

CHAPTER-II TRADE TAX/VALUE ADDED TAX

2.1 Tax administration

Trade Tax (TT) (known as Commercial Tax after December 2007) is the major source of revenue of the State and contributed 61 *per cent* (₹ 20,825.18 crore) of the total tax revenue (₹ 33,877.60 crore) to the State exchequer during the year 2009-10. The levy of commercial tax is governed by the provisions of the Uttar Pradesh Trade Tax Act, 1948 (UPTT Act) and rules made thereunder upto 31 December 2007, and thereafter by the provisions of the Uttar Pradesh Value Added Tax Act, 2007 (UPVAT Act). The levy of Central Sales Tax is regulated by the provisions of the Central Sales Tax Act, 1956 (CST Act) and the rules made thereunder.

The UPTT Act provides that as soon as an assessment is made by the concerned Assessing Authority (AA) (Commercial Tax Officer) he shall send the dealer a notice in form XI, together with a copy of the assessment order and the dealer shall pay the tax so assessed within 30 days from the receipt of the notice. The demand notice depicts tax already paid by the dealer and the balance due from him. If the dealer fails to deposit the tax, it can be recovered as arrears of land revenue under the provisions of the Uttar Pradesh Zamindari Abolition and Land Reforms Act, 1950 (UPZA & LR Act). A Recovery Certificate (RC) in this regard is forwarded by the AAs to the District Collectors for collection of the amount specified therein. However, with effect from October 1998, in 14 districts¹, the AAs have been empowered to act as recovery officers of their concerned circles and have been entrusted the work of recovery under UPZA & LR Act. They work under the overall control of the Commissioner Commercial Tax (CCT).

The Principal Secretary, *Kar Evam Nibandhan* Uttar Pradesh, is the administrative head at Government level. The overall control and direction of the Commercial Tax Department vests with the CCT, Uttar Pradesh with headquarters at Lucknow. He is assisted by Additional Commissioners, Joint Commissioners (JCs), Deputy Commissioners (DCs), Assistant Commissioners (ACs) and Commercial Tax Officers (CTOs).

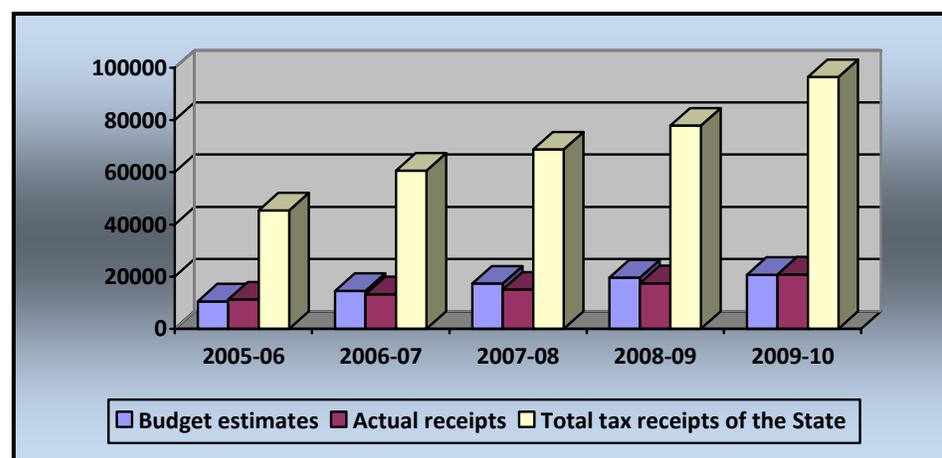
2.2 Trend of receipts

Actual receipts from Trade Tax/VAT during the last five years 2005-06 to 2009-10 along with the total tax receipts during the same period is exhibited in the following table and graph:

¹ Agra, Aligarh, Allahabad, Bareilly, Noida, Gorakhpur, Ghaziabad, Jhansi, Kanpur, Lucknow, Meerut, Moradabad, Saharanpur, Varanasi.

(` in crore)

Year	Budget estimates	Actual receipts	Variation excess(+) shortfall (-)	Percentage of variation	Total tax receipts of the State	Percentage of actual Trade Tax/VAT receipts vis-à-vis total tax receipts
2005-06	10,524.00	11,284.67	(+) 760.67	(+) 7.23	45,349.15	24.88
2006-07	14,528.00	13,278.82	(-) 1,249.18	(-) 8.60	60,599.52	21.91
2007-08	17,314.10	15,023.10	(-) 2,291.00	(-) 13.23	68,672.47	21.88
2008-09	19,705.00	17,482.05	(-) 2,222.95	(-) 11.28	77,830.73	22.46
2009-10	20,741.27	20,825.18	(+) 83.91	(+) 0.40	96,420.95	21.60



2.3 Analysis of arrears of revenue

The arrears of revenue as on 31 March 2010 amounted to ` 16,453.30 crore of which ` 11,462.56 crore were outstanding for more than five years. The following table depicts the position of arrears of revenue during the period 2005-06 to 2009-10:

(` in crore)

Year	Opening balance of arrears	Amount collected during the year	Closing balance of arrears
2005-06	7,209.68	1,246.65	8,456.33
2006-07	8,456.33	6,113.24	14,569.19
2007-08	14,569.19	3,487.63	11,081.94
2008-09	11,081.94	4,307.91	15,389.85
2009-10	15,389.85	1,063.45	16,453.30

2.4 Cost of VAT per assessee

The cost of VAT per assessee during the period from 2008-09 to 2009-10 is tabulated below:

Year	Number of dealers	Gross collection (` in crore)	Expenditure on collection (` in crore)	Cost per assessee (in `)
2008-09	5,79,900	17,482.05	272.54	4,699.78
2009-10	5,75,434	20,825.18	358.43	6,228.86

2.5 Arrears in assessment

The details of assessments relating to commercial tax pending at the beginning of the year, additional cases that became due for assessment during the year, cases disposed during the year and cases pending at the end of the year as furnished by the Commercial Tax Department during 2005-06 to 2009-10 are mentioned below:

Year	Opening balance	Cases which became due for assessment	Total	Cases disposed of during the year	Cases pending at the close of the year
2005-06	5,30,722	5,33,349	10,64,071	5,22,962	5,41,109
2006-07	5,41,109	6,00,531	11,41,640	5,64,532	5,77,108 ²
2007-08	5,76,968	6,19,710	11,96,678	2,58,011	9,38,667
2008-09	9,38,667	5,33,358	14,72,025	9,50,313	5,21,712
2009-10	5,21,712	1,83,378	7,05,090	6,92,704	12,386

2.6 Cost of collection

The gross collection in respect of major revenue receipts, expenditure incurred on collection and percentage of such expenditure to the gross collection during the years 2007-08, 2008-09 and 2009-10 along with the relevant all India average percentage of expenditure on collection to gross collection for 2008-09 are mentioned below:

Head of revenue	Year	Gross collection	Expenditure on collection	Percentage of cost of collection to gross collection	(` in crore)
					All India average percentage for the year 2008-09
Commercial tax	2007-08	15,023.10	228.19	1.52	0.88
	2008-09	17,482.05	272.54	1.56	
	2009-10	20,825.18	358.43	1.72	

The cost of collection was two times higher than the all India average.

The Government needs to take appropriate measures to bring down the cost of collection.

2.7 Revenue impact of audit

During the last five years (excluding the report of the current year), we through our Audit Reports had pointed out non/short levy, non/short realisation, underassessment/loss of revenue, incorrect exemption, concealment/suppression of turnover, application of incorrect rate of tax, incorrect computation etc., with revenue implication of ` 1,644.16 crore in 7,044 cases. Of these, the Department/Government had accepted audit observations in 419 cases involving ` 8.93 crore and had since recovered ` 1.32 crore, the details are shown in the following table:

² The closing balance as on 31 March 2007 does not tally with the opening balance as on 1 April 2007.

(` in crore)

Year	No. of units audited	Amount objected		Amount accepted		Amount recovered	
		No. of cases	Amount	No. of cases	Amount	No. of cases	Amount
2004-05	468	1,150	152.48	8	1.01	4	0.05
2005-06	411	1,169	161.29	47	1.45	6	0.11
2006-07	473	1,548	74.60	38	0.36	6	0.02
2007-08	489	1,210	1,191.14	124	0.51	114	0.46
2008-09	591	1,967	64.65	202	5.60	128	0.68
Total	2,432	7,044	1,644.16	419	8.93	258	1.32

2.8 Results of audit

On test check of the assessments and other records of commercial tax offices, conducted during 2009-10, we found non/short levy of tax, non/short levy of tax due to misclassification of goods and incorrect rate of tax, irregular exemption, etc. of ` 77.32 crore in 2,711 cases, which fall under the following categories:

(` in crore)

Sl. No.	Categories	Number of cases	Amount
1.	Transition from Trade Tax to VAT (A Review)	01	-
2.	Non/short levy of penalty/interest	917	25.95
3.	Non/short levy of tax	911	26.95
4.	Irregular grant of exemption from tax	539	16.40
5.	Incorrect classification of rate of goods	68	0.71
6.	Misclassification of goods	52	1.10
7.	Irregularities relating to central sales tax	29	0.47
8.	Mistake in computation	39	0.65
9.	Turnover escaping tax	09	0.31
10.	Other irregularities	146	4.78
Total		2,711	77.32

During the year 2009-10, the Department accepted under assessments and other deficiencies of ` 7.13 crore involved in 559 cases of which 33 cases involving ` 14.62 lakh had been pointed out during 2009-10 and the remaining in the earlier years. The Department recovered ` 35.99 lakh in 112 cases during the year 2009-10, of which eight cases involving ` 1.97 lakh related to the year 2009-10 and the balance to the earlier years.

A review on ‘**Transition from Trade Tax to VAT**’ and a few illustrative cases involving ` 15.95 crore are mentioned in the succeeding paragraphs.

