# CHAPTER II: SALES TAX/VAT

## 2.1 Results of audit

Test check of the assessment cases and other records relating to the Taxation Department during the year 2008-09 revealed evasion, underassessment, non/short levy of tax and concealment of turnover, irregular grant of exemption etc., amounting to Rs. 809.92 crore in 102 cases which can be categorised as under.

**(Rupees in crore)**

| Sl. no. | Category | Number of cases | Amount |
|---|---|---|---|
| 1. | **Transition from Meghalaya Sales Tax to VAT (A review)** | 01 | 754.28 |
| 2. | Irregular grant of exemption | 13 | 16.37 |
| 3. | Non/short levy of penalty | 12 | 12.13 |
| 4. | Evasion of tax | 13 | 9.05 |
| 5. | Turnover escaped assessment | 09 | 5.18 |
| 6. | Loss of revenue | 08 | 1.35 |
| 7. | Underassessment of tax | 09 | 1.34 |
| 8. | Non/short levy of interest | 06 | 0.70 |
| 9. | Other irregularities | 31 | 9.52 |
| **Total** | | **102** | **809.92** |

During the year 2008-09, the department accepted irregularities in 15 cases and one review amounting to Rs. 765.02 crore pertaining to 2008-09. The department recovered Rs. 12.94 lakh in four cases during the year.

A review on '**Transition from Meghalaya Sales Tax to VAT'** involving Rs. 754.28 crore and a few illustrative audit observations involving Rs. 30.71 crore are mentioned in the succeeding paragraphs.

## 2.2 Transition from Sales Tax to VAT in Meghalaya

***Highlights***

- The growth rate of revenue over the previous year after implementation of VAT touched a high of 50.12 *per cent* in 2005-06. Although the rate had fallen in the subsequent years, it still recorded a healthy 24.98 *per cent* growth in 2008-09.

***(Paragraph 2.2.6.1)***

- The department failed to detect and register 606 dealers who sold taxable goods of Rs. 27.44 crore. This resulted in evasion of tax of Rs. 2.08 crore. Besides, penalty of Rs. 3.91 crore was also leviable.

***(Paragraph 2.2.8.2)***

- In the absence of a mechanism for monitoring the receipt of the returns, the assessing officers could not detect non-submission of returns by 11,816 dealers between May 2005 and March 2009 and consequently penalty of Rs. 372.21 crore could not be levied.

***(Paragraph 2.2.9.4)***

- In the absence of a mechanism to check input tax credit claimed by the dealers coupled with the failure to scrutinise returns effectively, the department failed to detect excess claim of input tax credit of Rs. 30.40 crore by 69 dealers.

***(Paragraph 2.2.11)***

- Three bottling plants sold 26,84,292 cases of liquor, but tax of Rs. 34.20 crore was not levied. Further, the State Government had to suffer loss of revenue of Rs. 4.15 crore due to the delay in implementation of VAT on liquor.

***(Paragraph 2.2.12.1 & 2.2.12.2)***

- Due to the implementation of defective tax remission scheme for new industries, State Government had to pay Rs. 7.98 crore from its exchequer.

***(Paragraph 2.2.14)***

- There was loss of revenue of Rs. 73.56 lakh due to non-deduction of tax at source. Further, Rs. 62.09 lakh though deducted at source; was not deposited into the Government account.

***(Paragraph 2.2.16.1)***

- The department failed to prefer claim of compensation due to the implementation of VAT which led to loss of revenue of Rs. 247.49 crore.

***(Paragraph 2.2.20)***

### 2.2.1 Introduction

The empowered committee of State Finance Ministers constituted by the Government of India in its meeting held on 23 January 2002 unanimously decided to introduce VAT in all the States and Union Territories with effect from 1 April 2003. The empowered committee issued a white paper (January 2005) defining the basic designs of the state level VAT. The white paper, however, allowed the states to adopt appropriate variations in their VAT Acts, consistent with the basic design. The VAT system which is a destination/consumption based tax system and has provisions for set-off of the tax paid on the previous purchases seeks to address problems of double taxation of commodities, multiplicity of taxes, surcharge and additional surcharge on sales tax etc., in the sales tax structure that resulted in a cascading tax burden.

The MVAT Bill was passed by the State Assembly in March 2003 and got the Presidential assent in February 2005. The Government of Meghalaya repealed the Meghalaya Sales Tax (MST) Act, Meghalaya Finance (Sales Tax) (MFST) Act, Meghalaya Purchase Tax (MPT) Act and enacted the Meghalaya Value Added Tax (MVAT) Act 2003 from 1 May 2005.

Under MVAT Act, goods are classified into five schedules based on their social and economic importance and are taxable at the rates of 'nil', one, four, 12.5 *per cent* and non-VATable goods at the rates as prescribed in the schedule (at first point).

**The transitional process from Meghalaya Sales Tax to VAT was reviewed by audit which revealed a number of deficiencies as discussed in the succeeding paragraphs.**

### 2.2.2 Organisational set up

The Principal Secretary, Excise, Registration, Taxation and Stamps Department is the overall incharge of the Taxation Department at the Government level. The Commissioner of Taxes (COT) is the administrative head of the Taxation Department. He is assisted by a Deputy Commissioner of Taxes (DCT) and two Assistant Commissioners of Taxes (ACT). The ACT also functions as the Appellate Authority. At the district level, the Superintendents of Taxes (ST) are entrusted with the work of registration, scrutiny of the returns, collection of tax, levy of interest/penalty, issue of road permits/declaration forms etc. The STs are assisted by the Inspectors of Taxes (IT) for surveys, inspections and other ancillary works in relation to registration, assessments and collection of the taxes. With a view to checking evasion of taxes, the Government has constituted an enforcement branch comprising of one ST and some ITs with jurisdiction over the entire State.

### 2.2.3 Audit objectives

The review was conducted to ascertain whether

- there was proper planning for implementation of the MVAT Act and the transition from sales tax to VAT was effected timely and efficiently.

- organisational structure was adequate and effective.
- the provision of the MVAT Act and the Rules made thereunder were adequate and enforced properly to safeguard the revenue of the state.
- internal control mechanism existed in the department and was adequate and effective to prevent leakage of revenue, and
- the system which has been in place for four years was working efficiently.

### 2.2.4 Scope of audit

The review was conducted through test check of the records for the years 2005-06 to 2008-09 of the COT and seven out of 10 district STs[4] and two checkposts[5] between May and July 2009. Selection of the assessment records was made after dividing the records in four strata on the basis of the gross turnover[6] of the dealers and 50, 30, 20 and 10 *per cent* of the assessment records were selected from the four strata respectively. Besides, records of the Forest Department, State Legislative Assembly and North Eastern Indira Gandhi Regional Institute of Health and Medical Science were cross checked with the assessment records of the concerned dealers.

### 2.2.5 Acknowledgement

Indian Audit and Accounts Department acknowledges the cooperation of the Taxation Department in providing the necessary information and records for audit. An entry conference was held on the 11 August 2009 which was attended by the Commissioner and Secretary, Government of Meghalaya, Excise, Registration, Taxation and Stamps (ERTS), the COT and the DCT in which the objectives, scope and methodology of audit were explained. The draft review report was sent to the Government/department on the 16 October 2009 for their response. An exit conference was held on the 14 December 2009 with the Commissioner and Secretary, ERTS, the COT and the ACT in which the results of audit and the recommendations were discussed. The Government/department has accepted most of the audit findings/recommendations and assured to take action. The cases in which they have furnished specific replies or have countered the contention of audit, have been appropriately included in this report under the respective paragraphs.

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4 ST Shillong Circles I, II, III, IV, VI, Purchase Tax, Nongpoh, Nongstoin and Jowai.

5 Byrnihat and Umkiang.

6 1st stratum-Rs. 10 crore and above.
2nd stratum-Rs. 1 crore and above but below Rs. 10 crore.
3rd stratum-Rs. 50 lakh and above but below Rs. 1 crore.
4th stratum-below Rs. 50 lakh.

## Audit findings

### 2.2.6 Financial analysis

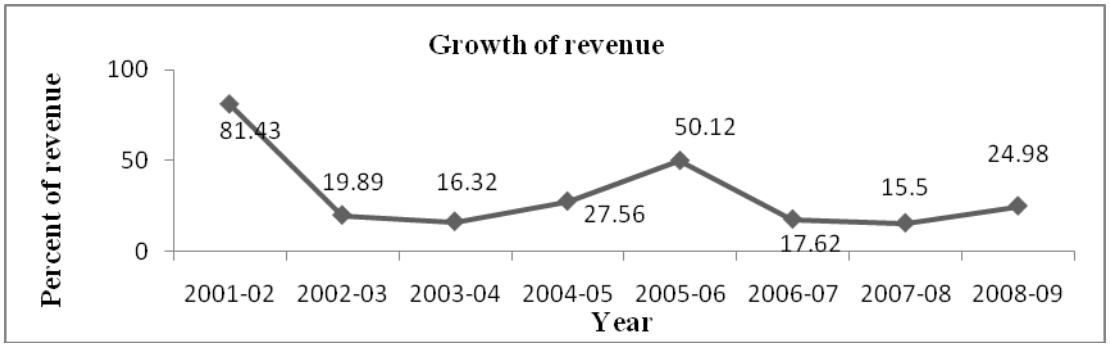
#### 2.2.6.1 Pre-VAT and post-VAT tax collection

The comparative position of pre-VAT (2001-02 to 2004-05) and post-VAT (2005-06 to 2008-09) tax collection and the growth rate in each year is furnished below.

**Table No. 1**

| Sl. no. | Pre-VAT | | | Post-VAT | | |
|---|---|---|---|---|---|---|
| | Year | Actual collection[7] (Rs. in crore) | Percentage of growth | Year | Actual collection[8] (Rs. in crore) | Percentage of growth |
| 1. | 2001-02 | 59.78 | 81.43 | 2005-06 | 159.65 | 50.12 |
| 2. | 2002-03 | 71.67 | 19.89 | 2006-07 | 187.78 | 17.62 |
| 3. | 2003-04 | 83.37 | 16.32 | 2007-08 | 216.89 | 15.50 |
| 4. | 2004-05 | 106.35 | 27.56 | 2008-09 | 271.07 | 24.98 |
| **Average growth** | | | **36.30** | | | **27.06** |

**Chart No. 1**




Thus, the average growth rate during 2001-02 to 2004-05 was 36.30 *per cent* while the average growth rate for 2005-06 to 2008-09 was 27.06 *per cent*. The growth rate of revenue over the previous year after implementation of VAT touched a high of 50.12 *per cent* in 2005-06. Although the rate had fallen in the subsequent years, it still recorded a healthy 24.98 *per cent* growth in 2008-09.

#### 2.2.6.2 Reconciliation of revenue collected

The Budget manual stipulates periodical reconciliation of the receipts as per the books of the department with those booked by the Accountant General (Accounts and Entitlements) by the controlling office.

It was, however, noticed that no reconciliation was carried out during the last 10 years and as such, there was wide variation between the departmental figures and figures booked by the AG (A&E). As an instance, the variations between the

7 Collection under Sales Tax (MST+MFST+PT), and Motor Spirits and Lubricants Acts.

8 Collection under Sales Tax (MST+MFST+PT) upto 30.4.2009 and collection of arrears thereafter, VAT and Motor Spirits and Lubricants Acts.

figures relating to collection under the minor head 'sales of motor spirits and lubricants' as reflected in the Departmental records and Finance Accounts are shown below.

