



Chapter III
State Excise

CHAPTER-III STATE EXCISE

3.1 Tax Administration

The Kerala State Excise is the law enforcement agency that administers laws relating to liquor, narcotic drugs and psychotropic substances and medicinal preparations containing alcohol and narcotics in the State. Kerala Excise department has its headquarters in Thiruvananthapuram. The principal duties of the department are protection, augmentation and collection of excise revenue and enforcement of the acts and various rules made thereunder. The duties of the department are broadly classified as collection of revenue, enforcement activity to prevent illicit liquor production, sale and trafficking and campaign against alcoholism. Liquor includes spirits of wine, arrack, spirits, wine, toddy, beer and all liquid consisting of or containing alcohol. An individual has no fundamental right over the manufacture and trade of liquor. Absolute right on liquor is vested with the State. Government formulates Abkari policy of the State every year. The policy formulated by the State Government is implemented by the Excise department.

3.2 Internal Audit

The Internal Audit Wing (IAW) in State Excise department is under the direct control of the Excise Commissioner. The Wing consists of one Joint Commissioner of Excise assisted by one Assistant Excise Commissioner, three Superintendents, four Excise Inspectors and eight Preventive Officers. Offices in districts in which more vehicles are seized, collectable revenue are pending and delay in collection is noticed are prioritised in internal audit. The total number of auditable units in the department is 295 (sub-offices) which is required to be audited annually. However, due to insufficient manpower resources, only 36 units (12 *per cent*) were planned for audit during 2023-24. IAW audited all 36 units planned. During the year, out of the 2,272 outstanding observations, department cleared 591 internal audit observations (26.01 *per cent*).

3.3 Results of Audit

There were 24 auditable units during 2023-24 in the State Excise department. Out of these, five units were selected for audit. Scrutiny of the records of these units during 2023-24 disclosed instances of non/ short realisation of excise duty and Licence fee and other irregularities involving ₹1.64 crore. In addition, a SSCA on 'Manufacture and Sale of Foreign Liquor in Kerala' was also undertaken during the year. The instances pointed out are illustrative only as these are based on the test-check of records. Non levy of fee, irregular transfer of licences and other irregularities involving ₹75.21 crore fall under the following categories as given in **Table 3.1**.

Table 3.1: Details of under assessment of tax and other irregularities

(₹ in crore)

Sl. No.	Categories	Amount
1	Subject Specific Compliance Audit on 'Manufacture and Sale of Foreign Liquor in Kerala'	73.57
2	Non levy of fee and fine on unauthorised reconstitution of Board of Directors of Companies	0.80
3	Irregular transfer of Foreign Liquor Licence	0.84
Total		75.21

Source: Records maintained by Accountant General.

During the course of the year, department accepted short levy and other deficiencies involving ₹0.14 crore in five paragraphs pointed out by Audit. Department realised an amount of ₹0.10 crore in four paragraphs during the year 2023-24.

3.4 Subject Specific Compliance Audit on Manufacture and Sale of Foreign Liquor in Kerala

3.4.1 Introduction

Manufacture and sale of liquor for human consumption comes under State List in the Seventh Schedule of the Constitution of India. The Abkari Act 1 of 1077⁸⁶ was originally enacted by the Raja of Cochin and adopted by Government of Kerala since 1967. The State Excise department executes the provisions of the Act and regulate the liquor sector by issuing licences for manufacture and storage, permits for transportation and sale of liquor. Revenue from liquor comprises Excise Duty and Fees collected by Excise Department, and Sales Tax and Turnover Tax collected by State Goods and Services Tax (GST) Department. Thus, the sale of foreign liquor in Kerala is monitored by both State Excise and State GST department.

Foreign Liquor is manufactured in Distilleries, Compounding, Blending & Bottling (CB&B) Units and Breweries of Kerala. Kerala State Beverages (Manufacturing and Marketing) Corporation Ltd. (KSBC) is the sole wholesale distributor of Indian Made Foreign Liquor (IMFL), Foreign made Foreign Liquor (FMFL), beer and wine in the State. KSBC procures liquor from manufacturers in the State, by import from other States and from abroad and transported to its licensed FL-9⁸⁷ Warehouses for wholesale to other Foreign Liquor (FL) licensees. KSBC is entrusted to pay Excise duty on behalf of the manufacturers, collect and remit Sales Tax and is liable to pay Turnover Tax for the sale of liquor.

The licence to vend foreign liquor in retail is granted:

- i) to KSBC and Kerala State Cooperative Consumer Federation (CONSUMERFED)
- ii) to hotels, restaurants and clubs that serve alcoholic drinks for consumption ‘on the premises’ to visitors.

In addition, the Canteen Stores Department (CSD) and Central Armed Police Force (CAPF) were granted licences [BW1(A)]⁸⁸ for a Bonded Warehouse for procuring foreign liquor under bond to cater the need of serving/ retired defence personnel and paramilitary forces.

As per Kerala General Sales Tax (KGST) Act, 1963, the dealers selling liquor are liable to pay Sales Tax, Turnover Tax and Cess on sale of liquor.

⁸⁶ 5th day of August 1902, corresponding to the 31st day of *Karkadagom* month in *Kollam Year* (Malayalam Calendar) 1077.

⁸⁷ An FL-9 licence authorises the possession and supply of foreign liquor in wholesale.

⁸⁸ BW1(A) licence is granted to CSD, Ministry of Defence and Central Police Canteen, Ministry of Home Affairs, GoI for the purpose of storage in Bonded Warehouses.

3.4.2 Organisational Structure

The State Excise department is headed by Additional Chief Secretary, Taxes (Excise) at the Government level. The Commissioner of Excise is the head of the department and is assisted by two Additional Excise Commissioners (Enforcement) & (Administration), and four Joint Excise Commissioners. The department is divided into three zones (South, Central and North) under the control of Joint Excise Commissioners (Zonal). Deputy Excise Commissioner is the head of the Excise Division Office at district level. Excise Division Office is divided into Excise Circle Offices and subdivided into Excise Range Offices.

An Excise Office is functioning in each of the manufacturing and warehousing unit in the State under the supervision of Excise Circle Inspector or Excise Inspector for monitoring the activities.

3.4.3 Audit Objectives

The subject specific compliance audit was conducted to ascertain whether:

- the provisions of the Acts/ Rules governing the manufacture/ import, transportation, storage and sale of Foreign Liquor and beer were complied with.
- the revenue realisable was demanded and collected in time.
- the internal control mechanism existing in the department is adequate and effective in enforcing the provisions of the Act/ Rules.

3.4.4 Audit Criteria

The criteria of audit are sourced from:

- i. The Abkari Act 1 of 1077
- ii. Kerala Foreign Liquor (Compounding Blending and Bottling) Rules, 1975
- iii. Kerala Distillery & Warehouse Rules, 1968
- iv. Brewery Rules, 1967
- v. Foreign Liquor Rules, 1953
- vi. The Kerala General Sales Tax Act, 1963
- vii. Kerala General Sales Tax Rules, 1963
- viii. Kerala Liquor Transit Rules, 1975
- ix. Annual Abkari Policies
- x. Excise Manual
- xi. Food Safety and Standards Act, 2006
- xii. Government Orders, Circulars, Notifications etc.

3.4.5 Audit Scope and Methodology

The Subject Specific Compliance Audit (SSCA) was conducted from 22 April 2024 to 01 April 2025, covering the period from 2021-22 to 2023-24. The methodology of Audit includes test check of records at Taxes (Excise) Department, Government of Kerala (GoK) and office of the Commissioner of State Excise. Four districts⁸⁹ were selected for detailed audit by Simple Random Sampling Without Replacement (SRSWOR) method. In the selected districts, Audit test checked all offices under the Deputy Excise Commissioner, all Excise units in the Distilleries/ CB&B Units/ Breweries/ Warehouses, and all the offices under the Deputy Commissioner, Taxpayer Services Divisions of State GST Department. In addition, offices of the Deputy Excise Commissioner at KSBC (Headquarter) Thiruvananthapuram, Canteen Stores Department (CSD) at Kochi, and Bonded Warehouse, Central Reserve Police Force (CRPF), Pallippuram were also covered in Audit.

An Entry Conference with the Joint Secretary to Government, Taxes (Excise) and the Commissioner of Excise was conducted on 03 September 2024 to discuss the Audit Plan and methodology. Exit Conference was held on 17 July 2025 with Additional Secretary, Taxes (Excise), Additional Excise Commissioner and Commissioner, State GST department, where the audit findings were discussed. The views expressed by the State Government during the Exit Conference and the written replies to the draft report have been suitably incorporated in the relevant paragraphs.

Audit Findings

Revenue from manufacture, import and sale of foreign liquor are being collected by State Excise department and State GST department. As per the provisions in the Abkari Act and various rules made thereunder, the State Excise department is entrusted with close monitoring and supervision of activities related to manufacture, transportation, storage, and sale of liquor in the State and to collect Excise Duty for the manufacture of liquor and fees for issuing licences and transit passes. However, major share of revenue from foreign liquor are Sales Tax and Turnover Tax collected under Kerala General Sales Tax (KGST) Act, 1963, by the State GST department. Revenue collected on sale of liquor by Excise department and State GST department for the period covered under audit is as furnished in **Table 3.2** below:

Table 3.2: Revenue collection on sale of liquor in Kerala

Year	Excise Revenue in crore	Sales tax on sale of foreign liquor in crore	Turnover tax in crore
2021-22	2,032.23	9,165.41	1,222.02
2022-23	2,875.95	13,060.32	1,704.58
2023-24	2,944.01	13,322.04	1,742.41

Source: Departmental records.