2.9 Transition from Trade Tax to Value Added Tax

Highlights

- Tax Audit wing of the Department is not functional even after the lapse of three years of VAT implementation.
(Paragraph 2.9.9)
- Dealers, having turnover of ` one crore and above are required to submit the Annual Audited Accounts whereas according to provisions of the Income Tax Act, all the dealers, having turnover of ` 40 lakhs and above keep an audited annual accounts.
(Paragraph 2.9.12.2)
- Abolition of all the 83 check posts, working at strategic points, round the clock resulted in non confirmation of the delivery of the transit passes at the exit point of the check posts by the vehicles coming from outside the states and bound for any other place outside the state.
(Paragraph 2.9.13)
- The State Legislature introduced levy of additional tax under the Uttar Pradesh Value Added Tax Act, 2008 with effect from 1 June 2009, though the White Paper on Value Added Tax (VAT) specifically discouraged levy of additional tax.
(Paragraph 2.9.15)
- Verification of deposits by the dealers is still being done by the Deputy Commissioner (Administration) whereas as per VAT rules it is to be done by the concerned Assessing Authorities.
(Paragraph 2.9.17)

2.9.1 Introduction

The Union Government in the Ministry of Finance had constituted an Empowered Committee of State Finance Ministers (Empowered Committee), to resolve the variations in the State Sales Tax Act and to introduce state level Value Added Tax (VAT). The Empowered Committee, after deliberation, had issued a White Paper (January 2005) defining the basic designs of the State level VAT. The White Paper, however, allowed the states to adopt appropriate variations in their VAT Act, consistent with the basic design. The major designs put forth in the White Paper were as follows:

- The manufacturers and traders will be given input tax credit for purchase of inputs including that on capital goods meant for use in manufacture or resale.
- Input tax credit, remaining unadjusted till the end of the second year, and also on exports, will be refunded to the dealers.
- The dealers will submit self assessment returns declaring their tax liability under the state level VAT and these self assessment returns will be

considered as deemed assessment, except where notice for the audit of books of accounts of the dealer was issued.

- Audit of books of accounts of the dealer will be de-linked from tax collection wing to remove any bias.
- The existing incentive schemes will be continued in a manner deemed appropriate by the State, after ensuring that the VAT chain is not affected.
- Taxes such as turnover tax, surcharge, additional surcharge and special additional tax would be abolished.

Major variations in the repealed Act (Uttar Pradesh Trade Tax Act) with the Uttar Pradesh Value Added Tax Act were as follows:

The UP Trade Tax Act, 1948 (UPTT Act) and rules made thereunder had governed the levy of tax on sales and purchases of goods prior to the implementation of VAT in Uttar Pradesh. The President of India approved the introduction of the Uttar Pradesh Value Added Tax Bill, 2007 in November 2007. The Bill was promulgated by an ordinance in December 2007 and enacted as the UP Value Added Tax Act, 2008 (UPVAT Act) with effect from 01.01.2008 repealing the UPTT Act on sales and purchases of goods.

- The repealed Act provided for the levy of tax at the first stage of sale/purchase or at the last stage on selected goods whereas the UPVAT Act provides for the levy of tax at each stage on value addition and the input tax credit on purchases to nullify the cascading effect.
- The repealed Act provided for compulsory assessment in all cases; whereas, under the UPVAT Act more reliance is placed on self assessment returns. In place of the provision of direct assessment in the repealed Act, the UPVAT Act provides powers to audit the books of accounts, maintained by the dealers, on selective basis, before final assessment.
- On introduction of the UPVAT Act various declaration forms prescribed for concessions and exemptions under the repealed Act were abolished. The UPVAT Act contains 82 sections and five schedules. Under Section 79 of the UPVAT Act, the State Government had notified (March 2008) the UP Value Added Tax Rules, 2008 (UPVAT Rules), prescribing the procedures to be followed while implementing the Act.
- The White Paper provided for basic rates of four *per cent*, 12.5 *per cent* and on special category one *per cent*. Consistent with the White Paper, the rate of tax under the UPVAT Act given in schedule II was four *per cent* on



a majority of goods. In schedule V, goods other than those specified anywhere in the schedule are taxable at the rate of *12.5 per cent* and in Schedule III, goods are taxable at the rate of *one per cent*. Schedule I contains the goods on which no tax is leviable and Schedule IV provides tax ranging from *four per cent* to *32.5 per cent*. With effect from 01.06.2009, the State has introduced an additional tax at the rate of *0.5 per cent* on goods classified in Schedule-II, other than declared goods and at the rate of *one per cent* on all goods except goods mentioned in Schedule I to IV of UPVAT Act. These rates of additional tax were revised with effect from 19.02.2010.

- Under the repealed Act, every registered dealer was allotted with a separate registration number. After implementation of the UPVAT Act, these dealers were allotted eleven digits number known as tax payer's identification number (TIN). The new dealers under the UPVAT Act were also issued with TIN.
- The UPVAT Act provides for payment of a lump sum amount as composition in lieu of the tax, to the dealers whose total turnover in a financial year had not exceeded ` 50 lakh with certain terms and conditions.

We reviewed the transitional process from Trade Tax to VAT in the state, which revealed a number of deficiencies in the process and also lacunae in the UPVAT Act, Rules made thereunder and notifications issued from time to time.

2.9.2 Organisational setup

The Principal Secretary (Commercial Tax-Entertainment Tax), Uttar Pradesh is the administrative head at Government level. The overall control and direction of the Commercial Tax Department is with the Commissioner Commercial Tax, Uttar Pradesh with headquarters at Lucknow.

After implementation of the VAT Act, the Department has been geographically organised into 20 zones, each headed by an Additional Commissioner and these zones are further divided into 45 Regions each headed by a Joint Commissioner. A total of 436 sectors, each headed by a Deputy Commissioner, are working in these 45 regions.

2.9.3 Audit objectives

Since the VAT Act has been in place for two and a half years we conducted the review to ascertain whether:

- planning for implementation and the transition from the Trade Tax Act to VAT Act was effected timely and efficiently;
- the organisational structure is adequate and effective;
- the provisions of the VAT Act and Rules made thereunder, are adequate and enforced properly to safeguard the revenue of the State; and
- an internal control mechanism exists in the Department and is adequate and effective to prevent leakage of revenue.

2.9.4 Scope and methodology of audit

The review covered the period from 2004-05 to 2008-09. We conducted the review in two phases. In the first phase, from August 2009 to March 2010 we checked the assessment cases finalised during 2004-05 to 2008-09. In the second phase between May 2010 and August 2010, we checked the records on VAT for the period 01.01.2008 to 31.03.2008.

There are 45 regions, under 20 zones of the department. Based on high revenue generation and the regions sharing borders with other states, we categorised the regions in three risk areas-high, medium and low. Regions contributing more than 70 *per cent* revenue were classified as high risk areas, regions contributing more than 20 *per cent* revenue were classified as medium risk areas and regions contributing about 10 *per cent* revenue were classified as low risk areas. For the purpose of the review, out of 440 assessment offices, 105 offices were identified. 22 units belong to high risk areas, 28 units of medium risk areas and 11 units of low risk areas. Two units of mobile squads, each from high risk and medium risk, were also taken up for review. Besides, information was also collected from the 20 assessment offices and 20 units of mobile squads. To ensure uniform coverage of all parts of the State, units were selected from the North, South, East, West and Central zones of the State. The information on issues relating to implementation of VAT Act was collected from the office of the Commissioner Commercial Tax and from the administrative section of the Commercial Tax Department in the Government Secretariat.

2.9.5 Acknowledgement

We acknowledge the cooperation of the *Kar Evam Nibandhan Vibhag*, Uttar Pradesh and the Department of Commercial tax in providing information and records for audit. The entry conference with the Department was held on 5 May 2010 wherein the criteria, scope and methodology of the audit was discussed. The Department was represented by the Additional Commissioner (*vidhi*). The exit Conference was held with the Department on 26 November 2010 wherein the draft review was discussed. The Government was represented by Joint Secretary (Commercial Tax-Entertainment Tax). The response of the Department to the draft review has been incorporated in the appropriate places in the succeeding paragraphs.

Audit findings

2.9.6 Financial analysis

2.9.6.1 Reconciliation of revenue collected

Para 125 of the Budget Manual provides for reconciliation of the departmental figures with the figures booked in the office of the Accountant General (Accounts and Entitlement) to ensure accuracy in the departmental accounts.

We noticed variations between the figures published in the Annual Report of the Commercial Tax Department (CTD) and figures of Finance Accounts under the Major Head 0040 - Sales Tax.

The figures as reflected in the Annual Report of the CTD and the Finance Accounts are shown below:

(₹ in crore)

Year	As per Annual report of the CT Department	As per Finance Accounts	Difference
2004-05	9,226.37	8,888.31	338.06
2005-06	11,805.32	11,284.67	520.65
2006-07	14,053.85	13,278.82	775.03
2007-08	15,021.83	15,023.10	(-) 1.27
2008-09	17,403.68	17,482.05	(-) 78.37

Source: Reports of the Comptroller & Auditor General of India (Revenue Receipts) - Government of Uttar Pradesh and Annual report for the year 2008-09 of the Commercial Tax Department.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that the reconciliation is being conducted now and therefore the difference between two sets of figures of accounts has come down considerably. The fact, however remains that the Department still could not reconcile the figures with those of the Finance Accounts.

