid correctly; and

(iv) internal controls were effective to safeguard interest of revenue.

4.4 Audit scope

Records of 235 manufacturing units as well as related range offices, in 63 out of 93 commissionerates of central excise, for the period 2002-03 to 2005-06 (upto 30 September 2005), were test checked. The revenue paid by these units during the year 2004-05 was Rs.1928.81 crore.

AUDIT FINDINGS AND RECOMMENDATIONS

MACRO ISSUES

4.5 Excessive Cenvat to PLA ratio in Plastic Sector

Revenue trend of central excise collected relating to plastics, under 63 commissionerates, was as given in the table 1 below: -

Table No.1

Central Excise revenue data relating to plastics

(Amount in crore of rupees)

Year	No of units	Duty paid through PLA	Duty paid through Cenvat	Total duty paid	Percentage of Cenvat to PLA	All commodities percentage of Cenvat to PLA
2002-03	4464	1610.67	2885.74	4496.41	179.16	64.44
2003-04	4938	1829.01	3891.74	5720.75	212.78	73.34
2004-05	5179	2335.61	5385.12	7720.73	230.56	77.34
2005-06 (Upto 30 September 2005)	4865	856.55	2647.02	3503.57	--	--

Figures furnished by commissionerates.

Audit observed that: -

- The percentage of Modvat/Cenvat availed to duty paid in cash in respect of plastic (chapter 39) had been consistently and significantly higher than the all India figures for all commodities.
- Percentage of Cenvat to duty paid in cash has increased from 179.16 per cent during the year 2002-03 to 230.56 per cent during the year 2004-05.
- In Aurangabad and Delhi I commissionerate, percentage of Cenvat to duty paid in cash was as high as 1429 per cent and 745.83 per cent, respectively.

The above facts (excessive Cenvat to PLA ratio) could be indicative of misuse of Modvat/Cenvat scheme by the plastic sector (as also commented upon in this review) in particular unless the tariff structure itself is an inverted one.

Recommendation No.1

Government should investigate/ascertain the exact reasons for such high duty payment by Modvat/Cenvat rather than cash duty payment and based on such investigation (i) plug the loopholes to avoid misuse of Cenvat by plastic sector and; (ii) correct the duty structure (if inverted tariff) to maintain the Cenvat chain in an effective manner.

While responding (January 2007), the Ministry agreed with audit's concern and informed that percentage of Cenvat credit was an important risk parameter based on which they select units for audit/investigation. They, however, explained that the high percentage of Modvat/Cenvat duty payment in plastic sector could be because of low value addition.

MICRO ISSUES

4.6 Manufacture

4.6.1 Probable short accountal/suppression of finished goods

Rule 4 of Central Excise Rules, 2002, stipulates that no excisable goods, on which any duty is payable, shall be removed without payment of duty from any place, where they are produced or manufactured or from a warehouse, unless otherwise provided in the Act/Rules.

(i) M/s. Ori Plast Limited, Balasore in Bhubaneshwar I commissionerate, engaged in the manufacture of HDPE/PVC pipes and fittings, produced and cleared 63,61,918 meters of pipes and 7,59,366 pieces of fittings (as per the central excise records) during the year 2002-03. Cross verification with commercial records of the assessee disclosed production of HDPE pipes as 66,79,366 meters and PVC pipes as 9,18,594 pieces. Thus, there was a probable short accountal/suppression of 3,17,448 meters of pipes and 1,59,228 pieces of fittings on which excise duty to the extent of Rs.29.30 lakh was liable to be paid by the assessee, alongwith penalty and interest.

(ii) Similarly, M/s. Machino Plastic Limited, Gurgaon in Delhi III commissionerate, engaged in the manufacture of plastic produced 4,368 MT of finished goods by consuming 4370 MT of polyproplene, a major input during 2003-04. But a test check of their records revealed that during the year 2004-05, 5075 MT of the same finished goods were produced by consumption of the 5180 MT of the same input. Taking into consideration the input-output ratio of the previous year, the production of the finished goods during the year 2004-

05 should have been 5,177 MT. There was, thus, a probable short accountal of 102 MT of finished product. This resulted in non-payment of excise duty of Rs.22.58 lakh including education cess.

