

Chapter VII

Effectiveness of internal controls

7.1 Introduction

Internal control is an integral process that is effected by an entity's management and personnel and is designed to address risks and to provide reasonable assurance that in pursuit of the entity's mission, the following general objectives are being achieved:

- executing orderly, ethical, economical, efficient and effective operations;
- fulfilling accountability obligations ;
- complying with applicable laws and regulations ;
- safeguarding resources against loss, misuse and damage.¹⁷

7.2 Result of Audit

During the course of examination of records, we came across several instances in areas such as internal audit, scrutiny, deficiencies in the prescribed Manual which suggest that the department should look into the adequacy of extant systems and procedures. We communicated these observations to the Ministry through 94 draft audit paragraphs having financial implication of ₹ 179.69 crore. The Ministry/Department accepted (December 2014) the audit observations in 93 draft audit paragraphs having financial implication of ₹ 178.65 crore of which ₹ 57.12 crore had been recovered. Out of above 93 paras in 75 paras the Ministry/Department initiated/completed corrective action having financial implication of ₹ 145.43 crore. We have furnished the details of these paragraphs in Appendix III. The objections are covered under three major headings:

Scrutiny of returns

Internal audit of assesseees

Other Issues

7.3 Inadequate scrutiny of returns

We came across six instances while examining ST-3 returns at ranges where we observed that liability to pay tax escaped the notice of the authorities due to inadequate scrutiny of returns.

¹⁷ INTOSAI GOV 9100 – Guidelines for Internal Control Standards for the Public Sector

7.3.1 Service Tax collected but not deposited into Government Account

Section 68 of the Finance Act, 1994, provides that every person providing any taxable service shall pay Service Tax at the rate prescribed. Rule 6 of the Service Tax Rules, 1994, stipulates that Service Tax shall be paid to the credit of the Central Government by the 6th day of the month, if the duty is deposited through internet banking or by the 5th day of the month in any other case, immediately following the calendar month in which the payments are received. If the assessee fails to credit the tax or any part thereof to the account of the Central Government within the period prescribed, he shall pay simple interest at prescribed rates under Section 75 of the Finance Act, 1994.

During the scrutiny of ST-3 returns in Central Excise and Service Tax Range, Behror in Jaipur-I Commissionerate on ACES system and cross verification from the records of service receivers, CERA noticed that five service providers had provided service of manpower supply and collected Service Tax amounting ₹ 71.66 lakh from two service receivers during 2011-12 and 2012-13. These five service providers either did not file ST-3 returns for the relevant period or filed nil return. Therefore, Service Tax of ₹ 71.66 lakh needs to be recovered from these service providers alongwith interest chargeable under Section 75 and penalty under Section 76 and 77 of the Finance Act, 1994.

When we pointed this out (February 2014), the Commissionerate replied (May 2014) that these five service providers had made partial Service Tax payment for ₹ 40.71 lakh and action for recovery of the differential outstanding dues of Service Tax was being initiated by issuing demand-cum-show cause notices against all the defaulters. The Commissionerate further stated that two assesseees could not file ST-3 return for 2011-12 and 2012-13 as their registration numbers are shown as surrendered on ACES.

The Commissionerate's reply indicates the need to set in place a mechanism to cross-check data relating to surrendered registrations with remittances reaching the Government Account.

We await the Ministry's response (December 2014).

7.3.2 Non-detection of assessee's non-compliance with Cenvat Credit Rules, 2004

As per Para 1.2.1.1 of Manual for Scrutiny of Service Tax Returns, 2009, the purpose of preliminary scrutiny is to ensure inter alia timely submission of return, timely payment of dues. As per Para 1.2B of the Service Tax Return Scrutiny Manual, preliminary scrutiny is to be conducted in respect of all returns. Annexure 2.1 enumerates the checklist for preliminary scrutiny of returns which inter alia specifies at Sr. 14(a) that the department is expected to verify whether the conditions of Rule 6(3) of Cenvat Credit Rules, 2004 are prima facie satisfied.

Rule 6(3) of Cenvat Credit Rules, 2004, provides that the provider of output service, opting not to maintain separate accounts shall follow either of the following options, (i) the provider of output service shall pay an amount equal to 5 per cent (with effect from April 2011 to March 2012) and 6 per cent (with effect from April 2012) of the value of exempted services; or (ii) pay an amount equivalent to the Cenvat credit attributable to inputs and input services used in or in relation to the manufacture of exempted goods or for provision of exempted services.

