

CHAPTER-II Sales Tax/Value Added Tax

2.1 Tax administration

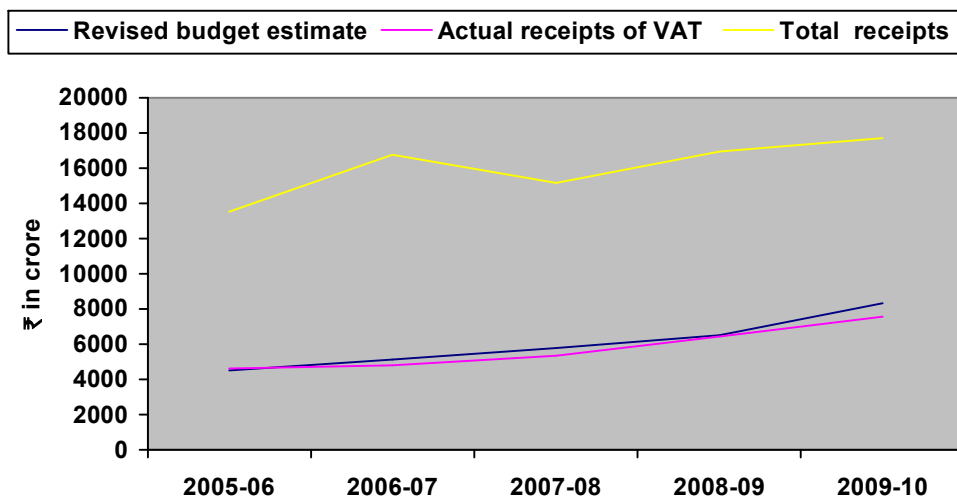
The Financial Commissioner, Taxation and Principal Secretary to the Government of Punjab is overall incharge of the Excise and Taxation Department. Subject to the overall control and superintendence of the Excise and Taxation Commissioner (ETC), the administration of the Punjab Value Added Tax Act, 2005 (PVAT Act)/Central Sales Tax Act (CST Act) is carried out by the Additional Excise and Taxation Commissioner (Addl. ETC), Joint Excise and Taxation Commissioners (JETCs) at the headquarters, Deputy Excise and Taxation Commissioners (DETCs) at the divisional level and Assistant Excise and Taxation Commissioners (AETCs), Excise and Taxation Officers (ETOs) and other allied staff at the district level. The authorities performing duties within their jurisdictions as specified by the Government under the Punjab Value Added Tax Act are called as Designated Officers (DOs).

2.2 Trend of receipts

The actual receipts from Sales Tax/Value Added Tax (VAT) during the last five years from 2005-06 to 2009-10 along with the total tax receipts during the same period is exhibited in the following table and graph.

(₹ in crore)

Year	Revised budget estimates	Actual receipts	Variation excess (+)/shortfall (-)	Percentage of variation	Total tax and non-tax receipts of the State	Percentage of actual VAT receipts to the total receipts
2005-06	4,500.00	4,626.88	(+) 126.88	(+) 2.82	13,525.71	34.21
2006-07	5,125.00	4,829.02	(-) 295.98	(-) 5.78	16,761.74	28.81
2007-08	5,778.00	5,342.49	(-) 435.51	(-) 7.54	15,153.14	35.26
2008-09	6,529.62	6,435.63	(-) 93.99	(-) 1.44	16,934.10	38.00
2009-10	8,320.00	7,577.49	(-) 742.51	(-) 8.92	17,692.18	42.83



The actual receipts of VAT increased from 4626.88 to 7577.49 during the period 2005-06 to 2009-10 an increase of 64 per cent.

It may be seen that variations between budget estimates and actual receipts ranged between (-) 8.92 per cent and 2.82 per cent.

2.3 Analysis of the arrears of revenue

The pre VAT and post VAT position of arrears of revenue on account of non-recovery of sales tax/value added tax during the year 2001-02 to 2009-10 is as under:-

(₹ in crore)

Pre VAT			Post VAT			
Year	Arrears during the year	Cumulative arrears	Year	Arrear		Cumulative arrears
				Addition	Clearance	
2001-02	--	262.57	2005-06	145.26	--	760.91
2002-03	172.95	435.52	2006-07	786.93	--	1,547.84
2003-04	30.65	466.17	2007-08	486.78	--	2,034.62
2004-05	149.48	615.65	2008-09	--	1,174.52	860.10
			2009-10	--	484.12	375.98

The above table shows that the arrears of tax due under the pre VAT period ending March 2005 was ₹ 615.65 crore, which was reduced to ₹ 375.98 crore in the post VAT period ending March 2010. Out of ₹ 375.98 crore, ₹ 169.09 crore were outstanding for more than five years. The Department had made explicit provisions in the PVAT Act to recover the arrears of tax due under the repealed Act. The details of clearance of arrears of ₹ 1,174.52 crore during the year 2008-09 and ₹ 484.12 crore during 2009-10 were called for, but reply was not received (October 2010).

2.4 Assessee profile

The number of dealers registered during the year showing separately the large taxpayers and small dealers, number of dealers required to file returns, number of returns received etc. are mentioned below:

Total no. of dealers registered upto 31 March 2009	No. of dealers registered during the year 2009-10	Large tax payers during the year 2009-10	Small dealers during the year 2009-10	No. of dealers required to file returns during the year 2009-10	No. of returns received during the year 2009-10	No. of returns not received by the Department during the year 2009-10	No. of notices issued to the dealers who failed to furnish returns during the year 2009-10
1,81,940	11,514	149	1,93,305	1,93,454	1,85,941	7,513	7,513

2.5 Arrears in assessment

The number of cases pending for assessment at the beginning of the year, becoming due during the year, disposed during the year and pending at the end of each year during 2005-06 to 2009-10 as furnished by the Department in respect of sales tax are mentioned below:

Year	Opening balance	Cases which became due for assessment	Total	Cases disposed during the year	Cases pending at the end of the year
2005-06	2,95,968	1,46,121	4,42,089	1,58,593	2,83,496
2006-07	2,83,496	1,62,447	4,45,943	87,560	3,58,383
2007-08	3,58,383	----	3,58,383	30,460	3,27,923
2008-09	80,650	----	80,650	27,623	53,027
2009-10	53,027	----	53,027	12,968	40,059

The closing balance of 2007-08 includes 2,47,273 cases pertaining to VAT and there is no provision for regular assessment under the PVAT Act 2005. Thus, the opening balance of 2008-09 and thereafter depicts the sales tax cases only. The Department needs to complete the pending assessment cases pertaining to pre-VAT period in a time bound manner. As of 1 April 2009, 53,027 assessment cases had become time barred. An illustrative case of loss due to failure to complete the assessment in time is discussed in paragraph 2.10.9.

2.6 Cost of collection

The gross collection in respect of sales tax/value added tax, expenditure incurred on their collection and the percentage of such expenditure to the gross collection during the years 2005-06 to 2009-10 alongwith the relevant all India average percentage of expenditure on collection are mentioned below:

(₹ in crore)

Head of revenue	Year	Gross collection	Expenditure on collection	Percentage of expenditure to gross collection	All India average percentage of expenditure to collection
Taxes on sales, trade etc./VAT	2005-06	4,626.88	49.06	1.06	0.91
	2006-07	4,829.02	41.78	0.87	0.82
	2007-08	5,342.49	45.81	0.86	0.83
	2008-09	6,435.63	48.53	0.75	0.88
	2009-10	7,577.49	59.83	0.79	-

The increase in cost of collection in 2009-10 was due to implementation of the pay commission's recommendations. However, the percentage of expenditure to the gross collection in the State was lower than the All India average since 2008-09.

2.7 Analysis of collection

The breakup of the total collection at pre-assessment stage and after regular assessment of VAT/sales tax, for the year 2009-10 and the corresponding figures for the preceding four years as furnished by the Department is mentioned below:

(₹ in crore)

Head of revenue	Year	Amount collected at pre-assessment stage	Amount collected after regular assessment	Penalty for delay in payment of taxes and duties	Amount refunded	Net collection as per the Department	Net collection as per the Finance Account	Percentage of column 3 to 8
1	2	3	4	5	6	7	8	9
Taxes on sales, trade etc./VAT	2005-06	4,603.05	46.83	5.68	37.15	4,618.41	4,626.88	99.48
	2006-07	4,967.60	37.08	3.25	220.05	4,787.88	4,829.02	102.87
	2007-08	6,128.94	49.04	14.15	320.84	5,871.29	5,342.49	114.72
	2008-09	7,397.86	14.67	4.27	373.80	7,043.00	6,435.63	114.95
	2009-10	8,634.88	20.76	4.15	375.66	8,284.13	7,577.49	113.95
	Total		168.38	36.50	1333.50	30,611.71	28,819.51	

We observed that:

- the percentage of tax collected (at pre assessment stage/at the time of filing of returns) before regular assessment has been increasing from the year 2005-06 to 2008-09 when it reached 114.95 *per cent* of the total net collection. However, it declined to 113.95 percent during 2009-10. The Department collected ₹ 168.38 crore after regular assessment conducted during the years 2005-06 to 2009-10 which proved that assessments were not being conducted properly as commented in paragraph 2.10.9.
- the tax due in the cases detected during test check of selective cases conducted by Audit during the period from 2005-06 to 2009-10 amounted to ₹ 314.54 crore, which is almost two fold higher than the amount collected by the Department after regular assessment. The high amount of leakage of revenue detected by Audit only in test checked cases vis-a-vis the amount collected after regular assessment, points towards a need for the Government to strengthen the tax administration.

