

## CHAPTER-II: TAXES ON SALES, TRADE, ETC.

### 2.1 Results of audit

Test check of the records of the sales tax offices, conducted during the year 2008-09, disclosed underassessments of tax, non/short levy of interest/penalty, etc., amounting to Rs. 195.03 crore in 688 cases which fall under the following categories:

(Rupees in crore)			
Sl. No.	Category	Number of cases	Amount
1.	Transition from sales tax to value added tax (A review)	01	4.07
2.	Incorrect grant of exemption	08	6.74
3.	Non/short levy of tax	62	5.66
4.	Non-levy of interest	27	1.45
5.	Non-forfeiture of tax collected in excess	10	0.34
6.	Non/short levy of resale tax	17	0.31
7.	Non/short levy of cess	08	0.22
8.	Non/short levy of additional tax	16	0.20
9.	Short levy of output tax	176	73.04
10.	Non/short levy of interest/penalty	125	43.49
11.	Excess/incorrect allowance of input tax credit	92	34.60
12.	Excess/incorrect allowance of transitional relief	47	5.19
13.	Other irregularities	99	19.72
<b>Total</b>		<b>688</b>	<b>195.03</b>

During the course of the year 2008-09, the department accepted underassessments of tax amounting to Rs. 21.47 crore in 627 cases pointed out in audit in earlier years and, of that, recovered Rs. 12.98 crore in 495 cases.

After the issue of a draft paragraph, the department recovered the entire amount of Rs. 20.32 lakh in two cases.

A review on “Transition from sales tax to value added tax” involving Rs. 4.07 crore and few illustrative audit observations involving Rs. 3.34 crore are mentioned in the following paragraphs.

## **2.2 Review on Transition from Sales Tax to Value Added Tax**

### **Highlights**

- The average growth rate of revenue collection in post VAT period (2005-06 to 2007-08) declined by 0.48 *per cent* compared to average growth rate in pre VAT period (2002-03 to 2004-05).  
**(Paragraph 2.2.6)**
- Software got developed for implementation of VAT was not found suitable by the department. Also, the software was not tested before implementation nor was the source code obtained.  
**(Paragraph 2.2.7.5)**
- Scrutiny of assessment records of VAT revealed several cases of non-observance of provisions of Acts/Rules, non/short levy of tax, arithmetical inaccuracies, non-levy of penalty, etc. amounting to Rs. 3.66 crore.  
**(Paragraph 2.2.9.2)**
- Non-levy of penalty for non-filing of annual statement by 3,145 dealers for the year 2006-07 and 3,304 dealers for the year 2007-08 amounted to Rs. 15.57 crore.  
**(Paragraph 2.2.9.3)**
- There was no provision under the KVAT Act for disallowing the input tax credit on capital goods where the KVAT paid on capital goods is capitalised and depreciation claimed.  
**(Paragraph 2.2.11.1)**

### **2.2.1 Introduction**

**2.2.1.1** The Government of India recognised the need for rationalising the existing tax system by introduction of Value Added Tax (VAT) which would result in expansion of tax base, ensure buoyancy in revenue flow and ensure better compliance. The States represented by the Empowered Committee in its meeting held on 23 January 2002 unanimously decided to implement VAT.

**2.2.1.2** The White paper on VAT envisaged the following:

- i) That VAT would widen the tax base and ensure buoyancy in revenue;
- ii) Set off of tax paid at the earlier points in respect of goods sold which would eliminate cascading effect;
- iii) Other taxes would be abolished and overall tax burden rationalized; and
- iv) Promotes voluntary compliance by providing for acceptance of returns filed by the dealers on self assessment basis.

In pursuance, the Government enacted the Karnataka Value Added Tax Act, 2003 (KVAT Act) with effect from 1 April 2005.

**2.2.1.3** Some of the differences between the KVAT Act and the Karnataka Sales Tax (KST) Act were as under:

- KST was a first point levy at the rates ranging from one to 20 *per cent*. In addition, turnover tax (TOT) at one to three *per cent* on first sales turnover depending on the total turnover and at one *per cent* on second and subsequent sales turnover was leviable up to 31 March 2002. Further, with effect from 1 April 2002, resale tax (RST) was leviable at the rate of 1.5 *per cent* on second and subsequent sales turnover. Besides, additional tax at one *per cent* was also leviable on first sales turnover with effect from 1 June 2003. Under KVAT Act, tax is levied at prescribed rates at every point of sale after allowing deduction towards tax paid at the previous point (input tax credit).
- Under the KST Act supporting documents and declarations were required to be submitted along with the returns whereas VAT system provides for voluntary payment of tax by dealers and acceptance of returns on self assessment basis without requiring production of any supporting documents and declarations.
- Under the KST Act assessments were made in all the cases after scrutiny of books of accounts whereas in the VAT system scrutiny of books of accounts are made only in selected cases taken up for audit.
- Under the KST Act concessional rate of tax was levied on sale of industrial inputs to industrial units, sales to Government department and other specified bodies on production of prescribed declarations. Also sales to 100 *per cent* Export Oriented Units (EOU) were exempted subject to production of prescribed certificate obtained from the EOU. However, no such concessions/exemptions are provided under the KVAT Act.

**2.2.1.4** The salient features of KVAT Act are as under:

All the dealers registered under the KST Act were liable to get registered under the KVAT Act. Every dealer whose total turnover exceeds or who reasonably expects his total turnover to exceed Rs. 2 lakh as computed in the year ending 31 March 2005 was liable to get registered under the KVAT Act. The KVAT Act and rules framed thereunder also provided for voluntary registration by dealers whose turnover was less than the prescribed limit, and *suo moto* registration by competent authority of the department after conducting survey, inspection or enquiry. All dealers registered under the KVAT Act were assigned Taxpayers Identification Number (TIN). Under the KVAT Act, every dealer is liable to pay tax on the sale of taxable goods by him after deducting tax paid on his purchases with certain restrictions.

Every registered dealer shall be liable to pay tax on his taxable turnover,

a) in respect of goods mentioned in

- i) Second Schedule at the rate of one *per cent*
  - ii) Third Schedule at the rate of four *per cent*
  - iii) Fourth Schedule at the rate of twenty *per cent*
- b) in respect of other goods at the rate of twelve and a half *per cent*
- c) in respect of transfer of property in goods involved in the execution of works contract at the rates specified in the Sixth Schedule from 1 April 2006.
- Goods specified in the First Schedule and any other goods specified by a notification of the State Government were generally exempt.

