FOURTEENTH KERALA LEGISLATIVE ASSEMBLY

COMMITTEE
ON
PUBLIC ACCOUNTS
(2016-2019)

ELEVENTH REPORT

(Presented on 7th February, 2018)

SECRETARIAT OF THE KERALA LEGISLATURE

THIRUVANANTHAPURAM

2018

FOURTEENTH KERALA LEGISLATIVE ASSEMBLY

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On

Paragraphs relating to Commercial Taxes Department contained in the Report of The Comptroller and Auditor General of India for the year ended 31 March 2011 (Revenue Receipts)

351/2018.

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INTRODUCTION

I, the Chairman, Committee on Public Accounts, having been authorised by the Committee to present this Report, on their behalf present the 11th Report on paragraphs relating to Commercial Taxes Department contained in the Report of the Comptroller and Auditor General of India for the year ended 31st March, 2011 (Revenue Receipts).

The Reports of the Comptroller and Auditor General of India for the year ended 31st March, 2011 (Revenue Receipts) was laid on the Table of the House on 6th March, 2012.

The Committee considered and finalised this Report at the meeting held on 30-1-2018.

The Committee place on record their appreciation of the assistance rendered to them by the Accountant General in the examination of the Audit Report.

V. D. SATHEESAN,

Chairman,
Committee on Public Accounts.

Thiruvananthapuram,
30th January, 2018.

REPORT

DEPARTMENT OF COMMERCIAL TAXES

Tax administration

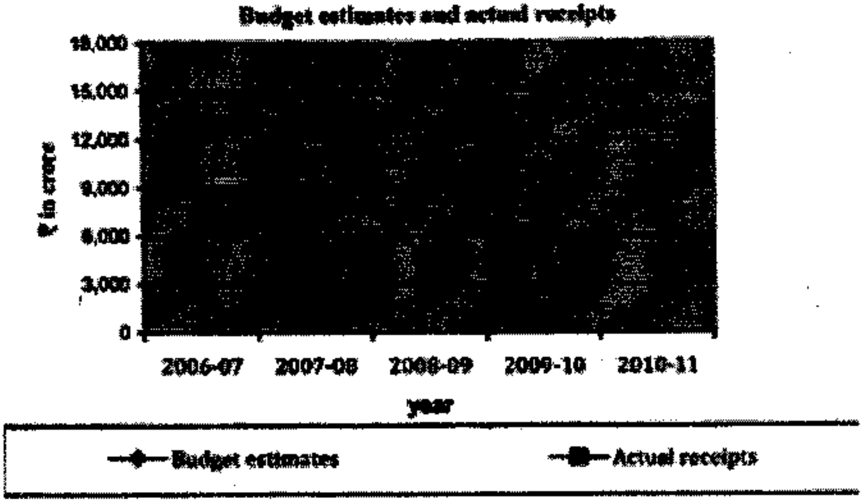
The Commercial Taxes Department contributes a major part of the revenue of the State. The revenue is derived from the assessment and collection of different taxes like sales tax, value added tax and central sales tax which are regulated by the Kerala General Sales Tax Act, 1963, the Kerala Value Added Tax Act, 2003, the Central Sales Tax Act, 1956 and notifications issued by the Department from time to time. The Department is under the administrative control of the Secretary to Government, Taxes. The Commissioner of Commercial Taxes administers the Acts and Rules. He is assisted by Joint Commissioners, Dy. Commissioners, Asst. Commissioners and Commercial Tax Officers. The assessment, levy and collection of tax is done by Assistant Commissioners and Commercial Tax Officers.

Trend of receipts

Actual receipts from VAT/tax on sales, trade etc. during the last five years (2006-07 to 2010-11) along with the budget estimates during the same period is exhibited in the following table and graph.

(₹ in crore)

Year	Budget Estimates	Actual receipts	Variation	Percentage of variation	Total tax receipts of the State	Percentage of actual receipts vis-a-vis total tax receipts	Percentage of growth rate
2006-07	7,930.38	8,563.31	(+) 633.93	(+) 7.98	11,941.82	71.71	21.67
2007-08	10,035.51	9,371.76	(-) 663.75	(-) 6.61	13,668.95	68.56	9.44
2008-09	10,616.39	11,377.13	(+) 760.74	(+) 7.17	15,990.18	71.15	21.39
2009-10	12,733.94	12,770.89	(+) 36.95	(+)0.29	17,625.02	72.46	12.25
2010-11	15,125.69	15,833.11	(+) 707.42	(+)4.67	21,721.69	72.89	23.97



We noticed that the Department was able to achieve a healthy growth rate of 23.97 per cent, the highest in the last five years, during 2010-11.

Assessee profile

The number of dealers registered at the end of 2008-09, 2009-10 and 2010-11 is shown below:

2008-09	1,59,207
2009-10	1,59,665
2010-11	1,69,298

We noticed significant increase (9,633) in the number of dealers during 2010-11. The VAT collection from the top 50 dealers in the State was ₹4,610.75 crore which was 29.12 per cent of the total collection. Out of the total dealers, 24,712 dealers constituting 14.60 per cent were paying tax at 0.5 per cent under the category of presumptive tax payers.

Tax collection from KGST during 2010-11 was ₹ 7,402.07 crore as per the Finance Accounts prepared by the Accountant General (A&E). However, our analysis revealed that tax as per the returns filed by five major dealers alone was ₹ 7,368.45 crore and the month wise collection under the KGST recorded by the Department was ₹ 7,243.64 crore. Hence, the Department may reconcile the figures and rectify the difference.

Receipt of VAT per assessee

The receipt of VAT/sales tax per assessee during 2010-11 was ₹ 9.15 lakh, which was higher than the previous year's receipt of ₹ 7.79 lakh by ₹ 1.36 lakh.

