

Chapter 4 : Pre and Post VCES tax administration

The circumstances leading up to the necessity of introducing the VCES reflect upon failures on part of the department in carrying out compliance verification. The penal provisions for non-registration, non/short payment of tax, non-filing of returns etc. and the parameters for selection of assessee units for internal audit are available in public domain. But, as these systems in place are not observed and the penal provisions are not sufficiently deterrent in nature, the perceived risk of detection of non-compliance is low. This view of audit is corroborated by the fact that only 66,072 existing as well as new registrants declared tax dues amounting to ₹ 7,750 crore under VCES as against 10,00,000 non/stop filers when the Scheme was announced.

One time amnesty Scheme like VCES can be a real one time solution for the problem it sought to redress only if the tax systems are strengthened and follow up mechanism is made stringent. But, we observed that during post-VCES period, the department failed to initiate stringent action against the stop-filers/non-filers, who had enjoyed the immunity provisions under VCES and again reverted back to the habit of non-filing of returns.

4.1 Pre VCES tax administration

Identification of stop filers or non-filers through ACES and conduct of internal audit of the assessee units are two important processes available with tax administration to test check compliance by assessees to the existing rules. Declarants under VCES should have come into tax net if department followed these processes as discussed below:-

4.1.1 Identifying Non-compliance by Registered Service Providers

We observed from the data received from 20 Commissionerates out of 35 selected Commissionerates that out of 24,166 declarations for an amount of ₹ 3,031.30 crore, 5,381 declarations involving ₹ 328.26 crore were new registrants. Thus, only around 22 per cent in terms of number and 11 per cent in terms of amount of the declarations related to new registrations.

From the above, it was evident that disclosure of large amount of 89 per cent of unaccounted income under VCES was by existing registrants, which was symptomatic of the malaise of poor tax administration over the years that enabled concealment of taxable income by the existing assessees.

This was brought to the notice of Ministry (April 2016) and Ministry stated (June 2016) that the scheme was also for the existing assessees, who were either stop filer or non-filers and attributed increasing number of defaulters

to substantial increase in service tax assesses without a corresponding increase in the number of tax collectors. They felt that VCES was a step to give a chance to defaulters for tax compliance as well as being a regular filer of returns by giving some incentives.

4.1.2 Inadequate or inefficient internal audit by department

Internal audit is one of the main compliance verification mechanism in the department, which involves selection of assessee units on the basis of risk parameters and scrutiny of records of the assessee to ascertain the level of compliance with the prescribed rules and regulations. As per paragraph 5.1.2 of Service Tax Audit Manual, 2011 tax payer whose annual service tax payment (including Cash and Cenvat) was rupees three crore or more in the preceding financial year would be subjected to mandatory audit each year.

We noticed that in case of 26 declarants scrutinised by audit in eight Commissionerates involving tax dues of ₹ 23.74 crore lack of proper monitoring/lapse on the part of internal audit in initiating timely action enabled the assessees to come under VCES and disclose large amount of defaulted tax dues. It resulted not only in postponement of revenue flow into Government account to that extent but also in extending undue benefit to the declarants by way of immunity from penal provisions.

When we pointed this out (between October 2015 and January 2016) the field formations of Ministry stated in nine cases (May 2016) that post restructuring of the department, the parameter on selecting units for conducting audit rest with DG Audit only. Hence, the question of inadequate or inefficient internal audit by department was not relevant. In four cases it stated that due to shortage of staff and work pressure certain issues might have escaped from audit. In 13 cases reply was awaited.

The reply of the Ministry was awaited.

A few illustrative cases are given below:-

4.1.2.1 An assessee in Hyderabad ST Commissionerate, paid service tax exceeding rupees three crore each year from 2010-11 to 2013-14 and therefore was to be mandatorily covered by internal audit every year. However, we observed that the assessee unit was last audited during October 2007, for the period up to August 2007 and thereafter no audit was conducted till April 2013.

The assessee had rendered sponsorship services in connection with Federation International De Football Association (FIFA) and the service tax payable on the said services for the period from 1 July 2010 to 31 March

2012 worked out to ₹ 15.69 crore and the same had not been discharged by the assessee.

