

Chapter II
Tax on Sales, Trade etc.

EXECUTIVE SUMMARY – CHAPTER - II

Growth in tax collection	During 2012-13, the increase in tax collection was 18.86 <i>per cent</i> against 19.62 <i>per cent</i> during the previous year. Though the number of dealers shows a substantial increase every year, it was not reflected in VAT collection.
Internal Audit was weak	Internal Audit Wing (IAW) was able to audit only 56 units out of 356 units planned for audit during the year.
Effective follow up of audit observations	The Department accepted ₹ 6.56 crore in 675 cases pointed out by Audit and recovered ₹ 6.51 crore in 673 cases. Efforts made by the Department in realising 99 <i>per cent</i> of accepted cases are appreciable.
Results of audit	In 2012-13, records of 164 units relating to Kerala General Sales Tax (KGST) and Kerala Value Added Tax (KVAT) were test checked and 1,919 observations involving ₹ 237.91 crore were pointed out of which 65 cases involving ₹ 0.53 crore were accepted.
What is highlighted in this Chapter	Cases involving money value of ₹ 595.35 crore were pointed out in the Performance Audit on Assessment, levy and collection of Value Added Tax on transfer of goods involved in works/supply contract. 14 paragraphs involving money value of ₹ 25.14 crore are also presented.
Conclusion	The Department needs to improve the internal control system including strengthening of internal audit so that weaknesses in the system are addressed and omissions pointed out by Audit are prevented or detected and remedied in a timely manner.

CHAPTER-II: TAX ON SALES, TRADE ETC.

2.1 Tax administration

The Commercial Taxes Department contributed 74.85 *per cent* of the revenue of the State during 2012-13. The revenue is derived from the assessment and collection of different taxes like General Sales Tax (GST), Value Added Tax (VAT) and Central Sales Tax (CST) which are regulated by the Kerala General Sales Tax Act (KGST), 1963, The Kerala Value Added Tax Act (KVAT), 2003, the Central Sales Tax Act (CST), 1956 and notifications issued by the Department from time to time. The Department is under the administrative control of the Secretary to Government, Taxes Department. The Commissioner of Commercial Taxes (CCT) administers the Acts and Rules. He is assisted by Joint Commissioners, Deputy Commissioners, Assistant Commissioners and Commercial Tax Officers. The assessment, levy and collection of tax is done by Assistant Commissioners and Commercial Tax Officers.

KGST is leviable on sale of Ganja and opium, foreign liquor and certain petroleum products. VAT is leviable on the intra state sale of remaining commodities and CST on interstate sales.

2.2 Trend of receipts

Budget Estimates (BEs) and actual receipts from tax on sales, trade etc. during the year 2008-09 to 2012-13 along with the total tax receipts during the same period is exhibited in the following table and graph.

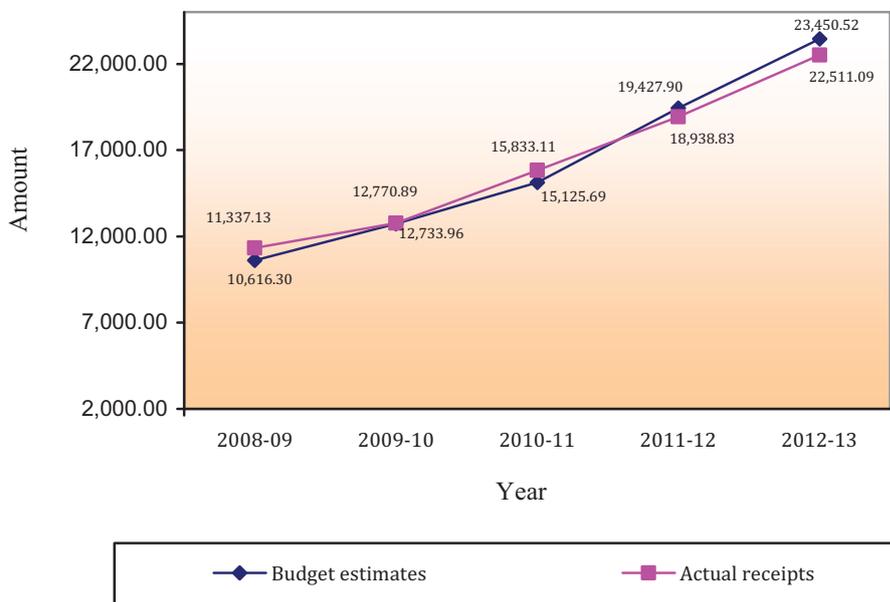
(₹ in crore)

Year	Budget estimates	Actual receipts	Variation	Percentage of variation	Total tax receipts of the State	Percentage of actual receipts to total tax receipts	Percentage of growth over previous year
2008-09	10,616.39	11,377.13	(+) 760.74	(+) 7.17	15,990.18	71.15	21.39
2009-10	12,733.94	12,770.89	(+) 36.95	(+) 0.29	17,625.02	72.46	12.25
2010-11	15,125.69	15,833.11	(+) 707.42	(+) 4.67	21,721.69	72.89	23.97
2011-12	19,427.90	18,938.83	(-) 489.07	(-) 2.52	25,718.60	73.64	19.62
2012-13	23,450.52	22,511.09	(-) 939.43	(-) 4.01	30,076.61	74.85	18.86

Source : Finance Accounts of relevant years

Budget estimates and actual receipts

(₹ in crore)



Audit noticed that the Department was able to achieve a growth rate of 18.86 *per cent* during 2012-13. The reason for variation between budget estimates and actual receipts, though called for (July 2013), was not furnished by the Department (February 2014).

2.3 Assessee profile

The number of dealers registered as at the end of 2010-11, 2011-12 and 2012-13 are shown below:

2010-11	1,69,298
2011-12	1,86,987
2012-13	1,98,836

Source : Kerala Value Added Tax Information System

Audit noticed an increase of 11,849 in the number of dealers during 2012-13 over the preceding year. As per the information furnished by CCT, the VAT collection from 50 top dealers in the State was ₹ 3,679.63 crore which is 30.23 *per cent* of the total VAT collection of ₹ 12,171.70 crore. Out of the total dealers 27,701 dealers constituting 13.93 *per cent* were paying tax at 0.5 *per cent* under the category of presumptive tax payers.

Tax collection from KGST during 2012-13 was ₹ 9,921.57 crore as per the Finance Accounts prepared by AG (A&E) Kerala. The tax payable by five¹ major dealers alone comes to ₹ 9,938.19 crore as per their returns, which requires reconciliation so as to rectify the differences, if any.

2.4 Receipt of VAT per assessee

The receipt of VAT/sales tax per assessee during 2012-13 was slightly higher when compared to that of 2011-12 as shown below :

Year	No. of assessees	Total collection (₹ in crore)	Receipt per assessee (₹ in lakh)
2011-12	1,86,987	18,558.12	9.92
2012-13	1,98,836	22,093.27	11.11

2.5 Arrears in sales tax assessments

The Department furnished the position of arrears of assessment under sales tax which is as shown below:

Opening balance	7,117
Addition during 2012-13 including remanded cases	5,272
Total	12,389
No. of assessments completed	5,347
Arrear cases – 3,794	
Current cases – 1,381	
Remanded cases – 172	
Closing balance	7,042

Department completed 5,347 assessments which was 43.12 *per cent* of arrears outstanding

Audit recommends the Government to give direction to assessing authorities to complete assessments in a time bound manner.

2.6 Cost of collection

The gross collection of revenue receipts under the head, tax on sales, trade etc., expenditure incurred on collection and the percentage of expenditure to gross collection during 2008-09 to 2012-13 along with the All India average percentage of expenditure on collection to gross collection for relevant years are mentioned below:

¹ Kerala State Beverages Corporation (₹ 5,376.33 crore), Indian Oil Corporation (₹ 2,104.42 crore), Bharat Petroleum Corporation (₹ 1,377.27 crore), Hindustan Petroleum (₹ 1,050.39 crore) and Reliance Industries (₹ 29.78 crore).

Year	Collection	Expenditure on collection of revenue	Percentage of expenditure to gross collection	All India average percentage over the preceding year
	(₹ in crore)			
2008-09	11,377.13	102.59	0.90	0.83
2009-10	12,770.89	126.01	0.99	0.88
2010-11	15,833.11	115.61	0.73	0.96
2011-12	18,938.83	166.55	0.88	0.75
2012-13	22,511.09	162.05	0.71	0.83

Source: Finance Accounts and Departmental figures.

Audit noticed that the expenditure on collection was lower than the All India average. The increase in revenue collection by 18.86 *per cent* and the corresponding decrease in expenditure on collection of revenue during the year is appreciated which is significant considering the increase in All India average for the year.

2.7 Analysis of collection

Tax revenue collected on tax on sales, trade etc., during the last three years as recorded in the books of the Accountant General (A&E) Kerala is given below:

Revenue head	(₹ in crore)			Increase in 2012-13 over 2011-12 (Percentage)
	2010-11	2011-12	2012-13	
Sales Tax	7,402.07	8,754.38	9,921.57	13.33
VAT	8,097.15	9,803.74	12,171.70	24.15
CST	310.42	292.66	320.88	9.64

The above table indicates that during 2012-13 collection of VAT increased by ₹ 2,367.96 crore and of sales tax increased by ₹ 1,167.19 crore.

2.8 Impact of audit

During the last four years, Audit pointed out non/short levy, underassessment/loss of revenue, incorrect exemption, application of incorrect rate of tax etc., with revenue implication of ₹ 3,631.66 crore in 12,324 paragraphs. Of these, the Department/Government accepted audit observations involving ₹ 796.16 crore and had since recovered ₹ 34.69 crore. The details are shown in the following table:

Year	(₹ in crore)					
	Paragraphs included in the IRs		Paragraphs accepted during the year		Recovery during the year	
	No.	Amount	No.	Amount	No.	Amount
2008-09	2,182	754.35	342	149.70	203	9.40
2009-10	4,451	1,122.54	657	558.60	588	5.02
2010-11	3,152	944.66	797	81.18	522	15.70
2011-12	2,539	810.11	537	6.68	430	4.57
Total	12,324	3,631.66	2,333	796.16	1,743	34.69

The recovery position as compared to the accepted cases during the last four years

was very low being only 4.36 per cent. The insignificant recovery of ₹ 34.69 crore against the money value of ₹ 796.16 crore relating to the accepted cases during the period 2008-09 to 2011-12 highlights the failure of the Department in recovering promptly the Government dues even in respect of cases accepted by them.

2.9 Working of internal audit wing

The internal audit wing (IAW) in the Commercial Taxes Department commenced functioning from 1 June 2009. The wing headed by the Deputy Commissioner is assisted by three Assistant Commissioners and five Commercial Tax Officers. During the year 2012-13, against the target of 356 units, 56 units were audited leaving 300 units in arrears. There were 146 IRs with 2,150 observations involving ₹ 50.10 crore outstanding. The Department has not prepared a separate internal audit manual.

Audit recommends that the IAW may be strengthened so that they could achieve the planned audit target. Besides, a mechanism needs to be installed for timely settlement of the audit observations raised by the IAW.

2.10 Results of audit

In 2012-13, Audit test checked the records of 164 units relating to KGST and KVAT. Audit detected underassessment of tax and other irregularities involving ₹ 833.26 crore in 1,920 cases which fall under the following categories :

(₹ in crore)			
Sl. No.	Categories	No. of cases	Amount
1	Assessment, levy and collection of VAT on transfer of goods involved in the execution of works/supply contract (A Performance Audit)	1	595.35
2	Turnover escaping assessment	841	86.02
3	Grant of irregular exemption	296	42.19
4	Application of incorrect rate of tax	131	25.03
5	Grant of excess input tax credit	216	9.50
6	Incorrect grant of concessional rate of tax	11	1.74
7	Non/short levy of Interest	9	0.38
8	Other lapses	415	73.05
Total		1,920	833.26

The Department accepted underassessment and other deficiencies of ₹ 6.56 crore in 675 cases, of which 65 cases involving ₹ 0.53 crore were pointed out in audit during the year 2012-13 and the rest in earlier years. An amount of ₹ 6.51 crore was realised in 673 cases of which 65 cases involving ₹ 0.53 crore were pointed out during the year 2012-13.

A draft paragraph was issued (June 2013) involving ₹ 5.04 lakh, in which the department had recovered the entire amount.

A Performance Audit on '**Assessment, levy and collection of VAT on transfer of goods involved in the execution of works/supply contract**' with financial impact of ₹ 595.35 crore and a few illustrative audit observations involving ₹ 25.09 crore are mentioned in the following paragraphs.

2.11 Performance Audit on ‘Assessment, levy and collection of VAT on transfer of goods involved in the execution of works/supply contract’

2.11.1 Highlights

- ❖ There was no separate sub head for classifying/crediting of VAT receipts received from works contractors.

(Paragraph 2.11.8)

- ❖ Form 10 C showing the details of works contracts awarded was not furnished to the CTD by the Public sector undertakings /Government Departments and by private sector.

(Paragraph 2.11.10)

- ❖ No survey was conducted in the five districts for identifying unregistered works contractors. Audit cross verified the details collected from other departments with KVATIS and found that 484 contractors were not registered under the KVAT Act.

(Paragraph 2.11.11)

- ❖ A difference of ₹ 630.21 crore was noticed between the contract amounts awarded to the subcontractors and that depicted by them in their returns. The tax effect involved in these cases amounted to ₹ 124.51 crore.

(Paragraph 2.11.12.2)

- ❖ Audit noticed that in three cases, the developers accepted the advance payment from the prospective buyers without paying VAT of ₹ 63.03 crore.

(Paragraph 2.11.13.2)

- ❖ Application of incorrect rate of tax resulted in short levy of tax of ₹ 7.26 crore in two cases.

(Paragraph 2.11.19)

- ❖ Audit observed that contractors were allowed to pay tax at a compounded rate of three *per cent* in contravention of the provisions of the Act.

(Paragraph 2.11.20.2)

2.11.2 Introduction

Tax on Works Contract was governed by Kerala General Sales Tax Act 1963 (KGST) upto 31 March 2005. Thereafter the levy, assessment and collection of tax on works contract is governed by Kerala Value Added Tax (KVAT) Act 2003 and the Kerala VAT Rules (Rules) made thereunder. The inter state purchases relating to Works Contract is governed by Central Sales Tax Act (CST) 1956. Section 2(iv) of the KVAT Act stipulates that Works contract (WC) includes any agreement for carrying out for cash or for deferred payment or other valuable consideration the construction, fitting out, improvement, repair, manufacture, processing, fabrication, erection, installation, modification or commissioning of any movable or immovable property. Government is empowered to issue notifications and Department can issue circulars for the administration of the KVAT Act and Rules. Works contract tax (WCT) is accounted alongwith commercial taxes under major head 0040. Assessment of works contracts is done under Section 6 of the Act. The works contractor can opt for compounding scheme under Section 8 of the Act. In the case of works awarded, tax shall be deducted from the payments made to the contractor by the awardee. In the case of compounding, if the option is accepted, tax due will be calculated by the assessee and remitted monthly. Important terminology/ provisions governing taxation of works contractors under KVAT Act is as explained in the Annexure II.

Reasons for selection of topic for the performance audit

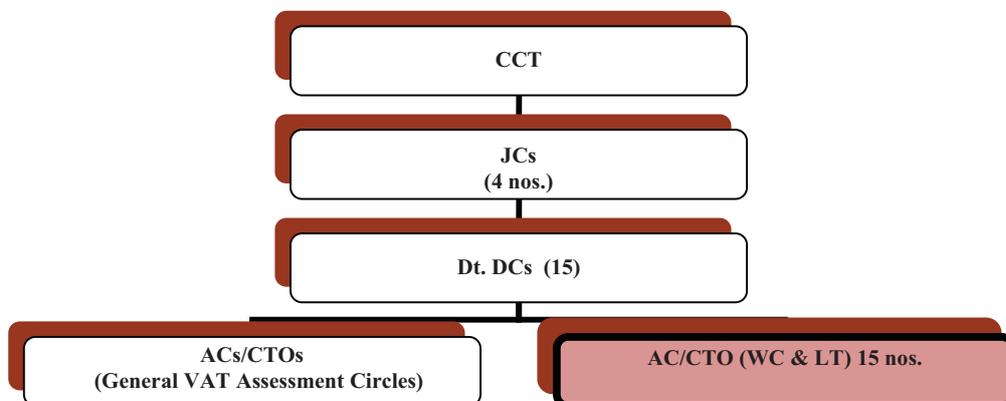
During the local inspections it was found that returns filed by the works contract assesseees were error prone and the Department was not paying enough attention to scrutinise the returns. Compliance deficiencies in the works contract were persisting and reported in previous Audit Reports as mentioned in Annexure III. Hence, it was felt appropriate to audit this area considering the inherent risk and control risk. The observations of Audit are discussed in the succeeding paragraphs.

2.11.3 Organisational setup

The Department of Commercial Taxes is administered at Government level by the Secretary to Government and the Commissioner of Commercial Taxes (CCT) is the head of the Department. There are four Joint Commissioners (JC), namely, JC –I, JC (General), JC(Law) and JC(Audit and Inspection) to assist the CCT. The district level administration of the offices is carried through 15 Deputy Commissioners (DC) in 15 tax districts. DC in each district is the administrative head of the offices in that district. Assessment, levy and collection are done by Assistant Commissioners and Commercial Tax Officers respectively in special circles and ordinary circles. Assessment, levy and collection of tax in respect of works contractors are done in two sets of establishments viz.

- Exclusive works contract circles - 15 numbers. These are attached to the offices of the Deputy Commissioners in 15 tax districts.
- Regular VAT assessment circles along with VAT – 132 numbers.

ORGANOGRAM



2.11.4 Main objectives for Audit

The Performance Audit (PA) was conducted to ascertain whether:

- ❖ the provisions of the KVAT Act and the KVAT Rules governing the registration, assessment, levy and collection of tax from works contractors are adequate and effective;
- ❖ a data bank containing the construction work going on in the state is maintained by the Department and the information is utilised in registration of the dealers and for other purposes;
- ❖ a system exists in the Department to ensure that the turnovers reflected in the returns filed by the dealers agree with the value of the contracts awarded by the major awarders² and also includes the amount of inter-state purchases made for execution of contracts;
- ❖ Internal Audit wing exists and effectively checks timely assessments, levy and collection of revenue to prevent the leakage of revenue.
- ❖ corrective measures are taken to rectify the defects pointed out by statutory audit and Internal Audit wing;

2.11.5 Audit Criteria

The criteria for the PA were derived from the provisions and rules of central and state laws mentioned below and the notifications/orders issued by the Government from time to time thereunder.

