

CHAPTER-II GST, TAXES/ VAT ON SALES, TRADE, ETC.

2.1 Tax Administration

Kerala General Sales Tax (KGST)/ Kerala Value Added Tax (KVAT)/ Goods and Services Tax (GST) laws and rules made thereunder are administered at the Government level by the Secretary, Taxes. The Commissioner, SGST Department is the head of the SGST Department who is assisted by Additional Commissioner, Joint Commissioners (JCs), Deputy Commissioners (DCs), Assistant Commissioners (ACs) and State Tax Officers (STOs). The assessment, levy and collection of tax are done by ACs and STOs.

KGST is leviable on sale of ganja, opium, foreign liquor and certain petroleum products. KVAT was leviable on the Intra-State sale of remaining commodities and Central Sales Tax (CST) on Inter-State sales. GST came into effect from 01 July 2017 subsuming VAT, CST etc.

2.2 Internal Audit

The Internal Audit Wing (IAW) of the SGST Department is monitored by the Commissioner. The effective functional unit of IAW for the year 2019-20 and 2020-21 was one Joint Commissioner assisted by 10 Deputy Commissioners, one Assistant Commissioner and 16 State Tax Officers. No specific training has been imparted to the officers of the IAW. During 2019-20, out of the overall outstanding 14,896 paragraphs, only 1,558 paragraphs (10.46 *per cent*) were cleared and during 2020-21, out of the overall outstanding 17,154 paragraphs, only 2,394 (13.96 *per cent*) were cleared. The reason for the low clearance in observations made by IAW, though called for (August 2021) has not been furnished (September 2022).

2.3 Results of Audit

There were 186 auditable units during 2019-20 and 295 auditable units during 2020-21 in the SGST Department. Out of these, Audit selected 106 units for test check during the year 2019-20 and 42 units during the year 2020-21. Test check of the records relating to KVAT/ KGST and CST assessments and connected documents during 2019-21 showed under-assessment of tax and other irregularities in 670 cases relating to non/ short levy of tax/ interest, irregular allowance of input tax credit, escape of turnover from assessment, misclassification and other lapses amounting to ₹471.33 crore. These cases are only illustrative as these are based on the test-check of records. As this was test audit in the test-checked cases and the audit observation is of a nature that may reflect in other cases not covered in test audit, the Department may therefore, like to internally examine the position in rest of the units with a view to ensure that the instances of non-compliance are taken care of by taking remedial measures, and may also fix responsibility for the lapses in all such

cases. Audit pointed out some of the similar omissions in the earlier years also. Not only do these irregularities persist, but they also remain undetected till the next audit is conducted. Under-assessment of tax and other irregularities involving ₹483.23 crore in 672 cases which fall under the following categories are given in **Table - 2.1**.

Table - 2.1
Details of under-assessment of tax and other irregularities

(₹ in crore)

| Sl. No. | Categories | Number of cases | Amount |
|--------------|--|-----------------|---------------|
| 1 | Compliance Audit on 'Transitional credits under GST' | 1 | 10.15 |
| 2 | 'Processing of refund claims under GST' | 1 | 1.76 |
| 3 | Short payment of tax due to escape of turnover from assessment | 178 | 127.04 |
| 4 | Short payment of tax due to excess/ irregular availing of input tax credit | 199 | 271.80 |
| 5 | Short payment of tax due to misclassification/ incorrect rate of tax | 88 | 27.34 |
| 6 | Others | 205 | 45.14 |
| Total | | 672 | 483.23 |

During the course of the years 2019-21, the Department accepted under-assessment and other deficiencies amounting to ₹69.08 crore in 642 cases, which were pointed out by Audit. An amount of ₹17.76 crore pointed out in 814 cases were realised during the year.

The Department recovered an amount of ₹0.18 crore under the amnesty scheme⁵ in two cases (₹0.43 crore) pointed out by Audit during 2019-21. A few Audit observations involving ₹63.19 crore are given in the succeeding paragraphs.

⁵ The Government has unveiled an amnesty scheme to settle outstanding tax dues pertaining to the period before the introduction of the GST to clear the backlog of arrear demand by waiving interest/ penalty and giving reduction in tax arrears.

2.4 GST Registrations

2.4.1 Pan-India GST Registrations

The category-wise registrations under GST have been given in **Table - 2.2** below:-

Table - 2.2
Details of registrations

| Category of Registrant | No. of Registrants as on 31 March 2020 | Percentage of total as on 31 March 2020 | No. of Registrants as on 31 March 2021 | Percentage of total as on 31 March 2021 |
|---|--|---|--|---|
| Normal taxpayers | 2,97,897 | 84.03 | 3,01,411 | 84.39 |
| Composition taxpayers | 49,462 | 13.95 | 47,862 | 13.40 |
| Tax Deductors at Source | 6,189 | 1.75 | 6,765 | 1.90 |
| Tax Collectors at Source | 351 | 0.10 | 543 | 0.15 |
| Input Service Distributors | 84 | 0.02 | 81 | 0.02 |
| Others (Casual, NRTP, OIDAR) ⁶ | 536 | 0.15 | 498 | 0.14 |
| Total Registrants | 3,54,519 | 100 | 3,57,160 | 100 |

Source: Details furnished by SGST Department.

The total registrations under GST as on 31 March 2020 and 31 March 2021 were 3.55 lakh and 3.57 lakh respectively of which normal taxpayers accounted for around 84 *per cent* and composition taxpayers were around 13 *per cent* for both years.

GST Return filing pattern

2.4.2 Filing pattern of GSTR-1 and GSTR-3B

The trends of filing of GSTR-1⁷ and GSTR-3B⁷ as on 31 March 2021 for the period from April 2019 to March 2021 as compiled from the summary reports shared by SGST Department, have been depicted in **Table - 2.3**.

⁶ NRTP - Non Resident Taxable Person, OIDAR - Online Information Database Access and Retrieval Services.

⁷ GSTR-1 is a return filed monthly or quarterly by a registered entity containing details of all outward supplies regarding goods or services (sales). GSTR-3B is a return containing the summary of a business owner's outward and inward supplies.

Table - 2.3
Filing pattern of GSTR-1 and GSTR-3B

| Return Type | GSTR-1 | | | GSTR-3B | | | | |
|-------------|----------|----------------|---------------|------------------------|----------------|--|------------------------|---------------------------|
| | Months | Due for filing | Returns filed | Return filing per cent | Due for filing | Returns filed as on 31 March 2020 & 2021 | Return filing per cent | Returns filed by due date |
| April'19 | 2,79,475 | 1,44,723 | 51.78 | 2,79,475 | 2,61,094 | 93.42 | 1,04,985 | 37.57 |
| May'19 | 2,81,241 | 1,45,491 | 51.73 | 2,81,241 | 2,62,829 | 93.45 | 93,352 | 33.19 |
| June'19 | 2,83,381 | 2,59,120 | 91.44 | 2,83,381 | 2,64,437 | 93.32 | 89,386 | 31.54 |
| July'19 | 2,86,357 | 1,47,373 | 51.46 | 2,86,357 | 2,66,915 | 93.21 | 80,093 | 27.97 |
| Aug'19 | 2,88,647 | 1,48,406 | 51.41 | 2,88,647 | 2,69,041 | 93.21 | 1,10,898 | 38.42 |
| Sep'19 | 2,90,072 | 2,64,510 | 91.19 | 2,90,072 | 2,70,324 | 93.19 | 1,22,458 | 42.22 |
| Oct'19 | 2,92,185 | 1,50,372 | 51.46 | 2,92,185 | 2,72,402 | 93.23 | 1,03,078 | 35.28 |
| Nov'19 | 2,94,858 | 1,51,999 | 51.55 | 2,94,858 | 2,74,570 | 93.12 | 61,145 | 20.74 |
| Dec'19 | 2,96,505 | 2,68,222 | 90.46 | 2,96,505 | 2,76,258 | 93.17 | 1,05,625 | 35.62 |
| Jan'20 | 2,98,159 | 1,52,544 | 51.16 | 2,98,159 | 2,77,464 | 93.06 | 96,142 | 32.25 |
| Feb'20 | 3,00,095 | 1,52,339 | 50.76 | 3,00,095 | 2,78,709 | 92.87 | 1,05,642 | 35.20 |
| Mar'20 | 3,01,901 | 2,65,196 | 87.84 | 3,01,901 | 2,79,594 | 92.61 | 2,71,920 | 90.07 |
| April'20 | 1,93,566 | 1,13,654 | 58.72 | 1,95,050 | 1,84,457 | 94.57 | * | |
| May'20 | 1,93,414 | 1,14,051 | 58.97 | 1,95,022 | 1,84,366 | 94.54 | | |
| June'20 | 1,94,481 | 1,79,414 | 92.25 | 1,96,310 | 1,85,177 | 94.33 | | |
| July'20 | 1,95,549 | 1,12,831 | 57.70 | 1,97,610 | 1,85,892 | 94.07 | | |
| Aug'20 | 1,96,501 | 1,12,737 | 57.37 | 1,98,824 | 1,86,685 | 93.89 | | |
| Sep'20 | 1,97,755 | 1,76,458 | 89.23 | 2,00,319 | 1,87,599 | 93.65 | | |
| Oct'20 | 1,99,049 | 1,00,499 | 50.49 | 2,01,929 | 1,88,588 | 93.39 | | |
| Nov'20 | 2,00,859 | 98,987 | 49.28 | 2,03,928 | 1,90,280 | 93.31 | | |
| Dec'20 | 2,02,428 | 1,84,865 | 91.32 | 2,05,638 | 1,91,605 | 93.18 | | |
| Jan'21 | 2,03,034 | 1,45,961 | 71.89 | 1,52,614 | 1,38,185 | 90.55 | | |
| Feb'21 | 2,03,974 | 1,48,100 | 72.61 | 1,53,993 | 1,39,363 | 90.50 | | |
| Mar'21 | 2,05,006 | 1,86,439 | 90.94 | 2,42,645 | 1,94,184 | 80.03 | | |

*Return filed by due date for the period 2020-21 has not been furnished by the Department.

The filing of GSTR-3B for April 2019 was 93.42 per cent while the filing per cent for March 2021 was only 80.03 per cent. It was noticed that GSTR-3B returns were being filed within the due date on an average by 38.34 per cent taxpayers and 55 per cent filed the returns after due date (status based on 2019-20)

- i. The filing percentages of GSTR-1 returns were throughout less in comparison to the corresponding filing of GSTR-3B returns during the period April 2019 to March 2021. The introduction of GSTR-3B

resulted in filing of returns with ITC claims which could not be verified and it appears to have disincentivised filing of even GSTR-1.

- ii. With the changes made to returns mechanism, GSTR-1 has been the only return which would provide invoice level details. Further, GSTR-1 contains GSTIN-wise details of supplies made and hence by collating details from across various GSTR-1 returns, it would be possible to prepare a profile of taxpayers which could be used to identify liable businesses not registered under GST or those under-reporting their turnover.

GSTR-3B being only a summary return, short-filing of GSTR-1 implied that the tax departments did not have complete invoice level details as filed by the suppliers, which could be used to verify details given in GSTR-3B or to arrive at turnover. Since filing of GSTR-1 is mandatory, short-filing is an area of concern and needs to be addressed.