⁸⁹ Thrissur, Palakkad – Central Region, Pathanamthitta – Southern Region and Kasargod – Northern Region.

Audit examined various activities such as transportation of raw material, manufacture, import, transport, transit, storage of foreign liquor and collection of revenue from its sales. Important audit findings related to State Excise and State GST departments are discussed in the succeeding paragraphs.

3.4.6 Manufacture and Import of liquor

In Kerala, the production of Indian Made Foreign Liquor (IMFL) is carried out under the regulatory framework of the Kerala Distillery & Warehouse Rules, 1968, the Kerala Foreign Liquor (Compounding, Blending and Bottling) Rules, 1975, and the Brewery Rules, 1967. Currently, ten distilleries, seven CB&B units, and two breweries operate in the State under the supervision of the Excise department. These units do not distil Spirit or Extra Neutral Alcohol (ENA)⁹⁰ locally; instead, they source these essential raw materials from other States. The manufacturing process involves compounding the imported spirit with water, colouring, and flavouring agents to produce IMFL. Audit verified the records relating to purchase of ENA, compounding, blending and bottling operations for manufacture of IMFL and the observations noticed are given below:

3.4.6.1 Non demand of Excise Duty, Sales Tax and Turnover Tax on liquor manufactured from ENA found short/ unaccounted

Rule 47A(4)(b) of the Kerala Distillery and Warehouse Rules, 1968 requires that ENA imported is to be jointly measured by Excise officials and the licensee, with allowable transit wastage of 0.1 *per cent* for every 400 km (to be restricted to actual transit wastage or 0.5 *per cent*, whichever is less), and actual stock be recorded in Form D-31⁹¹. Under Rule 102, the officer-in-charge must conduct quarterly stocktaking of all spirits, record it in the registers, and report the findings to the Deputy Excise Commissioner (DEC), who would verify the statements during visits. As per Rule 34, wastage beyond 0.5 *per cent* per quarter attracts a fine of ₹20 per Proof Litre (PL). The Commissioner's circular (24 April 2018) reiterated the need for quarterly stock taking of ENA and its verification by the DEC. Further, Rule 9 of the *ibid* Rules mandates gauging of all vessels before use, and Rule 27(2)(b) of the Legal Metrology Rules, 2011 requires re-verification and stamping of storage tanks every 60 months.

Travancore Sugars and Chemicals Ltd. (TSCL) is a distillery in Thiruvalla, which manufactures IMFL by compounding ENA and bottling it for sale to the KSBC. To facilitate this, TSCL is permitted to store ENA in gauged tanks. Excise officials, along with the distillery personnel, are required to carry out joint physical verification of the spirit stock quarterly and certify the quantity as of the verification date. ENA is procured from distilleries outside Kerala

⁹⁰ ENA means spirit obtained by rectification/ re-distillation of rectified spirit having Indian Standard specification (IS: 6613-1972).

Strength of ENA is measured in 'degree proof'. If the alcohol percentage in Bulk Litre (volume of ENA in litre) is multiplied by a factor of 7/4 the resultant figure is the degree proof.

PL=BL * (degree proof/100).

⁹¹ Register of verification of consignments of liquor received at the Distillery/ Warehouse.

and transported to the distillery in tanker lorries, for which the Excise department issues permit. Upon arrival, Excise officials are required to verify the quality and quantity of the ENA before it is unloaded into the distillery's storage tanks.

Scrutiny of the records maintained at Excise unit office at the distillery; Audit noted the following:

- On 30 June 2021, the Excise officials intercepted two tanker lorries transporting 40,000 Bulk litre (BL) each of ENA to the distillery and detected a shortage of 20,386 BL of spirit. The loss was assessed and confirmed as 20,386 BL with 12,687 BL missing from one vehicle and 7,699 BL from the other. The drivers admitted that the spirit had been illicitly sold in Madhya Pradesh with the alleged involvement of certain employees of the distillery. The department released the remaining quantity of ENA to the distillery after levying a fine of ₹6,76,072, calculated at ₹20 per Proof Litres (PL), treating the shortage as transit wastage.
- Subsequent to the detection of spirit theft on 30 June 2021, the Excise department identified further discrepancies in the spirit stock held in the storage tanks of the distillery during stock verification. On 07 September 2021, the shortage was determined to be 4,60,659.1 BL, equivalent to 7,72,064.6516 PL. Accordingly, a demand notice was issued to the distillery on the same date for ₹1,54,41,293 calculated at ₹20 per PL. In response, the licensee stated that they had not availed the permissible storage wastage allowance of 0.5 *per cent* per quarter, as quarterly stock verifications had not been conducted. Based on this, the Department allowed a storage wastage of 3,12,608.626 BL for the period from 2013–14 to the first quarter of 2021–22. After deducting the allowable wastage, the revised shortage was computed as 1,48,050.384 BL (equivalent to 2,43,542.882 PL), and a revised demand for ₹48,70,858 was issued on 14 June 2022. The licensee subsequently remitted the amount in full.

Audit noticed that the department regularised the shortage of spirit detected on 07 September 2021 in the storage tanks of the distillery, by imposing a fine, after granting storage wastage allowance for a period of nine years. However, records revealed that a stock certificate issued after a joint physical verification conducted on 31 March 2021 by the Excise officials in charge of the distillery and company staff, indicated no discrepancy in the ENA stock. In view of the mandatory requirement for quarterly stock verification, the retrospective allowance of maximum permissible storage wastage over a nine-year period, without supporting records of actual physical verification, is irregular. Further, the theft of ENA detected on 30 June 2021 was also regularised by treating it as normal transit wastage.

Audit observed that the ENA transported into Kerala by the distillery is intended solely for the manufacture of liquor for human consumption, a process that generates substantial revenue for the State through Excise Duty, Sales Tax, and Turnover Tax. The distillery, having taken the ENA into stock,

was obligated to utilise it to produce IMFL. Therefore, any shortfall in production arising from missing ENA represents a loss to the State exchequer. Based on the unaccounted quantity of 4,60,659 BL of ENA, it was estimated that 10,26,435 BL (equivalent to 1,14,048 cases) of liquor could have been produced. The resultant loss of revenue to the State was calculated at **₹49.68 crore**, as detailed in **Appendix XXXII**.

In the case of the ENA theft, Audit noted that the consignment was intercepted before it entered the premises of the distillery and was therefore not recorded in the unit's stock register. ENA consignment was imported based on the permit issued to the distillery. Hence, the overall responsibility lies with the distillery. Based on the quantity of 20,386 BL of ENA diverted, it is estimated that 44,735 BL of liquor⁹² could have been produced. The resultant revenue loss to the State has been calculated at **₹2.20 crore** as detailed in **Appendix XXXIII**.

The failure to detect any shortage during earlier joint verifications, followed by the discovery of significant discrepancies in ENA stock during inspections by higher officials, conducted after a theft incident, highlights serious shortcomings in the monitoring and stock verification processes at the distillery's premises. While a Police FIR was filed for the theft, the department neither initiated any action to recover the revenue lost due to the shortage of ENA in the distillery's stock, nor did it pursue recovery from the individuals involved in the diversion of ENA. Thus, the total unrecovered loss to the State exchequer comes to **₹51.88 crore**.

On this being pointed out (June 2025), Government stated (July 2025) that strict directions are issued to conduct surprise and independent stock verification at the distillery. It was also furnished that the department will make a proposal to Government to implement real time tracking system of ENA while in transit and a technology based monitoring system to record the quantity of spirit used by distilleries and the quantity lost as wastage while bottling.

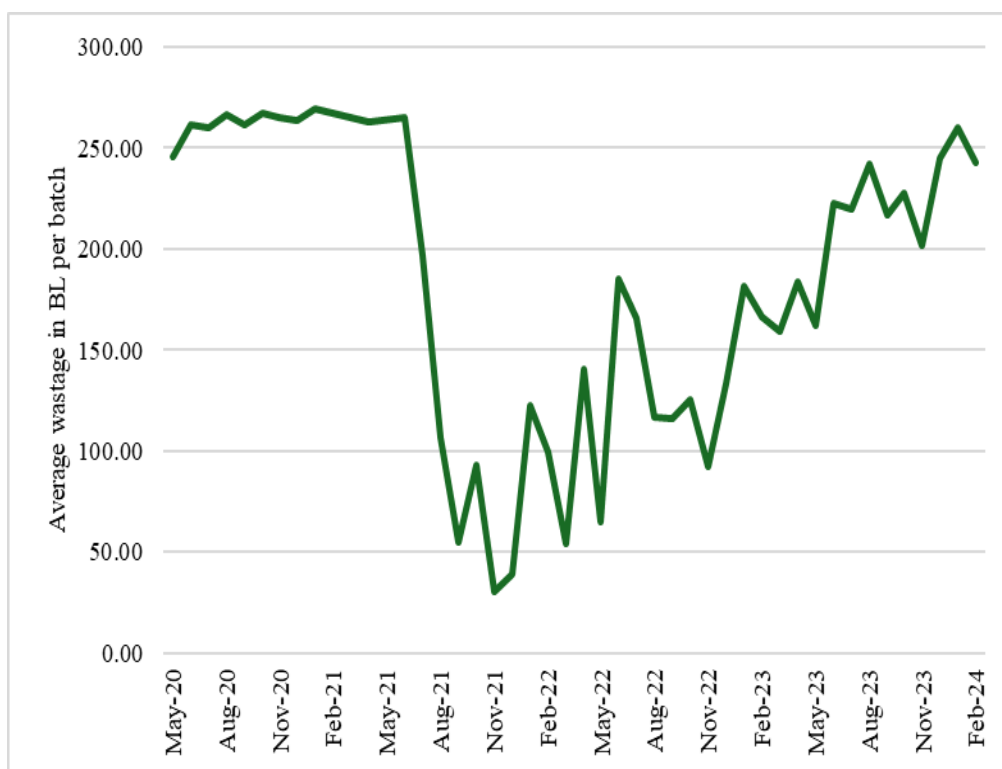
The reply did not specify any action taken or proposed, to recover the loss sustained to the State exchequer due to the unaccounted ENA at the distillery.