² Awarders:- Include Government departments/local authorities/public sector undertakings such as Public Works Department, Local Bodies, Kerala Water Authority, Kerala State Electricity Board, Oil Companies, Cochin Shipyard, Cochin Port Trust, various power projects etc.

State Laws

- The Kerala Value Added Tax Act 2003
- The Kerala Value Added Tax Rules 2005.

Central Laws

- The Central Sales Tax Act 1956
- The Central Sales Tax (R&T) Rules 1957

In addition to above, various decisions promulgated by various courts have also been taken into account while conducting the audit.

2.11.6 Scope and methodology of Audit

Audit conducted the PA as per an approved study design matrix during the period from January to June 2013 covering the period from 2007-08 to 2011-12. Based on VAT collection 14 districts were stratified into 12 strata and six districts³ were selected by stratified random sampling. Subsequently, Thrissur district was included in place of Idukki as suggested by the CCT, Thiruvananthapuram at the entry meeting on the reason that contract works are more in Thrissur district compared to Idukki district. The primary data collected from the Office of the CCT and assessment circles in six selected districts⁴ were cross checked with the secondary data collected from the Directorate of Industries and Commerce, Kerala Water Authority (KWA), Kerala Public Works Department (KPWD), Vikram Sarabhai Space Centre (VSSC), Directorate of Radiation Safety and various Public Sector Undertakings.

Audit conducted an entry conference on 08 March 2013 with the Secretary to Government (Taxes) and the CCT, wherein the scope and methodology of audit were discussed. The draft note was sent (July 2013) to the Department/Government and the Audit findings and recommendation were discussed with the Secretary to Government (Taxes) and the CCT in the exit conference held on 26 September 2013. The deficiencies pointed out in PA were accepted by the Department/Government in the exit conference. The Secretary to Government (Taxes) appreciated the findings of the PA and opined that the report and the recommendations are eye opener to the Department and that the implementation of the same would boost revenue collection from works contract. The response of Department/Government was considered while finalising the PA.

2.11.7 Acknowledgement

Audit acknowledges the co-operation extended by the Commercial Taxes Department, Department of Industries and Commerce, Department of Ports, Directorate of Radiation Safety, Airport Authority of India, KPWD, VSSC and

³ Ernakulam, Idukki, Kottayam, Kozhikode, Palakkad and Thiruvananthapuram.

⁴ Ernakulam, Kottayam, Kozhikode, Palakkad, Thiruvananthapuram and Thrissur.

KWA for providing necessary information and the inputs required for the preparation of the Report.

System deficiencies

2.11.8 Revenue collection for Works Contracts

KVAT is credited in 0040 tax on sales, trade etc. However there was no separate sub head for classifying credit of VAT received under Works Contract. In the absence of sub head the actual collection of Works Contract Tax could not be assessed/analysed *viz-a-viz* the actual receipts of VAT collection.

There are 15 circles responsible for assessment and collection of works contract tax. The year wise position of works contract receipts as furnished by Department was as under:

Year	WC Tax	Total VAT collection	Rate of increase in WCT	Rate of increase in VAT
	(₹ in crore)		(in percentage)	
2007-08	284.00	5,014.80	-	-
2008-09	397.36	5,881.97	15.93	17.29
2009-10	420.17	7,235.26	24.26	23.01
2010-11	473.82	8,097.15	11.86	11.91
2011-12	522.78	9,803.74	25.04	21.08

Source : Finance Accounts and figures of Commercial Taxes Department

Audit however noticed that apart from the above 15 circles, collection of tax from works contracts is also being done by regular assessment circles. Several dealers engaged in execution of works contract were registered and assessed at regular VAT assessment circles. Larsen & Toubro Ltd, Kone Elevator Ltd, Otis Elevator Ltd, Kirloskar Brothers Ltd, Blue Star Ltd, Voltas Ltd etc., are some examples. The receipts from such assesseees were not reckoned as works contract receipts. Instead, receipts from works contract circles alone were being shown as tax collected from works contractors. Thus, the total revenue realised from works contract could not be ascertained.

In the exit conference, the Secretary to Government (Taxes), informed that the feasibility of opening a separate head of account for works contract will be looked into.

Audit recommends that the Department may initiate action to introduce a new subhead under the major head 0040 Tax on sales, trade etc., for identification of the works contract tax.

2.11.9 Absence of a separate TIN number to identify works contract assessees

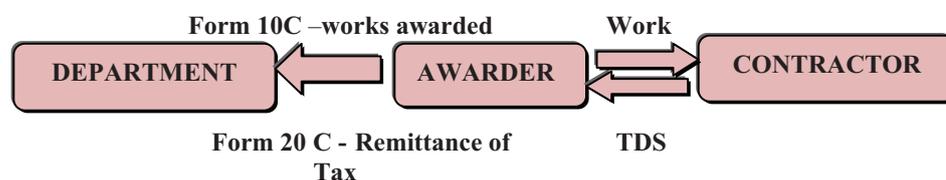
All VAT dealers including works contract dealers are given an eleven digit Tax Identification Number (TIN) on registration. However, the works contractors cannot be identified from other dealers in the roll of Commercial Taxes Department (CTD). Only way to identify the works contractor is to allot a separate identification number for works contractors apart from the general TIN or the general TIN may be prefixed/suffixed with a code.

The general TIN may be prefixed or suffixed so as to identify the works contractors from other dealers.

2.11.10 Failure in identification of works contractors due to non submission of declarations in Form 10C

• **Public Sector Undertakings/Government Departments**

Rule 32 of the KVAT Act stipulates that every awardee,⁵ including a Department of the State or Central Government, shall forward a return to the assessing authority showing the details of works contract awarded during every quarter, in Form No.10C, so as to reach the assessing authority on or before the 10th day following the quarter ending 30 June, 30 September, 31 December and 31 March every year. Filing of return in Form 10C is a key control instituted in the statute to enable the Department to ascertain the information regarding the construction activities in the State.



Audit found that KPWD was awarding contract to private contractors but did not file the Form 10C to CTD. Same was the case with Kerala State Transport Project (KSTP), Kerala Water Authority (KWA), Kerala State Electricity Board (KSEB) and Bharat Petroleum Corporation Limited (BPCL). As such Audit could not ascertain whether all the contractors have been brought under the tax net.

In the exit meeting (September 2013), the Secretary (Taxes) accepted the views of Audit and stated that filing of return in Form 10C will be ensured in future.

• **Private sector in State**

Audit noticed that the contract works in the State were also being executed by the private sector. They are also not filing returns in Form 10C. CTD was not maintaining any record of these contractors and as such CTD was unaware of the

⁵ As per Section 2 (vii) of the Act, awardee means any person who awards any works contract to a contractor for execution.

quantum of turnover relating to such works being executed by contractors in the state.

Audit recommends that the Department should develop a system to monitor quarterly/annually, the receipt of declaration in Form 10C filed by awarders both in respect of Government and private awarders.

2.11.11 Absence of a system to detect unregistered works contractors

Section 15A of the KVAT Act 2003, stipulates that where a dealer liable to be registered under this Act has failed to inform the registering authority of his liability to be registered, the registering authority, after conducting such survey, inspection or enquiry, as may be prescribed, proceed to register such person as a dealer. Survey is an important tool to detect unregistered contractors and to widen the tax base. The Department⁶ also has emphasized the importance of conducting survey. Under Section 67(1)(a) of the Act, registering authority may direct that if a person required to register himself as a dealer under the Act, did not get himself registered, he shall be liable to pay by way of penalty, an amount not exceeding twice the amount of tax or other amount evaded or sought to be evaded where it is practicable to quantify the evasion or an amount not exceeding ten thousand rupees in any other case.

- **Failure to conduct street survey**

Audit noticed that no survey for identifying/registering of works contractors was conducted in five⁷ of the six test checked districts during the period from 2007-08 to 2011-12.

Audit collected information of contractors from three⁸ other departments and cross verified the data with the Kerala Value Added Tax Information System (KVATIS). Out of 496 contractors checked, it was observed that only 12 contractors were registered with KVAT Act and 484 contractors were not registered (Annexure IV).

Due to the failure of the Department to conduct adequate survey, the unregistered contractors remained outside the tax net. The extent of tax evaded in this regard could not be quantified in the absence of data. However, the penalty under Section 67(1)(a) of ₹ 48 lakh could have been levied which was also not done.

- **Failure to use data available in the Department for registration of contractors**

Under Section 10 of the Act, every awarder has to deduct tax at source (TDS) and remit to the Department (Rule 42). The awarder while remitting tax shall file a return alongwith a statement in Form 20C. Form 20C contains the details like name of contractors, amount of contract, payments of tax deducted at source etc.

⁶ Circular No.34/2005 dated 12.12.2005 and Circular No.43/2007 dated 19.10.2007.

⁷ Ernakulam, Kottayam, Palakkad, Thiruvananthapuram and Thrissur.

⁸ District Industries Centre, Department of Ports, Department of Tourism.

Audit cross verified the details of tax deduction statement in Form 20C available in the assessment circles /data collected from VSSC with KVATIS in the six districts selected in PA and found that 352 unregistered contractors were executing works contracts valued at ₹ 634.35 crore in 945 cases. Eventhough data was available with the Department itself, it made no efforts to register the dealers. Once the dealers were identified, the data should have been handed over to the intelligence wing for confirmation of facts and registration done accordingly.

During discussion in the exit conference (September 2013), the Secretary to Government (Taxes) informed that a mechanism is being brainstormed to bring the works contractors into the tax net and he assured that all efforts would be taken to gather information from local bodies/implementing agencies for identifying unregistered works contractors.

Audit recommends that

- ***A streamlined system may be evolved by the Department to identify/detect the unregistered works contractors and bring them to the tax net.***
- ***There should be a system for collecting the details of contracts awarded by Government agencies/Departments so as to make the cross verification effective.***

Audit recommends that the Department should insist on filing of Form10C by the awarders and ensure that it was cross checked with the returns filed by the contractors to avoid the suppression of turnover by the assessees.

2.11.12 Internal control mechanism

Internal controls are intended to provide reasonable assurance on proper enforcement of laws, rules, departmental instructions etc., and to pinpoint lapses in the implementation of systems and products with a view to prevent frauds and other irregularities. Internal controls also help in creation of reliable financial and managerial information system for adequate safeguards against evasion of revenue.

2.11.12.1 Lack of control in exempting TDS

The Rule provides that the contractors to whom 20E certificate is to be issued by the assessing authority should be regular tax payers and the final payment to them shall not be made unless contractor produces liability certificate issued by the assessing authority. Liability certificate is the certificate issued by assessing authority showing the dues outstanding against the contractor as on date which should be deducted from payments made to the contractor.

Audit scrutiny of the records in CTO (WC<), Ernakulam revealed that demands ranging from ₹ 1.16 lakh to ₹ 6.71 crore raised against nine contractors to whom Form 20E certificates were issued, are pending for collection. This indicates that final payment was made to the contractors without adjusting the tax

pending against the contractors. One of the cases is discussed here to highlight the nature of deficiency. M/s BPCL, Kochi was the awarder of the contractor, M/s BOC India, a Calcutta based company for executing works contract. The assessing authority issued certificates in Form 20E based on which M/s BOC India received payments amounting to ₹ 25.02 crore without having the value added tax deducted at source during the period upto August 2010. On receiving the major portion of the contract amount, M/s BOC India left the state entrusting the remaining portion of the work with a sub-contractor. Since, the contractor did not pay the VAT, the assessing officer completed (December 2012) their VAT assessment under Section 25 of the KVAT Act and raised (January 2013) a demand of ₹ 3.60 crore. Since the demand was not cleared, the assessing authority issued requisition for revenue recovery to the revenue authorities of West Bengal. The dues could not be realised till date of audit (June 2013).

This could have been avoided if the certificate in Form 20E was not issued by the assessing authority to M/s BOC India as it was not a regular tax payer of the state government. Also, the final payment should have been made by the awarder, M/s BPCL only after ascertaining the balance dues from the contractor as per the liability certificate issued by the assessing authority.

Department/Government may examine the case in detail to see under what circumstances the exemption was allowed to the contractor.

2.11.12.2 Suppression of turnover due to lack of control in sub contracted works

Explanation 1 to section 8(a) of KVAT Act, provides for excluding the amount paid to a registered sub contractor. For this, the contractor has to furnish a certificate in Form 20H issued by such sub contractor. The Form 20H submitted by the sub contractor indicates only the gross amount of the contract but does not indicate the actual amount of payment made to the sub contractor. The Empowered Committee of State Finance Ministers (ECSFM) came out with a unanimously approved white paper on VAT which *inter-alia* emphasized the need for cross verification of data between various implementing and taxation authorities so as to check tax evasion and to ensure growth of revenue.

Audit cross verified the data collected from awarders such as KWA, VSSC, KPWD, Airport authority of India and Kerala Sustainable Urban Development Project with the assessment records of contractors and found that in nine⁹ assessment offices the contractors had further subcontracted part of the work. There was variation between the amount of contract allotted by the contractors and the returns filed by the sub-contractors. As per Form 20H submitted by 21

⁹ Works contract offices Ernakulam, Idukki (selected for sampling at the initial stage, later on the request of CCT, another district Thrissur was taken in its place. Since information was already collected same was included), Kozhikode, Mattancherry, Palakkad, Thiruvananthapuram and Special Circle II, Ernakulam, Special Circle, Thiruvananthapuram, Second Circle, Thiruvananthapuram

assesseees to the awarders, the total amount of contract allotted to sub contractors was ₹ 1,049.58 crore. However, the subcontractors in their returns submitted to the CTD had depicted the amount as ₹ 419.37 crore. Thus, there was a difference of ₹ 630.21 crore which needs investigation. A few instances are given below:

(₹ in crore)

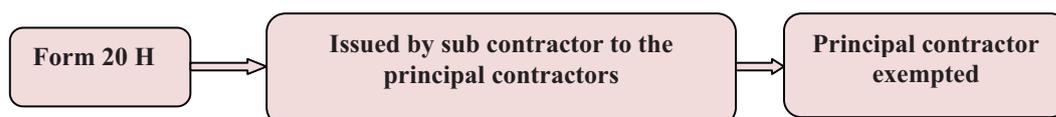
Sl. No.	Name of the Office	Name of the awarder/ name of the assessee	Amount for which the principal contractor availed exemption based on Form 20H	Amount shown in the returns filed by the sub-contractor/ year	Difference in the amount received/ reported
1.	CTO, WC, Ernakulam	IHI Corporation/ M/s Vijaya Tanks & Vessels	72.58	64.60 (2009-10)	7.98
2.	CTO, WC, Ernakulam	M/s Shapoorji Pallanji/ M/s Siemens Building Technology	10.49	0.04 (2009-10)	10.45
3.	CTO, WC, Palakkad	M/s Shapoorji Pallanji/ M/s Hooma Interrial Decoration	14.16	0.00 (2009-10 to 2011-12)	14.16
4.	CTO, WC, Kozhikode	M/s Shapoorji Pallanji/ M/s NJ Constructions	1.13	0.00 (2009-10 to 2011-12)	1.13
5.	CTO, Spl. Circle II, Ernakulam	JBIC, KWA/ M/s Kirloskar Brothers Ltd	111.14	13.00 (2008-09 to 2011-12)	98.14

The reasons for the difference though called for were not furnished by the Department. The tax effect involved in these transactions amounted to ₹ 124.51 crore including interest and penalty as shown in Annexure V.

Audit recommends that the Department should develop a fool proof system to ensure the actual amount of payment made to subcontractors.

2.11.12.3 Deduction of sub contracted work from taxable turnover without Form 20H

Exclusion of subcontracted work from taxable turnover is a high risk area in the assessment of works contract tax under Section 6. The same risks are prevailing in the assessment under compounding (Section 8) due to the deficiencies in Form 20H. In addition, Audit found cases where subcontracted work was excluded without Form 20H.

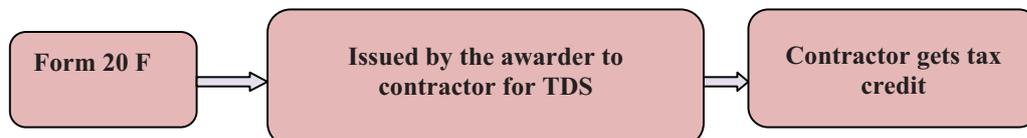


Audit scrutinised 58 assessment files of works contractors who opted for payment of tax under Section 8(a)(i) of KVAT Act and observed that out of the above, 19 assesseees in four¹⁰ assessment circles, availed deduction of a portion of their turnover as amount paid to the sub contractors for that part of works executed through them. But the assesseees did not furnish the certificate in Form 20H required in support of their claims. The assessing authority did not disallow the claim for deduction in the absence of required certificate. This resulted in short levy of tax of ₹ 10.27 crore including interest and penalty as shown in Annexure VI.

During discussion in the exit conference, the Secretary to Government (Taxes), accepted the recommendation insisting the production of valid documents/declaration in support of each claim.

2.11.12.4 Tax credit availed without furnishing details of TDS in Form 20F

As per Section 10 of KVAT Act 2003, every awarder shall deduct from each payment made by him to any works contractor, the tax payable by the contractor in respect of works contract awarded. Rule 42(4) and 42(8) of KVAT Rules 2005 provide that where an awarder deducts tax from the payment due to the contractor, he shall issue a certificate to such contractor in Form 20F and the contractor can adjust the amount deducted by the awarder against his tax dues. If an assessee adjusts the TDS against his tax dues, he shall furnish the copies of Form 20F certificate issued by the awarder.



Audit scrutinised 62 assessment files of works contractors and observed that four assesseees in two¹¹ assessment circles adjusted from their tax dues certain amount as TDS without furnishing the certificate in Form 20F required in support of their claim. In the absence of Form 20F, the correctness of TDS claimed by the contractors is not verifiable. The assessing authority should have taken note and disallowed the claim. However, the claim was allowed without required certificate. This resulted in short levy of tax of ₹ 35.87 crore including interest and penalty as shown in Annexure VII.

Assessing officers should ensure that concessions/exemptions are allowed against valid certificates required as per Act/Rules.

¹⁰ Works Contract offices, Ernakulam, Kottayam, Kozhikode and Thiruvananthapuram.

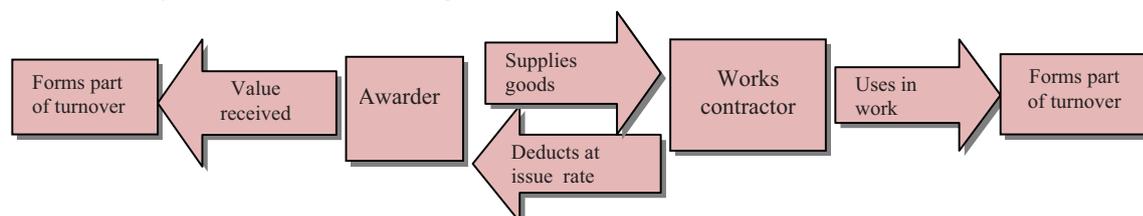
¹¹ Works Contract offices Ernakulam and Thiruvananthapuram.