Revenue from GST, bi-monthly compensation received from the Government of India and details regarding Integrated Goods and Services Tax are detailed in **Appendices - VII, VIII and IX** respectively.

2.5 Compliance Audit on 'Transitional credits under GST'

2.5.1 Introduction

Introduction of Goods and Services Tax (GST) was a significant reform in the field of indirect taxes in our country, which replaced multiple taxes levied and collected by the Centre and States. GST is a destination based tax on supply of goods or services or both, which is levied at multiple stages wherein the taxes will move along with supply. The tax, which is levied simultaneously by the Centre and States on a common tax base, accrues to the taxing authority having jurisdiction over the place of supply. Central GST (CGST) and State GST (SGST)/ Union Territory GST (UTGST) are levied on intra-State supplies, whereas Integrated GST (IGST) is levied on inter-State supplies. Availability of ITC of taxes paid on inputs, input services and capital goods for set off against the output tax liability is one of the key features of GST. This avoids cascading effect of taxes and ensures uninterrupted flow of credit from the seller to buyer. To ensure the seamless flow of input tax from the existing laws into the GST regime, 'Transitional arrangements for input tax' were included in the GST Acts to provide for the entitlement and manner of claiming input tax in respect of appropriate taxes or duties paid under existing laws.

2.5.2 Transitional arrangements for input tax

Section 140 of the SGST Act, 2017, (and CGST/ UTGST Acts) enables the taxpayers to carry forward the ITC earned under the existing laws to the GST regime. The Section, read with Rule 117 of Kerala GST Rules, 2017, prescribes elaborate procedures in this regard. Under transitional arrangements for ITC, the ITC of various taxes paid under the existing laws such as Central Value Added Tax (CENVAT), State Value Added Tax (VAT) etc., are eligible to be carried forward to GST regime as under:

(a) Closing balance of credit in legacy return: The closing balance of VAT credit/ CENVAT credit available in the returns filed under the existing law for the month immediately preceding the appointed day can be taken as credit in the Electronic Credit Ledger (ECL).

(b) Unavailed credit on capital goods: The balance instalment of unavailed credit on capital goods can be taken by filing the requisite declaration in TRAN-1.

(c) Credit on duty paid stock: A registered taxable person, who was not liable to be registered under the existing law or who was engaged in the sale of exempted goods, may take the credit of the duty/ tax paid on goods held in stock based on the invoices.

(d) Credit on duty paid stock when registered person does not possess the document evidencing payment of excise duty/ VAT: A registered taxable

person, other than the manufacturer or service provider, who does not have excise or VAT invoice, is eligible to take credit on the duty paid stock.

(e) **Inputs in transit:** The inputs received on or after the appointed day but where the duty or tax on the same was paid by the supplier under the existing law are also eligible for Transitional credit.

(f) **Tax paid under the existing law under composition scheme:** The taxpayers who had paid tax at fixed rate or fixed amount in lieu of the tax payable under existing law, now working under normal scheme under GST can claim credit of duty on their input stock, semi-finished and finished stock on the appointed date.

All registered taxpayers, except those who were opting for payment of tax under the composition scheme (under Section 10 of the Act), were eligible to claim Transitional credit by filing TRAN-1 declaration within 90 days from the appointed day. The time limit for filing TRAN-1 declaration was extended initially till 27 December 2017. However, many taxpayers could not file the declaration within the due date due to technical difficulties. The due date for filing TRAN-1 declaration was further extended to 31 March 2020 for those taxpayers who could not file TRAN-1 declaration due to technical difficulties and those cases recommended by the GST Council.

2.5.3 Context and materiality

The Transitional credit, being one-time flow of ITC from the legacy regime into the GST regime, can be availed both by the taxpayers migrating from the previous regime as well as new registrants under GST. As of June 2018, 3.72 lakh taxpayers were registered under GST, out of which 9,664 taxpayers had claimed SGST credit.

2.5.4 Audit objectives

Transitional credit claims directly impact GST revenues as the credit is eligible for set off against the output tax liability of taxpayers. Thus, the audit of Transitional credit was taken up with the following objectives, seeking assurance on:

- i. Whether the mechanism envisaged by the Department for selection and verification of Transitional credit claims was adequate and effective; and
- ii. Whether the Transitional credits carried over by the assessee into GST regime were valid and admissible.

2.5.5 Audit Scope, Methodology and Coverage

The Audit scope comprised review of Transitional credit declarations filed by the taxpayers under Section 140 of the SGST Act, 2017, from the appointed

date⁸ to the end of March 2020. This involved examination of adequacy of rules specified for Transitional credit under the Act, effectiveness of departmental verification process, follow up action taken on the deviations detected, process adopted for implementation of cross-jurisdictional functions regarding Transitional credit and independent examination of selected transitional credit claims for compliance assurance.

The verification of TRAN-1 declarations and collection of details were carried out at the Assessment Circle Offices of SGST Department. The period of coverage of audit was from 2017-18 to 2019-20 and audit was conducted from March 2021 to July 2021.

A sample of 1,174 transitional cases amounting to ₹ 42.66 crore pertaining to the seven⁹ districts was identified for detailed verification. The sample was selected, keeping in view the representation from various types of ITCs (from table 5(c), 6(b) etc. of TRAN-1) and the financial materiality threshold of ₹ 50,000.

An entry conference was held with the Additional Secretary to Government, Taxes Department, Principal Commissioner of CGST, Kochi, Commissioners of CGST of Thiruvananthapuram and Kozhikode, Special Commissioner of SGST on 5 March 2021, wherein the objective, scope and methodology of audit were discussed. The exit conference was held on 23 September 2021 with the Secretary, Taxes Department, Commissioner, SGSTD and Commissioners of CGST, wherein the Audit findings were discussed.

2.5.6 Audit criteria

Section 140 of the SGST Act, 2017, governs the transition of ITC from legacy Kerala Value Added Tax (KVAT) provisions. The Section read with Rule 117 of the SGST Rules, 2017, and relevant Notifications/ Circulars issued by CBIC/ State constitute the criteria for Audit.

Audit findings

The extent of deficiencies noticed during the audit of Transitional credit cases selected for detailed audit are detailed in **Appendix - X**. Audit findings and the lapses identified are included in the subsequent paragraphs.

2.5.7 Irregular claim of transitional credit on goods in stock with duty paid documents

As per Sections 140(3), 140(4)(b) and 140(6) of SGST Act, 2017, and Rule 117(4) of Kerala GST Rules, 2017, the amount of Value Added Tax and Entry Tax paid on inputs held in stock and inputs contained in semi-finished or

⁸ 1 July 2017.

⁹ Alappuzha, Idukki, Kannur, Kasaragod, Kottayam, Kozhikode and Wayanad.

finished goods held in stock on the appointed day supported by invoices/ documents evidencing payment of tax can be carried forward to ECL as credit by the GST registered person in the following circumstances:

- i. The person was not liable to be registered under KVAT Act.
- ii. The person was engaged in sale of exempted goods.
- iii. Goods suffered tax at first point of sale and subsequent sales were not subjected to tax.
- iv. The person was entitled to take ITC at the time of sale of goods.
- v. The person was paying tax at fixed rate under KVAT Act.

Taxpayers were required to claim credit under Table 7(c) for the stock supported by invoices.

Audit noticed that in 27 (28.72 *per cent*) out of 94 cases, credits were carried forward even though these taxpayers did not fulfil any of the above mentioned criteria. Non-adherence of the above provisions resulted in the availing of irregular Transitional credit amounting to ₹6.25 crore as detailed in **Appendix - XI**.

On this being pointed out (June 2021), the Government stated (November 2021) that notices were issued in 14 cases involving an amount of ₹0.25 crore. Replies to the remaining 13 cases are awaited (September 2022).

Illustrative cases are given below:

- (a) M/s QRS Retails Ltd. (GSTIN: 32AAACQ1665J1ZJ), a taxpayer coming under the jurisdiction of Statue Range in Thiruvananthapuram South Division had claimed credit of ₹4.49 crore as eligible duties in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock on the appointed day. Verification of claims revealed that the taxpayer was a regular taxpayer who dealt with electronic goods during the KVAT regime and is not eligible to avail credit for such goods. The irregular credit claimed by the taxpayer amounts to ₹4.49 crore.
- (b) M/s Trinity Global (GSTIN: 32AAIFT0033A1Z1), a taxpayer coming under the jurisdiction of Alappuzha Range in Alappuzha Division had claimed credit of ₹0.35 crore as eligible duties in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock on the appointed day. Verification of claims revealed that the taxpayer was a regular taxpayer who dealt with white goods, telephone and telephone equipment during the KVAT regime and he is not eligible to avail credit for such goods. The irregular credit claimed by the taxpayer amounts to ₹0.35 crore.

2.5.8 Irregular claim of Transitional credit on goods in stock without duty paid documents

As per Section 140(3) of Kerala GST Act, 2017, and Rule 117(4) of Kerala GST Rules, 2017, a registered person, holding stock of goods which have suffered tax at the first point of their sale in the State and the subsequent sales of which are not subject to tax in the State shall be allowed to avail ITC on goods held in stock in respect of which he is not in possession of any document evidencing payment of VAT in the following conditions:

- i. The credit shall be allowed at the rate of 60 *per cent* on such goods which attract State tax at the rate of nine *per cent* or more and 40 *per cent* for other goods of the State tax applicable on supply of such goods.
- ii. The scheme shall be available for six tax periods from the appointed date.
- iii. Such goods were not wholly exempt from tax under the KVAT Act, 2003.
- iv. The registered person availing of this scheme and having furnished the details of stock held by him, submits a statement in FORM GST TRAN-2 at the end of each of the six tax periods during which the scheme is in operation indicating therein the details of supplies of such goods effected during the tax period.

The amount of credit allowed shall be credited to the ECL of the applicant maintained in FORM GST PMT-2 on the Common Portal.

Scrutiny of TRAN-1 and TRAN-2 declarations of taxpayers who availed input tax credit revealed that in respect of six (2.96 *per cent*) out of 203 cases, credits were not within the purview of the above provision. This resulted in irregular claim of Transitional credit amounting to ₹2.89 crore as detailed in **Appendix - XII**.

On this being pointed out (June 2021) the Government stated (November 2021) that reply from the Central jurisdiction is awaited.

An illustrative case is given below:

M/s QRS Retails Ltd. (GSTIN: 32AAACQ1665J1ZJ), a taxpayer coming under the jurisdiction of Statue Range in Thiruvananthapuram South Division had claimed credit of ₹2.59 crore as eligible duties in respect of inputs held in stock and inputs contained in semi-finished or finished goods held in stock and was not in possession of an invoice or any other document evidencing payment of tax in respect of inputs on the appointed day. Verification of claims revealed that the taxpayer was a regular taxpayer who dealt in electronic goods during KVAT regime and was not eligible to avail credit for such goods. The irregular credit claimed by the taxpayer amounted to ₹2.59 crore.

2.5.9 Excess carry forward of ITC

As per Section 140(1) of the SGST Act, 2017, a registered person, other than a person opting to pay tax under Section 10, shall be entitled to take in his ECL the amount of Value Added Tax and Entry Tax, if any, carried forward in the return relating to the period ending with the day immediately preceding the appointed day, furnished by him under the existing law in such manner as may be prescribed. The registered person shall not be allowed to take credit in the following circumstances:

- i. Where the said amount of credit is not admissible as ITC under the Act; or
- ii. Where he has not furnished all the returns required under the existing law for the period of six months immediately preceding the appointed date; or
- iii. The said credit is attributable to any claim related to Section 3, Section 5(3), Section 6, Section 6A or Section 8(8) of the Central Sales Tax (CST) Act, 1956 which is not substantiated in the manner, and within the period, prescribed in Rule 12 of the CST (Registration and Turnover) Rules, 1957.

