

CHAPTER II SALES TAX

2.1 Results of audit

Test check of the assessment files, refund records and other connected documents of the Commercial Taxes Department conducted during 2006-07 revealed underassessments of sales tax amounting to Rs. 389.08 crore in 1,264 cases, which broadly fell under the following categories.

(Rupees in crore)

Sl. No.	Nature of irregularity	No. of cases	Amount
1.	Short payment of tax due to under declaration of VAT	1	170.00
2.	Incorrect grant of exemption	213	110.44
3.	Non/short levy of tax	520	22.47
4.	Non-levy of penalty	29	9.42
5.	Application of incorrect rate of tax	140	5.76
6.	Other irregularities	361	70.99
	Total	1,264	389.08

During the year 2006-07, the department accepted underassessments and other deficiencies of Rs. 122.22 crore in 548 cases of which 124 cases involving Rs. 102.55 crore were pointed out in audit during the year 2006-07 and the rest in the earlier years. Out of this, Rs. 24.23 lakh in 14 cases was realised.

A few illustrative cases involving Rs. 179.59 crore are mentioned in the following paragraphs.

2.2 Short payment of tax due to under declaration of VAT

Under the Andhra Pradesh Value Added Tax (VAT) Act, 2005, liquor is taxable at the point of first sale in the State. Under the provisions of the Act, every registered dealer shall submit monthly returns along with the proof of payment of tax. If any mistake is detected in the return submitted by the dealer, the assessing authority (AA) shall issue a notice of demand for any short payment of tax. There is no provision in the VAT Act to grant an exemption of any taxable turnover. Further, the Act provides for making of rules to carry out the purpose of the Act.

During the audit of Agapura circle, it was noticed in August 2006 that a dealer while furnishing monthly returns for the year 2005-06, declared VAT of Rs. 2,039.95 crore instead of Rs. 2,209.95 crore, on taxable turnover of Rs. 3,157.08 crore. The AA did not raise the demand for short payment of VAT of Rs. 170 crore.

After the case was pointed out, the Government issued orders in February 2007¹, amending the VAT Rule with retrospective effect from April 2005, exempting turnover relating to additional trade margin of 10 *per cent* charged by the assessee though the Act did not provide for it.

Even after amending the rule, VAT payable by the dealer was Rs. 2,109.67 crore on the taxable turnover of Rs. 3,013.81 crore. This has resulted in short payment of VAT of Rs. 69.72 crore.

2.3 Excess credit of transitional relief

The VAT Act and Rules 2005, provide relief on sales tax at the commencement of the Act. According to the VAT Rules, on the first day of the commencement of the Act, if a dealer has in stock any goods on which sales tax has been paid under the APGST Act, that dealer shall be entitled to claim credit of sales tax for such goods which were purchased from 1 April 2004 to 31 March 2005.

During the audit of three circles², it was noticed between June and October 2006 that in three cases, the dealers were entitled to sales tax credit of Rs. 1 lakh against which the dealer availed the credit of Rs. 12.70 lakh. The AAs allowed excess credit of relief on sales tax of Rs. 11.70 lakh on the goods.

After the cases were pointed out, the Government stated in September 2007 that in one case show cause notice was issued; while in other case revision was under process. In respect of the remaining case, the Government replied in December 2007 that the relief allowed on the purchases made from outside the State was in order since the same were tax paid. The reply is not tenable since tax was not paid under the APGST Act.

¹ G.O.Ms.No.174 Rev (CT-II) dt.13 February 2007

² Hyderabad (Agapura, Nacharam), Mancherial

2.4 Incorrect grant of exemption

2.4.1 Under first schedule to the APGST Act, all liquors are taxable at the rate of 70 *per cent* at the point of first sale in the State. However, the Government in March 2001, granted exemption from the levy of tax on the amount of additional trade margin of 10 *per cent* charged by the Andhra Pradesh Beverages Corporation Limited as special privilege fee on the sale of IML/beer with effect from 1 April 2001.

During the audit of Agapura circle, it was noticed between August and September 2006 that the AA while finalising the assessment (March 2006) incorrectly exempted special privilege fee of Rs. 308.09 crore instead of Rs. 180.56 crore from levy of tax. This resulted in short levy of tax of Rs. 89.27 crore.

After the case was pointed out, the revisional authority revised the assessment in August 2007 determining tax of Rs.89.27 crore.

The matter was referred to the department in January 2007 and the Government in February 2007; their reply has not been received (December 2007).

2.4.2 Electrical items, groundnuts, stainless steel wire, articles of cast iron, computer software and flavoured milk are taxable under the APGST Act.

During the audit of five circles³, it was noticed between February and November 2006 in six cases that while finalising assessments between November 2004 and June 2006 for the years 2002-03 to 2004-05, AAs incorrectly exempted turnover of Rs. 4.44 crore relating to electrical items, groundnuts, stainless steel wire, articles of cast iron, computer software and flavoured milk. This resulted in non/short levy of tax of Rs. 37.73 lakh.