2.11.13 Turnover escaped assessment

2.11.13.1 Materials supplied to contractor by the awarder

Rule 9 (2A) of the KVAT Rules provides that, if an awarder supplies a portion of the goods involved in the execution of the works contract and deducts the value of such materials from the payment made to the contractor, the turnover of the goods so supplied shall form part of the total turnover of the awarder as well as the contractor. Thus value of goods is liable to tax on two accounts;

- (a) By the works contractor - under works contract tax
- (b) By the awarder – under general VAT assessment



Audit noticed that two assesses who were awarders of various works contracts, supplied materials to the contractors for use in works contract. The value of material so supplied was exigible to tax.

Audit obtained information from BPCL regarding the supply of Bitumen upliftments by KPWD during the last five years and found that bitumen value at ₹ 1,238.75 crore was supplied to KPWD which in turn supplied to various contractors. As per Section 20(1), KPWD was required to file a return before the commercial taxes department. However, Audit noticed that Public works department had not filed returns during the above period. In the absence of returns, it is not ascertainable whether tax due was paid by them. VAT chain has broken at this stage. The KPWD was required to file Form 10C which was not done.

The KSEB has in its accounts shown that material valued at ₹ 113.12 crore was supplied to contractors against work orders awarded by them. No centralised returns were being submitted by the KSEB. The returns submitted by the various branches were also not produced before Audit. Audit could therefore not ascertain whether the tax was paid correctly.

The tax effect involved in above cases at the rate of 12.5 per cent works out to ₹ 210.59 crore $\{(\text{₹ } 1,238.75 \text{ crore} + \text{₹ } 113.12 \text{ crore}) \times 12.5 \text{ per cent}\}$.

It is therefore recommended that Government may issue instructions to the KPWD for filing the VAT returns and also a consolidated VAT return by the KSEB.

2.11.13.2 Escape of contract receipts of developers

The construction of apartments after accepting advance from prospective buyers on a prior agreement will come under the purview of works contract under

Section 2(iv)¹² of the KVAT Act. This has been established by the decision¹³ of Supreme Court of India and subsequently clarified¹⁴ by the CCT. Since most of the developers/builders undertake to build/develop any immovable property after accepting advance payment, they will come under the purview of the Act.

Audit found that in three cases, the developers accepted advance payments from the prospective buyers after entering into agreement with them. Though the transactions were eligible to be taxed under Section 6(1)(f) of KVAT Act, these developers were not assessed to tax as works contractors. The assessing authority also did not assess to tax the receipts of the developers under the Act. This resulted in short levy of tax, interest and penalty of ₹ 63.03 crore as shown below:

Sl. No.	Office to which related	Name of the assessee	Year	Turnover escaped assessment	Short levy of tax, interest and penalty
				(₹ in crore)	
1	CTO, WC, Kozhikode	M/s Queens Habitat	2011-12	7.58	2.25
2	CTO, WC Ernakulam	M/s DLF Home Developers (P) Ltd	2007-08 to 2011-12	194.48 ¹⁵	60.32
3	CTO, WC, Palakkad	Shri Jayaram CS , Sai Property Developers	2009-10	11.70	0.46
Total					63.03

Since this is a major area for tax collection, Audit recommends that the investigation wing should be vigilant to locate such cases.

2.11.13.3 Permission granted incorrectly to compound the contract receipts by builders/developers

Rule 11(1A) of Kerala Value Added Tax Rules, 2005 stipulates that every dealer in works contract shall file copies of the Agreements executed for construction along with application for compounding. Further, every contractor shall file a declaration in form No 49, containing the details of ongoing projects along with the returns.

Audit scrutinised 567 assessment records in respect of 205 builders for the period from 2008-09 to 2011-12 and observed that the assesseees were allowed to compound their contract receipts amounting to ₹ 3,481.22 crore either without

¹² Works contract includes agreement for carrying out construction etc.

¹³ K. Raheja Development Corporation Vs State of Karnataka, (141 STC 298(SC)2005)

¹⁴ Circular No.3/2010 dated 5.3.2010

¹⁵ Escape of turnover was worked out at the base rate of ₹ 3,500 per square meter for an area of 5,55,650 square meter

production of contract agreements or with the contract agreements which were not valid¹⁶ for the reason that they were executed in stamp paper worth ₹ 50/ ₹ 100.

In the absence of copies of valid agreements and declarations stipulated, the assessing officer should not have granted permission for compounding. Instead the total turnover should have been assessed under Section 6(1)(f), after allowing permissible deductions and input tax credit, which would have fetched additional revenue of ₹ 611.73 crore.

During discussion in the exit conference, the Secretary to Government (Taxes), accepted the recommendation on insisting of production of valid documents/ declaration in support of each claim.

Department should direct the assessing officers to see whether compounding is allowed based on proper application for compounding along with documents required as per provisions of Act/Rules.

2.11.14 Internal Audit

The internal audit wing commenced functioning from 1 June 2009. The details of units audited by the internal audit wing during the year 2009-10 to 2011-12 is as follows:

Year	No. of units to be audited	No. of units audited	Percentage of coverage	No. of cases detected	Amount of objection	Amount realised
					(₹ in lakh)	
2009-10	356	12	3.37	417	452.04	Not available
2010-11	356	46	12.92	919	330.53	
2011-12	356	32	8.99	445	2,738.20	

(Source: Data from Commercial Taxes Department)

Audit observed that the coverage of units audited was very low and the details of amount realised were not made available. As such the effectiveness of the internal audit wing could not be ascertained.

Compliance deficiencies

2.11.15 Sales treated as works contract to reduce tax liability

Adopting wrong classification to reduce tax liability is a major risk area in self assessment. Audit found instances where the assessing officer had accepted this wrong classification. Treating sales as works contract is one such example. Under explanation below the table under Rule 10(2)(b), no deduction in respect of labour shall be allowed out of the total contract amount for the supply and installation of any machinery equipment or any other system, where the goods involved are

¹⁶ Under the Kerala Stamp Act 1959 as amended vide Finance Act 2007, development agreements are to be stamped at the rate applicable to conveyance deeds.

transferred in the ‘knocked down’ condition (unassembled form) and assembled and installed, and the skill and labour employed for installation is only incidental to the supply of such goods.

The supply and installation of commodities like lift/elevator, air conditioner, surveillance camera, bus body etc., were classifiable as sales¹⁷ but not works contract. Thus these items are taxable under the provisions of VAT Act and exemption cannot be given for labour and other charges.

Audit scrutinised the records of 21 contractors who undertake supply and installation of lift, air conditioners and construction of body on chassis of vehicles, and observed from their returns that in respect of 12 cases in six¹⁸ assessment circles, the above works were treated as works contract claiming exemption towards labour and other charges under Rule 10. Short levy of tax in this regard worked out to ₹ 35.62 crore including interest and penalty as shown in Annexure VIII.

During exit meeting (September 2013), the Secretary (Taxes) accepted the Audit observation and assured that action would be taken in the above cases.

2.11.16 Incorrect exemption from payment of tax on sales to Special Economic Zone



Declaration in Form 43 for exemption

Section 6(7)(b) of KVAT Act provides that, works contract to any unit situated in the Special Economic Zone (SEZ) in the State is exempted from tax subject to the production of declaration in Form 43 issued by the unit. The CCT has also clarified¹⁹ that the exemption is for contractor only and sub contractors who execute work for a contractor in SEZ are not eligible for exemption under this Section. Audit checked assessment records in respect of fourteen assessees in four²⁰ assessment circles, who executed work in SEZ and observed that in six cases, exemptions amounting to ₹ 67.55 crore were allowed without production of declaration in Form 43. In the absence of Form 43, there is no mechanism to ensure that the work has been executed for SEZ units. Further, Audit observed that in one case,²¹ a sub contractor who executed work for a contractor in SEZ was incorrectly granted exemption from payment of tax. Short levy of tax

¹⁷ M/s Kone Elevators (India) Ltd. Vs State of AP (2005) 140 STC 22 and M/s Mckenzie's Ltd. Vs State of Maharashtra (SC) – Supply and installation of lifts and elevators, construction of body on chassis of vehicles are sales, not works contract.

¹⁸ Works Contract Offices Ernakulam, Mattancherry, Thrissur, Special Circle I Ernakulam, Special Circle II Ernakulam, Third Circle, Thrissur.

¹⁹ Order No C3.48469/08/CT dated 08.01.2009

²⁰ Works Contract Offices, Ernakulam, Thrissur, Special Circle I, Ernakulam Special Circle II, Ernakulam

²¹ Works Contract Office, Ernakulam

including interest and penalty amounted to ₹ 14.12 crore. Short levy in these cases amounted to ₹ 81.67 crore (Annexure IX).

A foolproof mechanism should be instituted to ensure that the provisions of the Act/Rules are observed scrupulously while accepting claim for concessions/exemptions admissible in the case of sales to units in SEZ.

2.11.17 Deduction of labour and other charges from turnover which are not ascertainable from the accounts

Under Rule 10(2)(a) of KVAT Rules, the taxable turnover can be determined by allowing the deductions viz., labour charges, charges for planning and designing, charges for machinery and tools used, cost of consumables, establishment and overhead charges and profit earned etc., if they are ascertainable from accounts. Under Rule 10(2) (b), where the actual turnover in relation to a works contract, in which the transfer of goods takes place not in the form of goods but in some other form, is not ascertainable from the books of accounts of the dealer or where the dealer has not maintained any accounts, the total turnover in respect of such works contract shall be computed after deducting labour and other charges from the total amount of contract at the rates prescribed in the Rule.

Audit noticed that, in the case of 16 assesseees in four²² assessment circles, the deduction allowed was more than the permissible limits though the details of labour and other charges are not ascertainable from their accounts. This mistake was not detected and rectified by the assessing authority which resulted in short levy of tax, interest and penalty amounting to ₹ 188.05 crore as shown in Annexure X.

Inadmissible/excess deductions from turnover should invariably be avoided while accepting returns/finalising the assessments.

2.11.18 Variation between accounts and returns

Section 42 stipulates that every dealer whose total turnover in a year exceeds ₹ Sixty lakh shall get his accounts audited annually by a Chartered Accountant and shall submit copy of the audited statements of accounts and certificates. Section 42(2) of the Act provides that where any dealer detects any omission or mistake in the annual return submitted by him with reference to the audited annual accounts, he shall file revised annual return rectifying the mistake or omission along with the audit certificate accompanied by proof of payment of such tax, interest and penal interest.

In four²³ assessment circles, out of 21 test checked, there was difference in the contract receipt returned and the contract receipt accounted in eight cases. But neither the assessee revised their annual return and paid the balance tax due nor

²² Works Contract Offices, Ernakulam and Idukki, Mattancherry Special Circle II, Ernakulam

²³ Works Contract Offices Ernakulam, Thiruvananthapuram and Thrissur, Special Circle II, Ernakulam.

the assessing authority assessed the balance turnover. This resulted in short levy of tax of ₹ 11.08 crore including interest and penalty as shown in Annexure XI.

2.11.19 Application of incorrect rate of tax

Section 6(1)(f) of KVAT Act provides that in the case of transfer of goods involved in execution of works contract, where the transfer is not in the form of goods but in some other form, tax shall be levied at the rate of 12.5 *per cent* and when the transfer is in the form of goods at the rates prescribed under the respective Schedules. Proviso 9 below Section 6(1)(f) of the Act provides that in respect of transfer of goods other than declared goods²⁴ into works contract if the transfer is not in the form of goods, the rate applicable shall be 12.5 *per cent*.

Audit noticed in two cases in two assessment circles, that goods other than declared goods were assessed at four *per cent* instead of 12.5 *per cent* resulting in short levy of tax at differential rate of 8.5 *per cent* including interest and penalty amounting to ₹ 7.26 crore as detailed below:

Sl. No.	Office to which related	Name of the assessee	Year	Turnover on which incorrect rate was applied	Short levy
				(₹ in crore)	
1.	CTO, Special Circle II, Ernakulam	M/s Larsen & Toubro Ltd.	2010-11	20.75	5.79
2.	CTO, WC, Ernakulam	M/s Sterling & Wilson	2010-11	5.30	1.47
Total					7.26

2.11.20 Compounding of works contract tax

Compounding is beneficial to assesseees due to the lower rate of tax liability of three *per cent*. The contractor may either file separate application for compounding for individual work or single option for payment of tax under the scheme in respect of all works undertaken by him during a year. Audit found the following deficiencies/irregularities in this system.

2.11.20.1 Delay in approval of compounding application

Rule 11 of the KVAT Rules stipulates that to exercise the option for compounding, the assesseees have to obtain permission from the assessing authority. The assessing authority may grant permission or reject it as per merits of the case. Audit found that there was a long delay in taking decision by the assessing officers. Thus, out of the 17,423 applications received in 15 offices, approval was granted in 8,980 cases only and 8,443 cases were pending for want of approval. Delay in processing the compounding applications may result in acceptance of returns filed by ineligible dealers as if compounded.

²⁴ Declared goods are goods declared by Section 14 of the Central Sales Tax Act 1956 (Central Act 74 of 1956) to be of special importance in interstate trade or commerce. Sand is not a declared good.

2.11.20.2 Short levy of tax due to inadmissible compounding

Under Section 8(a) of the KVAT Act, contractors can opt for payment of tax at compounded rate of three *per cent*. For availing the facility, conditions specified under the Act are to be satisfied. Audit noticed that in many cases option for compounding was admitted in contravention to the provisions of the Act as illustrated below:

- Under proviso to Section 8(a) of the Act, compounding is not admissible to contracts in which the transfer of materials is in the form of goods.
Audit noticed that out of the 24 assessment circles checked, in four²⁵ assessment circles, six contractors, who were engaged in the supply of poles, doors and windows etc., were permitted to compound. This was not regular since the predominant portion of the contract was for supply.
- Under Rule 11(1A), for compounding, works contractor shall file copies of agreement executed for work along with the application for compounding. In one case²⁶, the assessee was allowed to compound without contract agreements. In another case²⁷, the contractor was allowed to compound without an application as stipulated in Rule.

Inadmissible compounding in above cases resulted in short levy of ₹ 37.99 crore including interest and penalty as shown in Annexure XII.

2.11.21 Conclusion

- The Department does not have a system to identify works contract assessees and the works contract tax collection.
- The Department does not have a macro perspective of the constructional activities in the State. Deficiencies in surveys resulted in non-registration of unregistered contractors.
- The Department does not have an effective system and procedure for inter-departmental cross verification of data with other buying/implementing departments.
- The internal control mechanism existing in the Department was not adequate.

2.11.22 Summary of recommendations

The Government/Department may ensure that

- ❖ separate identification numbers/code are assigned to work contractors

²⁵ Works contract offices, Kottayam, Mattancherry, Thrissur and CTO Wadakancherry

²⁶ Works contract office, Kottayam

²⁷ Works contract office, Thiruvananthapuram

- ❖ separate account subhead are provided for accounting receipts under works contracts.
- ❖ regular survey and inter-departmental cross verification of data are conducted to identify the works contractors by strengthening the intelligence wing and suitable measures for registration are taken promptly.
- ❖ valid documents in support of compounding are produced by the applicant timely.
- ❖ internal control mechanism is adequate to plug revenue loss, detecting the defects/deficiencies promptly.
- ❖ various declaration forms in support of claims for concession/exemptions are verified properly.

2.12 Non-observance of provisions of Acts/Rules

The Kerala General Sales Tax/Kerala Value Added Tax/Central Sales Tax Act and Rules made there under provide for:

- (i) levy of tax/interest/penalty at the prescribed rates;*
- (ii) allowing exemption of turnover subject to fulfilment of the prescribed conditions; and*
- (iii) allowance of input tax credit as admissible.*

It was noticed in audit that the AAs while finalising the assessment did not observe some of the provisions which resulted in non/short levy/non-realisation of tax/interest/penalty as mentioned in the paragraphs 2.13 to 2.26.

Value Added Tax**2.13 Short levy of tax due to misclassification*****Commodities were misclassified which resulted in short levy of tax*****2.13.1** (CTO, Special Circle I, Ernakulam)

As per Sl. No.25 of the notification²⁸ date 2006, Eau-de-cologne (a perfume), detergents, shampoos and cosmetics are taxable at 12.5 *per cent* under Section 6(1) of KVAT Act.

Sales turnover for 2008-09, 2009-10 and 2010-11 conceded by M/s Procter & Gamble Hygiene & Health Care Ltd., Kochi, a dealer in health care

products, included medicine taxed at four *per cent* on maximum retail price and napkins and diapers assessed at four *per cent*. Audit cross verified the details of check post declarations in KVATIS module with the annual returns filed by the assessee for the years 2008-09 to 2010-11. Audit scrutiny revealed that during these years, the assessee stock transferred into the State Eau-de-cologne, detergents, shampoos and cosmetics amounting to ₹ 23²⁹ crore. But the assessee did not concede in their annual returns for the respective years any sale of goods taxable at 12.5 *per cent*. Thus, sales turnover conceded as medicine included that of Eau-de-cologne (a perfume), detergents, shampoos and cosmetics. The misclassification of corresponding sales resulted in short levy of ₹ 5.49 crore (Tax ₹ 4.28 crore, cess ₹ 0.04 crore, interest ₹ 1.17 crore).

This was pointed out (October 2012) to the Department and reported (January 2013) to Government. Their reply has not been received (February 2014).

2.13.2 (CTO, Special Circle I, Ernakulam)

Under Section 6(d) of KVAT Act 2003, goods not falling under any of the schedules to the Act is taxable at 12.5 *per cent*. Damp proof or water proof compound of HSN 3824.40.10 is not included in any of the schedules to KVAT Act and hence is liable to be taxed at 12.5 *per cent*.

M/s Pidilite Industries Ltd., Kochi, a dealer in adhesives, paints etc., self assessed tax on sales turnover of Dr.Fixit Super latex and Dr.Fixit Pedicrete for ₹ 6.63 crore for the year 2010-11 at four *per cent* applicable to chemicals instead of at 12.5 *per cent* on

water proofing compound. As per data provided by the manufacturer in internet, Dr.Fixit Super latex and Dr.Fixit Pedicrete are multipurpose SBR latex based product for general repairs and economical waterproofing applications. Incorrect

²⁸ Vide SRO 82/2006

²⁹ Eau-de-cologne amounting to ₹ 5.04 crore, ₹ 9.05 crore and ₹ 8.10 crore during 2008-09, 2009-10 and 2010-11 respectively and detergents, shampoos and cosmetics amounting to ₹ 50.33 lakh and ₹ 30.86 lakh during the years 2008-09 and 2009-10

application of four *per cent* instead of 12.5 *per cent* resulted in short levy of ₹ 66.62 lakh (Tax ₹ 56.38 lakh, cess ₹ 0.56 lakh, interest ₹ 9.68 lakh).