- the refunds allowed during the years 2005-06 to 2009-10 also registered a consistent increase. It reached ₹ 375.66 crore in 2009-10 from ₹ 37.15 crore in 2005-06 which is almost ten times higher, whereas the amount collected after regular assessment during these years ranged between ₹ 14.67 crore to ₹ 49.04 crore.
- The net collection during the year 2009-10 as intimated by the Department was ₹ 8,284.13 crore whereas, it was ₹ 7,577.49 crore as per the Finance Accounts, which indicated that the Department was not reconciling the net collection with the office of the Accountant General (A&E) Punjab.

2.8 Impact of audit

Revenue impact

During the last five years, Audit through its audit reports had pointed out non/short levy, non/short realisation, underassessment/loss of revenue, incorrect exemption, concealment/suppression of turnover, application of incorrect rate of tax, incorrect computation etc., with revenue implication of ₹ 258.86 crore in 1,547 paragraphs. Of these, the Department/Government had accepted audit observations in 241 paragraphs involving ₹ 5.24 crore and recovered ₹ 3.18 crore in 227 cases. The details are shown in the following table:

(₹ in crore)

Year	Number of units audited	Amount objected		Amount accepted		Amount recovered	
		No. of cases	Amount	No. of cases	Amount	No. of cases	Amount
2004-05	228	382	23.40	60	0.71	60	0.71
2005-06	239	399	52.86	75	1.24	44	0.81
2006-07	242	241	14.08	29	0.88	31	0.61
2007-08	88	230	133.50	59	0.34	63	0.67
2008-09	138	295	35.02	18	2.07	29	0.38
Total	935	1547	258.86	241	5.24	227	3.18

2.9 Results of audit

Test check of the records of 87 units relating to sales tax/VAT during 2009-10 revealed underassessment of tax and other irregularities involving ₹ 55.55 crore in 157 cases which fall under the following categories:

(₹ in crore)

Sl. No.	Categories	No. of cases	Amount
1.	Performance audit of Transition from sales tax to Value Added Tax (A review)	1	20.82
2.	Loss of revenue due to excess refund of VAT	7	0.09
3.	Non/short levy of sales tax/VAT	64	16.40
4.	Incorrect grant of exemption from tax	4	0.51
5.	Non/short levy of penalty	6	4.31
6.	Other irregularities	75	13.42
Total		157	55.55

During the year 2009-10, the Department accepted audit observations involving ₹ 1.06 crore in four cases and recovered ₹ 3.68 crore in 148 cases pertaining to the audit findings of previous years.

A few illustrative audit observations involving ₹ 5.35 crore and a review on **Transition from sales tax to value added tax** with financial impact of ₹ 20.82 crore are discussed in the following paragraphs.

2.10 Performance Audit of Transition from Sales Tax to Value Added Tax

Highlights

- The VAT was introduced by the Punjab State Government w.e.f. 1st April 2005. The post VAT collection increased from ₹ 4626.88 crore to ₹ 7577.49 crore during the period 2005-06 to 2009-10 and the average growth rate during the period was 12.75 *per cent*. The number of registered dealers also increased from 1.46 lakh to 1.93 lakh.

(Paragraph 2.10.5)

- The shortages in manpower adversely affected the working of the Department in terms of shortfalls in scrutiny of returns and tax audits, an essential feature of the VAT system of levy.

(Paragraph 2.10.6.3)

- There was loss of revenue of ₹ 12.76 crore in time barred assessments under the Punjab General Sales Tax Act 1948.

(Paragraph 2.10.9)

- As a result of surveys conducted, 1937 dealers could be registered by the Department during the period 2005-06 to 2009-10, however two districts of Barnala and Patiala did not conduct any survey whereas negligible number of surveys were conducted in Ludhiana and Ropar district.

(Paragraph 2.10.10.3)

- Though 876 dealers in four districts had not filed quarterly returns, and 6654 dealers had not filed their annual statements, Department had not taken action under the Rules to initiate penal proceedings.

(Paragraph 2.10.11)

- It was seen that over the period 2005-06 to 2008-09, 10.98 lakh tax returns filed by the dealers were not scrutinised, non-scrutiny ranging from 70 to 100 percentage. Refunds allowed to the dealers were not pre-audit. Audit noticed omissions and irregularities in returns not scrutinised, resulting in short levy/payment of tax of ₹ 2.37 crore.

(Paragraph 2.10.11.2)

- Non-finalisation of the assessment as required in the Deferment & Exemption Rules saved under the Punjab Value Added Tax Act resulted in excess carry forward/availment of exemption of ₹ 1.47 crore.

(Paragraph 2.10.12)

- The PVAT Act/Rules prescribed for audit of returns by the Departmental Officer, to be carried out within a period of six years from the date of furnishing of returns. The State Government had neither finalised the parameters for audit of returns nor had they operationalised the module for Tax Audit in COVIS (October 2010).

(Paragraph 2.10.15)

- Internal audit of VAT returns was non-existent.

(Paragraph 2.10.18)

2.10.1 Introduction

The Empowered Committee of the State Finance Ministers in a conference held on 16 November 1999 issued a 'White Paper' for introduction of the VAT in India. Accordingly, the Committee unanimously decided in January 2002 to implement VAT. The white paper envisaged that after the introduction of VAT:

- ❖ the cascading effect of the existing taxation laws of the States would be eliminated due to credit of tax paid on purchase for resale or for use in manufacture;
- ❖ other taxes would be abolished and the overall tax burden would be rationalised. The Central Sales Tax (CST) would also be phased out;
- ❖ the overall tax would increase and there would be higher revenue growth; and
- ❖ there would be self assessment by the dealers and set off would be given for input and tax paid on previous purchases.

The Government of Punjab repealed the Punjab General Sales Tax Act (PGST Act), 1948 and enacted the Punjab Value Added Tax Act, 2005 (PVAT Act) for implementation of VAT with effect from 1 April 2005. Under the PGST Act, sales tax was levied at the last stage of sale except the goods notified for levy of tax at the first stage of sale in the State; whereas under the PVAT Act, VAT is levied at every stage of sale in the supply chain within the State and simultaneously, tax paid if any, at the earlier stages is allowed as input tax credit (ITC), by deduction from the tax payable at the subsequent stage.

2.10.1.2 Difference between PVAT and PGST

Some of the differences between the PVAT Act and the repealed PGST Act are as under:

- ❖ VAT is a multi-point taxation system, the repealed Act had a single point taxation system;
- ❖ The VAT system relies more on the dealers to pay tax willfully and submit self assessed returns whereas under the repealed Act, supporting documents were required to be produced along with the returns;
- ❖ The PVAT Act provides for tax audit of the dealers, but no norms have been fixed for assessment separately. Whereas under the repealed Act, hundred per cent of the returns were being assessed;
- ❖ The executives have a reduced control over the dealers under the VAT regime in comparison to the repealed Act; and
- ❖ Under the PGST Act, the goods were taxable under nine different tax groups i.e. one per cent, two per cent, three per cent, four per cent, eight per cent, 12 per cent, 20 per cent, 25 per cent and 30 per cent. In addition, surcharge at the rate of 10 per cent of the tax assessed was also

leviable on goods other than the declared goods. Under the PVAT Act, goods are taxable under six tax groups i.e. one *per cent*, four *per cent*, 8.8 *per cent*, 12.5 *per cent*, 20 *per cent* and 27.5 *per cent* and there is no provision for levy of surcharge.

With a view to assess the implementation of VAT, it was decided to review the transition from sales tax to value added tax. The review revealed a number of system and compliance deficiencies, which have been discussed in the subsequent paragraphs.

2.10.2 Audit objectives

The review was conducted to ascertain whether:

- the transition from sales tax to value added tax was effected in time and efficiently;
- the provisions of PVAT Act and Rules made thereunder were adequate and enforced effectively to safeguard the revenue of the State;
- there were lacunae in the provisions of the Act, the Rules and the procedures in safeguarding the revenue; and
- the internal control mechanism existed in the Department was adequate and effective to prevent the leakage of revenue.

2.10.3 Scope of audit

With a view to ascertain the effectiveness of transition from sales tax to value added tax, the records of two divisions¹ out of six divisions and nine districts² out of twenty four districts in the State were test checked covering the period from 2005-06 to 2009-10. In addition, records in the office of ETC Punjab, Patiala were also scrutinised. The review was conducted between April to June 2009, in April 2010 and some additional information were collected in July 2010. The divisions/districts were selected on the basis of revenue by adopting the probability proportion to size method. Filing and scrutiny of returns, tax audit and audit of assessment and monitoring of the refund cases were identified as risk areas for detailed scrutiny.

2.10.4 Acknowledgement

The Indian Audit and Accounts Department acknowledges the co-operation of the Excise and Taxation Department in providing necessary records and information to Audit.

2.10.5 Pre VAT and Post VAT collection

The comparative position of pre VAT sales tax collection (2001-02 to 2004-05) and post VAT (2005-06 to 2009-10) tax collection and the growth rate in each of the years is furnished in the table and chart below:-

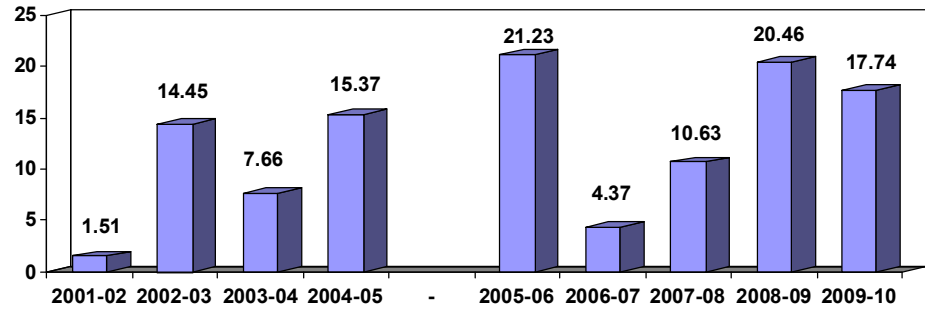
¹ Ludhiana and Patiala.