2.9.6.2 Trend of revenue

The comparative position of pre-VAT trade tax collection (2004-05 to 2006-07), post-VAT tax collection (2007-08 to 2009-10), growth rate and average growth rate of tax collection in each of the years covered in the review is given in the following table:

(in crore)

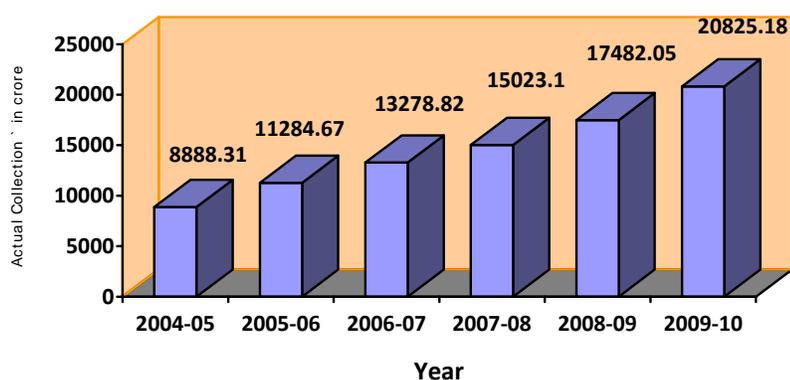
Year	Pre-VAT			Year	Post-VAT		
	Actual collection	Percentage of growth over previous year	Average percentage of growth rate of three years		Actual collection	Percentage of growth over previous year	Average percentage of growth rate of three years
2004-05	8,888.31	15.67		2007-08 ³	15,023.10	13.14	
2005-06	11,284.67	26.96	20.10	2008-09	17,482.05	16.37	16.21
2006-07	13,278.82	17.67		2009-10	20,825.18	19.12	

Source: Reports of the Comptroller & Auditor General of India (Revenue Receipts) - Government of Uttar Pradesh.

It is evident from the above table that the average growth rate during 2004-05 to 2006-07 was 20.10 *per cent* while it was 16.21 *per cent* from 2007-08 to 2009-10. The average growth rate in the post VAT period therefore registered a decrease of 3.89 *per cent*. The percentage growth of actual collection for the year 2007-08 was below the growth rate of 2006-07 whereas VAT was implemented since 1.01.2008 and in the new system, tax was to be recovered after each value addition. In the same way during 2008-09 and 2009-10, growth rate of actual collection is below 20 *per cent* whereas during 2005-06 it was above 25 *per cent* during pre-VAT period.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that after implementation of the VAT about 200 commodities of public use were exempted from tax. Commodities taxable at the rate of six and eight *per cent* under the UPTT Act were put in the slab of four *per cent* under the VAT Act. Further, reduction in the rate of Central Sales Tax from four to three *per cent* and in the next year to two *per cent* also affected the gross collection of revenue.

Year wise Actual Collection



³ Composite period of pre-VAT and post-VAT.

2.9.6.3 Variation between budget estimates and actual receipts

As per the provision of Para 25 of the Budget Manual, in the preparation of the budget the aim is to achieve as close an approximation to the actual as possible. It is therefore essential that not only all items of revenue and receipts should be provided but the arrears, if any, standing over from past years for collection should be included in the budget estimates.

The budget estimates formulated by the Government for collection of revenue under UP VAT Act and actual collection for the years 2007-08 to 2009-10 are given in the following table:

(in crore)

Year	Budget estimates	Percentage of increase in budget estimates over the previous year	Actual receipts	Percentage of increase in actual receipts over the previous year
2007-08 ⁴	17,314.10	19.18	15,023.10	13.14
2008-09	19,705.00	13.80	17,482.05	16.37
2009-10	20,741.27	5.26	20,825.18	19.12

Source: Reports of the Comptroller & Auditor General of India (Revenue Receipts) - Government of Uttar Pradesh.

It is evident from the above table that after the implementation of the VAT Act, while the percentage of increase in actual receipts has been showing an increasing trend during 2007-08 to 2009-10, the budget estimates show a decreasing trend during that period. In 2009-10 percentage of increase in budget estimates is only 5.26. It indicated that budget estimates were not based on actual receipts and arrears of previous years as per the provision of the budget manual.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that budget estimates are received from the Finance Department and every year revised budget estimates are prepared at a fixed growth rate. We do not agree as the percentage of increase in budget estimates for the year 2009-10 is much below the percentage increase in actuals for the year 2008-09.

The Government may therefore take necessary steps to ensure that the provisions of the budget manual are followed while formulating the budget estimates, so that these are close to the actual receipts.

2.9.7 Preparedness and transitional process

The Empowered Committee of State Finance Ministers constituted by the Government of India felt that the state level VAT system should be simultaneously implemented by all the states of the Union so as to avoid problems in implementation as well as to the trade and industry. The White Paper was an expression of the genuine commitment of the states to the implementation of the VAT system from 1 April 2005.

⁴ Composite period of Pre-VAT and Post-VAT.

While the majority of the states implemented the VAT Act between April 2005 to January 2007, in UP the VAT Act was implemented from 01 January 2008.

2.9.7.1 Creation of awareness of the VAT system among the dealers

The implementation of the UPVAT Act was assigned to the Department of Commercial Tax. The Department made concerted efforts to create awareness of the new Act among the stakeholders *viz.*, the dealers. Booklets outlining the UPVAT law and an accounting tool covering the requirements of UPVAT law, was developed and were distributed free of cost to the dealers. Besides, awareness about the VAT was also created through print media.

2.9.7.2 Reorganisation of the department and analysis of the staff position

We observed that after the implementation of the VAT Act, the set up of the Department was reorganised and the number of zones, assessment offices and AAs were increased by 46 *per cent* and 30 *per cent* respectively but the ministerial staff and structure of the internal audit remained unchanged. Further, the status of persons-in-position is much below the sanctioned number of posts for the last four years. These shortages may hamper revenue generation. Details regarding category-wise organisational set-up and staff position during the pre-VAT and post-VAT period is given in **Appendix-I**.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that proposal was sent to the Government for appointment of various categories of officials but only 49, 38 and 29 junior clerks, stenographers and drivers could be filled up. Further, the proposal has been sent to the Government in August 2010 for appointment in various categories of posts.

The Government may therefore consider taking necessary steps for carrying out comprehensive manpower review in the Department of Commercial Taxes.

2.9.7.3 Increase in number of dealers vis-à-vis increase in number of assessment offices

The White Paper issued by the Empowered Committee provided for self assessment of tax liability by the dealers. Under the VAT Act, compulsory assessment at the end of each year had been dispensed with and a *per cent* check has been provided for.

The position of the average number of dealers per assessing office before and after implementation of VAT is given in the following table:

Pre-VAT				Post-VAT			
Year	Number of dealers	Number of assessment offices	Average number of dealers per office	Year	Number of dealers	Number of assessment offices	Average number of dealers per office
2005-06	4,77,433	241	1981	2008-09	5,79,900	441	1315
2006-07	5,14,350	241	2134	2009-10	5,75,434	441	1305
2007-08 ⁵	5,15,826	241	2140				

Source: Information supplied by the Commercial Tax Department.

Under the UPTT Act, when all the cases were assessed *cent per cent*, the average number of dealers ranged from 1981 to 2140 per assessment office⁶ and after the implementation of VAT Act when the provision of carrying out *cent per cent* assessment has been replaced with a percentage checking of assessments, the average number of dealers has been reduced to between 1305 and 1315 per assessment office. It may be seen from the above table that after implementation of the VAT Act, the increase in the number of offices of the assessment is 83 *per cent* whereas increase in the number of dealers after the implementation of VAT Act is only 12.42 *per cent*.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that before implementation of VAT, 1000 dealers per assessing office was the ideal norm and under the VAT system, offices were restructured keeping in view the above figure. The Department accepted that in the pre-VAT period, the number of dealers per Assessment office was much higher but the offices were not restructured.

The Government may therefore consider reviewing the position at fixed intervals for equal distribution of work amongst the assessing officers of the Department.

2.9.7.4 Uneven allotment of dealers for assessment work

We scrutinised the system of deployment of dealers under the charge of an AA. Information regarding allotment of dealers under the charge of three levels of AAs collected from 21 assessment offices⁷ of 11 districts during the year 2009-10 is given below:

Range of number of dealers	Dealers per Deputy Commissioner	Dealers per Assistant Commissioner	Dealers per Commercial Tax Officer
0 to 100	10	Nil	Nil
101 to 200	9	Nil	1
201 to 300	Nil	6	2
301 to 400	1	6	5
401 to 500	1	7	3
501 and above	Nil	2	10

⁵ Composite period of pre-VAT and post-VAT.

⁶ In each assessment office, there are three assessing authorities - Dy. Commissioner, Assistant Commissioner and Commercial tax officer.

⁷ DC-10 & 11 Agra, DC-3 & 9 Allahabad, DC-7 & 8 Aligarh, DC-3 Bareilly, DC-12, 17 & 21 Kanpur, DC-16 Lucknow, DC-7 & Sardhana Mandal Meerut, DC-3 & 7 Moradabad, DC-3 & 8 Muzaffarnagar, DC-10 & 14 Noida and DC-5 & 6 Varanasi.

We observed that under the charge of a Dy. Commissioner, an Assistant Commissioner and a Commercial Tax Officer the minimum number of dealers allotted were 49, 211 and 153 respectively whereas the maximum numbers of dealers were 454, 790 and 1536 respectively for the purpose of assessment. We analysed the criteria of distribution of the dealers and found that a district was divided on the basis of geographical location. It is evident that in each city some of the areas have more commercial activities and some areas are non-commercial, i.e. purely residential areas. This geographical distribution caused variation in allotment of number of dealers. Further, no norms for allotment of dealers have been fixed by the Department with reference to the number of dealers. The figures depicted in the above table reveals that the work distribution (allotment of the dealers) among the AAs was not uniform.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that sectors will be re-structured to avoid such differences from the beginning of the year 2011-12.

The Government may consider allotment of dealers in a more scientific way to ensure equal distribution of dealers amongst the AAs.

2.9.7.5 Cross verification

Under the UPVAT law, cross verification of records of purchasing/selling dealers and cross check of data available with other taxation departments were of utmost importance to ensure proper realisation of Government revenue. With a view to help the Commercial Taxes departments of various States and Union Territories in monitoring the sales/purchases made in the course of interstate trade and commerce, the Empowered Committee of State Finance Ministers authored a website named Tax Information Exchange System (TINXSYS) as a repository of interstate transactions.