Scrutiny of ST-3 Returns of Division III under Service Tax-I, Mumbai Commissionerate revealed that M/s National Securities Depository Ltd. (NSDL) provided taxable as well as exempted services during the period October 2011 to March 2012. The assessee had not exercised any option in contravention of the provisions of Rule 6 *ibid*. The value of exempted services for the aforesaid period amounted to ₹ 68.93 lakh on which the assessee did not reverse attributable Cenvat credit which was recoverable alongwith interest. It was observed that preliminary scrutiny of these returns was not conducted by the range.

When we pointed this out (February 2013), the Ministry stated (November 2014) that the assessee had discharged total tax liability by reversing the Cenvat credit of ₹ 14.62 lakh along with interest of ₹ 6.76 lakh for the period from April 2010 to June 2012. The reply of the Ministry is silent on the failure of the range to carry out the preliminary scrutiny of the returns.

7.4 Internal Audit of assessees

The three important prongs of the compliance verification system adopted by the department comprise returns' scrutiny, audit, and anti-evasion. Compliance verification through audit entails conduct of audit at assessee premises by following prescribed procedures including selection of assessee units based on risk parameters and scrutiny of records of the assessee to ascertain the level of compliance with the prescribed rules and regulations.

Internal Audit is empowered under the Service Tax Rules, 1994, to access the records of the assessee at their registered premises. Every Commissionerate has, within its Internal Audit section, an Audit cell, manned by an Assistant/Deputy Commissioner and Auditors and headed by an Additional/Joint Commissioner. The Audit cell is responsible for planning, monitoring and evaluating the audits conducted. Audit parties consisting of Superintendents and Inspectors carry out the audit at assessee premises in accordance with the Audit Plan and as per the procedures outlined in the Service Tax Audit Manual, 2011.

We attempted to check the adequacy of coverage of assessee as well as the quality of audits undertaken by the internal audit parties by auditing a sample of assessee falling under one of the following two categories a) already audited by a departmental audit party and b) due for audit but not covered by departmental audit at the time of audit by CERA. We noticed cases involving Service Tax implication of ₹ 32.70 crore which are discussed in the following paragraphs. We communicated these observations to the Ministry through 16 draft audit paragraphs, the Ministry accepted the audit objection to the extent of revenue involved in four cases and we are awaiting the Ministry's response in remaining cases.

7.4.1 During the course of CERA's examination of records in selected assessee premises already covered by internal audit, we came across certain instances where audit parties of the Commissionerate had omitted to point out certain significant cases of non-compliance by assessee.

7.4.1.1 Non-payment of Service Tax

As per clause 31 of Section 65 of the Finance Act, 1994, (as applicable prior to 1 July 2012), "Consulting Engineer" means any professionally qualified engineer or engineering firm who either directly or indirectly renders any advice, consultancy on technical matter in any manner to a client in any one or more disciplines of engineering but not in the discipline of computer hardware engineering or computer software work.

Further, the CBEC vide its Circular dated 4 July 1997 has clarified the scope of the service of a consultant, which shall include the service of construction, supervision and project management. CBEC also clarified vide its Circular dated 6 May 2011 that services of architect and consulting engineer hired in relation to construction of roads, tunnels and bridges etc. will not be exempted from levy of Service Tax.

M/s National Hydro-electric Power Corporation (NHPC) Ltd., in Patna Commissionerate, was entrusted with the work of construction, supervision and project management of road projects in Bihar under the Prime Minister

Gram Sadak Yojna (PMGSY) and for this work, the assessee was to be paid consultancy fee at the rate of 10 per cent of the total project cost. As the work of construction, supervision and project management is covered under the definition of consulting engineering services, the service provided by the assessee was a taxable service. The assessee received ₹ 96.89 crore during 2008-09 to 2011-12 as consultation fees, but Service Tax amounting to ₹ 10.31 crore was not paid.

Internal audit, though carried out for the period upto 2009-10, had not pointed out the lapse which was subsequently detected by CERA.

When we pointed this out (January 2013), the Ministry stated (November 2014) that the show cause notice issued was adjudicated vide order-in-original dated 13 June 2014 confirming the demand of ₹ 10.31 crore. The assessee had paid the Service Tax amount alongwith interest of ₹ 5.35 crore and penalty of ₹ 2.58 crore. The reply of the Ministry is silent on the failure of internal audit party to detect the lapse.