The input tax under this category was required to be claimed under Table 5(c) of TRAN-1 declaration.

Audit verified the transitional claims of 867 taxpayers and noticed that the taxpayers had carried forward irregular ITC in 22 claims (2.54 *per cent*) amounting to ₹0.67 crore under Table 5(c) of TRAN-1 declaration. These irregularities included transition of excess credit due to non-matching of closing balance of the credit in the last KVAT return and credit claimed without filing legacy returns.

Significant findings in each of these categories are illustrated below:

(a) **Non-matching of closing balance of the credit in the last KVAT return**

Audit noticed that 19 (2.19 *per cent*) out of 867 taxpayers carried forward higher transitional credits in the ECL than the amount declared in their last return under KVAT. The irregular availing of Transitional credit, without adhering to the provision of SGST Act, involved an excess credit carry forward of ₹0.63 crore as detailed in **Appendix - XIII**.

On this being pointed out (June 2021) the Government stated (November 2021) that notices were issued in four cases involving an amount of ₹0.04 crore. Replies in the remaining 15 cases are awaited (September 2022).

Illustrative cases are detailed below:

- i) M/s EICL Limited (GSTIN: 32AAACE5011C1ZM), a taxpayer coming under the Veli Range in Thiruvananthapuram North Division, had carried forward ₹0.24 crore as closing ITC balance from the KVAT returns under Table 5(c) of TRAN-1. However, verification of KVAT returns of the taxpayer revealed that the actual ITC balance as per the said returns was only ₹0.64 lakh leading to an excess credit carried forward of ₹0.24 crore.
- ii) M/s Muthoot Homez (GSTIN: 32AAECM1840M6ZF), a taxpayer coming under the Statue Range in Thiruvananthapuram North Division had carried forward ₹0.15 crore as closing ITC balance from the KVAT returns under Table 5(c) of TRAN-1. However, verification of KVAT returns of the taxpayer revealed that the actual ITC balance as per the said returns was 'NIL' leading to an excess credit carried forward of ₹0.15 crore.

(b) Transitional credit claimed without filing legacy returns

Audit noticed that three (0.35 *per cent*) out of 867 taxpayers claimed Transitional credit of ITC balances remaining in the accounts even though they have not filed all the returns as required under the existing law. Amount of credit transitioned in three such cases amounted to ₹0.04 crore as detailed in **Appendix - XIV**.

On this being pointed out (June 2021) in Audit, the Government stated (November 2021) that notice was issued in one case involving an amount of ₹0.88 lakh. Replies in the remaining two cases are awaited (September 2022).

2.5.10 Irregular availment of transitional credits on capital goods

As per Section 140(2) of the SGST Act, 2017, a taxpayer other than a person opting to pay tax under Section 10, shall be entitled to take in his ECL, credit of unavailed portion of ITC in respect of capital goods not carried forward in a return, furnished under an existing law for the period ending with the day immediately preceding the appointed day. This is subject to the provision that the taxpayer shall not be allowed to take credit unless the said credit was admissible as ITC under the existing law and is also admissible as ITC under GST Act.

The unavailed ITC on capital goods represents the amount that remains after subtracting the amount of ITC already availed in respect of capital goods by the taxable person under the existing law from the aggregate amount of ITC to which the said person was entitled in respect of the said capital goods under the existing law.

Taxpayers were required to claim unavailed ITC of capital goods under Table 6(b) of TRAN-1 declaration.

As per KVAT monthly returns of 192 taxpayers, Audit noticed in 12 cases (6.25 *per cent*) that the unavailed portion of credit on capital goods was 'Nil' and in eight cases (4.17 *per cent*) the unavailed portion of credit was less than the credit claimed in TRAN-1 declaration. Thus, the Transitional credit on capital goods amounting to ₹0.34 crore in 20 cases was inadmissible as detailed in **Appendix - XV**.

On this being pointed out (June 2021), the Government stated (November 2021) that notices were issued in eight cases involving an amount of ₹0.08 crore and ₹0.06 crore recovered in three cases. Replies in the remaining cases are awaited (September 2022).

Illustrative cases are given below:

- i) M/s QRS Retails Ltd. (GSTIN: 32AAACQ1665J1ZJ), a taxpayer coming under the jurisdiction of Statue Range in Thiruvananthapuram North Division had claimed unavailed ITC in respect of capital goods amounting to ₹0.10 crore under Table 6(b) of TRAN-1 declaration. Verification of KVAT return for June 2017 revealed that the taxpayer had 'NIL' credit as unavailed KVAT capital goods credit to carry forward to GST regime. The irregular credit claimed on such goods amounts to ₹0.10 crore.
- ii) M/s Lilly Whites Garments Pvt. Ltd. (GSTIN: 32AABCL9777F1ZB), a taxpayer coming under the jurisdiction of Statue Range in Thiruvananthapuram North Division had claimed unavailed ITC in respect of capital goods amounting to ₹0.06 crore under Table 6(b) of TRAN-1 declaration. Verification of KVAT return for June 2017 revealed that the taxpayer had 'NIL' credit as unavailed KVAT capital goods credit to carry forward to GST regime. The irregular credit claimed on such goods amounts to ₹0.06 crore.

2.5.11 Conclusion

Audit noticed deviation from Act/ Rules in 75 cases (6.39 *per cent*) amounting to ₹10.15 crore (23.79 *per cent*) out of 1,174 cases amounting to ₹42.66 crore test-checked in Audit. The deficiencies noticed were primarily on irregular claim of Transitional credit on goods in stock, excess carry forward of ITC and irregular availment of Transitional credits on capital goods.

2.5.12 Recommendation

The verification of Transitional Credit claims should not be allowed to linger and the Department should ensure that it is completed expeditiously as per the merits of the case in a time bound manner.

2.6 'Processing of refund claims under GST'

2.6.1 Introduction

The provisions pertaining to refund contained in the GST laws aim to streamline and standardise the refund procedures under GST regime. It was decided that the claim and sanctioning procedures would be completely online. Due to the unavailability of Electronic Refund module in the common portal, a temporary mechanism was devised and implemented which involved physical submission of application and supporting documents.

Later, the refund procedure was made fully electronic from 26 September 2019 (also called Automation of Refund Process). The Circulars issued by the Government of India as per the recommendations of the GST Council meetings are being followed by the State GST Department also. However, all refund applications filed on the common portal before 26 September 2019 are to be processed manually as was done prior to deployment of the new system.

2.6.2 Audit Scope and Methodology

The Audit was conducted between December 2020 and May 2021 to assess the adequacy of the statutory provisions of refund and effectiveness of its internal control mechanism to dispose of the refund applications. For this GSTN provided pan-India Refund Data for the period from July 2017 to July 2020. For the period prior to 26 September 2019, i.e., pre-automation period, the refund applications under each category were sorted out in descending order of refund amount claimed by taxpayers. The sorted refund applications were divided into four quartiles for drawing the sample.

For selecting refund applications filed after 26 September 2019, a composite risk score was devised using risk parameters such as refund amount claimed (60 *per cent*), delay in sanctioning refund (15 *per cent*), refund sanctioned/refund claimed ratio (10 *per cent*) and issue of deficiency memo. Based on the risk score arrived as per this process, refund applications were selected.

Based on the above procedure, a sample of 868 out of 6,026 refund cases pertaining to Kerala State was selected for Audit. Out of these, 451 cases relate to refunds filed after 26 September 2019. Of the 417 cases relating to refunds filed prior to 26 September 2019, in 72 cases though ARN¹⁰ was generated, refund applications were not submitted by the taxpayer to the proper officer¹¹ for refund processing. Thus, the total number of cases test-checked during the audit was 796.

¹⁰ ARN : Application Reference Number. On submission of refund application, ARN number is generated against the refund application. Taxpayers can track refund status using this number.

¹¹ Section 2(91) of the Kerala State Goods and Services Tax Act, 2017.

Apart from the above, communication of refund orders to and from the counterpart Tax Authorities for the purpose of payment of the sanctioned refund amount of tax were also test checked.

Audit Findings

2.6.3 Acknowledgment not issued within time

During audit scrutiny of 796 refund cases it was noticed that the delay in issue of acknowledgement in 167 cases (21 *per cent*) ranged from one to 198 days as detailed in **Appendix - XVI**. Of these, 154 cases were delayed by one to three months, 10 cases were delayed by three to six months and three cases were delayed by more than six months. Further, acknowledgements were not issued in 108 cases (13.75 *per cent*). Thus, the Department did not adhere to the timelines for issuing acknowledgement as prescribed in the rules *ibid*.

The matter was reported to the Government (October 2021). The Government replied (February 2022) that during the relevant period there were technical glitches in the GST website which made the process slower. Moreover, in many cases the assesseees were not aware of the documents to be submitted along with the application for refund. Therefore, the entire claim had to be verified with reference to the returns and the annexures submitted to ensure the veracity of the claim and to prevent loss of revenue. The same had caused delay in issuing acknowledgement and processing of refunds in certain cases. Further, no loss of revenue could be attributed for the technical default of delay in issuing acknowledgments.

The reply is not acceptable as the Rule stipulates that if the claim submitted by the assesseees is not supported by requisite documents, the officer concerned should issue deficiency memo within 15 days and direct the assessee to re-submit the claim. Such re-submitted claims are to be treated as fresh claims and acknowledgements have to be issued within 15 days from the date of submission. Audit pointed out only those cases in which neither acknowledgement nor deficiency memo was issued within the stipulated time (July 2022).

2.6.4 Refund orders not sanctioned in time

Audit observed that in 276 cases (34.67 *per cent*) out of the 796 cases examined, there was delay in sanctioning of refunds ranging from one to 628 days. Of these, 201 cases were delayed by one to three months, 53 cases were delayed by three to six months and 22 cases were delayed by more than six months. Further, the Department did not pay interest of ₹51.03 lakh which was due to the claimants.

The matter was reported to the Government (October 2021). The Government replied (February 2022) that before sanctioning a refund, the proper officer had to scrutinise the GSTR1, GSTR3B, ECL, purchase invoices, etc. for the

relevant period. In certain cases, deficiency memos were issued to the assessee and due to the delay in obtaining the replies the applications were kept pending as the GST website was not fully functional during the relevant period. The delay in processing the refunds had occasioned only due to the above mentioned reason and was neither willful nor negligent. Moreover, no loss of revenue was caused to the State exchequer due to the delay in sanctioning or by payment of interest for the delay in processing the refund.

The reply of the Government is not acceptable, as Audit excluded those cases in which delay was due to delay in furnishing of replies by the taxpayers. Moreover, as per the statute, the Government should pay interest for the delayed payment of refunds (July 2022).