Arrears in sales tax assessments

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

Opening balance	9,267
Addition during 2010-11 including remanded cases	3,826
Total	**13,093**
No of assessments completed	6,947
Arrear cases - 6,155	
Current cases - 512	
Remanded cases - 280	
Closing balance	6,146

The Department completed 6,947 assessments under the KGST which was 53.05 per cent of the assessments due for finalisation.

We recommend the Government to complete assessments of the remaining cases in a time bound manner.

[Audit paragraphs 2.1 to 2.5 contained in the Report of the Comptroller and Auditor General of India for the year ended 31st March 2011 (Revenue Receipts).

Notes furnished by the Government on the above audit paragraph is included as Appendix II]

While seeking explanation regarding the reason for variation in the figures exposed by the Audit and the reason for non-reconciliation, the witness, Commissioner of Commercial Taxes deposed that since the oil companies contributed towards CST and VAT also in addition to KGST and it would be reconciled accurately by taking into account the amount under CST & VAT. In this context an official from the office of the Accountant General pointed out that there was difference in figures as total receipts as per the returns filed by 5 major dealers, constitute ₹ 7368.45 crore and as per the records produced by the department at the Audit total amount towards KGST as per all assessment was ₹ 7243.64 crore and this was not reconciled, the witness, Commissioner of Commercial Taxes replied that a detailed reply should be furnished to the Committee after studying the case properly. The Committee accepted the explanation furnished by the department.

2. Regarding the audit observations about the increase in VAT/Sales tax per assessee during 2010-11, the department depose that there was a steady increase (10%) in receipt of VAT/Sales Tax per assessee and the Committee accepted the explanation.

3. When the committee sought the present position regarding KGST assessments the witness, Commissioner of Commercial Taxes Department replied that about 48 cases of Pre-VAT period (2004-05) were pending , and most of them were subjudice in nature. He also supplemented that out of the latest 1176 cases 753 belonged to the period of 2013-2014. To a query of the Committee, that how much money had to be realised, related to pre-VAT period the witness replied that it could be ascertained only after completing the assessment process. Regarding the disciplinary action, initiated against the least performed officers the Committee was informed that the officers who were placed under suspension had been reinstated to the service but disciplinary action has been pending. Then the Committee appreciated the department for settling as much as 40000 tax assessment cases in a record time and termed it as the commendable achievement of the department.

Conclusions/Recommendation

4. The Committee directs the Taxes Department for conducting immediate reconciliation of KGST, CST and VAT returns from the assessees to rectify the variations in tax figures.

Cost of Collection

The gross collection of revenue reciepts under the head, tax on sales, trade etc., expenditure incurred on collection and the percentage of expenditure to gross collection during 2006-07 to 2010-11 along with the all India average percentage of expenditure on collection to gross collection for relevant years are mentioned below:

Year	Collection	Expenditure on collection of revenue	Percentage of expenditure to gross collection	All India average percentage over the previous year
	(₹ in crore)			
2006-07	8,563.31	78.21	0.91	0.91
2007-08	9,371.76	89.75	0.96	0.82
2008-09	11,377.13	102.59	0.90	0.83
2009-10	12,770.89	126.01	0.99	0.88
2010-11	15,833.11	115.61	0.73	0.96

Source: Finance Accounts and Departmental figures.

We are glad to note that the Department had reduced the cost of collection by 8.25 per cent during 2010-11.

Analysis of collection

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

(₹ in crore)

Revenue head	2008-09	2009-10	2010-11
Sales Tax	5,881.97	5,212.92	7,402.07
VAT	5,035.19	7,235.26	8,097.15
CST	425.38	292.94	310.42

The above table indicates that during 2010-11 collection of sales tax increased by ₹ 2189.15 crore and VAT collection by ₹ 861.89 crore. We observed that the significant increase of 41.99 per cent under Sales tax was due to steady increase in the price of petroleum products during 2010-11.

[Audit paragraphs 2.6 to 2.7 contained in the Report of the Comptroller and Auditor General of India for the year ended 31st March 2011 (Revenue Receipts).

Notes furnished by the Government on the above audit paragraph is included as Appendix II]

5. As the witness, deposed that the cost of collection recorded in the years 2010-2011, and 2012-2013 were lower than the national average, but in 2011-12, it was a little bit more than national level. The Committee approved the explanation submitted by the department.

6. Taking into account of the audit observation on the analysis of tax collection made by the Accountant General, the Committee opined that four factors viz, turn over, rate of tax, inflation and efficiency administration, hugely affects the tax collection. Then the Committee decided to recommend the Taxes Department that a statistical analysis should be done regarding the individual contribution of the above mentioned four factors.

Conclusion/Recommendation

7. The Committee directs the Taxes department to conduct a factor/statistical analysis regarding the individual contribution of the factors such as Turn over, Rate of tax, Inflation and Efficiency Administration on tax collection and to report thereon at the earliest.

Impact of audit

Revenue impact

During the last four years, we pointed out non/short levy, underassessment/loss of revenue, incorrect exemption, application of incorrect rate of tax etc., with revenue implication of ₹ 2,520.43 crore in 8,692 paragraphs. Of these, the Department/Government accepted audit observations involving ₹ 1,200.30 crore and had since recovered ₹ 20.06 crore. The details are shown in the following table:

(₹ in crore)

Year of Audit Report	Paragraphs included		Paragraphs accepted		Amount recovered	
	No.	Amount	No.	Amount	No.	Amount
2006-07	1,004	309.17	179	250.50	108	3.18
2007-08	1,055	334.37	299	241.50	181	2.46
2008-09 Vol I	2,181	459.11	341	32.77	203	9.40
2008-09 Vol II	1	295.24	1	116.93	-	-
2009-10	4,451	1,122.54	657	558.60	588	5.02
Total	**8,692**	**2,520.43**	**1,477**	**1200.30**	**1,080**	**20.06**

The recovery position as compared to the accepted cases during the last four years was very low being only 1.67 per cent. The insignificant recovery of ₹ 20.06 crore against the money value of ₹ 1,200.30 crore relating to the accepted cases during the period 2006-07 to 2009-10 highlights the failure of the Department in recovering the Government dues promptly even in respect of cases accepted by them.

