Report of the Comptroller and Auditor General of India for the year ended March 2016

Voluntary Compliance Encouragement Scheme, 2013

Union Government
Department of Revenue
Indirect Taxes – Service Tax
Report No. 22 of 2016

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Laid on the table of Lok Sabha/Rajya Sabha _____

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Preface

This Report has been prepared for submission to the President of India under Article 151 of the Constitution of India.

The Report contains significant results of the performance audit on Voluntary Compliance Encouragement Scheme, 2013 and covers the period from October 2007 to December 2012.

The instances mentioned in this Report are those which came to notice in the course of test audit conducted during the period 2015-16.

The audit has been conducted in conformity with the Auditing Standards issued by the Comptroller and Auditor General of India.

Audit wishes to acknowledge the cooperation received from the Department of Revenue, Central Board of Excise and Customs and its field formations at each stage of the audit process.

Executive summary

The Performance Audit on Service Tax Voluntary Compliance Encouragement Scheme, 2013 (VCES) was conducted in 35 selected Commissionerates to study whether the Scheme achieved its intended goals through seeking assurance regarding mechanism devised by the department for its implementation, addressing of the systemic failures that necessitated the VCES and monitoring of post-VCES compliance by the declarants.

The key aims of the scheme viz. encouraging non-filers or stop filers to file returns and tax base broadening were not achieved as only 66,072 existing as well as new registrants declared tax dues amounting to ₹ 7,750 crore under VCES as against 10,00,000 non/stop filers when the Scheme was announced and only around 22 per cent of the declarations filed related to new registrations. The Performance Audit revealed deficiencies in the design and enabling provisions of the Scheme, non-compliance to provisions prescribed in various stages and inadequacies in tax administration as detailed below:

a. The Scheme envisaged grant of immunity for truthful declaration of service tax dues. No basic documents in support of tax liability declared were prescribed and verification of correctness of declaration was restricted only to mere check of arithmetic accuracy. Even basic facts apparent on the face of the declaration were not verified.

(Paragraph 2.1.1)

b. Clarifications given by Board regarding pending demand notice, inquiry, audit or investigation, which would make the declarant ineligible for the scheme, were contradictory to the provisions and the intention of the scheme. This resulted in extension of unintended benefit amounting to ₹ 129.84 crore in 332 cases.

(Paragraphs 2.2.1, 2.2.2 and 2.2.3)

c. Deficient design of VCES application form and non-prescription of proper database by Board deprived department the benefit of having valuable data for post-Scheme analysis and monitoring.

(Paragraphs 2.3.1 and 2.3.3)

d. The safeguards prescribed in Cenvat Credit Rules, 2004, to avail Cenvat (input) credit were not given due consideration while making payments under VCES admissible for availing Cenvat credit in future.

(Paragraph 2.3.5)

e. In 444 cases in 20 Commissionerates, involving tax dues of ₹ 85.97 crore, we found deficiencies in verification of eligibility criteria.

(Paragraph 3.4)

f. We noticed in 169 cases, involving tax dues of ₹ 20.96 crore, that though the declarants had not paid the declared tax dues as per due dates prescribed, the declarations were not made ineligible for the scheme.

(Paragraphs 3.7 and 3.8)

g. Audit attempted to examine truthfulness of declarations made by cross-verification of declared tax dues in two commissionerates with details available with other authorities (viz. Income Tax Department, Commercial Taxes Department and Registrar of Companies) and found short declaration of tax dues to the extent of ₹ 4.35 crore in eight cases.

(Paragraph 4.2)

h. One time amnesty Scheme like VCES can be a real one time solution for the problem it sought to redress only if the tax systems are strengthened and follow up mechanism is made stringent. In 15 Commissionerates where data was made available to audit, we observed that only 62 per cent of the returns due for filing were actually filed post-VCES and no action was taken by the department against non-filers.

(Paragraph 4.3.1)

i. The department did not initiate any action to recover the balance of the declared tax dues or to levy applicable interest and penalty in respect of 78 rejected cases involving an amount of ₹ 23.02 crore.

(Paragraph 4.3.2)

j. The scheme was introduced with undue haste as the department responded with 'lack of time' to several audit observations.

(Paragraph 5.1)

Summary of Recommendations

Part-1 <u>Recommendations to be considered while framing any amnesty Schemes in future</u>

1. The use of IT platforms, integrated with the existing automated systems, for self declarations as well as scrutiny and follow up by the department for such Schemes may be considered.
2. Defining checklists for verifying the truthfulness of declaration filed by the declarants.
3. Identification of challans related to such schemes must be ensured by use of IT Platforms.
4. Provisions/clarification issued should not dilute the safeguards prescribed in the existing provisions as well as the express intention of the Scheme.

Part-2 <u>Recommendations for corrective action Post VCES</u>

5. Cenvat credit should be allowed in respect of only those service tax payments under this Scheme for which documents prescribed in rule 9 of Cenvat Credit Rules, 2004 are available.
6. The amnesty Scheme should be followed by an extensive drive to bring evaders to tax net through departmental investigation and vigilance wings, so as to send a strong message to the defaulters who did not come clean despite the Scheme, to have effective deterrent effect and also to boost morale of regular tax payers.
7. A rigorous follow-up procedure through monitoring of filing of returns and scrutiny of such returns should be ensured to facilitate success as well as impact assessment of the Scheme.

Chapter 1 : Introduction

1.1 Background

In Budget 2013 Speech, the Finance Minister disclosed that while there were nearly 17,00,000 registered assessees under service tax, only about 7,00,000 filed returns. He, therefore, proposed to introduce "Voluntary Compliance Encouragement Scheme, 2013" (VCES) in order to motivate the registered assessees, who had stopped filing returns, to file returns and pay the tax dues. As per VCES, a defaulter may avail of the Scheme on condition that he files a truthful declaration of service tax dues since 1 October 2007 and makes the payment in one or two installments before prescribed dates. The Finance Bill, 2013 further mentioned that "to encourage voluntary compliance and broaden the tax base, it is proposed to provide one time amnesty by way of (i) waiver of interest and penalty; and (ii) immunity from prosecution, to the stop filers, non-filers or non-registrants or service providers (who have not disclosed true liability in the returns filed by them during the period from October 2007 to December 2012) who pay the tax dues". Accordingly, the Finance Act, 2013 introduced the VCES.

The Scheme was effective from 10 May 2013 and was open up to 31 December 2013. The Scheme could be availed only by those to whom no show cause notice (SCN) or notice of audit or summons were issued prior to 1 March 2013. As per Scheme, if the assessee makes declaration and pays at least 50 per cent of the service tax dues before 31 December 2013 and balance before 30 June 2014, they get immunity from interest and penalty. If declarant does not pay the balance 50 per cent tax or part of unpaid tax dues by 30 June 2014, he was given an option to pay the same with interest by 31 December 2014. If declarant fails to pay the tax dues, either fully or in part, as declared by him, such dues along with interest[1] thereon shall be recovered under the provisions of Finance Act, 1994 and Finance Act, 2013.

1.2 Legal Provisions

1.2.1 VCE Scheme

The Scheme is covered in Chapter VI of the Finance Act, 2013 under Sections 104 to 114. The gist of major provisions of the Scheme are as under: -

[1] 15 per cent if value of taxable services is less than ₹ 60 lakh and 18 per cent if the value is ₹ 60 lakh or more.

❖ **Section 105 : Definitions**

- "Chapter" means chapter V of Finance Act, 1994
- "declarant" means any person who makes a declaration under sub-section (1) of section 107;
- "Designated Authority (DA)" means an officer not below the rank of Assistant Commissioner of Central Excise as notified by the Commissioner of Central Excise for the purposes of this Scheme;
- "tax dues" means the service tax due or payable under the Chapter or any other amount due or payable under section 73A thereof, for the period beginning from 1 October 2007 and ending on 31 December 2012 including a cess leviable thereon under any other Act for the time being in force, but not paid as on 1 March 2013.

❖ **Section 106 (1) : Person who may make declaration of tax dues**

- Any person may declare his tax dues if no notice or an order of determination has been issued or made on the same under section 72[2] or section 73[3] or section 73A[4] of the Chapter V of Finance Act, 1994 before 1 March 2013.
    - Provided if a notice or an order of determination has been issued to a person in respect of any period on any issue, no declaration shall be made of his tax dues on the same issue for any subsequent period.
    - Provided if any person has furnished return[5] and disclosed his true liability, but has not paid the same or any part thereof, he cannot make declaration for the period covered by the said return.

❖ **Section 106 (2) : Circumstances in which the DA shall reject such declaration, duly recording reasons**

a) If an inquiry or investigation in respect of a service tax not levied or not paid or short levied or short paid has been initiated by any of the following ways and such inquiry, investigation or audit is pending as on 1 March 2013:-

i) search of premises under section 82 of the Chapter; or

ii) issuance of summons under section 14 of the Central Excise Act, 1944, as made applicable to the Chapter under section 83 thereof; or

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[2] Section 72 deals with the assessment of value of taxable service

[3] Section 73 is regarding recovery of service tax not levied or paid or short levied or short paid or erroneously refunded

[4] Section 73 A deals with remittance of service tax

[5] Under section 70 of chapter V of Finance Act, 1994 - prescribed for furnishing of returns.

iii) requiring production of accounts, documents or other evidence under the Chapter or the rules made thereunder; or

b) an audit has been initiated.

❖ **Section 107 : Procedure for making declaration and payment of tax dues**

(1) Subject to the provisions of this Scheme, a person may make a declaration to the DA on or before 31 December 2013 in prescribed form and manner.

(2) The DA shall acknowledge the declaration in prescribed form and manner.

(3) The declarant shall pay at least 50per cent of the declared tax dues on or before 31 December 2013 and submit proof of such payment to the DA.

(4) The balance remaining unpaid after 31 December 2013 shall be paid by the declarant on or before 30 June 2014.

Provided in case of failure to pay the balance in full or part, he shall pay the same on or before 31 December 2014 along with interest as prescribed for the period of delay starting from the 1 July 2014.

(5) Notwithstanding anything contained in sub-section (3) and sub-section (4), any service tax which becomes due or payable by the declarant for the month of January 2013 and subsequent months shall be paid by him in normal course as per chapter V of Finance Act, 1994.

(6) The declarant shall furnish to the DA details of payment made from time to time under this Scheme along with a copy of acknowledgement issued to him.

(7) On furnishing the details of full payment of declared tax dues and the interest, if any, the DA shall issue an acknowledgement of discharge of such dues to the declarant as prescribed.

❖ **Section 108 : Immunity from penalty, interest and other proceeding**

(1) Notwithstanding anything contained in any provision of the Chapter, the declarant, upon payment of the declared tax dues and interest as applicable, shall get immunity from penalty, interest or any other proceeding under the Chapter.

(2) Subject to the provisions of section 111, a declaration made under VCES shall become conclusive upon issuance of acknowledgement of discharge and no matter shall be reopened thereafter in any proceedings under the Chapter or before any authority or Court relating to the period covered by such declaration.

❖ **Section 109 : No refund of amount paid under the Scheme**

Any amount paid in pursuance of a declaration made under VCES shall not be refundable under any circumstances.

❖ **Section 110 : Tax dues declared but not paid**

Where the declarant fails to pay the tax dues, either fully or in part, as declared by him, such dues along with interest thereon shall be recovered under the provisions of section 87 of the Chapter.

❖ **Section 111 : Failure to make true declaration**

In case the Commissioner of Central Excise has reasons to believe that the declaration made by a declarant under this Scheme was substantially false, he may, for reasons to be recorded in writing, serve a SCN on the declarant within one year from the date of declaration.

❖ **Section 112 : Removal of doubts**

It was clarified that the benefit, concession or immunity granted on is limited to that specified in section 108.

❖ **Section 113 : Power to remove difficulties**

If any difficulty arises in giving effect to the provisions of this Scheme, the Central Government may, by order, not inconsistent with the provisions of this Scheme, remove the difficulty. But, any such order can be issued only up to two years from the date on which the provisions of this Scheme come into force and shall be laid before each House of Parliament, as soon as may be after it is made.

1.2.2 STVCE Rules

Service Tax Voluntary Compliance Encouragement Rules, 2013 (STVCE Rules) were notified (May 2013) prescribing rules regarding the form and manner of declaration and its acknowledgement, payment of tax dues and of issuing acknowledgement of discharge of tax dues. Gist of Service Tax VCES Rules, 2013 are given below:

❖ **Rule 2(1) Definitions**

a) "Act" means the Finance Act, 2013;
b) "Form" means the Forms annexed to these rules;
c) "Scheme" means the Service Tax Voluntary Compliance Encouragement Scheme, 2013 as specified in the Act;

❖ **Rule 3 Registration**

Any person, who wishes to make a declaration under the Scheme, shall take registration.