On this being pointed out (July 2005), the department issued a show cause notice for Rs.22.58 lakh.

4.7 Valuation

Rule 5 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rule, 2000 provides that only the actual cost of transportation including insurance was to be deducted for arriving at 'transaction value'. Further, the Board vide its circular dated 30 June 2000 clarified that in addition to the amount charged as price from the buyer, any other amount recovered by the assessee by reason of or in connection with sale, shall also form part of the assessable/transaction value.

4.7.1 M/s. Amiantit Fiberglass Industries (India) Private Limited, in Goa commissionerate, engaged in manufacture of glass reinforced pipes and glass reinforced tanks, collected freight in excess of what was actually paid to the transporters. Such excess realisation of freight was, therefore, required to be included in transaction value. Non-inclusion of such freight element in the transaction value resulted in undervaluation of excisable goods to the extent of Rs.77.18 lakh and consequent short levy of duty of Rs.12.34 lakh during the period 2003-04 to 2004-05.

4.7.2 Other cases of undervaluation

Test check of records revealed that in 12 other cases, there was undervaluation due to non-inclusion of additional consideration resulting in non-payment of duty of Rs.19.94 lakh, out of which Rs.12.32 lakh had since been recovered, at the instance of audit.

4.7.3 Undervaluation of goods captively consumed

Rule 8 of Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 stipulates that where excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in manufacture of other articles, assessable value shall be 115 per cent (110 per cent with effect from 5 August 2003) of the cost of production of such goods.

(i) M/s. Ajay Poly (P) Limited, New Delhi in Delhi II commissionerate, engaged in manufacture of PVC compound and PVC basket cleared their products to sister units for captive use, in the manufacture of other articles. Test check of their records revealed that goods were valued at lower rate based on transaction value instead of on value arrived by cost construction method i.e. 115 per cent/110 per cent of cost of production. This resulted in short payment of duty of Rs.18.97 lakh for the period from July 2000 to July 2004.

(ii) M/s. Essel Propack Limited, in Thane I commissionerate, engaged in the manufacture of plastic laminated web, cleared these products to related person, viz. M/s. Essel Packaging (Nepal) Private Limited for consumption on 'transaction value' instead of on the value

determined in accordance with Rule 8 of the Valuation Rules. This resulted in undervaluation of goods and short payment of excise duty to the extent of Rs.17.53 lakh.

On this being pointed out (October 2005), the department admitted the objection (July 2006) and intimated the recovery of Rs.17.53 lakh (August 2006).

(iii) Similarly there were eight other cases of short payment of duty of Rs.28.38 lakh due to non-adoption of cost construction method, of which Rs.13.20 lakh had since been recovered, at the instance of audit.

4.8 Cenvat credit

Under Modvat/Cenvat scheme, credit is allowed for duty paid on 'specified inputs' and 'specified capital goods' used in manufacture of finished goods. Credit can be utilised towards payment of duty on finished goods subject to fulfilment of certain conditions. A few cases of incorrect availment of Modvat/Cenvat credit, noticed in test audit are elucidated in the following paragraphs: -

4.8.1 Incorrect availment of Cenvat on the inputs used in trial run

Rule 3 of Cenvat Credit Rules, 2004 provides that a manufacturer shall be allowed to take credit on any inputs. Further, Rule 2, ibid defines 'inputs' as goods used in or in relation to the manufacture of final product whether directly or indirectly. CESTAT, in the case of M/s. Reliance Industries Limited, Surat {2004 173 ELT 106} held that inputs used in trial run production are not eligible for Modvat/Cenvat credit.