This was pointed out (October 2012) to the Department and reported (January 2013) to Government. Government stated (May 2013) that notice was issued to the dealer proposing to assess the turnover. Further report has not been received (February 2014).

2.14 Short levy of tax due to application of incorrect rate of tax

Rate of tax applied on the taxable turnover was less than the rate applicable as per the statute

2.14.1 (CTO, Special Circle II, Ernakulam)

As per Section 6(1) (f) of KVAT Act, 2003, in the case of transfer of goods involved in execution of works contract, where the transfer is not in the form of goods but in some other form, rate of tax is 12.5 *per cent*.

M/s HCL Infosystems Ltd., Kochi filed annual returns for the year 2008-09 and 2009-10 showing the following details.

Particulars	₹ in crore)	
	2008-09	2009-10
Total turnover	95.10	90.07
Taxable turnover	87.36	80.75
Annual maintenance contract amount received	8.76	10.07
Exemption claimed	7.43	8.55
Taxable turnover conceded	1.32	1.53

The assessee had annual maintenance contract receipt of ₹ 8.76 crore and ₹ 10.07 crore during 2008-09 and 2009-10 respectively. They availed exemption of ₹ 7.43 crore and ₹ 8.55 crore towards labour and other charges. The assessee had not transferred any part of the goods in the form of goods as such remaining turnover was taxable at the rate of 12.5 *per cent*. But balance turnover of ₹ 1.32 crore and ₹ 1.53 crore were assessed to tax at four *per cent*. Application of incorrect rate of tax resulted in short levy of ₹ 30.50 lakh at the differential rate of 8.5 *per cent* (Tax ₹ 24.23 lakh, cess ₹ 0.24 lakh, interest ₹ 6.03 lakh).

After this was pointed out (between November 2011 and January 2012), Government stated (November 2013) that the assessments were revised as pointed out by Audit and the assessee remitted ₹ 7.92 lakh. Further report has not been received (February 2014).

2.14.2 (CTO, II Circle, Thiruvananthapuram)

Bakery products including biscuits sold under brand name, registered under the Trade Mark Act 1999 are liable to be taxed at 12.5 *per cent*, under Sl.No.11 of list of 12.5 *per cent* taxable goods notified under KVAT Act, 2003.

M/s Ambadi Food Products, Thiruvananthapuram was a manufacturer of bakery products selling goods under a brand name

‘Appoos’ registered under Trade Mark Act 1999. It filed annual return for 2008-09 assessing the turnover of ₹ two crore at the rate of four *per cent*. Assessing authority while completing assessment under section 25 (1) fixing the taxable turnover as ₹ 2.07 crore, assessed tax on the entire turnover at four *per cent* instead of the correct rate of 12.5 *per cent* applicable to branded food products. This resulted in short levy of ₹ 23.51 lakh (Tax ₹ 17.63 lakh, cess ₹ 0.18 lakh, interest ₹ 5.70 lakh).

The case was pointed out (December 2011) to the Department and to the Government in June 2013. Government stated (September 2013) that assessment had been completed creating an additional demand of ₹ 17.81 lakh as tax and ₹ 6.41 lakh as interest and revenue recovery steps were initiated against the dealer. Further report has not been received (February 2014).

- (CTO, Special Circle, Kottayam)

M/s Kerala Bakers, a manufacturer and dealer of biscuits with trademark registration under Trademark Act 1999, self assessed to tax their sales turnover relating to biscuits of ₹ 45.02 lakh and ₹ 53.66 lakh for 2005-06 & 2006-07 respectively at four *per cent*. Audit scrutiny of assessment records of the assessee for the years 2005-06 and 2006-07 revealed that the assessee sold biscuits with registered trade mark ‘Thomsons’. However, the assessing authority did not assess to tax the turnover at 12.5 *per cent*. Short levy due to application of incorrect rate worked out to ₹ 10.52 lakh (Tax ₹ 8.39 lakh, interest ₹ 2.13 lakh).

After these cases were pointed out (February 2009) in audit, the Department stated (December 2012) that the assessments had been completed (December 2011) creating additional demand of ₹ 13.63 lakh. Further report has not been received (February 2014).

2.14.3 (CTO, Special Circle, Malappuram)

As per notified list of goods taxable at 12.5 *per cent* under KVAT Act, 2003, cosmetics including hair oil, hair cream etc., are taxable at 12.5 *per cent*. As per proviso 13 to section 6(1) of the Act, tax payable on *ayurvedic* cosmetic products manufactured under a drug license granted under the Drugs and Cosmetics Act, 1940 (Central Act 23 of 1940) containing added medicaments having subsidiary therapeutic or prophylactic uses shall be four *per cent* for the period from 1 April 2005 to 12 November 2009.

M/s Santhosh Pharmacy, Kadalundi Nagaram was a manufacturer and dealer in *ayurvedic* products. During 2010-11, they self assessed to tax the turnover of *ayurvedic* cosmetic products for ₹ 2.58 crore at four *per cent* on maximum retail price. Even though *ayurvedic* cosmetic products are taxable at 12.5 *per cent*, the assessing authority did not take any

action to assess the tax at correct rate. This resulted in short levy of ₹ 18.83 lakh (Tax ₹ 16.50 lakh, cess ₹ 0.16 lakh, interest ₹ 2.17 lakh).

This was pointed out (May 2012) in audit to the Department and reported to Government in January 2013. Government stated (August 2013) that notice under Section 25(1) of the Act had been issued to the dealer proposing additional demand of ₹ 13.59 lakh. Reason for shortfall in assessment at differential rate of tax has not been furnished. Further report has not been received (February 2014).

2.14.4 (CTO, (WC), Thiruvananthapuram)

Under section 6(1) (f) of the KVAT Act, transfer of goods involved in the execution of works contract where the transfer is not in the form of goods, but in some other form is liable to be taxed at 12.5 *per cent*. Tyre retreading contract is a works contract not in the form of goods and is taxable at the rate of 12.5 *per cent*.

M/s Kerala State Engineering and Transport Development Co-operative Society, Trivandrum is an assessee engaged in tyre retreading and trading of automobile spare parts. As per the VAT abstracts furnished by the assessee, they had turnover of ₹ 30.02

lakh and ₹ 36.93 lakh during 2008-09 and 2009-10 respectively relating to tyre retreading. Though turnover of tyre retreading is taxable at 12.5 *per cent*, the assessee self assessed the turnover at four *per cent*. The assessing authority also did not complete the assessments applying the correct rate. Failure to assess the turnover at 12.5 *per cent* resulted in short levy of ₹ 7.26 lakh (Tax ₹ 5.69 lakh, cess ₹ 0.06 lakh, interest ₹ 1.51 lakh).

The case was pointed out (January 2012) to the Department and to the Government in May 2013. Government stated (July 2013) that assessments for the two years were revised (March 2012) creating total additional demand of ₹ 6.01 lakh. Further report has not been received (February 2014).

- **(CTO (WC<), Kollam)**

M/s Quilon Tyres and Treads, Kollam was a works contractor engaged in tyre retreading. The assessee had a contract receipt of ₹ 69.07 lakh during 2009-10 from retreading of tyres. The assessee assessed to tax the value of materials transferred amounting to ₹ 52.64 lakh at four *per cent* after deducting labour and other charges instead of at the rate of 12.5 *per cent*. Failure to levy tax at 12.5 *per cent* on the value of goods transferred resulted in short levy of ₹ 5.51 lakh (Tax ₹ 4.47 lakh, cess ₹ 0.04 lakh, interest ₹ 1 lakh).

After this being pointed out (February 2012) in audit, the Department stated (June 2012) that tyre retreading is a composite contract in which VAT was levied on that part of contract receipt after deducting the service. The reply is not correct since the materials transferred were not in the form of goods and the turnover should have been assessed to tax at 12.5 *per cent* instead of four *per cent*. The case was reported to Government in September 2012; their reply has not been received (February 2014).

- (CTO, II Circle, Palakkad)

M/s Shreyas Enterprises, Palakkad was a dealer in medicine. During 2009-10, the assessee assessed tax on a turnover of an *ayurvedic* cosmetic product at four *per cent*, though the reduced rate was applicable upto 12 November 2009 only. Though *ayurvedic* cosmetic products are 12.5 *per cent* taxable with effect from 13 November 2009, the assessing authority did not take any action to assess the tax at correct rate. Short levy of tax on the estimated turnover of ₹ 23.20 lakh from 13 November 2009 to 31 March 2010, worked out to ₹ 2.41 lakh (Tax ₹ 1.97 lakh, cess ₹ 0.02 lakh, interest ₹ 0.42 lakh).

When this case was pointed out (January 2012) in audit the Department stated (May 2012) that the assessment had been revised (February 2012) creating additional demand of ₹ 2.58 lakh. Further report has not been received (February 2014).

2.14.5 (CTOs II Circle and III Circle Thiruvananthapuram, Special Circle I, Ernakulam and II Circle, Palakkad)

Mixing machines, cake machines, slicer, roto oven, gas oven, grinder, egg beater are coming under entry 32(1)(a)(b) and 32(3) of notified list taxable at 12.5 *per cent*. Under Section 11(5)(c) of the Act, no input tax credit shall be allowed for the purchases from a dealer paying compounded tax under Section 8 of the KVAT Act.

Audit noticed between September 2011 and October 2012 that, the following assessee assessed to tax whole or part of their turnover at a rate lower than the rate at which they were assessable. The assessing

authority also did not take any action to assess tax at correct rate. This resulted in short levy of tax, cess and interest of ₹ 35.37 lakh in four cases as detailed below:

				(₹ in lakh)
Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Short levy of Tax, cess and interest
1.	M/s Sahya Trading Corporation, <u>Thiruvananthapuram</u> CTO, III Circle, Thiruvananthapuram	2009-10 Bakery machines, Kitchen machines 12.5%	The entire local sales turnover of ₹ 1.41 crore was assessed to tax at four <i>per cent</i> though the items dealt in by the assessee were cake machine, slicer, roto oven etc, which included in the notified list of goods taxable at 12.5 <i>per cent</i> . (Tax ₹ 11.99 lakh, cess ₹ 0.12 lakh, interest ₹ 2.42 lakh).	14.53
The Department stated (May 2012) that the assessment has been completed by creating an additional demand of ₹ 17.65 lakh. Further report has not been received (February 2014).				
2.	M/s Trivandrum Metals and <u>Electricals</u> CTO, II Circle, Thiruvananthapuram	2009-10 Electrical goods 12.5%	The assessee conceded in their profit and loss account a gross profit of 86.09 <i>per cent</i> in four <i>per cent</i> taxable items and a gross loss of 41.29 <i>per cent</i> in 12.5 <i>per cent</i> taxable items. The abnormal profit in four <i>per cent</i> taxable goods and abnormal loss in 12.5 <i>per cent</i> taxable goods were due to misclassification of 12.5 <i>per cent</i> items as four <i>per cent</i> taxable items to reduce tax liability. (Tax ₹ 9.33 lakh, cess ₹ 0.09 lakh, interest ₹ 1.89 lakh).	11.31

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Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Short levy of Tax, cess and interest
	The Department accepted the audit observation and revised assessment (February 2012) by creating additional demand of ₹ 16.40 lakh. Further report has not been received (February 2014).			
3.	M/s Asian Paints Ltd., <u>Palarivattom</u> CTO, Special Circle I, Ernakulam	2009-10 Paints 12.5%	The turnover of the assessee was assessable at 12.5 <i>per cent</i> and four <i>per cent</i> . The assessing officer reckoned the turnover taxable at 12.5 <i>per cent</i> as ₹ 399.34 crore while completing assessment for 2009-10 under Section 25. However, audit scrutiny revealed that the turnover taxable at 12.5 <i>per cent</i> was ₹ 399.87 crore. The assessing officer had assessed the difference of ₹ 53.45 lakh at four <i>per cent</i> (Tax ₹4.54 lakh, cess ₹0.05 lakh, interest ₹1.28 lakh).	5.87
	The Department accepted the audit point (September 2012) and revised the assessment rectifying the defect. Further report has not been received (February 2014).			
4.	M/s Quality Machinery <u>Suppliers.</u> CTO, II Circle, Palakkad	2009-10 Machinery, electrical goods etc. 12.5%	As per the annual return filed, the assessee had purchased machinery and electrical goods taxable at the rate of 12.5 <i>per cent</i> taxable goods for ₹ 38.07 lakh. There was no appreciable difference between opening and closing balances as per the profit and loss account. The dealer self assessed to tax ₹ 5.51 lakh at 12.5 <i>per cent</i> and the balance turnover was assessed at four <i>per cent</i> only. Applying the conceded gross profit of 6.93 <i>per cent</i> , the sales turnover of 12.5 <i>per cent</i> taxable goods would have been ₹ 40.71 lakh (Tax ₹ 2.99 lakh, cess ₹ 0.03 lakh, interest ₹ 0.64 lakh).	3.66
	The Department while accepting the audit observation stated (May 2012) that assessment was completed (March 2012) creating additional demand of ₹ 3.72 lakh. Further report has not been received (February 2014).			
			Total	35.37

2.15 Short levy of tax due to incorrect claim of input tax credit/special rebate

Input tax credit/special rebate was availed in excess in the case of interstate sale resulting in short levy of tax.

2.15.1 (CTO, Special Circle, Perumbavoor)

Under proviso 3 to Section 11(3) read with proviso 3 to Section 12(1) where any goods purchased in the State are subsequently sent outside the State or used in the manufacture of goods and the same are sent outside the State by sale in the course of inter-state trade, which is exempted from tax, input tax credit and special rebate shall be limited to the amount of input tax /purchase tax paid in excess of four *per cent* on the purchase turnover of such goods sent outside the State.

M/s. E.V Mathai & Sons, Kothamangalam, Ernakulam was a manufacturer of pipes of all kinds. Their exempted interstate sale of rubber sheet and rubber products constituted 72.17 *per cent* and 73.70 *per cent* of the total disposal of such goods during 2009-10 and 2010-11 respectively. Total purchase turnover of the assessee for the years 2009-10 and 2010-

11 was ₹ 85.99 crore and ₹ 160.89 crore respectively. Since the assessee had exempted interstate sales, input tax credit/special rebate was admissible only on 27.83 *per cent* and 26.30 *per cent* of the value of goods consumed. These amounted to ₹ 23.90 crore and ₹ 42.08 crore respectively during these years. Against these the assessee availed ITC/ special rebate on the turnover of ₹ 26.24 crore and ₹ 50.33 crore respectively as per their annual return for above years. This resulted in availing input tax credit in excess on a turnover of ₹ 2.35 crore and ₹ 8.25 crore during 2009-10 and 2010-11 respectively and consequent short levy of ₹ 49.95 lakh (Tax ₹ 42.40 lakh, cess ₹ 0.42 lakh, interest ₹ 7.13 lakh).

The case was pointed out (July 2012) to the Department and to the Government in December 2012. Government stated (May 2013) that assessment had been completed (January 2013) creating additional demand of ₹ 32.19 lakh and the amount is pending collection. Reason for shortfall in additional demand has not been furnished. Further report has not been received (February 2014).

- (CTO, Special Circle, Malappuram)

M/s Arya Vaidyasala, Kottakkal, Malappuram, filed annual return for 2010-11 conceding total disposal of goods as ₹ 165.35 crore. As per annual returns filed by the assessee, interstate stock transfer amounting to ₹ 37.96 crore constituted 22.96 *per cent* of the total disposal of goods. Though the assessee should have reversed input tax credit of ₹ 49.54 lakh, being the input tax credit/special rebate availed on the turnover of ₹ 12.38 crore, proportionate to the turnover of stock transfer, they reversed only ₹ 10.69 lakh. This resulted in short levy of ₹ 44.33 lakh (Tax ₹ 38.84 lakh, cess ₹ 0.39 lakh, interest ₹ 5.10 lakh).

The case was pointed out (May 2012) in audit, to the Department and reported to Government in January 2013. Their reply has not been received (February 2014).

- (CTO, Mannarkad)

M/s Associated Agro Machineries, Palakkad, was a dealer in power tillers and spares. During 2010-11, the assessee procured goods valued ₹ 1.44 crore locally and stock transferred the same to other states. Since entire goods purchased locally were stock transferred, four *per cent* input tax credit of ₹ 5.77 lakh on local purchase turnover was liable to be reversed. However, they reversed input tax credit of ₹ 18,784 only. This resulted in short levy of ₹ 6.65 lakh (Tax ₹ 5.58 lakh, cess ₹ 0.06 lakh, interest ₹ 1.01 lakh).

The case was pointed out (November 2012) to the Department and pointed out (July 2013) to the Government. Government stated (December 2013) that the assessment was revised (December 2012) creating additional demand of ₹ 6.76 lakh and an amount of ₹ 4.05 lakh has been collected (February to July 2013) and instalment was granted for the balance amount. Further report has not been received (February 2014).