² AETCs Ludhiana I, II, III, Fatehgarh Sahib, Barnala, Mohali, Patiala, Ropar and Sangrur.

(₹ in crore)

Pre VAT			Post VAT		
Year	Actual collection	Percentage of growth	Year	Actual collection	Percentage of growth
2001-02	2,684.33	1.51	2005-06	4,626.88	21.23
2002-03	3,072.44	14.45	2006-07	4,829.02	4.37
2003-04	3,307.94	7.66	2007-08	5,342.49	10.63
2004-05	3,816.38	15.37	2008-09	6,435.63	20.46
			2009-10	7,577.49	17.74

Percentage of growth of revenue



(Pre VAT)

(Post VAT)

The average growth rate from 2001-02 to 2004-05 under the repealed Act was 10.54 per cent, whereas the average growth rate from 2005-06 to 2009-10 under the PVAT Act was 12.75 per cent. The year-wise details are given below:-

Year	Pre VAT	
	Actual collection (₹ in crore)	Number of registered dealers
2001-02	2,684.33	1,51,433
2002-03	3,072.44	1,43,297
2003-04	3,307.94	1,49,120
2004-05	3,816.38	1,49,621
Post VAT		
2005-06	4,626.88	1,46,121
2006-07	4,829.02	1,62,447
2007-08	5,342.49	1,68,267
2008-09	6,435.63	1,81,940
2009-10	7,577.49	1,93,454

The reasons for slow growth rate in 2006-07 were attributed by the Department (October 2009) to more refunds (₹ 200 crore) as compared to the refunds (₹ 80 crore) made in 2005-06. Increase in general rate of tax from 8.8 per cent to 12.5 per cent, conversion of many of the tax free items as taxable, imposition of tax on every point were some of the reasons attributed for the increase in revenue during the VAT regime.

2.10.6 Preparedness and transitional process

2.10.6.1 Planning for implementation of VAT in the State

With a view to have smooth implementation of VAT in the State, the Government initiated the process of registration of existing dealers by asking them to submit the fact sheet and copy of the original registration certificate pertaining to PGST as well as CST by 30 April 2003. If the dealer was found eligible for VAT registration, then VAT Registration Number (VRN) allocated by the Head Office was issued. Further, the Department brought out a 'Tax Payers Guide' for creating awareness of VAT in Punjab in March 2005. For easy understanding, a question and answer format in simple language was also used. Through this guide, the public and stakeholders were made aware that VAT is a new system of tax collection under which tax is charged at each stage of sale.

2.10.6.2 Training of staff

The Department had a Staff Training School at Patiala for imparting training to the staff. The Department published manuals for reference to the field officers for successful implementation of the VAT.

Test check of the data supplied by the Department in July 2010 regarding training to the staff revealed that 462 out of 730 officers/officials were trained between April 2005 and March 2010 for implementation of VAT. However, it was observed that the Department had not fixed any target for imparting training for implementation of VAT, as even after five years of introduction of VAT only 63 *per cent* of the officers/officials had been trained (March 2010).

2.10.6.3 Shortage of manpower

Manpower management is a key factor for smooth and efficient working of a Department and shortage of personnel impacts the output. The overall position of sanctioned strength³ vis-à-vis the vacancies in the cadres from Group A to Group C as furnished by the Department are given below:

Year wise/cadre wise sanctioned strength and men in position.					
Year	Cadre	Sanctioned strength	Men in position	Vacancies	Percentage of vacancies
2004-05	A	380	352	28	7.37
	B	11	9	2	18.18
	C	517	340	177	34.24
	Total	908	701	207	22.80
2005-06	A	406	339	67	16.50
	B	14	9	5	35.71
	C	530	343	187	35.28
	Total	950	691	259	27.26
2006-07	A	410	325	85	20.73
	B	14	14	0	0.00
	C	530	324	206	38.87
	Total	954	663	291	30.50

³ Does not include the ministerial staff deployed in the district offices.

2007-08	A	412	315	97	23.54
	B	14	14	0	0.00
	C	530	329	201	37.92
	Total	956	658	298	31.17
2008-09	A	412	286	126	30.58
	B	14	12	2	14.28
	C	530	354	176	33.21
	Total	956	652	304	31.79
2009-10	A	412	274	138	33.49
	B	75	52	23	30.66
	C	554	478	76	13.71
	Total	1,041	804	237	22.76

We observed that vacancies had adversely affected the working of the Department and there were shortfalls in scrutiny of returns and tax audit etc. as pointed out in the paragraphs 2.10.11.2 and 2.10.15.

Audit findings

The deficiencies in the transition from sales tax to VAT noticed during the review are discussed in the succeeding paragraphs.

2.10.7 Computerisation of Value Added Tax Information System (COVIS)

The Computerisation of Value Added Tax Information System was reviewed and a mention was made in the Audit Report (Revenue Receipts) of the Comptroller and Auditor General of India for the year ended 31 March 2008. The audit findings highlighted that the computerisation was undertaken with a view to enhance the efficiency of the organisation in implementing the PVAT Act and Rules made thereunder. It was expected that the COVIS system would assist in maximising the collection of taxes, duties and levies which the Department imposes and collects. However, the utility of the COVIS was restricted on account of non-implementation of all the modules and partial utilisation of rest of the implemented modules. The unreliable and inaccurate data in the system further hampered its utility in monitoring the defaulters and preventing the leakage in revenue. Lack of input and validation controls resulted in various irregularities such as acceptance of wrong entries of vehicle number, unreliable master data of dealers, unauthorised alteration of data etc. Besides, logical access controls for preventing unauthorised alteration of data were found weak. Due to incomplete, inaccurate and unreliable data in the system, no assurance could be derived from the functioning of the system in its present status of implementation. The monitoring by the Department was deficient to the extent that the COVIS was not being used for generation of the Management Information System (MIS) reports which was otherwise expected after implementation of the COVIS.

The Government may consider rectifying the deficiencies in the COVIS.

2.10.8 Deficiencies in the Act and the Rules

There are some lacunae in the provisions of PVAT Act and Rules, which were not redressed by the Department even after five years of implementation of the Act in the State. These are described below:-

The Deferment and Exemption Rules 1991, (D&E Rules) under the PVAT Act provides that an assessment of a unit in respect of which deferment or exemption certificate had been granted shall be made in accordance with the provisions of the PGST Act and the Rules made thereunder.

(a) The PGST Act has since been repealed, but instructions for assessment under the D&E Rules in the VAT regime have not been issued so far.

Section 19(5) of the PVAT Act provided that ITC, on goods specified in Schedule H and liable to purchase tax under the Act when sold in the course of inter state trade or commerce, shall be admissible only to the extent of tax chargeable under the CST Act.

(b) The State Government amended Section 19(5) of the PVAT Act in March 2008 for allowing ITC on purchase tax paid equal to CST chargeable on the products of goods specified in Schedule H. But the matter regarding allowance of credit of ITC on purchase tax payable prior to the issue of notification of March 2008 had remained without clarification.

In an illustrative case, we found that a dealer under the jurisdiction of AETC Mohali who had filed self assessment returns for the year 2006-07, had claimed and was allowed credit of ITC on the purchase of cotton corresponding to ISS of cotton yarn valued ₹ 8.74 crore at the rate of four *per cent* instead of two *per cent*. This resulted in excess allowance of ITC of ₹ 5.87 lakh due to deficiency in the above mentioned Rules during the period from April 2005 to March 2008.

2.10.9 Loss due to time barred assessments

AETC, Mohali

The Punjab General Sales Tax Act 1948 provides that the Assessing Authority shall after hearing such evidence as the dealer may produce and such other evidence as the Assessing Authority may require on specified points, pass an order of assessment within a period of three years from the last date prescribed for furnishing the last return in respect of any period.

We found that in the exercise of his powers under the Act *ibid*, the ETC Punjab, Patiala had granted (April 2008) extension in 1,464 cases pertaining to the assessment year 2004-05 upto 31 March 2009 for finalising the assessment. Aggrieved by this order, six dealers approached the VAT Tribunal, Punjab, which set aside the impugned order on the ground that:

- (i) the reasons given in the order for granting extension in the period of limitation that the dealers had not furnished C forms and other documents and thus, the assessment could not be completed in 1,464 pending cases, were not valid and acceptable; and
- (ii) the opportunity of being heard was not provided to the appellants.

When the assessment under the Act could have been completed within the time of limitation without waiting for the assesseees to produce C forms or other documents, why the Department waited so long till the assessment cases became time barred lacked justification. Consequent upon the 33 assessment cases wherein the demands for tax of ₹ 12.76 crore becoming time barred, the State suffered a loss of revenue of ₹ 12.76 crore. Though the Department was asked to clarify whether any appeal has been filed, no reply has been furnished (October 2010).

2.10.10 Registration and database of dealers

2.10.10.1 Registration of the dealers

As per the PVAT Act, any person who was registered before 1 April 2005 under the PGST Act, and continued to be so registered on the day immediately before the said day, is liable to pay tax under the PVAT Act. The DO shall, within thirty days of receipt of application in the prescribed form, issue a fresh registration for VAT or turnover tax (TOT) dealership, as the case may be.