7.4.1.2 Non-payment of Service Tax

Rule 6 (1A) of the Service Tax Rules, 1994, provides that every person liable to pay Service Tax, may, on his own volition, pay an amount as Service Tax in advance, to the credit of the Central Government and adjust the amount so paid against the Service Tax which he is liable to pay for the subsequent period.

Provided that the assessee shall,-

- (i) intimate the details of the amount of Service Tax paid in advance, to the jurisdictional Superintendent of Central Excise within a period of fifteen days from the date of such payment; and
- (ii) indicate the details of the advance payment made, and its adjustment, if any in the subsequent return to be filed under Section 70 of the Act.

Gujarat Pipavav Port Ltd. in Bhavnagar Commissionerate, was liable to pay Service Tax of ₹ 3.67 crore for dredging service rendered during the month of July 2009. As seen from ST3 return for July 2009, the assessee paid ₹ 60.87 lakh through PLA and balance amount of ₹ 3.07 crore was stated to have been adjusted against advance Service Tax paid in earlier period. However, we did not find any advance payment in ST-3 returns for the period from April 2007 to June 2009. Further, no intimation or proof of advance payment of Service Tax was made available to Audit. Thus, the assessee failed to pay Service Tax of ₹ 3.07 crore.

When we pointed this out (March 2013), the Commissionerate accepted the audit observation (January 2014) and intimated that issuance of show cause notice was under process. Further development is awaited (May 2014).

We await the Ministry's response (December 2014).

7.4.1.3 Non-payment of interest on belated payment of Service Tax

As per Section 75 of the Finance Act, 1994, every person liable to pay Service Tax should pay simple interest at the prescribed percentage, in case the Service Tax payable was paid belatedly into the Government account. The rate of interest was 13 per cent per annum upto 31 March 2011 and at 18 per cent per annum thereafter, as per Notifications dated 10 September 2004 and 1 March 2011.

M/s Prestige Estates Projects Ltd., Bengaluru, in Bengaluru Service Tax Commissionerate, had paid Service Tax for the period from October 2010 to March 2012 with delay ranging from 1 day to 38 days. However, the assessee did not pay interest on any of these delayed payments of Service Tax. The interest payable worked out to ₹ 14.28 lakh for the period referred above.

Though the unit was visited by the Internal Audit Party of the Commissionerate during 2012-13, the non-payment of interest was not detected by them and this was also not pointed out in the preliminary scrutiny either. This resulted in this lapse remaining undetected until pointed out by CERA.

When we pointed this out (September 2013), the Ministry replied (September 2014) that the assessee paid (December 2013) ₹ 27.84 lakh towards interest for the period from July 2010 to March 2013. The reply of the Ministry was silent on the failure of the departmental parties to detect the non-payment of interest by the assessee.

7.4.1.4 Non-payment of Service Tax

Rule 3 (b) of the Point of Taxation Rules, 2011 provides that where the person providing the service, receives a payment before the time specified in clause (a) of Rule 3, the point of taxation shall be the time when he receives such payment, to the extent of such payment. The explanation to Rule 3 also states that wherever any advance by whatever name known is received by the service provider towards the provision of taxable service, the point of taxation shall be the date of receipt of each such advance.

M/s. Gujarat Pipavav Port Ltd, in Bhavnagar Commissionerate, provided Port services valued ₹ 317.52 crore against which it received an advance payment of ₹ 103.32 crore between July 2011 and March 2012. Thus, the assessee was liable to pay Service Tax of ₹ 33.77 crore on accrual basis during the

period July 2011 to March 2012. However, the assessee paid Service Tax of ₹ 32.13 crore on receipt basis. This resulted in short payment of Service Tax of ₹ 1.64 crore which is recoverable with applicable interest.

When we pointed this out (March 2013), the Commissionerate (January 2014) accepted the audit objection and stated that SCN is under issue. Further progress is awaited (December 2014).

We await the Ministry's response (December 2014).

7.4.1.5 Short levy of Service Tax due to misclassification

Section 65 of the Finance Act, 1994 (as applicable prior to 1 July 2012), defines 'Erection Commissioning or installation' service to mean any service provided by a commissioning and installation agency, in relation to erection, commissioning or installation of plant, machinery, equipment or structures whether prefabricated or otherwise etc. The service is taxable with effect from 10 September 2004.