❖ **Rule 4 Form of declaration**

The declaration of tax dues under the Scheme shall be made in Form VCES -1.

❖ **Rule 5 Form of acknowledgment of declaration**

The designated authority on receipt of declaration shall issue an acknowledgement thereof, in Form VCES -2, within a period of seven working days.

❖ **Rule 6 Payment of tax dues**

The tax dues payable under the Scheme along with interest, if any, under section 107 of the Act shall be paid to the credit of the Central Government. The Cenvat credit shall not be utilised for payment of tax dues under the Scheme.

❖ **Rule 7 Form of acknowledgement of discharge**

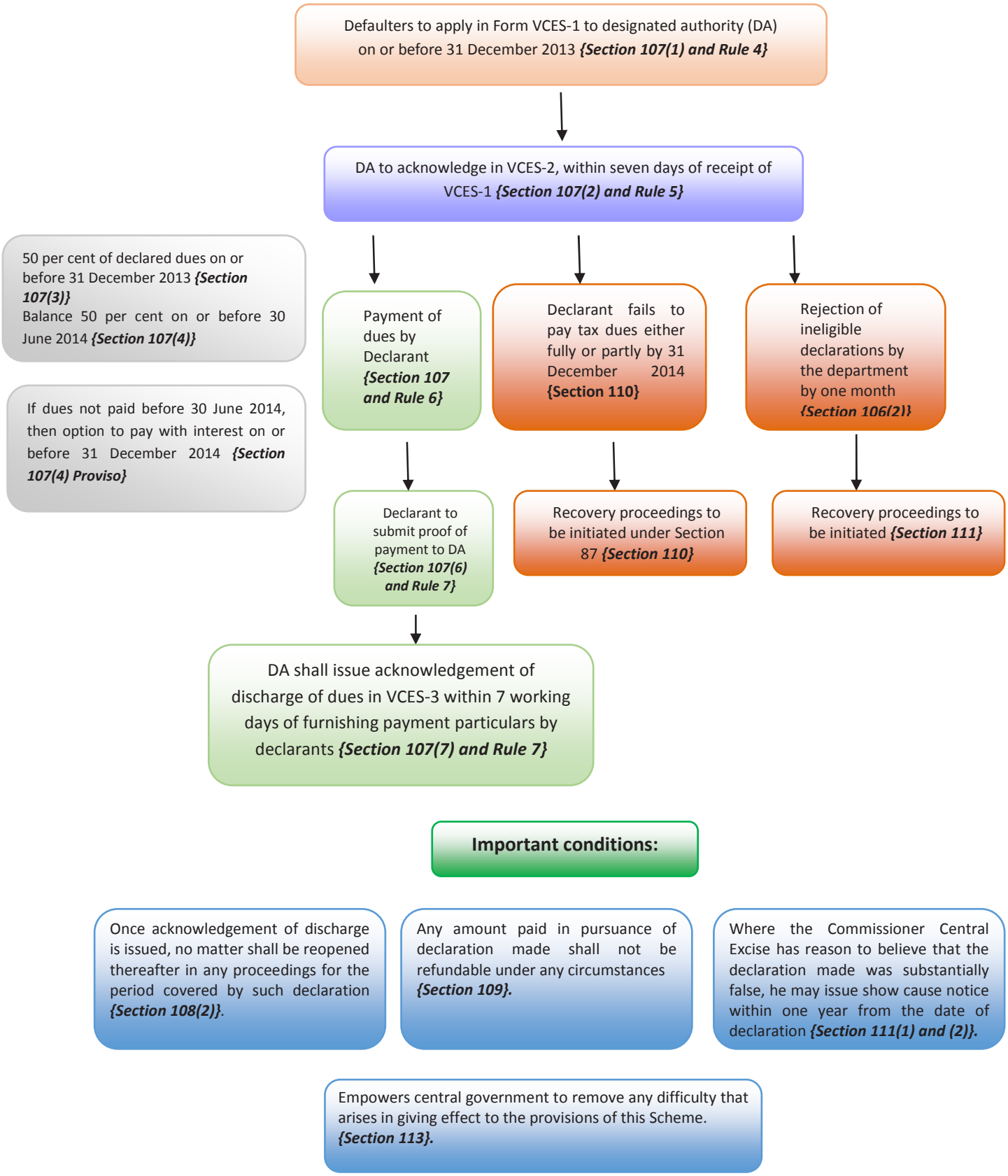
The designated authority shall issue an acknowledgement of discharge in Form VCES – 3 within a period of seven working days from the date of furnishing of details of payment of tax dues in full.

1.2.3 Circulars/Instructions issued by Board

Board issued clarifications in relation to this Scheme through various circulars/instructions dated 13 May 2013, 8 August 2013, 25 November 2013 and 11 December 2013.

The process envisaged in the legal provisions is depicted in flowchart 1.1.

Chart 1.1 : Flow chart on process prescribed for VCES



1.3 Why we chose this topic

This is an amnesty Scheme which was introduced for the first time after introduction of tax on services. As per Budget Speech of the Finance Minister delivered on 28 February 2013, the Scheme was aimed to motivate around 10,00,000 stop/non-filers to file returns and pay tax dues. However, only 66,072 declarations were received involving tax of ₹ 7,750.30 crore under this Scheme. In such a scenario, we felt that an independent assessment of the success of this Scheme was necessary.

1.4 Audit Objectives

The Performance Audit was conducted to study whether the Scheme achieved its intended goals through seeking assurance on whether:

(i) the mechanism devised by the Department for proper implementation and monitoring of VCES was in accordance with the guidelines of the Scheme;

(ii) systemic failures that necessitated the VCES had been duly addressed to improve the tax administration; and

(iii) proper mechanism was devised by the department to monitor compliance by the declarants subsequent to VCES Period.

1.5 Scope of audit and coverage

During the performance audit we selected and covered 35 Commissionerates[6] out of 145 Commissionerates and in the selected Commissionerates, 14,287 declarations out of 41,404 declarations were examined. The period of examination of this performance audit is from October 2007 to December 2012.

1.6 Acknowledgement

We acknowledge the co-operation extended by Central Board of Excise and Customs (CBEC) and its subordinate formations, in providing the necessary records for the conduct of this audit.

We discussed the audit objectives and scope of the performance audit in an entry conference with CBEC officers on 13 October 2015 and exit conference

[6] Ahmedabad-III, Ahmedabad-ST, Allahabad, Belagavi, Bengaluru-ST, Bhubaneswar-I, Chandigarh-I, Chennai-I ST, Chennai-II ST, Delhi-I, Delhi-III, Guntur, Gurgaon-ST, Guwahati, Hyderabad-ST, Indore, Jaipur, Jalandhar, Jamshedpur, Kanpur, Kochi, Kolhapur, Kolkata-I ST, Kolkata-II ST, Lucknow, Mumbai-II ST, Mumbai-VI ST, Mumbai-VII ST, Nashik-I, Patna, Pune-ST, Raipur, Rajkot, Salem and Vadodara-I

was held on 25 May 2016. The Ministry furnished the reply in May and June 2016 which were included in the report.

Chapter 2 : Design of the Scheme and enabling provisions

We analysed the objectives and intentions as brought out in the Scheme vis-à-vis the rules, clarifications and instructions issued by the Board to operationalise the Scheme. This analysis revealed that some of these enabling provisions/clarifications were contradictory to the objectives of the Scheme as discussed in subsequent paragraphs:-

2.1 Provisions to verify correctness of declarations

2.1.1 Verification of truthfulness of declaration made

As seen from the Finance Minister's budget speech for 2013-14, the Scheme envisaged that the tax defaulters will make a **truthful declaration** of service tax dues for which they would get a one time amnesty from payment of interest and penalty and immunity from prosecution.

In pursuance of this objective Section 107(1) of the Scheme, required declaration to be made in such form and manner as may be prescribed. Rule 4 of STVCE Rules prescribes form VCES-1 for filing declaration of tax dues and enclosures to VCES-1 as ***calculation sheet and any other records.*** The STVCE Rules, however, did not specify clearly the basic documents to be enclosed to VCES-1 in support of tax liability declared and it was left to the discretion of the declarant.

Board clarified vide letter dated 11 December 2013 that "the DA may cause arithmetical check as regards the correctness of computation of tax dues, the Scheme does not envisage investigation by the DA into the veracity of declaration." The basic provisions of the Scheme were thus negated by Board's clarification quoted ibid.

Verification of correctness of tax liability declared was, therefore, not done and verification was restricted to mere check of arithmetic accuracy.

We observed in 173 cases in 28 Commissionerates, involving tax dues of ₹ 23.13 crore, that the benefit of the Scheme was extended to the declarants, whose declarations had various discrepancies such as

- differences between calculation sheets and declarations made,
- grant of exemptions/abatements/deductions claimed under various notifications but had not furnished the required documents in support of exemption/abatement claims made by them,
- acceptance of amounts which did not fall under the definition of tax dues,

- wrong adoption of service tax rates.

When we pointed this out (between October 2015 and January 2016), the Ministry (May 2016) accepted the observation in 45 cases. The Ministry further stated (June 2016) that declarant was required to aver to the truthfulness of the declaration made and that the Scheme provided to reopen a declaration by the applicant only if found to be substantially false. They stated that it was not a Scheme for assessees to come forward and invite the departmental action against them and the circulars issued by the Board were in furtherance of the objectives of the Scheme. They further stated that only in a few cases commented upon by audit, substantially false information was given by the assessees on which due action was initiated by the respective Commissionerates and that the scheme had been largely successful otherwise.

The cases pointed out by audit here were those instances in which though the Scheme envisaged grant of immunity for truthful declarations, the same was granted by the department ***without verifying even basic facts which were apparent on the face of the declaration***. The number of cases pointed out by Audit being 'few' is not the point at issue, but of the department not carrying out even basic verification.

A few illustrative cases of non-verification of basic facts apparent on face of the declaration are given below:-

(a) Wrong claim of abatement/exemption

- An assessee in Mumbai-VII ST Commissionerate, declared (December 2013) tax dues of ₹ 85.43 lakh towards Works Contract service for the period April 2010 to December 2012. The declarant had incorrectly claimed abatement at 75 per cent amounting to ₹ 24.04 crore instead of admissible 60 per cent amounting to ₹ 19.23 crore. It resulted in excess claim of ₹ 4.81 crore, leading to short declaration of tax dues of ₹ 52.50 lakh.

  When we pointed this out (December 2015), the Ministry stated (May 2016) that the assessee paid service tax at the prevalent rate for the period i.e.10.30 per cent and there was no short payment of service tax. But the Ministry did not respond to our observation regarding excess availment of abatement.

- An assessee in Chennai-I ST Commissionerate, declared (December 2013) tax dues of ₹ 65.17 lakh for the period October 2007 to December 2012. VCES-3 was issued on 24 March 2015. The assessee deducted ₹ 10.70 crore towards exempted service, from the taxable

value. The correctness of such substantial amount of exemption claimed was not verified by the Department before issuing discharge certificate (VCES-3).

When we pointed this out (January 2016), the Ministry stated (May 2016) that VCES Scheme did not envisage investigation by the DA.

(b) Wrongful inclusion of tax dues

An assessee in Bengaluru ST Commissionerate, declared (December 2013) tax dues of ₹ 13.54 lakh for the period October 2007 to March 2011. On verification of the payment details furnished by the declarant along with the declaration, it was seen that entire amount of ₹ 13.54 lakh had been discharged during January/February 2013 itself and no amount was pending as on 1 March 2013. As the tax dues declared under VCES is defined as an amount due for the VCES period but not paid as on 1 March 2013, the declarant did not qualify for the Scheme. Department was required to initiate action for recovery of interest and penalty as service tax pertaining to period October 2007 to March 2011 was paid in January/February 2013 with inordinate delay. However, no details of initiation of action taken were forthcoming from the records.

When we pointed this out (December 2015), the Ministry agreed with audit observation and stated that the assessee was not traceable.

(c) Incorrect adoption of Service Tax Rate

An assessee in Rajkot Commissionerate, declared (October 2013) tax dues of ₹ 1.22 crore for the period from October 2008 to March 2012. The assessee, while calculating the tax liability for the year 2008-09, calculated service tax at the rate of 10.30 per cent instead of 12.36 per cent. The incorrect adoption of Service Tax rate resulted in short payment of service tax of ₹ 12.49 lakh. The department issued VCES-3 (February 2015) to the declarant without verifying the correctness of the tax payment.