[Audit paragraphs 2.8 contained in the Report of the Comptroller and Auditor General of India for the year ended 31st March 2011 (Revenue Receipts).

Notes furnished by the Government on the above audit paragraph is included as Appendix II]

8. Considering the audit observation that the Taxes Department failed to recover Government dues promptly even in the accepted cases, the Committee noticed that ₹ 3.18 crore and ₹ 2.46 crore have only been realised against the targeted amount of ₹ 250.50 crore and ₹ 241.50 crores respectively in the years 2006-07 and 2007-08, and committee asked the reason for the marginal difference between the accepted and collected amount, the witness, Commissioner of Commercial Taxes Department informed that the major portion of the realisation was done by means of Revenue recovery proceedings which were carried out by Revenue Department and many cases were under court stay. So realisation of tax was not so easy. But the Inspecting Assistant Commissioners of the Department had been collecting 50% above of the target assigned to them. The Committee expressed its anxiety and grave

concern over the fact that only five percent of the cases pointed out by Audit had been realised so far and the balance ninety five percent remains non collected. The Principal Secretary, Taxes Department detailed the practical difficulties for the speedy enforcement of revenue recovery proceedings. At this juncture, the Committee, directed the Taxes Department that the records should be kept with regard to the reasons explaining the delay involved in the effort to collect tax and recommended that stringent action must be initiated to expedite the revenue recovery proceedings by the department. The witness, Principal Secretary, Taxes Department agreed to do so.

Conclusions/Recommendation

9. The Committee admonishes the officials of the Taxes department for their indolent attitude in realising arrears even in accepted cases and the Committee directs that the department should take stringent action to expedite the revenue recovery proceedings.

Working of internal audit wing

The internal audit wing (IAW) in the Commercial Taxes Department commenced functioning from 1 June 2009. The wing is headed by a Deputy Commissioner, three Assistant Commissioners and six Commercial Tax Officers. During the year 2010-11, against the target of 132 units 22 units were audited leaving 110 units in arrears. The Department attributed the arrears to the ceiling fixed on Travelling Allowance to Audit Officers. There were 53 IRs with 755 observations involving ₹ 80.94 crore outstanding (October 2011). Further, during 2009-10 and 2010-11 there was no clearance of observations by settlement which indicated poor response to the observations of IAW. The Department has not prepared a separate internal audit manual.

[Audit paragraphs 2.9 contained in the Report of the Comptroller and Auditor General of India for the year ended 31st March 2011 (Revenue Receipts).

Notes furnished by the Government on the above audit paragraph is included as Appendix II]

10. With regard to the audit observation that the functioning of internal audit wing in the Commercial Taxes Department was flimsy, the Committee enquired the reason for non clearance of observation made by internal audit wing, the witness, Commissioner of

Commercial Taxes replied that even though the department was handicapped with scanty staff strength over the years, there was a significant increase in their performance. He also detailed that they made about 1,333 audit observation in the year 2013-14 which involved ₹ 16.75 crore and 3066 audit observation in four years contained about ₹62 crores. To a query of the Committee he also clarified that both the Audit and Internal Audit Wing (IAW) in the department is not one and the same and Audit Assessment Wing in the department has constituted by incorporating the personal of the Internal audit wing. The Committee opined that the IAW of the department could function more effectively than the audit wing and recommended that the Internal Audit Wing should be strengthened by providing adequate staff. The Committee also necessitated the importance of implementing AG report in this regard and directed that KVATIS module should be re-checked. Responding to this, the witness, Principal Secretary, Taxes Department informed that the server capacity of the department need to be enhanced so as to meet the requirements. In this context, Committee directed that, the response of the department on the A.G. report on KVAT should be prepared point by point giving supreme priority and opined that it would definitely be a helping hand to the Government, in terms of revenue collection. Endorsing the observation pointed out by the Committee, the witness Principal Secretary, Taxes Department informed that the discussions were already held with the Accountant General in this regard, and the department was contemplating the formulation of a module enabling transfer of audit observations directly from the Office of the Accountant General to the concerned offices. He also emphasized the need for strengthening the internal audit wing in the department and insisted for creating requisite number of posts for the smooth and efficient functioning of the internal audit wing in the department. In this regard an official from the Office of the Accountant General informed that none of the objection raised by IAW was cleared during the last two years. The Committee reiterated its earlier comment that the internal audit wing in the Taxes Department should be strengthened.

Conclusion/Recommendation

11. The Committee observed that none of the observation of Internal Audit Wing during 2009-10 and 2010-11 had not been cleared by the assessment wing. The committee opines that, the internal audit wing of the Taxes department need to function more effectively

Therefore, it recommends that the internal audit wing should be strengthened by providing adequate staff and directs the department to expedite actions to clear out the objections raised by the Audit within limited time frame.

Results of audit

In 2010-11, we test checked the records of 205 units relating to KGST and VAT. We detected underassessment of tax and other irregularities involving ₹ 944.66 crore in 3,152 cases which fall under the following categories:

(₹ in crore)

Sl. No.	Categories	No. of cases	Amount
1	**Compounding Scheme in Commercial Taxes Department (A review)**	1	38.35
2	**Utilisation of declaration forms in inter-state trade (A review)**	1	326.27
	Value Added Tax		
3	Turnover escaping assessment	878	156.51
4	Grant of irregular exemption	392	46.32
5	Application of incorrect rate of tax	258	71.44
6	Grant of excess input tax credit	550	20.74
7	Incorrect grant of concessional rate of tax	23	0.51
8	Non/short levy of interest	16	0.20
9	Other lapses	1,033	284.32
	Total	**3,152**	**944.66**

The Department accepted underassessment and other deficiencies of ₹ 66.22 crore in 750 cases, of which 332 cases involving ₹ 50.94 crore were pointed out in audit during the year 2010-11 and the rest in earlier years. An amount of ₹15.70 crore was realised in 522 cases of which 216 cases involving ₹ 2.44 crore were pointed out during the year 2010-11.