### **2.2.2 Organisational set up**

The Commercial Taxes Department (CTD) is under the administrative control of the Finance Department. It is headed by the Commissioner of Commercial Taxes (CCT) who is assisted by the Additional Commissioners at headquarters. There are 13 Divisional VAT Offices (DVO) in the State headed by Joint Commissioners and 148 Audit Offices headed by Deputy Commissioners. At the field level VAT is being administered through 95 Local VAT Offices (LVOs) and VAT Sub Offices (VSOs) headed by Assistant Commissioners and Commercial Tax Officers respectively.

### **2.2.3 Audit objectives**

The review was aimed to ascertain whether the

- planning for implementation and the transition from the KST Act to KVAT Act was effected timely and efficiently;
- organisational structure was adequate and effective;
- the provisions of the KVAT Act and the Rules made thereunder were adequate and enforced properly to safeguard the revenues of the State;
- the internal control mechanism existed in the Department and was adequate and effective to prevent leakage of revenue.

### **2.2.4 Scope and methodology of audit**

The review covered the period from 2005-06 to 2008-09 (up to December 2008) and was conducted between April and September 2009. Information on issues relating to implementation of VAT was called for from 10 VAT divisions<sup>1</sup> covering 41 LVOs, 25 VSOs, 40 Debt Management offices and 115 Audit offices and six Recovery Divisions covering 96 Recovery offices. In addition, 12 LVOs and three Audit offices were selected on random basis for test check with special emphasis on registration of dealers, monitoring of returns, verification of threshold limit for dealers, compliance with the provisions of the Act and deterrent measures. Besides, Management Information System (MIS) as at the end of December 2008 and other records in the office of the CCT were analysed. Further, points noticed during the course of local audit during the year 2008-09 are also included in the review.

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<sup>1</sup> DVO I to VI, Bangalore, Davangere, Gulbarga, Mangalore and Mysore.

### 2.2.5 Acknowledgement

An Entry conference was held in April 2009 with the Principal Secretary to Government of Karnataka, Finance Department and the CCT wherein the scope of audit, methodology and audit objectives were explained to the Department. Indian Audit and Accounts Department acknowledges the co-operation of the CTD in providing MIS and information from four divisions<sup>2</sup>. Information from the other DVOs has not been received (November 2009). The draft review report was forwarded to the Government and the Department in September 2009 and was discussed in the exit conference held in November 2009 with the Principal Secretary to Government of Karnataka, Finance Department and the CCT. The replies of the Government received during the exit conference and at other points of time have been appropriately included in the respective paragraphs.

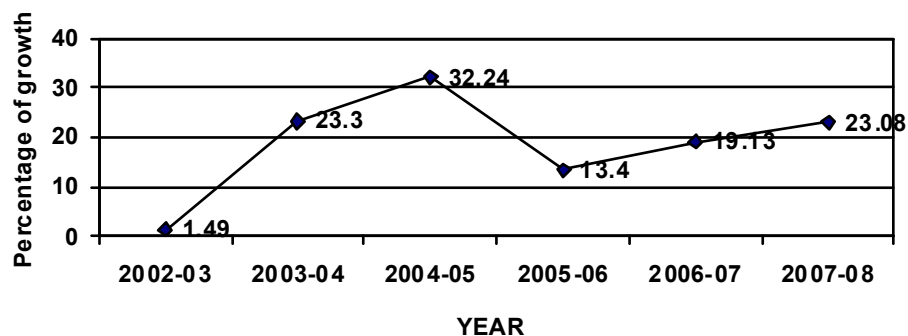
### Audit findings

#### 2.2.6 Pre-VAT and post-VAT tax collection

The comparative position of pre-VAT sales tax collection (2002-03 to 2004-05) and post-VAT (2005-06 to 2007-08) tax collection including VAT and the growth rate in each of the years compared to previous year is furnished below:

(Rupees in crore)

Pre VAT			Post VAT		
Year	Actual collection	Percentage of growth	Year	Actual collection	Percentage of growth
2002-03	4,658.74	1.49	2005-06	8,614.30	13.40
2003-04	5,744.15	23.30	2006-07	10,262.84	19.13
2004-05	7,595.99	32.24	2007-08	12,631.89	23.08



The average growth rate during 2002-03 to 2004-05 was 19.01 *per cent* while the average growth rate for 2005-06 to 2008-09 was 18.53 *per cent*. Thus, the average growth rate in the post VAT period registered a marginal decrease of 0.48 *per cent*.

Department stated that under the KST Act, for the purpose of additional resource mobilisation, rates of tax had been enhanced. Further, decrease in

<sup>2</sup> DVO V, Bangalore, Davangere, Mangalore and Mysore.

revenue collection after introduction of VAT was anticipated and hence the Government of India announced VAT loss compensation package for the years 2005-06 to 2007-08.

### **2.2.6.1 Arrears of Revenue under KVAT**

The Karnataka Commercial Taxes Manual (KCT Manual) prescribed maintenance of demand register to watch recovery of arrears of tax. However, no such registers are being maintained after implementation of VAT. Under the KVAT Act and Rules made thereunder, where a dealer or any other person is in default or is deemed to be in default in making a payment of tax or any other amount due under the Act, the authority concerned under the Act, may forward to the jurisdictional tax recovery officer, a certificate in the prescribed form. The tax recovery officer, on receipt of the certificate shall serve a notice in the prescribed form requiring defaulter to pay the amount. Further, interest on the defaulted amount and costs and charges incurred in respect of recovery proceedings are also recoverable.

As per the information furnished by the department, the position of arrears as at the end of March 2009 was as under:

(Rupees in crore)					
Year	Opening Balance	Accrued up to the year	Total	collection	Closing balance
2005-06	0	38.49	38.49	26.41	12.08
2006-07	12.08	43.41	55.49	18.56	36.93
2007-08	36.93	62.23	99.16	25.04	74.12
2008-09	74.12	75.70	149.82	22.49	127.33

### **2.2.7 Preparedness and transitional process**

#### **2.2.7.1 Planning for implementation of VAT in the State**

The Government of Karnataka, appointed in August 2001 M/s Crown Agents (technical consultants) to provide technical assistance to the CTD at a total cost of Rs. 20.33 crore. The technical consultants were to provide draft of VAT law including necessary regulations/rules, policy advice, reports on study of tax base and business practices, besides developing VAT Information Processing System (VIPS) and VAT Registration Number System (VRN) for computerisation of the department. A VAT Project Cell was also formed in CTD to work exclusively on VAT and interact with the technical consultants.

As per the agreement all the works were to be completed by the technical consultants by March 2002 to enable introduction of VAT in the State with effect from 1 April 2002 and only training programme to continue up to June 2002.