Works Contract Service has come under the Service Tax net with effect from 1 June 2007 and means a contract wherein transfer of property in goods involved in the execution of such contract is leviable to tax as sale of goods and such contract is for the purpose of carrying out work as specified under sub-clause (zzzza) of Section 65 of the Finance Act, 1994.

Again as per Service Tax (Determination of Value) Rules, 2006, the value of the taxable service is the 'gross amount' charged for providing such services except value of items as mentioned under rule 6 of the said Rules.

Further, Section 75 of the Act, envisages that, interest at prescribed rate is payable on delayed payment of Service tax.

Thus from the above it follows that if the specified contract is 'works contract' on which VAT/sales tax is payable, the service will be taxable under Works Contract Service. If the contract is a simple service contract (i.e. either no material is involved or even if some material is involved, VAT/sales tax is not payable), the service will be classifiable under respective heads of taxable service.

M/s Steel Products Ltd. (U-II) in Kolkata Service Tax Commissionerate, entered into an agreement with HG Power Transmission SDN-BMD, Selangor, Malaysia for erection of 400 KV D/C Akola-Aurangabad Transmission Line. The scope of the work included erection of towers, testing and commissioning of erected 400 KV D/C transmission line etc. The assessee issued bills to HG Power Transmission for such services and paid Service Tax at the rate of 2 per cent or 4 per cent (as applicable) under works contract service. As the service did not involve transfer of property and no sales tax

was payable or paid on such work, the assessee should have paid Service Tax at the rate of 12 per cent (or as amended) under 'Erection Commissioning or Installation Service'. Thus, misclassification of service resulted in short levy of Service Tax to the tune of ₹ 65.10 lakh during the period October 2007 to March 2009 which was recoverable along with applicable interest.

When we pointed this out (October 2009), the Commissionerate accepted the objection (February 2013). Further, the Commissionerate provided (April 2013) copy of the Show Cause Notice for Service Tax of ₹ 82.93 lakh covering the period from October 2007 to March 2012 along with applicable interest and equal amount of penalty.

The reply of the Ministry is awaited (December 2014).

7.4.1.6 Other cases

We noticed in five other cases, the instances of non-payment/short-payment of Service Tax, irregular availing of Cenvat credit etc. by the assesseees involving revenue of ₹ 88.21 lakh which were not pointed out by the internal audit parties of the department. The Commissionerates accepted the audit observation in all the cases.

We await the Ministry's response (December 2014).

We observe that though internal audit was carried out by the Internal Audit Party of the Commissionerate in all the above cases, the lapse remained undetected until pointed out by CERA.

7.4.2 Inadequacy of Service Tax Audit Manual provisions

As per the Director General of Service Tax's Action Plan circulated to Chief Commissioners on 26 May 2003, field formations were required to obtain information from major assesseees including PSUs and private sector organisations regarding various services being availed by them and to obtain details of such services providers including their addresses. Further, every range officer had to obtain information from major assesseees including PSUs regarding various services being availed by them and to obtain details of such service providers to broaden the tax base. However, there was no such corresponding provision in the Service Tax Audit Manual, 2011, which made it obligatory for the Service Tax Audit parties to collect (during audits at assessee premises) and forward similar details to Internal Audit Cell of Commissionerate/Division/Range concerned.

M/s Tarapore and Company Ltd. in Jamshedpur Commissionerate, engaged in providing mainly telecommunication service etc., paid a sum of ₹ 5.68 crore to 22 Manpower Recruitment agencies during the period from April 2010 to

March 2011, but Service Tax of ₹ 58.50 lakh at the rate 10.30 per cent was not paid by these service providers.

We observed that an internal audit team had conducted audit in M/s Tarapore and Company Ltd. in December 2010 and January 2012 but it had failed to communicate any details about non-fulfilment of liability/provision of service by these service providers to the Commissionerate or the concerned subordinate functionaries which would have facilitated initiation of action against the defaulting service providers.