Two reviews on "Compounding Scheme in Commercial Taxes Department" and "Utilisation of declaration forms in inter-state trade" with financial impacts of ₹ 38.35 crore and ₹ 326.27 crore and a few illustrative audit observations involving ₹ 85.03 crore are mentioned in the following paragraphs.

Introduction

The Kerala Value Added Tax Act, 2003 (KVAT), Kerala General Sales Tax Act, 1963 (KGST), Central Sales Tax Act, 1956 (CST) and the rules made thereunder govern the levy and collection of tax on sale or purchase of goods in the State.

During the KGST period, dealers in certain evasion prone commodities like jewellery, work contract, cooked food etc., were permitted to pay tax at compounded rates. This was a simplified procedure under which tax was not related to the turnover of the dealer for the assessment year. The tax payable under the compounding scheme was less than the tax payable under the regular scheme and was attractive to the dealers and hassle free. The Government's intention was to attract more dealers into the tax net.

While introducing the KVAT Act in 2005, a scheme was included under Section 8 for dealers in works contract, metal crusher units, cooked food, video cassette, medicine and jewellery. Similarly, dealers liable to pay turnover tax on sale of IMFL under Section 5(2C) of the KGST Act were given an option to pay tax at compounded rates based on the purchase value of liquor from 1 April 2005. This was called the Compounding Scheme.

Organisational setup

The Principal Secretary to Government (Taxes) heads the Department at the Government level and Commissioner is in charge of the Department at the Department level. The levy and collection of tax under the KVAT Act, 2003, the KGST Act 1963 and CST Act, 1956 is administered by the Commissioner of Commercial Taxes with the assistance of Joint Commissioners, Deputy Commissioners and Inspecting Assistant Commissioners. Assistant Commissioners (Assessment) and Commercial Tax Officers are delegated with powers for assessment, levy and collection.

Audit objectives

We conducted the review to:

- examine efficiency and effectiveness of the compounding scheme in achieving the intention of its introduction.

- see the extent of compliance with the prescribed rules and procedures, and

- identify potential risk areas leading to leakage of revenue.

Scope and methodology of audit

We conducted the review during the period from December 2010 to May 2011 and test checked the assessment records for the years 2005-06 to 2009-10 of dealers who had opted for compounding in 32 assessment circles out of 102 assessment circles spread over nine[1] revenue districts. We selected the samples by simple random number sampling method and collected details of import of gold from Customs house, Air cargo complex, Cochin International Airport at Nedumbassery and cross verified it with the assessment records of respective importers.

We also test checked the registers and records maintained in Commissionerate of Commercial Taxes as well as in selected Commercial Taxes assessment circles in the selected districts pertaining to dealers paying tax under the compounding scheme and also cross checked the data gathered from other sources ie. Customs house, KVATIS and TINXYS.

Acknowledgment

We acknowledge the co-operation extended by the Commercial Taxes Department, Customs house and Air Cargo complex. We conducted an entry meeting on 24th January, 2011 with the Secretary to the Government and explained the modalities of audit. The views expressed by the Secretary and the Commissioner of Commercial Taxes were taken care of. We conducted an exit conference on 13th June, 2011 with the Secretary (Taxes) and explained the important audit findings. The views of the Department at the time of exit conference and their responses to our queries/observations have been incorporated in the report.

1 Ernakulam, Kollam, Kottayam, Kozhikode, Malappuram, Palakkad, Pathanamthitta, Thiruvananthapuram and Thrissur.

AUDIT FINDINGS

Trend of revenue

The following are the details of budget estimate and actual receipt of the Commercial Taxes Department during the period 2005-06 to 2009-10.

(₹ in crore)

Year	Budget estimates	Actual receipt	Percentage of actual collection to budget estimates
2005-06	8,200.01	7,037.97	85.83
2006-07	7,930.38	8,563.31	107.98
2007-08	10,035.51	9,371.76	93.39
2008-09	10,616.39	11,377.13	107.17
2009-10	12,733.96	12,770.89	100.29

The following are the details of revenue realised under the compounding scheme:

(₹ in crore)

Commodity	2005-06	2006-07	2007-08	2008-09	2009-10
Gold	NA	47.24	60.83	83.94	112.21
Metal Crusher	#	#	13.45	20.19	21.98
IMFL	#	48.26	66.03	96.44	120.51

#details though called for were not furnished by the Department

The Commissioner of Commercial Taxes stated that details of works contract, medicine, video cassette and cooked food are not readily available.

The intention behind the introduction of Compounding Scheme was to bring more dealers under the tax net and thereby enhance revenue collection. But we found that the Department did not maintain a database of dealers who had opted for compounding. Hence, the Department was unable to evaluate whether they were able to attract more dealers into the tax net. Further, targets were not fixed for enlisting dealers and collection of tax. Due to these reasons the Department was unable to clearly assess the impact of the scheme and modify it for further improvement.

We recommend that the Government may develop a database of dealers who opt for compounding, to fix a target for collection of tax under the scheme and analyse the data in a scientific manner to refine the scheme.

[Audit paragraphs 2.10 to 2.11.6 contained in the Report of the Comptroller and Auditor General of India for the year ended 31 March, 2011 (Revenue Receipts).

Notes furnished by the Government on the above audit paragraph is included as Appendix II

12. With regard to the audit observation, the Committee asked the reason for non-existence of a system to watch the revenue realized under compounding scheme category wise, the witness, Commissioner of Commercial Taxes Department informed that compounding has been done through KVATIS at present. In this context the Committee remarked that necessary modifications should be done in the KVATIS to generate the category wise details of revenue realised (Compounded and non compounded).