Consequent on amalgamation of the assessee unit with another assessee declared (September 2013) tax dues of ₹ 15.69 crore not paid by the assessee. Thus, non-coverage of the assessee unit by internal audit each year from 2010-11 to 2012-13 enabled the assessee to conceal tax dues payable and subsequently come under VCES, thereby getting undue benefit of waiver of interest and penalty.

When we pointed this out (January 2016), the Ministry stated (May 2016) that the scope of observation was beyond the jurisdiction of VCES Scheme. It further stated that internal audit operates under certain parameters and slippage might have occurred during the same.

4.1.2.2 An assessee in Rajkot Commissionerate declared (December 2013) tax dues of ₹ 4.42 crore towards GTA, manpower recruitment agency service, etc., for the period from April 2011 to September 2012. We observed that an internal audit was conducted on the assessee unit on 26 December 2012 for the period from April 2011 to March 2012 and spot recovery of an amount of ₹ 14.77 lakh was made against the assessee for non-payment of interest on late payment of service tax. However, failure on the part on internal audit to detect non-payment of service tax of ₹ 4.42 crore enabled the assessee to come under VCES and get immunity from penal provisions.

This was brought to the notice of the department/Ministry in October 2015, the reply of the department/Ministry was awaited (May 2016).

4.1.2.3 An assessee in Mumbai-VI ST Commissionerate, declared (November 2013) tax dues of ₹ 3.76 crore towards construction of complex service for the period December 2010 to March 2012. We observed that the department had initiated an enquiry against the declarant for ascertaining service tax liability in respect of services under health club and fitness centre, mandap keeper, beauty treatment service, business exhibition service and rent-a-cab service. The enquiry culminated into issuance of SCN (December 2012) which was adjudicated in March 2013. During the course of enquiry, service tax returns filed and balance sheets for the years 2006-07 to 2010-11 were called for. Neither the SCN nor the OIO determined any service tax liability in respect of Construction of Complex Service.

We further observed that out of the total tax dues of ₹ 3.76 crore declared, an amount of ₹ 1.36 crore pertained to the period from December 2010 to March 2011 relating to construction of complex service. Though the balance sheet for the period 2010-11 was available at the time of initiation of enquiry, the department failed to detect non-payment of service tax of ₹ 1.36 crore,

which enabled the assessee to come under VCES and declare tax dues of ₹ 3.76 crore, which also included the amount of ₹ 1.36 crore, thereby extending undue benefit to the assessee by way of interest and penalty.

When we pointed this out (December 2015), the Ministry stated (May 2016) that it was merely a technical issue.

The reply of the Ministry was not acceptable since the case was highlighted to show how inadequate review of balance sheet by internal audit resulted into undue benefit to the declarant by way of immunity from penalty and interest.

4.2 Filing of truthful declarations

The Finance Minister, through the Scheme, hoped to appeal to non-filers/stop filers to voluntarily make truthful declaration of tax dues. It is, therefore, a natural expectation that such Schemes should be designed in a manner to make it difficult for the declarant to be untruthful.

Audit attempted to examine the truthfulness of the declarations in Chennai-I ST and Kochi Commissionerates by cross-verifying the quantum of tax dues declared with the details available with other authorities like Income Tax Department, Commercial Taxes Department and Registrar of Companies. We observed in eight cases in Chennai-I ST and Kochi Commissionerates that the tax dues declared under VCES were short by of ₹ 4.35 crore, in comparison with the data available with the other authorities.

Ministry stated (June 2016) that treating declarants on par with any other assessee, regular monitoring was being done and necessary action initiated.

A few illustrative cases are given below:-

(a) An assessee in Chennai-I ST Commissionerate, declared (September 2013) tax dues of ₹ 1.05 crore towards maintenance and repair services rendered by them for the period from November 2007 to March 2008. The VCES declaration was accepted and VCES-3 issued in February 2015.