2.6.5 Non-issue/ delay in sanction of provisional refund on account of zero-rated supply

During the audit period, 1,969 refund cases were processed on account of zero-rated supply of goods or services or both by the Department. Out of these, 364 refund cases were examined and it was noticed that in 277 refund cases (76.10 *per cent*) the provisional refunds were not sanctioned by the proper officer even though final refunds were sanctioned. Further, out of the 87 cases where provisional refunds were sanctioned, in 34 cases (39.08 *per cent*) there was delay in sanction of provisional refunds ranging from one to 337 days. Of these, 31 cases were delayed by one to three months, two cases were delayed between three to six months and one case was delayed by more than six months. This has resulted in non-observance of the provisions of Rule 91(2) of the KSGST Rules, 2017.

The matter was reported to the Government (October 2021). The Government stated (February 2022) that the said provision of the Act is only directory and not mandatory and 90 *per cent* of the claim is to be sanctioned only after ascertaining the veracity of the claim *prima facie*. The said cases needed detailed verification and so it caused a delay in sanctioning provisional refund.

The reply is not tenable as Rule 91(2) of KSGST Rules, 2017 stipulates that the proper officer shall make an order in Form GST RFD-04, sanctioning the amount of refund due to the applicant on a provisional basis within a period not exceeding seven days from the date of acknowledgement. As such, sanctioning of refund within seven days is a mandatory provision to be complied with. Moreover, it is also a part of the Government's policy of 'ease of doing business' to release the blocked revenue as soon as possible to the concerned businesses (June 2022).

2.6.6 Abnormal delay in communicating refund orders to counterpart Tax Authority

Audit scrutiny of the refund data made available by five¹² offices out of 15 offices of Joint Commissioners in Kerala State Goods and Services Tax Commissionerate revealed that out of 1,922 refund orders, 1,592 refund orders (82.83 *per cent*) were forwarded to the counterpart Central Tax Authority with delay ranging from one to 311 days. Of these, 1,523 cases were delayed by one to three months, 29 cases between three to six months and 40 cases were delayed by more than six months.

Further, it was also observed that out of 1,508 refund orders involving an amount of ₹42.58 crore which got transferred from the counterpart Central Tax Authority, 1,007 refund orders involving ₹28.55 crore (67.06 *per cent*) were received with delays ranging from one to 563 days. Of these, 914 cases were delayed by one to three months, 87 cases were delayed by three to six months and six cases were delayed by more than six months.

The matter was reported to the Government (October 2021). The Government stated (February 2022) that during the initial stage of implementation of GST, the Department had faced technical glitches which affected the procedures to be followed. Also, being a new tax system and having no previous experience there was delay of a few days in submitting the application to the Nodal Officer. As there is no loss of revenue, the delay in communicating refund orders to counterpart tax authority may be condoned.

The reply is not acceptable as any accepted application for refund, if not refunded within the period of sixty days, interest at such rate shall be payable in respect of such delayed refund. In the above reported cases, though refunds were sanctioned within the time limit, the payment of the same got delayed due to delay in communication. Moreover, there is no provision in the Act to condone the delay (July 2022).

2.6.7 Non-conducting of post-audit of refund claims

During Audit scrutiny of the 796 refund cases it was observed that none of these cases were sent for post-audit. This, apart from resulting in non-adherence to Commissioner's instructions, may also lead to possible loss of revenue to exchequer.

The matter was reported to the Government (October 2021). The Government stated (February 2022) that during manual sanctioning of refund, before sanctioning of refund, proper officers had obtained approval from higher authority and hence the concept of post-audit had no relevance.

¹² Offices of Joint Commissioner Thiruvananthapuram, Joint Commissioner Kollam, Joint Commissioner Kozhikode, Joint Commissioner Kannur and Joint Commissioner Kasaragod.

The reply is not tenable as CBIC on recommendation of GST Council vide circular No 17/17/2017-GST dated 15 November 2017 directed that post-audit of refund orders should be done as per the extant guidelines. The Commissioner of State GST had also issued directions in this regard. Hence the Department should adhere to the instructions issued by the Commissioner.

2.6.8 Irregular allowance of IGST and CGST refund despite drawback allowed at higher rate

During the audit period in 76 STOs, 1,969 refund cases were processed on account of zero rated supply of goods or services or both by the Department. Out of these, 364 refund cases were examined and it was noticed that in three refund cases in two¹³ STOs, the assessee availed Duty drawback at a higher rate and did not submit a copy of the self-declaration submitted to the jurisdictional Customs Officer to the effect that no ITC of CGST/ IGST is claimed, no refund of IGST paid on export goods is claimed and no CENVAT credit is carried forward. The allowance of ITC in respect of IGST and CGST resulted in irregular allowance of ₹0.15 crore.

The matter was reported to the Government (October 2021). The Government stated (February 2022) that in one case¹⁴ notice in DRC01A¹⁵ was issued to the taxpayer demanding an amount of ₹0.04 crore including interest. Replies in the remaining two cases are awaited (September 2022).

2.6.9 Irregularity in processing of refund of inverted duty structure

During the Audit of 25 STOs in KSGST Commissionerate, 1,548 refund cases on account of inverted duty structure were processed till 31 July 2020. Out of these, 296 refund cases were examined and it was noticed that seven refunds were issued irregularly. Out of this, in four cases in respect of two¹⁶ assessee, the proper officer erred in considering the 'Adjusted Total Turnover' correctly. This resulted in irregular allowance of refund of ₹0.02 crore as detailed in **Appendix - XVII (a)**. In the other three¹⁷ cases, refund was allowed on a commodity which was initially ineligible for refund and later allowed for the same under certain conditions. It was noticed that the assessee carried forward the net ITC from July 2018 to subsequent periods and was allowed refunds instead of disallowing the net ITC available at the end of July 2018. This resulted in non-reversal of ITC of ₹0.19 crore as detailed in **Appendix - XVII (b)**.

¹³ State Tax Office III Circle and State Tax Office IV Circle, Kozhikode.

¹⁴ S.M.Fruits.

¹⁵ As per Notification No. 49/2019-Central Tax dated 09.10.2019, the proper officer should, before serving the notice to the person chargeable with tax, interest and penalty under various sections, communicate the details of any tax, interest and penalty as ascertained by the said officer using this form.

¹⁶ Slipons India Private Limited and Holyprops Industries.

¹⁷ Supreme Narrow Fabrics, Supreme Textiles, Ariham Industries.

The matter was reported to the Government (October 2021). The Government stated (February 2022) that in three¹⁸ cases the taxpayer had reversed an amount of ₹0.14 crore through Form GST DRC 03¹⁹ and in one²⁰ case, an amount of ₹0.05 crore was reversed through GSTR 3B. Reply in the remaining three cases are awaited (September 2022).

2.6.10 Excess allowance of refund due to omission to exclude credit notes

During the scrutiny of 364 cases out of 1,969 refund cases processed on account of zero-rated supply of goods or services or both by the Department it was noticed that in one²¹ STO, refunds related to M/s IBS Software Services Pvt. Ltd. for three²² periods were sanctioned completely as claimed by the assessee, without deducting the input tax reversed by the suppliers by issuing credit notes. This resulted in excess allowance of refund of ₹0.14 crore.

The matter was reported to the Government (October 2021). The Government stated (February 2022) that the proper officer issued DRC07 creating an additional tax effect of ₹0.63 crore which includes other deficiencies also.

2.6.11 Excess grant of refund due to non-reversal of ITC on exempted supplies

Audit scrutiny of 364 cases revealed that in two refund cases in two²³ STOs, the entire ITC availed during the period was allowed while calculating the refund amount, though the assessee had exempted supplies during the relevant period. Non-reversal of proportionate ITC for the exempted supplies resulted in excess refund of ITC of ₹0.01 crore.

The matter was reported to the Government (October 2021). The Government stated (February 2022) that in one²⁴ case, detailed verification was being done. However, a show cause notice had been issued. Reply in the remaining one case is awaited (September 2022).

2.6.12 Refund sanctioned on time barred application

Audit scrutiny of 796 cases revealed that four refunds with respect to two²⁵ assesseees in two²⁶ STOs were issued beyond the period of limitation

¹⁸ Holyprops Industries, Supreme Narrow Fabrics, Supreme Textiles.

¹⁹ For intimation of voluntary payment made by the taxpayer or made against the show cause notice by the taxpayer.

²⁰ Ariham Industries.

²¹ Special Circle, Thiruvananthapuram.

²² For the relevant periods October 2017- November 2017, December 2017-January 2018 and February 2018-March 2018.

²³ Special Circle II, Ernakulam and Works Contract, Ernakulam.

²⁴ Amaco Impex Pvt. Ltd.

²⁵ M/s.Lunar Rubbers and AAK Exports.

²⁶ Special Circle, Thodupuzha and STO, Tirur.

prescribed under Section 54 of the KSGST Act, 2017, which resulted in irregular refund of ₹0.11 crore as detailed in **Appendix - XVIII**.

The matter was reported to the Government (October 2021). The Government stated (February 2022) that in three cases of one²⁷ taxpayer, Form GST DRC 01 was issued and the taxpayer had filed adjournment letter. Reply in the remaining one case is awaited (September 2022).

2.6.13 Non demand of tax in respect of ITC disallowed as ineligibly availed

During Audit scrutiny of 660 cases out of 3,517 refund cases relating to zero-rated supply of goods or services or both and inverted duty structure, it was noticed that in three refund cases in respect of two assesseees, the Department after verification of the input invoices disallowed ITC of ₹37.60 lakh as it was not matching with Form GSTR 2A for the relevant period. Even though the rejection of ITC was on account of ineligibility of the credit, the Department did not issue an order of demand to recover the ITC wrongly availed. This had resulted in non-demand of tax of ₹0.38 crore as detailed in **Appendix - XIX**.

The matter was reported to the Government (October 2021). The Government stated (February 2022) that in one²⁸ case, the proper officer issued DRC 07 creating an additional tax effect of ₹0.63 crore which includes other compliance deviations also. Reply in the remaining two cases are awaited (September 2022).

2.6.14 Excess refund sanctioned due to wrong admission of Net ITC

Audit examined 364 cases out of 1,969 refund cases relating to zero rated supply of goods or services or both and it was noticed that in one²⁹ case, the net ITC taken by the Department for calculating the maximum refundable amount included ITC for a previous period which got re-credited through manual orders in Form GST PMT 03 to the assessee's ECL. The re-credited ITC of ₹0.40 crore relates to the period from July 2017 to September 2017 which was disallowed by the Assessing Authority during that period. Reckoning the disallowed ITC for another period in arriving at the eligible refund is against the provisions of the Act. The irregular admission of ITC resulted in excess refund of ₹0.10 crore.

The matter was reported to the Government (October 2021). The Government stated (February 2022) that the proper officer had issued notice to the taxpayer.

²⁷ AAK Exports.

²⁸ IBS Software Services Pvt. Ltd.

²⁹ M/s NS Cashew Company (GSTIN 32AEEPR6378G1ZA), relevant period April 2018 to October 2018.

2.6.15 Irregular refund of excess balance in Electronic Cash Ledger

Audit examined 78 cases out of 1,078 refund cases relating to Electronic Cash Ledger revealed that in three cases in three³⁰ STOs, the entire Tax Deducted at Source (TDS) credit as reflected in the Electronic Cash Ledger of the assesseees were refunded, even though the assesseees did not fill up the prescribed undertaking as per Section 16(2)(c) and 42(2). Also the Department did not verify whether the tax liability was discharged on the value of supply received from the deductor. This had resulted in irregular sanction of refund amounting to ₹0.54 crore.