When we pointed this out (October 2015), the Ministry stated (May 2016) that VCES Scheme did not envisage investigation by the DA. The reply implied that basic checks like application of correct tax rates were not exercised while processing VCES application.

2.1.2 Non-stipulation of timeline for furnishing payment details

No time limit was stipulated for submission of payment particulars by the declarants to the department for taking timely action for recovery of defaulted dues.

We noticed delay, ranging between 1 and 644 days, in submission of payment particulars by the declarants to the department in 1,852 cases in 22 Commissionerates.

We noticed from the selected VCES files in 98 cases Belagavi (21) and Bengaluru ST (77), no details were kept on record indicating the payment of service tax dues declared under VCES, either paid in full or in part and hence the discharge certificates in VCES-3 had not been issued. It is further noticed in Bengaluru-ST Commissionerate department had addressed letters to 17 declarants, calling for the payment particulars from the declarants along with proof of payment. This was indicative of the fact that the department was not in a position to ascertain whether these declarants had paid the tax dues within the due dates to become eligible under the Scheme, even after a lapse of more than one year.

In the absence of mechanism to distinctly identify payments made under VCES, the department is totally dependent on assessees' response regarding their payment.

When we pointed this out (between October 2015 and January 2016), the Ministry, while admitting (June 2016) that non-stipulation of such time limit certainly caused delay in closure of the VCES cases, stated that fixation of a rigid time limit would have lead to disputes in cases where payment was made but the details submitted beyond the stipulated date. In such cases it would have been incorrect to deny substantive benefits owing to a procedural lapse. Further it stated the deposits made by the declarants were ascertained from assessee-wise details available on the NSDL site.

Audit finds Ministry's contention about time schedules leading to denial of substantial benefits misplaced. Fixation of time limit for submission of challans by declarants would not lead to denial of the benefits to the declarants since on the receipt of the same, the department was to issue VCES-3 to the declarants. Further, the NSDL site contained the regular as well as VCES related tax payment details with no facility to differentiate between the two.

2.2 Provisions regarding eligibility for the Scheme

We correlated the conditions prescribed in the Scheme to declare a person ineligible with the related clarifications/instructions issued by the Board and we noticed that the clarifications/instruction issued by the Board diluted the conditions prescribed in the Scheme as discussed in subsequent paragraphs.

2.2.1 Extension of benefits to declarants against whom inquiry, investigation or audit was initiated prior to 1 March 2013

Section 106(2)(a)(iii) stipulates that where a declaration has been made by a person against whom inquiry, investigation or audit has been initiated and the same is pending as on 1 March 2013, then, the DA shall, by an order, and for reasons to be recorded in writing, reject such declaration. Board clarified (August 2013) that the provisions of Section 106(2)(a)(iii) shall be attracted only in such cases where accounts, documents or other evidences are requisitioned by the authorised officer from the declarant under the authority of statutory provisions (viz. section 14 of Central Excise Act, 1944 Section 72 of Finance Act, 1994 and Rule 5A of Service Tax Rules, 1994) and the inquiry so initiated against the declarant is pending as on 1 March 2013. No other communication from the department would attract the provisions of section 106(2)(a)(iii) and thus would not lead to rejection of the declaration.

Section 106(2)(b) stipulated that where a declaration was made by a person against whom an audit had been initiated and the same was pending as on 1 March 2013, such a declaration was liable for rejection.

Board's clarification[7] (August 2013) that the date of the visit of auditors to the unit of the taxpayer would be taken as the date of initiation of audit diluted the provisions of Section 106(2).

We noticed that in 12 cases in eight Commissionerates, involving declared dues of ₹ 4.43 crore though action had been initiated against the declarants in terms of Section 106(2)(iii) much before 1 March 2013, they were extended the immunity benefits under VCES, in view of Board's clarification dated 8 August 2013 which resulted in loss of revenue to Government by way of interest and penalty.

When we pointed this out (between October 2015 and January 2016), the Ministry stated (June 2016) that the clarifications aimed at giving effect to the object and purpose of the Scheme by excluding simple letter / general query seeking the information or a unit earmarked but not audited from the ambit of "initiation of audit or investigation".

Audit is of the view that the clarification of the Board resulted in extension of VCES benefits even to cases where audit or inquiry were based on valid information or proper analysis and were not merely simple letters seeking general information. Thus the provisions of the Scheme were defeated.

[7] At Sl. Nos. 1 and 19 of Board's circular No.170/5/2013-ST dated 8 August 2013

Ministry further replied (June 2016) that specific decisions on VCES applications were taken by the DA after considering the prevailing conditions and thus the inquiry in the cases pointed out by audit could not be considered as specific or of roving nature. They also stated that success of VCES to collect revenue without litigation should be considered the mainstay of this scheme instead of procedural detailing.

Ministry contention could not be accepted as field formations, while responding (May 2016) to specific cases pointed out by audit, replied that they followed Board instruction regarding cut-off date in dealing with VCES application. Further VCES objective was to encourage service providers to file returns and not meant for litigation management.

A few illustrative cases are given below:-

2.2.1.1 An assessee in Belagavi Commissionerate, declared (September 2013) tax dues of ₹ 1.56 crore under the category of 'Minimum Take Or Pay charges' (MTOP), for the period from July 2012 to December 2012.

In this connection, it was seen in audit that the Jurisdictional Range Officer had made correspondence with the declarant regarding service tax liability on MTOP charges way back in September 2012 itself, followed by periodical correspondence and hence had proposed for rejection of the declaration. However, the DA dropped the proposal for rejection of the declaration, holding that mere correspondence with the declarant would not attract the provisions of Section 106(2)(a)(iii), in the light of the Board's clarification cited supra. Subsequently, acknowledgment in VCES-2 was issued to the declarant on 24 December 2013.

When we pointed this out (October 2015), the Ministry stated (May 2016) that after careful examination of all the facts and documents, the rejection proceeding were dropped by DA.

The reply of the Ministry could not be accepted as service tax on MTOP charges was not disclosed by declarant voluntarily and calling for specific information by the Range Officer could not be termed "mere correspondence".

2.2.1.2 An assessee in Chennai-I ST Commissionerate, declared (December 2013) tax dues of ₹ 1.03 crore in respect of renting of immovable property service for the period from 2008-09 to 2012-13. Survey, Intelligence and Research Cell (SIR Cell) initiated (December 2012) enquiry against him for non-payment of service tax on the same service by calling for details/documents such as audited financials records from 2007-08 to 2011-12, trial balance from April 2012 to September 2012 and details of other commercial properties owned, rented by him etc., and also issued a

reminder (January 2013). Thus the enquiry by way of calling for information from against the declarant was pending as on 1 March 2013. However, VCES-3 was issued to the assesse (July 2014).

When we pointed this out (January 2016), the Ministry stated (May 2016) that as per Board's circular dated 25 November 2013, the DA/Commissioner could decide depending on the facts and circumstances of each case as to whether the inquiry was of roving nature or the provisions of Section 106(2) was attracted in such cases. Since there was no specific instruction from the Commissioner for making this declarant ineligible under VCES, the declared amount was accepted and discharge certificate was issued.

The reply of the Ministry was not acceptable since the enquiry in this case was very specific and thus made the declarant ineligible for VCES.

2.2.1.3 An assessee in Guntur Commissionerate, declared (December 2013) tax dues of ₹ 5.92 lakh under VCES. We noticed that internal audit of the assessee unit was conducted (March 2013), for which an audit intimation letter was sent to the assessee well before 1 March 2013 and audit observations involving tax effect of ₹ 17.17 lakh were also issued. However, VCES-3 was issued (May 2014).

When we pointed this out (December 2015), the Ministry stated (May 2016) that as per Board's circular dated 8 August 2013 the date of visit of auditors to the unit of the tax payer would be taken as the date of initiation of audit.

As pointed out already the clarification resulted in extension of benefit even to cases where audit or enquiry were based on valid information or proper analysis as the audit did lead to raising of audit observations with tax effect.

2.2.2 Extension of benefits to declarants against whom SCNs were issued prior to October 2007

Section 106(1) stipulates that, any person may declare his tax dues in respect of which no notice or an order of determination under section 72 or section 73 or section 73A of the Chapter has been issued or made before 1 March 2013. It further "Provided that where a notice or an order of determination has been issued to a person in respect of any period on any issue, no declaration shall be made of his tax dues on the same issue for any subsequent period".

Board clarified[8] (August 2013) that as relevant period for VCES is October 2007 to December 2012, issuance of a SCN or order of determination for any period prior to October 2007, on an issue, would not make a person

[8] Vide point (5) of Board Circular No.170/5/2013-ST dated 8 August 2013

ineligible. Thus the Board's clarification is contradictory to the intention of the Finance Act, 2013.

We noticed in 20 cases, in 10 Commissionerates involving tax dues of ₹ 16.32 crore, though the department had issued SCNs, covering the period prior to the period of declarations, the declarants were allowed to avail the benefit of VCES, in view of the contrary clarification of the Board.

When we pointed this out (between October 2015 and January 2016), the Ministry (June 2016) quoted definition of tax dues and that section 106(1) deals with a person who may declare his tax dues. They further stated that both the provisos of Section 106 (1) should be read with the main clause and then it would imply that notices issued for the period prior to 1 October 2007 would not make the declaration ineligible for VCES.

Audit's appreciation of the provision is that the tax dues were defined only to limit the period relating to which unpaid taxes can be declared under VCES and therefore is unable to accept the department's stance about the definition having a bearing on pending notices or inquiry detailed in section 106(1).

A few illustrative cases are given below:-

2.2.2.1 An assessee in Belagavi Commissionerate, declared (December 2013) tax dues of ₹ 6.38 crore towards banking and other financial services, for the period April 2012 to June 2012 and paid the entire dues declared on 28 December 2013. Accordingly, VCES-3 was issued (August 2014) to the declarant.

We noticed that DGCEI, Mumbai had registered an offence case against the declarant on the same issue for the period from August 2006 to June 2007 and the demand was also confirmed.

When we pointed this out (October 2015), the Ministry stated (June 2016) that as per Board's circular dated 8 August 2013 the declarant was eligible to make declaration under the Scheme if SCN was issued for any period prior to October 2007.

The reply of the Ministry is not acceptable as Board's clarification is contradictory to the section 106(1) of the Finance Act, 2013.

2.2.2.2 An assessee in Kochi Commissionerate, declared (December 2013) tax due of ₹ 1.80 crore towards works contract service, for the period April 2012 to December 2012. We noticed that two SCNs had been issued for the previous period, one in January 2012, for the period October 2007 to September 2010 and another in April 2012, for the period October 2010 to

September 2011 for non/short payment of service tax under works contract service.

When we pointed this out (November 2015), the Ministry initially stated (May 2016) that though the SCNs were issued under works contract service but the issue was for availing ineligible exemption for different projects. Later Ministry (June 2016) took a stand that section talked about ineligibility under the scheme for declaration made for the same issue and not for the same category of service.

The reply of the Ministry was not tenable since VCES Scheme did not allow different treatment of projects falling under the same service i.e., works contract service. Further, the issue is also same in this case i.e., availing of ineligible exemption.

2.2.2.3 An assessee in Kochi Commissionerate, declared (September 2013) tax dues of ₹ 1.43 crore towards erection and commissioning service for the period April 2010 to December 2012. We noticed that Order-in-original was passed in respect of assessee for non-payment of service tax of ₹ 56.46 lakh towards the same service for the period from July 2003 to March 2006.

This was brought to the notice of the department/Ministry (December 2015) and the reply of the department/Ministry was awaited (May 2016).

2.2.2.4 An assessee in Rajkot Commissionerate, declared (December 2013) tax dues of ₹ 28.34 lakh towards construction services other than residential complex, for the period April 2008 to December 2012. VCES-3 was issued (December 2014) to the declarant. We noticed that an SCN had been issued on the same issue, for the period prior to November 2005.

When we pointed this out (October 2015), the Ministry stated (June 2016) that as per Board's circular of August 2013, the assessee was eligible for VCES.

Audit observed that in all the above cases, the department allowed the assessees to take the benefit under VCES though similar issues were noticed by the department for the earlier period. This also indicates that the department's wrong clarification resulted in undoing the intent of the provisions of Section 106 (1) of the Scheme.

2.2.3 Extension of benefits to declarants against whom inquiry, investigation or audit was initiated after 1 March 2013

The Scheme stipulated rejection of those declarations made by persons against whom inquiry, investigation or audit has been initiated and is pending as on 1 March 2013. It appears that neither Board envisaged nor field sought Board's intervention later regarding procedure to be followed in case assessees apply for VCES after initiation of audit inquiry or issue of notice after 1 March 2013 and during the operation of VCES. This resulted in extension of undue benefit to those declarations made subsequent to initiation of audit/investigation, which are not "voluntary".