M/s. Shree Rama Multi Tech. Limited in Ahmedabad III commissionerate, engaged in the manufacture of 'aluminium foil backed plastic' used various inputs for trial run production during the period 2004-05. The assessee availed Cenvat to the extent of Rs.1.31 crore on these inputs and expenditure incurred thereon was capitalised during the year 2004-05. Since these inputs were not used in or in relation to the manufacture of final products, the availment of Cenvat credit of Rs.1.31 crore was irregular and ought to have been reversed.

4.8.2 Incorrect availment of Cenvat credit on unspecified capital goods

Rule 2 of Cenvat Credit Rules, 2004 stipulates that Cenvat credit on capital goods is admissible only on specified capital goods used in the factory.

Six manufacturers availed of Cenvat credit of Rs.10.85 lakh irregularly on ineligible capital goods. Of these, Rs.5.96 lakh were reversed, at the instance of audit.

4.8.3 Excess availment of Cenvat credit on capital goods

Rule 4(2)(a) of Cenvat Credit Rules, 2004 provides that Cenvat credit, in respect of capital goods received in a factory at any point of time in a given financial year, shall be taken only for an amount not exceeding 50 per cent in the same financial year. Further, the Cenvat credit in respect of capital goods shall be allowed for the whole amount of the duty paid on such capital goods in the same financial year, if such capital goods are cleared 'as such' in the same financial year.

(i) M/s. Supreme Industries Limited and M/s. Nilkamal Plastics Limited, in Pondicherry commissionerate, engaged in manufacture of 'moulded plastic furniture', availed fifty per

cent of Cenvat credit of the duty paid on receipt of the moulds. After putting the moulds to use for some time, the assessees transferred the same to their sister concerns and availed the remaining 50 per cent of Cenvat credit to the extent of Rs.2.79 crore and Rs.1.37 crore respectively in the same financial year. Since the capital goods were used for sometime, the same were not cleared as such from the factory. The availment of 50 per cent of the remaining Cenvat credit was, therefore, irregular. This resulted in incorrect availment of Cenvat credit to the extent of Rs.4.16 crore. On this being pointed out (November 2005), the Department stated (February 2006) that SCNs for Rs.3.71 crore (April 2003 to December 2005) and Rs.2.09 crore (April 2002 to September 2003), respectively have since been issued.

(ii) M/s. Sumi Motherson Innovative Engineering Limited, in Noida commissionerate, availed 100 per cent Cenvat credit of Rs.42.18 lakh on capital goods in the same year viz. 2004-05. This resulted in excess availment of Cenvat credit to the extent of Rs.21.59 lakh during 2004-05.

(iii) Two other cases of irregular availment of 100 per cent of Cenvat in the same financial year are given in the table 2 below: -

Table No.2

(Amount in lakh of rupees)

Sl. No.	Commissionerate	Name of assessee	Amount of Cenvat credit	Amount reversed
1.	Bhubaneshwar II	M/s. Krishna Plast Pipes (P) Limited, Bargarh	5.25	
2.	Indore	M/s. Kirti Industries	2.37	2.37
		Total	**7.62**	**2.37**

4.8.4 Simultaneous availing of Modvat/Cenvat credit on capital goods and depreciation under Income Tax Act

Rule 4(4) of the Cenvat Credit Rules, 2004 prescribes that credit in respect of capital goods shall not be allowed, in respect of that part of the value of capital goods which represents the amount of duty on such capital goods, which the manufacturer claims as depreciation under Section 32 of the Income Tax Act, 1961.

M/s. Rexor India, Faridabad, in Faridabad commissionerate, availed Cenvat credit of Rs.45.89 lakh during 2004-05 and 2005-06 on capital goods. A test check of the records of assessee revealed that the assessee had claimed depreciation on Rs.45.89 lakh representing the amount of duty. As depreciation was charged on the capitalised value of capital goods which was inclusive of duty of excise, availment of credit to the extent of Rs.45.89 lakh was incorrect.