The matter was reported to the Government (October 2021).The Government stated (February 2022) that in one case³¹ the refund claimed by the taxpayer was on account of excess balance in Electronic Cash Ledger. Further, the assessee filed undertaking under Section 16(2)(c) and TDS certificates in Form GST 7A. In another case³², the TDS return for 2019-20 included invoices pertaining to the period 2018-19.

The reply is not tenable, as verification of tax returns, filed from the date of credit of TDS to the date of refund of it showed that the tax liability on the turnover on which TDS was effected was not discharged fully. Moreover, the statute allows refund of excess cash balance on account of TDS, only in cases where tax deducted in excess than is required is also paid by the deductor as per CBIC Circular No.125/44/2019 – GST dated 18 November 2019.

2.6.16 Refund of unutilised ITC other than by way of zero-rated supply or inverted duty structure

Audit examined 660 cases out of the 3,517 refund cases relating to zero-rated supply and inverted duty structure, and it was noticed that in three refund cases in three³³ STOs, the assesseees had availed ITC on inputs received for the entire relevant period³⁴ despite the fact that the assesseees were not having zero-rated sales after a certain period in the relevant period³⁵ of refund claim. It was also observed that the proper officers had taken the entire ITC claimed during the relevant period for determining the net ITC. Since the assesseees had not exported any goods during the last months of the relevant period for which refund was claimed, the unutilised ITC accumulated during such months in respect of the goods which were actually kept in stock was not to be refunded as per the provision. Refund of unutilised ITC accumulated during the tax

³⁰ Special Circle, Thiruvananthapuram, Works Contract, Thiruvananthapuram and STO, Adoor.

³¹ Adani Ports and Special Economic Zone Ltd.

³² Karippolil Enterprises.

³³ Special Circle, Kollam and STOs, Ottappalam and Alathur.

³⁴ Relevant period means the period for which the claim has been filed.

³⁵ M/s Sea Land Cashew – April to December 2018 (relevant period), Blissful Garments Pvt Ltd – April 2018 to March 2019 (relevant period), Transcedence Automation Pvt Ltd – April 2019 to March 2020 (relevant period).

periods, after the month of last export invoice, was irregular which amounted to ₹0.12 crore.

The matter was reported to the Government (October 2021). The Government stated (February 2022) that in one³⁶ case order of demand was issued and in another case³⁷, show cause notice was issued to the taxpayer. Reply in the remaining one case is awaited (September 2022).

2.6.17 Non-production of records regarding constitution of Consumer Welfare Fund

The Government of Kerala (GoK), constituted³⁸ the Consumer Welfare Fund and decided to operate a new head of account SH-87 (Consumer Welfare Fund under the Kerala State GST Act, 2017) below the existing head(s) of account MH-8229 and MIH-200.

Audit called for the details regarding the management of the Fund such as modes of crediting to the Fund, amount credited to the Fund, amount utilised from the Fund, Refund given from the Fund etc., which were not made available. Records such as minutes of discussion regarding the constitution of Fund, files relating to the constitution of the Fund, bylaw, if any, for the management of funds, etc. were also not made available to Audit. In a correspondence made by the CGST Department to the Director General of Anti-Profitteering, it was noticed that there was no electronic mode of payment for depositing money in the State Consumer Welfare Fund as of December 2020. In the absence of records/ data/ details, Audit could not ascertain how money was transferred to this Fund, utilisation of money from the Fund, etc. The matter was reported to the Government (October 2021). Reply of the Government is awaited (September 2022).

2.6.18 Conclusion

There was significant delay in issuance of acknowledgement and issuance of refund orders in 35 *per cent* of the cases. There was non-issue/ delay in sanction of provisional refund in 85 *per cent* cases and abnormal delay ranging from one to 311 days in communicating refund orders to the counterpart Tax Authority. There were cases of irregular allowance of refunds in case of inverted duty structure, irregular refund of excess balance in ECL, etc. The deviation ranged from 0.82 *per cent* to 85.44 *per cent* in the audit sample. None of the refund claims were subjected to post-audit. Department did not provide records/ data/ details of the State Consumer Welfare Fund.

³⁶ M/s Blissful Garments Pvt. Ltd.

³⁷ M/s Transcendence Automation Pvt. Ltd.

³⁸ Vide G.O.(Rt)No.1215/2019/Fin dated 18 February 2019.

2.6.19 Recommendations

The Government

- i) should ensure timely refunds as per GSTN formats;
- ii) may conduct post-audit of the refunds which will *inter alia* curtail the possible loss of revenue to exchequer;
- iii) may make available records/ details with respect to Consumer Welfare Fund for examination by Audit.

During the years 2019-21, 148 units under the SGSTD were audited including State Tax Offices/ Assessment circles. Some illustrative cases on application of incorrect rate of tax, incorrect exemption, incorrect assessment and short levy of purchase tax are detailed below:

2.7 Short levy of tax due to application of incorrect rate of tax

Application of incorrect rate of tax on the turnover of ₹312.30 crore resulted in short levy of tax and interest of ₹11.03 crore.

2.7.1. As per Section 8(a)(i) of KVAT Act, 2003, any works contractor who imports any goods into the State from other States or Country for incorporation in the works contracts and or who is registered under the provisions of the CST Act, 1956, may at his option, instead of paying tax in accordance with the provisions of Section 6, pay tax at the rate of seven *per cent* of the whole contract amount for all works contracts undertaken by him subject to certain conditions. The compounded tax payable on the works contracts awarded by GoK, Kerala Water Authority or Local Authorities shall be at five *per cent* on the whole contract amount. Under Section 31(5) of the Act, if the tax or any amount assessed or due under this Act is not paid by any dealer or any other person within the time prescribed, the dealer or the other person shall pay simple interest at the rate of twelve *per cent* per annum.

Audit conducted (April 2019) test check of assessment files and related records in eight Works Contract Circle Offices³⁹. On scrutiny, it was revealed that 31 assesseees out of the 1,156, who opted for paying tax at compounded rate of seven *per cent* for the works contract undertaken by the assessee and five *per cent* on the works contract awarded by the Government of Kerala, Kerala Water Authority or Local Authorities applied incorrect rate of tax on the taxable turnover of ₹312.30 crore instead of the applicable rate as per Section 8(a)(i). The application of incorrect rates of tax resulted in short levy of tax and interest of ₹11.03 crore as detailed in **Appendix - XX**.

On this being pointed out (August 2021), the Government stated (April 2021, September 2021, November 2021, December 2021, February 2022) that in 30 cases assessments were completed creating additional demand of tax. Out of this 30 cases an amount of ₹0.36 crore were collected in 12 cases under amnesty scheme⁴⁰. In the remaining one case reply is awaited (September 2022).

³⁹ Works Contract Offices at Alappuzha, Ernakulam, Kollam, Kottayam, Kozhikode, Malappuram, Mattancherry and Pathanamthitta.

⁴⁰ The Government has unveiled an amnesty scheme to settle outstanding tax dues pertaining to the period before the introduction of the Goods and Services Tax to clear the backlog of arrear demands by waiving interest/ penalty and giving reduction to tax arrears.

It is recommended that the Department may put adequate controls to conduct proper verification of records and ensure that there is no short payment of tax.

Failure of the Assessing Authorities to conduct proper verification of records resulted in short collection of tax and interest of ₹7.54 crore.

2.7.2. As per Section 6(1) (f) of the KVAT Act 2003, in the case of transfer of goods involved in the execution of works contract, where the transfer is not in the form of goods, but in some other form, tax is to be levied at the rate of 14.5 *per cent* and when the transfer is in the form of goods at the rates prescribed under the respective schedules. As per the proviso below the above sub-section the tax payable under Clause (f) in respect of transfer of declared goods not in the form of goods but in some other forms, shall be at the rate prescribed under the respective schedules. Under Section 31(5) of the Act, if the tax or any amount assessed or due under this Act is not paid by any dealer or any other person within the time prescribed, the dealer or the other person shall pay simple interest at the rate of twelve *per cent* per annum.

During 2018-19 and 2019-20, Audit test-checked the assessment files and connected records of 663 out of 10,026 works contractors registered in the four Works Contract Circle Offices⁴¹ for the period 2017-18. On scrutiny, it was revealed that five assesseees who opted for paying tax at non-compounded rate applied incorrect rate of tax on the taxable turnover. The failure of the Assessing Authorities to conduct proper verification of records while finalising the assessment resulted in short collection of tax and interest of ₹7.54 crore as detailed in **Appendix - XXI**.

On this being pointed out (July 2021) the Government stated (February 2022) that the assessment has been completed in four cases creating additional demand. In the case of M/s Larsen Toubro Limited, the Government replied (February 2022) that purchase of iron and steel only has been taken into consideration. But the claim of declared goods reported by the assessee includes the value of pipes, steel structurals and other steel items such as bars, sheets, hoops, strings, discs, rings, plates, forgings, tools, alloys and special steel of any other categories, etc. which are also defined under Section 14 of CST Act, 1956. The purchase of these items were reported under Part E and F columns of the return in Form No. 10B. Hence as per the revised quarterly returns and invoice-wise purchase statement uploaded along with returns, the total purchase of declared goods during the year is ₹83.73 crore. The purchase value to be considered is the net value after adjusting stock element and after deducting value of goods used in the course of work and the property which is not transferred to clients. To this net purchase value, gross profit is added to arrive at the transfer value.

⁴¹ Works Contract Offices at Ernakulam, Kottayam, Mattancherry and Pathanamthitta.

Therefore, the taxable turnover at five *per cent* of ₹126 crore is as per books of accounts and rate of tax applied is found correct.

The reply is not acceptable. As per the turnover of purchases/ stock transfer, returned under Part E and F columns of the return filed in Form No. 10B, the five *per cent* taxable items, other than Iron and Steel, reported by the assessee were plastic articles, pipes of all kinds, metallic products, cables of all kinds, aluminium products etc. None of these items comes under the items declared under Section 14 of CST Act 1956. It was also stated that the total purchase value of declared goods (including pipes and other five *per cent* taxable items) was ₹83.74 crore and the net purchase value should be arrived after adjusting stock element and after deducting value of goods used in the course of work and the property which is not transferred to clients. As per the statement furnished along with the reply, there was reduction in the stock during the year and there were goods used but not transferred to the clients. Hence, the net purchase value must be much lower than ₹83.74 crore and as per accounts the *per cent* of gross profit is about 8.50. Therefore, the transfer value will be ₹75.22 crore as worked out by Audit as against the claimed turnover of ₹126.37 crore. Moreover, the bifurcated purchase and stock of the declared goods as claimed was also not submitted with the reply. As such transfer of those five *per cent* items, not declared under Section 14 of CST Act 1956, into the execution of works contract attracts 14.5 *per cent* tax.

It is recommended that the Assessing Authorities shall conduct proper verification of records and ensure that the correct rate of tax is applied.

2.8 Short levy of tax due to incorrect exemption

Ineligible exemption claimed through the annual returns resulted in short levy of tax and interest of ₹9.72 crore.