We collected information from the IT wing of the office of the Commissioner of Commercial Taxes and found that 890 users have been created to verify the data of dealers as well as forms of the other States through this website. Central Sales Tax (CST) dealers' information and CST Form Baseline Data is sent

and uploaded in this website, but at present all the Central forms are being issued manually. Hence, the data relating to such forms are not available in the TINXSYS website resulting in non-verification of inter-State transactions.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that at present the forms are being distributed manually but these would be made available online very soon. After the start of this facility, online sharing of database with TINXSYS will be possible on the real time basis.

The Government may consider taking of necessary steps to make the system operational at the earliest.

2.9.7.6 Computerisation of the Department

The Commercial Tax Department has started the activities of computerisation of the Department in the second half of the financial year 2007-08. The consultants for the project, National Informatics Centre (NIC), developed a web based Integrated Application Software called Vanijyakar Automation System (VYAS).

The main aim of the project was to cater to the needs of the Department by providing Web based Citizen Centric services, such as use of technology to alter the way of services, exchange of information with the public and other Government Departments,

improving internal efficiency, exploiting true revenue potential and enhancement and up-gradation of the current applications.

The total projected cost for the Information Technology system was ` 45 crore and the target date for the finalisation is March 31, 2012. Till March 2010, expenditure of ` 27.26 crore has been incurred.

VYAS application system is presently running in 93 locations in decentralised mode. There is a core team of five officers at the Headquarters level and the IT wing operations are maintained by departmental officers with technical background. There are 20 zones, each headed by one Nodal officer and one IT Group member for operating the system. Since 1 January 2008, under the VYAS system modules and online application are operational.

During the course of our audit we noticed the following deficiencies related to the computerisation work:

- Automatic alerts are not generated to prompt the users to change their password periodically, though required as a prudent security policy.
- The process of data flow, to and from the local to the Central Server is yet to be stabilised and auto scheduling is still to be developed. There is no concurrent database at local and central server. Thus, analytical data at State level is not available, resulting in incomplete analytical reports of little use for MIS and Control.
- Collection of information from the four offices⁸ of the Joint Commissioner (Executive) Kanpur and six offices⁹ of the Dy. Commissioner (Assessment) revealed that no data was available in respect of exemptions/concessions of tax granted, though a reliable database, of exemptions/concessions of tax allowed to dealers is a prerequisite for informed decision making.
- Database of dubious or risky dealers based on their past history has not been prepared.
- The modules related to reports, user administration management and online application of MIS report are developed but not fully

⁸ JC (E) Range A, B, C & D Kanpur.

⁹ DC-3 & 9 Allahabad, DC-21 Kanpur, DC-16 Lucknow and DC- 3 & 7 Moradabad.

operational and some of the specific MIS reports are manually generated.

- There is no system continuity and disaster recovery plan and there are no defined responsibilities or teams to manage any system disaster.
- Documented methods for the Data Centre operations, performance monitoring, information security and contingency management, defined policy for the documented user administration, role management plan and defined hardware policy is lacking.
- The database management under the VYAS is done by the NIC but the Department had not implemented any long term policy to have its own IT professionals.
- There has been increase of 83 *per cent* in number of offices of assessment but the sanctioned number of computer operators remained unchanged.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that instructions have been issued to the offices for change of password and in subsequent application, it would be developed. Export/import utility has been provided in the software for transfer from local to Central server. Database of exemption and concession has not been maintained because it is not likely to continue beyond 2012. Provision for preparing a database of risky dealers has been made in the Tax Audit Manual. At present backups are taken and soon a disaster recovery site is proposed to be set up. At present the Department is using the data centre of NIC. In future the Department will switch over to State Data Centre having well defined policies. Hardware maintenance is being taken care of at the Zonal level. Proposal for additional posts from System Controller to Computer Operator has been sent to the Government.

We do not agree to the contention of the Department with regard to discontinuance of exemption/concession and data base of risky dealers as the VAT Act too provided for granting exemption of tax. Further under the Tax Audit Manual, system of preparation of database of risky dealers did not exist. There are no documented methods for Data Centre operations, performance monitoring, information security etc. at 93 local sites of the Department.

The Government may consider taking necessary steps to ensure that concurrent database at local and central server is available for use by skilled manpower.

2.9.7.7 Creation of manuals

A manual maps the processes and provides a reference point to navigate as well as for organising training on the new Act. It also lays down a framework of internal controls for effective monitoring.

Although the UP VAT Act has been in place for more than two and half years, the Department is yet to prepare a VAT manual. As a result, the various

wings of the Department do not have a reference point for effective practices.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that the Tax Audit Manual has been prepared and a manual relating to various work of the Department is under preparation.

The Government may consider issuing appropriate directions for bringing out a manual containing procedures to be followed day to day functioning of the various activities of the Commercial Tax Department at the earliest.

2.9.7.8 Training

We noticed that before implementation of VAT, training relating to VAT was imparted only to the officers and officials engaged in assessment of the cases at the zonal level. Besides, from time to time, training was also imparted in the training centre of the Department at Lucknow. Though officers and officials of the internal audit wing were also required to be trained, no such training was imparted to them.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that during the whole year training is imparted to officers/officials of the various wings but the Department could not give any specific reply regarding training of VAT to the officials of Internal Audit Wing, either before or after implementation of the VAT.

The Government may consider imparting training to the staff of the internal audit wing at regular intervals.

2.9.8 Registration of dealers

Under the provision of Section 17 of UPVAT Act, every dealer liable to pay tax i.e. taxable quantum of five lakh rupees, shall apply to the registering authority within the prescribed period and shall obtain registration certificate. There is no provision in the Act for compulsory registration of such dealers, who are found carrying on business above the threshold limit nor is there any mechanism to analyse the dealers carrying on business below threshold limit.

The number of registered dealers during the period from 2005-06 to 2009-10 vis-à-vis receipts per dealer is given in the following table:

(₹ in lakh)

Period	No. of dealers	Percentage of increase (+)/ decrease(-) with reference to previous year	Actual receipts	Percentage of increase in actual receipts with reference to previous year	Receipts per dealer
2005-06	4,77,433	--	11,28,467	--	2.36
2006-07	5,14,350	7.73	13,27,882	17.67	2.58
2007-08	5,15,826	0.29	15,02,310	13.14	2.91
2008-09	5,79,900	12.42	17,48,205	16.37	3.01
2009-10	5,75,434	(-)0.77	20,82,518	19.12	3.61

Source: Information supplied by the Commercial Taxes Department.

It could be seen from above that after implementation of the UPVAT Act, there was an increase in VAT receipts and receipts per dealer but in comparison with the increase in actual receipts, increase in number of registered dealers has been showing a declining trend in 2009-10.

2.9.8.1 Non-registration of dealers carrying out business above threshold limit

We collected information from the 24 offices¹⁰ of the Assistant Commissioner (Mobile Squad), and found that 7,777 dealers, with goods worth ` 96.46 crore were caught without valid documents during 2007-08 to 2009-10. After realising tax and penalty amounting to ` 37.48 crore, the vehicles were released. In all the cases, it was seen that the dealers were carrying on their business above the threshold limit. There is no provision in the Act for compulsory registration of such dealers.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that the Commissioner Commercial Taxes has issued¹¹ instructions to ensure registration of the unregistered dealers. But the Department could not intimate the number of dealers who have been registered after the issue of the circular. We feel that the specific provision may be made in the Act and Rule for registration of unregistered dealers.

The Government may consider providing for compulsory registration of unregistered dealers detected by the mobile squads and evolving a system to identify unregistered dealers who have crossed the threshold limit and get them registered.

2.9.8.2 Filing of e-returns

A dealer, whose aggregate of turnover is likely to exceed or has exceeded in preceding assessment year one crore rupees from 1 February 2009 and two crore rupees from 1 July 2009 or such amount as may be determined by the State Government from time to time, shall submit e-return online on the official website of the Department.

We collected information from the CCT and found that 3,09,366 and 1,62,875¹² e-returns were filed during 2008-09 and 2009-10 respectively. We had suggested in

October 2010 that the Government should make provision for submission of online return for all registered dealers.

The Department stated in December 2010 that filing of e-return has been made compulsory for all the dealers irrespective of the turnover vide Circular dated 21 December 2010.

¹⁰ AC (MS) 1 to 9 Agra, AC (MS) Badaun, AC (MS) Aam Tanda, Bareilly, AC (MS) A & B range Bareilly, AC (MS) Gazipur, AC (MS) 5 & 8 Ghaziabad, AC (MS) 1 to 5 Noida, AC (MS) Pilibhit, AC(MS) Shahjahanpur, AC (MS) 1 Varanasi.

¹¹ Circular No. 1004 dated 22 September 2010.

¹² The number reduced due to increase in limit from rupees one crore to rupees two crore.

2.9.9 Tax audit

Section 44 of the UPVAT Act, read with Rule 43 of the UPVAT Rules, provides for the examination related to the correctness of tax return or returns filed by a dealer to verify admissibility of various claims including claim of input tax credit by the departmental authorities in tax audit.

We collected information from 23 assessment offices¹³ and found that no tax audit wing has been created even after the new Act being in place for

more than two years and time barring period for the assessment of the cases of 2007-08 (01.01.2008 to 31.03.2008) is 31 March 2011. Further, no instructions in this regard were received in any offices of the AAs from the office of the Commissioner Commercial Tax.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that in each zone a unit of Tax Audit has been constituted. In each zone there is sanctioned post of one Joint Commissioner, two Deputy Commissioners, three Assistant Commissioners and three Commercial Tax Officers. However keeping in view the availability of the officers only 17 Joint Commissioners and three Assistant Commissioners have been posted to make it functional. Officers will be posted in the remaining audit units subject to availability of the officers.

We feel that delayed action to scrutinise the cases by tax audit wing may result in delay in realisation of additional tax, if due, for that period besides the cases being barred by limitation. Thus the Government may consider ensuring that Tax audit wing is made functional at the earliest.

2.9.10 Creation of Settlement Commission

Under the provision of section 62 of the UP VAT Act 2008, there shall be a Settlement Commission for settlement of amount of tax in case of imposition of penalty for concealment of the turnover or for unauthorised import of any goods by the dealer.