4.8.5 Non-reversal of credit on remission of duty

Board vide circular dated 1 October 2004 clarified that credit of excise duty paid on inputs used in the manufacture of the finished goods on which the duty has been remitted due to damage or destruction etc. was not permissible and the dues with interest should be recovered.

M/s. Supreme Industries Limited, in Indore commissionerate, is engaged in the manufacture of EPE sheets, air bubble film, etc. On destruction of finished/semi-finished goods in a fire accident on 22 August 2001, the commissioner vide adjudication orders dated 4 April 2003 remitted the duty of Rs.38.23 lakh payable on such goods. But the assessee did not reverse

the credit on inputs used in the manufacture of finished/semi-finished goods destroyed in the fire. This resulted in incorrect availment of credit of Rs.33.43 lakh. Besides, interest of Rs.22.15 lakh was also payable by the assessee.

4.8.6 Short payment of duty on goods cleared as scrap

Rule 16(1) of the Central Excise Rules, 2001/2002, provides that where any goods, on which duty is paid at the time of removal, are brought to any factory for being remade, refined, reconditioned or for any other reason, the assessee shall state particulars of such receipt in his records and shall be entitled to take Cenvat credit. Sub-rule 2 of Rule ibid, further provides that if the process to which the goods are subjected before being removed does not amount to manufacture, the manufacturer shall pay an amount equal to the Cenvat credit taken.

M/s. Cosmo Films Limited, in Vadodara II commissionerate, availed credit on final product received back in the factory for re-conditioning. The assessee, however, scrapped the goods and paid duty at scrap value. The duty so paid was less than the Cenvat credit availed. As the scrapping of goods by cutting did not amount to manufacture, the assessee was required to clear them by payment of duty equal to Cenvat credit taken. This resulted in short payment of duty to the extent of Rs.9.87 lakh, during the period from April 2002 to March 2005.

On this being pointed out (June 2005), the department intimated (December 2005) recovery of Rs.9.87 lakh.

4.8.7 Inputs cleared 'as such' to sister units

Rule 3(4) of Cenvat Credit Rules, 2001 as it existed before 1 March 2003 provided that when inputs or capital goods on which Cenvat credit has been taken are removed as such from factory, duty would be payable on value determined under Section 4 of Central Excise Act, 1944. If the removal of inputs is in the nature of transfer to sister unit, value of goods would be 115 per cent of cost of production in terms of Rule 8 and proviso to Rule 9 read with Rule 11 of Valuation Rules, 2000.

M/s. Lanxess ABS Limited, in Vadodara I commissionerate, is engaged in manufacture of plastic articles. The assesssee cleared inputs as such to their sister units, after payment of duty by adopting transaction value instead of 115 per cent of landed cost of inputs. This resulted in short levy of duty to the extent of Rs.11.15 lakh, for the period from July 2000 to February 2003.

Short payment of duty amounting to Rs.72.95 lakh due to non-adoption of value equivalent to 115 per cent of landed cost was also noticed in 14 other cases.

4.8.8 Non-reversal of Cenvat credit on material sent to job worker

Rule 4(5)(a) of the Cenvat Credit Rules, 2004, provides that if inputs or capital goods sent to job worker for further processing are not received back within 180 days, the manufacturer shall pay an amount equivalent to the Cenvat credit attributable to the inputs or capital goods by debiting the Cenvat credit or otherwise.

M/s. AV Light Automotive Limited, Faridabad and M/s. Perfect Pac Limited, Faridabad in Delhi IV commissionerate, cleared goods valuing Rs.3.11 crore and Rs.19.21 lakh for job work during the period from May 2002 to March 2005, respectively. But the material was not received back even after a period of 180 days. The assessees were required to reverse the

Cenvat credit of Rs.49.75 lakh and Rs.3.07 lakh, respectively. This resulted in irregular availment of Cenvat credit to the extent of Rs.52.82 lakh.