- Audit noticed between November 2011 and October 2012 that, in the following eight cases, the assessee who stock transferred goods outside the state claimed input tax credit/special rebate more than that admissible as per the Act. The assessing authority also did not disallow the excess claim. This resulted in short levy of tax, cess and interest of ₹ 1.16 crore as detailed below:

(₹ in lakh)				
Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Tax, cess and interest leviable
1	M/s Binani Zinc Ltd, Kochi CTO, Special Circle, Mattanchery at Aluva	2009-10 Zinc, Cadmium etc. 12.5% 4%	As per the annual return filed by the assessee, the total sales turnover was ₹ 418.57 crore for which an input tax credit claimed by the assessee was ₹ 1.58 crore. However, 92.51 <i>per cent</i> of the sales turnover (₹ 387.22 crore) was interstate stock transfer. Hence input tax paid upto four <i>per cent</i> on 92.51 <i>per cent</i> of goods purchased should have been reversed. Against the liability of reverse tax of ₹ 1.05 crore, the reverse tax admitted by the assessee was only ₹ 44.05 lakh. Short levy-(Tax ₹ 61.20 lakh, cess ₹ 0.61 lakh, interest ₹ 14.84 lakh.)	76.65
	Department stated (September 2012) that the accounts had been called for from the assessee to verify the points raised in Audit. The assessment is pending finalisation. Further report has not been received (February 2014).			
2	M/s The Highland Produce Co. Ltd. Alappuzha CTO, Special Circle, Alappuzha	2010-11 Tea & spices 4%	As per their annual return interstate stock transfer constituted 40.67 <i>per cent</i> of the total disposal of tea for the	12.83

Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Tax, cess and interest leviable
			year. Local purchase turnover of tea being ₹ 15.58 crore, four <i>per cent</i> tax on the proportionate purchase turnover of ₹ 6.34 crore was to be disallowed. The assessee had not claimed ITC/Special rebate on a purchase turnover of ₹ 3.64 crore. Though input tax at four <i>per cent</i> on the balance turnover of ₹ 2.69 crore had to be disallowed, the assessing authority did not disallow it. Short levy-(Tax ₹ 10.77 lakh, cess ₹ 0.11 lakh, interest ₹ 1.95 lakh.)	
On this being pointed out (January 2013) in audit, the Government stated (November 2013) that assessment has been completed (July 2013) incorporating the defects pointed out in audit and other defects. Further report has not been received (February 2014).				
3	M/s High Count Marketing Division, Aluva CTO, Special Circle, Mattancherry at Aluva	2009-10 Pipes 4%	Audit scrutiny revealed that the interstate stock transfer of ₹ 1.23 crore constituted 6.90 <i>per cent</i> of the total disposal/sale of goods amounting to ₹ 17.76 crore. The assessing authority did not limit the input tax credit to tax paid in excess of four <i>per cent</i> on purchase turnover of ₹ 1.24 crore proportionate to stock transfer. Short levy-(Tax ₹ 4.94 lakh, cess ₹ 0.05 lakh, interest ₹ 1.10 lakh).	6.09
Department stated (September 2012) that notice to complete the assessment had been issued to the assessee. Further report has not been received (February 2014).				
4	M/s Accelerated Freeze Drying Company Ltd. Alappuzha CTO, Special Circle, Alappuzha	2010-11 Pepper 4%	The assessee had local purchase of pepper for ₹ 2.99 crore from registered/unregistered dealers during 2010-11 and availed entire tax paid to registered dealers as ITC and special rebate on purchase tax due on purchase from unregistered dealers as per the annual return filed by it. Audit scrutiny of assessment records for the year 2010-11 of the assessee revealed that, interstate stock transfer constituted 38.70 <i>per cent</i> of total disposal of goods. The assessing authority did not disallow four <i>per cent</i> tax on proportionate local purchase turnover of ₹ 1.16 crore. Short levy-(Tax ₹ 4.63 lakh, cess ₹ 0.05 lakh, interest ₹ 0.79 lakh).	5.47
Government stated (July 2013) that assessment for the year 2010-11 was completed (March 2013) creating an additional demand of ₹ 7.01 lakh. Further report has not been received (February 2014).				

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Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Tax, cess and interest leviable
5	M/s Arya Vaidya Pharmacy (CBE) Ltd., Palakkad CTO, Special Circle, Palakkad	2009-10 Ayurvedic medicine 4%	The assessee availed as input tax credit and special rebate, entire tax paid/payable on local purchase turnover of ₹ 3.72 crore. Audit scrutiny revealed that for the year 2009-10 the total sales turnover of ₹ 48.77 crore included stock transfer of ₹ 13.99 crore (28.68 per cent). The assessing authority also did not limit the input tax credit/special rebate to the tax paid in excess of four per cent on the purchase turnover of goods stock transferred to out side the state. Short levy-(Tax ₹ 4.26 lakh, cess ₹ 0.04 lakh, interest ₹ 0.78 lakh).	5.08
Reply has not been received (February 2014).				
6	M/s Victoria Poly Form, Thrissur CTO, Special Circle, Thrissur	2010-11 Plastic articles 4%	As per its annual return for 2010-11 interstate stock transfer constituted 17.59 per cent of the total disposal of goods for the year. Local purchase turnover being ₹ 4.50 crore, four per cent tax on the proportionate purchase turn over of ₹ 79.22 lakh was to be disallowed. The assessing authority also did not disallow the ITC/Special rebate availed in excess. Short levy-(Tax ₹ 3.17 lakh, cess ₹ 0.03 lakh, interest ₹ 0.51 lakh).	3.71
Government stated (October 2013) that assessment had been completed (October 2012) creating additional demand of ₹ 4.45 lakh and RRC was issued to realise the amount. The assessee paid ₹ 1.48 lakh. Further report has not been received (February 2014).				
7	M/s The Nelliampathy Tea and Produce Co. Ltd., Kochi. CTO, Special Circle, Alappuzha	2010-11 Tea, Coffee etc. 4%	Audit scrutiny of trading account of tea and annual return of the assessee for the year 2010-11 revealed that, it stock transferred tea for ₹ 5.01 crore which constituted 38.31 per cent of total disposal of tea of ₹ 13.07 crore. They had purchased locally from unregistered dealers tea leaf valued ₹ 1.97 crore and availed exemption on entire purchase tax due as special rebate. The assessing authority did not limit the input tax credit/special rebate to the tax paid in excess of four per cent on the purchase turnover of goods stock transferred to out side the State. Short levy-(Tax ₹ 3.02 lakh, cess ₹ 0.03 lakh, interest ₹ 0.52 lakh.)	3.57
Reply has not been received (February 2014).				

Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Tax, cess and interest leviable
8	M/s Wellworth Marketing Enterprise, Aluva CTO, Special Circle, Mattancherry	2009-10 PVC pipes, valves etc. 4%	Out of the total turnover of ₹ 15.31 crore for the assessment year 2009-10, ₹ 52.44 lakh pertained to interstate stock transfer. The assessee had availed input tax credit for the entire local purchase of ₹ 14.78 crore and the assessing authority had accepted it. As per provision of the Act, the input tax credit of four <i>per cent</i> of the purchase value corresponding to stock transfer of ₹ 52.44 lakh had to be disallowed. Short levy (Tax ₹ 2.03 lakh, cess ₹ 0.02 lakh, interest ₹ 0.47 lakh).	2.52
Department stated (September 2012) that notice had been issued to the assessee. Further report has not been received (February 2014).				
Total				115.92

2.15.2 (CTO, Special Circle, Alappuzha)

Under Section 11 (5)(e) of KVAT Act, 2003 no input tax credit shall be allowed for the purchase of goods which are used in the manufacture, processing and packing of goods, specified in the First schedule of KVAT Act. Rubberised coir product is an item specified in entry 23 of Schedule I of KVAT Act.

M/s Kerala Balers (P) Ltd, Alappuzha, a manufacturer of coir products conceded local and interstate sale of rubberized coir products (exempted) which constituted 21.44 *per cent* of their

total sale during 2010-11. Local purchase turnover proportionate to exempted sale was ₹ 1.71 crore on which input tax credit and special rebate of ₹ 13.10 lakh was liable to be disallowed. Failure to disallow the same resulted in short levy of ₹ 15.61 lakh (Tax ₹ 13.10 lakh, cess ₹ 0.13 lakh, interest ₹ 2.38 lakh).

This was pointed out (November 2012) to the Department and reported to Government in January 2013. Government stated (November 2013) that the assessment has been revised (June 2013) and additional demand of ₹ 16.67 lakh including interest created. Further report has not been received (February 2014).

- (CTO, Special Circle, Alappuzha)

M/s Mayithara Home Décor (P) Ltd, Cherthala, a manufacturer of coir products (exempted from payment of tax) conceded local and interstate sale of coir products constituting 12.70 *per cent* of their total sale in the annual return for 2010-11. Local purchase turnover proportionate to exempted local and interstate sale was ₹ 34.28 lakh on which input tax credit of ₹ 3.65 lakh was incorrectly availed. This resulted in short levy of ₹ 4.35 lakh (Tax ₹ 3.65 lakh, cess ₹ 0.04 lakh, interest ₹ 0.66 lakh).

This was pointed out (November 2012) to the Department and reported to Government in January 2013. Government stated (October 2013) that assessment had been completed (May 2013) by disallowing ₹ 4.61 lakh which was the ITC with interest proportionate to the exempted sale and created additional demand of tax of ₹ 2.32 lakh and interest of ₹ 0.14 lakh. Further report has not been received (February 2014).

2.15.3 (CTO, Special Circle, Perumbavoor)

Government by a notification³⁰ *inter alia* excluded building material and fixtures used in construction activity from the purview of capital goods and hence these goods shall not be entitled for input tax credit.

M/s Kitex Childrens wear Ltd. Aluva was a manufacturer and exporter of readymade garments. Audit scrutiny of annual

return of the assessee for 2010-11 revealed that they availed input tax credit of ₹ 7.46 lakh on purchase of building materials costing ₹ 82.28 lakh. Though the assessee had no dealings in building materials which was also not coming under the purview of capital goods, the assessing authority did not disallow the claim. This resulted in short levy of ₹ 8.59 lakh (Tax: ₹ 7.46 lakh, cess: ₹ 0.07 lakh, interest: ₹ 1.06 lakh).

The case was pointed out (June 2012) to the Department in audit and reported to Government in December 2012. Government stated (July 2013) that assessment had been revised (February 2013). Report on recovery is awaited (February 2014).

2.15.4 (CTO, Special Circle, Thrissur)

Section 11(7) of the KVAT Act, 2003 states that if goods in respect of which input tax credit has been availed of are subsequently used, fully or partly, for purposes in relation to which no input tax credit is allowable under the section, the input tax credit availed of in respect of such goods shall be reverse tax.

M/s Modern Sanitary, Thrissur was a dealer in tiles, sanitary wares etc. The assessing authority in May 2011 accorded sanction for deleting the stock of broken and un-saleable goods of the assessee worth ₹ 71.05

lakh subject to the remittance of reverse tax of ₹ 43,795. During 2010-11 the assessee filed annual return recording reverse tax of ₹ 43,796 based on the sanction order of the assessing authority. Out of the total purchase, the local purchase of the assessee from 2008-09 to 2010-11 was 40.89³¹ *per cent*. Proportionate local purchase component of the disposed stock worked out to ₹ 29.05 lakh and reverse tax due thereon was ₹ 3.63 lakh. However, the assessing

³⁰ SRO No. 324/2005 dated March 2005

³¹ annual average percentage

authority did not fix reverse tax correctly proportional to local purchase involved. This resulted in short levy of ₹ 3.77 lakh (Tax ₹ 3.19 lakh, cess ₹ 0.03 lakh, interest ₹ 0.55 lakh).

The case was pointed out (September 2012) in audit to the Department and reported to Government in April 2013. Government stated (November 2013) that the assessment was revised and the additional demand created of ₹ 2.76 lakh was advised for collection under revenue recovery. Reason for shortfall in additional demand created is not furnished. Further report on recovery has not been received (February 2014).

2.15.5 (CTO, Special Circle, Palakkad)

Under Section 42(2) of KVAT Act 2003, where any dealer detects any omission or mistake in the annual return submitted by him with reference to the audited figures, he shall file revised annual return rectifying the mistake or omission along with the audit certificate. Where, as a result of such revision, the tax liability increases, the revised return shall be accompanied by proof of payment of such tax, interest due thereon and twice interest as penal interest.

M/s Palakkad Rubber Private Ltd. was a dealer in Crumb Rubber. In the tax return filed for 2005-06, the assessee availed input tax of ₹ 84.98 lakh by conceding purchase turnover as ₹ 20.64 crore. However, audit scrutiny (December

2011) of the P&L account revealed that the purchase turnover was ₹ 19.16 crore only. Thus the assessee availed input tax credit in excess of ₹ 5.92 lakh on a turnover of ₹ 1.48 crore. This resulted in short levy of ₹ 9.88 lakh (Tax: ₹ 5.92 lakh, interest: ₹ 3.96 lakh).

The case was pointed out (December 2011) to the Department and to Government in November 2012. Their reply has not been received (February 2014).

• (CTO, Special Circle, Palakkad)

M/s Snofield Foods Pvt. Ltd, Palakkad was a dealer in food products, food preservatives etc. In the annual return for 2009-10 the assessee included a purchase of ₹ 2.58 crore from VAT dealers and availed input tax credit of ₹ 15.31 lakh. But audit scrutiny of the P&L account revealed that the purchase turnover was ₹ 1.86 crore only. Thus the assessee availed input tax credit of ₹ 4.35 lakh in excess on a turnover of ₹ 71.99 lakh. This resulted short levy of ₹ 5.23 lakh (Tax: ₹ 4.35 lakh, cess: ₹ 0.04 lakh, interest: ₹ 0.84 lakh).

The case was pointed out (December 2011) to the Department and was reported to Government in November 2012. Their reply has not been received (February 2014).

2.16 Short levy of tax due to escape of turnover from assessment

Turnover conceded in the return was less than the turnover certified by the Chartered Accountants

2.16.1 (CTO Special Circle, Palakkad, Alappuzha, Thrissur and II Circle, Palakkad)

Under Section 42(2) of KVAT Act 2003, if there is omission or mistake in annual return with reference to audited annual accounts, the assessee is required to file revised annual return along with the audited statements and if tax liability increases he shall file proof of payment of balance tax, interest thereon and twice the interest as penal interest. Under Section 11(5) of the Act, no input tax credit shall be allowed for the purchases from a dealer paying compounded tax under Section 8 of the Act.

Section 25 of KVAT Act empowers assessing authorities to assess tax on any turnover which has escaped assessment, within five years from the last date of the year to which return relates.

Audit noticed between November 2011 and September 2012 that the following assessee had conceded in their annual return and assessed to tax only a part of the turnover certified in the audited accounts. The assessing authority also did not take any action to assess the escaped turnover under the Act. This resulted in

short levy of tax, cess and interest of ₹ 1.10 crore in five cases as shown below:

(₹ in lakh)

Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Tax, cess and interest leviable
1	<u>M/s MPS Steel Castings</u> CTO, Special Circle, Palakkad	2009-10 Iron and Steel 4%	In the annual return the local sales turnover was recorded as ₹ 92.84 crore. But in the P&L account (2009-10), the local sales turnover recorded was ₹ 102 crore. Thus there was a difference of ₹ 9.16 crore in sales turnover. Short levy-(Tax ₹ 36.61 lakh, interest ₹ 6.96 lakh).	43.57
Reply has not been received (February 2014)				
2	<u>M/s Arya Vaidya Pharmacy (CBE) Ltd., Palakkad</u> CTO, Special Circle, Palakkad	2009-10 Ayurvedic medicine 4%	As per the annual return total and taxable turnover of the assessee was ₹ 25.94 crore and ₹ 24.96 crore respectively. As per Form 13A ³² , the assessee had interstate sales for	35.15

³² Statement of particulars forming part of certified annual accounts.

Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Tax, cess and interest leviable
			₹ 7.37 crore which was not supported by declaration in Form C ³³ . Under CST Act 1956, as amended by Finance Act 2007, the tax payable by a dealer on his turnover relating to interstate sale not covered by declaration in Form C shall be at the rate applicable to sale within the State. VAT payable on sale of Ayurvedic medicine is four <i>per cent</i> . But the above interstate sales turnover was not included in the annual return. Short levy-(Tax ₹ 29.49 lakh, cess ₹ 0.30 lakh, interest ₹ 5.36 lakh).	
Reply has not been received (February 2014)				
3	M/s Thieh Ingots (P) Ltd., <u>Kanjikode</u> CTO, II Circle, Palakkad	2009-10 Iron and Steel products 4%	As per annual accounts (Form 13A) closing stock was ₹ 5.97 crore. However, as per closing stock inventory (Form 53 ³⁴) that was ₹ 3.75 crore. The shortage of ₹ 2.22 crore in closing stock was unaccounted sale. Corresponding sales turnover including gross profit of 3.11 <i>per cent</i> escaped assessment. Short levy-(Tax ₹ 9.19 lakh, cess ₹ 0.09 lakh, interest ₹ 1.95 lakh).	11.23
The Department stated (June 2012) that the assessment under Section 25 had been completed (March 2012) creating additional demand of ₹ 89.90 lakh. Further report has not been received (February 2014).				
4	M/s Hercules Automobiles International (P) Ltd. <u>Alappuzha</u> CTO, Special Circle, Alappuzha	2010-11 Motor Car 12.5%	The assessee recorded in their profit and loss account for the year 2010-11, a purchase turnover of consumables for ₹ 83.92 lakh. But as per annual return filed, the assessee did not assess to tax the corresponding sales turnover of ₹ 90.17 lakh (Based on the profit margin). Short levy-(Tax ₹ 11.27 lakh, cess ₹ 0.11 lakh, interest ₹ 2.05 lakh).	13.43
Reply has not been received (February 2014)				
5	M/s Manappuram Jewellers Ltd., <u>Valappad, Thrissur</u> . CTO, Special Circle, Thrissur	2010-11 Gold 4%	The assessment for the year 2010-11 was finalised under Section 25, in which the claim of purchase return of ₹ 98.61 lakh was allowed on the strength of credit notes issued by M/s Sunny Diamonds, another dealer in gold. The annual return and accounts filed by M/s Sunny Diamonds did not include any sales return. As such tax credit on sales return availed by the assessee is not in order. Further, the assessee claimed input tax credit of ₹ 1.40 lakh for purchases from another	6.25

³³ Form of declaration to be filed to avail concessional rate of tax under Central Sales Tax Act 1956.

³⁴ Closing stock inventory to be filed along with annual returns

Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Tax, cess and interest leviable
			dealer, who was paying compounded tax under Section 8 for which the assessee is not entitled for input tax credit. Short levy-(Tax ₹ 5.34 lakh, cess ₹ 0.05 lakh, interest ₹ 0.86 lakh).	
The assessing officer stated (September 2012) that the case had been re-opened and assessment completed (September 2012) and demanded tax and interest of ₹ 13.70 lakh. Further report has not been received (February 2014).				
Total				109.63

2.16.2 (CTO, Special Circle, Thrissur)

Under Section 25 of KVAT Act, 2003 if whole or part of business of a dealer escaped assessment to tax in any year the assessing authority may at any time within five years from the last date of the year to which return relates proceed to determine to best of its judgment the turnover which has escaped assessment and assess tax payable on the same.

M/s Saleesh Wood Industries, Venginissery, was a dealer in timber. During 2010-11, the assessee conceded a purchase turnover of ₹ 5.47 crore and sales turnover of ₹ 7.26 crore in the annual certified accounts. As per the

annual return filed, the assessee had procured through interstate stock transfer from other states timber valued at ₹ 4.47 crore during the year. However, this stock transfer was not considered by the assessee for arriving at the aggregate procurement of the year. This suppression of turnover had not been detected by the assessing authority also. This resulted in short levy of ₹ 51.26 lakh (Tax: ₹ 43.38 lakh, cess: ₹ 0.43 lakh, interest: ₹ 7.45 lakh).

The case was pointed out (September 2012) to the Department and reported to Government in April 2013. Their reply has not been received (February 2014).