We noticed that in 300 cases in 23 Commissionerates, involving tax dues of ₹ 109.09 crore, action had been initiated against the declarants by Internal Audit/CERA/Anti-Evasion/Preventive/DGCEI, subsequent to 1 March 2013 but prior to the dates of declaration and these declarants were extended the benefit under VCES, in view of the cut-off date of 1 March 2013 stipulated in the Finance Act, 2013.

A few illustrative cases are given below:-

2.2.3.1 An assessee in Mumbai-VI ST Commissionerate, declared (December 2013) tax dues of ₹ 6.96 crore towards supply of tangible goods for the period 2008-09, 2009-10 and 2012-13 (upto December 2012). On verification we noticed from the verification report received from the jurisdictional division dated 1 January 2014 an investigation had been initiated against the declarant by Anti Evasion, Vishakhapatnam-II Commissionerate on 12 March 2013 and subsequently, the assessee had made declaration under VCES.

When we pointed this out (December 2015), the Ministry stated (May 2016) that this being a policy matter, no action was warranted.

2.2.3.2 An assessee in Chennai-II ST Commissionerate, declared (September 2013) tax dues of ₹ 4.74 crore towards selling of space or time services, for the period June 2010 to March 2012**.** We noticed that Survey, Intelligence and Research (SIR) Cell had called for details like copies of balance sheets for the period from 2009-10 to 2012-13, copies of ST-3 returns filed, from the assessee regarding service tax on 29 August 2013 and 16 September 2013.

When we pointed this out (December 2015), the Ministry stated (May 2016) that there was no bar from filing of declaration in cases where enquiry, investigation or audit was initiated after 1 March 2013.

2.2.3.3 An assessee in Bengaluru ST Commissionerate, declared (June 2013) tax dues of ₹ 1.62 crore towards rent a cab services for period April 2008 to March 2012. The tax declared included the amount of ₹ 1.38 crore with

interest of ₹ 44.07 lakh pointed out by CERA, during the course of audit (May 2013) for the period from April 2008 to March 2012.

When we pointed this out (January 2016), the Ministry stated (May 2016) that since no audit or investigation was initiated before 1 March 2013, there was no restriction for the declarant to declare their tax dues under VCES.

2.2.3.4 An assessee in Kolkata-I ST Commissionerate declared tax dues of ₹ 1.09 crore on 29 November 2013 and ₹ 0.91 crore on 9 December 2013, for period April 2008 to December 2012, under the category of income from operations. VCES-3 was issued (April 2015).

We noticed that a search operation was conducted by the DGCEI, Kolkata Zonal Unit on 29 November 2013, which had resulted in detection of service tax evasion to the tune of ₹ 2.49 crore for the period from 2008-09 to 2012-13. As the date of detection on service tax evasion fell beyond 1 March 2013, the declarant was extended the benefit of immunity under VCES.

When we pointed this out (October 2015), the Ministry stated (May 2016) that as DGCEI initiated search operations after 1 March 2013, the declaration under VCES was in order.

Audit observed in all the above cases, declarations were made after detection by some authority and hence could not be termed voluntary. Due to the cut-off date of 1 March 2013 under Section 106(1) of the Finance Act, 2013, even in such cases which were already in the knowledge of the department, the declarants were allowed the benefit under the Scheme despite the fact that the declarations were not voluntary. Thus the said cut-off date resulted in extending undue benefit to the declarant by way of immunity from interest, penalty and other proceedings. Some of the declarants, as discussed, exercised the VCES option only to escape action under the normal rules regarding their undisclosed tax liability.

When we pointed this out (between October 2015 to January 2016), the Ministry while noting the audit contention stated (June 2016) that the Scheme did not bar the declarants in respect of whom the inquiry, audit or investigations was initiated after 1 March 2013 from availing the benefits under the Scheme and right of the assessees to opt for discharge of the dues under the VCES could not be denied.

Ministry's contention reflected point made by audit regarding shortcoming in the Scheme in respect of cases in which action was initiated by department after 1 March 2013 and perhaps a fit case calling for action under section 113.

Audit observed that the spirit of the Scheme and its purpose were compromised by department's restrictive defining of cut-off date vide the August 2013 circular and a short coming regarding cases initiated post 1 March 2013, which could have been addressed by invoking section 113. Thus the results of regular compliance verification mechanisms of the department post 1 March 2013 also ended up as VCES declarations.

2.3 Mechanism designed to implement provisions of the Scheme

2.3.1 Deficiency in Form VCES-1

Form VCES-1 did not specify status of declarants like Stop-filers, Non-filers, New Registrants or Active filers. Similarly, the information like date of registration and capacity in which declaration made (as service provider or recipient) were also not required to be furnished. For submission of calculation sheet along with VCES-1, it was merely mentioned that the existing format for calculation of tax dues as prescribed in ST-3 return may be used and no standard format was prescribed. In the absence of basic information regarding the declarants, the department was incapable of carrying out the due diligence on the declarations as discussed in the next chapter.

When we pointed this out (April 2016), the Ministry stated (May 2016) that the terms stop files/non-filers/active filers, active registrants were not recognized by Law and hence the same could not be incorporated in the form of VCES-1.They held that the VCES Forms have the virtue of simplicity and had verifiable information which was required for administering this Scheme.

The terms stop files/non-filers/non-registrants or service providers were recognised by the department and found specific mention in the memorandum of Finance Bill, 2013. Further, the necessary information along with other vital parameters like service provider/service recipient, could have been collected in the VCES-1 form, which would have given valuable data to the department for post-Scheme analysis and monitoring.

Ministry further stated (June 2016) that the suggestion of audit was noted for compliance in future.

2.3.2 Lack of distinction between payments made under VCES and regular tax payment

The Scheme does not provide use of distinct challans for payment of tax dues and declarants used the format of challans as specified for regular payment.

On account of not specifying the distinct challans, it would become difficult to verify whether the declarant had made the payment of "tax dues'' under the VCES or challans were towards their regular payment of service tax.

When we pointed this out (April 2016), the Ministry stated (June 2016) that it was not feasible to prescribe separate challans since there was very short time available between the announcement of the Scheme and the enactment of the actual launch of the Scheme. Further, it stated that separate challan for VCES would require the separate accounting head for the collections of difference services. Moreover, the deposits made by the declarants have been ascertained from assessee-wise details available on the NSDL site. Further on analyzing the VCES return and the periodical ST3 return action payment under VCES could be ascertained.

Audit is of the view that since the payments were made through use of an IT platform, a method of identifying VCES challans could have been possible.

A few illustrated cases are given below:-

2.3.2.1 An assessee in Mumbai-II ST Commissionerate, declared (November 2013) tax dues of ₹ 1.25 crore and VCES-3 was issued (September 2015).

We noticed that the payment of tax dues included two challans vide No.80427 and 80434 dated 4 September 2013 amounting to ₹ 65.92 lakh each. Out of which, ₹ 7.75 lakh were used for payment of tax dues under VCES and balance of ₹ 1.24 crore for regular service tax payments. Thus, from the challan it could not be ensured whether the amount paid by the declarant included VCES payment or entire payment related to regular payment of service tax.

When we pointed this out (December 2015), the Ministry stated (June 2016) that the suggestion of audit was noted for future compliance.

2.3.2.2 An assessee in Jaipur Commissionerate, declared (December 2013) tax dues ₹ 5.81 lakh. Fifty per cent of the dues (₹ 2.90 lakh) was deposited on 30 December 2013 by the declarant. Out of remaining tax dues of ₹ 2.90 lakh, ₹ 1.76 lakh was deposited on 30 June 2014. The balance amount ₹ 1.14 lakh was claimed as paid through a challan dated 7 September 2013 through which a consolidated amount of ₹ 1.80 lakh was paid by the declarant which includes regular as well as VCES payment. Thus, from the challan it could not be ensured whether the amount paid by the declarant included VCES payment or entire payment related to regular payment of service tax.

When we pointed this out (December 2015), the Ministry stated (June 2016) that though distinct challans were not prescribed, concerned Range Officer verified payment particulars from NSDL site.

The reply of the Ministry could not be accepted since the NSDL site contained the details of regular as well as VCES payments with no facility to differentiate between the two.

2.3.2.3 An assessee in Mumbai-VI ST Commissionerate, declared (November 2013) tax dues of ₹ 54.52 lakh towards Construction of Residential Complex, for the period July 2010 to September 2012 and accordingly, VCES-3 was issued (January 2015).

We noticed that a survey was conducted (November 2013) on the premises of the declarant. The declarant had admitted service tax liability of ₹ 14.80 lakh for the period April 2013 to September 2013 and submitted copies of GAR-7 challans dated 19 November 2013 and 22 November 2013 amounting to ₹ 15.00 lakh towards payment of the admitted service tax liability (November 2013). While submitting the proof of payments of the tax dues (June 2014) under VCES, the declarant had produced the same challans amounting to ₹ 15.00 lakh which were submitted towards the payments of the admitted service tax liability during the survey. It resulted the mis utilisation of challan.

When we pointed this out (December 2015), the Ministry stated (June 2016) that the suggestion of the Audit is noted for future compliance.

2.3.2.4 We noticed in eight cases in Kochi Commissionerate, involving total tax dues of ₹ 4.50 crore, same challans contained payments under VCES as well as regular service tax payments of ₹ 34.03 lakh, for post VCES period.

When we pointed this out (between November 2015 and January 2016), the Ministry stated (May 2016) that in all the cases declarants paid the declared tax dues.

Due to non-capturing of information as to whether the payments were against VCES or regular payments, there was scope for fraud by using same challans as evidence for regular payments and VCES payments.

2.3.3 Lack of database

A database is a collection of information that is organised so that it can easily be accessed, managed, and updated. For successful implementation of the Scheme, the Board should have prescribed an appropriate database for capturing of relevant data relating to VCES. Non-prescription of proper database resulted in each Commissionerate devising their own database for creating, updating, retrieving and monitoring of the Scheme regarding

payment of tax dues, incorrect application of rate of tax etc., lack of inter linking of electronic data/information already available in the application of ACES. Due to this, databases/information captured by the field formations were not helpful in proper implementation and monitoring of the Scheme.

In this connection it is pertinent to point out that the First report of the Tax Administration Reforms Commission observed (May 2014) that

"Implementation of VCES Scheme in 2013 is another example where the readiness of IT was not taken into account before the budget announcement. While the Scheme has been a great success in raking in additional revenue, the department has lost the opportunity to get valuable information on the nature of non-compliance. Even though the Scheme benefited the exchequer, the department was deprived of crucial real time information on sectors and regions that were non-compliant. Without the leverage of IT, a large amount of manual input is lying with the department, which is of little use from the perspective of analysis and future course of action."

When we pointed this out (April 2016), the Ministry stated (June 2016) that due to short time available between the announcement of the Scheme and its launching it was not possible to integrate and implement the VCES Scheme in the ACES application.

Audit is of the view that a hurried implementation lead to losing opportunity for better monitoring and administration of the Scheme. Interlinking of VCES data base with ACES could have been done afterwards.

2.3.4 Inadequate Review/Monitoring mechanism

A checklist is a type of informational job aid used to reduce failure by compensating for potential limits of human memory and attention. It helps to ensure consistency and completeness in carrying out a task. During the examination of records relating to the Scheme, it is observed that no checklists were prescribed at the Board level. Prescribing of the checklist enables the declarants to furnish complete records/information along with declaration. Similarly, on the departmental front, the DA may not skip the key tasks / basic checks required to be performed if appropriate checklist is available. Non-prescribing of checklist resulted in deficiencies in basic due diligence like verification of details in calculation sheet with the declaration as pointed out in paragraph 2.1.1 and 3.4.6.

We noticed the following deficiencies that in respect of cases scrutinised in selected Commissionerates:

- Incomplete information contained in the case files
- Contents not arranged in proper sequence

- ❖ VCES-1 applications not assigned with declaration numbers and dates
- ❖ Details of cases having been referred to various authorities to ascertain eligibility criteria in terms of Sections 106 (1) and 106(2) not kept on record
- ❖ Proper arrangements not made for processing VCES cases post restructuring of the department (October 2014)

The above deficiencies, in addition to the absence of other mechanisms as discussed in previous paras, indicate that required review/monitoring mechanisms were not in place during the implementation of the Scheme.

When we pointed this out (April 2016), the Ministry stated (May 2016) that the point was noted for further compliance.