We found that the dealers registered under the repealed Act had applied for registration under the PVAT Act and VAT or TOT registration numbers were issued to these dealers. However, the database of the dealers registered under the repealed Act vis-a-vis the dealers registered under the PVAT Act was not generated by the Department from the COVIS, even though separate modules for registration of dealers containing all the requisite information for the maintenance of database were available in the system.

The data of the dealers registered under the pre VAT and post VAT periods compiled by Audit on the basis of information collected from the Department is as under:-

Years	Number of assesseees	
	Pre VAT	Post VAT
2001-02	1,51,433	-
2002-03	1,43,297	-
2003-04	1,49,120	-
2004-05	1,49,621	-
2005-06	-	1,46,121
2006-07	-	1,62,447
2007-08	-	1,68,267
2008-09	-	1,81,940
2009-10	-	1,93,454

There was steady increase in the number of registered dealers in the VAT regime and it increased from 1,46,121 in 2005-06 to 1,93,454 in 2009-10.

2.10.10.2 Periodic analysis of dealers below the threshold limit

Under the PVAT Act, a dealer with turnover of more than ₹ five lakh but below ₹ 50 lakh is liable to be registered as Registered person and is liable to pay tax under this Act by way of turnover tax (TOT) at the rate of one *per cent* up to 7 June 2007 and at the rate 0.25 *per cent* thereafter on his taxable turnover. The dealer with turnover of ₹ 50 lakh or above is required to pay VAT at prescribed rates. Thus, it is important to keep a watch on the turnover of the TOT dealers at periodic intervals. Scrutiny revealed that eligibility for TOT liability (more than ₹ five lakh but below ₹ 50 lakh) and VAT liability (₹ 50 lakh and above) was ascertained solely on the basis of the returns and trading accounts submitted by the dealers. Thus, there is a need to undertake periodic scrutiny of the books of accounts of such dealers to assess and verify the threshold limits for the appropriate tax.

2.10.10.3 Survey to detect the unregistered dealers

The PVAT act provided that:

- ❖ No dealer who is liable to pay tax under the Act, shall carry on business as a dealer unless he has registered under the Act and has a certificate of registration.
- ❖ For identification of the persons, who are liable to pay tax but have remained unregistered, the Commissioner may order to conduct survey of such unregistered persons by issuing of notices to the persons to whom the unregistered dealer had made sale transactions and to the banks or financial institutions calling for the details and particulars of services rendered by them.

We noticed that 7,445 surveys were conducted by the Department in nine excise⁴ districts during the years from 2005-06 to 2008-09 and only 1,937 dealers were registered as a result of the surveys. We further observed that no survey was conducted by the AETCs, Barnala and Patiala during the aforesaid period, whereas negligible number (486) of surveys were conducted in two districts⁵ only during the year 2005-06.

⁴ Ludhiana-I, II, and III, Fatehgarh Sahib, Patiala, Sangrur, Ropar, Mohali and Barnala.

⁵ Ludhiana-I and Ropar.

2.10.10.4 Confirmation of securities

Under Section 25 of the PVAT Act 2005:

- ❖ Every person applying for registration shall furnish a security of ₹ 50,000 prescribed for securing proper and timely payments of tax payable by him.
- ❖ the security already furnished by a person registered under the PGST Act, 1948 shall be deemed to have been furnished under this Act, subject, however, to the confirmation from the sureties within a period of one year from the appointed day.

In the offices of three AETCs⁶, we observed that the securities in respect of 28,646 existing registered dealers were required to be confirmed by 31 March 2006 under the PVAT Act; out of this, 27,233 securities were confirmed within the prescribed/ extended period and 1,413 securities were still to be confirmed (April 2010).

2.10.10.5 Failure to obtain securities

The PVAT Rules, 2005 provide that the security or additional security or further security, as the case may be, required to be furnished for registration, shall be in the form of a bank guarantee from a local scheduled bank or in the form of a personal bond with two solvent sureties, acceptable to the designated officer in form VAT-3.

We analysed the COVIS data in the offices of AETC, Ludhiana-I and Patiala and found that 864 new dealers⁷ were registered without obtaining two sureties; of which, 719 dealers⁸ were registered without sureties and 145 dealers⁹ were registered with single surety only in contravention of the Rules.

2.10.10.6 Cancellation of the registration of dealers

The registration issued under the PVAT Act could be cancelled by the DO if the dealer failed to adhere to the provisions of the Act.

We observed in many cases that dealers continued business even after cancellation of their registration certificates. But the Act is silent and does not contemplate any action against such dealers.

The Government may consider incorporating a penal provision in the PVAT Act/Rules to contain the offending dealers who continued their business even after cancellation of the registration certificates.

⁶ Ludhiana-I, III and Ropar.

⁷ AETC, Ludhiana-I:466, AETC, Patiala:398.

⁸ AETC, Ludhiana-I:381, AETC, Patiala:338.

⁹ AETC, Ludhiana-I:85, AETC, Patiala:60.

2.10.10.7 Delay in cancellation of the Registration Certificates

The PVAT Rules provide that the order for cancellation of the registration shall be passed within a period of thirty days from the receipt of application.

We analysed the COVIS data in the offices of AETC, Ludhiana-I and Patiala and found that in 140 and 66 cases, the order of cancellation of the registration certificates were issued after 30 days with delays ranging from seven to 1,229 days.

2.10.10.8 Non-recovery of the registration fee

The PVAT Rules provide that:

- ❖ An application for registration shall be made in form VAT-I alongwith the receipt for a fee of ₹ 500 in form VAT-2.
- ❖ An application for obtaining registration for VAT or TOT by a person who had registered under the repealed Act, shall also be made in form VAT-I to the DO within 30 days from appointed day alongwith the original registration certificate granted under the repealed Act. No fee mentioned above shall be required to be deposited by such persons, if the application is made within the stipulated period.
- ❖ Under the PVAT Act, a taxable person who was registered under the repealed Act and whose registration had been continued under the PVAT Act, as TOT dealer shall be liable to pay tax on the stock held on 31 March 2005.

(a) We found that out of the 2,398 dealers to whom VAT/TOT numbers were granted by AETC Ropar, 1,853 dealers who were the existing registered persons under the repealed Act, had applied for registration under the PVAT Act after the stipulated period of 30 days and had not paid the registration fee of ₹ 9.27 lakh in contravention of the Rules.

(b) We observed that 1,216 persons, who were the existing registered persons under the repealed Act, had applied for and were allotted TOT registration number. When we called (April, 2010) for the records relating to the transitional stock held by these dealers, none of the AETCs selected in audit could produce the requisite records. As a result, the liability of tax payable on the transitional stock held on 31 March 2005 by these dealers could not be checked/verified in audit.

2.10.11 Return

2.10.11.1 Late/non-filing of returns

AETCs Ludhiana-I and Patiala

The Punjab Value Added Tax Act provides that if a person registered under this Act or any other person required to furnish return or annual statement without sufficient cause fails to furnish return or annual statement by the prescribed date, the Commissioner or the designated officer, may direct him to pay in addition to tax, interest or penalty under any other provision of the Act, a further penalty of a sum of ₹ 100 per day of default, subject to maximum of ₹ 10,000.

(a) We found that the COVIS table capturing the details of quarterly/annual returns did not have any field relating to penalty levied/realised from the defaulting dealers. In the absence of this provision in COVIS, non levy/short levy of penalty from the defaulting dealers could not be verified in audit. Analysis of the COVIS data revealed that 21,694 quarterly¹⁰ and 7,159 annual¹¹ returns were filed after the prescribed due dates during the period from 2005-06 to 2008-09. In the office of the AETC, Ludhiana-I, though 12,050 quarterly returns were filed after the due dates with delays ranging between one and 1,401

days, the department did not invoke the penal provisions under the Act. Similarly, in the offices of AETCs, Ludhiana-I and Patiala, though 7,159 annual returns were filed after the due dates with delays ranging between one and 1,193 days, penalty was not levied.

(b) We noticed that 40,338 dealers in four AETCs¹² were registered under the PVAT Act from the 42,947 numbers of the existing registered dealers under the repealed Act and thus 2,609 numbers of dealers though not registered under the PVAT Act were deemed to have been registered under section 93(i) this Act. They were required to file the returns but the returns were not filed by them till date. The Department did not reply when requested to intimate whether any notices for levy of penalty were issued to the dealers.

(c) We noticed that 876 dealers in five AETCs¹³ though registered under the PVAT Act had not filed 3,504 quarterly returns and 6,654 dealers had not filed their annual statement for the years 2005-06 to 2008-09 till date and the Department failed to identify the defaulters and levy penalty. The Department did not reply when requested to intimate whether any notices for penalty were issued to the defaulted dealers (September 2010).

¹⁰ AETC, Ludhiana-I:12,050 and AETC, Patiala:9,644.

¹¹ AETC, Ludhiana-I:4,879 and AETC, Patiala:2,280

¹² Ludhiana I, II, Sangrur and Ropar.

¹³ Ludhiana I, Ludhiana II, Fatehgarh Sahib, Mohali and Patiala.

2.10.11.2 Scrutiny of returns

Section 29 of the PVAT Act read with rule 43 of the PVAT Rules provides that the DO shall scrutinise every return filed under section 26 of the Act. Scrutiny of the returns filed by the dealers is a tool of enforcement strategy of VAT administration. If during scrutiny of the return, it is found that less tax has been paid than the tax actually payable, the DO shall serve a notice upon the person concerned directing him to rectify the same and to pay the amount of tax less paid, alongwith the interest payable under section 32 of the Act and produce the treasury receipt(s) to the DO, within the time specified in the said notice. However, no intimation under the PVAT Act shall be sent after the expiry of one year from the end of the financial year in which the return is filed.