4.8.9 Other cases

Thirty five other cases involving irregular availment of Cenvat credit on inputs/capital goods to the extent of Rs.71.67 lakh were noticed in audit. Of these, an amount of Rs.31.71 lakh was recovered at the instance of audit.

4.9 Service tax

Scrutiny revealed that some manufacturers of plastic articles had provided services to clients/received services, on which service tax was payable. In audit opinion, lack of information of taxable service provided in excise returns of manufacturers could be one of the reasons for non-detection of cases of non-payment of service tax by manufacturers. Some illustrative cases of non-payment of service tax noticed in audit, are mentioned in the following paragraphs.

4.9.1 Services rendered by foreign consultants

Rule 2(1)(d)(iv) of Service Tax Rules, 1994 as amended provides that a person receiving taxable service would have to pay service tax, if the service provider was non-resident or was from outside India and did not have any office in India.

(i) Scrutiny of records of M/s. GAIL India Limited, in Kanpur commissionerate, revealed that they availed services of foreign consultants viz. M/s. Nova Chemical Corporation, Switzerland and M/s. Mitsui Chemical, Japan and paid an amount of Rs.20.18 crore to these companies. Service tax amounting to Rs.1.95 crore was, however, not paid by the assessee in respect of payment made to non-resident service providers. Interest amounting to Rs.26.89 lakh and penalty Rs.1.95 crore was also payable.

(ii) Scrutiny of records of M/s. Petro Araldite (P) Limited, in Chennai I commissionerate, revealed that the assessee had paid service charges of Rs.4.26 crore to a foreign company viz. M/s. Vantico AG, Switzerland towards Management Consultancy services during 2003-04 to 2004-05. Service tax of Rs.40.46 lakh was, however, not paid by the assessee in respect of payment made to non-resident service providers. Besides interest of Rs.6.14 lakh and penalty of Rs.40.46 lakh was also payable.

(iii) Five other cases of non-payment of service tax of Rs.29.96 lakh on service rendered by foreign consultants were noticed in audit. On these being pointed out (August 2005), the department accepted the observation in one case and recovered Rs.2.02 lakh in another case (September 2005)

4.9.2 Erection, commissioning or installation service

Section 65(28) of Finance Act, 1994 (as amended by Finance Act, 2003) defines "commissioning and installation" as any service rendered by commissioning and installation agency in relation to erection, commissioning and installation of plant, machinery or equipment. Under notification dated 21 August 2003, in case of composite contract for supplying plant, equipment and its commissioning and installation, service tax is payable on 33 per cent of gross amount charged from customer.

(i) M/s. Jindal Poly Films Limited, in Nasik commissionerate, paid Rs.60 crore (approximately) to Bruckner Maschinenbay, Germany in foreign currency for supply,

erection, commissioning and installation of plant for the production of plain and co-extruded BOPP film. This amount included Rs.1.66 crore as service charges on which service tax of Rs.16.97 lakh was payable.

On being pointed out (September 2005), the department recovered (February 2006) service tax of Rs.16.97 lakh, alongwith interest of Rs.2.35 lakh.

(ii) In another case, M/s. Machino Plastic Limited, in Gurgaon commissionerate, did not pay service tax of Rs.0.78 lakh on Rs.7.68 lakh received as commissioning charges.

4.9.3 Service tax on intellectual property service

Service tax on intellectual property service was levied with effect from 10 September 2004. Under Section 65(55a) of the Finance Act, 1994 intellectual property service means transferring temporarily or permitting the use of any intellectual property right, any right to intangible property viz. trade mark, design, patent or any other similar intangible property under any law for the time being in force but does not include copy right.

(i) M/s. LG Polymers (I) Limited, in Visakhapatnam I commissionerate, received an amount of Rs.122.26 lakh for rendering services falling under the ambit of 'intellectual property right' service during the period from January 2005 to December 2005. Service tax and education cess amounting to Rs.12.47 lakh was not paid. Besides, penalty equal to service tax was payable. On this being pointed out (March 2006), the department stated (April 2006) that SCN had since been issued.