**Table 2**

**(Rs. in crore)**

| Year | Departmental records | Finance Accounts | Difference |
|---|---|---|---|
| 2004-05 | 50.05 | 43.21 | 6.84 |
| 2005-06 | 74.19 | 89.98 | (-)15.79 |
| 2006-07 | 77.29 | 1.83 | 75.46 |
| 2007-08 | 92.06 | 72.74 | 19.32 |
| 2008-09 | 76.83 | 27.46 | 49.37 |

**The Government needs to issue suitable guidelines, making it mandatory for the controlling offices to carry out reconciliation as per the extant orders.**

### 2.2.7 Preparedness and transitional process

#### 2.2.7.1 Computerisation of the Taxation Department and the check gates and their interlinking

Before implementation of VAT, computerisation of the Department was completed and the necessary hardware, power backup facilities and VSAT connectivity were put in place in all the unit offices. Provision of Disaster Recovery System was installed at the National Data Centre of the National Informatics Centre.

Scrutiny revealed that though more than four years have elapsed, all the modules of the software could not be implemented. The registration, return, *challan* and way bill modules have been operationalised while other modules for capturing data on the tax deducted at source, online connectivity with other offices, e-filing of the returns were yet to be implemented. Online connectivity of only one check post at Byrnihat with the Commissionerate and the unit offices has been completed while interlinking of the remaining check posts was still being executed. Due to this, the department could not effectively track the interstate movement of the goods and check evasion of tax.

**The Government may initiate steps to expedite interlinking of the remaining checkposts with the commissioner and other unit offices. Also, the remaining modules of software may be developed and made operational at the earliest.**

#### 2.2.7.2 Creation of manuals

Although the MVAT Bill was passed by the State Legislature in March 2003 and VAT has been in place for more than four years, the department is yet to prepare a VAT manual. As a result, the various wings of the department do not have a reference point for effective practices.

**The Government may expedite the preparation of the VAT manual.**

#### 2.2.7.3 Completion of assessments under the repealed Acts

Audit observed that though the department was aware of the implementation of VAT well in advance, no time limit has been prescribed for completion of the assessments under the repealed Acts. It was noticed that out of a total of 99,643 pending assessments, only 20,245 assessments were completed upto 31 March 2009. In addition to these pending assessments, large number of assessments, scrutiny of the returns have also become due under the MVAT Act and unless the department takes immediate concerted action, it will be difficult for it to cope with the huge backlog. Also, a large quantum of revenue may be remaining to be collected because of the pending assessments.

**The Government may consider prescribing specific timeframe for completion of the assessments under the repealed Acts.**

### 2.2.8 Registration and database of the dealers

#### 2.2.8.1 Carrying forward of the database of the dealers under the repealed Acts and confirmation of the securities provided by them

Under the MVAT Rules, in case of the dealers registered under the repealed Acts, the appropriate registering authority shall issue a fresh certificate of registration in lieu of the existing certificate. However, in cases where fresh certificate of registration cannot be granted immediately, the registering authority may permit such dealer to continue to remain registered under the MVAT Act till the dealer is registered formally within 121 days from the date of receipt of such application and beyond that with the permission of the higher authority. **It was noticed that there is no mechanism to check the status of continuity of business of the unregistered dealers and the dealers who had opted not to register under the MVAT Act. Absence of it may lead to evasion of tax.**

Scrutiny of the records revealed that out of 5,658 dealers registered under the repealed Acts, 2,232, 449, 974 and 517 dealers were registered under the MVAT Act during 2005-06, 2006-07, 2007-08 and 2008-09 respectively and the remaining 1,486 dealers neither applied for registration nor did the registering authority initiate any action to register them. Further, 1,940 dealers were irregularly registered belatedly after a period ranging between 11 and 47 months without the permission of the higher authority as required under the provision of the Act. Though in these cases, any sales made by the dealers and tax realised on such sales before the registration under the MVAT Act was irregular and liable for penal action, yet the STs did not initiate any action to ascertain the sales made during the intervening period. Thus, evasion of tax in these cases cannot be ruled out.

After this was pointed out, the Government stated (November 2009) that the cases of the dealers who had not applied for registration would be looked into after conducting necessary inquiry. The Government added that in respect of the dealers registered under the repealed Acts and who were granted MVAT registration certificates belatedly; their cases would be reviewed for penal action.

**The Government may quickly investigate the turnover of these dealers during the intervening period and levy tax, interest and penalty as per the provisions of the MVAT Act.**

### 2.2.8.2 Registration of new dealers

Under the MVAT Act, no dealer liable to pay tax shall carry on his business as a dealer unless he has been registered and possesses a certificate of registration (RC) within 30 days from the date of liability. If any dealer, liable to pay tax, fails to get himself registered, the prescribed authority shall register him and direct him to pay, by way of penalty, in addition to the amount of tax so assessed, a sum equal to the amount of assessed tax and not less than Rs. 5,000. To identify the unregistered dealers, the COT has ordered the ITs to conduct regular surveys and maintain a survey register. This register is to be verified by the concerned ST periodically and note his remarks. While conducting inspection of the office, the ACT/DCT concerned should verify the register. A monthly report of the results of the surveys conducted should be submitted to the COT for reviewing the performance of the ITs. Besides, the enforcement branch is also responsible for detection of the unregistered dealers and bring them under the tax net.

**Audit scrutiny, however, revealed that the department has not prescribed any definite time frame and target for conducting survey for detection of unregistered dealers.**

Deficiencies noticed in the system of detection of unregistered dealers are discussed below.

- Data collected from 10 unit offices revealed that only 382 dealers were registered on the basis of surveys conducted by the ITs during 2005-06 to 2008-09.
- Survey registers were not verified by the concerned ST and the ACTs/DCT never visited the unit offices during the last four years.
- No monthly report was sent to the COT. As such, the performance of the ITs was not reviewed at all.
- The EB during 2005-2006 to 2008-09, could not detect even a single dealer who was not registered. This is inexplicable as audit had found through cross verification of records of two forest divisions and scrutiny of the records of five unit offices that though 606 dealers/works contractors did not apply for registration and carried out works contract/sold taxable goods, the concerned officer-in-charge of the units could not detect the dealers and register them. This resulted in non/short realisation of tax of Rs. 5.99 crore including penalty as mentioned in the table below.

R2 Rs. 599 lakh

**Table 3**

**(Rs. in lakh)**

| Sl. no. | Number of dealer<br>Name of unit | Item | Turnover<br>Period of transaction | Tax/penalty | Total dues |
|---|---|---|---|---|---|
| 1. | 1<br>ST, Jowai | Lime stone | 213.00<br>May 2005 to June 2006 | 8.51<br>8.51 | 17.02 |
| The Divisional Forest Officer, Jaintia Hills Division sold 4,73,040 MT of lime stone to the permit holders, but did not apply for registration under the VAT Act. The concerned ST also did not initiate any action to register the division. | | | | | |
| 2. | 575[9]<br>ST, Shillong and Jowai | Sandstone and clay | 368.00<br>August 2005 and December 2008 | 45.66<br>45.66 | 91.32 |
| 3. | 15<br>STs, Circle I, III, IV, VI, Shillong and Jowai. | Taxable goods | 1157.00<br>May 2005 and March 2009 | 145.00<br>145.00 | 290.00 |
| 590 unregistered dealers supplied/sold sand stone, clay and other taxable goods. The concerned STs could not detect this and register them. | | | | | |
| 4. | 13<br>Circle I, Shillong | Works contract | 333.00<br>March 2006 and March 2007 | 8.79<br>33.27 | 42.06 |
| 13 unregistered dealers constructed retail outlets of M/s Numaligarh Refinery Limited which escaped notice of the concerned ST. The Numaligarh Refinery Limited, however, deducted tax of Rs. 24.48 lakh instead of Rs. 33.27 lakh. | | | | | |
| 5. | 2<br>Circles III and IV, Shillong | Works contract | 673.00<br>May 2005 and October 2007 | --<br>159.00 | 159.00 |
| Though the dealers were registered, the item 'works contract' was not included in their certificates of registration. Thus, the dealers while executing works contract, falsely represented that the item 'works contract' was covered by their RCs and thus, liable to pay penalty. | | | | | |
| **Total** | | | | | **599.40** |

**The Government needs to fix targets for EB and ITs for detection of unregistered dealers through regular surveys and gathering of information from different sources.**

### 2.2.8.3 Periodic analysis of the dealers below the threshold

Under the MVAT Act, every dealer whose turnover exceeds Rs. 1 lakh is liable to pay the tax. Dealers/works contractors with turnover not exceeding Rs. 5 lakh can opt to pay the tax at one *per cent* of the gross turnover under the Composition Scheme. Above this limit, the dealers are required to be registered and pay the tax at the prescribed rate.

Scrutiny of the records, however, revealed that the eligibility for tax liability under the composition scheme was ascertained on the basis of the returns submitted by the dealers only. **There was no system instituted for periodic scrutiny of the books of accounts to verify whether a dealer/contractor has crossed the above threshold.**

[9] Detected from verification of the records of the Divisional Forest Officers, Khasi Hills and Jaintia Hills Division.

After this was pointed out, the Government stated (November 2009) that the composition scheme for Works contract was being amended. The reply was silent regarding the dealers other than the works contractors.

**The Government may consider prescribing a system for periodic verification of the books of accounts of the dealers to detect cases of crossing the threshold.**

#### 2.2.8.4 Database of dubious/risky dealers

To prevent evasion of tax, a database of dubious dealers needs to be prepared based on their past history on fraud/concealment/usage of fake forms and updated at regular intervals. The database should be made online in the Department's website/TINXSYS, which will facilitate a watch on the dealers. Such a database, if available, can be used while selecting the dealers for audit assessments and consulted before finalising any assessment/scrutinising the returns for effective risk analysis.

### 2.2.9 Deficiencies in the Act and the Rules

The review revealed a number of deficiencies in the provisions of the MVAT Act and the Rules made thereunder which persisted during the period covered under the review. Some of the important deficiencies are discussed below.

#### 2.2.9.1 Deficiencies in the forms for submission of returns

Under Rule 30 of the MVAT Rules, all registered dealers paying the composite tax shall submit a correct and complete return in Form 5 quarterly within 21 days from the close of a quarter. Any other dealer liable to pay tax, but not composite tax, shall submit monthly return and pay due tax within 21 days from the end of the month.

It was, however, noticed that Form 5 is a quarterly return applicable to the dealers making payments of composite tax. No monthly tax return form for the other dealers has been prescribed. Further, in addition to the tax return, a correct and complete annual return has been prescribed in Form 6, but that form also applies to the dealers opting for the composite tax. Due to these anomalies, no dealer submitted the monthly/annual returns during the period 2005-09.

After this was pointed out, the Government stated (November 2009) that a different format for the dealers who opted for the composition scheme would be prescribed.

**The Government may immediately prescribe the monthly/annual return forms for the general dealers**.

#### 2.2.9.2 Mechanism to monitor filing of the returns

Under the MVAT Act, all the registered dealers shall file returns showing the details of the total turnover, exemption claimed, taxable turnover, output tax due, tax collected, input tax credit availed of, tax due including reverse tax credit, if any, and the tax paid separately for that return period. The return period is

monthly in majority of the cases and in some cases quarterly to be filed within 21 days from the end of the month or the close of the quarter as the case may be. In case of discovery of an error in a return, revised return may be furnished within 60 days from the date of submission of the original return.

Deficiencies noticed in the mechanism for monitoring the filing of the returns are mentioned below:

- Registers for receiving the returns have neither been prescribed nor maintained by any of the STs test checked. As such, it was not possible to ascertain the timely receipt of the returns/filing of the revised returns.
- There was no system of monitoring timely receipt of returns in the unit offices and action taken by the AOs for belated submission of the returns by the COT.
- There was no mechanism to ascertain whether notices were issued to the dealers who had not submitted the returns.