#### **2.2.7.2 Preparation of VAT Act/Rules, vetting of the Act and Rules by the Government**

The Draft VAT Law was approved by the Cabinet on 31 December 2002. The Draft VAT Law after receiving the assent of the President on 15 December 2004, was first published in the Karnataka Gazette, Extraordinary on the 23 December 2004.

### **2.2.7.3 Creation of awareness among the stake holders**

The Department organised a number of workshops/seminars for the departmental officers and stakeholders (Chambers of Commerce and Industries, Tax practitioners and Tax consultants) between November 2001 and March 2003. The Department also organised communication campaign through print and electronic media starting from March 2003.

### **2.2.7.4 Analysis of staff requirement and Re-organisation of the Taxation Department**

On introduction of VAT, 200 transition offices were formed with effect from 1 April 2005 for finalisation of assessments for the years up to 2004-05 under the KST Act which were continued till 2007-08.

For administration of VAT, the department was restructured on functional basis with effect from 1 April 2005 by creating 90 LVOs/VSOs, 101 Audit Offices, 75 Debt Management Offices besides continuing with the intelligence wing. The LVO offices in Bangalore were again reorganised according to PIN code during 2007-08 and 2008-09 and as at the end of 31 March 2009, 101 LVOs/VSOs were functioning in the State.

The details of assessment of staff requirement made by the department, if any, though called for (May 2009), have not been furnished (November 2009).

### **2.2.7.5 Computerisation of the Taxation Department and the check gates and their interlinking**

The VIPS and VRN systems were developed by the technical consultants at a cost of Rs. 7.09 crore. An attempt was made during July and August 2005 to operationalise VIPS and VRN systems. However, attributing inability to carry out the basic activities like returns processing, registration of dealers etc. and inadequate support in maintenance of the Software in fixing the bugs and improving the system, the CTD discontinued the usage of the VIPS and VRN. The work of Software Development and Support was entrusted to National Informatics Centre (NIC) during January 2006. The VAT Software (VATSOFT) developed by NIC was introduced from 2 August 2006.

In relation to computerisation of checkposts, the department stated (November 2009) that data entry is being successfully carried out in all the check posts. However, it was noticed that VIPS and VRN were not got tested before implementation. Also, the source code was not obtained from the technical consultants.

### **2.2.7.6 Creation of manuals and training of the staff**

The manual prepared by the technical consultants on registration and deregistration, returns and payment, repayment, cross reference, advisory visits, debt management, audit and anti-fraud strategy was not found suitable by the department. The department stated (November 2009) that the manuals prepared by the technical consultants were on the basis of proposed VAT law and due to changes in the working patterns, they are being re-written.

The department imparted training to its staff between November 2001 and July 2003 on VAT implementation and administration covering the modules relating to registration, returns and payment, refunds, input tax credits, debt management and audit.

### **2.2.7.7 Collection of arrears of taxes due under the KST Act and CST Act**

The position of arrears and collection under the KST Act and Central Sales Tax (CST) Act during the period 2005-06 to 2008-09 as furnished by the CTD was as under:

(Rupees in crore)

Year	Arrears	Additional demand raised	Total	Collection during the year	Write-off of revenue	Balance
2005-06	2,916.64	11,585.20	14,501.84	11,297.06	330.89	2,873.89
2006-07	2,873.90	16,242.69	19,116.58	14,255.06	564.34	4,297.19
2007-08	4,297.19	15,825.46	20,122.64	15,568.19	569.32	3,985.13
2008-09	3,985.13	16,459.96	20,445.09	16,646.67	793.62	3,004.80

Out of the balance of arrears, Rs. 366.67 crore was stayed by courts, Rs. 73.28 crore was covered by revenue recovery certificates, Rs. 43.13 crore was proposed to be written off and balance of Rs. 2,521.72 crore was under various stages of recovery.

### **2.2.8 Registration and database of dealers**

#### **2.2.8.1 Creation of database of dealers**

The CTD has been maintaining a database of registered dealers in VATSOFT which includes the name of the dealer, business and residential address and two major commodities as available in the application for registration. The database is being updated as and when new registrations are issued by the LVOs.

#### **2.2.8.2 Security deposit**

Under the KVAT Act and the Rules made thereunder, the prescribed authority may at any time demand from any dealer as security an amount equivalent to the tax anticipated to be payable by him in three months period. By a circular issued in August 2005, the CCT stipulated that the security deposits to be paid by the dealers are as below:

- a) For turnover not exceeding Rs. 10 lakh - Rs. 2,000/-.
- b) For turnover above Rs. 10 lakh - Rs. 3,000/-.
- c) For turnover above Rs. 25 lakh - Rs.10,000/-.

Details of the amount of security deposit collected from the dealers, if any, though called for (May 2009) were not furnished by the Department (November 2009).

#### **2.2.8.3 Excess allowance of transitional relief**

Under the KVAT Act and the Rules made thereunder, any registered dealer shall be entitled to transitional relief (TR) on tax paid under KST Act on



purchase of any goods and held in stock at the date of commencement of the KVAT Act for resale or use in manufacture as a component part or raw material, which are taxable under the KVAT Act. Further, every registered dealer claiming TR was required to make an application in Form 265 to the jurisdictional LVO and the LVO was required to issue a certificate in Form 270 indicating the amount to which the dealer is entitled as TR.

- As against 3,04,309 registered dealers as on 31 March 2005, no details were furnished by the department though requested for (April 2009) regarding the number of dealers who had filed application for claiming transitional relief, amount of transitional relief certified by the LVOs and actual transitional relief availed by the dealers.
- Test check of the records of a LVO in Bangalore (Urban) district in August 2008 revealed that as against TR of Rs. 19.78 lakh indicated in the Form 270 issued by the LVO in July 2005, a dealer in his return filed for five tax periods from August 2005 to December 2005 availed TR of Rs. 28.58 lakh. No action was taken by the LVO to demand and recover the excess TR availed by the dealer. This resulted in excess allowance of TR of Rs. 8.80 lakh.

After the case was brought to notice, the department stated (November 2009) that the case has been referred to audit<sup>3</sup>.

#### **2.2.8.4 Periodic analysis of dealers below threshold limit**

Under the KVAT Act, every dealer whose turnover does not exceed Rs. 15 lakh and who is not a works contractor, hotelier and a mechanised crushing unit has an option to pay tax at one *per cent* of his turnover by way of composition (COT) provided the dealer does not obtain goods from outside the State or from outside the country nor sells goods in the course of inter-state trade or in the course of export. Further every dealer whose total turnover within a period of four consecutive quarters exceeds the threshold limit shall cease to be eligible for COT and liable to pay VAT for the period starting from the first day of the month succeeding the month in which he exceeded the threshold. Separate quarterly returns have been prescribed for dealers who opted for COT.