3.4.6.2 Inconsistency in claiming bottling wastage by a distillery in Thiruvalla

Rule 10(5) of the Kerala Foreign Liquor (CB&B) Rules, 1975 allows a maximum bottling wastage of 0.5 *per cent*. Audit examined the bottling wastage claimed by the TSCL distillery for the period ranging from May 2020 to March 2024. Though the claims of wastage were within the allowable limit of 0.5 *per cent*, Audit noticed a peculiar pattern in the bottling wastage allowance during the period, as shown in the **Chart 3.1**.

⁹² $44,735/9 = 4,971$ cases of 9 one litre bottles.

Chart 3.1: Trend of bottling wastage claimed over 4 years



Source: Information collected from Excise department.

During a Joint Physical Verification conducted by Audit (24 September 2024) in the presence of Excise officials, it was observed that the plant was equipped with semi-automated bottling lines.

Audit observed that, while the average bottling wastage remained within the permissible limit of 0.5 *per cent*, in absolute terms, it consistently exceeded 250 BL per batch prior to July 2021. However, subsequent to the detection of major spirit theft on 30 June 2021, the departmental monitoring increased and this average bottling wastage sharply declined to below 50 BL per batch. During July 2021 to January 2022, this remained within the range of 50-100 BL per batch. However, thereafter this wastage gradually rose again and returned to the pre-incident levels of around 250 BL by January 2024. The company has not provided any justification for this subsequent increase in wastage. By claiming wastage allowance to the maximum permissible level and possible correlation between lower wastage subject to enhanced monitoring, raises valid concerns over possible diversion of spirit/ liquor and resultant revenue loss to the State. However, in the absence of verifiable data of bottling wastage, Audit could not quantify the financial impact.

On this being pointed out (June 2025), Government stated (July 2025) that there will be strict supervision in distilleries so that the bottling wastage does not go beyond the allowable wastage. It further stated that necessary directions have already been issued to reduce bottling wastage. It also pointed out that consistency of average bottling wastage cannot be maintained due to the change of workers engaged in bottling process at regular intervals.

The Government reply is not acceptable, as consistency of low bottling wastage was achieved for six months following the detection of theft and also remained lower than 250 BL for approximately two years.

Recommendation 29

Government may direct the department to ensure that surprise and independent stock verifications are conducted at regular intervals, by separate departmental teams, to ensure unbiased assessments and early detection of discrepancies. Government, on receipt of proposal from the department, may expedite the process of implementation of real-time tracking system in order to ensure end-to-end traceability of ENA. Government may also implement a continuous and technology-enabled monitoring system such as automated meters and sensors to record spirit usage and wastage per batch for bottling operations.

3.4.6.3 Non-demand of Security deposit from Canteen Stores Department and Central Reserve Police Force

As per Rule 3(b) of the Foreign Liquor (Storage in Bond) Rules, 1961, applicants seeking to store foreign liquor in bond⁹³ are required to execute an agreement in Form A. This agreement binds the licensee to comply with the provisions of the Abkari Act, associated rules and orders, and the conditions of the licence, including the obligation to remit the prescribed duty.

Audit observed that the CSD, under the Ministry of Defence, was granted a BW-1A licence effective from 08 June 1994 for operating a bonded warehouse at Kochi to supply foreign liquor to 'Unit Run Canteens'. The licence was granted with a condition that the licensee should deposit security amount fixed by the Excise department. However, Excise department failed to fix the amount to be deposited by the licensee.

The Chairman, Liquor Canteen, Group Centre Campus, CRPF, Pallippuram, Thiruvananthapuram, was granted BW-1A licence on 14 January 2019, subject to the condition of depositing ₹0.21 crore as security. The bond executed on 27 February 2019 in Form A claimed that the amount had been deposited with the Commissioner of Excise. However, Audit scrutiny (March 2025) revealed that the security deposit of **₹0.21 crore** had not been made. The department may investigate whether the claim made in the bond regarding the deposit of the security amount was false or if there was any diversion of the deposited funds.

Government accepted the audit findings during exit meeting (17 July 2025) and replied that since both are central government institutions this provision was not strictly enforced. Subsequently it was stated (July 2025) that the matter is being verified in detail and reply will be furnished on completion of verification.

⁹³ Liquor stored where excise duty is not paid.

3.4.6.4 Short collection of fine due to allowance of excess transit wastage of ENA

Rule 47A(4)(b) of the Kerala Distillery & Warehouse Rules, 1968 states that all consignments of spirits, upon arrival, should be verified by volume and strength jointly by Excise Officials and the licensee. Further, the sub rule 4(d) of the Rule, *ibid*, prescribes an allowance of wastage of spirit at the rate of 0.1 *per cent* for a journey of every 400 km or part thereof subject to a maximum of 0.5 *per cent* or the actual wastage, whichever is less. The licensee is required to pay a fine of ₹20 per PL on the loss of spirit in excess of the limit prescribed.

Audit verified the records relating to the import of ENA by various IMFL manufacturing units functioning in the four selected districts and found that in 373 instances, the maximum permissible transit wastage was allowed without considering the actual distance involved. The uniform allowance of maximum wastage, contrary to the provisions of the rules, indicates non-adherence to regulatory norms governing transit losses. The resulted non-levy of fine is worked out to **₹0.07 crore** as detailed in **Appendix XXXIV**.

Government stated (July 2025) that necessary directions were given to the Excise officials to issue notices to the firms from which fine is due on account of excess transit wastage.

3.4.6.5 Short levy of Tie-up fee

As per Rule 10B of the Kerala Foreign Liquor (CB&B) Rules, 1975 and Rule 47(B) of Kerala Distillery and Warehouse Rules, 1968 - Part I, IMFL manufacturers located outside the State may operate in CB&B Units within the State upon approval of tie-up arrangements by the Commissioner of Excise and payment of the prescribed fee. The tie-up fee was initially fixed at ₹2.00 lakh per arrangement. As per the Abkari Policy 2022-23, the Government revised⁹⁴ the fee to ₹5.00 lakh with effect from 01 April 2022.

Audit noticed that the following two licensees had remitted Tie-up fee for the year 2022-23 at the pre-revised rate of ₹2.00 lakh which resulted in total short levy of **₹6.00 lakh** as shown in **Table 3.3** below:

Table 3.3: Short levy of Tie-up fee from licensees

(₹ in lakh)

Sl. No.	Name of licensee	Name of brand owner	Order No. & date	Amount remitted	Short remittance
1	'A' Distillery, Mannuthy	'X' Distilleries and Breweries Pvt Ltd., Goa	PTD/2022/0002 28.03.2022	2.00	3.00
2	-do-	'Y' Ltd., Bangalore	PTD/2022/0001 27.03.2022	2.00	3.00

⁹⁴ G.O.(Ms.) No.18/2022/TD dated 31 March 2022.

Government stated (July 2025) that necessary directions were issued to Distillery Officer of 'A' Distillery, Mannuthy to get the balance amount remitted for the tie-up arrangements.

3.4.6.6 Non-demand of Cost of Establishment

Rule 13 read with Rule 14 of Distillery and Warehouse Rules, 1968 stipulates that the distillery shall be under the supervision and guard of excise officials and the cost of establishment of excise officials employed in the distillery shall be payable by the licensee in advance. Rule 13 read with Rule 13(9A) of Foreign Liquor Rules, 1953, all transaction in the FL-9 license shall be under the supervision of the excise officials posted in the premises and the cost of establishment of excise staff posted in the FL-9 licence premises shall be borne by the licensee. The licensee shall also be liable to pay the arrears of differential cost of establishment, if the rates of pay and allowances are revised by the Government retrospectively.

Audit verified the remittance of cost of establishment by the distilleries in the four selected districts and found that:

- (i) GoK revised the pay scales of its employees with effect from 01 July 2019. However, the arrears of pay and allowances drawn by Excise officials posted at 'B' Distillery, Cheemeny, for the period from July 2019 onwards, were not demanded from the licensee. Audit calculated the arrears of cost of establishment attributable to the pay revision at **₹0.07 crore** as detailed in **Appendix XXXV**, which remains unrecovered from the licensee.