(a) We found that in nine AETCs mentioned in the table below, only a nominal number of returns (11 per cent) were scrutinised by the DOs during 2005-09. It can be observed from the table that one year had lapsed after the expiry of the financial year in which the returns were filed and it is not possible to issue any intimation now, even if the returns are scrutinised and any short payments etc. are detected, since the returns are deemed to have been assessed.

Name of the AETCs	Period	Number of returns			
		to be scrutinised	scrutinised	not scrutinised	percentage of shortage
Ludhiana-I	2005-09	2,64,556	9,308	2,55,248	96
Ludhiana-II	-do-	2,42,884	24,269	2,18,615	90
Ludhiana-III	-do-	1,92,244	14,272	1,77,972	93
Fatehgarh Sahib	-do-	77,200	4,852	72,348	94
Patiala	-do-	1,58,348	64,848	93,500	59
Sangrur	-do-	1,48,624	Nil	1,48,624	100
Ropar	-do-	35,816	10,885	24,931	70
Mohali	2006-09	89,212	--	89,212	100
Barnala	2007-09	26,396	7,970	18,426	70
Total	-	12,35,280	1,36,404	10,98,876	89

(b) A centralised database exists in the COVIS to watch the work done by the designated officer in the field. But the Department had not generated any information from the database regarding the number of returns scrutinised vis-a-vis shortfall in scrutiny of returns. A few examples of loss of revenue due to non-scrutiny of the returns are given below:-

PVAT Act provides that amount of duties levied or leviable on goods under the Central Excise Act 1914 shall be deemed to the part of sale price.

A dealer under the AETC, Ludhiana III engaged in the business of manufacture and sale of yarn, terry towel etc. in his self assessment return for the year 2006-07, did not include the excise duty of ₹ 18.25 crore to his gross turnover. This resulted in short payment of tax of ₹ 73 lakh.

- A dealer of the AETC, Hoshiarpur engaged in the business of work contract claimed deduction of ₹ 6.19 crore against the admissible deduction of ₹ 2.48 crore on account of labour etc. in his self assessment return for the year 2006-07. This omission had resulted in short levy of output tax of ₹ 10.52 lakh.
- Four dealers of the AETCs, Ferozepur, Gurdaspur and Sangrur engaged in the business of work contract claimed ITC at the rate of 12.5 *per cent* on the purchase and consumption of material worth ₹ 1.83 crore, but paid output tax at the rate of four *per cent* instead of appropriate rate of tax on the items of material consumed in the execution of work done as per their self assessment return for the year 2006-07. This resulted in short levy of output tax of ₹ 15.58 lakh.
- A dealer of the AETC, Ludhiana-I had shown sales of ₹ 110.99 crore in his self assessment return for the year 2006-07 instead of the actual sales of ₹ 114.18 crore, as shown in his trading account. This resulted in suppression of sales of ₹ 3.19 crore and short payment of tax of ₹ 12.79 lakh.

In all the above mentioned cases the Department had not carried out the scrutiny. Though the period of completing the scrutiny in these cases has been expired.

2.10.12 Non-assessment of the exempted units

The PVAT Act provides that Section 10A, 10B and 30A of the repealed Act and rules framed thereunder giving tax concessions to industrial units and assessment thereof shall remain in force. Further, Section 11(3) of the repealed Act provides that assessment of an exempted unit should have been finalised within a period of three years from the last date prescribed for furnishing of the last return.

As the provision for assessment of the deferred and exempted units as saved under the PVAT Act, the assessment in such cases for the assessment year 2005-06 should have been finalised by November 2009. The Department stated (October 2009) that the last date would be 30 September 2010 and the assessments were being done. The reply of the Department is not acceptable as the assessment had to be completed before 20 November 2009 as required under Section 11 (3) of the Act *ibid*. Two instances of failure to finalise the assessment are given below:

AETC, Ludhiana-I

(a) We noticed in May 2009 that in his self assessment return for the year 2007-08, while computing the output tax, a dealer claimed deduction of ₹ 22.35 crore from his gross sales, treating the sale as sale made by exempted unit, whereas his exemption limit had expired on 16 May 2006 and as such the dealer was liable to pay tax on his entire sale from 17 May 2006. Thus, non finalisation of the assessment as required under the saved D&E Rules resulted in non-levy of output tax of ₹ 89.41 lakh. The Department stated (October 2009) that assessment proceedings had been initiated and final reply would be communicated in due course. The latest position of the case is awaited (October 2010).

AETC, Patiala

(b) We found that a dealer enjoying the benefit of exemption from payment of tax of ₹ 6.19 crore had availed the benefit of exemption of ₹ 2.85 crore leaving a balance of ₹ 3.34 crore as on 1 April 2005. The Department in May 2005 issued an entitlement certificate to the dealer for balance exemption of ₹ 3.92 crore instead of ₹ 3.34 crore as on 1 April 2005. We noticed that the dealer while filing his self assessment return for the year 2005-06 carried forward the balance exemption of ₹ 3.92 crore instead of ₹ 3.34 crore.

Thus, non-finalisation of the assessment as required in the saved (D&E) Rules and issue of incorrect entitlement exemption certificate by the DO resulted in excess carry forward of exemption of ₹ 58 lakh.

When we pointed out, the Department did not furnish any reply (October 2010).

The Government may consider auditing of the returns by prescribing the parameters to be adopted for selection of the returns and procedure of tax.

2.10.13 Input Tax Credit

AETC, Ludhiana-I and Sangrur

ITC is not admissible on the value of imported goods as provided in Section 13(1) of the PVAT Act.

(a) We found that out of the total purchases of ₹ 46.22 crore, two dealers had imported goods worth ₹ 19.79 crore, which was deductible from the total purchases for the purpose of claiming of

ITC. Against this, the dealers in their returns for the year 2006-07, had deducted only ₹ 1.71 crore and claimed ITC on the balance imported value of ₹ 18.08 crore treating it as local purchases which resulted in inadmissible ITC of ₹ 72.30 lakh.

When we pointed out, the Department did not furnish any reply (October 2010).

AETC, Ludhiana-I

ITC shall be allowed only to the extent by which the amount of tax paid in the state exceeds four *per cent* on purchase of goods used in the manufacturing or in packing of taxable goods sent outside the state by way of branch transfer.

(b(i)) We found that a dealer in his self assessment return for the year 2006-07 had shown branch transfer of ₹ 17.86 crore against the actual branch transfer of ₹ 20.79 crore as per the declarations in Form 'F' received from the purchaser. But the dealer apportioned ITC of ₹ 42 lakh against the apportionable ITC of ₹ 66 lakh. This resulted in short apportionment of ITC of ₹ 24 lakh.

When we pointed out, the Department did not furnish any reply (October 2010).

b(ii) We found that another dealer had shown in his self assessment return for the year 2006-07 the gross turnover of ₹ 145.80 crore, branch transfer of ₹ 97.90 crore and purchases eligible for ITC of ₹ 31.71 crore. The dealer had apportioned ITC of ₹ 46 lakh on account of branch transfer against the apportionable ITC of ₹ 51 lakh, which resulted in short apportionment of ITC of ₹ 5 lakh.

When we pointed out, the Department did not furnish any reply (October 2010).

AETC, Mohali

c(i) We found that a dealer in his self assessment return for the year 2006-07, had wrongly calculated input tax credit of ₹ 40.92 lakh instead of ₹ 32.30 lakh on the eligible purchases of ₹ 8.08 crore at the rate of four *per cent*. This resulted in excess claim of ITC of ₹ 8.62 lakh.

c(ii) We found that a dealer in his self assessment return for the year 2006-07 had claimed purchases of ₹ 25.35 crore against the actual purchases of ₹ 21.83 crore and thus claimed excess ITC of ₹ 14.11 lakh.

In all the above mentioned cases, the Department had not carried out the scrutiny/assessment/tax audit. Though the period of two years for scrutiny of return has expired. These cases can however be taken up for assessment with a period of six years.

2.10.14 Deficiencies in the Forms of returns

Scrutiny of monthly, quarterly and annual returns in form VAT-16, VAT-15 and VAT-20 respectively, which are required to be submitted by the dealers under Rule 36 and 40 of the PVAT Rules, revealed that columns regarding some most important information such as nature of business, details of commodities of sale/purchase made by the dealer were missing in the forms. The deficiencies in the forms could cause many difficulties to the Department to determine the deduction from turnover and application of correct rate of tax etc. and is also building up a database of assesses.

When we pointed out, the Department included the column regarding description of goods in the form of returns.

2.10.15 Tax audit

ETC, Patiala

As per the provisions of the PVAT Act and Rules made thereunder, the DO may conduct audit of any of the returns (including any document, information or statutory forms submitted) filed by a person in order to ascertain the correctness of return filed, the admissibility of various claims including ITC and refund. The audit is required to be carried out within a period of six years from the date of furnishing of the returns.

(a) The information regarding the norms/parameters adopted for selection of the returns for tax audit were called for from the ETC, Patiala but still awaited (October 2010). We noticed that a module for tax audit provided in the COVIS has not been made operational till date (October 2010).

Thus, neither the module for management of tax audit provided in the COVIS been utilised nor the functioning of tax audit been effectively monitored, though more than five years have elapsed after the introduction of VAT. We also noticed that the rules or executive instructions did not prescribe maintenance of any register or record to watch the progress of tax audit.