Test check of 200 cases of dealers under COT in 10 LVOs in five districts<sup>4</sup> revealed that though five dealers exceeded the threshold limit, they continued to file returns and pay tax under COT. No action was taken by the LVOs to issue notices and get the returns filed under VAT. The tax liability at the minimum rate of four *per cent* in these cases on the turnover exceeding the threshold limit amounted to Rs. 85,746.

#### **Deficiencies in the Act and Rules**

The review revealed deficiencies in the provisions of the KVAT Act and Rules, which persisted during the period covered under the review. Some of the important deficiencies are discussed below:

<sup>3</sup> Audit Offices headed by DCCTs

<sup>4</sup> Bangalore (Urban), Davangere, Dakshina Kannada, Kolar and Mysore.

## 2.2.9 Returns

Under the KVAT Act, every dealer shall furnish a return in such form and shall pay tax due on such return within twenty days after the end of the preceding month. Any dealer who fails to furnish a return or fails to pay tax due on any return shall be liable to pay tax together with interest.

### 2.2.9.1 Mechanism to monitor filing of returns

Under the KVAT Act where a registered dealer fails to furnish his monthly/final return on or before due date the prescribed authority shall issue an assessment to the registered dealer to the best of his judgement and the tax assessed shall be paid within 10 days from the date of service of such assessment on the dealer.

As per the MIS, 18,91,905 returns were not filed during 2005-06 to December 2008. Details are as under:

Year	Number of returns not filed	No. of returns for which Notice issued	Balance
2005-06	1,01,594	6,074	95,520
2006-07	6,18,846	39,469	5,79,377
2007-08	7,93,535	47,258	7,46,277
2008-09 (Upto December 2008)	3,77,930	46,792	3,31,138
<b>Total</b>	<b>18,91,905</b>	<b>1,39,593</b>	<b>17,52,312</b>

Details of action taken by the department in respect of the remaining 17,52,312 cases was not ascertainable.

Test check of 200 cases of non-filing of returns in 10 LVOs of five districts<sup>5</sup> revealed that no action was taken by the concerned LVOs to issue best judgement assessment in these cases. Out of these, in 59 cases, it was observed that there was a tax liability based on the last return filed by the dealers which worked out to Rs. 58.45 lakh as computed by audit.

Department stated that steps have been taken to get compliance from the concerned DVOs to take required action against assesseees not filing returns.

### 2.2.9.2 Scrutiny and verification of returns

Under the KVAT Act, every dealer is deemed to have been assessed to tax based on the return filed by him. However, where any return submitted is apparently incomplete or incorrect, the LVO shall issue notice requiring the dealer to submit a revised or corrected return. Some of the cases of incorrect/incomplete return could be attributed to:

- (i) mathematical error in calculation of tax
- (ii) input tax credit is claimed without filling the details of purchases
- (iii) adjustment of brought forward refund though no amount/lesser amount was shown as carried forward refund in the previous return

<sup>5</sup> Bangalore (Urban), Davangere, Dakshina Kannada, Kolar and Mysore.

Details of incomplete/incorrect returns received by various LVOs during the period 2005-06 to 2008-09 and notices issued to dealers to rectify the mistake are detailed in the following table:

Year	Number of error returns	Number of corrected returns received	Number of cases taken up for scrutiny	Tax, penalty and interest levied and collected (Rs. in lakh)	Balance error returns	Percentage of corrected returns received
2005-06	2,06,994	9,519	762	60.56	1,97,475	4.60
2006-07	4,10,229	41,262	1,723	-	3,68,967	10.05
2007-08	5,53,630	38,954	2,522	23.31	5,14,676	7.04
2008-09 (up to December 2008)	2,88,423	45,040	9,941	37.10	2,43,383	15.61
<b>Total</b>	<b>14,59,276</b>	<b>1,34,775</b>	<b>14,948</b>	<b>120.97</b>	<b>13,24,501</b>	

Percentage of corrected returns received ranged from 4.60 to 15.61. No details were available regarding the action taken in the remaining 13,09,553 cases.

After the cases were brought to notice, department stated (November 2009) that scrutiny and verification of returns could not be handled in scientific and organised manner due to excess work load at LVOs, lack of awareness on the part of dealers in filing returns and absence of mechanism to identify probable error returns. In order to overcome this, a newly formatted report called "Returns Data Entry Statistics" has now been put in place and a "Tax Analysis" Report is introduced. These would enable the department to closely monitor the correctness of the returns.

Scrutiny of assessment records of VAT revealed several cases of non-observance of provisions of Act/Rules, non/short levy of tax, arithmetical inaccuracies, non-levy of penalty, etc. as mentioned in the succeeding paragraphs.

### **Non/short levy of penalty**

Under the KVAT Act, every registered dealer liable to pay tax shall furnish a return as prescribed and shall pay the tax due on such return within 20 days after the end of the preceding month or any other tax period. A dealer who for any prescribed tax period furnishes a return which understates his liability to tax (output tax) or overstates his entitlement to a tax credit (input tax) by more than five *per cent* of his actual liability to tax, shall after being given the opportunity of showing cause in writing against the imposition of a penalty, be liable to a penalty at the rate of 20 *per cent* of such tax under or overstated up to 31 March 2006 and at 10 *per cent* thereafter.

Test check of the records of 34 LVOs in eight districts between October 2007 and November 2008 revealed that 59 assesseees had either understated the output tax or overstated the input tax credit amounting to Rs. 8.76 crore in their 365 monthly returns for the tax periods during the years 2005-06 and 2006-07. Penalty of Rs. 1.33 crore was either not levied or short levied by the AAs as mentioned below:

(Rupees in lakh)				
Sl. No.	District (number of assesseees)	Period of assessment/ Number of returns	Amount of tax involved	Non/short levy of penalty
1.	Bangalore (Urban) (44)	April 2005 to March 2007 (289)	655.17	98.53
2.	Belgaum (2)	April 2005 to January 2006 (19)	71.22	14.24

(Rupees in lakh)				
Sl. No.	District (number of assessees)	Period of assessment/ Number of returns	Amount of tax involved	Non/short levy of penalty
3.	Bellary (4)	April 2005 and September 2006 (14)	59.88	9.75
4.	Dakshina Kannada (2)	December 2005 and December 2006 (6)	8.93	1.20
5.	Davanagere (1)	November 2006 (1)	11.91	1.19
6.	Dharwad (1)	April and June 2005 (2)	8.92	1.78
7.	Ramanagara (4)	April 2005 and January 2007 (22)	47.53	4.75
8.	Tumkur (1)	April 2006 to March 2007 (12)	12.93	1.29
<b>Total (59)</b>		<b>(365)</b>	<b>876.49</b>	<b>132.73</b>

After the cases were brought to notice, the Government/department reported (November 2009) recovery of Rs. 44.61 lakh in 19 cases, issue of notices in 13 cases involving Rs. 21.64 lakh and stated that recovery is being pursued in the remaining cases.