2.16.3 (CTO, Muvattupuzha)

Timber is classified as evasion prone and floor rate per cubic meter has been specified. CCT directed³⁵ the assessing authority to ensure that selling price of commodities for which floor rate has been fixed is based on valuation adopted for the purpose of advance tax.

M/s M.M Import and Export, a dealer in timber, paid ₹ 81.94 lakh towards advance tax on imported timber during

2010-11 as recorded in the annual return filed by them. Dealer conceded an import purchase of ₹ 3.41 crore and local purchase of ₹ 15.22 lakh only in the

³⁵ Circular No. 3/2008

annual return. Audit scrutiny of the assessment records revealed that the cost of goods sold would work out to ₹ 8.95 crore as per the rate computed for advance tax. However, tax was assessed on a turnover of ₹ 6.69 crore only. This resulted in short levy of ₹ 32.02 lakh (Tax: ₹ 28.31 lakh, cess: ₹ 0.28 lakh, interest: ₹ 3.43 lakh).

When this was pointed out (May 2012) in audit, the assessing authority replied (May 2012) that notice to assess the escaped turnover had been issued. Further report has not been received (February 2014).

This was reported to Government in November 2012. Their reply has not been received (February 2014).

2.16.4 (15 Offices; 20 cases)

Explanation VII under Section 2(lii) of the KVAT Act 2003, stipulates that where a dealer sells any goods purchased by him at a price lower than that at which it was purchased and subsequently receives any amount from any person towards reimbursement of the balance of the price, the amount so received shall be deemed to be turnover in respect of such goods. It was judicially held³⁶ that credit notes issued by the manufacturer to the distributor towards recoupment of additional sale price is for the goods sold by him and such cases clearly attracts Explanation VII.

Audit noticed between September 2011 and October 2012 that in 15 offices, the discount/incentive received in 20 cases were not reckoned as turnover for assessing to tax, though the dealers concerned sold goods purchased by them at price lower than that at which they were purchased. The assessing authority also did not assess to tax the above amount. This resulted in short levy of tax, cess and

interest of ₹ 1.38 crore as detailed in the following table:

Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	(₹ in lakh)	
				Discount, Incentive etc. received subsequent to sale	Tax, cess and interest leviable
1	M/s MV Sons Trading Company, Chelakkara CTO, Special Circle, Thrissur	2010-11 Cement 12.5%	Goods purchased for ₹ 25.35 crore was sold for ₹ 25.09 crore. The P&L account recorded that the assessee received discount of ₹ 2.95 crore subsequently. This was not assessed to tax. Short levy-(Tax ₹ 36.92 lakh, cess ₹ 0.37 lakh, interest ₹ 5.96 lakh).	295.33	43.25
The Government stated (September 2013) that assessment under Section 25(1) had been completed (October 2012) creating additional demand of ₹ 37.29 lakh. Reason for shortfall in additional demand created has not been furnished. Further report has not been received (February 2014).					

³⁶ Cement house Vs State of Kerala (High Court of Kerala)

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Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Discount, Incentive etc. received subsequent to sale	Tax, cess and interest leviable
2	M/s Silverstone Speciality Rubber Products Pvt. Ltd, <u>Malappuram</u> CTO, Special Circle, Malappuram	2010-11 Rubber products 4%	As per P&L account of the assessee for the year sales price and purchase value of goods sold during the year were ₹ 77.59 crore and ₹ 78.63 crore respectively. The assessee received ₹ 294.77 lakh by way of 'waste and shortage reimbursement' subsequent to sale. This was not assessed to tax. Short levy-(Tax ₹ 11.79 lakh, cess ₹ 0.12 lakh, interest ₹ 1.55 lakh).	294.77	13.46
Reply has not been received from the Department/Government (February 2014).					
3	M/s Hycount Marketing <u>Division, Aluva.</u> CTO, Special Circle, Mattancherry	2009-10 PVC pipes 4%	As per annual account filed by the assessee the sale price and purchase price were ₹ 16.55 crore and ₹ 17.91 crore respectively. As per P&L account sale price and purchase price including freight were ₹ 17.78 crore and ₹ 19.30 crore respectively. Receipt of discount of ₹ 1.86 crore was also recorded in the P&L account. This was not assessed to tax. Short levy-(Tax ₹ 7.44 lakh, cess ₹ 0.07 lakh, interest ₹ 1.65 lakh).	.185.85	9.16
The Department stated that notice had been issued to the assessee. Further report has not been received (February 2014).					
4	M/s Bright Glass Traders, <u>Kannur</u> CTO, Special Circle, Kannur	2009-10 Glass, Plywood 12.5%	As per P&L account purchase price of goods sold during the year including direct expenses was ₹ 6.98 crore and the sales price was ₹ 6.77 crore. The dealer received from their suppliers an amount of ₹ 57.92 lakh towards purchase rebate which was recorded in the P&L account. This was not assessed to tax. Short levy-(Tax ₹ 7.24 lakh, cess ₹ 0.07 lakh, interest ₹ 1.25 lakh).	57.92	8.56
Department stated (August 2013) that assessment had been completed (November 2012) creating additional demand of ₹ 9.58 lakh. Further report has not been received (February 2014).					
5	M/s High Range Home <u>appliances, Kattappana.</u> AIT & CTO, Kattappana	2009-10 Telephone, Television etc.	As per P&L account of the assessee for the year actual purchase price including direct expenses of goods sold was ₹ 10.05 crore and sales price	63.50	8.55

Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Discount, Incentive etc. received subsequent to sale	Tax, cess and interest leviable
		12.5% 4%	₹ 9.98 crore. Though they recorded in their P&L account the discount received as ₹ 63.50 lakh, same was not assessed to tax. Short levy -(Tax ₹ 6.94 lakh, cess ₹ 0.07 lakh, interest ₹ 1.54 lakh).		
	The Government stated (August 2013) that assessment had been completed (March 2013) creating additional demand of ₹ 9.32 lakh. The assessee had paid ₹ 2 lakh and requested for granting maximum number of instalments for payment of balance tax. Further report has not been received (February 2014).				
6	M/s Leo Agencies, Kannur CTO, III Circle, Kannur	2009-10 Electronic goods, air conditioners, washing machines etc. 12.5%	As per the P&L account of the assessee for the year the actual sales and purchase including direct expenses were ₹ 362.98 lakh and ₹ 363.37 lakh respectively. The P&L account also recorded 'scheme incentive' of ₹ 47.01 lakh received subsequent to sale. This was not assessed to tax. Short levy -(Tax ₹ 5.87 lakh, cess ₹ 0.06 lakh, interest ₹ 1.01 lakh).	47.01	6.94
	The Government stated (July 2013) that assessment had been completed (February 2013) creating total additional demand of ₹ 7.77 lakh. Further report has not been received (February 2014).				
7	M/s St. Jude Agencies, <u>Kollam</u> CTO, III Circle, Kollam	2010-11 White cement 12.5%	As per the P&L account of the assessee for the year the actual purchase value of the goods sold during the year including freight was ₹ 8.20 crore and sale price ₹ 8.06 crore. The P&L account also recorded discount and price difference of ₹ 42.70 lakh received subsequent to sale. This was not assessed to tax. Short levy - (Tax ₹ 5.34 lakh, cess ₹ 0.05 lakh, interest ₹ 0.70 lakh).	42.70	6.09
	The Government stated (July 2013) that assessment had been completed (June 2012) under Section 25(1) of KVAT Act, 2003 creating additional demand of ₹ 5.39 lakh and the same was advised for revenue recovery. Reason for shortfall in additional demand created has not been explained. Further report has not been received (February 2014).				
8	M/s Kizhakkedathu Agencies, Ranni AIT & CTO, Ranni	2009-10 Cement and white cement 12.5%	As per the P&L account of the assessee for the year the actual purchase value of the goods including freight and coolie was ₹ 413.29 lakh which was sold for ₹ 405.21 lakh. The dealer received discount of ₹ 28.01 lakh subsequent to sale from cement supplier. This was not assessed to tax. Short levy - (Tax ₹ 3.50 lakh, cess ₹ 0.04 lakh, interest ₹ 0.81 lakh).	28.01	4.35

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Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Discount, Incentive etc. received subsequent to sale	Tax, cess and interest leviable
	The Government stated (March 2013) that assessment was completed (December 2012) creating additional demand of ₹ 4.67 lakh. Further report has not been received (February 2014).				
9	<u>M/s AA Traders, Ayur</u> CTO, Anchal	2008-09 Cement 12.5%	As per the P&L account of the assessee for the years 2008-09 and 2009-10, purchase turnover including loading charges were ₹ 179.92 lakh and ₹ 286.45 lakh respectively which were sold for ₹ 177.53 lakh and ₹ 282.70 lakh respectively. They received ₹ 7.01 lakh and ₹ 20.89 lakh respectively during the years towards discount. These were not assessed to tax. Short levy - (Tax ₹ 3.49 lakh, cess ₹ 0.03 lakh, interest ₹ 0.78 lakh).	7.01	4.30
		2009-10 Cement 12.5%		20.89	
	The Government stated (October 2013) that assessment for 2008-09 and 2009-10 had been completed (June 2011 and August 2012) creating additional demand of ₹ 1.08 lakh and ₹ 3.40 lakh respectively. The assessee remitted ₹ 25,000. Further report has not been received (February 2014).				
10	<u>M/s Seethi Oil Mills,</u> <u>Kodungallur</u> CTO, Special Circle, Thrissur	2010-11 Cement 12.5%	During 2010-11, the assessee sold cement to retailers for ₹ 6.01 crore at a price lower than its purchase price of ₹ 6.20 crore. Audit scrutiny revealed that the assessee did not assess to tax incentive and discount of ₹ 27.98 lakh received subsequently by him from the suppliers. Though the amount so received shall form part of the turnover, the assessing authority also did not assess tax on the above turnover. Short levy - (Tax ₹ 3.50 lakh, cess ₹ 0.03 lakh, interest ₹ 0.53 lakh).	27.98	4.06
	Reply has not been received from the Department/Government (February 2014)				
11	<u>M/s Vachaparambil</u> <u>Agencies, Pulinkunnu</u> CTO, Haripad	2007-08 Cement 12.5%	As per the P&L account of the assessee for 2007-08 and 2009-10, the purchase price were ₹ 164.93 lakh and ₹ 271.17 lakh respectively which were sold for ₹ 163.97 lakh and ₹ 262.42 lakh respectively. They received trade commission of ₹ 5.99 lakh and ₹ 18.95 lakh respectively during the years but they were not assessed to tax. Short levy - (Tax ₹ 3.12 lakh, cess ₹ 0.03 lakh, interest ₹ 0.80 lakh).	5.99	3.95
		2009-10 Cement 12.5%		18.95	
	Reply has not been received from the Department/Government (February 2014).				

Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Discount, Incentive etc. received subsequent to sale	Tax, cess and interest leviable
12	Shri. Job T Varghese, <u>Kunnamkulam</u> CTO, Kunnamkulam	2009-10 Electrical Items, TV, Refrigerator etc. 12.5%	As per annual return filed by the assessee for the year the sale price and purchase price were ₹ 3.67 crore and ₹ 3.70 crore respectively. The P&L account also recorded discount of ₹ 22.75 lakh received from the suppliers subsequently. This was not assessed to tax. Short levy-(Tax ₹ 2.84 lakh, cess ₹ 0.03 lakh, interest ₹ 0.49 lakh).	22.75	3.36
The Government stated that assessment was completed (May 2012) creating additional demand of ₹ 4.07 lakh. Further report has not been received (February 2014).					
13	M/s Varoor Agencies, Ayoor CTO, Anchal	2009-10 Cement and white cement 12.5%	As per annual return and P&L account of the assessee for the year, the actual purchase price of the goods sold during the year including loading charges was ₹ 2.28 crore which was sold for ₹ 2.25 crore. The P&L account also recorded discount of ₹ 20.59 lakh received from the manufacturer subsequent to sale. This was not assessed to tax. Short levy - (Tax ₹ 2.57 lakh, cess ₹ 0.03 lakh, interest ₹ 0.49 lakh).	20.59	3.09
The Government stated (October 2013) that assessment had been completed (March 2012) creating additional demand of ₹ 3.17 lakh. An amount of ₹ 1.17 lakh has been remitted by the assessee. Further report has not been received (February 2014).					
14	M/s Western IT Distributors, <u>Ernakulam</u> CTO, IV Circle, Ernakulam	2010-11 Computer systems and electronic goods 12.5% 4%	As per annual return and P&L account of the assessee for the year, the actual purchase value of goods sold during the year including freight was ₹ 35.47 crore which was sold for ₹ 35.25 crore. Though the P&L account also recorded discount and incentive of ₹ 60.17 lakh received from the supplier subsequent to sale, same was not assessed to tax. Short levy- (Tax ₹ 2.51 lakh, cess ₹ 0.03 lakh, interest ₹ 0.43 lakh).	60.17	2.97
The Government stated (July 2013) that assessment had been completed (December 2012) creating additional demand of ₹ 4.68 lakh. Further report has not been received (February 2014).					
15	M/s Parali Paints and <u>Hardwares, Aluva</u> CTO, I Circle, Kalamassery	2010-11 Paints and hardwares 12.5%	As per annual return and P&L account, the sale price and purchase price were ₹ 2.14 crore and ₹ 2.16 crore respectively.	20.01	2.96

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Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Discount, Incentive etc. received subsequent to sale	Tax, cess and interest leviable
			The P&L account also recorded the discount of ₹ 20.01 lakh. This was not assessed to tax. Short levy - (Tax ₹ 2.50 lakh, cess ₹ 0.03 lakh, interest ₹ 0.43 lakh).		
	The Government stated (August 2013) that assessment had been completed (April 2013) creating additional demand of ₹ 3.13 lakh. Further report has not been received (February 2014).				
16	Shri. K.A. Noushad, Central <u>Electricals, Malappuram</u> CTO, Special Circle, Malappuram	2010-11 Cable, wiring materials, electronic items 12.5% 4%	As per the P&L account of the assessee, they sold goods for ₹ 9.06 crore which were purchased for ₹ 9.09 crore. The P&L account also recorded direct income of ₹ 38.17 lakh received from their suppliers. This was not assessed to tax. Short levy-(Tax ₹ 2.47 lakh, cess ₹ 0.02 lakh, interest ₹ 0.33 lakh).	38.17	2.82
	Reply has not been received from the Department/Government (February 2014).				
17	M/s Jyothis Hardwares, <u>Cherthala</u> CTO, Cherthala	2009-10 Cement and hardwares 12.5%	As per the P&L account of the assessee, they sold goods for ₹ 6.52 crore at a price lower than the purchase price including freight, of ₹ 6.61 crore. The P&L account also recorded discount of ₹ 17.61 lakh received from the cement suppliers. This was not assessed to tax. Short levy-(Tax ₹ 2.20 lakh, cess ₹ 0.02 lakh, interest ₹ 0.38 lakh).	17.61	2.60
	The Government stated (July 2013) that assessment had been completed (January 2012) creating additional demand of ₹ 2.67 lakh. Further report has not been received (February 2014).				
18	M/s Crescent Enterprises, <u>Kalamassery</u> CTO, I Circle, Kalamassery	2010-11 Paints and hardwares 12.5%	As per annual return and P&L account, the actual purchase price of the goods sold during the year was ₹ 210.33 lakh and the sales price was ₹ 204.17 lakh. The P&L account also recorded discount of ₹ 17.46 lakh received from the supplier. This was not assessed to tax. Short levy- (Tax ₹ 2.18 lakh, cess ₹ 0.02 lakh, interest ₹ 0.38 lakh).	17.46	2.58
	The Government stated (August 2013) that assessment had been completed (April 2013) creating additional demand of ₹ 2.73 lakh and RRC issued. Further report has not been received (February 2014).				
19	M/s Kattuvila Agencies, <u>Kollam</u> CTO, II Circle, Kollam	2010-11 Cement 12.5%	The annual return and P&L account disclosed that the actual purchase price of goods sold during the year was ₹ 304.47 lakh and sales price was ₹ 303.89	17.34	2.52

Sl. No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Discount, Incentive etc. received subsequent to sale	Tax, cess and interest leviable
			lakh. The P&L account also recorded discount of ₹ 17.34 lakh. This was not assessed to tax. Short levy (Tax ₹ 2.17 lakh, cess ₹ 0.02 lakh, interest ₹ 0.33 lakh).		
	The Government stated (July 2013) that assessment had been completed (July 2013) under Section 25(1) of KVAT Act, 2003 creating additional demand of ₹ 2.81 lakh and the same was advised for revenue recovery. The assessee remitted ₹ 0.28 lakh (April 2013). Further report has not been received (February 2014).				
20	M/s G.P Cements, <u>Kareelakulangara</u> CTO, Haripad	2009-10 Cements 12.5%	As per annual return and P&L account of the assessee, the actual purchase of goods sold during the year including labour charge was ₹ 2.77 crore which was sold for ₹ 2.68 crore. The P&L account also recorded the discount of ₹ 16.36 lakh received from cement suppliers. This was not assessed to tax. Short levy- (Tax ₹ 2.05 lakh, cess ₹ 0.02 lakh).	16.36	2.07
	Reply has not been received from the Department/Government (February 2014).				
				Total	137.64

2.16.5 (CTO Special Circle I, Ernakulam, Mattancherry, Kottayam)

Under explanation III(ii) below Section 2(lii) of KVAT Act, discount on the price allowed in respect of any sale can be excluded from the turnover only if it is shown separately in the tax invoice and the buyer pays only the amount reduced by such discount. It was judicially held that discount allowed subsequent to sale through credit note will form part of the turnover. Under Rule 10(b) of KVAT Rules, in respect of goods sold and returned, deduction from turnover will be admissible only if they are returned within a period of 90 days from the date of delivery of goods.