We collected information from the office of the Commissioner, Commercial Tax and found that even after the new Act, being in force for more than two and a half years, a Settlement Commission has not been constituted, though a

Chairman was appointed on 15 September 2008.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that the Chairman of Settlement Commission has been appointed and appointment of its members is pending at the Government level.

The Government may consider ensuring that the Settlement Commission is made functional at the earliest.

¹³ DC-10 & 11 Agra, DC-3 & 9 Allahabad, DC-7 & 8 Aligarh, DC-3 & AC-3 Bareilly, DC-4, Ghaziabad, DC-12, 17 & 21 Kanpur, DC-16 Lucknow, DC-7 & Sardhana Mandal Meerut, DC-3 & 7 Moradabad, DC-3 & 8 Muzaffarnagar, DC-10 & 14 Noida and DC-5 & 6 Varanasi.

2.9.11 Self assessment

23 offices¹⁴ of Assessment

Under the UP VAT Act, every dealer who has submitted annual return of turnover of tax, in the prescribed form and manner, shall be deemed to have been assessed to an amount of tax admittedly payable.

We found that the cases for the year 2007-08 (1.04.07 to 31.12.07) were finalised under the provision of the UPTT Act and rules made thereunder but no case

was finalised for the period 1.01.2008 to 31.03.2008, under the VAT Act. The time barring period for finalisation of the assessment under the VAT Act for the above mentioned period is 31.03.2011.

We suggest that the assessment cases should be finalised proportionately in each month.

2.9.12 Deterrence in the System

2.9.12.1 Change in draft of penal provision

We studied 40 Judicial Pronouncements, delivered by the Allahabad High Court, related to imposition of penalty under the UPTT Act and found that 30 Judgements¹⁵ were delivered in favour of dealers. As per prevailing practice in the Department some cases which are found fit for further appeal in Supreme Court, are referred to State representative for further appeal but number of such cases are very few.

The penal provisions in the VAT Act were not redrafted keeping in view the judgements on the penal provisions under UPTT Act.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that the matter is being examined by the *Vidhi Anubhag* and if it was found necessary provision for imposition of penalties would be amended accordingly.

2.9.12.2 Differences with the Income Tax Act

Under the provision of Section 21(17) of UP VAT Act, every person carrying on business exceeding ` one crore, shall get his accounts audited by a Chartered Accountant (CA). But section 44-AB of the Income Tax Act 1961 provides monetary limit of ` 40 lakh for it.

We noticed that the dealers with gross turnover (GTO) of more than ` 40 lakh have to keep audited accounts under the Income Tax (IT) Act but they are not

¹⁴ DC-10 & 11 Agra, DC-3 & 9 Allahabad, DC-7 & 8 Aligarh, DC-3 & AC-3 Bareilly, DC-4 & 9 Ghaziabad, DC-12, 17 & 21 Kanpur, DC-16 Lucknow, DC-7 & Sardhana Mandal Meerut, DC-3 & 7 Moradabad, DC-3 & 8 Muzaffarnagar, DC-10 Noida and DC-5 & 6 Varanasi.

¹⁵ Cases of Judicial Pronouncements delivered against the Department are given in Appendix-II.

required to submit it to the UP Commercial Tax Department as monetary limit under the VAT Act is ₹ one crore. In the Madhya Pradesh VAT Act, the limits are the same as that of the IT Act. In the absence of provisions on the lines of the IT Act, the AAs are not in a position to cross-verify the information in the cases of dealers having GTO between ₹ 40 lakh and ₹ one crore.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that the VAT Act has been passed by the legislature after detailed discussion and consideration.

The Government may consider keeping the monetary limit of turnover at ₹ 40 lakh for getting the accounts audited by CAs in line with the provisions of the Income Tax Act.

Other related issues

2.9.13 Check points

Under the provision of Section 28 of UPTT Act and Section 49 of UPVAT Act, check posts at strategic points along its borders with the neighbouring states and under Section 45 of UPVAT Act, mobile squad units, inside the states, were responsible for checking the movement of goods, not covered by proper documents. But after the abolition of check posts the mobile squad units are the sole checking agency.

With a view to check the evasion of tax by irregular import of goods into UP and their non-accounting in the books of accounts by the dealers, check posts were established at strategic points along its borders with the neighbouring states. This system of check

posts existed at the time of implementation of the VAT Act but during 2008-09 and 2009-10, all the 83 check posts were abolished in two phases. The numbers of mobile squads has been increased to 150 from the earlier 54 but at present only 127 units are functional.

Details regarding vehicles which entered with unauthorised goods and amount of security/penalty recovered from them from 2003-04 to 2007-08, are given below:-

Year	2003-04	2004-05	2005-06	2006-07	2007-08
No. of check posts	78	81	81	83	83
No. of vehicles which entered with unauthorised goods	6,75,701	7,00,935	6,35,454	5,28,350	5,84,282
Amount recovered as security/penalty (₹ in crore)	127.71	123.75	135.46	141.69	149.88

Source: Annual report for the year 2008-09 of the Commercial Tax Department.

It is evident from the above table that a large number of traders entered the State without valid documents and when caught at the check posts, they paid the amount of security/penalty.

We observed that when check posts were working round the clock, the number of vehicles that entered with unauthorised goods ranged between five and seven lakh during 2003-04 to 2007-08. We also observed that during 2007-08 when 83 check posts were working at strategic points round the clock, 2282 unregistered dealers were caught by nine mobile squad units within the State. However, after abolition of check posts, 2,385 and 3,110 unregistered dealers were caught by the mobile squads during 2008-09 and 2009-10. In these cases goods worth ` 96.46 crore were seized and ` 37.48 crore were recovered between 2007-08 and 2009-10. Hence despite the existence of check posts, there was a possibility that dealers without valid documents were slipping through the check posts. Thus, abolition of check posts without creating an effective alternative has caused substantial loss of revenue to the State.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that it was decided by the Government of India that the State Government should abolish the barriers at the border of the State. In the light of the above order, for easy and smooth transportation of goods loaded vehicles, check posts were abolished in two phases and in order to make the checking system more effective, number of mobile squads have been increased. The fact however remains that the Department did not devise a system to ensure that vehicles transiting through UP border for other States do not off-load their goods in UP.

The Government may consider devising an effective mechanism to prevent the leakage of revenue after the abolition of check posts and also develop a system to ensure that vehicles transiting through UP to other states do not offload their goods in UP.

2.9.14 Claims for compensation of loss due to introduction of VAT

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.

We collected the information from the office of the Commissioner, Commercial Tax and found that claim of ` 189.96 crore has been worked out for the year 2007-08 (only for the month of February and March 2008) and submitted (7.01.2010) to Government of India. Scrutiny of the records of the office of the Principal Secretary *Kar Avam Nibhandhan* revealed that the compensation amount has not been received so far.

2.9.15 Levy of Additional Tax

The White Paper issued by the Empowered Committee *vide* paragraph 2.16 specifically discouraged levies of other taxes viz., turnover tax, surcharge, additional surcharge and special additional tax under the VAT system.

Provision of non-levy of other taxes was suggested to avoid multiple types of taxes and to have a more simplified tax structure under the VAT system.

We observed that after the implementation of the VAT Act, with effect from 01.06.2009, the State had introduced an additional tax at the rate of 0.5 *per cent* on goods classified in Schedule-II, other than declared goods and at the rate of one *per cent* on all goods except goods mentioned in Schedule I to IV of UPVAT Act. These rates of additional tax were revised with effect from 19.02.2010. This was in contravention to the basic concept of the State level VAT.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that Additional tax has been levied by the legislature after due consideration and other States have also levied the additional Tax.

2.9.16 Monitoring of exemption of tax

2.9.16.1 Exemption to Medical and Dental Colleges

Section 4(c) of the UPTT Act and Section 7(c) of UPVAT Act provides exemption of tax on taxable goods in case a notification is issued by the State Government in this behalf.

We observed that *vide* notification no. 1529 dated 21 May 1997, in case of Medical Colleges, no tax shall be charged on the

purchase of apparatus and equipments up to ` 10 crore for five years from the date of permission to open the College and in case of Dental Colleges the exemption limit was ` five crore for the period of five years from the date of permission to open the College with certain terms and conditions.

As the Medical and Dental Colleges are not registered in the Department, exemption of tax provided by special notification remains unmonitored. Tax free purchases beyond the prescribed monetary limit and beyond the stipulated time cannot be ruled out.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that suggestion of monitoring has been taken into account by the *Vidhi Anubhag* and wherever it would be necessary proposal for this would be sent to the Government but the Department could not tell how the cases of exemptions are being monitored in above mentioned cases.

The Government may consider ensuring that each notification issued in respect of grant of exemption contain the method/system of monitoring to determine the correctness of claims.

2.9.16.2 Exemption on sale of vehicles to Armed Forces/Defence establishments

Sansthaगत Vitta, Kar evam Nibandhan Anubhag-2 vide their notification no. 2372 dated 24.11.2009, provided that no tax shall be payable by a dealer on the turnover of sale of vehicles for personal use subject to fulfillment of certain terms and conditions and with the restriction of annual sale of 3000 two wheelers and 1,200 four wheelers of whole State. However, the Department did not prescribe any specific return for the dealers to ensure correctness of exemptions upto prescribed number of vehicles.

We noticed that the sale of vehicles to the members of Armed Forces of India/other defence establishments or defence Ex-servicemen are made within the State of UP through many canteen

stores departments/ Military canteens. There are a number of such canteen stores departments/Military canteens in UP. The notification has not clarified the modalities to monitor the number of vehicles sold and also not specified the nodal agency to monitor the same. In absence of monitoring agency, sale of vehicles exceeding the provided number in a year, cannot be ruled out.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that suggestion of monitoring has been taken into account by the *Vidhi Anubhag* and wherever it would be necessary proposal for this would be sent to the Government but the Department could not tell how the cases of exemptions are being monitored in above mentioned cases.