**The Government may take appropriate steps for regular monitoring of timely receipt of the returns and prompt action against the defaulters.**

#### 2.2.9.3 Scrutiny and verification of the returns

Deficiencies in the scrutiny and verification of the returns noticed in course of this review are discussed below.

- There is no record prescribed to ascertain whether scrutiny of the returns has been carried out and the result of such scrutiny.
- As per the information furnished by the department, during 2005-06, 2006-07, 2007-08 and 2008-09, scrutiny of the returns of only 'nil', 59, 79 and 284 cases respectively had been completed.
- Since none of the dealers furnished the monthly returns or annual returns in case of turnover of more than Rs. 40 lakh alongwith the audit report certified by a CA, the statistical data of the scrutiny of the return as furnished by the department cannot be considered correct.
- No provision was made in the MVAT Rules for submission of the monthly/quarterly and annual report showing scrutiny of the return due, scrutiny completed, returns pending for scrutiny.

**Immediate action needs to be taken by the Government to fix norms quantifying the number of scrutiny to be completed by each AO during a particular period including a mechanism for monitoring the compliance of such orders.**

#### 2.2.9.4 Result of scrutiny of the returns conducted by audit

Result of independent scrutiny of some selected files of eight STs in Shillong, Jowai and Nongpoh during the course of this review brought out many instances of short levy, excess availing of input tax credit, non/short levy of interest etc.

Instances of excess input tax credit are included in the paragraph relating to input tax credit. Remaining cases are discussed in the succeeding paragraphs.

- Under the MVAT Act, any dealer, who without reasonable cause, fails to furnish monthly or annual tax returns within the stipulated time shall be liable to pay penalty of Rs. 100 per day subject to a maximum of Rs. 10,000. Also, the AO will proceed to assess the dealer on best judgment basis.

Test check of the records revealed that 11,816 dealers failed to furnish monthly and annual returns during 2005-06 to 2008-09, but the concerned AOs neither served notices in form 54 nor proceeded to assess them on best judgment basis for the aforesaid period. For non-submission of the returns, penalty of Rs. 372.21 crore was leviable at the minimum rate, but was not levied.

- Under section 40 of the MVAT Act, if a dealer fails to pay the admitted tax within the due date, interest at the rate of two *per cent* per month is leviable on the amount by which the tax paid falls short for the entire period of the default.

It was noticed that 87 dealers paid the admitted tax of Rs. 20.51 crore as disclosed in 490 returns for the period between April 2005 and March 2009 belatedly after delays ranging between 5 days and 35 months. For belated payment of the tax, interest of Rs. 81.03 lakh was leviable at the minimum rate, but was not levied.

- Under the MVAT Act, if a registered dealer fails to pay the amount of the due tax and interest alongwith the return or the revised return, the COT may direct him to pay, in addition to the tax and the interest payable by him, penalty at the rate of two *per cent* per month on the tax and interest so payable.

It was noticed that 87 dealers defaulted in paying the tax and interest of Rs. 21.32 crore as per the returns. For default in payment of the tax, penalty of Rs. 84.23 lakh calculated at two *per cent* on the tax and interest though leviable was not levied.

- Under the MVAT Act, if a dealer conceals the particulars of his turnover or deliberately furnishes inaccurate particulars of such turnover, the COT may accept, by way of composition of offence, a sum not exceeding Rs. 5,000 or double the amount of tax, whichever is greater.

Cross verification of the records of 11 dealers registered under five sales tax units with the particulars of two cement manufacturing units revealed that the dealers purchased 'cement' valued at Rs. 33.63 crore between May 2005 and March 2009. But the dealers neither disclosed the turnover in their returns nor paid any tax. The dealers thus concealed purchase turnover of Rs. 33.63 crore and evaded tax of Rs. 3.69 core. Besides, penalty of Rs. 7.38 crore was also leviable.

- Under Section 61 of the MVAT Act, if a registered dealer collects any amount by way of tax in excess of the tax payable by him, he shall be liable to pay, in addition to the tax, a penalty of an amount equal to twice the sum so collected by way of tax.

It was noticed that though seven dealers collected tax of Rs. 15.13 crore in excess of their tax liability, the AOs did not take any action to forfeit it and deposit in the

Government account and levy penalty of Rs. 30.26 crore. This resulted in non-recovery of tax of Rs. 45.39 crore as mentioned in the table below.

**Table 4**

**(Rs in crore)**

| Sl. No. | Number of dealers<br>Name of the unit | Turnover<br>item | Tax collectible<br>Tax collected | Tax collected in excess<br>Penalty leviable | Total due |
|---|---|---|---|---|---|
| 1. | A cement manufacturing unit<br>ST, Jowai | 147.93<br>clinker | 5.91<br>18.49 | 12.58<br>25.16 | 37.74 |
| 2. | Three dealers<br>ST, Circles III, IV and VI, Shillong | 8.44<br>Taxable goods | 1.06<br>1.51 | 0.45<br>0.90 | 1.35 |
| 3. | Three oil companies<br>ST, Circle I,III, Shillong | 46.70<br>lubricants | 3.74<br>5.84 | 2.10<br>4.20 | 6.30 |
| **Total** | | | | | **45.39** |

- Under the MVAT Act, if a dealer fails to submit the returns and pay the tax, the AO shall complete the assessment on best judgment, after allowing the dealer an opportunity of being heard.

Test check of the records of the ST, Circle VI, Shillong revealed that a registered dealer purchased taxable goods valued at Rs. 1.63 crore between October 2005 and September 2006 from outside the State. The dealer disclosed turnover of Rs. 40 lakh in his return during the aforesaid period. Thereafter, the dealer neither submitted any return nor paid any tax. Further scrutiny revealed that the dealer was not traceable. Thus, due to non-initiation of the assessments on best judgment there was loss of revenue of Rs. 15.43 lakh.

After the cases were pointed out, the Government while accepting the audit observations stated (November 2009) that necessary steps were being taken to amend the MVAT Rules pertaining to the period of submission of the returns, the returns format, scrutiny of the returns etc.

**The Government may consider issuing guidelines, prescribing the points to be checked while scrutinising the returns.**

### 2.2.9.5 Documents to be furnished alongwith the return

Audit scrutiny revealed that though the MVAT Act and the Rules specify the records to be submitted alongwith the monthly and annual returns, these do not provide for submission of vital details like purchases made (inside and outside the State), opening and closing stock/trading and manufacturing accounts as applicable, utilisation of the declaration forms under State/Central Acts etc.

Since majority of the case will be scrutinised on the basis of the returns only, in the absence of these basic documents no meaningful scrutiny would be possible.

**The Government may amend the Act and the Rules to make the returns self sufficient.**

### 2.2.10 Tax audit

As per the MVAT Act, the COT shall randomly select dealers for audit assessments by 31 January every year and send the list to the appropriate audit

authority. The concerned audit officer shall issue a notice in form 21 and complete the audit assessments with copies to the concerned dealer and the COT. The Act also provides that no audit assessment shall be made after the expiry of five years from the end of the tax period to which the assessment relates.

**Audit scrutiny revealed that although more than four years have elapsed after introduction of the VAT in the State, neither the percentage of the dealers to be selected for audit assessment nor the criteria for such selection have been prescribed. No time frame has also been fixed for completion of the audit assessment.**

Cases for the year 2005-06 will be barred by limitation of time by 31 March 2011 and it may not be possible for the department to complete the entire process of prescribing the criteria for selection of dealers, percentage of dealers to be selected, framing the VAT manual/audit team and complete the audit assessments of 2005-06 by March 2011.

After this was pointed out, the Government while admitting the facts stated (November 2009) that an audit team with the DCT as its head had been constituted recently and audit assessments would be taken up only in those cases where the tax period to which the assessments relate are not more than five years old. The reply is not tenable as the Government should gear up to ensure that none of the cases gets time barred leading to non-detection of evasion of taxes.

**The Government may immediately prescribe the criteria, timeframe and percentage of the dealers and frame the VAT manual so that the audit assessments can be started immediately in the interest of revenue.**

### 2.2.11 Input tax credit

Under the MVAT Act, input tax credit (ITC) shall be allowed to a registered dealer on the purchase of the taxable goods (other than the goods specified in Schedule V[10] of the Act) within the State from another registered dealer for the purpose specified therein. For this, a dealer has to submit a statement of the purchase in which the invoice number, date, TIN of the dealer effecting sale, description and the value of the goods, VAT charged etc., are required to be entered alongwith the supporting documents. **However, it was observed that there is no column for description of the goods purchased making it difficult to check correct application of rate of tax.**

### System of cross verification of the records of selling dealers

Though the MVAT Act provides for submission of tax invoices alongwith the claims for input tax credit, **it was noticed that the tax invoices in support of ITC were not attached with the returns in majority of the cases.** No action was taken by the concerned AOs to obtain the tax invoices before allowing the claims. **Also, neither the Act/Rules nor the department has prescribed any**

[10] Liquor, lottery tickets, molasses, rectified spirit, medicine and drugs.

**system of cross verification of the input tax credit claims.** Thus, the department was allowing ITC without any supporting documents and further checks.

Cases of irregular allowance of input tax credit detected during the review are mentioned below.

- Test check of eight sales tax unit offices revealed that 66 dealers in their 552 quarterly returns submitted between May 2005 and December 2008 disclosed purchase of goods taxable at four *per cent* and 12 *per cent* amounting to Rs. 247.80 crore from within the state and showed the element of VAT as Rs. 15 crore. The ITC was adjusted against the output tax of Rs. 49.64 crore on the turnover of Rs. 517.64 crore. Further scrutiny of the records, however, revealed that the supporting documents like tax invoice, name of the selling dealer alongwith TIN, value, amount of VAT etc., were not furnished in support of the claim of ITC. The allowance of ITC of Rs. 15 crore without supporting documents was not correct.

R2 Rs. 1500 lakh

- Test check of the records of ST, Jowai revealed that a manufacturing unit purchased goods valued at Rs. 147.93 crore between April 2007 to March 2009 from another unit registered in the same office but claimed ITC of Rs. 18.49 crore instead of Rs. 5.91 crore as admissible. The AO failed to detect the lapse resulting in excess allowance of ITC of Rs. 12.58 crore.

R2 Rs. 1258 lakh

- Scrutiny of the records of the ST, Circle VI showed that a dealer sold lubricants valued at Rs. 19.50 crore during 2005-06 to 2008-09 and collected tax of Rs. 2.44 crore. The dealer claimed ITC of Rs. 2.31 crore against the output tax of Rs. 2.44 crore. Since lubricant is taxable under the Petroleum Taxation Act and, therefore, non-VATable, ITC claim of Rs. 2.31 crore was not admissible.

R2 Rs. 231 lakh

- A manufacturing unit registered under ST, Nongpoh claimed an ITC of Rs. 2.06 crore on the purchase of raw material valued at Rs. 51.57 crore within the State between October 2006 and July 2008. After adjustment of the output tax and liability of CST of Rs. 1.47 crore, the dealer was entitled to claim a refund of Rs. 59 lakh. But he claimed a refund of Rs. 1.10 crore resulting in excess claim of refund of Rs. 51 lakh which was also allowed by the AO.