### **Excess credit carried forward**

Under the KVAT Act and the Rules made thereunder, any dealer in whose case, on the basis of return filed for any tax period, the input tax deductible exceeds the output tax payable by him, such dealer may adjust the excess amount towards the tax payable by him for any other tax period.

Test check of the records of eight LVOs in four districts<sup>6</sup> between January and October 2008 revealed that 14 dealers in their 16 returns filed for the tax periods between July 2005 and March 2007 brought forward credit of Rs. 40.79 lakh from earlier tax periods and adjusted it towards the tax payable by them. However, the actual credit available in the earlier tax periods in these cases was Rs. 11.85 lakh only. The excess carry forward and adjustment of credit resulted in loss of revenue of Rs. 28.94 lakh.

After the cases were brought to notice, the Government/department stated (November 2009) that Rs. 2.66 lakh has been recovered in one case and remaining cases are being pursued by issue of notice/reassessment orders.

### **Excess allowance of input tax**

Under the KVAT Act and the rules made thereunder, input tax shall be deducted from the output tax by any dealer, in calculating the net tax payable subject to conditions prescribed.

Test check of the records of 12 LVOs in four districts<sup>7</sup> between February and September 2008 revealed that 14 dealers had claimed input tax credit of Rs. 2.49 crore in their 37 returns for the tax periods between April 2005 and March 2007. The input tax admissible as per provisions of the Act in these cases was Rs. 1.71 crore which resulted in allowing excess/incorrect input tax

<sup>6</sup> Bangalore (Urban), Belgaum, Chamarajanagar, Dakshina Kannada.

<sup>7</sup> Bangalore (Urban), Bellary, Dharwad and Mysore.

of Rs. 78 lakh. A few illustrative cases are mentioned below:

(Rupees in lakh)				
Sl. No.	District/ Number of dealers	Nature of omission	Input tax claimed/ Input tax allowable	Amount of excess/ incorrect input tax
1.	Bangalore (Urban) 1	The input tax on the purchase turnover of Rs. 2.80 crore during March 2006 works out to Rs. 34.94 lakh. However, the dealer had claimed input tax of Rs. 70.84 lakh due to arithmetical error.	70.84/ 34.94	35.90
2.	Bangalore (Urban) 1	The dealer in his return for the month of August 2005 claimed tax paid under CST Act on interstate purchases as input tax credit which was not admissible under KVAT Act.	2.06/ Nil	2.06

After the cases were brought to notice, the LVOs concerned accepted audit observations in three cases involving Rs. 1.35 lakh. Of these Rs. 95,466 was recovered in two cases and notice for reassessment was issued in the other case. Final reply in respect of the remaining cases has not been received (November 2009).

### **Underassessment of output tax**

Under the KVAT Act, every registered dealer shall be liable to pay tax on his taxable turnover at the rates specified in the relevant schedules to the Act. In respect of goods not specified in any of the schedules, tax is payable at the rate of 12.5 per cent.

Test check of the records of 12 LVOs in five districts<sup>8</sup> between February and November 2008 revealed that the taxable turnover of 22 dealers during the tax periods between April 2005 and March 2007 amounted to Rs. 40.98 crore. The output tax liability worked out to Rs. 4.07 crore. However, the dealers declared output tax liability of Rs. 3.22 crore only in their 56 returns filed between May 2005 and April 2007 which was accepted by the concerned LVOs. This was due to arithmetical mistakes, short declaration of taxable turnover, claiming of incorrect exemption on taxable turnover, etc. The underassessment of output tax amounted to Rs. 85.16 lakh.

After the cases were brought to notice, the Government/department reported (November 2009) that Rs. 19.09 lakh has been recovered in four cases and the remaining cases are being pursued by issue of notice/reassessment orders.

### **Non-forfeiture of VAT collected in excess**

Under the KVAT Act, when any amount is wrongly collected by way of tax or purporting to be by way of tax from any person by any dealer, whether knowingly or not, such dealer shall pay the entire amount so collected, to the prescribed authority within 20 days after the close of the month in which such amount was collected, notwithstanding that the dealer is not liable to pay such amount as tax or that only a part of it is due from him as tax under the Act. Such amount paid by the dealer to the extent it is not due as tax shall be forfeited to the Government and recovered from him.

<sup>8</sup> Bangalore (Urban), Bellary, Chitradurga, Dharwad, Ramanagara.

Test check of the records of five LVOs in Bangalore (Urban) and Mysore districts between February and July 2008 revealed that seven dealers had collected tax of Rs. 2.63 crore during the months from April 2006 to March 2007. It was noticed in their returns filed for these months, that the output tax payable as declared by them amounted to Rs. 2.28 crore. No action was initiated by the concerned LVOs to forfeit the excess tax of Rs. 34.67 lakh collected by the dealers.

After the cases were brought to notice, the Government/department reported (November 2009) that Rs. 8.95 lakh has been recovered in two cases and the remaining cases are being pursued by issue of notice/reassessment orders.

### **Short computation of net tax payable**

Under the KVAT Act and Rules made thereunder, every dealer shall be deemed to have been assessed to tax based on the return filed by him. Where any return submitted is apparently incomplete or incorrect, the jurisdictional LVO shall issue a notice in Form VAT 150 requiring the dealer to submit a complete or correct return within ten days of issue of the notice. The net tax payable by a registered dealer in respect of each tax period shall be amount of tax payable by him in respect of any taxable sale of goods (output tax) less the tax collected or payable under this Act on the sale of any goods to him for use in the course of his business (input tax).

Test check of the records of two LVOs in Bangalore (Urban) and Bellary districts between May and August 2008 revealed that two dealers in their returns filed for August 2005 and November 2005 declared output tax and input tax credit amounting to Rs. 44.89 lakh and Rs. 25.96 lakh respectively. However, as against the net tax payable by both amounting to Rs. 18.93 lakh, the dealers concerned declared and paid net tax of Rs. 12.13 lakh due to error in computation. No action was taken by the LVOs concerned to demand and recover the tax liability declared and paid short. The short computation of net tax amounted to Rs. 6.80 lakh.