As a result, no records or registers were maintained in the field offices to watch the number of dealers selected for tax audit, name of the audit team to whom the audit was assigned, number of assessments made and the nature of findings etc. Consequently, the correct position regarding tax audit conducted and corrective measures taken by the Department to remove discrepancies or to recover the short remittance of tax, if any, from the assessee could not be ascertained.

The Government needs to take action for auditing of the returns by prescribing the parameters to be adopted for selection of the returns and procedure of tax audit.

(b) The Department of Excise & Taxation, Government of Punjab decided to engage an expert to assist them in identifying revenue augmentation measures and also to identify areas of leakages in VAT collection. The Excise & Taxation Department entered into an agreement on 30th October 2008 with a private firm M/s Pricewaterhouse Coopers Kolkata for preparation of policies and procedure for conducting VAT audit and collection of information by the Information Collection Centres (ICCs) at a cost of ₹ 66 lakh plus out of pocket expenses. The scope of work *inter-alia* included 35 dealers chosen for VAT audit in three districts of Punjab.

The Department was asked to furnish copies of the audit reports of 35 dealers audited by the private firm and the revenue impact as a result of audit. The Department did not furnish any reply except giving the audit reports of three dealers.

2.10.16 Refunds

2.10.16.1 Audit of refunds issued to the dealers

AETC Ludhiana-I, II and III

Audit of refunds is an important function from the revenue point of view. Checking/audit of refunds finalised by the assessing authority was assigned to the AETC (Inspection) under the repealed Act. The Government vide notification had created the post of Senior Auditor in August 2007.

The AETC cum Senior Auditor did not conduct the audit of refunds in 9,992 cases valued at ₹ 394.36 crore except 38 refunds audited in the office of AETC, Ludhiana-I during 2005-06.

2.10.16.2 Inadmissible refunds

The Punjab tax on Entry of goods into Local Area Act, 2000 read with new conditions regulating deferment and exemption as contained in the Punjab VAT Act, 2005 provides that input tax credit on account of entry tax paid on the purchases shall not be admissible when goods are imported by an exempted/deferred unit, as the saved PGST (Deferment and Exemption) Rules do not permit any ITC/refund on purchases made from outside the state of Punjab.

(a) We noticed that while allowing the refunds in three AETCs¹⁴ pertaining to the years 2007-08 and 2008-09 to four dealers (between May 2008 and March 2009) who were also availing the benefit of exemption from payment of tax, the designated officers incorrectly allowed input tax credit on account of entry tax paid on import purchases made by the dealers. This resulted in inadmissible allowance of ITC and consequent grant of refund to the extent of ₹ 3.78 crore.

(b) We noticed that while allowing refund by the AETC, Mohali to a dealer for the quarter ended March 2007, the designated officer incorrectly worked out the ITC ₹ 5.57 crore instead of ₹ 5.53 crore on the purchases of ₹ 50.99 crore and this resulted in excess refund of ₹ 3.92 lakh.

¹⁴ Ludhiana III, Barnala and Ropar.

Section 13(4) of PVAT Act, 2005 provides that input tax credit on lubricants, shall be allowed only to the extent by which the amount of tax exceeds four *per cent*, provided that these goods are used in the production of taxable goods or captive consumption of power.

c(i) We noticed that while allowing refund by the AETC, Mohali to a dealer for the period from 1 October 2007 to 30 September 2008, the DO had incorrectly allowed ITC on the purchase of lubricants of ₹ 64.72 lakh at the rate of 12.5 *per cent* without retaining four *per cent*. This had resulted in excess refund of ₹ 2.59 lakh.

c(ii) We noticed that while allowing refunds of ₹ 2.33 crore and ₹ 1.41 crore for the quarters ended March 2008 and June 2008 respectively by the AETC, Ludhiana-III to a dealer, imported purchases corresponding to credit of entry tax allowed was not accounted for in the total purchases resulting in suppression of purchases of goods of ₹ 5.80 crore. This resulted in evasion of tax of ₹ 23.18 lakh.

When the matter was reported to the Department (April 2010), the Department replied that the amount of entry tax for the quarter ended December 2007 was included in the quarter ended March 2008. Similarly the entry tax for the quarter ended March 2008 was included in the quarter ended June 2008. The reply of the Department is not acceptable as the dealer had claimed and was allowed the credit of entire entry tax during the period of refunds in question.

2.10.17 Non-verification of goods vehicles passing through the State

ICC, Lalru

PVAT Act provides that where a goods carrier of one State bound for any other State passes through the State of Punjab, the owner or person incharge of such vehicle shall furnish, in duplicate, to the officer incharge of the check post or the Information Collection Centre (ICC), a declaration in respect of his entry into the State in the prescribed form and obtain from him a copy thereof duly verified. The owner or person incharge of the vehicle, shall deliver within 48 hours the aforesaid copy of the declaration to the officer incharge of the check post or ICC at the point of his exit from the State, failing which, he shall be liable to pay a penalty equal to fifty per cent of the value of goods involved.

We noticed that in respect of 1,762 vehicles¹⁵ carrying goods that entered into the State between April 2005 and March 2009 and declaring their exit point as ICC Lalru, the details of these vehicles were not available at ICC Lalru. In such circumstances, the Department was required to initiate action to trace these vehicles in the State and impose penalty for violation of the provisions of the PVAT Act. The Department did not follow the prescribed provisions of law.

When we pointed out, the Department did not furnish any reply (October 2010).

¹⁵ 1,008 (2005-06), 526 (2006-07), 91 (2007-08) and 137 (2008-09).

2.10.18 Internal Audit

Internal Audit Organisation (IAO) is a vital component of the internal control mechanism and is generally defined as the control of all controls to enable an organisation to assure itself that the prescribed systems are functioning reasonably well. IAO was set up in October 1981 as an independent organisation under the State Finance Department and was entrusted inter alia, with the internal audit of revenue receipts to safeguard against any loss or leakage of revenue arising under the various revenue heads including sales tax/VAT. By a notification of November 1991, the focus of audit was shifted from revenue to expenditure audit. However, the Government in June 2004 again introduced the internal audit of sales tax/VAT from the year 2004-05.

When we enquired (April 2010) from the selected AETCs as to whether the audit of sales tax/VAT was being conducted by the IAO or not, it was intimated (April 2010) that audit of VAT receipt was not being conducted by the IAO.

The Government may consider enforcing audit of revenue receipts by the IAO so as to avoid the risk of loss of revenue.

2.10.19 Conclusion

The transition from PGST Act 1948 to PVAT Act 2005 suffered due to lack of effective control measures and monitoring by the Department for the transition process. The database of the dealers registered under the repealed Act vis-à-vis the dealers registered under the PVAT Act was not generated by the Department from the COVIS, even though separate modules for registration of dealers containing all the requisite information for the maintenance of database were available in the system. Adequate steps were not taken to complete the assessments under the repealed Act within the prescribed time limit despite introduction of VAT in April 2005 and non finalisation of timely assessments resulted in loss of revenue to Government due to quashing of additional demands created in time barred cases. Abnormally low percentage of scrutiny of returns/tax audit left enough scope for leakage of revenue as test checked conducted by audit revealed many cases of non/short realisation/loss of revenue. Tax audit was neglected as no norms/parameters for selection were finalised by the Department till October 2010. The Department had negligible internal control over the issue of refunds. A few deficiencies in the Act and the Rules and absence of executive instructions too had contributed to failure of the field functionaries in implementing various provisions of the PVAT Act effectively.

2.10.20 Summary of recommendations

The Government may consider:

- *rectifying the deficiencies in the COVIS.*
- *incorporating a penal provision in the PVAT Act/Rules to contain the offending dealers who continued their business even after cancellation of the registration certificates;*
- *auditing of the returns by prescribing the parameters to be adopted for selection of the returns and procedure of tax audit;*

- *issuing instructions to the designated officers to ensure scrutiny of every return in time as provided in the PVAT Act; and*
- *enforcing audit of receipts by the Internal Audit Organisation so as to avoid the risk of loss of revenue.*

2.11 Audit observations

We noticed several cases of non-observance of provisions of Acts/Rules; non/short levy of tax, penalty and interest; incorrect allowance of exemption; incorrect determination of turnover and other cases during scrutiny of records of sales tax/VAT as mentioned in the succeeding paragraphs. These cases are illustrative and are based on a test check carried out by us. Such omissions on the part of Assessing Authorities (AAs)/DOs are pointed out in audit repeatedly, but not only the irregularities persist, they also remain undetected till we conduct audit. There is need for the Government to improve the internal control system so that such omissions can be detected and corrective measure taken.

2.12 Non-observance of the provisions of Acts/Rules

The Punjab General Sales Tax Act, 1948 (PGST Act), The Punjab Value Added Tax Act, 2005 (PVAT Act), The Central Sales Tax Act, 1956 (CST Act) and the Rules provide for:-

- (i) levy of tax at the prescribed rates,*
- (ii) exemption from tax and*
- (iii) correct determination of the tax/turnover.*

The AAs while finalising the assessment did not observe some of the provisions of Acts/Rules in the cases mentioned in paragraphs 2.12.1 to 2.13.2. This resulted in non/short levy and non-realisation of tax, interest and penalties of ₹13.01 crore.

2.12.1 Incorrect levy of concessional rate of tax

AETC, Jalandhar-II and AETC, Ludhiana-II

Under the CST Act, on inter state sales of goods made to the registered dealers and supported by declarations in Form C, CST is leviable at the concessional rate of four *per cent* or at such lower rate as applicable to the sale or purchase of such goods within the State. Tax on goods not covered by such declarations, in the case of declared goods, shall be calculated at twice the rate applicable in the State and in respect of other goods at 10 *per cent* or at the rate applicable to the sale of such goods inside the State, whichever is higher.