2.8.1 As per Section 8(a) of KVAT Act 2003, tax at the compounded rate is payable for the whole of contract amount received. Explanation I below this Section provides that the 'whole contract amount' shall not include the amount paid to sub-contractors for execution of the portion of works contracted, if the sub-contractor is a registered dealer liable to pay tax. As per Section 10, every awarder shall deduct from every payment made by him to any works contractor, tax payable by the contractor in respect of works contract awarded. Rule 42(2) of KVAT Rules 2005, provides that the awarder making such deduction shall pay the amount so deducted to the Assessing Authority along with a statement in Form No. 20C. Under Section 31(5) of the Act, failure to pay tax or any amount assessed or due, within the time prescribed, shall lead to payment of simple interest at the rate of twelve *per cent* per annum.

Audit test-checked records of 226 out of 3,573 works contractors registered in the Works Contract Circle Office, Ernakulam for the period 2015-16 and 2016-17. It was noticed that the assessee, Kerala State Construction Corporation Ltd. claimed exemption for ₹546.14 crore and ₹476.77 crore in the annual return for the years 2015-16 and 2016-17 respectively for sub-contractor payments. The claim of exemption was not supported by the declaration certificate in Form 20H⁴². The verification of the awardee details in the KVATIS further revealed that the dealer awarded sub contract works to various dealers for an amount of ₹428.12 crore and ₹435.73 crore for the years 2015-16 and 2016-17 respectively. The ineligible exemption of ₹159.06 crore claimed through the annual returns resulted in short levy of tax and interest amounting to ₹9.72 crore.

On this being pointed out (November 2020) the Government stated (September 2021) that the assessment was completed (July 2021) creating an additional demand of ₹5.08 crore for the year 2015-16 and ₹1.47 crore for the year 2016-17. Further progress is awaited (September 2022).

It is recommended that the Assessing Authorities may insist on the dealers to file declaration in Form 20H for which exemption is claimed.

Excess claim of eligible component as exemption in the annual return resulted in short levy of tax and interest amounting to ₹1.37 crore.

2.8.2 As per Rule 10(2)(a) of the KVAT Rules, 2005, works contract in which transfer of property takes place not in the form of goods but in some other form, the taxable turnover in respect of the transfer of property involved can be determined by allowing the deductions viz., labour charges for the execution of work, charges for planning and designing and architect fee, charges for obtaining on hire or otherwise, machinery and tools used for the execution of works contract, cost of consumables used, cost of establishment and overhead charges of the dealer to the extent it is relatable to the labour and services, profit earned to the extent it is relatable to the labour and services, amount paid to the sub-contractors as consideration for execution of the works contract whether wholly or partly subject to the production of prescribed certificate. Besides, according to Section 10(2)(b) of the Act, when labour and other charges are not ascertainable from the books of accounts maintained by the dealer engaged in the installation of elevators and escalators, the table below Rule 10(2)(b) of KVAT Rules provides for deduction of 15 percentage of the value of the contract as labour and other charges. Under Section 31(5) of the KVAT Act, 2003 failure to pay tax or any amount assessed or due, within the time prescribed attracts simple interest at the rate of twelve *per cent* per annum.

⁴² Declaration issued by the sub contractor to the principal contractor committing that tax in respect of the contract amount would be paid by the sub contractor.

Scrutiny of the records (October 2019) of the STO, Works Contract, Mattancherry revealed that an assessee M/s Kunnel Engineers and Contractors Private Limited showed contract receipts for non-compounded works as ₹31.69 crore and ₹23.95 crore in the annual returns for the years 2013-14 and 2015-16. The assessee claimed exemption from payment of tax by virtue of Rule 10 for ₹18.48 crore and ₹14.99 crore respectively in the annual returns for these years. Thus, deduction of 58 *per cent* and 63 *per cent* over the total non-compounded receipts was availed by the assessee in the respective years. As per the certified accounts, the exemptions as per Rule 10 of KVAT Rules were only 49 *per cent* and 52 *per cent* respectively for the years 2013-14 and 2015-16. The claim in excess of eligibility of labour component as exemption in the annual return resulted in short levy of tax and interest amounting to ₹1.37 crore.

On this being pointed out (November 2020), the Government stated (February 2021) that the assessments were completed for the years 2013-14 and 2015-16 creating an additional demand of ₹0.54 crore and ₹0.09 crore respectively and the demand notice was issued on February 2020 and March 2020 and is under revenue recovery (September 2022).

It is recommended that the Assessing Authorities may limit the claim of exemptions on the basis of Rule 10 of KVAT Rules.

2.9 Short levy of tax due to incorrect assessment

Incorrect assessment by the Assessing Authority resulted in short levy of tax and interest amounting to ₹6.36 crore.

2.9.1 As per Section 6(1) of KVAT Act, 2003, tea is taxable at the rate of five *per cent* as per entry 128 of third schedule to KVAT Act. Rule 10(1)(h)(i) of KVAT Rules, 2005, provides that at the time of determining taxable turnover, the turnover of sales or purchases made by a dealer through his agent in respect of which tax has been paid by the agent can be deducted from the total turnover of the dealer. However, to avail such deduction, the principal or agent claiming the deduction should furnish a declaration in Form 25F issued by the principal or agent, as the case may be.

Scrutiny (March 2021) of the assessment and refund files in the STO, Idukki, revealed that, an assessee, M/s Kannan Devan Hill Plantations Company Pvt. Ltd., claimed exemption from payment of tax for the sales turnover of tea amounting to ₹95.24 crore and ₹94.47 crore in the annual returns for the years 2012-13 and 2013-14 respectively. The tax due for these exempted turnovers were ₹4.76 crore and ₹4.72 crore for the respective years as per Section 6(1) of KVAT Act. The assessee claimed exemption as per Rule 10(1)(h)(i) of KVAT Rules. According to the certified copy obtained from the Deputy Commissioner, Idukki the assessee filed form 25F declarations for the years

2012-13 and 2013-14 which disclosed the sales turnover as ₹95.53 crore and ₹94.47 crore respectively. Further, the tax declared to be paid by agents through Form 25F were ₹3.16 crore and ₹3.17 crore only for the respective years.

Rule 10(1)(h)(i) of KVAT Rules, 2005 mandates that the turnover of sales or purchase made by the dealer through his agent in respect of which tax has been paid by the agent can only be deducted from the total turnover of the dealer. Hence, the assessee was eligible for a deduction in tax of ₹3.16 crore and ₹3.17 crore only for the respective years. However, the assessee availed deduction of ₹4.76 crore and ₹4.72 crore from the total tax payable for these years. Thus, there was a short payment of tax for these two years amounting to ₹1.60 crore and ₹1.55 crore.

The assessment for the year 2012-13 was completed in March 2019 and modified in May 2020 and the assessment for the year 2013-14 was completed in November 2019. However, while completing the assessments, the Assessing Authority failed to detect the short payment of tax for these two years. This resulted in short levy of tax and interest amounting to ₹5.34 crore.

On this being pointed out (October 2021), the Government stated (January 2022) that the assessment for the years 2012-13 and 2013-14 is completed by creating an additional demand of ₹3.83 crore and ₹2.95 crore respectively. Further progress is awaited (September 2022).

It is recommended that the Assessing Authorities shall conduct proper verification of records and ensure that there is no short payment of tax.

2.9.2 According to Section 6(2) of KVAT Act, 2003 every dealer who purchases taxable goods from any person other than a registered dealer shall pay tax on the purchase turnover of goods at the scheduled rate. Section 12 of KVAT Act, 2003 provides that in calculating the net tax payable by the dealer for a return period there shall be deducted from the tax payable for the return period a sum equal to the tax paid under Section 6(2). As per third proviso below Section 12(1), where the sale in the course of inter-state trade is exempted from tax, the special rebate under this section shall be limited to the amount of tax paid in excess of five *per cent* under Section 6(2). Interstate sale of natural rubber supported with C Form is exempted from tax as per GO(P) No.181/2011/TD dated 30 November 2011.

Audit test-checked (February 2020) 166 out of 738 records in the Office of the Assistant Commissioner, Special Circle, Kottayam. It was noticed that in the case of the assessee M/s Kaduthuruthy Rubber Marketing and Processing Society, the annual return for 2012-13 showed the purchase of rubber sheet from unregistered dealer as ₹31.72 crore and inter-state sales of rubber as ₹13.30 crore. The assessment was finalised (July 2018) by allowing special rebate of two *per cent* under Section 12 of KVAT Act on the turnover of

₹10.03 crore supported with Form C, whereas the inter-state sale of natural rubber was exempt from tax. The tax due under Section 6(2) for the purchase turnover of rubber sheets from unregistered dealers and sold within the State with the support of Form C is ₹0.50 crore (tax at the rate of five *per cent* for the turnover of ₹10.03 crore). The Assessing Authority failed to disallow the special rebate under Section 12 of KVAT Act to the assessee. Incorrect assessment resulted in short levy of tax and interest amounting to ₹0.67 crore.

The Government stated (November 2021) that the assessment in respect of the assessee was revised creating an additional demand of ₹1.01 crore as tax and interest. The dues outstanding are under revenue recovery (September 2022).

It is recommended that the Assessing Authorities shall check the returns thoroughly to avoid omissions while finalising the assessment.

2.9.3 Section 8(a)(ii) of KVAT Act stipulates that a works contractor, instead of paying tax in accordance with provisions of Section 6, can opt to pay tax at three *per cent* of the contract amount, after deducting the purchase value of goods excluding freight and gross profit element, purchased from outside the State. For the purchase value of goods so deducted the contractor should pay tax at the scheduled rate applicable to such goods.

Audit checked (February 2021) all the 31 assessment completed cases during 2019-20 in the STO, Works Contract, Kottayam. In the case of assessee M/s Vettoor Construction Engineers Private Limited it was noticed that as per the annual return the assessee remitted tax at the rate of three *per cent* on the total contract amount of ₹14.41 crore. As per Section 8(a)(ii) of KVAT Act the assessee was to pay tax at the rate of three *per cent* for the total contract amount of ₹14.41 crore after deducting the purchase value of goods purchased from outside the State (₹1.29 crore). For the purchase value of goods so deducted (₹1.29 crore) the assessee has to pay tax at the scheduled rate of 12.5 *per cent*. Further, the assessee remitted tax at the rate of 12.5 *per cent* for the inter-state purchase turnover of ₹0.31 crore, but did not pay tax for the inter-state purchase turnover of ₹0.98 crore. The Assessing Authority failed to invoke the provisions as per Section 8(a)(ii) of KVAT Act and assessed tax only for the suppression detected by the State Tax Officer (Intelligence) for ₹0.85 crore. These omissions on the part of Assessing Authority led to the incorrect assessment which resulted in short levy of tax and interest amounting to ₹0.19 crore.

On this being pointed out (September 2021), the Government stated (February 2022) that the case was reopened and created a demand of ₹0.13 crore after giving credit to all the amounts paid during the appeal stage of the original assessment order. Further progress is awaited (September 2022).

2.9.4 As per Section 8(a) of KVAT Act, 2003 as amended by Kerala Taxation Law Amendment Act 2014, a works contractor who is registered

under CST Act or who is an importer shall be liable to pay compounded tax at the rate of seven *per cent*. Proviso to this section states that the compounded tax payable by a works contractor in respect of works contract awarded by GoK, Kerala Water Authority or Local Authorities shall be five *per cent* with effect from 01 April 2014.