### **2.2.9.3 Annual statement**

Under the KVAT Rules every dealer was required to file an annual statement in prescribed form commencing from the end of the year on 31 March 2007 within sixty days after the end of the relevant year. Any dealer who fails to furnish the annual statement was liable to pay a penalty at Rs. 50 for each day of default. Filing of annual statement was dispensed with effect from 1 August 2008, as a result of which there is no mechanism for cross verification of the returns submitted by the assesseees.

As per the information furnished by Mysore Division and Bangalore Division-V, as against 35,824 dealers, 3,145 dealers did not file the statements during 2006-07. Similarly out of 47,139 dealers, 3,304 dealers did not file the statements during 2007-08. In respect of the defaulters penalty of Rs. 15.57 crore leviable upto 31 March 2009 was not levied. Information in respect of other divisions though called for (April 2009) has not been received (November 2009).

### 2.2.10 Tax audit

The KVAT Act provides for cases to be taken up for reassessment where the prescribed authority has grounds to believe that any return furnished which is deemed as assessed or assessment issued understates the correct tax liability of the dealer. The CCT vide circular issued during July 2005 specified the types of audit that can be chosen viz., Credit Returns, Big dealer audits, Deterrence audits and High Risk audits, Compliance Audit and Others. The circular also laid down broad guidelines on the selection of cases for audit.

#### 2.2.10.1 Time frame for completion of tax audit

The White paper envisaged that the audit work would be completed within 6 months. However, neither the Rules nor the administrative instructions issued by the Department prescribed any time frame for completion of the audit of selected cases.

#### 2.2.10.2 Percentage of dealers to be taken up for tax audit

The Empowered Committee envisaged that not more than 20 *per cent* of the total dealer population should be audited every year. However, minimum percentage of dealers to be taken up for audit has not been prescribed.

The total number of registered dealers, number of cases selected for audit, actual number of cases audited and additional demand raised after audit during the years 2005-06 to 2008-09 were as under:

Year	Number of dealers	Number of dealers selected for audit	Percentage to number of dealers	Number of dealers audited	Percentage to number of dealers	Additional demand raised in audit	
						Number of dealers	Amount (Rs. in lakh)
2005-06	3,54,721	9,646	2.72	5,882	1.66	2,783	3,121
2006-07	3,89,393	17,625	4.53	12,614	3.24	6,783	8,979
2007-08	4,31,029	16,029	3.72	11,029	2.56	7,065	13,328
2008-09	4,34,746	5,343	1.23	6,910	1.59	4,490	18,778
<b>Total</b>		<b>48,643</b>		<b>36,435</b>		<b>21,121</b>	<b>44,206</b>

It may be seen from the above table that in respect of 58 *per cent* of the audited cases, the department noticed underassessment of tax by the dealers. This also indicated that there was a need to increase the percentage of audit coverage which was mere 1.59 *per cent* to 3.24 *per cent*. Reasons for not auditing all the cases selected for audit was not forthcoming.

#### 2.2.10.3 Non/short levy of interest

Under the KVAT Act, every dealer shall be liable to pay simple interest at the rate of 1.25 *per cent* per month on any amount of tax which should have been declared on a return, but which has been omitted from it, and such interest is payable from the date the tax should have been declared. Further, under the Act, when any prescribed authority has grounds to believe that any return furnished understates the correct tax liability, it may re-assess to the best of its judgment the additional tax payable and raise demand of interest thereon.

Test check of the records of 11 LVOs in Bangalore (Urban) and Belgaum districts between November 2007 and November 2008 revealed that the AAs created additional demand of Rs. 3.40 crore on reassessments for 202 tax periods in respect of 24 dealers between January 2006 and February 2008. However, interest of Rs. 41.03 lakh though leviable was not levied.

After the cases were brought to notice, the Government/department reported (November 2009) that Rs. 13.24 lakh has been recovered in six cases and the remaining cases are being pursued by issue of notice/reassessment orders.

### **2.2.11 Input tax credit**

Under the KVAT Act, input tax in relation to a registered dealer means the tax paid or payable on the purchase of any goods for use in his business and includes the tax on purchase of goods by his agent on his behalf. Subject to restrictions as specified under the Act, a registered dealer can claim/adjust input tax paid on raw materials, intermediaries, inputs and capital goods for resale or for manufacture or any other process of other goods for sale.

#### **2.2.11.1 Deficiencies in the provisions for input tax credit**

Under the CENVAT Credit Rules, credit of duty paid on purchase of capital goods is allowed subject to the condition that the manufacturer shall not claim depreciation on the part of the value of capital goods which represents the amount of specified duty paid on such capital goods.

However, there is no such provision under the KVAT Act for disallowing the input tax credit on capital goods where the KVAT paid on capital goods is also capitalised and depreciation is claimed. Absence of such provision may lead to claiming of both input tax credit by the dealers under the KVAT Act as well as claiming of depreciation on the amount of KVAT paid.

### **2.2.12 Non-filing of copies of works contract agreements**

Under the KVAT Act with effect from 1 April 2007 every registered dealer and every dealer including owner of a land, liable to get registered under the Act, entering into a written agreement during any tax period for executing a civil works contract shall submit a copy of the agreement within the end of the subsequent tax period. In view of this provision all works contractors, co-developers of land, sub contractors are liable to file copies of agreement along with the monthly returns to the department. Failure to file such agreements attracts penalty of Rs. 2,000/- if such failure was the first during any year or Rs. 5,000/ if such failure was the second or subsequent during that year and in addition a further penalty not exceeding Rs. 200 per day of delay.

Test check of records in seven LVOs in five Districts<sup>9</sup> revealed that 1,919 registered works contractors had not filed copies of the agreement along with the monthly returns. The minimum penalty leviable in these cases worked out to Rs. 38.38 lakh.

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<sup>9</sup> Bangalore (Urban), Davangere, Dakshina Kannada, Kolar and Mysore.



### 2.2.13 Acceptance and disposal of appeal cases

Under the KVAT Act, any persons objecting to any order or proceedings affecting him passed under the provisions of the Act by the prescribed authority may appeal to the prescribed appellate authority after paying the tax or other amount in accordance with the order or proceedings against which an appeal has been preferred. Further, no appeal against an order of assessment shall be entertained by the appellate authority unless it is accompanied by satisfactory proof of the payment of tax and penalty not disputed in the appeal. The following table shows the number of appeal cases disposed during the period 2005-06 to 2008-09 in respect of 7<sup>10</sup> Divisions under KST and KVAT Acts.

Year	OB	Additions	Total	Disposal	CB
2005-06	1,322	3,735	5,057	3,233	1,824
2006-07	1,824	3,019	4,843	3,050	1,793
2007-08	1,793	4,971	6,764	3,265	3,499
2008-09	3,499	7,038	10,537	5,846	4,691

### 2.2.14 Deterrent measures

Provision has been made in the Act in Section 71 to 77 for levy of penalty in respect of defaults relating to registration, returns and assessments, unauthorised collection of tax, keeping of records, production of records and furnishing of information, issue of tax invoices, bills of sale, credit notes and debit notes, seals and unaccounted stocks.