When we pointed this out (September 2011), the Ministry while accepting the objection reported (December 2014) that in 19 cases show cause notices had been issued and in three cases the assessee deposited Service Tax along with interest. The Ministry further stated that desired changes have been made in the Service Tax Audit Manual, 2011 through insertion of Para No. 7.6.7 in the Manual in November 2014. **Audit is of the view that similar provision should be inserted in Central Excise Audit Manual, 2008 as big manufacturers also availed input services from many service providers who also charged Service Tax from them.**

7.4.3 Inadequate compliance with norms for coverage of mandatory units by internal audit

Para 5.1.2 of the Service Tax Audit Manual, 2011 envisages that service providers paying Service Tax of ₹ 3 crore or more (cash + Cenvat) in a year are to be audited every year mandatorily.

7.4.3.1 Non-payment of Service Tax on JNNURM projects

Service Tax on Construction of Complex service is leviable under sub-section 105(zzzh) of Section 65 of the Finance Act, 1994 (as applicable prior to 1 July 2012) with effect from 16 June 2005 vide notification dated 7 June 2005. Section 65(30a) defines construction of a complex as including construction of a new residential complex or a part thereof, completion and finishing services in relation to residential complex and repair, alteration, renovation or restoration of similar services.

Further, 'residential complex' means any complex comprising of a building or buildings, having more than twelve residential units, a common area and facilities or services such as park, lift parking space etc. vide Section 65(91a) of the Act.

Notification dated 22 June 2010 exempted the services provided to Jawaharlal Nehru National Urban Renewal Mission (JNNURM) and Rajiv Awas Yojana with effect from 1 July 2010.

M/s M.V. Omni Project (I) Ltd. in Ahmedabad Service Tax Commissionerate, was engaged in providing construction of complex service to Ahmedabad Municipal Corporation (AMC), Vadodara Mahanagar Seva Sadan (VMSS-BAP) and Vadodara Mahanagar Seva Sadan-Kisanwadi under JNNURM projects during the year 2007-08 to 2010-11.

During examination of records, we noticed that assessee provided services for construction of housing blocks having more than 12 residential units in each block and received ₹ 70.14 crore (including TDS) for the three projects between October 2007 and May 2010. After abatement of ₹ 41.74 crore, the assessee was liable to pay Service Tax of ₹ 1.86 crore, however the assessee did not pay any Service Tax. This resulted in non-payment of Service Tax of ₹ 1.86 crore on the abated value.

When we pointed this out (June 2011), the Commissionerate intimated (July 2013) that show cause notice issued in this matter (October 2011) was adjudicated (February 2013) confirming the demand of ₹ 1.86 crore.

We await the Ministry's response (December 2014).

7.4.3.2 Non compliance with Point of Taxation Rules

Rule 3 of the Point of Taxation Rules, 2011, as amended vide notification dated 31 March 2011 read with notification dated 27 June 2011 provides that unless otherwise provided, 'point of taxation' with effect from 1 July 2011 shall be the time when the invoice for the service provided or to be provided is issued. Further Section 75 of the Finance Act, 1994, provides that every person who fails to credit the tax or any part thereof to the account of the Central Government within the period prescribed shall pay simple interest at such rate as is for the time fixed by the Central Government.

M/s. Emirates in Division I of Mumbai ST-I Commissionerate, is registered under the category of Transport of passengers embarking on domestic/international journey by air services, Cargo Handling Services, Transport of Goods by air services etc. Audit scrutiny revealed that the assessee was selling tickets through IATA (International Air Transport Association) accredited agents and was receiving the sales report through IATA Billing Settlement Plan (BSP). As per BSP, the assessee was receiving sales report on fortnightly basis i.e. sales report for the first fortnight of a month was received in the last week of the same month and for the second fortnight, it was received in the first week of the next month. Thus, the amount was credited to the assessee's account in the month following the sales month. Further, scrutiny of details for working of Service Tax and ST-3 Return from July 2011 to March 2012 revealed that the assessee was paying Service Tax on receipt basis i.e. only after receiving the amount from its

agents, without adhering to the provisions of Point of Taxation Rules, 2011 which resulted in delayed payment of Service Tax on which interest amounting to ₹ 1.59 crore needs to be recovered.

When we pointed this out (March 2013), the Commissionerate intimated (April 2013) that the objection is prima-facie admitted. The Commissionerate stated that they are aware of such issues and the internal audit wing of the Commissionerate was conducting the audit of the said assessee during April 2013.

We observe that though the issue was in the knowledge of the Commissionerate, it had not pointed out the same through any of the compliance verification methods such as scrutiny or internal audit (though the assessee was a Category A unit) until CERA pointed out the objection. No Show Cause Notice was issued to the assessee as required under Section 73 of the Finance Act, 1994 (as amended). The Commissionerate did not take any action to recover the interest amount until Audit pointed out the lapse.