Conclusions/Recommendations

13. The Committee observes with concern that, non-maintenance of database of dealers who opt for compounding and notification of targets for enlisted dealers and collection of tax disabled the department to clearly assess the impact of compounding scheme. Therefore the Committee recommends that necessary modifications should be made in the KVATIS to generate category wise details of revenue realised under compounding as well as non compounding schemes.

WORKS CONTRACT

Incorrect grant of permission to pay compounded tax

Section 8 (a) of the KVAT Act, 2003 gives an option to a works contractor to pay tax at the rate prescribed thereunder on the whole contract receipt instead of paying tax in accordance with the provisions of section 6 of the Act. Under Rule 11 of the KVAT Rule

2005, the contractor is required to file an application in Form IDA along with a copy of agreement executed with the awarder of the contract and the work schedule for availing the benefit of the scheme. Further, Rule 24B stipulates that contractors who undertake construction or development of flats etc., should file a declaration in Form 49 containing the details of ongoing projects, transfer of apartment etc.

We test checked the assessment records of 51 contractors in three[2] assessment circles, and noticed that in 16 cases the applications filed were not accompanied by the documents required under Rule 11. However, the AA accepted the applications and accorded permission for payment of compounded tax instead of rejecting the same and levying tax under section 6 of the Act. This resulted in short collection of tax of ₹ 6.80 crore.

We pointed out the matter and the Commissioner opined that permission granted was conditional and the copies of agreements would be insisted upon at the time of submission of final return. The reply is not acceptable as Rule 11 (1) read with (1A) stipulates that application for exercising option for compounded tax under Section 8 shall be filed within 30 days from the date on which the contract in respect of which such option filed is concluded. Along with the application the dealer shall furnish a copy of the agreement executed by the contractor with the awarder and work schedule.

Section 8 (a) of the KVAT Act 2003, envisages that the benefit of payment of tax under the said section should not be applied to any work contract where the transfer is in the form of goods. The Supreme Court of India had ruled[3] that the work of supply and installation of elevator is not a work contract and hence not entitled for compounding.

We noticed that M/s Infosoft Digital Designing Services (P) Ltd., an assessee on the rolls of CTO, third circle, Thiruvananthapuram undertook a contract work which was in the nature of transfer of goods ie. "Supply and installation of flight information display system" and received ₹ 1.17 crore during the year 2008-09. The AA, however, permitted the contractor to pay compounded tax of ₹ 3.51 lakh.

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2 CTO(WC) Kottayam, Mattancherry and Thrissur.

3 Kone Elivator (India) Ltd., V/s State of Andhra Pradesh [140STC22(SC)].

Since the contractor transferred materials in the form of goods and the instant case is similar to the Supreme Court judgement cited above, he was not eligible to opt for the compounding scheme. The incorrect grant of permission resulted in short levy of tax of ₹12.27 lakh (including interest).

We pointed out the matter and the AA stated that the work forms a part of a composite contract which includes floor/ceiling/wall mounts as per site requirements and hence that will not fall under the category of transfer in the form of goods. The reply is not acceptable since out of the total contract amount of ₹ 1.76 crore, ₹ 1.63 crore (nearly 90 per cent) related to cost of equipment and only the balance of ₹ 0.13 crore related to installation charges, which was incidental to the main contract.

Application of incorrect rate of compounded tax

Section 8(a) of the KVAT Act 2003, as amended by the Kerala Finance Act 2008, specifies the rate of compounded tax payable by contractors having registration under the CST Act, 1956 as eight per cent of the whole contract receipt. It has further been provided under the said Section that in the case of any work covered under the above provisos which remains unexecuted fully or partly at the end of the year, the contractor shall continue to pay tax in respect of such works in accordance with the provisions of this clause.

By the Kerala Finance Act 2009, further provision has been inserted under Section 8(a) of the Act to the effect that in respect of works which commenced prior to 1st April, 2008 and which remains partly unexecuted as on 1st April, 2008 the contractor shall pay tax at the rates as it existed prior to 1st April, 2008 till the completion of work, or up to 31st March, 2009 whichever is earlier. This provision came into effect from 1st April, 2009 and is not applicable for 2008-09.

We found from the assessement records of four assessees in four works contract circles that the amount of compounded tax remitted for the year 2008-09 by these four works contractors was not at the rate prescribed, resulting in short remittance of tax and interest amounting to ₹ 6.64 crore as detailed below:

Name of Office	Name of assessee	Amount of contract receipt	Tax remitted	Tax due @ 8%	Short remittance (including cess)	Interest due
		₹ in lakh				
CTO (WC) Palakkad	Oceanus Dwelling (P) Ltd.	1,786.53	71.46	142.92	72.18	14.44
CTO (WC) Mattancherry	Sargam Builders	139.73	4.19	11.18	7.06	1.48
CTO (WC) Ernakulam	Assest Homes (P) Ltd.	8,125.50	194.99	650.04	459.61	96.52
CTO (WC) Pathanamthitta	Btech Builders	199.02	5.97	16.08	10.21	2.53
Total					**549.06**	**114.97**

M/s Vellappally Construction, an assessee on the rolls of CTO (WC), Kottayam having registration under the CST Act, opted for payment of tax under the compounded scheme and the AA permitted to pay compounded tax vide orders issued during October 2009. The assessee filed annual return for the year 2008-09 in form 10B disclosing a total contract receipt of ₹ 5.02 crore. Out of the total contract receipt, ₹ 4.96 crore was taxed at the rate of four per cent on the ground that it related to ongoing projects and the balance of ₹ 5.53 lakh at the rate of eight per cent. Our scrutiny of the accounts of the dealer filed with the Department revealed that during the year the assessee received ₹ 7.58 crore which related to new contract entered during the year 2008-09 attracting tax at the rate of eight per cent. Thus the AA did not notice the turnover that escaped assessment as well as application of incorrect rate of tax, which resulted in short remittance of tax of ₹ 50.15 lakh (including cess and interest).