The KVAT Act provides for levy of penalty up to Rs. 2,000/- for failure to maintain proper records and up to Rs. 5,000/- for non-production of records and non-furnishing of information in accordance with the requirement of the Act. However, in these cases minimum penalty has not been prescribed.

### 2.2.15 Internal audit

The internal audit wing (IAW) was functioning in the department up to 2004-05. On introduction of VAT the IAW was abolished leaving it vulnerable to the risk of control failure.

After this was brought to notice, the department stated that action is being initiated to constitute IAW at all the divisional VAT offices.

### 2.2.16 Conclusion

The above points reveal that the prevailing mechanism to conduct and monitor the main areas of levy and collection of tax viz., scrutiny and verification of returns, non-filing of returns, collection of tax, audit of dealers accounts is not adequate to ensure proper collection of taxes.

<sup>10</sup> JCCT (Appeals)-1, Bangalore, JCCT(Appeals)-2, Bangalore, JCCT(Appeals)-3, Bangalore, Malnad Division, Shimoga, JCCT(Appeals), Mysore, JCCT(Appeals), Gulbarga and JCCT(Appeals), Davangere.

### **2.2.17 Recommendations**

In view of the observations made in the review, Government may consider implementation of following recommendations:

- prescribing a minimum percentage of dealers for reassessment and time frame for completion of re-assessment.
- amending KVAT Act to allow input tax credit on capital goods subject to the condition that the dealer shall not claim depreciation on the part of the value of capital goods which represents the amount of KVAT paid on such capital goods.
- reviving the internal audit wing.

### 2.3 Other audit observations

*Scrutiny of assessment records of sales tax revealed several cases of non-observance of provisions of Acts/Rules, non/short levy of tax, interest and penalty as mentioned in the succeeding paragraphs in this chapter. These cases are illustrative and are based on a test check carried out in audit. Such omissions on the part of the Assessing Authorities (AAs) are pointed out in audit each year, but not only do the irregularities persist; these remain undetected till an audit is conducted. There is need for the Government to improve the internal control system including reviving and strengthening of internal audit.*

### 2.4 Non-observance of provisions of the Acts/Rules

*The Central Sales Tax Act (CST Act) 1956, the Karnataka Sales Tax Act (KST Act) 1957 and the rules made thereunder provide for:*

- (i) determination of total and taxable turnover;*
- (ii) levy of tax on sales/purchases of goods at prescribed rate;*
- (iii) levy of interest/penalty on belated payment of tax;*
- (iv) exemption/concessional rate of tax on notified goods/transactions subject to prescribed conditions;and*
- (v) reduction of tax paid on purchases from tax payable on sales.*

*The AAs while finalising the assessment did not observe some of the above provisions in cases as mentioned in paragraphs 2.4.1 to 2.4.8. This resulted in non/short levy/non-realisation of tax/interest/penalty of Rs. 3.34 crore.*

#### 2.4.1 Short levy of tax

Under the KST Act, tax is leviable on the purchases/sales at the rates mentioned in the relevant schedules to the Act. In the case of goods not specified in any of the schedules, tax is leviable as on unspecified goods. Under the CST Act 1956, tax at specified rates is levied on interstate sale of goods.

Test check of the records of 10 sales tax offices (STO) in three districts<sup>11</sup> between April 2007 and November 2008 revealed that while finalising 19 assessments of 19 dealers for the years 1998-99, 2000-01, 2001-02 and 2003-04 to 2005-06, the AAs either applied incorrect rates of tax on taxable turnover or assessed taxable turnover to a lesser extent. These were due to misclassification of goods and transactions, extending the benefit of concessional rate given under certain notifications to ineligible cases, etc. This resulted in short levy of tax of Rs. 1.20 crore

<sup>11</sup> Bangalore (Rural), Bangalore(Urban), Dakshina Kannada.

on taxable turnover of Rs. 9.35 crore. A few illustrative cases are mentioned below:

(Rupees in lakh)					
Sl. No.	District (number of cases)	Assessment year (month of assessment)	Audit of observation	Turnover involved	Tax levied short
1.	Bangalore (Urban) (1)	2004-05 (January 2008)	Against taxable turnover of Rs. 246.61 lakh reported by the dealer in his annual return, the AA levied tax on a turnover of Rs. 100.33 lakh. This resulted in escapement of turnover of Rs. 146.28 lakh from levy of tax.	146.28	15.26
2.	Dakshina Kannada (1)	2004-05 (March 2008)	Concessional rate of four <i>per cent</i> tax on sale of HSD <sup>12</sup> , prescribed under the notification dated 30 March 2002 was cancelled with effect from 1 August 2004. However, tax was levied between August 2004 and March 2005 at four <i>per cent</i> instead of 20 <i>per cent</i> .	81.21	12.99

After the cases were brought to notice, the Government/department reported revision of assessments and recovery of Rs. 19.44 lakh in five cases. Action taken in the remaining cases has not been received (November 2009).

#### 2.4.2 Incorrect levy of concessional rate of tax

Under the CST Act, in the case of sales made to a registered dealer, subject to furnishing of a declaration in form C, tax leviable shall be at the concessional rate of four *per cent* or the rate applicable to the sale or purchase of such goods inside the State whichever is lower. However, tax leviable on interstate sale of goods not supported by C forms shall be at the rate of 10 *per cent* or at the rate applicable for sale or purchase of such goods inside the State whichever is higher.

Test check of the records of a STO in Bangalore (Rural) district in April 2008 revealed that while finalising an assessment of a dealer for the year 2000-01, tax at the rate of four *per cent* was levied on a turnover of Rs. 1.71 crore as interstate sales to registered dealers. However, it was noticed that sales were made by the assessee to a dealer whose registration had already been cancelled and hence the levy of tax at the concessional rate was incorrect. This resulted in short levy of tax of Rs. 20.13 lakh.

The case was reported to the CCT in May 2008 and the Government in April 2009; their reply has not been received (November 2009).

<sup>12</sup> High speed diesel.

### 2.4.3 Excess/incorrect reduction of tax

Under the KST Act, where goods are sold under a brand name by a trade mark holder or brand name holder or any other dealer having the right as proprietor or otherwise to use the said name or trade mark either directly or through another on his own account or through others, exclusively to a marketing agent or distributor or wholesaler or any other dealer, subsequent sale of such goods by the latter shall also be liable to tax under the Act and the tax so payable shall be reduced by the amount of tax already paid on the sale of such goods by the former. However, the amount of additional tax and cess paid by the former were not eligible for reduction. Further, no reduction of tax was admissible in respect of goods which are sold or transferred to outside the State.