We await the Ministry's response (December 2014).

7.4.3.3 Short Payment of Service Tax due to undervaluation

As per Para 14.5 of CBEC's Circular F. No. B1/6/2005-TRU, dated 27 July 2005, if a contract for construction of commercial complex is a single contract and the construction of roads is not recognised as a separate activity as per the contract, then Service Tax would be leviable on the gross amount charged for construction including the value of construction of road.

Again, as per Para 14.6 of the above cited Circular, when services provided under a contract consist of a number of different elements, a view has to be taken on the basis of the facts and circumstances of each case as to whether the service provider has made a single overall supply or a supply of different services which are to be treated differently.

Further, Section 75 of the Finance Act, 1994, envisages that interest at prescribed rate is payable on delayed payment of Service Tax.

M/s Subhash Project & Marketing Ltd. (SPML) in Kolkata Service Tax Commissionerate, was engaged in providing different taxable services like 'Construction Services', 'Erection, Commissioning and Installation Services' and 'Maintenance and Repair Services'. We observed that The West Bengal Power Development Corporation Ltd. (WBPDCL) had awarded a contract for turnkey package for Erection and Services of Raw Water make-up system from Panchet Dam reservoir to Santaldih TPS (OC-125) to M/s SPML. The contract price for construction of such project was ₹ 33.13 crore. Scrutiny of the price break-up of the agreement revealed that the civil part of the

contract was bifurcated into separate units, such as residential quarters, road crossing and pipe bridge, service road etc. We further noticed that the assessee treated the above services as exempted and did not pay Service Tax on the amount received through RA Bills. Further scrutiny of the Billing and Collection details revealed that the assessee had received the amount of ₹ 5.33 crore for the year 2007-08 and 2008-09 for the said services. As the above contract was a single contract, the construction of road, bridges etc. are not recognizable as a separate activity. Therefore, as per the above mentioned provisions, Service Tax was leviable on the gross amount charged for the contract including the value of the construction of road, bridges etc. by the assessee under the above contract. This resulted in short payment of Service Tax to the tune of ₹ 65.87 lakh including cess due to undervaluation to the extent of ₹ 5.33 crore during 2007-08 and 2008-09.

When we pointed this out (March 2010), the Commissionerate accepted the issue and reported (April 2014) that demand has been confirmed along with applicable interest and penalty.

We await the Ministry's response (December 2014).

7.4.3.4 Non-deposit of Service Tax

Rule 6 (1) (i) of Service Tax Rules, 1994 provides that Service Tax shall be paid to the credit of the Central Government account by the 6th day of the succeeding month, if the duty is deposited electronically through internet banking and by 5th day of the succeeding month in any other case. Further, as per Section 73A of Finance Act, 1994, as amended, any person who is liable to pay Service Tax and has collected any amount in any manner as representing Service Tax, such person shall forthwith pay the amount so collected to the credit of the Central Government.

We noticed that M/s Ores India Private Ltd, Manoharpur, West Singhbhum, in Jamshedpur Commissionerate, realised an amount of ₹ 86.10 lakh as Service Tax during the period October 2010 to March 2011 from M/s IISCO. The assessee adjusted a sum of ₹ 33.68 lakh as input credit, but did not deposit ₹ 52.43 lakh against the amount realised during the period October 2010 to March 2011 as required under provisions of Finance Act and rule 6(1) *ibid*.

When we pointed this out (October 2011), the Ministry accepted the audit observation and stated (September 2014) that the assessee has deposited Service Tax of ₹ 61.54 lakh including interest of ₹ 8.50 lakh (during November 2011 to January 2012). Reply of the Ministry was silent on non conducting of Internal Audit of the assessee.

7.4.3.5 Non levy of interest on delayed payment of Service Tax

Rule 7 of Point of Taxation Rules, 2011 as amended with effect from 1 April 2011 provides that point of taxation when Service Tax is payable under reverse charge mechanism shall be the date on which payment is made to service provider, if the payment for such service is made within six months from date of invoice. However, if the payment for such service is not made within six months from date of invoice, the point of taxation will be determined as if Rule 7 does not exist and will be determined under Rule 3, 4, 5, 8 or 8A as applicable. Interest will also be applicable in this case.