On this being pointed out (June 2025), Government stated (July 2025) that necessary direction have been issued to DEC, Kasargod to recover the cost of establishment due to the pay revision arrears from July 2019.

- (ii) A distillery and a liquor warehouse of KSBC are functioning within the same premises at Thiruvalla. However, only a single Excise establishment - comprising one Circle Inspector, one Preventive Officer and three Civil Excise Officers was deployed for the supervision of both licensees. Although the Commissioner of Excise approved a formula for apportioning the cost of establishment between the two entities, Audit noted that the distillery and warehouse are distinct establishments holding separate licences. Ideally, separate Excise supervisory units should have been established for each, with the corresponding cost of establishment recovered independently. Further, when the distillery's production increased gradually (since 2008), three additional Excise officials⁹⁵ were deployed to supervise its operations. However, it was observed that no cost of establishment was demanded for these officials during the period covered under audit, resulting in a revenue loss to the Government. The non-recovery

⁹⁵ One Preventive Officer, one Civil Excise Officer and one Women Civil Excise Officer.

of this cost from TSCL amounted to ₹0.77 crore, as shown in Appendix XXXVI.

Government stated (July 2025) that, following a financial setback in 1996, the distillery had requested a reduction in the number of supervisory staff posted at the distillery, which was subsequently approved by the Government. When KSBC established a warehouse on the company premises in 1999, it was directed to bear the cost of the Excise establishment at the distillery, except for one Civil Excise Officer, whose cost was borne by the distillery until May 2023. During the year 2021, for ensuring sufficient staff for the supervision of the distillery, three officers were posted⁹⁶ by the DEC, Pathanamthitta. However, out of the three, one Women Civil Excise Officer was posted to KSBC for supervising the destruction of discarded liquor. It was also stated that though the distillery is liable to pay the cost of establishment of two excise officials and KSBC is liable to pay the cost of establishment of one woman excise official, no formal demand has been raised yet. Government assured that the same will be issued and further developments will be intimated in due course.

The non-demand of the cost of establishment of staff posted to the distillery and KSBC indicates that their pay and allowances continue to be borne by the State.

The audit findings such as failure to collect security deposits, incorrect levy of tie-up fees at outdated rates, irregular allowance of maximum transit wastage regardless of distance, and non-recovery of cost of establishment for Excise officials deployed to supervise increased production activities, point to significant lapses in enforcement of financial and regulatory provisions by the department. Such lapses reflect weak internal controls, non-adherence to prescribed rules, and poor cost-recovery mechanisms.

Recommendation 30

Government may instruct the department to establish a monitoring mechanism to ensure security deposits are collected and periodically reviewed. Automate fee and cost calculations, wherever feasible, to avoid manual oversight and may initiate action to recover any short-levied fees and establishment costs for additional officials deployed. Instruct the department to discontinue the blanket allowance of maximum permissible transit wastage and make the wastage allowance distance based as per rules.

3.4.6.7 Quality of the Foreign Liquor manufactured

As per Rule 26 of the Foreign Liquor Rules, 1953 liquor sold or kept for sale shall be of good quality and unadulterated. Nothing shall be added to increase their intoxicating power. The definition of 'Food' in Food Safety and Standards (FSS) Act, 2006, states that alcoholic drink is also a food item. GoI framed FSS (Alcoholic Beverages) Regulation, 2018 to ensure safety and standards of Alcoholic Beverages.

⁹⁶ Vide order No.DP2-3/202(3) dated 10 August 2021.

The Food Safety and Standards (FSS) Act, 2006 defines alcoholic drinks as food and empowers⁹⁷ the Food Safety Officer to take samples of any food (including liquor) intended for sale. As per Rule 26 of the Foreign Liquor Rules, 1953, liquor sold or kept for sale must be of good quality, unadulterated, and free from any additives intended to increase its intoxicating power. Rule 71 of Kerala Distillery and Warehouse Rules, 1968 mandates that colouring/ flavouring materials and essences used in liquor manufacture must be approved by the Commissioner of Excise and kept under the custody of the officer in-charge of the distillery.

Test check of the records on manufacture of liquor revealed that liquor samples were not being taken for analysis by Food Safety Officer, raw materials other than spirit and their proportion were not approved by the Commissioner of Excise and was not under the custody of Excise department.

Non-testing of liquor sample by the Food Safety Officer is compromising the quality assurance framework. Use of raw materials like colouring and flavouring agents without prior approval from the Commissioner of Excise, and their exclusion from the Excise department's custody, indicates significant regulatory oversight.

On this being pointed out (June 2025), Government stated (July 2025) that liquor is dispatched for sale only after obtaining the chemical analysis certificate from the Government Laboratory. Since the Abkari Rules do not contain any provision authorising the Food Safety Department to collect liquor samples, the Excise Department is not in a position to enforce such regulations. However, necessary instructions have been issued to Excise officials to ensure compliance with FSSA standards in Distilleries, Bottling Units, and Breweries.

The reply is not tenable as the observation pertains to the non-approval of raw materials other than spirit by the Commissioner and those were not under the custody of the Excise department. Moreover, the authority for taking samples by Food Safety Department is governed by the provisions of the Food Safety and Standards Act, 2006.

⁹⁷ Section 38 of FSS Act, 2006.

3.4.7 Storage of Liquor

Establishment of warehouses and supervision of storage of foreign liquor are governed by Foreign Liquor Rules, 1953, Kerala Distillery & Warehouse Rules, 1968 and Foreign Liquor (Storage in Bond) Rules, 1961. Two types of FL licences were issued for the storage of liquor in the State. FL-9 licence to KSBC for the possession and supply of foreign liquor in wholesale and BW-1A licence to CSD and Central Armed Police Force (CAPF) to store foreign liquor in their Bonded Warehouses. Kerala has 26 Warehouses managed exclusively by KSBC and one Bonded Warehouse each by CSD and CRPF. Scrutiny of records of warehouse management revealed the following points:

3.4.7.1 Non-establishment of permanent Excise Establishment at Warehouses

Rule 13(9A) of Foreign Liquor Rules, 1953 stipulates that the Commissioner of Excise shall post such officer or officers of the Excise Department as he deems fit, to be in charge of FL-9 licence premises. All the transactions in the FL-9 licence premises shall be under the supervision of the Excise staff posted in such premises. Rule 18 of Kerala Distillery & Warehouse Rules, 1968 stipulates that every warehouse shall ordinarily be supervised by an officer specially deputed by the Commissioner. The cost of establishment of Excise staff posted in the FL-9 licence premises shall be borne by the licensee concerned.

Government sanctioned⁹⁸ 17 new FL-9 warehouses to KSBC, and on application from KSBC licences were issued to three, one each at Thiruvananthapuram, Ernakulam, and Kozhikode and KSBC operationalised the warehouses accordingly. The Commissioner of Excise submitted⁹⁹ a proposal to the Government to create dedicated excise supervision units at each of the newly established warehouses. The proposal included the creation of one post each of Circle Inspector (CI) and Preventive Officer (PO), and two posts of Civil Excise Officer (CEO) per Warehouse. Though the Commissioner of Excise clarified that the establishment of these posts would not impose any additional financial burden on the Government, the proposal was not approved. As warehouse supervision is mandatory, the Excise department assigned supervisory responsibilities of the three warehouses to existing personnel. Each warehouse was placed under the charge of the CI of the local Excise Circle Office, assisted by a PO from the local Excise Range Office and a CEO on special duty deputed from another KSBC warehouse in the locality.

Though the salary and allowances of one CEO is paid by KSBC, the same for the CI and PO is borne by State exchequer. Since Government had not sanctioned the posts for the supervision of new warehouses, Excise Department could not claim cost of establishment of Preventive Officers posted in the three Warehouses from KSBC. This resulted in an avoidable

⁹⁸ G.O.(Ms.) No.11/2022/TAXES dated 03 February 2022.

⁹⁹ Vide letter dated 21 October 2022.

expenditure of at least ₹2.35 lakh per month (calculated at the lower most scale of pay of Preventive Officer) as detailed in **Appendix XXXVII**.

On this being pointed out, Government accepted (July 2025) the observation and stated that proposal for creation of posts of one Circle Inspector, one Preventive Officer and two Civil Excise Officers in all the newly formed FL-9 Warehouses were submitted by the department. However, the reply is silent on the recovery of cost of establishment borne by the Government so far.

Recommendation 31

Government may re-evaluate and promptly sanction the proposed supervisory posts for FL-9 Warehouses to ensure structured staffing and enable proper cost recovery from licensees.

3.4.8 Sale of Foreign Liquor

Licences for the possession and sale of foreign liquor, as well as for possession and use, are issued under Rule 13 of the Foreign Liquor Rules, 1953. The authority to grant licences for operating foreign liquor outlets and to collect the corresponding licence fees rests with the Excise department. Meanwhile, the responsibility for monitoring and assessing the collection of Sales Tax and Turnover Tax on the sale of foreign liquor lies with the State GST department.