Irregular grant of exemption

Section 8(a) (ii) of the KVAT Act inserted by Finance Act 2009, provides that any works contractor having registration under the CST Act or an importer as defined under the Act, opting for payment of tax under the compounding scheme should pay tax at the rate of three per cent of the contract receipt after deducting the purchase value of goods effected by way of interstate purchase and for the purchase value of goods so deducted should pay tax at the schedule rate applicable to such goods.

We noticed that M/s KMC Construction Ltd., an assesee on rolls of CTO (WC), Mattanchery who opted for payment of tax under the compounding scheme did not remit the tax due on goods valued ₹ 6.41 crore purchased interstate and transferred through works contract during the year 2009-10. This resulted in non remittance of tax of ₹ 60.57 lakh (including interest). However, we noticed that the assessee had disclosed ₹ 31.58 lakh as output tax due on "others" details of which are not ascertainable.

We observed that in the following cases, tax was computed on the contract receipt after deducting labour charges thereon instead of on the whole contract receipt. This resulted in short computation of tax of ₹ 25.99 lakh (including interest) as detailed below:

(1)	(2)	(3)	(4)	(5)	(6)
Name of office	Name of assessee/year	Contract receipt	Amount deducted towards labour	Tax due (including) Cess @ one per cent for 2008-09 and 2009-10 /interest	Total
		(₹ in lakh)			
CTO, WC, Thrissur	Swaraj Builders				
	2006-07	110.49	102.65	2.05 0.92	2.97

(1)	(2)	(3)	(4)	(5)	(6)
	2007-08	119.54	96.65	1.93 0.64	2.57
	2008-09	124.39	37.75	1.14 0.24	1.38
	2009-10	84.95	73.18	2.22 0.20	2.42
CTO, WC, Palakkad	Geogy George 2008-09	531.71	54.47	1.63 0.33	1.96
CTO, WC, Kottayam	SOJ Associates 2008-09	76.66	69.77	2.11 0.36	2.47
	Sanoj Mathew 2008-09	770.89	101.50	3.08 0.49	3.57
	South India Foundation 2008-09	192.32	111.86	3.39 0.54	3.93
Works Contract, Ernakulam	RDS Project Ltd. 2007-08	6,158.60	97.50	3.90 0.82	4.72
Total					**25.99**

We verified the cases locally and found that exemption claimed as labour in these cases were not for separate labour contract, but were part of composite contract under compounding scheme. The exemption allowed from the turnover was not correct.

Since the Department is fully computerised and returns are filed online, Government may consider building a validation in the software to ensure that the works contractors opting for compounding are not permitted to claim any deduction other than for payment to sub contractors.

Turnover escaped assessment

From the annual returns filed we noticed in the case of twelve contractors opting for payment of tax under the compounding scheme that the contract receipts returned was much lesser than that accounted for resulting in short remittance of tax of ₹ 4.65 crore (including interest) as detailed in the following table:

(1)	(2)	(3)	(4)	(5)	(6)	(7)
Name of Office	Name of Contractor	Year/ Contract receipt returned	Contact receipt as per A/cs	Turnover escaped	Tax due/Interest due	Total
			(₹ in lakh)			
CTO, Works Contact Ernakulam	M/s Jayakrishnan & Co.	2005-06 161.12	184.65	23.53	0.47 0.26	0.73
		2006-07 190.94	260.17	69.23	1.38 0.61	1.99
		2008-09 475.68	604.08	128.40	3.89 0.78	4.67
	NJK Builders (P) Ltd.	2006-07 471.31	621.21	149.87	3.00 1.32	4.32
		2007-08 397.80	682.59	284.79	5.70 1.82	7.52
	Asset Homes (P) Ltd.	2006-07 68.14	1,443.88	1,375.74	27.51 12.66	40.17
CTO, Works Contract Malappuram	K. Mosakutty	2007-08 140.53	210.36	69.83	2.10 0.31	2.41

(1)	(2)	(3)	(4)	(5)	(6)	(7)
CTO, Works Contract Kottayam	Thalapala Engineering company	2008-09 72.61	644.64	572.03	23.11 0.39	23.50
	Wexco Homes (P) Ltd.	2008-09 987.06	1,837.39	850.33	68.71 11.68	80.39
		2007-08 1,113.77	1,849.33	735.57	29.42 8.53	37.95
	Home Basics	2008-09 117.06	344.57	227.51	6.89 1.17	8.06
	Shaji Mathew	2007-08 1,117.55	1,232.15	114.60	2.29 0.73	3.02
CTO, Works Contract, Kozikode	Hilite builders	2008-09 2,458.13	4,912.15	2,454.02	198.28 25.78	224.06
CTO, Works Contract, Mattachery	JVN Properites	2008-09 96.87	158.42	61.55	1.86 0.37	2.23
CTO, Works Contract, Thrissur	Pentark Builders and developers	2008-09 388.36	576.49	188.13	15.20 2.89	18.09
	Trichur builders	2008-09 1,853.09	2,014.48	161.39	4.81 1.00	5.81
		Total				**464.92**

Shri Mohan Matew, Neelettu construction, a works contractor on the rolls of CTO (WC), Kottayam opted for payment of tax under the compounding scheme for the year 2009-10 and filed return in form 10B disclosing contract receipt of ₹ 4.05 crore. Scrutiny of the assessment records revealed that the contractor was issued certificate in form 20E for receiving contract amount of ₹4.24 crore without TDS from three awarders. However, contract amount returned as received from the said three awarders was ₹ 47.90 lakh only. Thereby contract amount of ₹ 3.76 crore had escaped assessment. This resulted in short remittance of tax of ₹ 11.38 lakh (at the rate three per cent+cess).