Further, Rule 3 (a) of Point of Taxation Rules *ibid*, provides that the point of taxation shall be the time when the invoice is issued if invoice is issued within 30 days from the date of completion of service.

Again, Rule 6 (1) of Service Tax Rules, as amended provides that Service Tax shall be paid to the credit of Government by 5th /6th of the month/quarter immediately following the month/quarter in which service is deemed to be provided. Failure to pay Service Tax by the due date attracts interest at the rate of 18 per cent per annum for delayed payment.

M/s Jamshedpur Continuous Annealing and Processing Company Pvt. Ltd. in Jamshedpur Commissionerate made an agreement for license and technology transfer for continuous annealing and processing line of joint venture with M/s Nippon Steel Corporation, Japan and hired its services on payment of ₹ 31.62 crore on which, the assessee was liable to pay Service Tax under reverse charge mechanism as per Rule 2(1) (d) (iv) of Service Tax Rules, 1994. It was further noticed that the bills were raised by the foreign-service provider in May and August 2012 after the completion of work (within the prescribed period) but payment of Service Tax was made in March 2013 after six months of raising the invoice. Thus, the assessee was liable to pay interest of ₹ 40.02 lakh for delayed payment of Service Tax under Rule 3 (a) of Point of Taxation Rules as point of taxation arose when invoices were issued.

When we pointed this out (July 2013), the Commissionerate accepted the audit observation and stated (January 2014) that the assessee has deposited the interest of ₹ 40.02 lakh.

We await the Ministry's response (December 2014).

Although, the unit was to be audited annually by the Internal Audit wing of the department as per prescribed norms in all the cases, no internal audit was conducted. This resulted in this lapse remaining undetected until pointed out by CERA.

7.5 Other Issue

Periodical show cause notice not issued

As per Section 73 of Finance Act, 1994, in normal course show cause notice is to be issued within one year (with effect from 28th May 2012, '18 months') and in case of fraud, Collusion, Wilful misstatement, suppression of facts etc. with intent to evade duty, within a period of five years from the relevant date. Further as per Section 73(6)(b) of the Act, relevant date inter alia means where no periodical returns as aforesaid filed, the last date on which such returns to be filed under the said rules. The Supreme Court in the case M/s Nizam Sugar Ltd. Vs Commissioner of Central Excise – 2006 (197) ELT 465 (SC) has held that the extended period of five years was not available to the department for the subsequent show cause notice which was issued based on the same set of facts of the earlier show cause notice as the full facts were known to the Department and hence suppression cannot be alleged.

Audit of SCN and adjudication records maintained in Raigad Commissionerate revealed that the Commissionerate had issued a show cause notice to the assessee M/s Hanil Era Textiles Ltd, an EOU, in October 2010 demanding ₹ 3.82 crore due to non payment of Service Tax under reverse charge basis, for the period 2005-06 to 2008-09 for service categories viz. Business Auxiliary Services, Storage and Warehousing Services and Goods Transport Services. The show cause notice was adjudicated vide Order In Original dated 30th March 2012.

However, the Commissionerate had neither covered the period of 2009-10 in the first show cause notice nor had issued a periodical show cause notice for the period 2009-10 within the stipulated period of one year.


When we pointed this out (July 2012), the Commissionerate (December 2013) stated that a draft show cause cum demand notice amounting ₹ 63.13 lakh for non-payment of Service Tax for the period of April 2009 to March 2011 was submitted to the Adjudication Section in June 2013 for issue. The last date for issuance of SCN was stated to be 24 October 2014.

However, the process of issuance of periodic show cause notice for 2009-11 period applying provisions for extended period after a lapse of four years is irregular in view of the above mentioned decision of Supreme Court in the case of M/s Nizam Sugar Ltd. Vs Commissioner of Central Excise, Andhra Pradesh. Thus, an amount of ₹ 63.13 lakh has got time-barred due to improper monitoring of the need for issue of periodic show cause notices

with respect to ongoing adjudication cases. Even going by Section 73 (6) (b), where no periodical returns are filed, relevant date would be the last date on which such returns were to be filed, hence the prescribed period had lapsed in this case.


We await the Ministry's response (December 2014).

New Delhi
Dated: 20 March 2015


(SANJEEV GOYAL)
Principal Director (Central Excise)

Countersigned

New Delhi
Dated: 21 March 2015


(SHASHI KANT SHARMA)
Comptroller and Auditor General of India