R2 Rs. 51 lakh

**The Government may prescribe a system of cross verification of the records of the selling dealers on a random basis before allowing the ITC. They may also consider amending the format of the return to provide for the particulars of the goods in the form.**

### 2.2.12 Deficiencies in the provision relating to goods taxable at the first point

**2.2.12.1** Before introduction of the VAT, the sales tax on liquor was being collected as a part of the state excise duty. There was no separate sales tax levied on the liquor. After introduction of the VAT, liquor became taxable at the rate of 20 *per cent* at the point of first sale within the State with effect from 1 May 2005.

However, VAT on liquor remained merged with the excise duty till 30 August 2005. The State Government authorised separate collection of VAT on liquor by delinking it from the excise duty from 31 August 2005.

After delinking, VAT was chargeable on the cost of liquor plus the excise duty. This was greater than the component of sales tax when it was part of the excise duty. The loss of revenue due to the delay in delinking VAT from the excise duty, varied between Rs. 14 and Rs. 1,222.60 per case of different brands of liquor. Test check of the records revealed that 21 bonded warehouses sold 6,83,050 cases of different brands of liquor between May and August 2008. Due to the delay in delinking the VAT from the excise duty, there was loss of revenue of Rs. 4.15 crore.

**2.2.12.2** In Meghalaya, liquor is taxable at the rate of 20 *per cent* at the point of first sale within the State with effect from 1 May 2005.

Test check of the records, however, revealed that three manufacturers of liquor (bottling plants) sold 26,84,292 cases of liquor between May 2005 and March 2009. Since bottling plant is the first seller within the State, tax of Rs. 34.20 crore was leviable, but the AO did not levy the tax resulting in loss of Rs. 34.20 crore.

**2.2.12.3** Medicine is taxable at six *per cent* on the maximum retail price under the MVAT Act. The rate of tax on the sale of the stock of medicines purchased by the retailers between May 2004 and April 2005 and lying in stores as on 1 May 2005, however, continued to be at eight *per cent* with surcharge at the rate of 20 *per cent*. The transitional arrangement was limited to two months from 1 May 2005.

Since the retailers were neither registered under the repealed Act nor under the MVAT Act, it was not possible to ascertain the transitional stock of these dealers. Thus, during the aforesaid period of two months, there was every possibility that the retailers purchased goods at six *per cent* and sold them at 9.6 *per cent* including surcharge and retained the tax so collected. Thus, there was loss of revenue at the rate of 3.6 *per cent* due to the issue of defective notification by the Government.

### 2.2.13 Forms for claiming exemption on sale of tax paid goods

Goods under Schedule V of the MVAT Act are taxable at the point of first sale. Subsequent sales within the State are then exempted from the payment of tax. But no form has been prescribed for claiming exemption from tax for the subsequent sales within the State. In the repealed Acts, for claiming exemption, the dealers were required to furnish a statement showing the dealers from whom the goods were purchased alongwith the bill numbers and date, description of the goods purchased and tax paid. No such executive instruction has also been issued till date in case of the sales made in the post-VAT period. As a result, cross verification of the purchase and sale of the tax-paid goods was not possible.

After this was pointed out, the Government stated (November 2009) that the dealers making subsequent sales were not liable to be registered and hence claim

of exemption from tax did not arise. The reply is not tenable as there are a number of dealers dealing in both VATable and non-VATable items and they claim exemption on the tax-paid sales.

**The Government may consider making it mandatory for the dealers to furnish the details while claiming exemption on account of first point taxable goods. Provisions may be made in the MVAT Act and Rules accordingly.**

### 2.2.14 Irregular grant of incentives to exempted industrial units

After introduction of the MVAT Act, the State Government implemented the Meghalaya Industries (Tax Remission) Scheme, 2006 substituting the Meghalaya (Sales Tax Concession) Scheme, 2001 from 1 October 2006. Under the new scheme, total exemption from the payment of tax was withdrawn and the units were allowed remission of 99 *per cent* of the tax payable and the balance was to be deposited in the Government account. However, in respect of the cement/clinker manufacturing units having output capacity of 600 tonnes per day, the remission was to be limited to 96 *per cent.* Besides, the units were also allowed ITC on their purchases.

Test check of the records of the ST, Jowai and Nongpoh revealed that four manufacturing units collected tax of Rs. 14.40 crore on the sale of goods between October 2006 and March 2009 and deposited Rs. 47 lakh in Government account and the balance Rs. 13.93 crore was retained by them as subsidy under the new scheme. **Thus, by allowing the dealers to collect and retain the output tax, the Government had allowed undue financial benefit to the incentive holders at the cost of the general public. Besides, due to the grant of ITC in addition to the remission of the output tax, the State had to pay Rs. 7.98 crore to two manufacturers from its own coffers.**

After this was pointed out, the COT stated that the benefit of the input tax credit was withdrawn with effect from 9 July 2009. The reply was, however, silent regarding the loss of revenue suffered by the State government between October 2006 and June 2009 due to the introduction of the defective Industrial Remission Scheme and also why retrospective effect was not given to the order.

The Government stated (November 2009) that since the Meghalaya Industries (Tax Remission) Scheme 2006 has been challenged in the court by some industrial units, no comments could be made. The reply is not tenable as the operation of the scheme was not stayed by the court.

**The Government may review the issue and consider retrospective amendment of the provisions of the scheme so that the loss can be made good.**

### 2.2.15 Deficiencies in the provision for cross verification of the records of other departments/sources like Central Excise, Income Tax Department, Tax Information Exchange System (TINXSYS) etc.

With a view to checking the evasion of tax, the Government has established an Enforcement Branch (EB) under the COT with one ST and some ITs having

jurisdiction over the entire State. The EB has been entrusted with the functions like intelligence gathering, interception of the vehicles carrying goods on transit between the entry and exit check gates and effective liaisoning with other departments like Central Excise and Customs etc.

**2.2.15.1** Mention was made in ***paragraph 6.2.17*** of the Audit Report for the year ended March 2008, Government of Meghalaya regarding evasion of tax due to delivery of the goods in the State of Meghalaya which are actually meant for other States leading to loss of revenue of Rs. 20.51 crore. Further verification during this review revealed the following:

- Test check of the TP Register of the ST, Byrnihat check post revealed that out of 402 TPs issued between November 2007 and March 2008, 56 TPs had not been received back till September 2008. Thus, these vehicles carrying taxable goods actually delivered the goods within the State which escaped the notice of the EB. Out of 56 vehicles, 11 vehicles did not furnish detailed particulars of the value of the goods carried. The remaining 45 vehicles carried taxable goods valued at Rs. 1.64 crore and evaded tax of Rs. 12.43 lakh.

- Similarly, test check of the record of the ST, Umkiang check post revealed that 24 vehicles carrying taxable goods valued at Rs. 74.51 lakh obtained the TPs from the entry check post but did not deliver these passes to the officer-in-charge of the exit check post at Byrnihat and thus, evaded tax of Rs. 9.08 lakh.

**The Government may consider a mechanism for effective monitoring of the vehicles carrying goods meant for other States passing through the State to arrest this persistent problem.**

**2.2.15.2** Though the EB was strengthened for intelligence gathering and cross checking the information of the dealers with other records/sources**, it was noticed that the department has not prescribed the periodicity, number of cases etc., for cross verification of the turnover with the records of the Income Tax and Central Excise Departments.**

After this was pointed out, the Government stated (November 2009) that the concerned IT might take up the case when any doubt arises regarding turnover disclosed by the dealer. The reply is not tenable as the department failed to show a single case which was cross verified with the two departments during the period of review. Besides, putting in place a regular system of cross verification of the records instead of a discretionary provision to check the cases on pick and choose basis would certainly be more effective.

**Mandatory provisions may be made in the MVAT Act/Rules to cross verify the records of the IT, CE Departments on the basis of specified criteria like high turnover, past instances of irregularities committed by a dealer including suppression of turnover, misuse of forms to wrongly claim exemption etc.**

**2.2.15.3** The empowered committee had instituted a database on interstate dealers commonly known as TINXSYS (Taxation Information Exchange System)

intended to serve as a centralised repository of all interstate transactions. Apart from verification of the dealers' accounts, the information available in TINXSYS can also be used for verification of the central statutory forms issued by other State Taxation Departments and submitted by the dealers in support of the claim for concessions/exemptions.

**Scrutiny of the records, however, revealed that the department has not issued any instructions for verification of the details given in the statutory forms filed by the dealers from the information available in the TINXSYS while allowing concessional rate/exemption of tax.** As such, cross verification of the statutory forms issued by the dealers of other states could not be carried out. Cases of availing of concessional rate of tax by utilising fake declaration forms have been reported in previous Audit Reports[11].

After this was pointed out, the COT stated (November 2009) that inter-operability software for online exchange of information between north eastern states was being developed. The Government endorsed the views of the COT. The reply is not relevant to the issue raised by audit as the software referred to is limited to the north eastern dealers while the TINXSYS is a national database.

**The Government may consider issuing instructions making it mandatory to cross verify the details given in the statutory forms filed by the dealers with reference to the data available in TINXSYS before allowing reduction/ exemption of tax.**

### 2.2.16 Provisions governing tax deducted at source

#### 2.2.16.1 System of sending the details of works contract/purchases by the works/buying departments to the Taxation Department

Under the MVAT Act, the person deducting tax shall issue a certificate of tax deduction to the payee in form 24. He shall maintain an account in the prescribed format and furnish a return to the concerned AO periodically. If a Government department fails to deduct tax at source, it is an offence and the COT may accept from the person charged with such offence, by way of composition of the offence, a sum not exceeding Rs. 5,000 or double the amount of tax, whichever is greater.

**Test check of the records revealed that no accounts in form 25 and return in form 26 were furnished to the Taxation Department by any of the Government Departments. No action was also taken by the AOs against the defaulting departments. It was also noticed that there was no system for periodic verification of the records of the works/buying departments by the AOs to detect issues of non/short deduction of tax at source.**

Cross-verification of the records of the Government departments with those of the dealers in respective circles revealed the following.

[11] Paragraph 6.26 of AR 2005-06; paragraph 6.23 of AR 2006-07; paragraph 6.22 of AR 2007-08; paragraph 2.7 of AR 2008-09.

- Three dealers registered in Circle III, Shillong executed lease transaction with the Government departments valued at Rs. 2.02 crore between January 2006 and January 2007. The departments neither deducted tax at source nor did the dealers deposit the tax. Thus, due to non-deduction of tax at source, the dealers concealed the turnover and evaded tax of Rs. 25.25 lakh.

- Six dealers registered in Circle III & IV, Shillong sold goods valued at Rs. 2.23 crore to the Government departments between June 2005 and January 2008 but the departments did not deduct tax at source. The dealers also concealed the turnover in their returns and evaded tax of Rs. 17.30 lakh.

- Eighteen dealers sold taxable goods/executed works contract of Rs. 3.38 crore to North East Indira Gandhi Regional Institute of Health and Medical Sciences between May 2005 and March 2008, but the department did not deduct tax of Rs. 31.01 lakh at source.

- Two dealers registered in Circle III, Shillong sold taxable goods valued at Rs. 5.61 crore to the Government departments between May 2005 and October 2007 and tax of Rs. 62.09 lakh was deducted at source. The amount deducted has not been deposited into the Government accounts (February 2010).

**The Government may prescribe a system for periodic verification of the records of the works/buying departments by the AOs to detect cases of non/short deduction of tax at source.**

### 2.2.16.2 Bar on purchase/engagement from/with unregistered dealers by buying Departments

Under the MVAT Act, deduction of tax at source is applicable even in the case of the unregistered dealers. There is no bar on buying departments for awarding works/supplies contracts to the unregistered dealers.