2.3.5 Normal safeguards regarding Cenvat credits not built into VCES

As per Rule 9(1) of Cenvat Credit Rules, 2004, the Cenvat credit shall be taken by the manufacturer or the provider of output service or input service distributor, as the case may be, on the basis of the documents prescribed thereunder. Further, as per Rule 9(2) of the said rules, as amended on 1 March 2007, no credit under sub-rule (1) cited supra shall be taken unless all the particulars prescribed under the Central Excise Rules, 2002 or the Service Tax Rules, 1994, as the case may be, are contained in the said document.

As per proviso below sub-rule (2), if the said document does not contain all the particulars but contains the details of duty or service tax payable, description of the goods or taxable services, assessable value, central excise or service tax registration number as the case may be, and the Deputy Commissioner/Asst. Commissioner is satisfied that the goods or services covered by the said document have been received and accounted in the books of account of the receiver, he may allow the Cenvat credit.

Thus, it follows that Cenvat credit shall be allowed only on fulfillment of the above conditions.

Further, as per the provisions of VCES, 2013, a defaulter may avail of the Scheme on condition that he files a truthful declaration of service tax dues pertaining to the period from 1 October 2007 to 31 December 2012 and makes the payment in one or two installments before prescribed dates. The Board, clarified[9] (January 2014) that the tax paid under VCES would be admissible as Cenvat credit after payment of tax dues in full and receipt of acknowledgement of discharge in VCES-3.

[9] vide circular dated 20 January 2014

VCES has no provisions to ascertain the veracity of the ST liability declared. The Scheme neither specifies nor denies furnishing of valid supporting statutory documents in support of service tax liability declared. Board's clarification that service recipient was eligible to avail Cenvat credit of tax paid under VCES runs contrary to the main rule under Cenvat Credit Rules cited supra which mandates documents for availing Cenvat credit. The safeguards prescribed in Cenvat Credit Rules, 2004, to avail Cenvat credit were not given due consideration while making payments under VCES admissible for Cenvat credit.

The provisions of VCES were meant for those who defaulted in payment of service tax dues and they were extended the benefit of waiver of interest/penalty and immunity from penal provision. The declarants who were allowed the benefit under VCES were also extended the benefit of availing credit of tax dues paid, without insisting for documents to avail the same. This enabled the declarants to avail double benefit of getting immunity for defaulted dues and availing Cenvat Credit in respect of defaulted dues paid under VCES, in view of Board's clarification. Thus Board's clarification proved detrimental to revenue by allowing double benefit by way of credit to defaulters who had already been extended immunity benefit, without calling for any supporting documents in support of tax dues declared.

When we pointed this out (April 2016) the Ministry stated (June 2016) that the point was noted for further compliance.

Chapter 3 : Observance of Mechanism devised to implement VCES

We examined the observance of mechanism devised by the department to monitor implementation of VCES and found non-compliance to provisions prescribed in various stages right from registration of declarants to issue of final discharge certificates.

3.1 Verification of Registration of declarants

As per rule 3 of VCES Rules, 2013, any person, who wishes to make a declaration under the Scheme, shall, if not registered, take registration under Rule 4 of the Service Tax Rules, 1994 before filing declaration.

As per rule 4(1) of Service Tax Rules, 1994, every person liable for paying service tax shall make an application to the concerned Superintendent of Central Excise for registration within 30 days from the date on which liability for the service tax arises under Section 66B of the Finance Act, 1994, as amended.

Status of registration of declarants at the time of filing of VCES declaration was called for from 35 selected Commissionerates. The information was supplied only by 14 Commissionerates. On analysis of this information, the following observations were made:-

In 17 cases in nine Commissionerates, involving tax dues of ₹ 18.27 crore, though the declarants were registered with the department as on the date of making declarations, the services which were declared were not found included in the registration certificates as stipulated by Rule 4(5A)[10].

When we pointed this out (between October 2015 and January 2016), the Ministry accepted the observation (May 2016) in three cases. In the remaining 13 cases it stated that non-inclusion of the specified services in registration appeared to be a technical lapse and had no revenue implication. In the remaining one case the reply was awaited.

The reply of the Ministry was not acceptable since one of the objectives of the Scheme was broadening of tax base. Registration of declarant under the specified service, would have enabled monitoring of the post-VCES compliance on the part of the declarant. Further, wrong mentioning of the

[10] Rule 4(5A) stipulates that where there is a change in any information or details furnished by an assessee at the time of obtaining registration (in ST-1) or if he intends to furnish any additional information or detail, such change or information or details shall be intimated in writing by the assessee to the jurisdictional AC/DC of Central Excise within a period of thirty days of such change.

name of the service by the declarant would result in depiction of incorrect service tax collections across services.

A few illustrative cases are highlighted below:-

3.1.1 An assessee in Mumbai-VI ST Commissionerate, had declared (November 2013) tax dues of ₹ 3.76 crore towards Construction of Complex service for the period December 2010 to March 2012. From the Registration certificate (Form ST-2), it was observed that the declarant was not registered for the service (i.e. Construction of Complex) against which the declaration had been made.

3.1.2 An assessee in Mumbai-VII ST Commissionerate, had declared (June 2013) tax dues of ₹ 2.29 crore in respect of 4 services (viz. Business Support Services; Management, Maintenance and Repair Services; Consulting Engineer's Services; and Survey and Exploration of Oil, Mineral and Gas) for the period October 2007 to December 2012. We noticed that the declarant was registered for two services only (Consulting Engineer services and Renting of immovable property service).

3.2 Verification of whether period declared was in conformity with the period envisaged under the Scheme

As per section 105 of the Chapter VI of Finance Act, 2013, declarant may declare tax dues for period from 1 October 2007 to 31 December 2012.

We observed in 61 cases, in 16 Commissionerates, involving tax dues of ₹ 3.61 crore, either the period of declaration fell beyond the period stipulated under the Scheme or no year-wise breakup was given to ascertain whether the period declared was within the period stipulated.

When we pointed this out (between October and December 2015) the Ministry, while accepting the observation in 36 cases, stated (May 2016) that the remedial action was already taken. Reply in the remaining 25 cases was awaited.

3.3 Verification of payment of the amounts shown as paid in calculation sheets

We noticed in 19 cases, in five Commissionerates, the declarants declared tax dues of ₹ 14.66 crore, after deducting an amount of ₹ 9.31 crore, which was claimed to have already been paid before the Scheme came into effect. However, as no details were found on record to ascertain whether the department verified the above fact, audit could not check the correctness of the claim of the declarants.

When we pointed this out (between October and December 2015), the Ministry stated (May/June 2016) that in 15 cases the declarants details were verified. Reply in remaining four cases were awaited (June 2016).

3.4 Check of Eligibility Criteria in terms of proviso to Section 106

Section 106(1) and (2) of the Finance Act, 2013, limited the benefits under VCES, to the declarants against whom no notice was pending or inquiry/investigation/audit was initiated and the same is pending, as on 1 March 2013. Board clarified (August 2013) that the DA, on having sufficient reasons, can serve notice of intention to reject the declaration within 30 days of the date of filing of the declaration stating the reasons and that the declarant would be given an opportunity to be heard before any order is passed.

We noticed following types of discrepancies in 444 cases in 20 Commissionerates, involving tax dues of ₹ 85.97 crore:-

a. Confirmation on status of cases pending against the declarants was not received from Anti Evasion Wing/Preventive/DGCEI, even after a lapse of stipulated period of one month for rejection of ineligible cases.

b. There were instances of cases pending show cause notice/order in original (SCN/OIO) as on 1 March 2013 against the declarants for the same period as declared by them under VCES.

c. VCES benefit was extended to the declarants against whom CERA had already made observations and the same was pending as on 1 March 2013.

d. There were instances, where no proof of checklist or details of inter/intra-departmental correspondence were available on record.

When we pointed this out (between October 2015 and January 2016), the Ministry stated (June 2016) that Board prescribed a period of 30 days for issuing the SCN to ensure that the declarant was at least aware of the fate of his declaration.

The reply of the Ministry was silent on our audit observations regarding non-receipt of information from other wings, extension of ineligible benefits and non-availability of proof of checklist or correspondence regarding verification.

A few illustrative cases are given below:-

3.4.1 CERA had made an observation (October 2012) in respect of an assessee in Mumbai-VII ST Commissionerate regarding non-levy of service tax

of ₹ 26.21 lakh under the service category of Scientific or Technical Consultancy for the period 2010-11. ***The issue appeared at Sl.No.7 of Appendix – II) of CAG of India's Audit Report No. 4 of 2015 (Service Tax)*** and the fact that this was being considered for inclusion in the CAG audit report was in the notice of the Commissionerate from October 2012[11]. The same assessee had declared (June 2013) tax dues amounting to ₹ 2.10 crore under various service categories including Scientific or Technical Consultancy for the period October 2010 to December 2012. An SCN was also issued (October 2013) for an amount of ₹ 1.76 crore, besides applicable interest.

The assessee paid (June/July 2013) the service tax amount demanded, including interest. We observed that tax dues declared (₹ 2.10 crore) included service tax dues of ₹ 1.50 crore in respect of scientific and consultancy services and other services pertaining to 2011-12 covered in the SCN. The department rejected the declaration partially for an amount of ₹ 38.86 lakh on the basis of audit observations raised (between October 2012 and March 2013) by EA 2000 allowing benefit of the Scheme for the balance amount of ₹ 1.11 crore. VCES-3 was issued (June 2014) for ₹ 1.72 crore. Further, it was also observed that same challans (for ₹ 1.46 crore) had been submitted in support of the payments of service tax in compliance with the above SCN as well as tax dues under VCES.

When we pointed this out (November 2015), the Ministry stated (May 2016) that while passing OIO the designated authority examined the matter in the light of Board's circular dated 25 November 2013 and the issues raised in the audit objection by EA 2000.

The reply of the Ministry was not acceptable in view of stipulation in Board's circular dated 8 August 2013 that declarant can declare the "tax dues" concerning an issue which was not a part of the audit para. The non-levy of service tax under the service category of Scientific or Technical Consultancy for the period 2010-11 was raised by CERA in October 2012 and admitted by the department (October 2013) and hence the application was liable for rejection.

3.4.2 An assessee in Kochi Commissionerate, declared (December 2013) tax dues of ₹ 1.76 crore towards broadcasting service for the period April 2011 to September 2012. We noticed that Service Tax Division, Kochi, initiated investigation in March 2011 and issued summons to the assessee in March 2012 and the same was pending on 1 March 2013. Further, internal audit observation on the same issue for the period October 2009 to July 2011 was also pending as on 1 March 2013. Hence the declaration filed by the assessee

[11] Vide Statement of Facts (SOF) issued

was ineligible for the benefit under VCES. However, VCES-3 was issued (January 2015).

When we pointed this out (November 2015), the Ministry stated (May 2016) that as SCN in pursuance of internal audit objection was issued in October 2013, no SCN was pending as on 1 March 2013 and that audit observation cannot be considered as pending as SCN was issued.

The reply of the Ministry proved that internal audit observation raised on same issue was pending on 1 March 2013 as SCN was issued in October 2013.

3.4.3 An assessee in Bengaluru-ST Commissionerate declared (December 2013) tax dues of ₹ 1.34 crore towards banking and other financial service, covering the period from October 2007 to December 2012. We noticed that five SCNs were issued during the period from 2008 to 2012 and an OIO was passed (January 2014) against the declarant, confirming the demand of service tax of ₹ 1.82 crore, covering the period from 1 June 2007 to 31 March 2012 for the same services as declared under VCES. Since SCNs were pending as on 1 March 2013, the declaration was liable for rejection.

When we pointed this out (December 2015), the Ministry stated (May 2016) that the VCES application was liable for rejection, as reported by commissionerate concerned.

3.4.4 An assessee in Patna Commissionerate, declared (December 2013) tax dues of ₹ 97.16 lakh. We noticed that summon against the declarant had been issued by DGCEI, Hyderabad on 2 July 2012 and an inquiry had also been initiated before 1 March 2013. The declarant was not eligible and the declaration was to be rejected by the DA, but it was not done. The Joint Commissioner (Service Tax), Central Excise & Service Tax Headquarters, Patna observed (March 2015) in the VCES file that the declaration made by the assessee should have been rejected and the issuance of VCES-3 in this case was not proper.

When we pointed this out (January 2016), the Ministry stated (May 2016) that since VCES-3 was not issued to the assessee due to pending SCN, declaration filed might be treated as rejected. But details of actual action taken were awaited.