The Government may consider prescribing a periodic and specific return for the dealers selling vehicles to the members of Armed Forces/Defence establishments in Uttar Pradesh.

Compliance deficiencies

2.9.17 Verification by treasury and reconciliation of discrepancy

24 offices¹⁶ of Assessment

Under the provision of Rule 52 of the repealed UPTT Rules 1948, the Assistant Commissioner (Administration) or Dy. Commissioner (Administration) was responsible for verification of the deposits made by the dealer, during the month, with the records of the treasury or sub-treasury. But under Rule 14 of the UPVAT Rules 2008, the Assessing Authorities were designated the task of verification of accounts.

We found that even after the new UPVAT rules were in place for more than two and a half years, verification of deposits were still being done under the system prevailing in the pre-VAT period i.e. the verification is

being done by the Dy. Commissioner (Administration) and not by the AAs.

¹⁶ DC-10 & 11 Agra, DC-3 & 9 Allahabad, DC-7 & 8 Aligarh, DC-3 Bareilly, AC-3 Bareilly, DC-9 Ghaziabad, DC-12 & 21 Kanpur, DC-15, 16 & 17 Lucknow, DC-7 & Sardhana Mandal Meerut, DC-3 & 7 Moradabad, DC-3 & 8 Muzaffarnagar, DC-10 & 14 Noida, DC-5 & 6 Varanasi.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that the suggestion given by the Audit is being examined.

The Government may consider ensuring that the verification system, prevailed in pre-VAT period is discontinued and system of reconciliation of deposit of tax works according to the UPVAT rules.

2.9.18 Finalisation of assessment

34 offices¹⁷ of Assessment

Under the provision of Rule 232 of departmental manual (based on Trade Tax Act), monthly quota for finalising the assessment order was fixed for different category of Assessing Authority. As per rules, Dy. Commissioner (Assessment) would finalise 10 cases per month.

We collected information for the years 2008-09 and 2009-10 and found that the bulk of the cases were finalised during the month of March. The percentage of finalisation of the total cases in the

month of March was 79 per cent and 77 per cent during 2008-09 and 2009-10 respectively.

We observed that as per provision of the existing manual, cases were not finalised as per norms fixed. This quota has been fixed so that cases might be finalised only after thorough, intensive and indepth checking of the books of accounts and other statements, filed by the dealer.

Under the provision of the VAT Act/Rules no such quota for finalisation of the assessment has been fixed. As the new manual has not yet been prepared, no guidelines have been provided in this regard. It is evident that most of the cases are finalised at the end of the financial year.

The Government may consider ensuring that the cases are finalised according to the provision of the existing manual till the creation of new manual.

2.9.19 Unused declaration forms

21 offices¹⁸ of Assessment

Under the UPTT Act, various declaration forms were prescribed for allowing concessional rate of tax or exemption from the levy of tax on purchases. With effect from 1 January 2008, after the implementation of the VAT Act, the previous system of exemption and concessions of tax, based on declaration forms, has been discontinued.

We noticed that assessment cases for the year 2007-08 (01.04.2007 to 31.12.2007) have been finalised. In such cases, where the assessments are finalised and there is no need of declaration forms,

¹⁷ Details are given in Appendix-III.

¹⁸ DC-10 & 11 Agra, DC-3 & 9 Allahabad, DC-7 & 8 Aligarh, DC-3 Bareilly, DC-12, 17 & 21 Kanpur, DC-16 Lucknow, DC-7 & Sardhana Mandal Meerut, DC-3 & 7 Moradabad, DC-3 & 8 Muzaffarnagar, DC-10 & 14 Noida, DC-5 & 6 Varanasi.

such forms issued in the previous system should have been taken back from the dealers to avoid any misuse.

We found that even after introduction of the new system for more than two and a half years, the Department has not issued any order to take back such forms from the dealers.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that action is being taken by the *Vidhi Anubhag* to cancel the obsolete forms.

The Government may consider ensuring that the order regarding cancellation of unused declaration forms are issued at the earliest to avoid misuse of unused declaration forms.

2.9.20 Internal Control Mechanism

Internal audit is a vital component of the internal control mechanism and is generally defined as the control of all controls to provide reasonable assurance of proper enforcement of laws, rules and departmental instructions. Internal control also helps in creation of reliable financial and management information system for prompt and efficient services and for adequate safeguards against evasion of tax and other irregularities.

The internal audit wing has been functioning under the administrative control of the CCT and the Department has sanctioned 13 posts of Audit Officers, 40 posts of Sr. Auditors and 51 posts of Auditors. However all the 13 posts of Audit Officers, nine posts of Sr. Auditors and 46 posts of Auditors were lying vacant. Internal audit is being conducted with the aid of 60 *per cent* Sr. Auditors/Auditors, without any supervision of Audit Officers. As per the Audit plan total auditable units, number of offices audited by internal audit and number of offices left unaudited for the period 2005-06 to 2009-10 are given in the following table:

Year	Auditable units as per Audit Plan	Audited units	Unaudited units
2005-06	613	360	253
2006-07	619	363	256
2007-08	619	520	99
2008-09	621	562	59
2009-10	618	432	186

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that due to lack of manpower internal audit of all the auditable units could not be conducted and a proposal was sent to the UP Public Service Commission in 2002-03 and 2007-08 followed by several reminders for filling up the vacant posts of the Auditors. At present, only 10 Auditors have been provided by the Commission. As far as appointments of Audit Officers is concerned, it would be filled up on clearing of departmental examination by the Sr. Auditor Grade-I.

The Government may consider taking appropriate steps to ensure that vacant post in each cadre are filled up so that internal audit of all the units identified in the audit plan could be conducted.

2.9.21 Conclusion

We analysed the transitional process from Trade Tax to VAT and noticed that the VAT Act did not provide for conducting of surveys for identification of unregistered dealers. Computerisation of the Department has not been completed even after the new Act being in place for more than two and a half years. Check posts were abolished without developing an effective alternative to check the inflow of the dealers without valid documents. The Government resorted to levy of additional tax instead of tapping potential areas of revenue.

2.9.22 Summary of recommendations

The Government may consider:

- taking necessary steps to ensure that the provisions of the budget manual are followed while formulating the budget estimates;
- taking necessary steps for carrying out comprehensive manpower review in the Department of Commercial Taxes;
- reviewing the position at fixed intervals for equal distribution of work amongst the assessing officers of the Department;
- allotment of dealers in more scientific way to ensure equal distribution of dealers amongst the AAs;
- taking necessary steps to make the system operational at the earliest;
- taking necessary steps to ensure that concurrent database at local and central server is available for use by skilled manpower;
- issuing appropriate directions for bringing out a manual containing procedures to be followed in day to day functioning of the various activities of the Commercial Tax Department at the earliest;
- imparting training to the staff of the internal audit wing at regular intervals;
- providing for compulsory registration of unregistered dealers caught by the mobile squads and evolving of a system to identify unregistered dealers who have crossed the threshold limit and get them registered;
- ensuring that Tax audit wing is made functional at the earliest;
- ensuring that the Settle Commission is made functional at the earliest;
- keeping the monetary limit of turnover at ` 40 lakh for getting the accounts audited by CAs in line with the provisions of the Income Tax Act;
- effective devising an mechanism to prevent the inflow of tax evading dealers after the abolition of check posts and also develop a system to ensure that vehicles transiting through UP border for other states do not offload their goods in UP;
- ensuring that the verification system, prevailed in pre-VAT period is discontinued and system of reconciliation of deposit of tax works according to the UPVAT rules;

- ensuring that the cases are finalised according to the provision of the existing manual till the creation of new manual;
- ensuring that the order regarding cancellation of unused declaration forms are issued at the earliest to avoid misuse of unused declaration forms; and
- taking appropriate steps to ensure that vacant post in each cadre are filled up so that internal audit of all the units identified in the audit plan could be conducted.

2.10 Other audit observations

Our scrutiny of the assessment records of the Commercial Tax Department revealed several cases of non-observance of the provisions of the Acts/Rules, non/short levy of tax/penalty/interest, irregular exemption, incorrect application of rate of tax, etc. as mentioned in the succeeding paragraphs in this chapter. These cases are illustrative and are based on our test check. Such omissions on the part of Assessing Authorities (AAs) have been pointed out by us each year, but not only do the irregularities persist; these remain undetected till an audit is conducted. We feel that there is need for the Government to improve the internal control system including strengthening of internal audit.

2.11 Non-compliance of the provisions of the Act/Rules

The UPTT Act provides for :

- (i) levy of tax and interest at the prescribed rates*
- (ii) imposition of penalties for various kinds of trade offences;*
- (iii) charging of interest in case of belated payment of admitted tax; and*
- (iv) exemption/concessional rate of tax subject to prescribed conditions.*

The AAs while finalising the assessments did not observe some of the above provisions. This resulted in short levy of tax/penalty amounting to ` 3.37 crore as mentioned in the following paragraphs:

2.11.1 Non/short levy of tax due to application of incorrect rate of tax and misclassification of goods

The AAs while finalising the assessments, did not apply the correct rate of tax, given in the schedule of rates and in some of the cases lower rate of tax was applied due to misclassification of goods which resulted in non/short levy of tax of ` 1.40 crore as mentioned in the following paragraphs:

Three Commercial Tax Offices

Under section 8 of the CST Act, 1956, tax on inter-State sale of goods (other than declared goods) not covered by declaration in Form 'C' is leviable at the rate of 10 per cent or at the rate applicable on sale or purchase of such goods inside the appropriate State, whichever is higher.

2.11.1.1 We observed that three dealers made inter state sale of DEPB¹⁹, spirit and alcohol worth ` 50.70 lakh without declaration in Form 'C' during the years 2005-06 and 2006-07. The AA while finalising the assessments between September 2007 and March 2009 levied tax at lower rates instead of the rates applicable. This resulted in short levy of tax amounting to ` 6.78 lakh as mentioned in the following table:-

¹⁹ Duty Entitlement Pass Book.