After the cases were pointed out, the department/Government stated in March/September 2007 that the assessments were revised (September 2006 and May 2007) in two cases involving Rs. 2.46 lakh out of which Rs. 1.44 lakh was adjusted against tax holiday in one case. Revised show cause notices were issued in two cases and revision of the assessment was being processed in one case. The reply in the remaining case has not been received (December 2007).

2.4.3 Under Section 5C of the APGST Act, sale of articles of food and drinks in restaurants or catering houses or hotels, irrespective of their being tax suffered, are taxable at the rate of eight *per cent* with effect from 31 December 1999 if the turnover of a dealer exceeds Rs. 2 lakh in a year.

During the audit of Nellore-I circle, it was noticed in November 2005 that the AA while finalising the assessments of a dealer for the years 2002-03 and 2003-04 incorrectly exempted turnover of Rs. 1.23 crore relating to sale of food from levy of tax. This resulted in non-levy of tax of Rs. 9.80 lakh.

³ Hyderabad (Basheerbagh, MJ Market, Tarnaka), Madanapalli, Secunderabad (Ramgopalpet)

After the case was pointed out, the Government stated in September 2007 that show cause notice had been issued for revision of the assessments.

2.5 Short levy of tax on works contracts

Under Section 5F of the APGST Act, every dealer has to pay tax at the prescribed rate on his turnover of transfer of property either as goods or in some other form involved in the execution of works contract subject to exemptions and deductions provided for, under sub clauses (a) to (l) of Rule 6(2) of APGST Rules.

2.5.1 Incorrect computation of turnover

In determining the turnover of a dealer, deductions specified under the APGST Rules, shall be allowed from the turnover of the dealer if accounts are maintained as required under Rule 45(1-C) of the APGST Rules. If detailed accounts are not maintained and the amounts specified under Rule 6(2) are not ascertainable from the accounts of a dealer, his turnover shall be determined after deducting the amount calculated at percentages prescribed under Rule 6(3) (ii). Deductions on account of cost of establishment, bank charges, audit fee, sales tax and income tax are not exempted from levy of tax under the APGST Rules.

During the audit of Assistant Commissioner (AC), large tax payers unit (LTU) Hyderabad (Rural) and 46 circles⁴, it was noticed between January 2005 and December 2006, that the AAs while finalising the assessments between July 2003 and December 2006 in 91 cases for the years 2001-02 to 2004-05, incorrectly arrived at taxable turnover of Rs. 158.98 crore instead of Rs. 228.57 crore. The short determination of taxable turnover of Rs. 69.59 crore with tax effect of Rs. 6.47 crore was due to allowance of inadmissible deductions on account of cost of establishment, bank charges, audit fee, sales tax and income tax etc.

After the cases were pointed out, the Government stated between September and December 2007 that the assessments had been revised in 33 cases out of which Rs. 8.01 lakh had been collected in two cases; show cause notices/revised show cause notices for revision of assessments had been issued in 33 cases and revision of assessment was being processed in six cases. In two cases, the assessments had been partly revised. However, in these cases it was contended that turnover representing sales tax and income tax were statutorily exempted from tax. The revision needs re-examination as under Rule 6(1) tax collections are not exempted. In one case, the Government

⁴ Ananthapur, Bhongir, Gudur, Guntur (Brodipet, Lalapet), Hyderabad (Agapura, Ashoknagar, Basheerbagh, Hydernagar, Hyderguda, Khairatabad, Madhapur, Musheerabad, Nacharam, Punjagutta, Rajendranagar, Saroomnagar, Tarnaka), Jagitial, Janagaon, Kadapa, Kakinada, Karimnagar, Khammam, Khammam-II, Kurnool-II, Kurnool-III, Medak, Madanapalli, Mahaboobnagar, Mancherial, Nirmal, Nizamabad, Ongole-I, Ongole-II, Peddapally, Rajahmundry (Aryapuram), Secunderabad (R.P. Road), Siddipet, Tuni, Visakhapatnam (China Waltair, Dabagardens, Dwarakanagar, Gajuwaka), Vuyyuru, Warangal (Fort Road)

stated (October 2007) that net turnover was in order. The reply is not tenable since the entire taxable turnover was not taxed. In another case, it was replied that the turnover on which tax was not levied related to salaries and wages, gross profit and tax exempted consumer goods, which were exempted under the APGST Rules. The reply is not tenable since these are inadmissible deductions under the APGST Rules. The replies in respect of the remaining cases had not been received (December 2007).

2.5.2 Incorrect grant of exemption on inter-State purchases

Under the proviso to Section 5F of the APGST Act, tax shall be leviable on the turnover of goods either obtained or purchased from other States by the contractor and used in the execution of works contracts.

During the audit of nine circles⁵, it was noticed between December 2005 and September 2006 that in 16 cases the AAs while finalising the assessments between August 2004 and March 2006 for the year 2001-02 to 2003-04, incorrectly exempted turnover of Rs. 25.53 crore relating to purchase of material from other States by contractors and used in the execution of works contracts resulting in short levy of tax of Rs. 2.04 crore.