3.4.5 An assessee in Raipur Commissionerate, declared (September 2013) tax dues of ₹ 25.25 lakh towards manpower recruitment and supply service and erection and commissioning services for the period April 2010 to December 2012. We noticed that CERA had observed (March 2012) that declarant had not charged service tax from an assessee though the latter had provided “Manpower supply and recruitment agency” service during 2009-10

and 2010-11. Since the audit observation was pending as on 1 March 2013, the declarant was not eligible under VCES.

When we pointed this out (November 2015) the department stated (November 2015) that the declarations were not to be rejected in a routine manner, however, information/document had been requisitioned from the declarant. But the Ministry in its reply stated (May 2016) that the assessee did not file any declaration under VCES.

The reply of the Ministry was not acceptable as the VCES application was received and Range Officer of ST Range IV, Raipur gave (October 2013) his remarks on the application. Final outcome of action initiated by the department was awaited.

3.4.6 An assessee in Lucknow Commissionerate, declared (December 2013) tax dues of ₹ 1.55 crore towards Security Services for the period April 2011 to December 2012, paid final installment (February 2014) and accordingly, VCES-3 was issued (April 2014). We observed that the Internal audit wing had made an observation regarding short payment of service tax of ₹ 61.70 lakh for the period from 2008-09 to 2010-11 on the same issue.

When we pointed this out (December 2015), the Ministry stated (May 2016) that the internal audit para on the same issue pertained to the period 2008-09 to 2010-11 whereas the declarant filed VCES declaration for the period from April 2011 to December 2012.

The reply of the Ministry is not acceptable since the audit observation raised by internal audit is pending and as such acceptance of VCES application is incorrect.

Ministry further quoted (June 2016) point No.4 of Board's circular dated 25 November 2013 which deals with tax dues paid by assesse after the date of the scheme coming into effect i.e. 10 May 2013.

The reply of the Ministry is not relevant to the audit objection.

3.4.7 In 99 cases, in Bhubaneswar-I Commissionerate, involving tax dues of ₹ 16.53 crore, verification reports for having exercised eligibility checks from Range Superintendents were not kept on record.

When we pointed this out (November 2015), the Ministry, while accepting (May 2016) that out of 99 cases only in 11 cases the eligibility checks from the Range Officer were on records, attributed non-traceability of records in the remaining 88 cases to restructuring of the department. Final reply on these 88 cases was awaited.

3.5 Non-initiation of action in terms of Section 111

Section 111(1) and 111(2) of Chapter VI of the Finance Act, 2013, empowers the Commissioner to serve notice on the declarant in respect of declarations found to be substantially false, within one year from the date of declaration.

3.5.1 We noticed that in 15 cases in eight Commissionerates, involving tax dues of ₹ 9.46 crore, even though there were sufficient reasons to believe that the declarations made were false, no action was initiated by the department.

When we pointed this out (between October 2015 to January 2016) the Ministry stated (May/June 2016) in nine cases that the VCES Scheme permitted the DA only to check arithmetical accuracy as per Board circular of December 2013. In one case the Ministry accepted the audit observation. In the remaining five cases reply is still awaited.

One such case is illustrated below**:-**

An assessee in Chennai-II ST Commissionerate, declared (December 2013) tax dues of ₹ 1.92 crore towards business auxiliary service (activation commission) for the period October 2007 to December 2012. We noticed that the assessee had calculated service tax on the transaction value of ₹ 3.98 crore for the year ended 31 March 2009, whereas the assessee had earned service income on business auxiliary services and other services of ₹ 5.40 crore, as per the profit and loss account. As such, there was reason to believe that declaration was substantially false.

When we pointed this out (November 2015) the Ministry stated (May 2016) that adequate care was taken by the verifying the correctness of declaration as per Board's circulars relating to VCES. It was further stated that the declarations were sent to all the divisions to check eligibility of the declarations and only after getting clearance, the declarations were processed.

The final reply of the Ministry regarding incorrect calculation of service tax on the transaction value was awaited (June 2016).

3.5.2 In Guntur and Hyderabad ST Commissionerates, we observed that 45 declarants under service category "construction of residential apartments" classified their service as Construction of Complex Service and discharged service tax liability. Audit observed that these services were classifiable under Works Contract Service. The misclassification resulted in short payment of service tax of ₹ 3.00 crore. In all the above cases the department issued discharge certificates between January 2014 and January 2015.

When we pointed this out (December 2015) the Ministry stated (May 2016) that the activity was more appropriately classifiable under Construction of

complex services, being a more specific description for which no specific abatement was available. It further stated that it was decided that amounts involving more than ₹ 25 lakh only were to be investigated with regard to the truthfulness as well as to classify under works contract services.

The reply of the Ministry was not acceptable in light of Board's letter dated 22 May 2007 which stipulated that the contracts treated as works contract for the purpose of levy of VAT/sales tax should also be treated as works contract for the levy of service tax. Out of above 45 cases the audit found the VAT registration in 22 cases. Hence these declarants were classifiable under works contract services. Moreover, no authority was quoted regarding decision to investigate only cases involving more than ₹ 25 lakh.

3.5.3 An assessee in Bengaluru ST Commissionerate, declared (October 2013) tax dues of ₹ 1.02 crore, for the period from October 2007 to December 2012. We noticed from the case file that an offence case had been registered by the ADGCEI, Bengaluru Zonal Unit for the service tax liability of ₹ 5.00 crore vide its letter dated 30 August 2013. From the above it was evident that, though there was reason to initiate action under Section 111, no action had been initiated by the department.

When we pointed this out (January 2016) the Ministry stated (May 2016) that (a) the declarant showed a total service tax amount as ₹ 2.98 crore pertaining to the period from 2007-08 to 2012-13 (upto December 2012), of which he has already paid an amount of ₹ 1.96 crore and filed VCES declaration for the remaining amount of ₹ 1.02 crore, (b) ADGCEI worked out tax liability for the past 5 years from Balance Sheet and the investigation covers upto 30 June 2013, and (c) As the figures arrived at by the declarant and the ADGCEI were not exactly for the comparable period, the declaration filed by the declarant was within the parameter of VCES.

The Ministry's reply was not acceptable as a difference of ₹ 2.02 crore (representing 40 per cent) in tax liability for a difference in period of just six months was a red flag, that Ministry should have investigated.

3.6 Acceptance of revised declarations, in contravention of Board's Circular

Board clarified (August 2013) that the declarant was expected to declare his tax dues correctly. In case, the mistake was discovered suo moto by the declarant himself, he might approach the DA, who after taking into account the overall facts of the case, might allow amendments to be made in the declaration. That too, provided that the amended declaration was furnished by declarant before the cut-off date for filing of declaration i.e. on 31 December 2013.

We noticed that revision of declarations consequent to departmental action or revisions beyond 31 December 2013 in contravention of Board circular cited ibid in the following cases:-

3.6.1 An assessee in Salem Commissionerate, declared (June 2013) tax dues of ₹ 1.60 crore, towards "Mining services" rendered, based on the action initiated by the DGCEI, Madurai Regional Unit, Madurai. Subsequently, the DA in letter dated 22 July 2013, stated that the declarant was liable for service tax towards mining services rendered as sub-contractors, which was omitted to be included in the declaration. Based on the above letter, the declarant filed revised declaration on 31 December 2013, declaring ₹ 2.33 crore, including the service tax payable on the services pointed out by the DA. The Department accepted the revised declaration and issued VCES-3 (February 2015) which was not in order as the assessee has not revised declaration suo moto.

When we pointed this out (December 2015), the Ministry stated (May 2016) that as long as revised declaration was filed before the due date, the same would be squarely covered by the VCES.

The declarant filed the revised declaration consequent upon initiation of action by DGCEI. The Ministry's reply proved audit point as they did not consider the primary condition of suo moto declaration and allowed revision of declaration by taking only the cutoff date.

3.6.2 Similarly in two other cases in Kochi and Chennai-II ST Commissionerates respectively have also revised the declaration filed consequent of action by DGCEI. Hence this was not in order as the assessees did not revise the declarations suo moto.

When we pointed this out (November 2015) the Ministry stated (June 2016) that as long as revised declaration was filed before the due date, the same would be squarely covered by the VCES.

The reply of the Ministry was not acceptable as the revision of declaration could not be considered as made suo moto.

3.6.3 An assessee in Ahmedabad ST Commissionerate, declared (December 2013) tax dues of ₹ 51.11 lakh. The same was revised for ₹ 20.51 lakh on 11 March 2014. The department issued the VCES-3 (October 2014). Since the revised declaration was submitted by the declarant after 31 December 2013, the action taken by the department was not in order.

Similarly, in two other cases in Jaipur Commissionerate revised declarations after 31 December 2013. However, discharge certificates were issued.

When we pointed this out (December 2015) the Ministry stated (May 2016) that in one case the declarant revised declaration on the instruction from the DA and hence the time limit prescribed for suo moto declaration was not applicable. They stated in respect of all the cases that as the delay was only procedural in nature and applications should not be rejected on such frivolous grounds.

The reply of the Ministry was not acceptable since the Scheme did not empower the DA to request the declarant to furnish revised declaration and prescribing a cut-off date for amending the application had no sanctity if non-adherence to the same was considered frivolous ground.

3.7 Monitoring of payment of first installment

As per Section 107(3) of the Finance Act, 2013, one of the conditions of the VCES was that the declarant shall pay at least an amount equal to 50 per cent of the declared tax dues under the Scheme, on or before 31 December 2013. Therefore, if the declarant fails to pay at least 50 per cent of the declared tax dues by 31 December 2013, he would not be eligible to avail the benefits of the Scheme. In cases where declarants fail to pay taxes within 31 December 2014, action has to be initiated under section 87 of the Finance Act, 1994. Also, such payments should be made in cash and not adjusted through Cenvat credit.

We noticed in 116 cases, in 11 Commissionerates, involving tax dues of ₹ 19.47 crore, the declarants had not paid their first installment i.e., 50 per cent of declared amount within the due date of 31 December 2013. Hence, all the above cases not eligible for consideration under VCES.

When we pointed this out (December 2015), the Ministry accepted the observation (May 2016) in 41 cases. In nine case it stated that that as per section 110 the declarant was eligible to pay the part payment with interest under section 87, since the section 110 deals with the situations where declarants fails to pay the tax dues, either fully or in part, as declared by him within prescribed limit. In 49 cases it stated that letters were issued calling for details in all such cases where proof of payment of the remaining 50 per cent of tax dues were not submitted by the declarants. In the remaining 17 cases reply is still awaited.

The reply of the Ministry was not relevant since the audit observation pertained to non- payment of first installment which within prescribed period, thereby making these declarations ineligible for VCES.

A few illustrative cases are given below:-

3.7.1 An assessee in Mumbai VII ST Commissionerate, declared (December 2013) tax dues of ₹ 85.43 lakh towards works contract service for the period April 2010 to December 2012. We noticed that the assessee had paid an amount of ₹ 43.25 lakh in two installments on 21 January 2014 and 8 March 2014, but had not paid the amount of ₹ 42.72 lakh towards first installment by 31 December 2013. However, no action was taken by the department to disallow the assessee under VCES.

3.7.2 An assessee in Jalandhar Commissionerate, declared (September 2013) tax dues of ₹ 75.98 lakh towards renting of immovable property service, for the period April 2008 to December 2012. We noticed that the assessee had paid an amount of ₹ 21.30 lakh only by 31 December 2013, as against 50 percent of ₹ 37.99 lakh payable. However, no action was taken by the department to disallow the assessee under VCES.

When we pointed this out (December 2015) the Ministry stated that a notice under section 87 has been issued to the assessee.

3.7.3 An assessee in Vadodara-I Commissionerate, declared (September 2013) tax dues of ₹ 23.52 lakh for the period January 2012 to December 2012. The declarant was liable to pay ₹ 11.76 lakh as first installment by 31 December 2013. However, only ₹ 4.63 lakh was paid by 31 December 2013. The DA issued (March 2014) SCN to the declarant, proposing rejection of claim. The declarant represented (March 2014) that due to acute financial crises, he could not pay the 50 per cent tax dues by 31 December 2013. Declarant further stated that if the first 50 *per cent* tax dues was not paid by 31 December 2013, the same could be paid with interest by 30 June 2014 and paid the interest of ₹ 6.48 lakh on entire tax dues from January 2012 (i.e. from actually payable date). Though the claim was liable for rejection, the DA issued (July 2015) VCES-3 to the declarant on the basis of declarant's representation, without even adjudicating the SCN issued.

When we pointed this out (November 2015) the Ministry stated (May 2016) that as per section 110 the declarant was eligible to pay the part payment with interest under section 87, since the section 110 deals with the situations where declarants fails to pay the tax dues, either fully or in part, as declared by him within prescribed limit.