The Government may consider prescribing minimum percentage of the certificates filed by works contractors along with returns to be checked/cross verified by AA for exemption from TDS etc.

Omission to forfeit the illegal tax collection

Section 30(2) of KVAT Act 2003 restricts works contractors paying tax under Section 8(a) of the Act from collecting tax up to 31st March, 2008. Section 72(1) of the Act provides to forfeit to Government any sum collected by dealers by way of tax in contravention of section 30(2).

We noticed that the following works contractors, who opted for payment of tax under the scheme, collected tax as evidenced from accounts as well as from the agreement entered into with the awarders. The AA did not forfeit the amount collected by way of tax of ₹ 15.60 crore to the Government as detailed below:

(₹ in lakh)

Name of office	Name of assessee	Year	Contract receipt	Tax collected	Interest	Total
(1)	(2)	(3)	(4)	(5)	(6)	(7)
CTO (WC) Ernakulam	Mather Projects	2005-06	2,687.50	94.91	56.00	150.91
		2006-07	5,359.99	182.83	85.93	268.76
		2007-08	8,469.67	338.79	118.58	457.37

	Novel Villas	2005-06	839.51	16.79	9.91	26.70
		2006-07	1,497.97	29.96	14.08	44.04
		2007-08	1,721.64	34.43	12.05	46.48
	Korath Gulf Links	2006-07		3.04	1.43	4.47
		2007-08		14.51	5.08	19.59
	Kent Construc tion	2006-07	285.58	6.57	3.09	9.66
		2007-08	845.68	33.83	11.84	45.67
	Desai Homes	2005-06	4,421.77	88.44	52.18	140.62
		2006-07	5,747.48	114.95	54.03	168.98
		2007-08	5,893.76	117.88	41.26	159.14
CTO (WC) Pathanamthitta	Tropicana Reality Developers	2007-08	380.03	7.61	2.82	10.43
	B-Tech Builders	2007-08	262.94	5.28	1.95	7.23
Total						**1,560.05**

We pointed out the matter and the AA replied that agreement contains a clause for payment of tax including sales tax, but the clause by itself is not the basis to conclude that the dealer has collected tax from the customers. The reply is not acceptable as the contract agreement clearly specifies the payment of tax to be paid along with each installment. Further, while applying for compounding the dealer had filed the copy of the agreements which clearly indicated the element of tax payable to the dealer by the purchasers.

[Audit paragraphs 2.11.7.1 to 2.11.7.5 contained in the Report of the Comptroller and Auditor General of India for the year ended 31st March, 2011 (Revenue Receipts).

Notes furnished by the Government on the above audit paragraph is included as Appendix II]

14. Regarding the audit observation about incorrect grant of permission to pay compounded tax, the committee accepted the explanation furnished by Department.

15. With regard to the audit observation that the contractors viz. M/s Oceanus Dwellings (P) Ltd., M/s B-Tech Builders, M/s Sargam Builders, Assets Homes (P) Ltd., and M/s Vellappally structures, had incorrectly remitted the amount of compounded tax for the year 2008-09, as against the prescribed rate that, resulted in short remittance of tax and interest amounting to ₹ 6.64 crore, the Committee sought the explanation regarding the same. In the case of M/s Oceanus Dwellings (P) Ltd., there was variation of figures booked by the audit. In this regard, the witness, Commissioner of Commercial Taxes appraised that M/s Oceanus Dwelling (P) Ltd., had different projects which were compounded @ 4% and @ 8% and accordingly tax was calculated separately and difference pointed out by Audit might be due to the calculation of tax at flat rate of 8% for all projects. The cases of M/s B-Tech builders and M/s Sargam Builders were pending and mistake occurred in the annual audit statement of Asset Homes (P) Ltd. had been rectified subsequently. Regarding, M/s Velappally Construction, the Committee sought the reason for the short remittance of tax of ₹50.15 lakh, an official from the Office of the Accountant General detailed that as per the statements filed by the firms, there was huge variation between the opening and closing balances and as per the submitted data all the ongoing projects were completed in the year 2007-08 and new projects were started from 2008-09 and tax was calculated accordingly. In this context, the Committee directed the Taxes Department to furnish a clear response to the audit objection and the witness, Commissioner of Commercial Taxes agreed to do so.

16. Regarding the irregular grant of exemption to M/s KMC Constructions Ltd., the Committee was informed that an amount of ₹ 2,43,72,497 was allowed as subcontract which was not included in the original returns submitted for audit. The CCT submitted that the AA reported that documents to prove subcontract was available with firm. The Committee accepted the explanation furnished by the Department.

17. With regard to the audit observation that irregular exemption on labour was claimed by M/s Swaraj Builders the Committee wanted the details, and the witness, Commissioner of Commercial Taxes Department replied that deduction was done on the basis of separate labour contract. In this context an official from the Office of the Accountant General intervened and informed that large amount of money seems to be deducted as labour component in compounded cases and opined that eventhough separate labour contract was liable to tax in the case of composite contract labour component could not be deducted in compounding. But since documents were not available for auditing they could not ascertain the exact position. In response to the comment made by the Accountant General regarding the non availability of document, the Committee directed the department to produce the documentary evidence before the Accountant General to counter the comments and the witness, Commissioner of Commercial Taxes agreed to do so.

18. To a query of the Committee, about the recollection of the amount exempted irregularly to Geogy George (2008-09), CTO (WC) Palakkad the CCT assured to submit the report for verification by AG at the earliest.

19. In the case of Soj Associates, the committee directed the department to submit the documents on labour contracts to AG immediately.