In view of the evasion of tax by the dealers coupled with non-submission of the returns by the Government departments as pointed out in the preceding paragraph, works contracts/supplies awarded to the unregistered dealers are fraught with the risk of leakage of revenue.

**The Government may consider making necessary amendment in the Act/Rules barring the Government departments from entering into works/supplies contracts with unregistered dealers.**

## 2.2.17 Deterrent measures

### 2.2.17.1 Deficiencies in the deterrent measure

As per the MVAT Act, non-submission of the audit certificates by the dealers having turnover of more than Rs. 40 lakh attracts maximum penalty of Rs. 10,000. Though the Act provides for suspension of the registration certificate in case of recurrence of the offence, this provision was not seen to have been invoked. Since the audited account is the sole basis on which the actual turnover of a dealer can be ascertained, the nominal penalty in these cases may be misused

by the dealers to evade tax. **Thus, the quantum of penalty for first, subsequent or continued offence may be separately fixed to make the deterrent measure more effective.**

The Government accepted (November 2009) the audit observation and stated that necessary action would be taken to make penal provisions more deterrent.

### 2.2.17.2 Absence of minimum penalty for offence

- Under the MVAT Act and the Rules, an assessee has the option to file a revised return, alongwith the interest, penalty etc., in addition to the differential tax and interest. However, the Act does not provide for levy of the minimum amount of penalty in cases where best judgment assessment is resorted to. Though, a penalty of a sum not exceeding one and half times of tax can be levied under Section 45, it is left to the discretion of the assessing authority. In such cases, it was noticed that either no penalty or only a small amount of penalty was levied on the ground that *mens rea* was not proved.

- Under the MVAT Act, if a dealer himself detects an omission before the initial scrutiny and submits a revised return showing an increase in the liability of the tax, in addition to the payment of the balance tax, he is also liable to pay interest under Section 40 and two *per cent* of the tax and interest as penalty under Section 36(3). But if a return is rejected during the initial scrutiny under Section 39(2) only interest is payable. Thus, there is inconsistency in the penal measures in similar types of offences which needs to be rectified.

- The MVAT Act, *inter alia,* stipulates two types of penal provisions for serious offences like carrying business without being registered, failing to furnish the returns and pay the tax without reasonable cause, furnishing false returns, concealing the particulars of the turnover, evading payment of tax etc. While Section 90 provides for imposition of fine not exceeding Rs. 10,000, Section 96 provides for compounding of the offences for a sum of Rs. 5,000 or double the amount of tax, whichever is higher. Thus, two types of penal provisions exist for the same kind of offence and discretion in levy of any of these penalties may be beneficial to some dealers and detrimental to others.

**In the interest of revenue and to increase transparency, the Government may make provisions in the Act/Rules to fix minimum penalty for each type of offence based on its magnitude. It should not be left to the discretion of AO. There must be specific distinction between the amount of penalty leviable for the first offence and subsequent offences as well as for wilful default.**

### 2.2.18 Internal control

Internal controls are intended to provide reasonable assurance of orderly, efficient and effective operations, adherence to the laws, regulations and management directives and maintenance of reliable data. Effective internal controls both in the manual and computerised environment are pre-requisites for efficient functioning of any department. Following deficiencies were noticed in the internal control mechanism:

### 2.2.18.1 Maintenance of registers in unit offices

It was noticed that there was no register for recording the receipt of the returns/revised returns in any of the test checked units. Even in cases where the returns were available in the assessment files, the date of submission/receipt was neither mentioned by the dealer nor by the AO. No register had been prescribed to record the names of the dealers whose returns were scrutinised. Road permit/way bill registers were not maintained by most of the AOs.

Further, neither the MVAT Act/Rules nor any departmental circular prescribes recording of the details in a separate register of the total turnover, taxable turnover, output tax, input tax credit, tax payable etc. In case of any requirement, these have to be compiled from the information in respective assessment files which are not kept systematically.

### 2.2.18.2 Reports and Returns

The COT, Meghalaya prescribed that a monthly report on the survey of the dealers by the ITs shall be submitted by the ITs to the COT.

Test check revealed that the monthly report on the survey of the dealers by the ITs has never been submitted to the COT. The review of the performance of the ITs could not, therefore, be carried out by audit.

### 2.2.18.3 Inspection by supervisory officers

Regular inspection of the unit offices/check gates by the ACT/DCT/COT is essential to ensure satisfactory functioning of all the offices.

Scrutiny revealed that no inspection had ever been carried out by the aforesaid officials which is yet another instance of lack of internal control mechanism.

### 2.2.19 Internal audit

Internal audit is one of the most vital tools of the internal control mechanism and functions as the ‘eyes’ and ‘ears’ of the management and evaluates the efficiency and effectiveness of the mechanism. It also independently appraises whether the activities of the organisation are being conducted efficiently and effectively.

It was observed that the Taxation Department has no independent internal audit wing. The Examiner of Local Accounts (ELA) is responsible for conducting the internal audit of the department. The Government stated that internal audit of Taxation Department was taken up annually by the ELA. The reply is not tenable as cross verification of the records of the ELA revealed that no internal audit had been conducted by the ELA since the introduction of VAT.

**The Government may consider strengthening the mechanism for internal control including internal audit.**

### 2.2.20 Claims for compensation of loss due to introduction of VAT

The VAT Act was implemented in Meghalaya with effect from May 2005. The Government of India (GOI) agreed to compensate the State Government for loss of revenue, consequent to the implementation of VAT and issued guidelines in June 2006 mentioning the modalities for compensation claims. As per the guidelines, VAT receipts were to be compared with the revenue of the pre-VAT period, suitably extrapolated on the basis of the average of three best growth rate of revenue of the previous five years. According to the norms prescribed by the GOI, the revenue loss was to be worked out by including the tax revenue generated from the commodities like petrol, diesel, aviation turbine fuel, liquor, lottery brands which had been kept outside the VAT and were subject to 20 *per cent* floor rate of tax and the credits on account of the input tax under VAT adjusted against the CST from the overall tax revenue of the VAT year. The resultant net revenue was to be compared with the projected tax revenue for working out the loss on account of introduction of VAT. The rates of compensation were to be 100, 75 and 50 *per cent* during the first, second and third year respectively of the implementation of VAT.

Scrutiny of the records of the COT revealed that the State Government did not prefer any such claim for the year 2005-06 to 2007-08. Further scrutiny revealed that against the projected revenue of Rs. 115.12 crore, Rs. 210.13 crore and Rs. 389.85 for the year 2005-06, 2006-07 and 2007-08, the actual collection was Rs. 75.81 crore, Rs. 151.13 crore and Rs. 101.97 crore respectively. The Government did not prefer any claim for compensation of loss of revenue of Rs. 247.49 crore due to the introduction of VAT. The loss of revenue would be even more if the amount of input tax adjusted against the interstate sales and the arrear of sales tax revenue collected during the VAT period could be ascertained. Audit also could not collect the figures due to the non-completion of the assessments and non-submission of the arrears of sales tax revenue collected during the post-VAT period.

### 2.2.21 Conclusion

Analysis of the transitional process from sales tax to VAT revealed various deficiencies in the process and lacunae in the MVAT Act and Rules. Even after four years of implementation of VAT in the State, the VAT manual has not been finalised due to which neither the audit assessments could be started nor could the working of other functional areas of the department streamlined. Though computerisation has been initiated, all the modules of the software were yet to be implemented and the check posts, except one, were not inter-linked with the Commissionerate/unit offices. There was no system for periodic verification of the books of accounts to detect whether a dealer had crossed the threshold. Delayed and inadequate scrutiny of returns left enough scope for leakage of revenue. No monitoring system existed regarding surveys made by the ITs to detect unregistered dealers and scrutiny of the return by the STs. The procedure prescribed for the incentives under the MVAT law resulted in undue enrichment of the incentive holders. The department has not instituted a system of cross

verification with the records of other dealers/IT, CE Department/TINXSYS while scrutinising returns/audit assessments. Internal control mechanism was weak. There was no internal audit. No inspection had also been conducted by departmental officers and no reports were submitted to the prescribed authority.

### 2.2.22 Summary of recommendations

The Government may consider implementing the recommendations noted under the paragraphs included in the review with special emphasis on the following for rectifying the deficiencies.

- Preparing a VAT manual to streamline the working of the department.
- Taking appropriate steps to ensure monitoring of the timely receipt of the returns and prompt action against the defaulting dealers.
- Prescribing the norms/guidelines for scrutiny of the returns by the AOs and monitoring its' progress.
- Prescribing the criteria, timeframe, and percentage of dealers and frame the VAT manual for starting the audit assessments immediately.
- Prescribing cross verification of information in the returns with various other sources to increase the control over evasion of tax.
- Retrospectively amend the provisions on input tax credit to the incentive holders so that the loss of revenue could be made good.
- Fixing separate quantum of penalty for first, subsequent or continued offence to make the deterrent measure more effective, and
- Strengthening the internal control mechanism including internal audit.

## 2.3 Other audit observations

*Scrutiny of the assessment records of the Taxation Department indicated cases of non-observance of the provisions of the Acts/Rules, non-short levy of tax, turnover escaping assessment, concealment of turnover etc., which are mentioned in the succeeding paragraphs of this chapter. These cases are illustrative and are based on test check carried out in audit. Such omissions on the part of the AOs 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 strengthening of the internal audit to ensure that such omissions are detected, rectified and avoided in future.*

## 2.4 Short levy of tax due to incorrect application of rate

**Short levy of tax of Rs. 6.76 lakh and interest of Rs. 2.78 lakh due to incorrect application of rate**

Under the Meghalaya (Sale of Petroleum etc.) Taxation Act, tax shall be levied at the first stage of sale of the taxable goods in the State. As per entry 3 of the Act, diesel oil is taxable at the rate of 12.5 *per cent* with effect from 21 September 2004.

Scrutiny of the records of the Superintendent of Taxes (ST), Jaintia Hills District, Jowai revealed (June 2008) that two dealers disclosed turnover of Rs. 1.50 crore for the period from October 2004 to March 2007 and paid tax of Rs. 12.01 lakh at the pre-revised rate of eight *per cent* instead of Rs. 18.77 lakh at 12.5 *per cent.* The AO assessed the dealers accordingly between May and October 2007. Thus, due to the application of incorrect rate, tax of Rs. 6.76 lakh was short levied. Besides, interest of Rs. 2.78 lakh was also leviable.

After the cases were pointed out, the Government while admitting the facts stated (January 2010) that the dealers had been reassessed and Rs. 8.78 lakh had been recovered from them. Realisation of the balance amount has not been intimated (February 2010).

## 2.5 Concealment of turnover

**Thirteen registered dealers concealed turnover of Rs. 54.96 crore and evaded tax of Rs. 2.74 crore on which penalty of Rs. 5.48 crore was also leviable**

Under the Meghalaya Value Added Tax (MVAT) Act, 2003, if any dealer conceals the particulars of his turnover or evades in any way the liability to pay tax, he shall be liable to pay, in addition to the tax, penalty not exceeding Rs. 5,000 or double the amount of the tax payable on the sale turnover, whichever is greater. The provision of the Act applies *mutatis mutandis* in case of the assessment and reassessment under the Central Sales Tax (CST) Act, 1956.

Further, sale of the declared goods in the course of interstate trade is taxable at the concessional rate of four *per cent* upto 31 March 2007 and three *per cent* thereafter, if such sale is supported by a declaration in form 'C', otherwise such sale is taxable at the rate of eight *per cent* upto 31 March 2007 and four *per cent* thereafter. The Commissioner of Taxes (COT), Meghalaya in his notification dated March 2002 fixed the rate of advance tax at Rs. 1,800 for 15 MT coal based on its prevailing market price ranging between Rs. 1,400 and Rs. 1,500 per MT.