(ii) In other four cases, assessees did not pay service tax of Rs.23.93 lakh on the amount of Rs.2.35 crore recovered for rendering intellectual property right service. In addition, they were liable to pay penalty of Rs.23.93 lakh.

4.9.4 Banking and financial services

Service tax on 'banking and financial services' was levied with effect from 16 July 2001. Under Section 65(12) of the Finance Act, 1994, banking and other financial services, inter-alia, include financial leasing services including equipment leasing and hire purchase. The Government clarified on 9 July 2001 that in case of hire purchase agreement, finance charges together with processing charges/documentation charges would form part of the consideration for the services rendered, thereby constituting value of taxable service on which service tax is payable.

A scrutiny of records of M/s. GE India Industrial Private Limited, in Vadodara I commissionerate, revealed that they had realised lease charges of Rs.1.75 crore on account of financial leasing services during April 2004 to December 2005. The service tax amounting to Rs.16.93 lakh was, however, not paid. Besides, assessee was liable to pay penalty equal to service tax of Rs.16.93 lakh.

4.9.5 Irregular availment of service tax credit

Rule 2 of Cenvat Credit Rules, 2004 defines 'input service' as any service (i) used by a provider of taxable service for providing an output service, or (ii) used by the manufacturer, whether directly or indirectly, in or in relation to the manufacture of final products and clearance of final products from the place of removal. Further, Rule 3 of the Rules, ibid allows credit of any input service received by the manufacturer of final product or by the provider of output services on or after the 10th day of September, 2004.

M/s. Supreme Petro-Chem Limited, in Raigad commissionerate, availed credit of service tax paid on various services during the period from September 2004 to February 2005 which was not used for the manufacture of goods directly or indirectly in their unit. This resulted in irregular availment of service tax credit of Rs.29.09 lakh. On this being pointed out (September 2005), the department admitted (April 2006) the observation.

In seven other cases, assessees availed of service tax credit of Rs.1.60 lakh irregularly. On this being pointed out (February 2006), credit of Rs.1.19 lakh was reversed by six assessees

4.9.6 Other cases on non-payment/short payment of service tax

Scrutiny of records of manufacturers of plastic and articles revealed that in seven other cases, service tax of Rs.19.45 lakh payable on various services provided by them, was not paid. Besides interest of Rs.0.40 lakh and penalty of Rs.19.45 lakh was also payable.

On this being pointed out (December 2005), the department accepted the objection in two cases and recovered Rs.2.24 lakh including interest.

Recommendation No.2

Since a large number of manufacturers are also providing services on which service tax is leviable, the Board may consider making necessary changes in the format of excise assessment returns of manufacturers to include information relating to taxable services provided by the manufacturers.

While responding to the recommendation, the Ministry stated (January 2007), that registration for Central Excise as well as service tax is based on PAN allotted by Income Tax department and once the entry and processing of returns is automated under Automation of Central Excise and Service Tax (ACES) project, it would be easier to obtain and co-relate service tax data for each manufacturer.

4.10 Internal controls

Under rule 6 of Central Excise Rules, 2002, the assessee is required to follow self-assessment procedure. Departmental officers are, inter-alia, responsible for ensuring the correctness of the assessments made by the assessees; issuing SCN in the event of non-payment, short payment or erroneous refund; adjudicating SCN within prescribed time limit, and enforcing recovery in case of confirmed demands.

Some illustrative cases of ineffective internal control mechanism, noticed during the course of review, are narrated below: -

4.10.1 Non-levy of interest

Rule 7(4) of Central Excise Rules, 2002 prescribes that on finalisation of provisional assessment, the assessee shall be liable to pay interest under Section 11AA or Section 11AB of the Act from the first day of the month succeeding the month for which such amount is determined, till the date of payment.