20. In the case of NJK Builders (P) Ltd., an official from the office of the Accountant General firmly stood for the reconciliation of figures booked in the Accounts and Tax returns in order to ascertain the quantum of amount escaped from assessment and the witness Commissioner of Commercial Taxes agreed with the suggestion made by the Accountant General.

21. With regard to the audit reference on M/s Assets Homes Pvt. Ltd., CTO (WC) Ernakulam the Committee reiterated that the opinion from the Law Department regarding whether land value need to be taken into account for the calculation of tax should urgently be secured to settle the issue the witness Commissioner of Commercial Taxes agreed to do so.

22. With regard to audit objection in respect of Shri Mosakutty, Moothadathu House, Morayur, Malappuram, Home Basics (2008-09) CTO (WC) Kottayam, Shaji Mathew (2007-08), Hilite Builders (2008-09) CTO (WC) Kozhikode, JUN Properties, M/s Pentark Builders and Developers for the year 2008-2009, M/s Thrissur Builders (2008-09), Shri Mohan Mathew, Neelettu Construction, the committee accepted the explanation furnished by the department.

23. With regard to Wexco Homes (P) Ltd., the CCT appraised that the firm regularly pay tax every year, but cumulative figures were shown in the account statement. But the representative from the Office of the Accountant General submitted that cumulative figure could not be shown in the accounts, it should be 'for the year receipts'. Then the Committee directed to submit a detailed reply, the witness, Commissioner of Commercial Taxes Department agreed to do the same. The Committee was also informed that the case of Thalapala Engineering RR proceedings was not completed.

24. The Committee was informed that the tax collected mentioned in form 13A was not actually collected tax, but it was the tax element of the transfer value of materials and an official from Office of the Accountant General submitted that the firm had not produced any document to prove that the figure was wrongly entered. The witness, Commissioner of Commercial Taxes Department assured to re-examine the case as per the direction by the Committee.

Conclusions/Recommendations

25. The committee realises that tax evasion has been occurred in many cases due to incorrect application of compounding tax rate as well as turnover. Therefore the Committee urges the Taxes Department to furnish a comprehensive report regarding the system of tax compounding and turnover assessment with special emphasis on the measures to curtail revenue lapse.

MECHANISED METAL CRUSHER UNIT [SN 8(B)]

Incorrect computation of compounded tax

The KVAT Act allows dealers producing granite metal with the aid of mechanised crushing unit to pay tax at the rates specified under Section 8(b) on the basis of the jaw size of the crushers used by them. The Act, as it stood up to 31st March, 2008, provided for levy of tax on primary crushers[4] at the rate of 50 per cent of the rates specified in accordance with jaw size, thereby assessing each and every primary crushing unit. The Act was amended with effect from April 2009. The Minister for Finance in the budget speech clarified: "the amendment was made to clear doubt regarding tax on primary crushers and made primary crushers as a whole for the purpose of computation of compounded tax, at the rate of 50 per cent of the aggregate of the tax payable on secondary crushers[5]".

M/s K K Rocks and Granites India Pvt. Limited, a mechanised metal cursher unit on the rolls of CTO, third circle, Thiruvananthapuram had opted for payment of tax under section 8(b) of the Act for the year 2007-08. The unit possessed a cone crusher of jaw size 36" X 8" which is classified separately from 2007-08 onwards as it is neither a primary nor a secondary crusher on which tax was paid at the rate of ₹ 3.60 lakh (secondary crusher) instead of at the correct rate of ₹ 7.50 lakh resulting in short remittance of tax of ₹ 3.90 lakh.

We found from the inspection report dated 4th July, 2008 available in the records of CTO, Thiruvalla that M/s Panachayil Industries was in possession of 14 metal crusher units, which they opted for compounding in 2008-09. However, in 2009-10, they opted for compounding of nine crusher units only. The AA had no details regarding disposal of plant and machinery by the dealer and hence the matter needs to be investigated as to whether there was short levy of compounding tax during 2009-10.

Non-consideration of addition made in fixed assets (Plant and machinery)

We test checked the accounts of metal crusher units, and noticed that in the following cases, considerable addition to fixed asset (Plant and machinery) was accounted for during the years. The assessing authorities did not ascertain whether the addition was due to purchase of crusher units. Considering the huge amount of addition made in the fixed asset, the possibility of undisclosed crusher unit in these cases cannot be ruled out. This requires detailed enquiry by the AA.

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4 Primary crushers are crushers in which rocks upto 5ft by 4ft by 4ft in size were crushed to size of 12 inches or smaller.

5 At secondary crusher, the crushed stone passes over a screen and the metal is again crushed into smaller size.

Sl. No.	Name of Office	Name of the assesee	Year	Addition made to fixed asset during the year (₹ in lakh)
1	CTO, 3rd Circle, Thiruvananthapuram	KK Rocks and Granites India (P) Ltd.	2007-08	41.50
			2008-09	174.02
2	Special Circle, Thrissur	M/s Thomson Granite (P) Ltd.	2009-10	23.46
3	CTO, Angamaly	M/s Poabs Granite Products (P) Ltd.	2008-09	1,466.59
4	CTO, Thiruvalla	M/s Panachayil Industries	2006-07	135.43
			2007-08	300.54
			2008-09	309.84

We recommend that the Government may consider issuing instructions for periodical inspection of metal crusher units so as to ascertain the number of units in the possession of the assessee.

[Audit paragraphs 2.11.8 contained in the Report of the Comptroller and Auditor General of India for the year ended 31st March, 2011 (Revenue Receipts).

Notes furnished by the Government on the above audit paragraph is included as Appendix II]

26. With regard to the audit observation about M/s K.K.Rocks and Granites India Private Ltd., the Committee was informed that part of the additional demand was collected and the balance was to be realised. In this regard an official from the Office of the Accountant General remarked that the departmental figure and the figure shown as assessment in the returns were different. The committee directed the Accountant General to verify the documents, and the Accountant General agreed to do the same.