Scrutiny of the records of the ST, Jaintia Hills District, Jowai revealed (June 2008) that 13 dealers sold 8.74 lakh MT of coal in the course of interstate trade between October 2005 and December 2007. The dealers disclosed turnover of Rs. 67.47 crore in their returns for the aforesaid periods duly supported by 'C' forms instead of Rs. 122.43 crore calculated at the minimum rate of Rs. 1,400 per MT as fixed by the COT. The AO while completing the assessments between April 2007 and March 2008 also ignored the rate fixed by the COT. This resulted in non-detection of concealment of turnover of Rs. 54.96 crore and consequent evasion of tax of Rs. 2.74 crore. Besides, penalty of Rs. 5.48 crore was also leviable for the concealment of turnover.

After this was pointed out, the Government stated (January 2010) that the sales turnover was determined as per books of accounts of the concerned dealers and not on the estimated price fixed by the COT. The reply is not tenable as minimum turnover should have been determined based on the prevailing market price of Rs. 1400 per MT of coal as intimated by the COT.

## 2.6 Non-levy of tax and penalty on misuse of 'C' form

**Two companies purchased goods at concessional rate for use in manufacture of cement but utilised these for other purposes resulting in non-levy of tax of Rs. 63. 70 lakh and penalty of Rs. 1 crore**

Under the CST Act, a registered dealer may purchase goods from a registered dealer of another State at a concessional rate by utilising declaration in form 'C'. Further, if any person after purchasing the goods for any of the purposes specified in the declaration form fails to make use of the goods for any such purpose, he is liable to pay penalty not exceeding one and half times the amount of tax. It was judicially held[12] by the Supreme Court that the expression "in the manufacture of goods" should encompass the entire process carried out by the dealer for converting raw materials into finished goods.

**2.6.1** Scrutiny of the records of the ST, Jowai revealed (June 2008) that a company[13] engaged in the manufacture of cement, purchased motor spirit valued at Rs. 5.10 crore on 18 October 2006 from outside the state by utilising one declaration in form 'C' for use in manufacture/processing of goods for sale, but the company started commercial production from 11 May 2007 only. Thus, goods so purchased at concessional rate were not used in the manufacture of cement and

12 J.K. Cotton Spinning and Weaving Mills Co. Ltd. Vs. The STO Kanpur (1965) 16 STC.563 (SC)

13 Megha technical and Engineering Pvt. Ltd.

the company was liable to pay tax of Rs. 63.70 lakh. Besides, penalty not exceeding Rs. 95.55 lakh was also leviable for misuse of form 'C' but not levied.

**2.6.2** Another cement manufacturing company[14] registered under ST, Jowai imported motor cars, GC sheets, air conditioner, electronic goods, tent and accessories etc valued at Rs. 43.93 lakh between April 2002 and January 2008 at the concessional rate against declarations in form 'C' for use as raw material for the manufacture of cement. Since the goods so purchased at the concessional rate could not be used as raw material for manufacture of cement, the company was liable to pay penalty upto Rs. 4.93 lakh for misuse of 'C' forms which was, however, not levied and realised by the AO.

After this was pointed out, the Government stated (January 2010) that the AO had been asked to re-examine the cases for imposition of penalty. Further report is awaited (February 2010).

## 2.7 Evasion of tax by furnishing false returns

**Four registered dealers concealed turnover of Rs. 5.32 crore in their returns and evaded tax of Rs. 41.78 lakh on which penalty of Rs. 83.56 lakh was also leviable**

Under the MVAT Act, if any dealer furnishes a false return of turnover, he shall be liable to pay, in addition to the tax, a penalty not exceeding Rs. 5,000 or double the amount of tax payable on the sale turnover, whichever is greater. The provision of the Act applies *mutatis mutandis* in case of assessment and reassessment under the CST Act. Further, sale of declared goods in the course of interstate trade is taxable at the concessional rate of four *per cent* upto 31 March 2007 if such sale is supported by declaration in form 'C', otherwise such sale is taxable at the rate of eight *per cent*.

Scrutiny of the records of the ST, Jaintia Hills District, Jowai revealed (June 2008) that four dealers sold coal valued at Rs. 3.43 crore to the dealers of Guwahati, West Bengal, Rajasthan during April 2005 to March 2007. The turnover was supported by declarations in form 'C' and the dealers were assessed between November 2005 and June 2007 at a concessional rate of four *per cent.* Further, scrutiny of the records revealed that these dealers had also sold 34,817 MT of coal valued at Rs. 5.32 crore which was dispatched through Umkiang check gate located at the exit point of Meghalaya on the road connecting states like Assam (southern part), Manipur, Mizoram and Tripura during the aforesaid period. Although the records of despatch of coal were forwarded to the AO by the officer incharge of taxation check gate, the AO did not include the turnover while finalising the assessments. Thus, failure of the AO to ensure proper assessment by verifying all the concerned records available with him led to evasion of tax of Rs. 41.78 lakh. Besides, penalty of Rs. 83.56 lakh was also leviable for concealment of turnover.

[14] Hill Cement Ltd.

After this was pointed out, the Government stated (January 2010) that notices had been issued to the dealers for reopening the cases. Report on reassessment and recovery of tax is awaited (February 2010).

## 2.8 Evasion of tax by utilising fake declaration forms

**Five dealers utilised fake 'C' forms and evaded tax of Rs. 19.21 lakh on which penalty of Rs. 38.42 lakh was also leviable**

Under the CST Act, on interstate sale of goods which are covered by a valid declaration in form 'C', tax is leviable at a concessional rate of four *per cent.* In case of the declared goods, if not covered by a valid declaration in form 'C', tax is leviable at the rate of eight *per cent*. Further, under the MVAT Act, if any dealer evades in any way the liability to pay tax, he shall be liable to pay, by way of composition of offence, a sum not exceeding Rs. 5,000 or double the amount of tax, whichever is greater. In Meghalaya, coal is taxable at the rate of four *per cent*.

Scrutiny of the records of the ST, Jowai revealed (June 2008) that five dealers sold coal in the course of interstate trade valued at Rs. 4.80 crore to a dealer of Kolkata in West Bengal between January and March 2007 and produced eight declarations in form 'C' issued by the purchasing dealer. The AO also accepted the declaration forms and assessed the dealers accordingly on different dates between May 2007 and June 2007. Verification of the records of the Commissioner of Commercial Taxes, West Bengal revealed that the dealer who issued the form was neither registered nor was any declaration form issued to him. Thus, the declaration forms submitted by the dealers of Meghalaya were fake and tax should have been levied at the rate of eight *per cent* instead of four *per cent.* This resulted in evasion of tax of Rs. 19.21 lakh. In addition, penalty of Rs. 38.42 lakh was also leviable for deliberate submission of fake 'C' forms.

After this was pointed out, the Government stated (January 2010) that the case had been taken up with the Taxation Department of West Bengal. Fact however remains that the reply of the Taxation Department of West Bengal is available with the audit which could have been obtained and the assessments revised in the interest of revenue.

## 2.9 Short levy of tax due to misclassification of goods

**Levy of tax at the rate of eight *per cent* against the leviable rate of twelve *per cent* on the turnover of Rs. 1.33 crore led to short levy of tax of Rs. 4.91 lakh and interest of Rs. 3.70 lakh**

As per the schedule attached to the Meghalaya Finance (Sales Tax) Act, electronic goods were taxable at the rate of 12 *per cent* at the point of first sale in the State. Further, if any dealer fails to pay the full amount of tax by the due date, he shall be liable to pay the interest at the prescribed rate for the period of default

on the amount by which the tax paid falls short. It was held[15] by the Supreme Court of India that an item can be regarded as an electronic goods if its functions are controlled electronically by microprocessor.

Test check of the records of the ST, Circle II, Shillong revealed (April 2008) that a dealer sold vacuum cleaners and aquaguards (water purifiers) valued at Rs. 1.33 crore between April 2003 and April 2005. The AO assessed the dealer at the rate of eight *per cent* treating the goods as electrical goods. Since aquaguards and vacuum cleaners are operated through microchips or microprocessors, these goods should have been treated as electronic goods as per the aforesaid judgment of the apex court and taxed at rate of 12 *per cent*. Thus, application of incorrect rate due to the misclassification of the goods led to short levy of tax of Rs. 4.91 lakh. Besides, interest of Rs. 3.70 lakh was also leviable.

The case was reported to the department/Government in July 2008; their reply has not been received (February 2010).

## 2.10 Non-detection of fraudulent representation of fact resulting in evasion of tax

**A dealer purchased cement valued at Rs. 1.05 crore at concessional rate which was not included in the certificate of registration and evaded tax of Rs. 13.09 lakh. Beside penalty of Rs. 26.18 lakh was also leviable**

Under the MVAT Act, if any registered dealer falsely represents when purchasing any class of goods that goods of such class are covered by the certificate of registration, he shall be liable to pay, in addition to the tax recoverable under the Act, penalty not exceeding Rs. 5,000 or double the amount of tax which would have been payable on the sale turnover, whichever is greater.

Test check of the records of the ST, Circle I, Shillong revealed (April 2008) that a dealer disclosed purchase of onion and mineral water valued at Rs. 75,000 and Rs. 65,000 respectively at the concessional rate from outside the State by utilising two declarations in form 'C'. Cross verification of the assessment records of the selling dealer registered in Assam, however, revealed that the dealer of Meghalaya actually purchased cement valued at Rs. 1.05 crore between August and December 2006 by utilising those two 'C' forms. The dealer neither disclosed purchase and sale of cement in his returns nor was the item included in his certificate of registration. The dealer, thus, falsely represented while purchasing goods that cement was covered by his certificate of registration which strangely was not noticed by the AO. Thus, due to the concealment of the purchase of Rs. 1.05 crore by fraudulent method, the dealer evaded tax of Rs. 13.09 lakh. The tax effect would be even more if elements of profit could be ascertained. Besides, penalty of Rs. 26.18 lakh was also leviable. **The department also needs to investigate, fix responsibility and take appropriate administrative action for non-verification of such basic facts.**

15 BPL Limited Vs state of Andhra Pradesh 121 STC 450 (SC).

After this was pointed in July 2008, the COT while admitting the facts stated (September 2009) that the dealer was not traceable. The area IT was asked to conduct an inquiry and submit report on the whereabouts of the dealer. Further report has not been received (February 2010).

The cases were reported to the Government in July 2008; their reply has not been received (February 2010).

## 2.11 Turnover escaping assessment

**Tax of Rs. 26.75 lakh was underassessed due to escaping of turnover of Rs. 4.65 crore**

Under the Meghalaya Finance (Sales Tax) Act, if the COT is satisfied that the sale of any taxable goods has escaped the assessment in any period or has been underassessed, he may at any time within eight years of the end of the aforesaid period, serve on the dealer a notice and proceed to reassess the dealer accordingly.

**2.11.1** Test check of the records of the ST, Circle III, Shillong revealed (April 2008) that a dealer disclosed turnover of Rs. 20.42 lakh in his returns between April 2004 and March 2005 and was assessed in January 2006 accordingly. Scrutiny of the assessment records, however, revealed that the dealer actually sold goods valued at Rs. 1.02 crore[16] during the aforesaid period. Thus, turnover of Rs. 81.22 lakh escaped assessment resulting in underassessment of tax of Rs. 6.50 lakh.