Test check of the records of STO in Bangalore (Urban) district in June 2008 revealed that while finalising the assessment of a dealer<sup>13</sup> for the years 2003-04 and 2004-05 in March 2007 reduction of tax of Rs. 2.25 crore and Rs. 2.41 crore respectively was allowed by the AA. Of these, reduction of tax of Rs. 33.48 lakh was allowed twice, once as tax paid on closing stock of the year 2003-04 and again on the opening stock of the year 2004-05. In addition reduction of Rs. 6.45 lakh on the goods transferred to outside the State during 2003-04, additional tax of Rs. 23.37 lakh and cess of Rs. 36.95 lakh paid by the first dealer for both the years were allowed. This resulted in excess/incorrect tax reduction of Rs. 1 crore.

The case was reported to the CCT in July 2008 and the Government in May 2009; their reply has not been received (November 2009).

### 2.4.4 Non/short levy of resale tax

Under the KST Act, from 1 April 2002, every registered dealer was liable to pay resale tax at the rate of 1.5 *per cent* on such portion of the total turnover which is not liable to tax under other provisions of the Act, after allowing such deductions as are admissible under the Act.

Test check of the records of five STOs in two districts<sup>14</sup> between April and December 2008 revealed that while finalising eight assessments of seven dealers for the years 2003-2004 and 2004-05, resale tax was either not levied or levied short on the turnover of Rs. 19.07 crore. This was due to incorrect grant of exemption, incorrect determination of turnover, etc. This resulted in non-levy of resale tax of Rs. 19.96 lakh.

After the cases were brought to notice, the Government/department reported revision of assessments and recovery of Rs. 14.37 lakh in three cases. In respect of the remaining cases, reply has not been received (November 2009).

### 2.4.5 Excess collection of tax

Under the KST Act, a registered dealer is prohibited from collecting any amount by way of tax in excess of that specified in the Act. Where any

<sup>13</sup> exclusive wholesaler for 'Akai' brand electronic goods.

<sup>14</sup> Bangalore (Urban) and Hassan.

collection is made in excess of the tax due to the Government the same is required to be remitted to the Government account. Also, the AA shall forfeit such amount to the Government. The excess tax collected and remitted by the dealer, but not forfeited by the AA will stand at the credit of the dealer in the books of the department.

Test check of the records of six STOs in Bangalore (Rural) and Bangalore (Urban) districts between April and July 2008 revealed that while finalising seven assessments of seven dealers for the years 2003-04 and 2004-05, tax of Rs. 10.80 crore was levied. Against this, the dealers had collected tax of Rs. 11.09 crore. The excess tax collected by the dealers amounted to Rs. 29.10 lakh. Of this only Rs. 7.70 lakh was forfeited by the AAs concerned. Non/short forfeiture of tax collected in excess amounted to Rs. 21.40 lakh.

After the cases were brought to notice, the AAs concerned accepted audit observations in three cases involving Rs. 14.89 lakh and issued notices for forfeiture of excess tax collected. In respect of remaining cases, reply has not been received (November 2009).

The cases were reported to the CCT between May and September 2008 and the Government in April 2009; their reply has not been received (November 2009).

#### **2.4.6 Non-levy of additional tax**

Under the KST Act, every registered dealer was liable to pay additional tax at the rate of one *per cent* of taxable turnover except where such turnover relates to sale of industrial inputs. Further, in accordance with the clarification issued by the State level 'Authority for Clarification and Advance Rulings' constituted by the CCT under the KST Act, the additional tax is leviable on any sales turnover even though tax is exempted by way of any notification.

Test check of records of three STOs in Bangalore (Rural) and Bangalore (Urban) districts between April and June 2008 revealed that while finalising six assessments of five dealers for the years 2003-04 and 2004-05, additional tax was not levied on a turnover of Rs. 20.81 crore. Of these, in two cases benefit of notification granting exemption of tax was incorrectly extended to additional tax while in other four cases additional tax was omitted to be levied. The non-levy of additional tax amounted to Rs. 20.81 lakh.

After the cases were brought to notice, the Government/department reported revision of assessments and recovery of Rs. 1.06 lakh in two cases. In respect of the remaining cases reply has not been received (November 2009).

#### **2.4.7 Non-levy of cess**

Under the KST Act, with effect from 1 February 2004, in addition to the tax payable on sale or purchase effected by any dealer, there shall be levied and collected, Road Cess at the rate of 10 *per cent* of tax for the purpose of establishing a Road Maintenance Fund. Similarly, with effect from 1 February 2004, in addition to the tax payable on sale or purchase effected by any dealer, there shall be levied and collected, Infrastructure cess at the rate of 5 *per cent* of tax for the purpose of various infrastructure projects across the

State, equity investment in Bangalore Mass Rapid Transit Limited and establishing a Mukhya Manthri Grameena Rasthe Abhivruddhi Nidhi.

Test check of the records of three STOs in three districts<sup>15</sup> between April and August 2008 revealed that while finalising five assessments of five assessees for the year 2004-05 between April and December 2007, cess of Rs. 20.39 lakh was omitted to be levied on tax of Rs. 1.36 crore levied.

After the cases were brought to notice, the Government/department reported revision of assessments and recovery of Rs. 7.63 lakh in three cases. In respect of the remaining cases reply has not been received (November 2009).

#### **2.4.8 Non-levy of interest**

Under the KST Act, tax or any other amount due is required to be paid within the prescribed time and, in the case of final assessments, this is to be paid within 21 days from the date of serving of demand notice. In case of default in making payments, the assessee is liable to pay interest at the rate of two *per cent* per month up to 31 March 2005 and at the rate of 1.25 *per cent* thereafter.

Test check of the records of five STOs in three districts<sup>16</sup> between October 2007 and December 2008 revealed that 14 dealers, against whom demand notices were served between December 2000 and October 2007, paid tax of Rs. 62.09 lakh between October 2006 and March 2008 after delay ranging from 3 to 77 months. However, interest of Rs. 11 lakh was not levied by the AAs concerned.

After the cases were brought to notice, the Government/department accepted audit observation in respect of five cases involving Rs. 2.88 lakh and recovered Rs. 1.18 lakh in two of them. In the remaining cases reply has not been received (November 2009).

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<sup>15</sup> Bangalore (Rural), Bangalore (Urban), Bellary.

<sup>16</sup> Bangalore (Urban), Davangere, Hassan.