In this regard, Ministry's attention is invited to the Gujarat High court judgement[12] where in it was held that if shortfall in the taxes could be accepted after charging interest under section 110, there was no need to

[12] In the High Court of Gujarat at Ahmedabad - Ramilaben Bharatbhai Patel Vs. Union of India and others {2014 (35) STR 695 (Guj.)}

make special proviso for extending time for depositing the remaining of the taxes under sub-section (4) of section 107. It was further held that section 110 pertains to compulsory recovery of taxes with interest, sub-sections (3) and (4) of section 107 refer to voluntary tax deposit by a declarant in terms of the Scheme and both these operate in separate fields. Thus the VCES declaration was liable for rejection as pointed out by audit.

Ministry further stated (June 2016) that this issue pointed out by audit was not generic but specific to certain Commissionerates only, where rectification measures were already taken.

3.8 Monitoring of payment of second installment

Section 107 stipulates that balance dues pending after paying first installment of not less than 50 per cent of tax dues declared, should be paid by the declarant before 31 June 2014. Declarants who fail to pay the balance before 31 June 2014 were also given an option to pay the same by 31 December 2014 with interest. Immunity under the provisions of Section 108 of the Finance Act, 2013, would be extended only to such declarants who make payment of tax dues declared, in accordance with the provisions of Section 107 of the Finance Act, 2013.

We noticed in 53 cases in 10 Commissionerates, involving whole/part of tax/interest dues of ₹ 1.49 crore were not paid by 31 December 2014. Hence, all the above declarants were not eligible for VCES.

When we pointed this out (between October 2015 and January 2016) the Ministry accepted the observation (May 2016) in three cases. In 17 cases it was stated that the declarants paid tax dues with interest subsequently and that penalty was not recoverable on tax dues declared under the Scheme or the reply was silent about levy of penalty. This stand of Ministry could not be accepted as Section 108 provided for immunity from penalty and other proceedings to declarant only on payment of tax dues by 30 June 2014/payment of balance tax dues with interest by 31 December 2014.

In 15 cases, Ministry stated that action under Section 87 was initiated and was under progress and reply awaited in 18 cases.

An illustrative case is given below:-

3.8.1 An assessee in Lucknow Commissionerate, declared (December 2013) tax dues of ₹ 60.89 lakh for the period April 2012 to December 2012 and deposited first installment of ₹ 30.45 lakh within the due date. The assessee deposited the balance amount ₹ 30.44 lakh only upto 7 July 2015, i.e., after the prescribed due date. Hence, the declaration of the assessee was required

to be disallowed under VCES Scheme and the entire amount along with interest should have been recovered.

When we pointed this out (October 2015), the Ministry accepted the observation (May 2016).

3.8.2 We observed in 441 cases in 18 Commissionerates who declared tax dues of ₹ 60.68 crore did not pay the second installment of dues either in part or in full, thereby making themselves defaulters under the Scheme. The department did not initiate action for recovery of the dues, along with interest and penalty, under Section 87 of Finance Act, 1994 ibid.

When we pointed this out (between October 2015 and January 2016), the Ministry while admitting the observation in 438 cases stated (May 2016) that remedial action was undertaken against the defaulters. Reply was awaited in three cases.

A reading of Section 110 along with Section 108 suggests that immunity from payment of interest and penalty may not be extended to the declarants in case of violation of the provisions of Section 108. However, Section 110 did not prescribe any mechanism to recover the amount of interest and penalty leviable from the date it became due. Section 87 of Finance Act, 1994, as amended from time to time stipulates mechanism for recovery of arrears. In case of defaulters under VCES, the tax dues declared but not paid can only be construed as arrears but not interest and penalty as it is not demanded and confirmed as per the relevant provisions of the Act.

Section 87 of the Finance Act, 1994, gives very wide powers to the Central Excise Officers to recover any amount payable under the service tax provisions. Further, as the defaulters are no more eligible for the immunity under the Scheme, other provisions like Section 73, 73A, 73C also can be used for recovery of the defaulted amounts along with interest and penalty. That is, the failure on the part of assessee in complying with the provisions of the Scheme would automatically invoke the extant provisions of Finance Act, 1994, which are permanent in nature.

Audit noticed that despite having extensive powers to make good the service tax dues, the department did not initiate any action under the general penal provisions in respect of in all above cases mentioned at Para Nos. 3.7 and 3.8, where the declarants did not comply with the conditions prescribed under the Scheme for availing the benefit of immunity from interest and penalty.

3.9 Treatment of Payments made prior to 10 May 2013 considered under VCES

Board clarified (August 2013) that VCES benefits cannot be availed where a person has made part payment of his tax dues before the Scheme was notified (i.e. 10 May 2013) and makes the declaration under VCES for the remaining part of the tax dues. In such cases, if any tax dues have been paid prior to enactment of the Scheme, any liability of interest or penalty thereon shall be adjudicated as per the provisions of the Chapter V of the Finance Act, 1994.

Gujarat High Court in the case of M/s. Sadguru Construction Company Vs. Union of India held that "circular cannot override the enactment and so tax due as on 1 March 2013 and paid after 1 March 2013 shall be eligible for declaration under VCES Act, 2013 even though the Scheme has been enacted on 10 May 2013".

After pronouncement of this judgement also the Board has not taken action to review the circular issued by them.

We observed in 46 cases in 13 Commissionerates, the declarants paid the amount of ₹ 7.05 crore towards service tax prior to the notification of the Scheme. Hence all these declarants are not eligible for VCES as per Board's circular. However, we noticed that the department issued VCES-3 certificates in 21 cases.

An illustrative case is given below:-

An assessee in Patna Commissionerate, declared (August 2013) tax dues of ₹ 10.08 lakh for the period July 2010 to December 2012. We noticed that entire tax dues declared had been paid by the declarant prior to 10 May 2013, i.e, prior to enactment of the Scheme. The department issued VCES-3 to the assessee.

When we pointed this out (December 2015) the Ministry stated (May 2016) that the declarant deposited the amount in the month of March 2013 i.e., before the pronouncement of the Scheme, however, since there was no adverse report from field formations, the VCES-3 was issued. The Ministry further stated (June 2016) that the judgement was delivered on 24 April 2016 whereas the VCES Scheme envisaged payment of the first instalment by 31 December 2013. So revision of the circular would have created confusion and lead to more disputes.

Ministry reply was not tenable as some field formations, following the High Court judgement, allowed the payment made by the declarants between 1 March 2013 to 10 May 2013, while some applications were rejected

quoting Board Circular. Thus there was no uniformity in treatment of tax dues paid between 1 March 2013 to 10 May 2013.

3.10 Cenvat credit utilised for payment of tax dues

Rule 6(2) of the STVCES Rules, 2013, envisages that Cenvat credit shall not be utilised for payment of tax dues under the Scheme.

We noticed in 28 cases in nine Commissionerates the declarants utilized Cenvat credit of ₹ 2.52 crore before arriving at the tax dues. The department rejected none of these cases and issued Form VCES-3 in 19 cases.

When we pointed this out (between October 2015 and January 2016) the Ministry stated (May 2016) that in 10 cases, action for denial of immunity was being initiated and the outcome would be intimated. In 11 cases, Ministry stated that the declarants paid entire tax dues declared in VCES in cash but reply was silent about adjustment of Cenvat credit for arriving at tax dues declared in VCES, which amounted to using Cenvat credit for part payment of tax dues. In seven cases, the reply of the Ministry was awaited.

Two illustrative cases are given below:-

3.10.1 An assessee in Jalandhar Commissionerate declared (December 2013) tax dues of ₹ 4.48 lakh, towards cable operator services, for the period April 2008 to December 2012. The declared amount of ₹ 4.48 lakh was arrived at, after adjusting an amount of ₹ 60.19 lakh through Cenvat credit. As Cenvat credit was not allowed for utilization for making payment of tax dues under VCES, the department should have disallowed the same, which was not done. This resulted in short declaration of service tax of ₹ 60.19 lakh. The department, by issuing VCES 3 on 4 August 2014, extended undue benefit to the assessee by way of immunity from interest and penalty.

When we pointed this out (December 2015) the Ministry stated (June 2016) that though VCES-3 had been issued, Commissionerate had been asked to provide further clarification.

3.10.2 An assessee in Allahabad Commissionerate, declared (September 2013) tax dues of ₹ 3.43 lakh towards advertisement income for the period July 2012 to December 2012, after adjusting the Cenvat credit of ₹ 8.03 lakh availed on input services, while the actual tax dues were ₹ 11.47 lakh. The Department issued VCES-3 (January 2014). As Cenvat credit was not admissible for utilising the payment of the tax dues declared by the declarant, the department was required to determine the actual tax liability by disallowing the adjustment of Cenvat credit, which was not done resulting in short declaration of service tax dues of ₹ 8.03 lakh.

When we pointed this out (December 2015) the Ministry stated (May 2016) that the declarant had deposited tax dues of ₹ 3.43 lakh in cash.

The reply of the Ministry was silent on short-declaration of tax dues to the tune of ₹ 8.03 lakh by adjusting the Cenvat credit from total tax dues.

Chapter 4 : Pre and Post VCES tax administration

The circumstances leading up to the necessity of introducing the VCES reflect upon failures on part of the department in carrying out compliance verification. The penal provisions for non-registration, non/short payment of tax, non-filing of returns etc. and the parameters for selection of assessee units for internal audit are available in public domain. But, as these systems in place are not observed and the penal provisions are not sufficiently deterrent in nature, the perceived risk of detection of non-compliance is low. This view of audit is corroborated by the fact that only 66,072 existing as well as new registrants declared tax dues amounting to ₹ 7,750 crore under VCES as against 10,00,000 non/stop filers when the Scheme was announced.

One time amnesty Scheme like VCES can be a real one time solution for the problem it sought to redress only if the tax systems are strengthened and follow up mechanism is made stringent. But, we observed that during post-VCES period, the department failed to initiate stringent action against the stop-filers/non-filers, who had enjoyed the immunity provisions under VCES and again reverted back to the habit of non-filing of returns.

4.1 Pre VCES tax administration

Identification of stop filers or non-filers through ACES and conduct of internal audit of the assessee units are two important processes available with tax administration to test check compliance by assessees to the existing rules. Declarants under VCES should have come into tax net if department followed these processes as discussed below:-

4.1.1 Identifying Non-compliance by Registered Service Providers

We observed from the data received from 20 Commissionerates out of 35 selected Commissionerates that out of 24,166 declarations for an amount of ₹ 3,031.30 crore, 5,381 declarations involving ₹ 328.26 crore were new registrants. Thus, only around 22 per cent in terms of number and 11 per cent in terms of amount of the declarations related to new registrations.

From the above, it was evident that disclosure of large amount of 89 per cent of unaccounted income under VCES was by existing registrants, which was symptomatic of the malaise of poor tax administration over the years that enabled concealment of taxable income by the existing assessees.

This was brought to the notice of Ministry (April 2016) and Ministry stated (June 2016) that the scheme was also for the existing assessees, who were either stop filer or non-filers and attributed increasing number of defaulters

to substantial increase in service tax assesses without a corresponding increase in the number of tax collectors. They felt that VCES was a step to give a chance to defaulters for tax compliance as well as being a regular filer of returns by giving some incentives.

4.1.2 Inadequate or inefficient internal audit by department

Internal audit is one of the main compliance verification mechanism in the department, which involves selection of assessee units on the basis of risk parameters and scrutiny of records of the assessee to ascertain the level of compliance with the prescribed rules and regulations. As per paragraph 5.1.2 of Service Tax Audit Manual, 2011 tax payer whose annual service tax payment (including Cash and Cenvat) was rupees three crore or more in the preceding financial year would be subjected to mandatory audit each year.

We noticed that in case of 26 declarants scrutinised by audit in eight Commissionerates involving tax dues of ₹ 23.74 crore lack of proper monitoring/lapse on the part of internal audit in initiating timely action enabled the assessees to come under VCES and disclose large amount of defaulted tax dues. It resulted not only in postponement of revenue flow into Government account to that extent but also in extending undue benefit to the declarants by way of immunity from penal provisions.

When we pointed this out (between October 2015 and January 2016) the field formations of Ministry stated in nine cases (May 2016) that post restructuring of the department, the parameter on selecting units for conducting audit rest with DG Audit only. Hence, the question of inadequate or inefficient internal audit by department was not relevant. In four cases it stated that due to shortage of staff and work pressure certain issues might have escaped from audit. In 13 cases reply was awaited.

The reply of the Ministry was awaited.