(` in lakh)

Sl. No.	Name of the unit	Assessment year (month & year of assessment)	Name of commodity	Value of goods	Tax leviable levied (per cent)	Differential rate of tax	Tax short levied
1.	DC-2 CT Bulandshahar	2005-06 (September 2007)	Alcohol	4.69	<u>32.5</u> 10	22.5	1.06
2.	DC-1 CT Dhampur	2006-07 (March 2009)	Alcohol (Spirit)	12.30	<u>32.5</u> 12	20.5	2.52
3.	DC-1 CT Noida	2005-06 (December 2008)	DEPB	13.69	<u>10</u> 0.5	9.5	1.30
		2006-07 (March 2009)	-do-	20.02	<u>10</u> 0.5	9.5	1.90
Total				50.70			6.78

We reported the matter to the Department and the Government between July 2009 and December 2009; their reply has not been received (October 2010).

Four Commercial Tax Offices

Under section 3A of the UPTT Act, tax on classified goods is leviable as prescribed in the schedule of rates, notified by the Government from time to time. The goods not classified in the prescribed schedule of rates, are taxable at the rate of 10 per cent with effect from 1 December 1998.

2.11.1.2 We observed that in the cases of six dealers for the period 2003-04 to 2007-08, the AAs while finalising the assessments between January 2006 and

March 2009, applied incorrect rate of tax on sale of goods worth ` 9.44 crore. This resulted in short levy of tax of ` 14.88 lakh. The details are shown in Appendix-IV.

After we pointed out these cases to the Department and the Government between September 2009 and January 2010, the Department stated in September 2010 that tax of ` 3.59 lakh has been levied (Sl. No. 1 & 2) in two cases. The report on recovery of the same and reply in the remaining cases from the Department and in all cases from the Government have not been received (October 2010).

14 Commercial Tax Offices

We observed between May 2009 and February 2010 that in the cases of 14 dealers, the AAs while finalising the assessments between February 2005 and March 2009 for the years 2003-04 to 2006-07, applied incorrect rate of tax on sale of goods valued at ` 14.87 crore due to misclassification of goods. This resulted in short levy of tax of ` 73.99 lakh. The details are shown in Appendix-V.

After we pointed out these cases to the Department and the Government between July 2009 and February 2010, the Department stated in September 2010 that the tax levied at Sl. No. 2 & 14 are correct. We do not agree with the reply of the Department, as taxability of the preserved food is at the manufacturer or importer point instead of the sale to consumer point which the AA had applied in these two cases.

Eight Commercial Tax Offices

Under Section 3-H of the UPTT Act read with the Commissioners' circular dated 3 May 2005 as applicable from 1 May 2005, State Development Tax (SDT) at the rate of one *per cent* of the taxable turnover shall be levied on a dealer whose annual aggregate turnover exceeds fifty lakh rupees. The SDT shall be realised in addition to the tax payable under any other provision of this Act.

2.11.1.3 We observed between February 2009 and February 2010 that in eight cases of dealers whose annual aggregate turnover exceeded ` 50 lakh, the AAs while finalising (October 2007 and March 2009) the assessments

for the years 2005-06 and 2006-07 did not levy Development tax on taxable turnover of ` 44.52 crore. This omission resulted in non-levy of State Development Tax of ` 44.53 lakh as detailed in Appendix-VI.

We reported the matter to the Department and the Government between April 2009 and March 2010; their replies have not been received (October 2010).

2.11.2 Non-imposition of penalty and non-charging of interest

The AAs while finalising the assessments, did not notice the offences committed by the dealers i.e. irregular transactions, transactions out of account books, transactions against the provisions of the Act and Rules. Though there are clear cut provisions for imposition of penalties and charging of interest in the Act, no action was initiated in this regard, resulting in non-imposition of penalty and non-charging of interest amounting to ` 1.97 crore as mentioned in the following paragraphs:

Four Commercial Tax Offices

Under section 15 A (1) (C) of the UPTT Act, if the Assessing Authority is satisfied that a dealer has concealed his turnover or has deliberately furnished incorrect particulars of his turnover, he may direct such dealer to pay by way of penalty, in addition to tax, a sum not less than 50 *per cent* but not exceeding 200 *per cent* of the amount of tax.

2.11.2.1 We observed between April 2008 and October 2009 that four dealers had concealed sales turnover of ` 6.79 crore during the years 1997-98 to 2006-07. The AAs while finalising their assessments between December 1999 and

March 2009 levied tax of ` 29.52 lakh but did not impose even the minimum penalty of ` 14.76 lakh. The details are given in the following table :

(` in lakh)

Sl. No.	Name of the unit	Assessment year (month & year of assessment)	Concealed turnover	Name of the commodity	Tax levied on concealed turnover	Minimum penalty leviable
1.	DC(A)-1,CT, Bhadohi	2000-01 (July 2003)	275.00	Woolen Yarn	9.88	4.94
		2001-02 (July 2003)	310.00	---do---	11.05	5.53
2.	JC (Corporate) Ghaziabad	2006-07 (March 2009)	40.00	Chocolate and Confectionery	3.60	1.80
3.	AC(A), CT, Hamirpur	1997-98 (December 1999)	15.00	Sand	1.13	0.56
		1998-99 (December 1999)	16.63	---do---	1.25	0.62
		1999-2000 (March 2002)	2.88	---do---	0.22	0.11
4.	DC(A)-2, CT, Moradabad	2004-05 (November 2006)	19.89	GI Pipes, Pipe fittings, Sanitary Goods	2.39	1.20
Total			679.40		29.52	14.76

After we pointed out these cases to the Department and the Government between June 2008 and December 2009, the Department stated between May 2009 and August 2010 that the penalty of ` three lakh in two cases (Sl. No. 2 & 4) has been imposed. The report on recovery and replies in the remaining cases from Department and in all cases from the Government have not been received (October 2010).

Five Commercial Tax Offices

Under section 15 (A) (1) (a) of the UPTT Act, if the Assessing Authority is satisfied that any dealer or other person has, without reasonable cause, failed to furnish the return of his turnover or fails to deposit the tax under the provision of this Act, he may direct the dealer to pay by way of penalty in addition to tax, if any payable by him, a sum which shall not be less than 10 per cent but not exceeding 25 per cent of tax due, if the tax due is upto ` 10,000 and 50 per cent if it is above ` 10,000.

2.11.2.2 We observed between October 2008 and December 2009 that six dealers had not deposited their admitted tax of ` 3.86 crore for the period 2005-06 and 2006-07 in time. The delay ranged between one and 125 days. The AAs while finalising the assessments between February 2008

and March 2009 were required to direct the dealers to pay penalty of ` 38.59 lakh in addition to the tax leviable which was not done. The details are shown in Appendix-VII.

After we pointed out these cases to the Department and the Government between December 2008 and December 2009, the Department stated in May 2009 that the penalty of ` 3.03 lakh in one case (Sl. No. 1) has been imposed. The report on recovery and replies in the remaining cases from the Department and in all cases from the Government have not been received (October 2010).

12 Commercial Tax Offices

Under section 8D (6) of the UPTT Act, a person responsible for making payment to a contractor, for discharge of any liability on account of valuable consideration payable for transfer of property in goods in pursuance of works contract, shall deduct an amount equal to four *per cent* of such sum, payable under the Act, on account of such works contract. In case of failure to deduct the amount or deposit the amount so deducted into the Government treasury before the expiry of the month, following the month in which the deduction was made, the Assessing Authority may direct that such person shall pay by way of penalty a sum not exceeding twice the amount so deducted.

2.11.2.3 We observed between January 2008 and February 2010, that 12 dealers, while making payment to the contractors, deducted tax of ` 30.38 lakh at source during the years 1997-98 to 2006-07 but did not deposit the same into the Government treasury within the prescribed time. The delay ranged between four days and 244 days. The AAs while finalising the assessments between

March 2005 and March 2009 failed to impose the maximum penalty of ` 60.76 lakh. The details are shown in Appendix-VIII.

After we pointed out these cases to the Department and the Government between March 2008 and March 2010, the Department stated between September 2008 and August 2010 that penalty of ` 14.41 lakh in four cases (Sl. No. 2, 3, 6 & 8) had been imposed. The report on recovery and replies in the remaining cases from the Department and in all cases from the Government have not been received (October 2010).

10 Commercial Tax Offices

Under section 10 & 10 A of the Central Sales Tax Act, if a registered dealer purchases any goods from outside the State at concessional rate of tax on the strength of declaration in Form 'C' by falsely representing that such goods are covered by his Registration Certificate under the Central Sales Tax Act or if the goods purchased from outside the State at concessional rate of tax are used for a purpose other than that for which the registration certificate is granted, the dealer is liable to be prosecuted. However, in lieu of prosecution, if the Assessing Authority deems it fit, he may impose penalty up to one and half times of the tax payable on the sale of such goods.

2.11.2.4 We observed between March 2008 and August 2009 that during the years 2001-02 to 2006-07, 10 dealers purchased goods valued at ` 3.58 crore at concessional rate of tax against declaration in Form 'C' which were not covered by their certificates of registration. The AAs while finalising the assessments between December 2005 and March 2009 did not levy penalty of ` 62.17

lakh. The details are shown in Appendix-IX.

After we pointed out these cases to the Department and the Government between April 2008 and December 2009, the Department stated between March 2008 and August 2010 that in three cases (Sl. No. 2, 4 & 6) penalty of ₹ 16.34 lakh has been imposed. The report on recovery of the same and replies in the remaining cases from the Department and in all cases from the Government have not been received (October 2010).

Two Commercial Tax Offices²⁰

Under section 8 (1) of the UPTT Act, every dealer liable to pay tax, is required to deposit the amount of tax into the Government treasury before the expiry of the month, following the month in which the tax was due. The tax admittedly payable by the dealer, if not paid by the due date, attracts interest at the rate of two *per cent* per month up to 11 August 2004 and there after at the rate of 14 *per cent* per annum on the unpaid amount, till the date of deposit.