Audit conducted an examination of the process followed by the Excise department in granting licences to vend foreign liquor, including compliance with the conditions attached to the licences issued. Audit also reviewed the registration of dealers, scrutiny of returns, and the assessment, levy, and collection of Sales Tax and Turnover Tax under the Kerala General Sales Tax (KGST) Act, 1963 by the State GST department. Several shortcomings were observed during the course of this examination as illustrated below:

3.4.8.1 Short levy of Turnover Tax

As per Section 5(2) of the KGST Act, 1963, every dealer in foreign liquor should pay Turnover Tax (ToT) on the turnover of foreign liquor at all points of sale in the State. The ToT should be levied on bar attached hotels, at the rate of ten *per cent* and at the rate of five *per cent* on other dealers. Section 2(xxvii) of the Act, *ibid*, Turnover means the aggregate amount for which goods are either bought or sold, supplied or distributed by a dealer i.e. it includes Sales Tax due or paid also.

Master Canteen, Liquor Canteen and Liquor Canteen, GC, CRPF Pallippuram are assesseees on the rolls of the Deputy Commissioner, Tax Payer Services (TPS) Division, Kazhakoottam. The assessment files of these assesseees were transferred to TPS Division, Kazhakoottam after completing assessments as detailed in **Table 3.4** below.

Table 3.4: Details of KGST assessment

Name of the Assessee	Master Canteen, Liquor Canteen, CRPF, Pallipuram	Liquor Canteen, GC, CRPF Pallipuram
TIN	32010887979	32010674826
Year of Assessment	2020-21	2019-20
Date of Assessment Order	13/10/2022	28/07/2021
Assessing Authority	Assistant Commissioner, III Circle, Thiruvananthapuram	Assistant Commissioner, I Circle, Thiruvananthapuram
Turnover fixed for Sales Tax (₹) (A)	7,67,13,081.75	7,52,41,431.00
Exemption allowed (₹)	0	3,34,36,907.00
Taxable Turnover fixed (₹)	7,67,13,081.75	4,18,04,524.00
Sales Tax due (₹) (B)	18,94,81,311.92	8,86,25,591.00
Turnover fixed for ToT (₹)	7,67,13,082.00	7,34,55,649.00
ToT due determined (₹) (C)	38,35,654.08	57,82,119.00
Total Tax due determined (₹)	19,25,49,835.00	9,44,07,710.00

Source: Departmental Records.

During the finalisation of KGST assessments, the Assessing Authority failed to include the sales tax component while computing the turnover for determining the ToT liability. This resulted in a short levy of ToT amounting to **₹1.65 crore** as shown in **Table 3.5** below:

Table 3.5: Short levy of turnover tax and interest due

TIN	Labels	32010887979	32010674826
Turnover to be reckoned for ToT (₹) (A) + (B) of Table 3.4	D = A+B	26,61,94,394	16,38,67,022
ToT due (₹)	E = 5% of D	1,33,09,720	81,93,351
ToT levied (₹)	F	38,35,654	57,76,962
Short levy of ToT (₹)	G = E - F	94,74,066	24,16,389
Interest due at 12% per annum (₹)		34,10,664 (04/21 to 03/24)	11,59,867 (04/20 to 03/24)
Total (₹)		1,28,84,730	35,76,256

Source: Calculations based on departmental records.

Audit observed that while finalising the KGST assessments, the Assessing Authority failed to include the sales tax component in the turnover used for calculating ToT liability. This oversight led to short levy of ToT, indicating a lapse in adherence to assessment procedures and resulting in loss of revenue to the Government.

On this being pointed out (May 2025), Government assured in the Exit Conference (July 2025) that the case will be reopened. Further SGST Department stated (August 2025) that action has been initiated u/s 35 (notice dated 01 July 2025) of the KGST Act for cancelling the impugned order.

3.4.8.2 Non-payment of Turnover tax by a Brewery at Kanjikode, Palakkad

As per Section 17(3) of KGST Act, 1963, if no return or incorrect or incomplete return is submitted by the dealer, the assessing authority shall assess the dealer to the best of its judgment. As per explanation - 1 to Section 5(2)(b) of the Kerala General Sales Tax Act, 1963, any distillery, brewery, winery established under Section 14 of the Abkari Act in the State are liable to pay Turnover Tax (ToT) at the rate of five *per cent* on the turnover on sale of foreign liquor including any Excise Duty payable on it.

Government vide Notification¹⁰⁰, exempted with effect from 01 December 2022, the Turnover Tax payable under Section 5(2)(i)(b) of KGST Act, by any distilleries in the State which sells liquor manufactured by it within the State to KSBC.

A brewery at Kanjikode, Palakkad registered under Deputy Commissioner, TPS Division, Palakkad, filed Annual Return for the year 2023-24. As per the audited accounts furnished in Form 50-B, the assessee claimed exemption from payment of ToT on the sale of beer, citing the Government Notification issued in December 2022. However, the said notification is applicable only to liquor manufactured by distilleries and does not extend to beer produced by breweries. Hence, the exemption claimed by the assessee was irregular, and the failure of the Assessing Authority to initiate action for recovery of ToT resulted in non-levy of tax of **₹13.81 crore** as detailed in **Appendix XXXVIII**.

Audit observed that the assessee irregularly claimed exemption from ToT on the sale of beer based on a Government Notification and the Assessing Authority failed to scrutinise this claim, resulting in loss of revenue to the Government.

On this being pointed out (May 2025), Government in the Exit Conference (July 2025) stated that the assessment of the dealer for the year 2023-24 has been completed creating an additional demand of ₹16.50 crore.

3.4.8.3 Short levy/ collection of Sales Tax due to application of incorrect rate of tax

As per Section 5(1) of KGST Act, 1963, every dealer, whose total turnover for a year is not less than two lakhs rupees, shall pay tax on his taxable turnover at the rate mentioned against such goods in the Schedule, in respect of Foreign liquor, at the point of sale by the Kerala State Beverages (Manufacturing and Marketing) Corporation Limited (KSBC) and at the point of first sale in the

¹⁰⁰ S.R.O. No.1155/2022 dated 01 December 2022 (issued in G.O.(P) No.152/2022/Taxes).

State by a dealer liable to tax under this section except where the sale is to KSBC. The rate of Sales Tax on Foreign Liquor was increased from 135 *per cent* to 210 *per cent* with effect from 01 April 2018 vide Finance Act, 2018. Government further revised the rate as shown in the **Appendix XXXIX**, through Kerala General Sales Tax (Amendment) Act, 2022 with effect from 16 December 2022.

Scrutiny of assessment records revealed that in one case, the assessee failed to revise the applicable tax rate for the financial year, and in another case, the revised rate was not applied from the effective date of revision. In both instances, the assessing officers accepted the returns filed by the assessee without verifying the correctness of the applicable rates. This resulted in short levy of tax of **₹3.73 crore** as detailed below:

- (a) Audit scrutiny of the assessment records for the year 2018-19 of the assessee Liquor Canteen, GC, CRPF Pallippuram revealed that a taxable turnover of ₹3.09 crore was declared, against which tax including Additional Sales Tax (AST) amounting to ₹4.60 crore and surcharge of ₹0.46 crore were remitted. However, the tax was computed by erroneously applying the rate of 135 *per cent*, instead of 210 *per cent*. This resulted in short payment of tax. However, Foreign Liquor sales are exempt from AST as per Section 5D of Kerala General Sales Tax Act, 1963. The Kerala Finance Act, 2018 withdrew surcharge (10 *per cent*) on Sales Tax with effect from 01 April 2018. Short payment of tax has been quantified at **₹3.19 crore** as shown in **Appendix XL**.

On this being pointed out (May 2025), Government in the Exit Conference (July 2025) assured that the issue will be examined in detail during assessment. SGST Department further stated (August 2025) that action has been initiated under Section 35 (notice dated 01 July 2025) of the KGST Act for cancelling the impugned order.

- (b) Audit analysis of the Liquor Supply Chain Management database of the KSBC revealed that the revised tax rates effective from 16 December 2022 were not promptly incorporated into the system as shown in **Appendix XLI**. The assessee remitted tax based on the system-generated calculations, resulting in short collection of tax including interest, amounting to **₹0.54 crore** as detailed in **Appendix XLII**.

On this being pointed out (May 2025), Government in the Exit Conference (July 2025) assured that the issue will be examined in detail during assessment. Department further stated (August 2025) that the books of accounts of the KSBC is under verification. It was further stated that considering the voluminous nature of the records, a detailed reply will be furnished at a later stage.

This indicates a lapse in the assessment process and insufficient scrutiny of statutory compliance, resulting in revenue loss to the Government.

3.4.8.4 Short levy of tax due to irregular assessments

Audit noticed an instance of irregular assessment by assessing authorities which resulted in short levy of ToT amounting to **₹0.02 crore** as detailed below:

The assessment of an assessee on the rolls of TPS Division Irinjalakuda (TIN: 32XXXXXXXXXX) for the year 2020-21 was completed on 20 July 2022. Audit scrutiny revealed that the assessee had remitted ₹2.40 lakh towards ToT for the month of January 2021. However, the Assessing Authority while finalising the assessment for the year 2020-21, erroneously allowed credit for ₹4.47 lakh, resulting in an excess credit of ₹2.07 lakh and extending an undue benefit to the assessee.

Government stated (September 2025) that based on the audit objection, assessment was completed vide order dated 30 April 2025 creating a tax due of ₹2.07 lakh.