A few illustrative cases are given below:-

4.1.2.1 An assessee in Hyderabad ST Commissionerate, paid service tax exceeding rupees three crore each year from 2010-11 to 2013-14 and therefore was to be mandatorily covered by internal audit every year. However, we observed that the assessee unit was last audited during October 2007, for the period up to August 2007 and thereafter no audit was conducted till April 2013.

The assessee had rendered sponsorship services in connection with Federation International De Football Association (FIFA) and the service tax payable on the said services for the period from 1 July 2010 to 31 March

2012 worked out to ₹ 15.69 crore and the same had not been discharged by the assessee.

Consequent on amalgamation of the assessee unit with another assessee declared (September 2013) tax dues of ₹ 15.69 crore not paid by the assessee. Thus, non-coverage of the assessee unit by internal audit each year from 2010-11 to 2012-13 enabled the assessee to conceal tax dues payable and subsequently come under VCES, thereby getting undue benefit of waiver of interest and penalty.

When we pointed this out (January 2016), the Ministry stated (May 2016) that the scope of observation was beyond the jurisdiction of VCES Scheme. It further stated that internal audit operates under certain parameters and slippage might have occurred during the same.

4.1.2.2 An assessee in Rajkot Commissionerate declared (December 2013) tax dues of ₹ 4.42 crore towards GTA, manpower recruitment agency service, etc., for the period from April 2011 to September 2012. We observed that an internal audit was conducted on the assessee unit on 26 December 2012 for the period from April 2011 to March 2012 and spot recovery of an amount of ₹ 14.77 lakh was made against the assessee for non-payment of interest on late payment of service tax. However, failure on the part on internal audit to detect non-payment of service tax of ₹ 4.42 crore enabled the assessee to come under VCES and get immunity from penal provisions.

This was brought to the notice of the department/Ministry in October 2015, the reply of the department/Ministry was awaited (May 2016).

4.1.2.3 An assessee in Mumbai-VI ST Commissionerate, declared (November 2013) tax dues of ₹ 3.76 crore towards construction of complex service for the period December 2010 to March 2012. We observed that the department had initiated an enquiry against the declarant for ascertaining service tax liability in respect of services under health club and fitness centre, mandap keeper, beauty treatment service, business exhibition service and rent-a-cab service. The enquiry culminated into issuance of SCN (December 2012) which was adjudicated in March 2013. During the course of enquiry, service tax returns filed and balance sheets for the years 2006-07 to 2010-11 were called for. Neither the SCN nor the OIO determined any service tax liability in respect of Construction of Complex Service.

We further observed that out of the total tax dues of ₹ 3.76 crore declared, an amount of ₹ 1.36 crore pertained to the period from December 2010 to March 2011 relating to construction of complex service. Though the balance sheet for the period 2010-11 was available at the time of initiation of enquiry, the department failed to detect non-payment of service tax of ₹ 1.36 crore,

which enabled the assessee to come under VCES and declare tax dues of ₹ 3.76 crore, which also included the amount of ₹ 1.36 crore, thereby extending undue benefit to the assessee by way of interest and penalty.

When we pointed this out (December 2015), the Ministry stated (May 2016) that it was merely a technical issue.

The reply of the Ministry was not acceptable since the case was highlighted to show how inadequate review of balance sheet by internal audit resulted into undue benefit to the declarant by way of immunity from penalty and interest.

4.2 Filing of truthful declarations

The Finance Minister, through the Scheme, hoped to appeal to non-filers/stop filers to voluntarily make truthful declaration of tax dues. It is, therefore, a natural expectation that such Schemes should be designed in a manner to make it difficult for the declarant to be untruthful.

Audit attempted to examine the truthfulness of the declarations in Chennai-I ST and Kochi Commissionerates by cross-verifying the quantum of tax dues declared with the details available with other authorities like Income Tax Department, Commercial Taxes Department and Registrar of Companies. We observed in eight cases in Chennai-I ST and Kochi Commissionerates that the tax dues declared under VCES were short by of ₹ 4.35 crore, in comparison with the data available with the other authorities.

Ministry stated (June 2016) that treating declarants on par with any other assesse, regular monitoring was being done and necessary action initiated.

A few illustrative cases are given below:-

(a) An assessee in Chennai-I ST Commissionerate, declared (September 2013) tax dues of ₹ 1.05 crore towards maintenance and repair services rendered by them for the period from November 2007 to March 2008. The VCES declaration was accepted and VCES-3 issued in February 2015.

We observed that the declarant had taken service tax registration on 28 August 2013 and as such they did not file any ST-3 returns, before submitting VCES application. Verification of annual accounts of the assessee obtained from the Registrar of Companies revealed that the assessee had income of ₹ 28.91 crore and ₹ 8.28 crore, under job receipts, for the years 2008-09 and 2009-10 respectively. However, tax dues on these income related to services were not declared by the assessee under VCES.

When we pointed this out (January 2016) the Ministry stated (May 2016) that the Finance Act, 2013 did not prescribe any financial documents to be submitted to the department to prove the veracity of declaration.

(b) An assessee in Chennai-I ST Commissionerate declared (December 2013) tax dues of ₹ 25.88 lakh under VCES in respect of works contracts service for the years 2010-11 and 2012-13. Verification of VAT returns filed by the assessee with the Commercial Taxes Department, Tamil Nadu, revealed that the assessee reported taxable turnover of ₹ 7.61 crore in his VAT returns towards value of material transferred during the execution of works contracts for the year 2011-12. It was evident from this disclosure that the assessee executed works contracts during the year 2011-12 but failed to declare corresponding service income under VCES.

When we pointed this out (January 2016), the Ministry stated (May 2016) that VCES Scheme did not envisage investigation by the DA.

(c) An assessee in Kochi Commissionerate, declared (December 2013) tax dues of ₹ 13.07 lakh for the period from October 2007 to December 2012 under VCES towards business auxiliary service and goods transport agency service and VCES-3 was issued in August 2014.

The assessee declared "Nil" income for the years 2009-10 and 2011-12 under works contract service. However, on verification with the returns (TIN 32151046307) filed with the Commercial Tax Office for the period 2009-10 and 2010-11 and the disclosure of the assessee for 2011-12, audit observed taxable service under Works Contract during the years 2009-10 to 2011-12 was ₹ 17.92 crore. However, tax dues on this income was not declared by the assessee under VCES.

This was brought to the notice of the department/Ministry in January 2016; the reply of the department/Ministry was awaited (May 2016).

This drives home the need to put a system in place, through use of technology and integration of data bases, which would make it difficult for declaration/assessees to be untruthful.

4.3 Post VCES tax administration

Any amnesty Scheme would be called a success only when the beneficiaries of such Schemes pay the declared tax dues and continue to pay taxes and comply with other statutory duties during the period subsequent to the period covered under the Scheme.

Ministry, while agreeing on certain points made by audit and accepting that specific instances of failures or bottlenecks might have remained at the Commissionerate level, stated that the larger success achieved by the scheme cannot be denied plainly. They stated that Commissionerates have their own mechanism of scrutiny of returns, anti-evasion and audit to ensure compliance and that this fact cannot be negated that the assesses base in Service Tax is huge and to tap the entire assesses pool through one single scheme is not possible.

Audit only made a limited point based on facts regarding tax administration that came to notice post-VCES as discussed below:

4.3.1 We analysed the returns due to be filed by the declarants during the post-VCES period (i.e. April 2013 to March 2015) in 15 Commissionerates where data was made available. We observed in 4,209 cases in these Commissionerates, only 13,003 returns filed by declarants as against 21,045 returns[13] due to be filed. This accounted for 62 per cent of the returns due for filing. Action taken by the department against the non-filers was not forthcoming from the records.

The very purpose of the Scheme was to enable an errant tax defaulter to return to the path of honesty. We noticed that many beneficiaries failed to adopt the path of rectitude and civic responsibility, post VCES period, calling to question the success of the Scheme.

The department had failed to initiate stringent action against the stop-filers/non-filers, who had enjoyed the immunity provisions under VCES and again reverted back to the habit of non-filing of returns.

When we pointed this out (between October and December 2015) the Ministry stated (May 2016) that the action was initiated in 12 Commissionerates. Reply was awaited in respect of the remaining three Commissionerates.

4.3.2 The department did not initiate any action to recover the balance of the declared tax dues or to levy applicable interest and penalty in respect of the rejected cases. The total tax dues involved in the 78 rejected cases in 11 Commissionerates amounted to ₹ 23.02 crore.

When we pointed this out (between October 2015 and January 2016) the Ministry stated (May 2016) that the remedial action was initiated against the declarants.

[13] At five half yearly returns due per assessee

Chapter 5 : Conclusion and Recommendations

5.1 Conclusion

The performance audit revealed that the Scheme was drafted with a number of ambiguities and deficiencies which could have been removed through use of Section 113 and by issuing appropriate clarifications. Instead clarifications were issued contrary to the spirit of the scheme.

The responses of the department revealed that their intention was only to rake in whatever revenue they could and not to use this as an opportunity to improve tax administration. Even elementary checks and balances were not put in place to ensure filing of truthful declarations by the declarants and for department to rely on the "truthfulness" of the declarations. Provision to preempt untruthful declarations and provisions to check substantially false declarations were as good as redundant. Further, the scheme was introduced with undue haste as the department responded with 'lack of time' to several audit observations.

The hope that the one time amnesty scheme will motivate defaulters to come back into the tax fold has had a limited impact as a considerable number of declarants under the scheme have reverted to being non-filers.

5.2 Recommendations

VCES stipulates that after issuance of VCES-3, no action in any manner can be taken against the declarants. As per the statistical information received from the Ministry, from the total processed declarations, the discharge certificates (VCES-3) were issued in 71 per cent cases. Keeping this in view, the recommendations for this Performance Audit are given in two parts viz., recommendations that should be considered while framing any amnesty Schemes in future and recommendations relating to areas where corrective action is feasible post VCES period.

Part-1 <u>Recommendations for future reference</u>

1. The use of IT platforms, integrated with the existing automated systems, for self declarations as well as scrutiny and follow up by the department for such Schemes may be considered.
2. Defining checklists for verifying the truthfulness of declaration filed by the declarants.
3. Identification of challans related to such schemes must be ensured by use of IT Platforms.
4. Provisions/clarification issued should not dilute the safeguards prescribed in the existing provisions as well as the express intention of the Scheme.

The Ministry accepted the first three recommendations and, in respect of recommendation No.4, stated that it must be noted that the purpose of this Scheme was to cover as many defaulters as possible and that there should not be any attempt to defeat the purpose of the Scheme.

Audit opines that the section 113 of Finance Act, 2013 gives powers to remove difficulties but without being inconsistent with the provisions of this Scheme.

Part-2 <u>Recommendations for corrective action Post VCES</u>

5. Cenvat credit should be allowed in respect of only those service tax payment under this Scheme for which documents prescribed in rule 9 of Cenvat Credit Rules, 2004 are available.
6. The amnesty Scheme should be followed by an extensive drive to bring evaders to tax net through departmental investigation and vigilance wings, so as to send a strong message to the defaulters who did not come clean despite the Scheme, to have effective deterrent effect and also to boost morale of regular tax payers.
7. A rigorous follow-up procedure through monitoring of filing of returns and scrutiny of such returns should be ensured to facilitate success as well as impact assessment of the Scheme.

The Ministry accepted all the above recommendations and stated that an instruction had been issued for follow up action regarding declarants as well as sectors which had given rise to a lot of declarations.

New Delhi **(HIMABINDU MUDUMBAI)**
Dated: 18 July 2016 **Principal Director (Service Tax)**

Countersigned

New Delhi **(SHASHI KANT SHARMA)**
Dated: 18 July 2016 **Comptroller and Auditor General of India**

Abbreviations

Abbreviations

ACES	Automation of Central Excise and Service Tax
ADGCEI	Additional Director General Central Excise Intelligence
CAG	Comptroller and Auditor General of India
CBEC	Central Board of Excise and Customs
CCE	Commissioner of Central Excise
Cenvat	Central Value Added Tax
CERA	Central Excise Receipt Audit
DA	Designated Authority
DG	Director General
DGCEI	Directorate General of Central Excise Intelligence
EA 2000	Excise Audit 2000
FIFA	Federation International De Football Association
GTA	Goods Transport Agency
IT	Information Technology
Ltd.	Limited
MTOP	Minimum Take Or Pay charges
NSDL	National Security Depository Limited
OIO	Order In Original
Pvt.	Private
SCN	Show Cause Notice
SIR	Survey, Intelligence and Research
SOF	Statement of Facts
ST	Service Tax
STVCE Rules	Service Tax Voluntary Compliance Encouragement Rules, 2013