Audit noticed between April 2011 and November 2012 that in the following four cases, the turnover conceded in the annual returns were arrived at after deducting discount offered to customer through credit notes, sales return not proved etc. The assessing authority also did not assess to tax the above turnover. This resulted in short levy of tax, cess and interest of ₹ 1.11 crore as detailed below:

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(₹ in lakh)

Sl No.	Name of assessee Name of the circle	Period/ Commodity/ Rate(%)	Nature of irregularity	Tax, cess and interest leviable
1	<u>M/s Jos Electricals, Kochi</u> CTO, Special Circle, Mattancherry	2009-10 Electrical Goods 12.5%	In their P&L account for 2009-10, the turnover of ₹ 27.58 crore was arrived at after deducting discount offered to customers of ₹ 4.84 crore and sales return of ₹ 49.10 lakh, thus a total deduction of ₹ 5.33 crore. These deductions were not admissible since the discount was allowed subsequent to sale and eligibility for deduction of sales return was not proved. Short levy-(Tax ₹ 35.82 lakh, cess ₹ 0.36 lakh, interest ₹ 8.32 lakh.)	44.50
The Department stated (September 2012) that notice had been issued to the assessee to complete the assessment. Further report has not been received (February 2014).				
2	<u>M/s Redington India Ltd., Kochi</u> CTO, Special Circle I, Ernakulam	2010-11 Air conditioners, battery etc. 12.5%	The dealer was allowed tax credit of ₹ 35.21 lakh on account of credit note. However, no sales return was made as per Form 13A i.e. audited statement of accounts furnished by the dealer and sales turnover therein was less than that of annual return by ₹ 7.88 crore. Short levy-(Tax ₹ 35.21 lakh, cess ₹ 0.35 lakh, interest ₹ 6.05 lakh).	41.61
After this being pointed out to Government (January 2013) they stated (November 2013) that the assessment was completed under section 25(1) disallowing tax credit as pointed out by Audit. Collection particulars have not been intimated as offered by Government (February 2014).				
3	<u>M/s Ceyenar Chemicals Pvt. Ltd., Kottayam</u> CTO, Special Circle, Kottayam	2008-09 Chemicals, rubber sheet and rubber products 4%	The assessee had allowed trade discount of ₹ 4.08 crore on local sale. Since the discount allowed by the dealer was not included in the invoice, the discount allowed would form part of the turnover. However, neither the assessee nor the assessing authority assessed to tax the above turnover. Short levy-(Tax ₹ 16.32 lakh, cess ₹ 0.16 lakh, interest ₹ 3.95 lakh).	20.43
Government intimated that assessment was completed (November 2011) creating additional demand of ₹ 24.38 lakh. Further report has not been received (February 2014).				
4	<u>M/s Focus Corporation Pvt. Ltd, Kochi</u> CTO, Special Circle I, Ernakulam	2010-11 Motor Vehicles, automobile spare parts, computers etc. 12.5%	As per Form 13A, goods valued ₹ 3.12 crore were shown as goods returned within a period of ninety days. Against this the dealer claimed tax credit for ₹ 3.45 crore. The excess sales return of ₹ 33.13 lakh constituted discount allowed through credit notes for which deduction is not admissible. Short levy-(Tax ₹ 4.14 lakh, cess ₹ 0.04 lakh, interest ₹ 0.71 lakh).	4.89
Reply has not been received from Department/Government (February 2014).				
Total				111.43

2.16.6 (CTO, III Circle, Ernakulam)

Under Section 6(1) (c) of KVAT Act, transfer of right to use any goods for any purpose is taxable at four *per cent*. Royalty³⁷ received on intangible goods like copyright, patent etc., are also liable to be taxed as right to use.

M/s Sathyam Audios, Ernakulam was a dealer in audio and video CDs, tapes etc. Dealer filed annual return for 2009-10 conceding total and taxable turnover of ₹ 1.95 crore.

Audit scrutiny revealed that the assessee recorded in the P&L account a receipt of ₹ 4.57 crore by way of sales of video rights and royalty received which was not included in the taxable turnover shown in the annual return. This resulted in short levy of ₹ 22.69 lakh (Tax: ₹ 18.27 lakh, cess: ₹ 0.18 lakh, interest: ₹ 4.24 lakh).

The case was pointed out (March 2012) to the Department and reported to the Government in November 2012. Government stated (October 2013) that assessment had been completed (December 2012) creating additional demand of ₹ 24.38 lakh. The assessee remitted ₹ 7.37 lakh. Further report has not been received (February 2014).

2.16.7 (CTO, (WC<), Kannur)

Section 8 of the KVAT Act stipulates that any works contractor, may at his option instead of paying tax in accordance with the provisions of Section 6 of the said Act, pay tax at the compounded rate of three *per cent* of the whole contract amount received during 2009-10. Under Section 25 of the KVAT Act, an assessing authority can proceed to determine, to the best of its judgement, the turnover which has escaped assessment to tax and assess the tax payable thereon.

M/s Zewar Commercial Construction (P) Ltd. a works contractor, opted to pay tax at compounded rate of three *per cent* during 2009-10. They conceded a turnover of ₹ 2.97 crore as per annual return filed for the year 2009-10. But as per the P&L account for the year their income was ₹ 5.72 crore. This resulted in escape

of ₹ 2.75 crore from assessment and consequent short levy of ₹ 9.65 lakh (Tax: ₹ 8.24 lakh, cess: ₹ 0.08 lakh, interest: ₹ 1.33 lakh).

This was pointed out (August 2011) in audit to the Department and reported (April 2012) to Government. Government stated (September 2013) that assessment under section 25 of the Act had been completed (November 2012) by the assessing authority creating additional demand of ₹ 12.61 lakh. Further report has not been received (February 2014).

³⁷ [2009] 24 VST 333(Ker) KREEM Foods Pvt. Ltd Vs State of Kerala

2.16.8 (CTO, Special Circle Thiruvananthapuram)

Under Section 8 of KVAT Act, 2003, any dealer in ornaments or wares or articles of gold may at his option, instead of paying tax in accordance of provisions of Section 6, may pay at prescribed percentage of the highest tax payable or paid whichever is higher during any of the three consecutive years preceding that to which such option relates. Under Section 42(2) of the Act where any dealer detects any omission or mistake in the annual return submitted by him with reference to the audited figures, he shall file, along with the audit certificate, revised annual return rectifying the mistake or omission. Where as a result of such revision, the tax liability increases, the revised return shall be accompanied by proof of payment of such tax, interest due thereon and twice the interest as penal interest. Bullion is taxable at one *per cent* under the Act.

M/s Kalyan Jewellers, Trivandrum a dealer in gold opted for payment of tax under compounding scheme for jewellery items during 2009-10. For bullions and fancy items they had to pay tax at the full rate of one *per cent* and 12.5 *per cent* respectively. During 2009-10 the assessee conceded the turnover of bullion in the annual return as ₹ 4.36 crore. But as per P&L A/c for the year the turnover of bullion was ₹ 11.77

crore. Escape of turnover of bullion for ₹ 7.41 crore from assessment resulted in short levy of ₹ 8.91 lakh (Tax: ₹ 7.41 lakh, cess: ₹ 0.08 lakh, interest: ₹ 1.42 lakh).

This was pointed out to the Department in November 2011 and was reported to Government in November 2012. Government stated (October 2013) that assessment for the year 2009-10 had been reopened (June 2013) under Section 25 (1) of the KVAT Act 2003. Further report has not been received (February 2014).

2.16.9 (CTO (WC<), Kannur)

As per Section 8(a)(i) of the KVAT Act 2003, works contractor other than those registered under CST Act, 1956 or an importer can opt to pay compounded tax at three *per cent* of the whole contract amount. Rule 9(1) (c) of the KVAT Rules, 2005 further provides that the total turnover of a dealer shall be the aggregate of contract amount received or receivable.

M/s Udumbanthala Syndicate, Kannur was a works contractor who opted to pay compounded tax during 2009-10. They assessed to tax a turnover of ₹ 2.76 crore at three *per cent*. Audit scrutiny of balance sheet of the assessee revealed that they

received ₹ 4.21 crore as advance for flat during 2009-10. The assessing authority also did not assess to tax the entire turnover. This resulted in escape of turnover of ₹ 1.45 crore from assessment and consequent short levy of ₹ 5.08 lakh. (Tax: ₹ 4.34 lakh, cess: ₹ 0.04 lakh, interest: ₹ 0.70 lakh).

This was pointed out (August 2011) to the Department and reported to Government in April 2012. Government stated (October 2012) that assessment under section 25 of the Act had been completed (October 2012) creating additional demand of ₹ 2.66 lakh. The assessee paid ₹ 0.80 lakh. Further report has not been received (February 2014).

2.16.10 (CTO, Perinthalmanna)

Under Entry 67 of list of 12.5 *per cent* taxable goods notified³⁸ under KVAT Act, sale of bodies built on chassis of motor vehicles attracts tax @ 12.5 *per cent*. Hon. Supreme Court of India held³⁹ that construction of motor bodies on chassis supplied, is a contract for sale of goods and not a contract for work and labour.

M/s Taaz Tech, Kootilangadi is a dealer engaged in the construction of body on motor vehicles. They filed annual return for 2010-11 conceding a total and taxable turnover of ₹ 1.16 crore. They also recorded in their P&L account ₹ 31.68

lakh as labour charges received during the year. Since the construction of motor bodies on chassis supplied cannot be considered as works contract, the labour charges received should have been included in the annual return as taxable turnover. Failure to include labour charges received in the taxable turnover resulted in short levy of ₹ 4.64 lakh (Tax: ₹ 3.96 lakh, cess: ₹ 0.04 lakh, interest: ₹ 0.64 lakh).

When the case was reported (October 2012), Department replied (December 2012) that assessment had been modified (October 2012) creating an additional demand of ₹ 4.75 lakh. Further report has not been received (February 2014).

³⁸ SRO 82/2006

³⁹ MC Kenzies Ltd. Vs The State of Maharashtra 16 STC 518 (SC)

2.16.11 (CTO, Special Circle, Thrissur)

Under Section 2(xliv) of KVAT Act 2003, sale price includes any sum charged for anything done by the dealer in respect of the goods or service at the time of or before delivery thereof. Under Section 31(5) of the Act, failure to pay tax or any amount assessed or due, within the time prescribed attracts simple interest at the rate of twelve *per cent per annum*. Further, it was judicially held⁴⁰ by the Hon. Supreme Court of India that if the seller is under obligation to transport goods to the place of the buyer any incidental or transportation expenses charged will form part of the sale consideration.

M/s Best Ready Mix Concrete, a dealer of ready mix concrete conceded a total and taxable turnover of ₹ 16.72 crore⁴⁰ for 2010-11 as per the annual return filed by them. As per the assessment records of the assessee, they had an income of ₹ 23.95 lakh and ₹ 3.33 lakh towards concrete freight and pump charges respectively as recorded in their profit and loss accounts for the year 2010-11. But they did not

include in their sales turnover, freight and pump charge, though they were received in respect of services provided before delivery of goods. Escape of turnover of ₹ 27.28 lakh from assessment resulted in short levy of ₹ 4.03 lakh (Tax: ₹ 3.41 lakh, cess: ₹ 0.03 lakh, interest: ₹ 0.59 lakh).

The case was pointed out (September 2012) to the Department and was reported to Government in February 2013. Government stated (September 2013) that assessment had been completed and RRC issued (December 2012) for realising the additional demand of ₹ 4.13 lakh. The assessee paid ₹ 1.91 lakh. Further report has not been received (February 2014).

• (CTO, Special Circle, Perumbavoor)

M/s Vellackamattathil Industries, Kothamangalam was a manufacturer of pre stressed concrete poles. As per the annual return for the year 2010-11, the assessee self assessed to tax a turnover of ₹ 9.15 crore. As per the certified P & L accounts for 2010-11, the assessee received ₹ 83.05 lakh towards transportation charges. In the agreement with KSEB, it was stipulated that contract is for manufacture and supply including transportation to various electrical circles. As such the amount received towards transportation charges should form part of the turnover under the Act. But neither the assessee nor the assessing authority assessed to tax the above turnover. This resulted in short levy of ₹ 3.79 lakh (Tax: ₹ 3.32 lakh, cess: ₹ 0.03 lakh interest: ₹ 0.44 lakh).

The case was pointed out (July 2012) to the Department and to the Government in December 2012. The Government stated (May 2013) that the assessment had been completed (October 2012) creating an additional demand of ₹ 3.96 lakh and RRC

⁴⁰ 34 VST 2010(SC) India Meters Vs State of Tamil Nadu.

was advised for collecting the amount. Further report has not been received (February 2014).

2.17 Reckoning of sales as works contract and consequent short levy of tax

The assessee reckoned sales as works contract to reduce tax liability.

(CTO, Special Circle I, Ernakulam)

Explanation to Rule 10(2)(b) of KVAT Rules 2005 stipulates that no deductions shall be allowed out of the total contract amount for the supply and installation of any machinery equipment or any other system where the goods involved are assembled and installed and the labour employed for installation is only incidental to the supply of such goods. It was judicially held⁴¹ that if the major component of the end product is the material consumed in producing the chattel to be delivered and skill and labour are employed for converting the main components into the end products but the skill and labour are only incidentally used then the delivery of the end product by seller to the buyer will constitute a sale and not works contract.

M/s Voltas Ltd. Kochi was a dealer in AC, air cooler etc., and a works contractor for supply and installation of AC and air coolers. They filed a separate return, during 2009-10 conceding ₹ 13.45 crore as works contract receipts. They availed exemption of ₹ 3.15 crore and balance turnover of

₹ 10.30 crore only was assessed to tax. Sale considered incorrectly as works contract to avail inadmissible deduction resulted in short levy of ₹ 66.73 lakh (Tax: ₹ 55.52 lakh, cess: ₹ 0.56 lakh, interest: ₹ 10.65 lakh).

The case was pointed out (November 2011) in audit to the Department and reported to Government in November 2012. The Department stated (June 2012) that notice had been issued to the assessee. Further report has not been received (February 2014).

⁴¹ Kone Elevators (India) Pvt. Ltd. Vs. State of Andhra Pradesh [140 STC 22(SC)]

2.18 Incorrect reckoning of taxable turnover in works contract

Taxable turnover was not arrived at as stipulated in KVAT Rules resulting short levy of tax.

As per rule 10(2)(a) of the KVAT Rules 2005, in relation to works contract, in which transfer of property takes place not in the form of goods but in some other form, the taxable turnover in respect of the transfer of property involved in the execution of works contract shall be arrived at after deducting labour and other charges specified thereunder from the total amount received for the execution of the works contract. However, if the taxable turnover so arrived falls below the cost of goods transferred in the execution of works contract, an amount equal to the cost of goods transferred in the execution of works contract together with profit, if any, shall be the taxable turnover in respect of such works contract.

Audit noticed between October 2011 and February 2012 that, in the following five cases the works contractors conceded taxable turnover in their annual returns which were less than the turnover arrived at as per the provisions of KVAT Rules 2005. This resulted in short levy of tax, cess and interest of ₹ 66.72 lakh as detailed below.

(₹ in lakh)

Sl. No.	Name of assessee Name of the circle	Period	Nature of irregularity	Tax, cess and interest leviable
1	M/s Poonam Grah Nirman (Pvt.) Ltd, Ambalapuzha. CTO (WC<), Alappuzha	2009-10	The works contractor filed annual return for 2009-10 conceding a taxable turnover of ₹ 2.99 crore. Cost of goods transferred in the works contract was ₹ 5.11 crore. Gross profit conceded by the assessee being ₹ 1.43 lakh, the taxable turnover as per the provisions would come to ₹ 5.12 crore. However, the assessing authority has not taken any action to determine the taxable turnover as per the above provision. Short levy-(Tax ₹ 26.65 lakh, cess ₹ 0.27 lakh, interest ₹ 4.84 lakh).	31.76
The Government stated (February 2013) that assessment was completed (November 2012) under Section 25 of the KVAT Act. Further report has not been received (February 2014).				
2	Shri. Anas Babu. CTO (WC), Thiruvananthapuram	2008-09 2009-10	The works contractor filed annual return for 2008-09 and 2009-10 conceding taxable turnover of ₹ 88.53 lakh and ₹ 70.70 lakh respectively. Cost of goods transferred to the work during the years were ₹ 1.20 crore and	13.95

Sl. No.	Name of assessee Name of the circle	Period	Nature of irregularity	Tax, cess and interest leviable
			₹ 1.04 crore respectively. The taxable turnover as per the provisions would come to ₹ 1.32 crore and ₹ 1.15 crore. However, the assessing authority did not assess to tax the balance turnover. Short levy-(Tax ₹ 10.88 lakh, cess ₹ 0.11 lakh, interest ₹ 2.96 lakh).	
Department stated (April 2012) that the assessments for both the years had been revised (March 2012) creating additional demand of ₹ 9.29 lakh and ₹ 8.00 lakh. Further report has not been received (February 2014).				
3	M/s B. Ajith Kumar and K. Kamarudeen CTO, (WC<), Kollam	2009-10	The works contractors filed annual return for 2009-10 conceding taxable turnover of ₹ 32.75 lakh and ₹ 44.72 lakh respectively. Cost of goods transferred to the work of the above contractors during 2009-10 were ₹ 51.59 lakh and ₹ 93.25 lakh respectively. The taxable turnover as per the provisions would come to ₹ 65.40 lakh and ₹ 99.40 lakh (adding GP at the rates conceded as per their accounts). However, the assessing authority has not taken any action to determine the taxable turnover as per the above provision. Short levy-(Tax ₹ 10.92 lakh, cess ₹ 0.11 lakh, interest ₹ 2.42 lakh).	13.45
When this case was pointed out (July 2013) Government stated (December 2013) that assessment was revised creating additional demand of ₹ 6.90 lakh with interest and ₹ 3.50 lakh was collected. Further report has not been received (February 2014).				
4	Shri Anil Kumar G CTO (WC), Thiruvananthapuram	2009-10	The works contractor filed annual return for 2009-10 conceding a taxable turnover of ₹ 38.95 lakh. Cost of goods transferred to the work during the year was ₹ 48.83 lakh. The taxable turnover as per the provisions would come to ₹ 64.57 lakh (including the conceded GP of ₹ 15.74 lakh). However, the assessing authority did not assess to tax the balance turnover of ₹ 25.63 lakh. Short levy-(Tax ₹3.20 lakh, cess ₹ 0.03 lakh, interest ₹ 0.68 lakh).	3.91
Department stated (April 2012) that the assessment for the year had been revised (March 2012) creating additional demand of ₹ 2.01 lakh. Further report has not been received (February 2014).				
5	Shri. Alexander Oommen CTO (WC), Thiruvananthapuram	2009-10	The works contractor filed annual return for 2009-10 conceding taxable turnover of ₹ 83.92 lakh. Cost of goods transferred to the work during the year was ₹ 1.04 crore. The taxable turnover as per the provisions would	3.65

Sl. No.	Name of assessee Name of the circle	Period	Nature of irregularity	Tax, cess and interest leviable
			come to ₹ 1.08 crore including GP of ₹ 4.09 lakh. However, the assessing authority did not assess to tax the balance turnover of ₹ 23.89 lakh. Short levy-(Tax ₹ 2.99 lakh, cess ₹ 0.03 lakh, interest ₹ 0.63 lakh).	
Department stated (April 2012) that the assessment for the year had since been revised (March 2012) creating additional demand of ₹ 3.74 lakh. Further report has not been received (February 2014).				
Total				66.72

2.19 Short levy of tax due to incorrect computation of tax

Tax was levied at lower rate of three per cent against four per cent provided in the KVAT Act.