Recommendation 32

Government may develop and circulate detailed standard operating procedures (SOPs) to Assessing Authorities of State GST, on common areas of error including exemption eligibility to ensure uniformity in assessments. Government may also institute accountability mechanisms for assessment errors and conduct regular internal audits to evaluate the quality of assessments.

3.4.8.5 Short levy of Excise Duty on Beer and consequent short levy of Sales Tax

As per Rule 1 of Foreign Liquor (Storage in Bond) Rules, 1961, liquor stored in Bonded Warehouse should be removed only upon payment of the applicable Excise Duty. In addition to Excise Duty, an Import Fee¹⁰¹ is also chargeable at the time of removal of liquor. For beer, the Excise Duty is fixed at ₹5 per bulk litre (BL) and the Import Fee at ₹2 per BL. As per the Kerala General Sales Tax Act, 1963, Sales Tax and ToT are levied on the total turnover, which includes the Excise Duty component. Beer sold by the CSD is subject to Sales Tax at the rate of 82 *per cent* with effect from 19 May 2020, and a Turnover Tax at the rate of one *per cent*.

Audit observed that CSD, as a bonded warehouse licensee, was liable to remit Excise Duty and Import Fee at the rates prescribed at the time of removal of beer for sale. The Excise Unit functioning within CSD levied Excise Duty at the rate of ₹3 per BL instead of ₹5 per BL. Scrutiny of records for the period 2021-22 to 2023-24 revealed that the total Excise Duty levied, at the incorrect rate, was ₹20.28 lakh, resulting in a short levy of ₹13.52¹⁰² lakh. This short levy of Excise Duty also led to consequential short levy of Sales Tax and ToT

¹⁰¹ Vide Notification S.R.O. No.268/95.

¹⁰² ₹20,28,527 x (5-3)/3.

amounting to ₹11.09 lakh and ₹0.25¹⁰³ lakh respectively. Total short levy worked out to ₹0.25 crore.

The application of incorrect rate resulted in a short levy of Excise Duty, indicating a lapse in compliance by the Excise Officials, with the applicable tax regulations and leading to a loss of revenue to the Government.

On this being pointed out (June 2025), Government stated (July 2025) that detailed report would be submitted soon.

Recommendation 33

Government may direct the Excise Department to strengthen its compliance and monitoring mechanisms to prevent revenue leakages arising from incorrect duty application and inadequate verification.

3.4.9 Transit Permits issued for Transportation of Liquor

As per Rule 3 of Kerala Liquor Transit Rules, 1975, no liquor should be moved from one place in a State to another place in that State or to any other State through the territory of Kerala except under a permit issued by Excise department. Rule 3B stipulates that if liquor has to be moved through the State, the officer-in-charge of the entry check post after verifying the permit shall depute two Excise guards to escort the liquor from the entry check post to the exit check post. The officer-in-charge of the exit check post, after verification of the consignment allows the consignment to exit the State territory after reporting to the permit issuing authority. As per Rule 8, liquor moved under this permit should not be sold inside the State of Kerala.

The Commissioner of Excise has issued instructions¹⁰⁴ (December 2020), to facilitate safe transit of liquor under permit. The Circular directed to provide escort to the consignment of liquor under Transit permits and directed the officer in charge of the exit check post to ensure that sufficient Excise officials accompanied the consignment. Audit test checked the movement of liquor under transit permits issued by the Joint Excise Commissioners (JEC) and found the following:

3.4.9.1 Transit Permits issued for Mahe

Audit observed that Mahe, a part of the Union Territory of Puducherry located between Kannur and Kozhikode districts of Kerala, imports IMFL through Kerala under Transit permits issued by the JEC, North Zone. To monitor such movement, two Excise check posts (New Mahe and Azhiyur) are functioning at both ends of the National Highway passing through Mahe. During the period 2021-22 to 2023-24, 4,470 Transit permits were issued for the import of liquor into Mahe. Audit cross-verified¹⁰⁵ 359 of these permits with the records maintained at the two Excise check posts and found that 22

¹⁰³ 1 per cent of (13.52 lakh+11.09 lakh).

¹⁰⁴ Circular No. EXC44/2020 Excise dated 22 December 2020.

¹⁰⁵ Selected the permits issued during one month in each year (December 2021 and 2023, July 2022).

permits, involving 1,10,720 BL of IMFL, had no corresponding records of exit as detailed in **Appendix XLIII**, indicating possible diversion to Kerala market for illicit sale. The estimated revenue loss due to the possible diversion of 12,302 cases¹⁰⁶ of IMFL amounts to ₹5.10 crore¹⁰⁷.

It was also observed that the officers in charge of the exit check posts did not report the details of outbound consignments to the permit-issuing authority, thereby weakening the control mechanism and enabling misuse of the transit permits.

On this being pointed out (24 October 2024), the JEC Kozhikode replied that the officials in check posts had started reporting from 26 October 2024.

Government stated (July 2025) that necessary directions were issued to provide escort facilities for the consignments passing through the State with transit permits. It was also stated that, so far, no incidents of diversion of liquor for illicit sale had been reported.

The Government reply is not tenable as even though no cases of illegal sale have been reported yet, possibility of illegal sale could not be ruled out.

3.4.9.2 Transit permits issued by the JEC, Central Zone, Kochi

During the period 2021-22 to 2023-24, a total of 324 Transit Permits were issued by the JEC, Kochi for transporting liquor from/ to Kerala through the Excise Check Post at Walayar. Scrutiny of records maintained at the Walayar Check Post revealed that 78 Transit permits (**Appendix XLIV**), covering the movement of 43,651 cases of FMFL, did not register an exit through the said check post. In the absence of data on the quantity of FMFL transported, Audit could not quantify the potential revenue loss.

Though there were clear instructions, the permit-issuing authority failed to ensure that the consignments reached their intended destinations by deploying officials to escort the goods. Since the consignments covered under these permits involved non-duty paid liquor, the possibility of misuse or diversion of liquor under the guise of transit cannot be ruled out.

Government stated (July 2025) that necessary directions had been issued for the proper maintenance of consignment registers for liquor passing through check posts. It was also stated that QR code embedded labels were introduced for liquor transported within the State, with effect from 01 April 2025.

Recommendation 34

Government may introduce a GPS-enabled transit permit system with real-time tracking and automated for route deviations or delays alerts to Excise Enforcement Wing, to monitor whether consignments reach their intended destinations.

¹⁰⁶ No. of cases of one litre bottle: $110720.4/9 = 12,302$ cases.

¹⁰⁷ Excise Duty @ 729.67 x 12,302 cases = ₹0.90 crore and Sales Tax @ 3,416.71 x 12,302 cases = ₹4.20 crore.

3.4.10 Inadequate regulatory framework for implementing Statutory Provisions

Though there is provision to deny licence to abkari defaulters and offenders, the absence of clear regulation restricts Excise officials from taking appropriate actions. Instances noticed are detailed below:

3.4.10.1 Absence of regulatory support allows tax defaulters to retain Abkari Licences

Abkari Act defines Abkari Revenue as “*revenue derived or derivable from any duty, fee, tax, fine or confiscation, imposed or ordered under the provisions of this Act, or of any other law for the time being in force relating to liquor or intoxicating drugs*”. Section 26 of the Act stipulates that the Commissioner may cancel or suspend any licence or permit granted if any fee, duty, tax or rental payable by the holder thereof be not duly paid. Licences for serving IMFL and beer are granted as per Rule 13 of the Foreign Liquor Rules, 1953.

Since Abkari revenue includes tax related to the sale of liquor, the tax levied under the KGST Act, 1963 on such sales also constitutes Abkari revenue. Therefore, FL licensees with outstanding Sales Tax arrears are deemed Abkari defaulters, and their licences are liable to be cancelled or suspended.

The State GST Department collects Sales Tax and ToT from liquor dealers operating within the State. An examination of the Demand Collection Balance (DCB) statements maintained in the GST offices of the selected districts revealed that revenue arrears were pending collection from these dealers as shown in **Table 3.6** below:

Table 3.6: GST Arrears as per DCB statement

Sl.No.	District	GST Arrears (₹ in crore)
1	Palakkad	299.81
2	Thrissur	40.35
3	Pathanamthitta	28.95
4	Kasargod	5.80

Test check of assessment records revealed that 15 dealers in four districts continuously defaulted in filing of tax returns and payment of tax as detailed in **Appendix XLV**. Though it was mandated under Section 13 of KGST Act, 1963, that every dealer whose annual turnover is not less than rupees one lakh, took registration, Audit noticed that the licensees under Abkari Act functioned without obtaining or after cancellation of KGST registration as detailed in **Appendix XLVI**.

The FL Rules stipulate that, for the annual renewal of licences, the applicant must produce a certificate from the Abkari Workers’ Welfare Fund Inspector confirming the remittance of arrears of contributions. However, though the

Abkari Act defines the tax levied on liquor sales as part of Abkari revenue, there is no corresponding requirement in the FL Rules to produce a clearance certificate from the State GST department.

In the absence of such a regulation, the Excise department renewed the FL licences annually without ensuring the remittance of taxes under KGST Act.