**2.11.2** Test check of the records of the ST, Circle I, Shillong revealed (April 2008) that a dealer disclosed turnover of Rs. 8.48 crore in his returns between April 2004 and March 2005 and the AO assessed the dealer in September 2006 accordingly. However, scrutiny of the assessment records revealed that the dealer actually sold taxable goods valued at Rs. 11.71 crore[17]. Thus, turnover of Rs. 3.23 crore escaped assessment resulting in underassessment of tax of Rs. 12.94 lakh.

**2.11.3** Test check of the records of ST, Circle IV, Shillong revealed (April 2008) that a dealer disclosed turnover of Rs. 2.10 lakh in his return for the period between April 2002 and March 2004 and was assessed on different dates between December 2005 and April 2007. Further scrutiny, however, revealed that the dealer actually sold goods valued at Rs. 63.05 lakh[18]. Thus, turnover of

16

| Opening stock | + | Purchase | – | closing stock | = | Sale |
|---|---|---|---|---|---|---|
| Rs.3.16 lakh | + | Rs. 102.36 lakh | _ | Rs. 3.89 lakh | = | Rs. 101.63 lakh |

17

| Opening stock | + | Purchase | – | closing stock | = | Sale |
|---|---|---|---|---|---|---|
| Not recorded | + | Rs. 11.85 crore | _ | Rs. 14.08 lakh | = | Rs. 11.71 crore |

18

| Opening stock | + | Purchase | – | closing stock | = | Sale |
|---|---|---|---|---|---|---|
| Nil | + | Rs. 68.19 lakh | – | Rs. 5.14 lakh | = | Rs. 63.05 lakh |

Rs. 60.95 lakh escaped assessment resulting in underassessment of tax of Rs. 7.31 lakh.

After the cases were pointed out, the AO, Circle IV while admitting the facts stated (September 2009) that the assessment has been rectified and a demand notice issued to the dealer accordingly. Report on recovery of the assessed tax and the replies in respect of the dealers under Circle I and III have not been received (February 2010).

The cases were reported to the department/Government in July 2008; their reply has not been received (February 2010).

## 2.12 Loss of revenue due to delay in assessment

**Non-completion of assessment of a dealer on best judgment basis led to loss of revenue of Rs. 14.95 lakh**

Under the taxation laws of Meghalaya, if a dealer fails to submit the returns alongwith the payment of the admitted tax or after submission of returns, fails to produce the books of accounts despite notices, the AO shall complete the assessments on best judgment basis. It was judicially held[19] by the Supreme Court that the Superintendent of Taxes is bound to make assessment to the best of his judgment if the dealer fails to submit the return and produce the books of accounts.

Test check of the records of the ST, Circle I, Shillong revealed (April 2008) that registration certificates were granted to a dealer under both MF (ST) and CST Act with effect from 16 June 2003. The dealer imported taxable goods valued at Rs. 1.25 crore between December 2003 and March 2005, but neither submitted any return nor paid any tax. The AO did not initiate any action to complete the assessment on best judgment basis and recover the assessed tax. Further scrutiny, however, revealed that the dealer had closed down his business with effect from May 2005. Thus, failure of the AO to complete the assessments on best judgment basis had resulted in loss of revenue of Rs. 14.95 lakh.

After this was pointed out in July 2008, the COT while admitting the facts stated (August 2009) that the dealer could not be traced out inspite of best efforts. While indicating lack of control and poor surveillance on the part of the department, the reply was silent about the reasons for non-initiating best judgment assessments of the dealer. Besides, no further action was initiated to send the case to the *bakijai*[20] officer to recover the amount as arrears of land revenue.

The cases were reported to the Government in July 2008; their reply has not been received (February 2010).

## 2.13 Loss of revenue due to the failure to levy tax on closing stock

19 CIT Vs Segu Buchiah Setty (1970) 77 ITR 539 SC.

20 Recovery officer.

**The AO failed to levy tax on the closing stock of a dealer at the time of closure which led to the loss of revenue of Rs. 3.01 lakh**

Under the taxation laws of Meghalaya, every dealer is liable to pay tax on the stock of goods remaining unsold at the time of closure of his business.

Test check of the records of the ST, Circle I, Shillong revealed (April 2008) that a dealer was assessed to tax upto 31 March 2004 on the basis of the returns furnished. Thereafter, the dealer neither furnished any return nor was he assessed by the AO on best judgment basis. The dealer, however, closed down his business on 31 March 2005 leaving stock of goods valued at Rs. 30.70 lakh remaining unsold at the time of closure of his business. Though the dealer was liable to pay tax on the closing stock, the AO did not initiate any action to assess him and realise the assessed tax. Thus, failure of the ST to levy tax on closing stock led to loss of revenue of Rs. 3.01 lakh.

After this was pointed out in April 2008, the AO while admitting the facts stated (September 2009) that the dealer had been assessed and the case referred to the *bakijai* officer for recovery of the assessed tax as an arrears of land revenue. Report on recovery of tax has not been received (January 2010).

The cases were reported to the Government in April 2008; their reply has not been received (February 2010).

## 2.14 Loss of revenue due to irregular grant of authorisation certificate

**Irregular grant of authorisation certificate led to undue exemption of Rs. 15.22 lakh**

Under the Meghalaya Industries (Sales Tax Exemption) Scheme, 2001 notified under the Industrial Policy 1997, new units established on or after 15 August 1997 will be eligible for the sales tax exemption on the sale of finished products manufactured by such units provided that a tax exemption certificate in the form of a certificate of authorisation (CA) is granted to these units by the AO. Before granting the CA, the AO shall satisfy himself that every information furnished by the applicant is factually correct and based on the information contained in the eligibility certificate (EC) granted to the units by the Industries Department.

Test check of the assessment records of the ST, Circle III, Shillong revealed (April 2008) that a manufacturer was granted an EC for manufacturing grills, rolling shutters, almirahs, doors and windows and other fabricated metal products. The AO while granting the CA, however, included an additional item "steel poles" which was not in the EC. The dealer sold steel tubular poles valued at Rs. 3.80 crore between April 2004 and April 2005 and was exempted from the payment of tax based on the CA issued to him. This irregular grant of CA led to undue exemption of tax of Rs. 15.22 lakh.

After this was pointed out, the AO stated (August 2008) that the item steel tubular poles was covered by other items of EC. The reply is not tenable as steel tubular

poles are manufactured as per the specifications of Bureau of Indian Standards and, therefore, cannot be classified under other fabricated metal products.

The case was reported to the Government in July 2008; their reply has not been received (February 2010).

## 2.15 Non-forfeiture of tax

**Non-forfeiture of tax of Rs. 33.20 lakh irregularly collected on exempted goods**

Under the sales tax laws of Meghalaya, if any dealer collects any sum by way of tax in respect of the sale of any goods on which no tax is payable, the tax so collected shall be forfeited to the Government. Further, clause 4 (iii) of the Meghalaya Industries (Sales Tax Exemption) Scheme, 2001 provides for total exemption on the sale of the finished products within the State.

Test check of the records of the ST, Circle III, Shillong revealed (April 2008) that a manufacturing unit which was exempted from sales tax under the Industrial Scheme of 2001 sold finished goods valued at Rs. 4.57 crore between April 2003 and March 2004 and collected tax of Rs. 33.20 lakh on the sale of such exempted goods. The AO, however, did not forfeit the tax of Rs. 33.20 lakh so collected. Thus, inaction on the part of the AO resulted in non-forfeiture of tax of Rs. 33.20 lakh.

After this was pointed out, the ST stated (August 2008) that the dealer did not charge any tax on the aforesaid turnover and as such sales made by the dealer was in accordance with the provision of the Meghalaya industrial policy scheme, 2001. The reply is not tenable as the records revealed that the turnover of sales made was inclusive of the element of tax.

The case was reported to the Government in July 2008; their reply has not been received (February 2010).

## 2.16 Irregular grant of exemption under the CST Act

**Interstate sale of Rs. 69.88 crore not supported by declaration form was irregularly exempted resulting in non-levy of tax of Rs. 8.39 crore and interest of Rs. 6.92 crore**

Under Sections 8 (4) and (5) of the CST Act as amended in May 2002, the State government is empowered to issue notification granting exemption to the eligible industrial units from payment of tax in respect of those interstate sales which are supported by declarations in form 'C' or 'D' as the case may be. If interstate sales made by the exempted units are not supported by declarations in form 'C' or 'D', such units are liable to pay tax at 10 *per cent* or the local rate of tax, whichever is higher. Further, under the provisions of the Meghalaya Sales Tax Act, if any dealer fails to pay the full amount of the admitted tax within the due date(s), he is liable to pay interest at the prescribed rate for the period of default, on the amount by which tax paid falls short.

Scrutiny of the records of the ST, Ri-Bhoi District, Nongpoh revealed (July 2008) that two manufacturing units sold goods valued at Rs. 69.88 crore in course of the interstate trade between April 2003 and September 2005 without being supported by the declarations in form 'C' and 'D'. The units claimed exemption from the payment of tax as per the Industries (Sales Tax Exemption) Scheme, 2001 issued under section 8 (5) of the CST Act. The AO, while finalising the assessments between March and May 2007 admitted the claims and assessed the manufacturing units accordingly. The grant of exemption to the manufacturers was irregular as the sales were not supported by declarations in form 'C' and 'D' resulting in underassessment of tax of Rs. 8.39 crore. Besides, interest of Rs. 6.92 crore was also leviable.

After the cases were pointed out, the AO stated (September 2008) that the exemption from the payment of tax was granted as per the Government notification dated 12 April 2001. The reply is not tenable as the exemption was subject to production of form 'C' or 'D' in support of the interstate sales.

The cases were reported to the Government in August 2008; their reply has not been received (February 2010).

## 2.17 Underassessment of tax due to acceptance of invalid 'C' forms

**Acceptance of invalid declaration forms covering transaction of Rs. 1.58 crore led to underassessment of tax of Rs. 19.80 lakh**

Under the CST Act, every dealer who in the course of interstate trade sells to a registered dealer shall be liable to pay tax at the concessional rate of four *per cent* provided the selling dealer furnishes to the prescribed authority in the prescribed manner a declaration in form 'C'.

Scrutiny of the records of the ST, Ri-Bhoi District, Nongpoh revealed (July 2008) that a manufacturer of water filter and spare parts sold goods valued at Rs. 20.35 crore between April 2005 and March 2006 in the course of interstate trade duly supported by declarations in form 'C'. The dealer claimed exemption from the payment of tax under the Meghalaya Industries (Sales Tax Exemption) Scheme 2001 and the AO assessed the dealer in January 2008 accordingly. Further scrutiny of the 'C' forms, however, revealed that three 'C' forms covering Rs. 1.58 crore issued by a dealer of Mumbai were not in prescribed form as provided under the CST Act. But the AO accepted the invalid forms resulting in underassessment of tax of Rs. 19.80 lakh.

After this was pointed out, the ST stated (March 2009) that the 'C' forms were in the prescribed format. The reply is not tenable as the aforesaid declarations were not in prescribed form as provided under Rule 12(1) of the CST (Registration and Turnover) Rules, 1957.

The cases were reported to the Government in August 2008; their reply has not been received (February 2010).

## 2.18 Underassessment of tax due to incorrect application of rate

**Application of incorrect rate of tax under the CST Act led to underassessment of tax of Rs. 7.60 lakh**

Under the CST Act, on interstate sale of goods not supported by declaration in form 'C', tax shall be calculated at the rate of 10 *per cent* or at the rate applicable to the sale or purchase of such goods inside the State, whichever is higher. However, in the case of declared goods, tax shall be calculated at twice the rate applicable to the sale or purchase of such goods inside the State. In Meghalaya, 'iron and steel' and 'bitumen emulsion' are taxable at four *per cent* and 12.5 *per cent* respectively.