We observed that the declarant had taken service tax registration on 28 August 2013 and as such they did not file any ST-3 returns, before submitting VCES application. Verification of annual accounts of the assessee obtained from the Registrar of Companies revealed that the assessee had income of ₹ 28.91 crore and ₹ 8.28 crore, under job receipts, for the years 2008-09 and 2009-10 respectively. However, tax dues on these income related to services were not declared by the assessee under VCES.

When we pointed this out (January 2016) the Ministry stated (May 2016) that the Finance Act, 2013 did not prescribe any financial documents to be submitted to the department to prove the veracity of declaration.

(b) An assessee in Chennai-I ST Commissionerate declared (December 2013) tax dues of ₹ 25.88 lakh under VCES in respect of works contracts service for the years 2010-11 and 2012-13. Verification of VAT returns filed by the assessee with the Commercial Taxes Department, Tamil Nadu, revealed that the assessee reported taxable turnover of ₹ 7.61 crore in his VAT returns towards value of material transferred during the execution of works contracts for the year 2011-12. It was evident from this disclosure that the assessee executed works contracts during the year 2011-12 but failed to declare corresponding service income under VCES.

When we pointed this out (January 2016), the Ministry stated (May 2016) that VCES Scheme did not envisage investigation by the DA.

(c) An assessee in Kochi Commissionerate, declared (December 2013) tax dues of ₹ 13.07 lakh for the period from October 2007 to December 2012 under VCES towards business auxiliary service and goods transport agency service and VCES-3 was issued in August 2014.

The assessee declared “Nil” income for the years 2009-10 and 2011-12 under works contract service. However, on verification with the returns (TIN 32151046307) filed with the Commercial Tax Office for the period 2009-10 and 2010-11 and the disclosure of the assessee for 2011-12, audit observed taxable service under Works Contract during the years 2009-10 to 2011-12 was ₹ 17.92 crore. However, tax dues on this income was not declared by the assessee under VCES.

This was brought to the notice of the department/Ministry in January 2016; the reply of the department/Ministry was awaited (May 2016).

This drives home the need to put a system in place, through use of technology and integration of data bases, which would make it difficult for declaration/assesseees to be untruthful.

4.3 Post VCES tax administration

Any amnesty Scheme would be called a success only when the beneficiaries of such Schemes pay the declared tax dues and continue to pay taxes and comply with other statutory duties during the period subsequent to the period covered under the Scheme.

Ministry, while agreeing on certain points made by audit and accepting that specific instances of failures or bottlenecks might have remained at the Commissionerate level, stated that the larger success achieved by the scheme cannot be denied plainly. They stated that Commissionerates have their own mechanism of scrutiny of returns, anti-evasion and audit to ensure compliance and that this fact cannot be negated that the assesses base in Service Tax is huge and to tap the entire assesses pool through one single scheme is not possible.

Audit only made a limited point based on facts regarding tax administration that came to notice post-VCES as discussed below:

4.3.1 We analysed the returns due to be filed by the declarants during the post-VCES period (i.e. April 2013 to March 2015) in 15 Commissionerates where data was made available. We observed in 4,209 cases in these Commissionerates, only 13,003 returns filed by declarants as against 21,045 returns¹³ due to be filed. This accounted for 62 per cent of the returns due for filing. Action taken by the department against the non-filers was not forthcoming from the records.

The very purpose of the Scheme was to enable an errant tax defaulter to return to the path of honesty. We noticed that many beneficiaries failed to adopt the path of rectitude and civic responsibility, post VCES period, calling to question the success of the Scheme.

The department had failed to initiate stringent action against the stop-filers/non-filers, who had enjoyed the immunity provisions under VCES and again reverted back to the habit of non-filing of returns.

When we pointed this out (between October and December 2015) the Ministry stated (May 2016) that the action was initiated in 12 Commissionerates. Reply was awaited in respect of the remaining three Commissionerates.

4.3.2 The department did not initiate any action to recover the balance of the declared tax dues or to levy applicable interest and penalty in respect of the rejected cases. The total tax dues involved in the 78 rejected cases in 11 Commissionerates amounted to ₹ 23.02 crore.

When we pointed this out (between October 2015 and January 2016) the Ministry stated (May 2016) that the remedial action was initiated against the declarants.

¹³ At five half yearly returns due per assessee