Government stated (July 2025) that as per the judgement in WA No. 2467/2015 sales tax could not be considered as Abkari revenue and hence, defaulters of sales tax are not Abkari defaulters. Since there is no provision in Foreign Liquor Rules to demand sales tax arrears from the licensee, the FL licence were renewed annually even though the licensee is a defaulter of Sales Tax.

The reply is not acceptable. As per Section 3(1) of the Abkari Act 1 of 1077, revenue derived from tax ordered under the provisions of any law being in force, relating to liquor is Abkari revenue. Hence, a default on payment of tax levied on the sale of liquor is an Abkari default. Moreover, the judgement referred in Government reply was not produced to Audit.

3.4.10.2 Absence of rule provisions for reconstitution of Board of Directors of Companies manufacturing Foreign Liquor

As per Section 67(2) of Abkari Act, the Excise Commissioner (EC) may impose a fine of ₹3,00,000 (Rupees three lakh only) each on any person or persons holding a licence or permit under this Act for violation by way of reconstitution, alteration or modification without the permission of the Commissioner of any deed on the strength of which any licence is granted. Section 67(3) provides that the EC may regularise such an irregular constitution on payment of fine imposed under sub-section 2 and after accepting such fee as may be prescribed by rules.

The Foreign Liquor Rules, 1953, vide Rule 19(iii), fixed the requisite fee for reconstitution as rupee one lakh. However, no such provision included in Kerala Distillery and Warehouse Rules, 1968, Kerala Foreign Liquor (CB&B) Rules, 1975, and the Brewery Rules, 1967.

In Kerala there are 10 licences granted under the Kerala Distillery and Warehouse Rules, 1968, seven under the Kerala Foreign Liquor (Compounding, Blending and Bottling) Rules, 1975 and two licences under the Brewery Rules, 1967.

Audit noticed that the Excise department had imposed fine and fee on four Distillery/ breweries¹⁰⁸ functioning in the selected Districts, for reconstituting the Director Board/ partnership without obtaining prior permission of the Excise Commissioner.

Against the order, the licencees filed writ petition and the Hon'ble High Court of Kerala vide judgement (07 December 2024) set aside the order of the EC.

¹⁰⁸ A distillery at Pambady (₹48 lakh), a distillery at Meenakshipuram (₹12 lakh), a distillery at Govindapuram (₹6 lakh and ₹3 lakh) and a brewery at Kanjikode (₹36 lakh).

The Hon'ble High Court observed that the Excise department imposed the penalty for reconstitution of Board of Directors/ partnership of the Companies/ partnership firms manufacturing liquor without any rule provision in Kerala Distillery and Warehouse Rules, 1968/ Kerala Foreign Liquor (Compounding, Blending and Bottling) Rules, 1975/ the Brewery Rules, 1967.

Thus, the absence of a rule provision led to setting aside the demand notices amounting to ₹1.05 crore in four districts for reconstitution without prior sanction.

Government stated (July 2025) that in the Abkari Policy for the year 2025-26, it was decided to introduce fee for reconstitution made in the Director Board/ Partnership of licences issued under Kerala Distillery and Warehouse Rules, 1968, Kerala Foreign Liquor (Compounding, Blending and Bottling) Rules and Brewery Rules.

Recommendation 35

Government may amend the Foreign Liquor Rules to mandate the production of a clearance certificate from the State GST department as a prerequisite for annual licence renewal which will ensure that all tax liabilities under the KGST Act are settled before renewal. Government may also initiate action to insert explicit legal provisions requiring prior approval from the Excise Commissioner for any reconstitution of the Board of Directors or partnership in licensed entities.

3.4.11 Effectiveness of Internal Control

Internal control mechanism is intended to provide reasonable assurance of proper enforcement of Act, Rules and departmental instructions. It is the responsibility of the department to ensure a proper internal control mechanism exists in the department in monitoring the collection of Excise Duties, fees, penalties and in prevention and detection of frauds, evasion of duties, fees etc. Audit noticed many deficiencies, non-compliance of important rule provisions etc., which shows weaknesses in the internal control mechanism.

3.4.11.1 Non-imposition of fine for unauthorised reconstitution and non-collection of fees for regularisation resulted in non-realisation of ₹16.00 lakh.

Rule 13(C) of Foreign Liquor Rules, 1953 stipulates that no partnership will be granted with a licence, if any of the partners are abkari defaulters or offenders under Abkari Act, 1902 or Narcotic Drugs and Psychotropic Substances Act, 1985. Rule 19(i) read with Rule 19(ii) of the Rules *ibid*, states that reconstitution of partnership by addition or deletion of members or reconstitution of Directors of a Company resulting in change of ownership shall be a deemed transfer of licence and hence requires previous sanction of the Excise Commissioner (EC). As per Section 67(2) of Akbari Act, 1902, the EC may impose a fine of rupees three lakh each on any person or persons

holding a licence for violation by way of reconstitution, without the permission of the EC. Section 67(3) provides that the EC may regularise such an irregular constitution on payment of fine and requisite fee from the licensee and under Rule 19(iii) of Foreign Liquor Rules, 1953, the requisite fee was fixed as rupee one lakh. Rule 14 of the Rule *ibid* stipulates that the licences referred to in Rule 13 expires at the end of the financial year.

In the event of reconstitution of a partnership or the Board of Directors of a company, the licensee must submit an application for prior permission and regularisation of the reconstitution through the ‘*Service Plus*’ portal of the Excise Department. In cases where prior permission is not obtained, the licensee must apply for regularisation of the reconstitution through the same portal. Every FL licence must be renewed annually by submitting an online application through the portal before the beginning of each financial year. The renewal application form includes a mandatory field to provide details of the current Directors or partners of the company or firm.

In a separate instance, Audit verified (January 2024) the records relating to FL-3(Bar)/ FL-11(Beer Parlour) licences, maintained in the office of the EC and found that EC had regularised the reconstitution of Directors/ partnership of 60 FL licence during the audit period 2022-23. Audit examined the reconstitution details of Boards of Directors of companies and partnership firms by cross-verifying data from the Ministry of Corporate Affairs (MCA) and the Registrar of Firms. It was found that apart from the sixty reconstitutions approved by the EC, three companies and one partnership firm, operating hotels with FL-3/ FL-11 licences, had reconstituted their Boards or partnerships. These changes amounted to a change in ownership as defined under Rule 19(i) of the FL Rules, 1953.

Audit analysed the application records available in the ‘*Service Plus*’ portal and found that none of the four licensees had submitted applications either for prior permission or for regularisation of the reconstitution. Scrutiny of the licence renewal applications for the financial year 2022-23 and 2023-24 revealed that three licensees did not disclose the changes in the names of their Board of Directors. In the case of the fourth licensee, the licence was issued and subsequently cancelled during the period 2022-23.

Audit found that the four licensees failed to disclose accurate information, deliberately suppressing details of reconstitution in their submissions to the Department. Audit identified these reconstitutions by cross-verifying publicly available data from the Ministry of Corporate Affairs and from the Registrar of Firms, a department under Government of Kerala.

Since the four reconstitutions were carried out without obtaining permission from the Excise Commissioner and remained unregularised (March 2025), the impact on revenue are non-collection of fees of **₹4.00 lakh** for regularisation of reconstitution and non-imposition of fine of **₹12.00 lakh** for unauthorised reconstitution as shown in **Appendix XLVII**. Audit observed that the Excise department currently lacks an internal mechanism to collect and cross-verify such information from external sources. Besides leading to revenue leakage, absence of such cross-verification mechanism on the

information furnished by the licensees will undermine the effective enforcement of Rule 13(C) of the Foreign Liquor Rules, 1953, which seeks to prevent abkari defaulters and offenders from becoming directors in companies holding FL licences.

On this being pointed out (May 2024), Government stated (July 2024 and July 2025) that, in three cases department had accepted the observation, among which notices had already been issued in two cases to regularise the unauthorised reconstitution while in the third case, direction was given to the Deputy EC to issue notice. In the remaining case, the licensee submitted an application for regularisation; however, as the licensee has been convicted by the CBI court, the application is pending.

3.4.11.2 Delay in calibrating the vessels

Rule 9 of the Kerala Distillery and Warehouse Rules, 1968 states that all vessels in the distillery should be gauged/ calibrated to the satisfaction of the Excise Commissioner. As per Rule 34 of the said Act, an account of the spirit stock should be taken at an interval not exceeding three months, and the distillers shall pay to the Government a fine of rupees twenty per PL on spirit which could not be accounted for in excess of an allowance of half *per cent* for wastage. Similar rule provisions are included in the Kerala Foreign Liquor (CB&B) Rules, 1975 as well.

The receipt, storage, and issue of spirit should be carried out under the strict supervision of the Excise department. Quarterly verification of spirit stock must be conducted, and fine should be imposed in cases of excess wastage. Timely calibration of storage tanks is essential to ensure the accuracy of spirit stock and the quantity of liquor blended therein.

A test check of records of 11 Distillery/ CB&B units functioning in the four districts revealed that, in six of these units, the calibration of vessels used for spirit storage and blending operations had expired as early as 2018. The details are given in **Appendix XLVIII**.

Audit observed that, though the Department is empowered to levy fines for excess storage wastage resulting from non-calibration, such shortages in spirit adversely impact IMFL production, thereby leading to potential loss of revenue in the form of Excise Duty and Sales Tax.