Audit checked (February 2021) all the 31 assessment completed files, during 2019-20 in the STO, Works Contract, Kottayam. In the case of an assessee M/s S J Enterprises it was noticed that as per the audited accounts for the year 2015-16 the assessee received contract receipt of ₹2.73 crore for Non-Government work and ₹5.74 crore for Government work. While finalising the assessment for the year 2015-16 in December 2018 the Assessing Authority levied tax at the rate of seven *per cent* for ₹ 0.07 crore, five *per cent* for ₹5.04 crore and three *per cent* for ₹3.36 crore. As per Section 8(a) of KVAT Act, 2003 as amended vide Kerala Taxation Law Amendment Act 2014, the assessee was liable to pay tax at the rate of seven *per cent* for Non-Government work amounting to ₹2.73 crore and five *per cent* for Government work amounting to ₹5.74 crore. The incorrect assessment by the Assessing Authority resulted in short levy of tax and interest amounting to ₹0.16 crore.

On this being pointed out (September 2021), the Government stated (February 2022) that revised orders were issued creating demand of ₹0.20 crore and the dealer opted for amnesty scheme 2021 to settle the demand. Further progress is awaited (September 2022).

It is recommended that the Assessing Authorities may be advised to cross check all the mandatory checks before finalising the assessment.

2.10 Non-recovery of tax due to incorrect assessment

Failure of the Assessing Authority to disallow the credit already given resulted in short levy of tax and interest of ₹0.64 crore.

As per Section 66 of KVAT Act, 2003, any authority including Appellate Tribunal and Settlement Commission issuing any order or proceedings under this Act may, on application or otherwise, at any time within four years from the year in which the order was passed by it, rectify any error apparent on the face of the record.

Audit test-checked 136 assessment files of the STO, Works Contract, Palakkad. It was noticed (May 2018) in the case of M/s Oceanus Dwellings Private Limited that while completing the assessment for the first quarter of 2011-12 in February 2012, ITC, advance tax and tax paid totaling to ₹0.38 crore paid along with the return was allowed as credit. This credit was again allowed while fixing tax for the remaining period in December 2017. The failure on the part of the Assessing Authority to disallow the credit already allowed resulted in short levy of tax and interest of ₹0.64 crore.

On this being pointed out (July 2021), the Government stated (January 2022) that the error apparent on the face of the record was rectified and revised assessment order was passed creating a demand of ₹1.53 crore and revenue recovery proceedings are initiated. Further progress is awaited (September 2022).

It is recommended that the Assessing Authorities shall check all the previous assessments done in respect of the assessee before completing the final assessment of the relevant period.

2.11 Short levy of tax due to incorrect application of concessional rate

Incorrect application of concessional rate of five per cent instead of 14.5 per cent resulted in short levy of tax and interest amounting to ₹0.61 crore.

Proviso below Section 6(1)(f) of KVAT Act provides that where sale of goods other than petroleum products, manufactured in the State is to Kerala State Electricity Board (KSEB), the tax payable under clause 6(1)(d) (i.e. 14.5 per cent) shall, subject to such conditions and restrictions as may be prescribed, be at five per cent. Rule 12C(5) of KVAT Rules provides that every dealer who is a manufacturer effects any sale of taxable goods manufactured by him in the State to KSEB shall furnish a declaration in Form No. 48 duly signed and sealed by the buyer and produce on demand for verification by any authority under the Act.

Audit test checked (February 2021) 68 out of 106 assessment files for the period 2019-20 in the STO, Works Contract, Kottayam. It was observed that the assessments of the assessee M/s Pooja Industries, for the years 2015-16 and 2016-17 were completed in May 2019 and December 2019 respectively. Audit noticed that the assessee furnished Form 48 for the turnover of ₹9.42 crore out of ₹11 crore and ₹11.15 crore out of ₹13.82 crore for the years 2015-16 and 2016-17 respectively. The turnover not covered in Form 48 was received from KSEB in the form of transportation charge, hire charge and price revision. The turnover not covered by Form 48 was taxable at the rate of 14.5 per cent as per Section 6(1)(d) of KVAT Act. The Assessing Authority failed to notice the same and levied tax at the concessional rate of five per cent on the turnover not covered by Form 48. This resulted in short levy of ₹0.40 crore and ₹0.21 crore towards tax and interest respectively.

On this being pointed out (August 2021) the Government stated (January 2022) that for the years 2015-16 and 2016-17 the transportation and hire charges are related to sales effected to KSEB and the concessional rate availed is supported by Form 48 declaration. As such there is no irregularity in assessing the transportation and hire charges received and the self assessed price variation at five per cent.

The reply is not acceptable, as Explanation III(i) below Section 2(lii) states that the amount for which goods are sold shall include any sum charged for anything done by the dealer in respect of the goods sold at the time or before delivery thereof. Tax is levied on the entire turnover which includes material value as well as expenses incurred by the assessee at the time or before the delivery of materials.

It is recommended that an adequate system be put in place to cross check all the mandatory records before finalising the assessment.

2.12 Non-levy of tax

Omission to levy tax by the Assessing Authority for a turnover of ₹2.62 crore resulted in short collection of tax and interest of ₹0.30 crore.

As per Section 3(4) of KVAT Act, all officers and persons employed for the execution of the Act shall observe and follow the orders, instructions and directions of the officers superior to them.

Audit test checked 114 (50.22 per cent) out of 227 assessment files for the period 2019-20 in the STO, Special Circle, Palakkad in January 2021. It was observed that the assessment for the period 2011-12 of the assessee M/s Rathna Steels was originally completed in August 2016 with a total turnover of ₹20.04 crore creating an additional demand of tax of ₹0.07 crore. The assessee filed appeal against this order. While examining the documents produced by the assessee, the Deputy Commissioner (Appeals) dismissed the appeal in March 2018 and observed that the turnover to the tune of ₹4.8 crore was not assessed. The Appellate Authority ordered in March 2018 that the Assessing Authority shall initiate separate assessment for assessing the under assessed turnover only. Audit noticed in January 2021 that while completing the assessment in August 2018 the Assessing Authority omitted to levy tax on the turnover of ₹2.62 crore resulting in short collection of tax and interest of ₹0.30 crore.

On this being pointed out (July 2021) the Government (September 2021) stated that the assessment was completed creating an additional demand of ₹0.37 crore. The dues outstanding are under revenue recovery. Further progress is awaited (September 2022).

It is recommended that cross checking the details available in the previous assessment orders, if any pertaining to the period, would enable avoiding any omissions while finalising the assessments.

2.13 Short levy of tax due to irregular allowance of ITC

The Assessing Authority allowed claim of ITC for the subsequent exempted sale which resulted in short levy of tax and interest of ₹0.13 crore.

Section 6(1) of KVAT Act 2003 states that cardamom is taxable at the rate of five *per cent* as per entry 120 (6)(c) of third schedule to KVAT Act. Rule 12A of KVAT Rules 2005 specifies that where taxable goods are used during a return period partly in relation to taxable transaction and partly in relation to exempted or non-taxable transaction, the input tax paid or special rebate to which the dealer has become entitled to during such return period shall be apportioned between taxable and exempted or non-taxable transactions on the basis of the ratio of taxable and exempted turnover during the period in which the ITC or special rebate or refund is claimed.

Audit checked (March 2021) all the 36 VAT assessments completed during 2019-20 in the STO, Kattappana. Scrutiny of the assessment files revealed that the assessee M/s Green Valley Spices, in the annual return for the year 2016-17, disclosed ₹2.81 crore as exempted sales of cardamom at auction center for the period from April 2016 to July 2016. During the same months, the purchase of cardamom from registered dealers was shown as ₹2.37 crore for which the assessee availed ITC of ₹0.09 crore. The ITC availed for purchases from registered dealers for subsequent exempted sale was to be disallowed in accordance with the provision envisaged in Rule 12A. The Assessing Authority allowed this irregular ITC availed by the assessee, which resulted in short levy of tax and interest of ₹0.13 crore.

On this being pointed out (September 2021), the Government stated (January 2022) that the assessment for the year 2016-17 was completed creating an additional demand of ₹0.34 crore. Further progress is awaited (September 2022).

It is recommended that the Assessing Authorities shall conduct proper verification of records and ensure that ineligible input tax credit is not availed by the assesseees.

2.14 Short levy of purchase tax and excess claim of special rebate

Incorrect assessment by allowing ineligible exemption and by not limiting the special rebate to the extent of output tax paid resulted in short levy of tax and interest amounting to ₹0.12 crore.

Section 12(1) of KVAT Act allows a rebate equal to the tax paid under Section 6(2) to the dealer. This amount (special rebate) shall be deducted from the tax payable for the return period to arrive at the net tax payable by the dealer,

provided the special rebate shall not exceed the output tax payable in respect of such goods or goods manufactured out of such goods. As per proviso below Section 6(1) of KVAT Act, the tax on sale of cardamom, at the point of auction only, conducted at the auction center shall be at the rate of two *per cent* and as per Section 6(2) of KVAT Act, every dealer who purchases cardamom from any unregistered dealer is liable to pay purchase tax on the purchase turnover of cardamom at the rate of five *per cent*.

Audit checked all the 32 assessment files of STO, Vandiperiyar for the years 2016-17 and 2018-19. It was noticed that during 2016-17, the assessee M/s Perumpallil Spices, purchased cardamom from unregistered dealers for ₹3.37 crore and sold cardamom at auction centre for ₹3.33 crore and claimed exemption from payment of tax. The assessee claimed tax exemption through Form 25F⁴³ stating that the auction centre paid the tax. The assessee also claimed exemption from payment of tax for ₹1.51 crore on the local purchase of cardamom from unregistered dealers and special rebate of ₹ 0.09 crore for cardamom in the annual return.

Audit verified Form 25F produced by the assessee and observed that the auction centre remitted ₹0.06 crore instead of ₹0.07 crore as output tax for the sale of cardamom valued at ₹3.33 crore. As per Section 12(1) of KVAT Act, the special rebate on account of this sale cannot exceed the output tax paid and the special rebate eligible to the assessee was ₹0.06 crore. Besides, the assessee was liable to pay tax on the cardamom valued at ₹3.37 crore purchased from unregistered dealer, except for the closing stock of cardamom available with the assessee, under Section 6(2) of KVAT Act at the rate of five *per cent*.

The Assessing Authority completed the assessment for the year 2016-17 in July 2018 by allowing the exemption claimed by the assessee on purchase from unregistered dealer. Further, the Assessing Authority did not limit the special rebate for cardamom sale to ₹0.06 crore as stipulated in the Act. This resulted in short levy of tax and interest amounting to ₹0.12 crore.

On this being pointed out (October 2021) the Government stated (February 2022) that the assessment for the year 2016-17 was completed creating an additional demand of ₹0.15 crore. Further progress is awaited (September 2022).

It is recommended that the Assessing Authorities may check Form 25F before allowing the exemption in respect of payment made by the Principal/ Agent.

⁴³ Form 25F-Declaration of payment of tax by the Principal/ Agent.

2.15 Short levy of purchase tax due to excess availment of special rebate

Excess allowance of special rebate availed by the assessee resulted in short levy of tax and interest amounting to ₹0.21 crore.