We found (between April and June 2009) that while finalising the assessments for the years 2003-04 to 2004-05 of two dealers engaged in the business of sports goods and Jewellery, the AAs erroneously assessed tax of ₹ 3.62 lakh against the tax leviable of ₹ 29.69 lakh as the sale of only ₹ 4.54 lakh out of ₹ 3.02 crore was supported by the prescribed declaration forms. This omission resulted in short levy of CST of ₹ 26.07 lakh.

When we pointed out (between April and June 2009), the Department intimated in November 2009 that the AETC, Jalandhar-II had taken up the case for suo motto re-assessment.

The reply in respect of the other case is awaited (October 2010).

We reported the matter to the Government (between December 2009 and February 2010); the reply is awaited (October 2010).

2.12.2 Application of incorrect rate of tax

AETC, Barnala

As per Section 29 (1) of the PVAT Act, on filing of returns by the dealer, if any tax is found due, a notice of demand specifying the sum due shall be sent to the dealer. However, no intimation under the PVAT Act shall be sent after the expiry of one year from the end of the financial year in which the return is filed.

We found in February 2009 that one dealer in his self assessment returns/ annual return for the year 2005-06 had shown the tax on taxable turnover of batteries valued at ₹ 58.48 lakh at the rate of four *per cent* instead of the correct rate of 12.5 *per cent*. The Department accepted the returns filed, but no notice of demand for the short paid amount of tax of ₹ 4.97 lakh as required under the Act was issued.

When we pointed out (November 2009), the AETC, Barnala stated that an assessment had been framed by creating an additional demand of ₹ 10.85 lakh and recovery proceedings were in progress.

2.12.3 Non-levy of tax

AETC, Ludhiana-III

Under the PGST (D&E) Rules, as saved under the PVAT Act, the transfer of products from one unit to another unit within the State of Punjab shall be deemed as sales and liable to tax.

We found during scrutiny of the refunds for the second quarter of the year 2008-09 (June 2009) that a dealer who was engaged in the business of manufacture and sale of yarn, paper and terry towel having single TIN number for all the three units. The dealer was filing a single return for all

these units. He was enjoying the benefit of exemption from payment of sales tax/VAT on the unit of manufacture and sale of yarn only. The dealer made transfer of the products produced by his exempted unit valued at ₹ 30.56 crore to his own terry towel division. While the notional tax liability for sale to other dealers within the State of Punjab and interstate sales was worked out and adjusted against the exemption limit but the dealer omitted to work out the notional tax liabilities on the transfer in his own terry units in his self assessment return. This resulted in non-levy of notional tax and excess carry forward of exemption of ₹ 1.22 crore.

We reported the matter to the Department and the Government in January 2010. The Department replied that branch transfer within the State can be made to another dealer having his separate independent TINs and can not be treated as branch transfer in the case of inter-unit of the same concern. The reply is not acceptable as there is no provision in Act/Rules in case of an exempted unit for allowing inter-unit transfers as tax free.

2.12.4 Short assessment of central sales tax

AETC, Muktsar

As per Section 8 of the CST Act, a dealer who in the course of inter state trade or commerce sells to the Government departments any goods, was liable to pay tax at the concessional rate of four *per cent* upto 31 March 2007 provided the sales were supported by certificates in form D. Further, the tax payable by the dealer on the sale of goods in the course of inter state trade or commerce not falling within the provisions stated above, 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 was higher.

We found in October 2009 that an assessee engaged in the manufacture and sale of paper and enjoying the benefit of exemption from payment of tax, had exhibited an inter state sale (ISS) of paper valuing ₹ 138.53 crore in his self assessment return for the year 2006-07. Out of this, the sales of ₹ 48.06 crore were assessed to be the ISS made to the Government departments. During scrutiny of the return, we found that:

An ISS of ₹ 47.61 crore made to the Government departments duly supported by D forms had been assessed at the rate of one *per cent* instead of the correct rate of *four per cent*. This mistake of assessing ISS at the rate of *one per cent* resulted in short assessment of notional central sales tax and excess carry forward of exemption of ₹ 1.43 crore.

We reported the matter to the Department and the Government (between December 2009 and March 2010); their replies are awaited (October 2010).

2.12.5 Inadmissible claim of input tax credit

AETC, Muktsar

The PGST (D&E) Rules as saved under the PVAT Act, provides that a unit availing benefit of deferment or exemption from payment of tax, shall be entitled to refund of tax paid or payable by it on the purchases made from a taxable person within the State, for use in manufacturing, processing or packing of taxable goods. The amount of refund allowed shall be added to the notional tax liability of the unit availing the exemption. No input tax credit shall be admissible in respect of such purchases.

We found in October 2009 that in his self assessment return/annual return for the year 2005-06, an assessee availing the benefit of exemption from payment of tax under the PVAT Act 2005, instead of claiming the refund of ₹ 6.97 lakh on account of tax paid on the purchases of raw material has brought forward and utilise it in the assessment year 2006-07 which was irregular and resulted into excess availment to exemption to this extent.

We reported the matter to the Department and the Government (between October 2009 and February 2010); their replies are awaited (October 2010).

2.12.6 Excess claim of input tax credit

AETC, Jalandhar-I and AETC, Patiala

As per section 2(ze)(i) of the PVAT Act, reverse input tax credit means an amount of input tax credit, which is required to be reversed by a taxable person on account of credit note for output tax received from the seller of goods on purchases in respect of which input tax credit is claimed. Similarly, a taxable person shall deduct from his gross turnover of sales, amount allowed as cash discount or trade discount/rebate, provided such discount is in accordance with the regular trade practice.

We found in June 2009 and July 2009 that two dealers in their self assessment returns/annual returns and trading account for the year 2006-07 had shown the receipts of credit notes, cash/trade discount and rebate valued at ₹ 2.01 crore received on gross purchases of ₹ 12.97 crore, but had omitted to deduct these receipts from the gross purchases as required under the rules *ibid*. These mistakes of non deduction of the receipts on account of credit notes, cash/trade discount and rebates from the gross purchases resulted in excess claim of input tax credit of ₹ 8.18 lakh.

We reported the above mentioned cases to the Department and the Government (between February 2010 and March 2010); In one case of AETC Jalandhar-I, the Department stated that discount received by the dealer was nothing to do with the total sale figures of the company as purchase figures of the consigners being a part of promotional sales. The reply is not acceptable in view of provision of section 2 (ze)(i)

which states that the ITC is required to be reversed on account of credit notes/discount for output tax received from the seller of goods or purchases in respect of which ITC is claimed. Reply in respect of the other dealer is awaited (October 2010).

2.12.7 Non-reversal of input tax credit

Rule 24(1) of the PVAT Rules provides that where a taxable person has used the goods purchased partially for taxable/tax free sales, but is unable to maintain accounts as provided in the Rule 23 and the sales made by him include sale of tax free goods and taxable goods, then it shall be presumed that the goods so purchased during the tax period have been used in proportion of turnover of sales of tax free goods and accordingly the input tax credit shall be disallowed in that proportion.

(a) In the office of three AETC¹⁶s, we found between November 2008 and June 2009 that four assessees engaged in the manufacture and sale of yarn, hosiery, oil and cattle feed, in their self assessment returns for the year 2005-06 and 2006-07 had shown sales of tax free goods of ₹ 26.97 crore and taxable goods of ₹ 59.45 crore out of the total turnover of ₹ 86.42 crore. The dealers had used the taxable goods in the manufacture of tax free and taxable goods and failed to maintain the separate accounts as required under the rule 23 of Rules ibid. In terms of rule 24, the dealers were required to reverse the ITC to the extent of the taxable goods used in the manufacture of tax free goods. This failure to reverse the ITC

resulted in excess claim of ₹ 54.16 lakh. The Department accepted the returns filed by the dealers and no notice of demand for the short paid tax of ₹ 54.16 lakh as required under the Act was issued.

AETC, Patiala

Rule 21(1) and (2) of the PVAT Rules provide that no input tax credit shall be admissible to a person for the tax paid on purchase of goods, if such goods are lost or destroyed or damaged beyond repair because of any theft, fire or natural calamity and the input tax credit availed on such goods shall be reversed immediately on occurrence of such event.

(b) We found in June 2009 that an assessee in his self assessment return for the year 2006-07 had claimed and utilised input tax credit of ₹ 49.40 lakh on the purchase of goods valuing ₹ 5.36 crore. Further, during scrutiny of the trading account, we found that goods valuing ₹ 53.58 lakh were destroyed by fire on which the proportionate input tax credit was required to be reversed. But, no reversal of the proportionate input tax credit of ₹ 6.36 lakh was carried out resulting in excess utilisation of credit of equivalent amount.

¹⁶ Ludhiana-I, Ludhiana-III and Moga.

We reported the above mentioned cases of non-reversal of input tax credits to the Department and the Government (between January 2010 and March 2010). The AETC, Patiala reported (July 2010) recovery of ₹ 2.97 lakh from the assessee and stated that the balance recovery would be effected in installments.

2.12.8 Inadmissible availment of exemption from payment of tax

AETC, Muktsar

Under the PGST (D&E) Rules as saved under the PVAT Act, exemption from payment of sales/purchase tax is admissible to a unit selling the manufactured products mentioned in the eligibility certificate.

We found in October 2009 that an assessee engaged in the manufacture and trading of yarn and also availing the benefit of exemption from payment of tax for manufacturing of yarn (end product) claimed exemption of tax on the sale of ₹ 79.71 crore (Local sales and inter state sale) instead of

₹ 77.31 crore (yarn) reflected in the books. The Department needs to take action to reconcile the difference in figures.