(CTO (WC<), Kozhikode)

As per first proviso under Section 8(a) (ii) of the KVAT Act, 2003, compounded tax applicable to work contactors having CST registration in respect of works contract awarded by Government of Kerala, Kerala Water Authority and Local Authorities shall be four *per cent* of the whole contract amount.

M/s Uralungal Labour Contract Co-operative Society, Vadakara an assessee undertaking works contract filed annual return conceding compounded taxable turnover of ₹ 49.52 crore. Audit scrutiny revealed that contract receipts amounting to ₹ 48.73 crore received from works awarded by Government of

Kerala were assessed to tax at three *per cent* instead of four *per cent*. This resulted in short levy of ₹ 48.31 lakh (Tax: ₹ 40.88 lakh, cess: ₹ 0.41 lakh, interest: ₹ 7.02 lakh).

This was pointed out (September, 2011) to Department and reported to Government in March 2012. Government replied that assessing authority completed the assessment of the society in April 2012. After adjusting the excess TDS of ₹ 16.96 lakh an additional demand of ₹ 26.69 lakh as tax and ₹ 6.41 lakh as interest had been created. Further report has not been received (February 2014).

2.20 Short levy of interest

The remittances made by the assessee were not appropriated first towards interest as per the provisions of Act resulting in short levy of interest.

(CTO, North Parur)

Under Section 31 (6) of KVAT Act, 2003 where any dealer has failed to include any turnover of his business in any return filed or where any turnover or tax has escaped assessment, interest for delay in payment shall accrue and the tax due on such turnover with effect from such date on which the tax would have fallen due for payment, had the dealer included the turnover in the return. Under Section 91 of the Act, when payment towards tax or any other amount due is made, it shall be appropriated first towards interest accrued, the balance available shall be appropriated towards principal outstanding.

M/s German Physical Laboratory, North Parur was a dealer in Agarbathi, Tea, Bed cover etc. The assessee filed annual return for 2005-06 disclosing total and taxable turnover of ₹ 7.32 lakh. Intelligence wing of the Commercial Taxes Department had conducted an inspection (September

2007) at the business place and detected turnover suppression. The assessee remitted ₹ 8 lakh and ₹ 5 lakh in November 2007 and March 2009 respectively. The assessing authority finalised the assessment in February 2009. However, while furnishing requisition to Revenue Recovery authorities (January 2010) remittances made in November 2007 and March 2009 were appropriated towards principal. Failure to levy interest on the tax due from May 2006 and appropriate remittances first towards interest, resulted in short demand of ₹ 8.28 lakh (Tax: ₹ 7.53 lakh, interest: ₹ 0.75 lakh).

The case was pointed out (February 2012) to the Department and to the Government in November 2012. Government stated (May 2013) that assessment was completed (June 2012) creating additional demand of ₹ 8.51 lakh and revenue recovery proceedings had been initiated against the dealer. Further report has not been received (February 2014).

2.21 Non-levy of surcharge

Surcharge leviable under Kerala Surcharge on Taxes Act was not levied.

(CTO, Aluva)

Under Section 3(1A) of the Kerala Surcharge on Taxes Act, 1957, in the case of national or multinational companies functioning in the state as retail chains or direct marketing chains who import not less than 50 per cent of their stock from outside the state or country, the tax payable under KVAT Act, 2003 on goods shall be increased by a surcharge at the rate of 10 per cent, if 75 per cent of the sales are retail business, and total turnover exceeds five crore rupees.

M/s Alga Marketing (P) Ltd., Aluva, a direct marketing chain, self assessed to tax turnover of nanometer energy cup, magnetic bracelets etc., at four per cent instead of 12.5 per cent during 2010-11. Assessing authority revised the assessment (June 2011) to set right the

misclassification. Though assessee is importing more than 50 per cent of its stock from outside the state and the items were sold to unregistered customers, the assessing authority failed to assess surcharge of ₹ 17.02 lakh on output tax of ₹ 1.70 crore. This resulted in short levy of surcharge and interest of ₹ 19.23 lakh (Surcharge: ₹ 17.02 lakh, interest: ₹ 2.21 lakh).

When the case was pointed out (May 2012) to the Department, it was stated that assessment had been revised (September 2012) creating additional demand of ₹ 19.61 lakh. The matter was reported to Government in November 2012; their reply has not been received (February 2014).

2.22 Non-assessment of tax on trade discount received

The quantity discount received by the assessee which formed part of turnover was not assessed to tax.

(CTO, Special Circle, Kannur)

As per Section 7 of KVAT Act, 2003 where a dealer allows any trade discount or incentive in terms of quantity in goods in relation to any sale effected by him, the quantity so allowed as trade discount or incentive, shall be deemed to be a sale by the dealer, who allows such trade discount or incentive and a purchase by the dealer who received such trade discount or incentive and such sale shall form part of the sale in relation to which such trade discount or incentive is allowed.

M/s ABC Associates, Kannur, a dealer in sanitary wares and fittings self assessed to tax a turnover of ₹ 11.80 crore during 2009-10. Audit scrutiny revealed that the assessee did not record in its annual

return the quantity discount⁴² amounting to ₹ 32.43 lakh received during the year and corresponding sales turnover was not assessed to tax. Though this discount was part of the turnover, the assessing authority did not assess to tax. This resulted in short levy of ₹ 5.09 lakh (Tax: ₹ 4.42 lakh, cess: ₹ 0.04 lakh, interest: ₹ 0.63 lakh).

This case was pointed out (June 2011) in audit to the Department and reported to Government in October 2012. Government stated (September 2013) that assessment had been completed (June 2013) creating additional demand of ₹ 4.52 lakh as tax and cess and ₹ 1.72 lakh as interest. Further report has not been received (February 2014).

⁴² Discount allowed in terms of goods instead of on price.

Sales Tax

2.23 Short levy of tax due to application of incorrect rate of tax

Rate of turnover tax applied on the taxable turnover was less than the rate applicable as per KGST Act.

2.23.1 (CTO, Special Circle, Palakkad)

Under Section 17 of the KGST Act if the return submitted by the dealer appears to be incorrect or incomplete, the assessing authority shall assess the dealer to the best of its judgement. Under rule 18(5) of Kerala General Sales Tax Rules, scrutiny of accounts is mandatory before final assessment of tax payable.

M/s Malabar cements Ltd., Palakkad, a cement manufacturing company conceded in the revised return 15 *per cent* taxable turnover for the year 2004-05 as ₹ 92.56 crore. The assessment was finalised (August 2010)

adding discount of ₹ 5.75 crore and freight charges of ₹ 10.46 crore to the 15 *per cent* taxable turnover. Reckoning proportionate addition made in respect of discount and freight the total turnover taxable at 15 *per cent* should have been ₹ 103.07 crore. But the turnover assessed to tax at 15 *per cent* was ₹ 77.73 crore only. The differential turnover was assessed to tax at lower rates of three, five and eight *per cent*. This resulted in short levy of ₹ 3.22 crore (Tax and AST: ₹ 1.80 crore, interest: ₹ 1.42 crore).

This was pointed out (November 2011) to the Department and reported (November 2012) to Government. Their reply has not been received (February 2014).

2.23.2 (CTO, Special Circle, Palakkad)

Under Section 8(2) (b) of Central Sales Tax Act, 1956 tax on interstate sale of goods other than declared goods not covered by declaration in Form C is 10 *per cent* or the rate applicable to sale or purchase of such goods inside appropriate state, whichever is higher. Under KGST Act 1963, sale of batteries attracted tax at 15 *per cent* under Sl. No. 13 of first schedule to the Act. For the year 2001-02 additional sales tax at 15 *per cent* of the tax is also leviable from 23 July 2001 under Section 5D of KGST Act.

The Central Sales Tax assessment for the year 2001-02 of M/s ITI Ltd., Kanjikode West, Palakkad a dealer engaged in manufacture and sale of batteries, was finalised (July 2010) assessing tax at 15 *per cent* for the interstate sale turnover of batteries for ₹ 13.09 crore for the period from 23 July 2001 to 31 March 2002

which was not covered by declaration in Form C without considering the additional sales tax of 15 *per cent* during the period. This resulted in short levy of ₹ 72.80 lakh (Tax and AST: ₹ 29.47 lakh, interest: ₹ 43.33 lakh).

This was pointed out (November 2011) to the Department and reported to Government in November 2012. Their reply has not been received (February 2014).

2.23.3 (CTO, Special Circle, Thiruvananthapuram)

Under Section 5(2)(1)(b) of the KGST Act, 1963 in force from April 2005 every dealer in foreign liquor other than bar attached hotel is liable to pay turnover tax at five *per cent* on turnover of foreign liquor. By a notification issued under the Act on 19 August 2005, turnover tax on sales turnover of IMFL by military, naval, air force and NCC canteen and canteen stores department was reduced to one *per cent*.

While finalising (March 2011), the turnover tax assessment of Unit Run (CSD) Canteen, Southern Air Command, Trivandrum a dealer in IMFL⁴³ for 2005-06, the sales turnover of IMFL for the period from 1 April 2005 to 18 August 2005 amounting to ₹ 1.37 crore was assessed to tax only at 0.5 *per cent* instead

of the correct rate of one *per cent*. This resulted in short levy of turnover tax and interest of ₹ 10.32 lakh (Turnover tax: ₹ 6.18 lakh, interest: ₹ 4.14 lakh).

The case was pointed out (November 2011) to the Department and to the Government in June 2013. Government stated (September 2013) that the mistake was rectified (December 2011) under Section 43 of KGST Act and the dealer had remitted turnover tax short levied as pointed out in audit. Details of remittance have not been received. But interest of ₹ 4.14 lakh pointed out in audit has not been realised. The amount of ₹ 6.83 lakh remitted by the assessee should have been adjusted towards interest leviable as on date of remittance. Details of recovery are awaited (February 2014).

⁴³ IMFL – Indian Made Foreign Liquor

2.24 Short levy of Interest

Interest leviable under KGST Act for delayed payment of tax was not levied.

2.24.1 (CTO, Special Circle, Thiruvananthapuram)

Under Section 23(3A) of KGST Act, where any dealer has failed to include any turnover of his business in the return filed or any turnover escaped assessment, interest under Section 23(3) shall accrue on the tax due on such turnover with effect from the date on which the tax would have fallen due for payment.

M/s Benoy Marbles and granites, Thiruvananthapuram was a dealer in marble, granites, ceramic tiles etc. When KVAT was introduced in 2005-06, the KGST assessments of Pre-VAT period 2002-03, 2003-04, 2004-05 of the assessee were

pending. These pending KGST assessments of the assessee were completed only in June 2010 under the 'fast track method'⁴⁴. While finalising the assessment, the suppression of turnover of ₹ 1.77 crore detected by the investigation branch (IB) was assessed to tax, but interest on tax due on turnover suppressed by the assessee was not demanded. This resulted in short levy of interest of ₹ 1.20 crore.

When this case was pointed out (December 2011) to Department, the assessing authority replied that as the assessee had not compounded the offence, there was no question of escape of turnover and the dealer was not liable to pay interest under section 23(3A). The reply is not correct as the quantum of suppression detected was established by the IB and the assessee paid tax due on suppressed turnover. As such the assessee is liable to pay interest under section 23 (3A) from the date on which tax was fallen due. The case was reported to Government in November 2012; their reply has not been received (February 2014).

• (CTO, Special Circle, Palakkad)

M/s Premier Agro Products (P) Ltd., Palakkad, was a dealer in wheat products. The original KGST assessment of the dealer for 1997-98 completed in June 2002 was modified on March 2007 and again modified on November 2008. When this assessment was further modified in March 2011 based on order of AC (Appeals), Palakkad, levying tax due of ₹ 48.32 lakh, interest was demanded only for eight months from March 2007 instead of from the date tax had fallen due for payment *i.e.* May 1998. This resulted in short levy of interest of ₹ 1.14 crore.

When this was pointed out (December 2011) in audit, the Department stated in September 2012 that the assessee is liable to pay interest only from April 2007 based on decision reported in 10 KTR⁴⁵ 476. The reply is not correct as the decision relates to interest under Section 23(3) and the objection relates to interest

⁴⁴ As per Kerala Finance Act 2007

⁴⁵ Kerala Tax Reporter

under section 23(3A). The decision in the case of PK Damodaran cannot also be applied here as the assessment was completed subsequent to over ruling of that case.

The case was reported to Government in November 2012, their reply has not been received (February 2014).

2.24.2 (CTO, Special Circle, Thiruvananthapuram)

Under section 23(3A) of the KGST, Act 1963 if any dealer has failed to include any turnover or taxable turnover of his business or to pay the tax due thereon, interest on the tax due on such turnover shall accrue with effect from the date on which the tax due would have fallen due for payment. Under section 55(c) of the Act, where any tax or any other amount due or demanded under the Act is paid, the payments so made shall be appropriated first towards interest accrued on such tax and the balance available shall be appropriated towards principal outstanding.

M/s Muthoot Hotels Private Ltd. (Taj Green Cove Resort), Kovalam was an assessee running a bar attached hotel of five star category. The assessee filed annual return for 2005-06 conceding a total and taxable turnover of ₹ 26.50

lakh. Intelligence wing of the commercial taxes department had conducted an inspection (March 2006) at the business place and detected turnover suppression. The assessee admitted the offence and compounded the same and remitted ₹ 74.09 lakh from October 2008 to December 2010. Audit scrutiny revealed that while finalising the assessment in March 2011 by fixing the total taxable turnover as ₹ 2.16 crore, the assessing authority adjusted these remittances towards principal. Failure to levy interest from May 2006, on tax due on the escaped turnover and appropriate remittances aggregating ₹ 74.09 lakh first towards interest resulted in short demand of balance tax and non-levy of interest thereon aggregating to ₹ 52.21 lakh.

When this case was pointed out (December 2011) in audit, the Department stated in April 2012 that the assessment was revised in April 2012 creating an additional demand of ₹ 53.60 lakh. Government stated (November 2013) that the assessee had paid (July 2012) ₹ 18.75 lakh towards the revised demand. Further report has not been received (February 2014).

- (CTO Special Circle, Thiruvananthapuram)

M/s Kovalam Hotels Private Ltd, (Now M/s Leela Ventures Kovalam) was a bar attached hotel of five star category. The assessee filed annual returns for 2005-06 conceding a total turnover of ₹ 115.61 lakh. Intelligence wing of the commercial taxes department had conducted an inspection at the business place and detected turnover suppression. The dealer admitted the offence and compounded the same and remitted ₹ 70.14 lakh from November 2008 to March 2009. Audit scrutiny revealed that while finalising the assessment in August 2010 by fixing the total turnover as ₹ 486.44 lakh assessing authority adjusted these remittances towards principal. Failure to levy interest from May 2006, on tax due on the escaped turnover and appropriate remittances aggregating ₹ 70.14 lakh first towards interest resulted in short demand of balance tax and non-levy of interest thereon aggregating to ₹ 32.10 lakh.

This case was pointed out (December 2011) to Department; the Department stated in April 2012 that the assessment was revised in April 2012 creating an additional demand of ₹ 34.14 lakh. Further report has not been received (February 2014).

2.25 Short levy of tax/penalty due to non-utilization of information in crime file for assessment

Details available in the crime files were not made use of while completing the assessments.

(CTO, III Circle, Thiruvananthapuram)

Section 17(4) of the KGST Act, 1963 provides for acceptance of return of some specified category of dealers without formal assessment. Under section 17(5A) if such assessment is reopened for assessment of escaped turnover or otherwise and tax paid by the dealer is found to be less than tax which he is liable to pay, the dealer should pay tax together with thrice the amount as penalty. Under Section 19(1) if whole or any part of a business of a dealer has escaped assessment, assessing authority may within five years from the expiry of the year to which tax relates proceed to determine to the best of its judgment, turnover which has escaped assessment and tax payable on such turnover.

M/s Christ Agencies, Valiyathura was a dealer in coconut oil, coconut cake etc. The KGST assessments of the dealer for the years 2002-03 and 2003-04 were completed under Section 17(4) by accepting the turnover returned by the assessee. The intelligence wing of the Department detected (February 2006) sales suppression of ₹ 1.22 crore and ₹ 22 lakh respectively in these years by the assessee. Intelligence Officer (IB), determined (July 2010) tax evaded in 2002-03 and 2003-04 as ₹ 5.63 lakh and ₹ 1.05 lakh

respectively and levied penalty of ₹ 11.26 lakh and ₹ 2.11 lakh. Assessing officer reported (November 2010) that as the crime files were received by him only in September 2009, contents of the same cannot be utilised for reopening of assessment as the case had become time barred. Failure of the Department to take prompt action resulted in non-realisation of revenue of ₹ 54.03 lakh. (Tax: ₹ 26.73 lakh, interest: ₹ 27.30 lakh).

The case was reported (January 2012) to the Department and to the Government in June 2013. Government stated (October 2013) that the assessment for 2002-03 and 2003-04 had since been revised on June 2013 and July 2013 respectively. Revenue recovery proceedings were initiated to recover the additional demand of ₹ 63.27 lakh. Further report has not been received (February 2014).

2.26 Short levy due to incorrect computation of compounded tax

While computing the compounded tax, rate was applied on incorrect turnover tax reckoned for previous year.

(CTO, Cherthala)

Section 7 of KGST Act, 1963, as amended from July 2006, stipulates that any bar attached hotel not being a star hotel, heritage hotel or club may, at its option pay tax on the turnover of foreign liquor calculated at one hundred and forty percent of the purchase value of such liquor or at one hundred and fifteen *per cent* of the highest turnover tax payable by it as conceded in the return or accounts or the turnover tax paid for any of the previous consecutive three years, whichever is higher.

M/s Keerthi Palace, Pattanakkad was an assessee engaged in the business of bar attached hotel. The assessing authority assessed turnover tax of ₹ 14.74 lakh during the year 2006-07. Audit scrutiny revealed that during the year 2007-08 instead of levying turnover tax at

115 *per cent* of ₹ 14.74 lakh, tax levied was only ₹ 14.74 lakh itself. Consequently turnover tax for 2008-09 was levied at 115 *per cent* of tax incorrectly arrived at for 2007-08. Thus for the years 2007-08 and 2008-09 turnover tax was assessed as ₹ 14.74 lakh and ₹ 19.13 lakh respectively instead of ₹ 16.95 lakh and ₹ 19.49 lakh considering 115 *per cent* of the tax paid during previous years. Incorrect computation of compounded tax resulted in short levy of ₹ 2.57 lakh.

The case was pointed out (October 2011) in audit to the Department and to the Government in June 2013. Government stated (September 2013) that assessments were revised creating total additional demand of ₹ 2.84 lakh and the entire demand was collected under revenue recovery. Further report has not been received (February 2014).