Scrutiny of the records of the ST, Ri-Bhoi District, Nongpoh revealed (July 2007) that a manufacturer of steel sheet disclosed sale of Rs. 1.38 crore between April and September 2005 in course of the interstate trade. Though the dealer failed to furnish 'C' forms in support of sales, the AO assessed (February 2007) the dealer incorrectly levying tax at four *per cent* instead of eight *per cent*. Thus, incorrect application of rate by the AO led to underassessment of tax of Rs. 5.52 lakh.

Another manufacturer registered in ST, Nongpoh sold bitumen emulsion valued at Rs. 24.52 lakh between April and September 2005 in the course of interstate trade but failed to furnish 'C' forms in support of sales. The AO assessed the dealer incorrectly at 4 *per cent* instead of 12.5 *per cent* resulting in underassessment tax of Rs. 2.08 lakh.

After the cases were pointed out, the AO while admitting the facts stated (March 2009) that both the dealers had been reassessed and fresh demand notices had been issued. Report on recovery of tax has not been received (January 2010).

The cases were reported to the Government in August 2008; their reply has not been received (February 2010).

## 2.19 Loss of revenue due to irregular cancellation of the registration certificate

**Cancellation of the registration certificate without surrendering the unused declarations led to loss of revenue of Rs. 92.58 lakh**

Under the CST Act and Rules made thereunder, unused declaration forms remaining in stock with a registered dealer at the time of cancellation of his registration certificate shall be surrendered to the ST. Further, if any dealer evades the payment of tax wilfully or conceals his liability to pay the tax, the COT may accept by way of composition of such offence, a sum not exceeding Rs. 1,000 or double the amount of tax, whichever is greater.

Scrutiny of the records of the ST, West Garo Hills, Tura revealed (November 2008) that a cement dealer disclosed turnover of goods valued at Rs. 13.51 lakh between October 2002 and March 2003 and the AO assessed the dealer in April 2003 accordingly. As prayed by the dealer, the AO also cancelled the registration certificates of the dealer under the Meghalaya Finance Sales Tax and the CST Act with effect from April 2003 without obtaining the unused declaration forms

issued to the dealer. Cross verification of the records of a dealer registered in Guwahati (Assam), however, revealed that the dealer imported cement valued at Rs. 2.57 crore between April and September 2003 by utilising two declaration forms. The dealer thus evaded tax of atleast Rs. 30.86 lakh on the aforesaid turnover. Besides, penalty of Rs. 61.72 lakh was also leviable. Thus, due to the irregular cancellation of the registration certificate by the AO, there was loss of revenue of Rs. 92.58 lakh.

After this was pointed out, the ST while admitting the facts stated (March 2009) that the dealer had been asked to produce the books of accounts for verification. The reply was silent regarding the omission to collect the unused declaration forms at the time of cancellation of RC which was fraught with the risk of misuse and ultimately led to loss of revenue. Further reply has not been received (January 2010).

The cases were reported to the department/Government in January 2009; their reply has not been received (February 2010).

## 2.20 Short levy of tax due to irregular assessment at the concessional rate

**Irregular assessment at the concessional rate on sales of Rs. 4.22 crore supported by invalid 'C' form led to underassessment of tax of Rs. 6.19 lakh**

Under the CST Act, every registered dealer who sells goods in the course of interstate trade to another registered dealer shall pay tax at the concessional rate of three *per cent* upto 31 May 2008 and two *per cent* thereafter, provided the selling dealer furnishes declarations in form 'C' in support of sales; otherwise tax is leviable at the rate applicable to the sale or purchase of such goods inside the State. In Meghalaya, coal is taxable at the rate of four *per cent*.

Scrutiny of the records of the ST, West Garo Hills, Tura revealed (November 2008) that two dealers sold coal valued at Rs. 4.22 crore in course of interstate trade to a dealer of Rajasthan between January 2008 and June 2008 and furnished two declarations in form 'C' in support of the aforesaid sales. The AO accepted the 'C' forms and assessed the dealers between May and August 2008 at the concessional rate of three *per cent* upto 31 May 2008 and two *per cent* thereafter. Further scrutiny of the 'C' forms, however, revealed that the forms were issued to the dealer of Rajasthan on 22 July 1996 by the Taxation Department of Rajasthan whereas he was registered with effect from 12 April 1997. Since the declaration forms were issued to the dealer before the date of liability, the forms were invalid and liable for rejection. Thus, irregular assessment at the concessional rate on the sales supported by the invalid declaration forms had resulted in underassessment of tax of Rs. 6.19 lakh.

After the cases were pointed out, the ST while admitting the facts stated (March 2009) that both the dealers had been reassessed. Recovery particulars of the assessed tax have not been received (January 2010).

The cases were reported to the department/Government in January 2009; their reply has not been received (February 2010).

## 2.21 Non-levy of interest

**For default in payment of tax, interest of Rs. 24.83 lakh though leviable was not levied**

Under the MVAT Act, if any dealer fails to pay the admitted tax on the due date, simple interest at the rate of two *per cent* per month from the first day of the following month will be leviable.

Scrutiny of the records of the ST, Nongpoh revealed (July 2008) that a dealer was assessed to tax of Rs. 80.97 lakh in June 2007 for the period from September 2005 to March 2006. The dealer, however, had not paid the entire amount of tax of Rs. 80.97 lakh till the date of audit. For non-payment of the tax, interest of Rs. 24.83 lakh was leviable but was not levied by the AO.

After the case was pointed out, the ST while admitting the facts stated (April 2009) that the assessment for the aforesaid period had been rectified, interest had been levied and a notice of demand issued to the dealer for payment. A report on recovery has not been received (January 2010).

The cases were reported to the Government in August 2008; their reply has not been received (February 2010).

## 2.22 Non-levy of tax due to non-completion of the assessment

**Delay in completion of the assessment led to non-payment of tax of Rs. 13.73 lakh including interest**

Under the Meghalaya Finance (Sales Tax) Act, every dealer was required to submit a return alongwith the payment of the admitted tax within 30 days of the close of each six monthly period. If a dealer failed to submit returns or after submission of the returns, failed to produce the books of accounts despite notices, the AO was to complete the assessments on best judgment basis.

Test check of the records of the ST, Nongpoh revealed (July 2008) that a manufacturer of black wire, GI wire etc., imported raw material valued at Rs. 85.01 lakh between October 2003 and September 2004 but the dealer neither filed any return nor paid any tax. The AO did not initiate any action either to issue notice for submission of the return or to assess the dealer on best judgment basis. Cross verification of the records of the Registrar of Companies, Shillong, however, revealed that the dealer had sold finished goods valued at Rs. 49.94 lakh and Rs. 58.81 lakh under the MFST and CST Act respectively between April 2003 and March 2004. Thus, failure of the AO to initiate timely action to assess

the dealer on best judgment basis led to non-levy of tax of Rs. 6.70 lakh. Besides, interest of Rs. 7.03 was also leviable.

After this was pointed out, the Government stated (January 2010) that the assessment had been completed on best judgment basis and a demand notice had been issued for the payment of tax and interest. A report on recovery has not been received (February 2010).

## 2.23 Irregular rectification of assessments

**Irregular rectification of assessment led to underassessment of tax of Rs. 5 lakh**

Under the Meghalaya (Sales of Petroleum etc.) Taxation Act, the authority which made an assessment may at any time within three years from the date of such assessment, rectify any such mistake apparent from the records of the case and shall within the like period rectify any such mistake as has been brought to the notice by the dealer.

Scrutiny of the records of the ST, Circle 1, Shillong revealed (January 2009) that a dealer was assessed in April 2004 for the period from April 2001 to December 2001 on the basis of the returns and the books of accounts produced and tax of Rs. 2.59 crore was assessed and realised from the dealer. However, in January 2008, the dealer prayed for rectification of some mistake which were apparent from the records and the assessment for the aforesaid periods were rectified in February 2008 and tax of Rs. 2.54 crore was assessed. Since rectification was carried out after a lapse of more than three years, such rectification was irregular and contrary to the provisions of the Act. The irregular rectification had resulted in underassessment of tax of Rs. 5 lakh.

After this was pointed out in March 2009, the Government, while admitting the facts stated (January 2010) that rectification of assessment proceedings for the aforesaid period would be completed. Further report regarding rectification and recovery of tax is awaited (February 2010).

## 2.24 Irregular grant of exemption

**Irregular grant of authorisation certificate led to irregular grant of exemption of Rs. 32.01 lakh**

Under Section 2(i) of the Meghalaya Industries (Sales Tax Exemption) Scheme, 2001 notified under the Industries Policy 1997, new industries set up on or after 15 August 1997 will be eligible for sales tax exemption on the sale of the finished products manufactured by such units provided that the tax exemption certificate in the form of certificate of authorisation (CA)[21] is granted by the Taxation Department. Further, manufacturing of cement[22] consists of preparation of raw

[21] To be issued on the basis of the eligibility certificate issued by the Industries Department.

[22] Clinker Ultratech Cement Limited Vs Principal Secretaries, Department of Industries and Commerce and other (2008) II VST 881 (kara).

mix, production of clinker[23], grinding of clinker in a factory and blending of ground cement with silica.

Scrutiny of the records of the ST, Circle III, Shillong revealed (January 2009) that a manufacturer of cement, sold clinker valued at Rs. 2.56 crore between April 2007 and March 2008 and claimed exemption from the payment of tax under the Industrial Policy 1997 and the dealer was exempted from the payment of tax. Since clinker is not a finished product, it was not eligible for the exemption under the Industrial Exemption Scheme. While issuing the CA, the AO, however, granted exemption from the payment of tax on the sale of cement as well as clinker. Thus, erroneous inclusion of clinker in the CA resulted in irregular grant of exemption of Rs. 32.01 lakh.

After this was pointed out, the Government stated (January 2010) that the item 'clinker' was not included in his certificate of registration through oversight, which would be amended accordingly. The reply is not tenable as the amendment in the certificate of registration cannot be made retrospectively and also the eligibility certificate issued by the Industries Department covered exemption on sale of cement only. Further reply has not been received (February 2010).

## 2.25 Incorrect deduction of turnover

**Incorrect deduction of taxable turnover of Rs. 2.35 crore led to short levy of tax of Rs. 18.80 lakh**

Schedule II of Meghalaya Sales Tax Act stipulated that the sales turnover of food or other articles or any drinks whether or not intoxicating served for consumption in any eating house, restaurant, or hotel was taxable at the rate of eight *per cent*.

Scrutiny of the records of the ST, Circle II, Shillong revealed (January 2009) that the proprietor of a restaurant disclosed sale turnover of Rs. 3.53 crore for different period between April 2001 and April 2005 and claimed deduction of Rs. 2.35 crore being sale of non-taxable goods and the AO assessed the dealer in March 2008 accordingly. Since the turnover of a restaurant consists of only the proceeds of sale of food items and drinks consumed, the exemption granted was irregular. This resulted in underassessment of tax of Rs. 18.80 lakh.

After this was pointed out, the Government stated (January 2010) that non-taxable items like milk, curd, *lassi* consumed in the restaurant were exempted from the payment of tax. The reply is not tenable as any food or drinks consumed in a restaurant were taxable as per the aforesaid schedule. Further reply has not been received (February 2010).

[23] Lime stone, clay, bauxite and iron ore sand in specific proportions when heated in a rotating kiln at 2770 degree fahrenheit, they begin to form cinder lumps known as clinker.