We reported the matter to the Department and the Government (February 2010); their replies are awaited (October 2010).

2.12.9 Excess allowance of exemption

AETC, Bathinda

Notification prescribing the VAT conditions under the PVAT Act, subject to which the concessions granted under the PGST (D & E) Rules, were allowed to be continued, provides that the quantum of deferment of or exemption from payment of tax, as the case may be, availed during a return period by a unit, shall be calculated by adding the output tax on interstate sales, output tax on inter state stock transfer, the amount of refund allowed and the output tax on local sales.

(a) We found in September 2009 that a dealer engaged in the manufacture of yarn and enjoying the benefit of exemption from paying tax, had not calculated in his VAT return for the year 2006-07 the quantum of exemption correctly by adjusting the output tax on inter state sales of ₹ 1.20 crore; output tax of ₹ 1.15 crore on inter state stock transfer duly supported by Form F; the amount of refund of ₹ 3.71 crore allowed during the return period and the output tax on local sales of ₹ 2.97 crore. The total amount of exemption, after

taking into account his output tax liability on interstate sales, inter state stock transfer, refund and the local sales, was erroneously worked out as ₹ 4.15 crore instead of ₹ 9.03 crore. This resulted in excess allowance of exemption of ₹ 4.88 crore.

AETC, Muktsar

(b) We found in October 2009 that two dealers engaged in the manufacture of yarn and paper and enjoying the benefit of exemption from paying tax, had in their self assessment returns for the year 2006-07 not calculated the quantum of exemption correctly by adjusting the amount of refund of ₹ 2.29 crore allowed to them during the return period. This resulted in excess allowance of exemption of ₹ 2.29 crore.

We reported the above mentioned cases of excess amount of exemption to the Department and the Government (February 2010); their replies are awaited (October 2010).

2.12.10 Inadmissible refund

AETC, Amritsar-I

As per condition No.2 of the PGST (D&E) Rules as saved under the PVAT Act, tax paid on purchase of goods shall not be refunded, if the goods so purchased are used in the manufacture, processing or packing of the tax free goods. With effect from 22 December 2006, the goods 'Blanket' manufactured by units other than composite unit had been declared as tax free. A composite unit is an unit which purchases raw material and uses the same for the production of some other kind of goods which are further used as raw material.

We noticed in October 2009 that a dealer engaged in the manufacture and sale of blankets and enjoying the benefit of exemption from tax, had been allowed refund of ₹ 8.16 lakh in August 2008. On examination of VAT invoices related to the VAT return for the year 2007-08, we found that he had made purchases of acrylic yarn from other dealers for use in the manufacture of blankets. These purchases of direct raw material rendered the dealer to lose the status of a composite unit. As such, the blankets manufactured by this dealer are to be treated as tax free commodity. The mistake of the AETC to consider the dealer as a composite unit and the grant of refund resulted in loss of revenue of ₹ 8.16 lakh.

We reported the matter to the Department and the Government (March 2010); their replies are awaited (October 2010).

AETC, Jalandhar-II

As per Rule 52(4) of the PVAT Act, tax has to be determined correctly. Further, excess of input tax credit over the output tax is refundable.

We found in September 2009 that the AETC had allowed (June and December 2008) refunds of ₹ 14.56 lakh in respect of the quarters ending March and June 2008. On cross verification of the refund order

with the VAT-15 returns and worksheet filed by the dealer, we found that the AETC did not verify the VAT -15 returns correctly because the dealer had an arithmetical mistake in calculating the ITC at the rate of four percent on net purchases of ₹ 3.77 crore. The ITC of ₹ 18.28 lakh instead of ₹ 15.07 lakh

was adjusted against the output tax. This mistake had resulted in incorrect refund of ₹ 3.21 lakh.

We reported the matter to the Department and the Government (between September 2009 and March 2010); their replies are awaited (October 2010).

2.12.11 Non-levy of Purchase tax

AETC (Inspection) Ludhiana-III

In terms of entry No. 1 of Schedule D appended to the PGST Act, as amended by notification No. S.O.13/PA/46/48/S-5/ Amd/ 2002 dated 24.4.2002 made applicable from 12.11.2001, wheat when purchased within the State of Punjab for processing by the flour mills having five or more installed roll bodies was exempted from payment of the purchase tax.

We found (March 2008) that while finalising (September 2005) the assessment for the year 2001-02 of a dealer engaged in the business of atta, maida etc; the AA allowed exemption from payment of purchase tax on the entire purchase of wheat valued at ₹ 2.82 crore; but the exemption allowed from payment of purchase tax on the wheat valued at ₹ 73.38 lakh purchased within the State prior to 12.11.2001 was not admissible. This mistake resulted in non levy of purchase tax of ₹ 2.93 lakh.

We reported the matter to the Department and the Government (October 2009); their replies are awaited (October 2010).

2.12.12 Excess allowance of exemption

AETC, Amritsar-I and AETC, Ferozepur

As per Section 19 of the PVAT Act, VAT is leviable on the taxable turnover of purchase of goods specified in schedule H at the rate of four *per cent*. In the case of an exempted unit, the dealer has to pay the purchase tax and claim refund. The amount of refund so claimed shall be liable to be adjusted against exemption.

We noticed in October 2009 that four dealers engaged in the business of rice shelling were enjoying the benefit of exemption from payment of sales tax/VAT. As per VAT returns for the year 2006-07, the dealers had purchased paddy (Schedule-H item) valuing ₹ 23.11 crore but had neither paid purchase tax nor claimed refund as required under the PVAT Act. This resulted in excess allowance of exemption of ₹ 92.46 lakh.

We reported the matter to the Department in October 2009. The DO, Ferozepur stated (October 2009) that both purchase tax and sales tax liability were lying in the hands of dealers and tax liability occurred only on the taxable turnover of the taxable person. The tax/exemption could not be reduced taking into consideration both factors as input tax credit was available against purchases and output tax was to be calculated against sales tax liability. The contention of the DO is not acceptable as the fact remained that

in terms of provisions under Section 19 ibid read with conditions under the PGST (D&E) Rules, the element of tax paid or payable along with notional output tax liability shall form part of the quantum of exemption in the case of exempted unit. No reply was furnished by the DO, Amritsar-1.

We reported the matter to the Government (February 2010); the reply is awaited (October 2010).

2.13.1 Short levy of tax due to incorrect deduction from turnover

AETC, Ludhiana-II and AETC, Gurdaspur

Section 5(1-A) of the PGST Act provides that in the case of a dealer who brings goods (which are taxable at the first stage of sale in the State of Punjab) from outside the State, are liable to tax when such dealer sells those goods for the first time within the State of Punjab.

(a) We found (between January 2007 and May 2009) that while finalising the assessment of two dealers engaged in the sale of auto parts and duplex board for the years 2001-02 to 2004-05 (assessed during February 2007 and December 2008), the AA erroneously allowed deduction of ₹ 92.16 lakh towards sales of auto parts and duplex board sold to the registered dealers in the state against production of declaration forms. Since the auto parts and duplex board were taxable at the first stage of sale, the deduction allowed against the declaration forms was not correct. This mistake resulted in non-levy of tax of ₹ 6.73 lakh.

AETC, Jalandhar-I

As per condition (5-A) of the PGST (D&E) Rules saved under the PVAT Act, a taxable person shall be entitled to deduct from his turnover the value of the goods purchased from the exempted electronic units provided the goods so purchased are used in the manufacturing of taxable goods or are sold to a taxable person or any other person within the State or are sold in the course of inter-state trade or commerce. He shall pay tax only on the value addition at the prevalent rate of tax.

(a) We found (July 2009) that a dealer had in his VAT return for the year 2006-07 claimed deduction of ₹ 8.65 crore from his gross turnover on the ground that he had made purchases from an exempted electronic unit. On examination of VAT-20 return with the list of his purchases, we found that the dealer was not entitled to the deduction of ₹ 4.02 crore as he had made purchases from an electronic unit named M/s L.G. Electronics Pvt. Ltd. which is not an exempted unit. This mistake to claim inadmissible deduction of ₹ 4.02 crore resulted in loss of revenue of ₹ 50.27 lakh.

We reported the matter to the Department and the Government (March 2010); their replies are awaited (October 2010).

2.13.2 Short computation of turnover

Gross turnover as defined under the PGST Act/PVAT Act, includes the aggregate of sales and purchases actually made by any dealer during the given period. Further, the return as defined in the PVAT Act means a true and correct account of business pertaining to the return period in the prescribed form.

(a) In the offices of three AETCs¹⁷, we found that two dealers in their self assessment return under PVAT Act and two assessing authorities¹⁸ while finalising the assessment under the PGST Act for the years 2004-05 to 2006-07, had wrongly computed the gross sales and purchases as ₹ 17.64 crore and ₹ 94.94 crore instead of ₹ 21.82 crore and ₹ 92.89 crore as depicted in the trading account respectively.

AETC, Patiala

(b) We found in June 2009 that a dealer engaged in the business of work contract, in his self assessment annual return for the year 2006-07 showed the gross receipt as ₹ 1.60 crore instead of ₹ 2.33 crore mentioned in the TDS certificates issued by the contractees. This discrepancy resulted in short computation of turnover of ₹ 72.96 lakh.

The discrepancies in the return/accounts figures regarding short computation of turnover, need to be reconciled for necessary action by the department.

We reported the matter to the Department and the Government (between October 2009 and March 2010); their replies are awaited (October 2010).

¹⁷ Ludhiana-II (one dealer), Mohali (one dealer) and Muktsar (Two dealers).

¹⁸ Ludhiana-II and Muktsar.