Section 12(1)(a) of KVAT Act 2003 stipulates that the net tax payable by a dealer for a return period shall be deducted from the tax payable for the return period⁴⁴, a sum equal to the tax paid under Section 6(2) and as per fourth proviso to Section 12(1)(b) of the Act, the special rebate shall not exceed the output tax payable in respect of such goods or goods manufactured out of such goods. According to proviso below Section 6(1) of KVAT Act, the tax on sale of cardamom, at the point of auction only, conducted at the auction center shall be at the rate of two *per cent* and as per Section 6(2) of KVAT Act, dealer who purchases cardamom from any unregistered dealer is liable to pay purchase tax⁴⁵ on the purchase turnover of cardamom at the rate of five *per cent*.

Audit scrutinised 70 self assessment files of STO, Idukki for the years 2015-16 and 2016-17 during November/ December 2019 and noticed that the assessee, M/s K E Zidhique, in the annual returns disclosed purchase of cardamom from unregistered dealers as ₹2.94 crore and ₹2.34 crore for 2015-16 and 2016-17 respectively. The assessee was liable to pay tax on this purchase turnover at the rate of five *per cent*. During the same period the sale of cardamom at auction centre was shown as ₹2.98 crore and ₹1.89 crore for which the assessee was liable to pay output tax at the rate of two *per cent*. As per Section 12(1)(b) read with Section 6(1) of KVAT Act, the assessee was eligible to avail special rebate at the rate of two *per cent* only for the amount of goods sold at auction centre which comes to ₹0.06 crore and ₹0.04 crore respectively. However, the assessee availed special rebate at the rate of five *per cent* amounting to ₹0.15 crore and ₹0.09 crore respectively for the corresponding years. Special rebate availed in excess of eligibility resulted in short levy of tax and interest amounting to ₹0.21 crore for the years 2015-16 and 2016-17.

On this being pointed out (September 2021), the Government stated (February 2022) that based on the audit observation assessment for the years 2015-16 and 2016-17 were completed by creating a demand of ₹0.14 crore and ₹0.06 crore for the years 2015-16 and 2016-17 respectively on March 2021. The dealer filed appeal before the first Appellate Authority and the case is now pending disposal with the First Appellate Authority (The Joint Commissioner

⁴⁴ As per Section 2(xli) of KVAT Act 2003 'Return period' means and includes a calendar month or a quarter of an year or an year.

⁴⁵ As per Section 6(2) of the KVAT Act 2003 'every dealer who purchases taxable goods from any person other than a registered dealer shall pay tax on the purchase turnover of goods at the rates specified under sub-section (1)'.

(Appeals)). No action can be initiated for recovery of revenue till the appeal is disposed, hence the Department should make efforts for timely disposal of the appeal so that the revenue due to the Government is received without delay.

It is recommended that the Assessing Authorities may insist the dealers to claim eligible special rebate on the basis of Section 6 and Section 12 of the KVAT Act.

2.16 Short levy of purchase tax

The Assessing Authority failed to identify the short payment of purchase tax while issuing the pre-assessment notice resulting in short levy of tax and interest of ₹0.18 crore.

Section 12(1) of KVAT Act allows a rebate equal to the tax paid under Section 6(2) to the dealer. This amount (special rebate) shall be deducted from the tax payable for the return period to arrive at the net tax payable by the dealer, provided the special rebate shall not exceed the output tax payable in respect of such goods or goods manufactured out of such goods. As per proviso below Section 6(1) of KVAT Act, the tax on sale of cardamom, at the point of auction only, conducted at the auction center shall be at the rate of two *per cent* and as per Section 6(2) of KVAT Act, every dealer who purchases cardamom from any unregistered dealer is liable to pay purchase tax on the purchase turnover of cardamom at the rate of five *per cent*.

As per the Kerala Finance Bill 2016, the sale of cardamom, at the point of auction, was exempted from tax for the period 01 April 2016 to 17 July 2016. Later, Commissioner of Commercial Taxes vide Circular No.18/2016 dated 27 August 2016 declared that the sale of cardamom conducted at the auction centre is to be taxed at two *per cent* with effect from 18 July 2016.

Scrutiny of the assessment and refund files in the STO, Kattappana revealed that the annual return of the assessee M/s Green Valley Spices for the year 2016-17 showed purchase of cardamom from unregistered dealers as ₹7.81 crore against which an exemption from payment of tax was claimed for a turnover of ₹3.64 crore. An amount of ₹0.21 crore was shown as output tax due for the balance turnover of ₹4.17 crore. In addition, the assessee claimed special rebate of ₹0.20 crore from the tax payable. This special rebate was claimed on a turnover of ₹3.93 crore relating to the purchase of cardamom from unregistered dealers in the annual return. The assessee sold cardamom at the auction centre for ₹12.32 crore during the year and claimed exemption for the entire amount.

Three exemptions claimed by the assessee in the annual return cannot be allowed by the Assessing Authority due to following reasons:

- i. The sale at auction centre during April 2016 to July 2016 was ₹2.82 crore out of ₹12.32 crore. During this period, the sale at auction centre was fully exempted from payment of tax. The assessee was liable to pay output tax for the balance turnover of ₹9.50 crore at the rate of two *per cent* for the period from August 2016 to March 2017.
- ii. Total sales turnover of cardamom was for ₹17.52 crore. Percentage of taxable sales affected at the auction centre to that of the total sales of cardamom is 54.2 *per cent* which comes to ₹4.23 crore. The assessee is eligible to avail special rebate from tax payable at the rate of two *per cent* only for the value of goods purchased from unregistered dealers (₹4.23 crore) and sold at auction centre. Balance tax payable under Section 6(2) for ₹4.23 crore at the differential rate of three *per cent* with interest works out to ₹0.18 crore.
- iii. The exemption from payment of purchase tax on a turnover of ₹3.64 crore was availed without enabling any provision in the Act or Rules.

Moreover, while issuing the pre-assessment notice in August 2020 the Assessing Authority failed to identify the short payment of tax. This resulted in short levy of tax and interest of ₹0.18 crore.

On this being pointed out (October 2021), the Government stated (January 2022) that the assessment for the year 2016-17 was completed by creating an additional demand of ₹0.34 crore. Further progress is awaited (September 2022).

It is recommended that the Assessing Authorities shall conduct proper verification of records to ensure that excess exemption is not claimed by the assessee and that there is no short payment of purchase tax.

KGST

2.17 Short levy of tax due to incorrect assessment

Incorrect assessment of turnover by the Assessing Authority resulted in short levy of tax and interest of ₹12.38 crore.

Section 5(a) of KGST Act, 1963 stipulates that every dealer who, in the course of his business, purchases from a registered dealer or from any other person any goods, the sale or purchase of which is liable to tax under this Act, in circumstances in which no tax is payable, under sub-section (1), (3), (4) or (5) and dispatches them to any place outside the State except as a direct result of sale or purchase in the course of inter-state trade or commerce; shall, whatever be the quantum of the turnover relating to such purchase for a year, pay tax on the taxable turnover relating to such purchase for the year at the rates mentioned in Section 5. As per Section 5(1)(a) of the Act, sale of Aviation Turbine Fuel (ATF), Motor Spirit (MS) and High Speed Diesel (HSD) by an Oil Marketing Company (OMC) to another OMC is exempted.

According to Section 6A of CST Act, 1956 read with Rule 12(5) of CST (Registration & Turnover) Rules, 1957, movement of goods from one State to another occasioned not by the reason of sale and the physical movement properly proved shall be exempted from tax in the State.

Audit test checked the assessment and related records in the STO, Special Circle II, Ernakulam. In the case of assessee M/s Indian Oil Corporation Limited, it was noticed that the assessment for the years 2012-13 and 2013-14 were completed in October 2018 and March 2019 respectively. Scrutiny of the assessment orders (February 2021) and related documents revealed that the assessee made local purchase of ATF from M/s Bharat Petroleum Corporation Ltd, a registered dealer in the State, for ₹899.72 crore and ₹1,074.33 crore for these years. The purchase of ATF from another OMC is exempted from payment of tax under Section 5(1) of KGST Act. The assessee transferred the ATF outside the State to the tune of ₹6.53 crore and ₹14.22 crore in 2012-13 and 2013-14 respectively without payment of tax, in violation of conditions as stipulated in Section 6A of CST Act. Failure of the Assessing Authority to levy tax under Section 5(A) of KGST Act for the turnover of ATF purchased without payment of tax and subsequent transfer outside the State other than by way of sale at the time of assessment for the years 2012-13 and 2013-14, resulted in short levy of tax and interest of ₹12.38 crore.

On this being pointed out (September 2021), the Government stated (February 2022) that as the time for revising the assessment order expired, the request to invoke the power of *suo motu* revision under Section 35 of KGST Act, 1963 is submitted. Further progress is awaited (September 2022).

It is recommended that the Department should initiate action to recover the dues to the Government before the expiry of the limitation period under Section 35 of KGST Act, 1963 and also instruct the Assessing Authorities to strictly carry out all the mandatory checks before finalising the assessments.

2.18 Short levy of tax due to allowance of irregular exemption

Irregular exemption granted by the Assessing Authority resulted in short levy of tax and interest amounting to ₹0.69 crore.

The Government of Kerala vide G.O.(P)No.47/05/TD dated 31.03.2005 (SRO No.319/2005) issued notification which superseded all earlier notifications issued under Section 10 of KGST Act granting exemptions and/ reduction in the rate, in respect of the tax payable under the Act. As per SRO No. 319/2005, sale to Special Economic Zone (SEZ) is not exempted from payment of tax.

Audit scrutinised the assessment files and related records in the STO, Special Circle II, Ernakulam in January 2021. It was noticed that in the case of the assessee, M/s Bharat Petroleum Corporation Limited, the Assessing Authority while finalising the assessment for the year 2008-09 in March 2019 allowed exemption of ₹1.26 crore claimed by the assessee towards the sale of HSD to the SEZ as per SRO No. 151/2004. As per, SRO No.319/2005 sale to SEZ is not exempted. The exemption granted by the assessing officer for the sales turnover of HSD to SEZ was irregular which resulted in short levy of tax and interest amounting to ₹0.69 crore.

On this being pointed out (September 2021) the Government stated (February 2022) that as the time for revising the assessment order had expired, the Deputy Commissioner had submitted the request to invoke the power of *suo motu* revision under Section 35 of the KGST Act 1963 and a notice had been issued to the dealer. The dealer raised the contention that the order is barred by limitation of time and stated that as per the Hon'ble High Court order in WP (C) No.14467/2019 and WC (C) No. 21031/2019 dated 22 October 2019 stay was granted against the assessment order and demand notice, with direction to refrain from taking any coercive steps against the dealer in the above assessments.

The reply of the Government that the assessee raised the contention that the order is barred by order of limitation and is stayed by Hon'ble High Court in 2019 is not acceptable for the reasons stated below:

- i) The interim stay furnished to Audit was for the assessment year 2008-09 on the CST assessment.
- ii) The Audit objection is with reference to KGST assessment for the year 2008-09.

- iii) The Audit objection is not time barred. According to Section 17(7) of KGST Act 1963, extension of period for assessment was given by the Deputy Commissioner from time to time. The assessment for the year 2008-09 was completed on 25 March 2019. As per Section 17(4) of KGST Act, the assessment of the dealer for the previous five years can be reopened and the limitation prescribed will not apply.

It is the responsibility of the Department to get the interim stay orders vacated timely and safeguard the financial interest of the State.

It is recommended that the Government may put in place a system wherein the Assessing Authority has to mandatorily check all the relevant Government orders before finalising the assessment.