2.11.2.5 We observed between June 2009 and February 2010, that two dealers, who were assessed between May 2008 and October 2008 for the assessment years 2001-02 and 2003-04, had deposited the admitted tax of ₹ 30.90 lakh late. The

delay ranged between 1,107 and 1,828 days. Belated payment of admitted tax attracted interest of ₹ 20.91 lakh which was not levied by the AAs.

After we pointed out these cases to the Department and the Government between August 2009 and March 2010, the Department accepted the audit observation in September 2010 involving ₹ 15.64 lakh and recovered the same from one dealer. Reply for the other case has not been received from the Department and Government (October 2010).

2.12 Short levy due to freight charges not counted in turnover

Deputy Commissioner (A)-4, CT, Noida

Under section-2(i) of the UPTT Act, turnover means the aggregate amount for which goods are supplied or distributed by way of sale, by a dealer, for cash or deferred payment of other valuable consideration. Further, it has been judicially held²¹ that freight charges form part of turnover even if such charges are shown separately in the sale bills.

We observed (February 2009), that during the year 2005-06 a dealer charged ₹ 6.79 crore as freight on his sale during the year. The freight charged by the dealer was a part of his turnover. The AA while finalising the assessment in March 2008

did not include the freight amount in his sales turnover which resulted in short levy of tax of ₹ 67.91 lakh.

We reported the matter to the Department and the Government in September 2009; their replies have not been received (October 2010).

²⁰ DC (A)-7 CT, Lucknow and DC (A)-3 CT, Mau.

²¹ (1) M/s Black Diamond Beverage & Anr. Vs. The Commercial Tax Officer, Central Section, Assessment Wing, Calcutta and others. STI 1997 SC-272(2) CST Vs. Shivalik Motors and Tractors STI-2005 All.HC 744, 2005 NTN (Vol. 28) 150 All. HC.

2.13 Irregular grant of Recognition Certificate

Deputy Commissioner (Assessment) Commercial Tax, Fatehpur

The Government notification dated 21 May 1994 issued under section-4B of the UPTT Act, provides for special relief in tax to the manufacturer on purchase of raw material, processing material, consumable stores, machinery, plant, equipment, spare parts, accessories, components, fuel or lubricants for use in the manufacture of specified goods.

We observed that a dealer was granted Recognition Certificate for purchase of raw material at concessional rate of tax for conversion of MS Rod into MS Wire by drawing process. It has been judicially held²² that conversion of MS Rod into

MS Wire does not amount to manufacture. Since the dealer was not engaged in any manufacturing process, he was not entitled to concessional rate of tax on purchase of raw material valued at ` 6.80 crore during the years 2005-06 and 2006-07. This resulted in irregular grant of recognition certificate and loss of revenue of ` 13.60 lakh.

After we pointed this out to the Department and the Government between January 2009 and October 2009 the Department stated in June 2009 that tax of ` nine lakh for the year 2005-06 has been levied. The report on recovery and reply for the other year has not been received (October 2010).

2.14 Irregular exemption

Two Commercial Tax Offices²³

Under section 6(2) of the CST Act, inter state sale or purchase of goods affected by transfer of document of title to the goods during their movement from one state to another against form E-1/C, is exempted from payment of tax. The exemption is not admissible if there exists any purchase order prior to date of transfer of title of goods.

We observed for the period 2005-06 and 2006-07, that in two cases assessed between September 2008 and March 2009 the AAs allowed exemption from tax on sale of

goods worth ` 13 crore against form E-1/C, although the purchase orders were issued by the purchasers prior to transfer of title of goods as evident from details available in Form-C. As the purchase orders were issued prior to transfer of title of the goods, grant of exemption from tax of ` 1.30 crore was not in order.

We reported the matter to the Department and the Government in June 2009; their reply has not been received (October 2010).

²² CTT vs. Decent Industries STI 2005 All. H.C. 205:2005 NTN (Vol. 26) 202 All. H.C.

²³ DC (A)-2, CT, Allahabad and DC (A)-2, CT, Lucknow.

2.15 Short levy of tax due to calculation mistake

Three Commercial Tax Offices

We observed that in case of three dealers who were assessed between December 2004 and March 2009 for the years 2002-03 and 2006-07, mistakes were committed in calculation of tax which resulted in short levy of tax amounting to ` 37.28 lakh as mentioned below:

(` in lakh)						
Sl.No.	Name of the Unit	Assessment year (month & year of assessment)	Taxable turnover	Tax leviable	Tax levied	Tax short levied
1.	AC-6 CT Allahabad	2002-03 (December 2004)	1,047.99	32.96	30.64	2.32
2.	DC-9 CT Bareilly	2006-07 (March 2009)	753.09	37.65	3.77	33.88
3.	DC-20 CT Kanpur	2002-03 (March 2009)	12.00	1.20	0.12	1.08
Total			1,813.08			37.28

We reported the matter to the Department and the Government between January 2006 and February 2010; their replies have not been received (October 2010).

2.16 Non-observance of the terms and conditions of the Government notification and departmental orders

Two Commercial Tax Offices

Under the provisions of section 15 (C) of the Central Sales Tax Act read with the Commissioner's circular dated 29 March 2007, tax is levied on purchase of paddy inside the State. If the rice is produced out of such paddy, the purchase tax is deducted from the tax levied on sale of rice only in case of intra-State sale and if it is sold in the course of inter-State trade/commerce, such adjustment is not permissible.

We observed between February 2009 and May 2009 that two dealers purchased paddy from within the State and manufactured rice from it during the years 2003-04 to 2006-07. The

dealers made inter-State sale of rice manufactured from paddy on which purchase tax of ` 9.07 lakh was paid by the dealers. The AAs while finalising the assessments between October 2005 and September 2008 allowed the benefit of purchase tax of ` 9.07 lakh, which was irregular. This resulted in non-realisation of revenue of ` 9.07 lakh. The details are shown as below:

(₹ in lakh)

Sl. No.	Name of Unit	No. of dealers	Year of assessment (month & year of assessment)	Total CST sale	Tax levied	Irregular exemption of purchase tax
1.	DC (A), CT, Kosikalan, Mathura	1	2003-04 (August 2008)	107.56	4.30	2.38
			2005-06 (August 2008)	196.39	7.86	3.37
			2006-07 (September 2008)	86.95	3.48	1.68
2.	DC (A) CT Hardoi	1	2003-04 (October 2005)	33.54	1.41	0.64
			2004-05 (August 2006)	50.74	2.03	1.00
Total				475.18	19.08	9.07

We reported the matter to the Department and the Government between April 2009 and August 2009; their replies have not been received (October 2010).

2.17 Irregular grant of exemption of tax

DC Sector-16 Agra involving two institutions of KVIC

Vide notification dated 07.10.2004 exemption of tax is granted on manufacture of electronic goods. Voltage stabilizers, UPS and Inverters fall under the category of electrical goods and not under the category of electronic goods.

We noticed (November 2009) that during 2006-07, two institutions sold self-manufactured electrical goods (UPS, Stabilizer and Inverter) amounting to ₹ one crore. The AAs while

finalising the assessment in October 2008 granted exemption of tax of ₹ 11 lakh, as these institutions were authorised for the manufacturing of only electronic goods, the grant of exemption of tax on electrical goods was irregular.

We reported the matter to the Department and the Government in December 2010, their replies have not been received (December 2010).

2.18 Exemption of tax on free bonus scheme

DC Sector-12 Lucknow

Vide notification dated 15 January 2000, medicines and pharmaceutical preparations are taxable at the rate of eight *per cent* with effect from 17 January 2000 to 31 December 2007, at the point of sale by manufacturer or importer.

We noticed (November 2009) that during 2004-05 and 2005-06 a dealer imported medicines worth ₹ 78.28 crore on the strength of 716 import declaration forms and out of that, medicines worth ₹ 2.91 crore, were given free of cost, as bonus. The AAs while finalising assessment between February 2007 and March 2008 granted exemption of tax of ₹ 23.31 lakh on it. As the imported item was liable to be sold, grant of exemption of tax on free distribution of the medicine resulted in loss of

revenue amounting to ₹ 23.31 lakh. In the absence of any provision on free distribution, the grant of exemption of tax was irregular.

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that the dealer has not charged any amount from the purchaser regarding the medicine, hence, tax is not leviable on the medicines given as free bonus. We do not agree as all the items imported against the import declaration forms are liable to be taxed and there is no such provision neither in UPTT Act nor in rule regarding grant of such exemption.

2.19 Grant of Exemption of Entry tax

JC(C) Ghaziabad and one office²⁴ of DC involving two dealers

Vide notification No. 3238 dated 01 November 2001, no tax shall be levied and collected from the cent *per cent* export oriented manufacturing dealers on entry of capital goods, plant, machinery, spare parts, raw materials and consumable goods into the local area from any place outside that local area. Further, by issue of a circular No. 645 dated 12 January 2005, it was clarified that such exemption of entry tax on fuel/diesel would not be admissible to cent *per cent* export oriented units.

We noticed between October 2009 and November 2009 that during 2003-04 to 2006-07, two dealers had imported diesel and petroleum based products, valued at ₹ 193.09 crore. The AAs while finalising the assessment between March 2006 and March 2009

granted exemption of entry tax of ₹ 9.65 crore. The details are given below:

(₹ in crore)

Sl. No.	Name of unit	Number of dealers	Name of commodity	Year	Value of commodity	Rate of tax leviable	Non-levy of tax
1.	DC Sec 19 Ghaziabad	1	Diesel	2003-04 & 2004-05	11.50	5	0.57
2.	DC Sector 19 Ghaziabad/ Joint Commissioner (Corporate) Ghaziabad	2	Diesel	2005-06 & 2006-07	4.32	5	0.22
Carbon Black Feed Stock			2006-07	177.27	5	8.86	
Total					193.09		9.65

After we pointed this out to the Department and the Government in October 2010, the Department stated in December 2010 that in both the cases, the matter is being examined and if any irregularity is found, necessary action would be taken according to the rules.

²⁴ DC-19 Ghaziabad.