Government stated (July 2025) that necessary directions have been issued to calibrate the spirit tanks and to levy fines for excess wastage or shortage in spirit resulting from non-calibration.

3.4.11.3 Non receipt of Excise Verification Certificates

As per Rule 11 of Foreign Liquor Rules, 1953, the transport of liquor, in excess of the notified quantity, shall be covered by a transport permit issued by the Excise Inspector in charge of the Range of origin. A copy of the same shall be forwarded to the Excise Inspector in charge of the Range to which the consignment is destined. The Excise Inspector at the destination shall verify

the consignment of IMFL on arrival and see that the quantity is duly credited in the accounts of the licensee who transported the consignment.

The transport permit issued are known as Excise Verification Certificate (EVC) and EVC is a mechanism to prevent the misuse of the IMFL/ beer dispatched from the manufacturing units to the warehouses of KSBC and from there to FL-1/ FL-3 licensees.

Scrutiny of Dispatch/ Issue register of IMFL kept in the various distilleries/ CB&B Units/ FL-9 Warehouses in four districts revealed that during the period from 2021-22 to 2023-24, a total number of 10,139 EVCs were not received from the FL-9 warehouses/ FL-3 licensees as detailed in **Appendix XLIX**. The non-receipt of EVCs show lapses in ensuring the receipt of consignment at the exact destination.

Government stated (July 2025) that necessary directions were given to Excise Officials to trace out and issue EVCs on time.

Recommendation 36

Government may direct the Excise department to ensure periodic calibration of spirit storage tanks and blending vessels in all warehouses. Government may also explore the viability to implement digital inventory and transit management systems that track spirit movement, storage levels, calibration records, and EVC status in real time to enhance oversight and reduce manual lapses. The Department may also periodically cross verify the data available in the Service Plus portal with the website of the Ministry of Corporate Affairs or other institutions to identify the unauthorised reconstitutions and action has to be taken to fix responsibility in cases of granting undue benefit to the licensees.

3.4.11.4 Other Internal Control lapses

Other issues noticed relating to Internal Control are detailed below:

- (i) As per the Plastic Waste Management Rules, 2016, the primary responsibility for collection of used multi-layered plastic sachet or pouches or packaging is of Producers, Importers and Brand Owners who introduce the products in the market. They need to establish a system for collecting back the plastic waste generated due to their products. In Abkari Policy 2022-23, Government decided to stop the use of plastic bottles for liquor packaging from the financial year 2023-24.

Audit noticed that manufacturers of IMFL continued (January 2025) to use plastic (PET) bottles for packaging. During the audit period, a total of 654.89 million PET bottles were used by various distilleries for supplying liquor to KSBC in the four selected districts, as detailed in **Appendix L**.

Government stated (July 2025) that manufacturers of liquor in the State purchased the plastic bottles from the producers of plastic goods having EPR (Extended Producer Responsibility) registration. The Excise Department had taken possible efforts to reduce the usage of plastic bottles in liquor industry and to promote glass bottles.

- (ii) Rule 3 of Distillery and Warehouse Rules - Part II prescribes that the Deputy Commissioner of Excise will be responsible for the proper working of distilleries and warehouses. He should inspect them not less than once every half year and submit the notes of his inspection to the Commissioner. Audit examined the records pertaining to inspections conducted in distilleries/ warehouses in four districts by Deputy Commissioners during the period from 2021-22 to 2023-24 and found short fall in inspections as shown in the **Appendix LI**. During 2021-24 as against 72 inspections required to be conducted, only 24 inspections were conducted.

Government stated (July 2025) that necessary directions were issued to Deputy Excise Commissioners to conduct regular inspections in Distilleries & Warehouses, Compounding, Blending and Bottling Units and Breweries.

- (iii) Government created (21 October 1998) one post of Deputy Excise Commissioner (Law) and an office establishment with one post each of Excise Inspector, Preventive Officer and Civil Excise Officer functioning at Ernakulam for monitoring different court cases and to liaison with the Advocate General. Audit observed that though an office establishment is functioning for monitoring the court cases, basic records like register of court cases, register of cases under stay etc. are not being maintained. Non-maintenance of records/ registers leads to systemic inefficiencies in proper monitoring of cases, delay in getting stay orders vacated and consequent revenue realisation.

Government stated (July 2025) that necessary directions were issued to Deputy Commissioner (Law), Ernakulam to monitor court cases, maintain registers of court cases, cases under stay and the cases disposed and also to take necessary steps to vacate the stay orders.

- (iv) Excise Commissioner identified TSCL, Thiruvalla and Menonpara, Palakkad as the location to destruct the dead stock of liquor accumulated in warehouses and retail shops of KSBC. During the years 2021-22, 2022-23 and 2023-24 dead stock of 3.63 lakh cases and 6.19 lakh bottles of foreign liquor in Thiruvalla and 2.28 lakh cases and 10.04 lakh bottles of foreign liquor in Palakkad were discharged to open yard. Disposal of dead stock of liquor without any effluent treatment, is an environment hazard and is not in order. Moreover, Excise officials are not supervising the destruction of dead stock at

Menonpara, Palakkad by preparing *Mahazar*¹⁰⁹ in violation of the sanction order of the Commissioner of Excise.

Government stated (July 2025) that necessary directions were issued to the Excise Officials to destroy dead stock of liquor in a systematic manner after relevant documentation.

- (v) Rule 9 of Brewery Rules, 1967 states that the surveying officer shall be provided by the department with a standard saccharometer and thermometer for the purpose of measuring gravity for assessment of excise duty on beer. However, audit observed that the set of equipment was not available with the Excise officials at breweries in Kanjikode and Chalakudy.
- (vi) 24 instances of demand issued from September 2011 to March 2024 amounting to ₹3.05 crore as shown in **Appendix LII** are pending in courts and no earnest effort appears to have been taken for vacating the stay orders.

Government stated (July 2025) that necessary directions were issued to all Deputy Excise Commissioners to take speedy action for vacating stay orders on demand raised by Department to avoid revenue loss to Government.

The audit findings reveal lapses in internal control mechanisms within the Excise department. Non-adherence to mandatory inspection schedules by supervisory officers and failure to maintain critical records for effective court case monitoring were observed. Environmental protocols were breached during the destruction of dead stock, and use of standard equipment for duty assessment were neglected. The inadequate follow-up on court cases and pending collection of demands indicate systemic inefficiencies and weak enforcement.

Recommendation 37

Government may incorporate adherence to packaging norms and environmental responsibilities as a condition for licence renewal or continuation, with periodic inspections and compliance audits. Government may direct the Excise department to maintain an inspection calendar with a prescribed schedule of Excise officers and mandate submission of periodic compliance reports. Government may strengthen the legal monitoring unit by maintaining essential records to enable effective tracking and timely follow-up of litigation. Department may develop and implement a Standard Operating Procedure (SOP) for the disposal of dead stock of liquor, mandating treatment through environmentally compliant methods.

¹⁰⁹ A *Mahazar* is a document prepared by a police officer or public authority, often in the presence of witnesses recording important observations made during an investigation.

3.4.12 Conclusion

The Kerala Excise department has successfully evolved from a revenue-focused agency into a proactive institution addressing substance abuse through enforcement, awareness, and rehabilitation. Its achievements include major seizures of narcotic drugs and the launch of the Vimukti Mission in 2016. The mission works in close collaboration with schools, colleges, NGOs, and community organisations, establishing de-addiction centres in all 14 districts, forming Anti-Narcotics Clubs in educational institutions, and running state-wide awareness and de-addiction campaigns.

A significant innovation has been the preparation of a multi-departmental SOP to identify and rehabilitate children addicted to drugs, supported by legal awareness and counselling. Further, initiatives such as the *Nasha Mukh Nyaya Abhiyan*, implemented in partnership with National Legal Services Authority and Kerala State Legal Services Authority, aim to combat drug abuse through legal empowerment and humane enforcement. This integrated model of enforcement, prevention, and community rehabilitation stands as a replicable good practice for other states.

The Subject Specific Compliance Audit on Manufacture and Sale of Foreign Liquor in Kerala was undertaken to ascertain whether the Acts/ Rules governing the manufacture/ import, transportation, storage and sale of foreign liquor and beer were effectively implemented, revenue due were timely demanded and realised to the State Exchequer.

A review of the processes involved in the manufacture and sale of liquor revealed significant revenue losses arising right from the import of ENA through to the manufacture and sale of liquor. This was mainly due to shortages or unaccounted ENA in distilleries, excessive transit wastage, non-recovery of establishment costs for Excise staff deployed at distilleries and warehouses, turnover of liquor escaped assessment, application of incorrect tax rates and short levy of Turnover Tax. While the Excise department is solely responsible for revenue realisation on account of ENA import and liquor production, the sale of liquor and related revenue collection requires effective coordination between the Excise department and the State GST department.

The review also identified several compliance deviations, such as failure to surrender transit passes at exit check posts, non-establishment of permanent Excise offices at newly opened warehouses, inadequate measures to ensure the quality of liquor manufactured in the State and absence of initiatives for collection and recycling of discarded plastic liquor bottles. It was also noticed that inadequate regulatory framework hindered the effective enforcement of certain statutory provisions.