M/s. E.I. Tubond India Private Limited, Baroda in Vadodara I commissionerate, paid the differential duty of Rs.26.77 lakh relating to the period from December 2002 to December 2004. But the department did not recover due interest of Rs.3.79 lakh from the assessee.

On this being pointed out (September 2005), the department recovered an interest of Rs.3.79 lakh from the assessee.

Nine other cases of department's failure to recover interest of R.3.20 lakh under the various provisions of Central Excise Act and Central Excise Rules were noticed in audit. Of these, interest of Rs.75 thousand was recovered in five cases.

4.10.2 Default in payment of duty and incorrect utilisation of Cenvat credit

(i) Rule 8(4) of the Central Excise Rules, 2002, stipulates that where an assessee failed to pay fortnightly instalment of duty, beyond 30 days from the due date on one occasion or failed to adhere to the due dates and paid duty with delays ranging upto 30 days on any three occasions in a financial year whether in succession or otherwise, the facility of fortnightly payment of duty was to be forfeited for a period of two months or till such date on which all dues are paid, whichever is later. In such a case, assessee could discharge his duty liability only through personal ledger account (PLA) on consignment basis. Utilization of Cenvat credit during the period of forfeiture towards payment of duty attracts levy of penalty, not exceeding duty leviable on the goods cleared or ten thousand rupees, whichever is greater.

M/s. Bhansali Engineering Polymers Limited and M/s. Super Pack, in Bhopal commissionerate of Central Excise, defaulted in fortnightly payment of duty on three occasions between April 2002 and August 2002; M/s. Super Pack also defaulted in making payment of duty within 30 days on one occasion, during this period. The jurisdictional Assistant Commissioner/Deputy Commissioner ought to have issued necessary orders forfeiting the facility to pay dues in instalments and debarring the assessees to use Cenvat credit. This resulted in incorrect utilisation of Cenvat credit of Rs.1.13 crore and Rs.3.69 crore, respectively which would otherwise have been paid by cash. Besides, penalty under Rule 25 of the Central Excise Rules, 2002 was also leviable.

(ii) Rule 8(1) of the Central Excise Rules, 2002 as amended with effect from 1 March 2003 provides that the duty on the goods removed from the factory or the warehouse during the month shall be paid by the 5th day of the following month. Further, Rule 8(3) stipulates that till such time the amount of duty outstanding and the interest payable thereon are not paid, it shall be deemed that the goods in question in respect of which the duty and interest are outstanding have been cleared without payment of duty and where such duty and interest are not paid within a period of one month from the due date, the consequences and the penalties as provided in the rules, shall follow.

M/s. Nuchem Limited, in Faridabad commissionerate, defaulted in payment of duty of Rs.13.92 lakh for the month of April by more than one month. While the duty was deposited after one month, education cess of Rs.15 thousand was yet to be deposited by the assessee till the date of audit (July 2005). The department, however, failed to take action under Rule 25(a) and Rule 27 of the Central Excise Rules for levy of penalties.

On this being pointed out (July 2005), the department issued (September 2005) a show cause notice.

4.10.3 Cases pending adjudication

According to provisions of Section 11A of Central Excise Act, 1944, where SCNs had been issued, central excise officer was required to adjudicate cases within six months in normal cases and within one year, in cases of non-levy/short levy due to fraud, collusions etc., where it was possible to do so.

Test check revealed that in 22 commissionerates of central excise, adjudication of 100 SCNs issued to manufacturers of plastic and articles thereof, involving revenue of Rs.52.99 crore were pending for adjudication. Fifty nine per cent of the cases constituting 94 per cent of the total revenue involved were more than a year old. Around 10 per cent of cases involving 11 per cent of the value of pendency were pending adjudication for more than five years.

Despite the amendment brought in Section 11A of the Act, fixing time limit for adjudication of demand notices, albeit, with qualification 'where it was possible to do so', pace of finalisation was very slow. Such pendency was indicative of the need to monitor disposal of adjudication cases more effectively.