After the cases were pointed out, the Government stated between September and December 2007 that the assessments had been revised in two cases; show cause notices had been issued in six cases and revision of assessments was being processed in three cases. In respect of five cases (Aryapuram and Rajendranagar), the Government contended in September 2007 that the contract involved inter-State purchases, which were exempted from levy of tax. The reply is not tenable as the proviso to section 5F of the Act provides for tax on inter-State purchase of goods used in the execution of works contracts.

2.5.3 Short levy of tax under composition

The tax payable on works contracts can be compounded under Section 5-G of the APGST Act at four *per cent* with effect from 1 January 2000. However, when an assessee opts for composition of tax, no deduction is admissible and tax is payable on the total amount paid or payable to the assessee towards the execution of works contract excluding registered sub-contractors payment.

During the audit of 10 circles⁶, it was noticed between December 2005 and November 2006 that the works contractors opted for composition of tax. They were not entitled to any deduction from their taxable turnover. However, the AAs while finalising the assessments in 13 cases relating to the years 2001-02 to 2004-05, between April 2004 and August 2006, incorrectly allowed deductions of Rs. 8.50 crore from their gross turnover. This resulted in short levy of tax of Rs. 28.62 lakh.

⁵ Hyderabad (Hyderguda, Vidyanagar, Rajendranagar), Nirmal, Rajahmundry (Aryapuram), Secunderabad (Marredpally, Ramgopalpet), Visakhapatnam (Dabagardens and Kurupam Market)

⁶ Hyderabad (Begumpet, Basheerbagh, IDA-Gandhinagar, Khairatabad, Punjagutta, Rajendranagar, Tarnaka and Vidyanagar), Secunderabad (Malkajgiri and Marredpally)

After the cases were pointed out, the Government stated between September and December 2007 that the assessments had been revised and demand raised in two cases; show cause/revised show cause notices had been issued in seven cases and revision of assessment was being processed in four cases.

2.6 Sales tax incentives for industrial units

With a view to encouraging the growth of industries in the State, Industries Department has been notifying various incentive schemes from time to time providing sales tax incentives in the form of sales tax deferment and sales tax holiday (exemption) to industrial units.

For according sanctions under various incentive schemes, the Government constituted State level committee (SLC) and district level committee (DLC). On the basis of sanctions, the Commissioner of Industries issues final eligibility certificate (FEC) indicating the extent and duration of incentives for implementation by the Commercial Taxes Department.

Irregularities in sanction and availing of tax incentives noticed during the local audit of the Commercial Taxes Department are mentioned in the following paragraphs.

2.6.1 Availing of excess sales tax incentive

During the audit of two circles⁷, it was noticed between June/October 2006 in two cases that the AAs while finalising the assessments in March 2006 for the year 2002-03, allowed sales tax exemption of Rs. 9.52 crore upto 2002-03 against their sanctioned exemption limit of Rs. 6.08 crore. The AAs failed to detect the mistake resulting in excess availing of sales tax exemption of Rs. 3.44 crore.

After the cases were pointed out, the Government stated between September and December 2007 that the assessments had been revised in both the cases and demands totalling Rs. 174.39 lakh raised.

2.6.2 Non-recovery of sales tax incentives due to closure of production before the stipulated period

Under the incentive schemes, industrial units availing of sales tax incentives were to be in continuous production in the manufacture of approved lines, without any break in production except for a break not exceeding one year owing to reasons beyond their control. The incentives granted were liable to be recovered if the unit went out of production for a period exceeding one year during the period of availing such incentives.

⁷ Bhongir, Secunderabad (S.D. Road)

During the audit of seven circles⁸, it was noticed between August 2005 and November 2006 that nine industrial units availing of sales tax incentives stopped production during the period of availing such incentives between 1999-2000 and 2005-06. Incentives amounting to Rs. 2.18 crore availed by these units were not recovered by the department.

After the cases were pointed out, the Government stated between April and December 2007 that action was being taken to recover the arrears in two cases, notices had been issued in four cases, while in one case the Industries Department had been addressed in September 2006 for cancellation of deferment facility to the unit and for initiating the recovery process. In one case, the audit observation was accepted but action proposed to be taken was not indicated. The reply in respect of the remaining case has not been received (December 2007).

2.6.3 Incorrect adjustment of deferment on products not specified in the sanction

Sales tax incentives are admissible only to the products manufactured and sold by the industries specified in the FEC.

During the audit of three circles⁹, it was noticed between August 2005 and September 2006 in four cases finalised between November 2004 and March 2006 that sales tax exemption/deferment of Rs. 50.97 lakh was granted for the period 2001-02 to 2003-04 though the products were not specified in the FECs. This had resulted in incorrect adjustment of tax deferred from tax due.

After the cases were pointed out, the Government stated between September and December 2007 that the assessments had been revised in two cases and demands totalling Rs. 14.67 lakh raised; in one case (Kakinada circle) show cause notice had been issued and action was being taken to issue final orders for collection of the tax. The reply in respect of the remaining case has not been received (December 2007).

2.6.4 Non-recovery of interest on belated payment of deferred sales tax

The Government order¹⁰ dated March 1993 stipulates that the deferred sales tax allowed in each year is to be paid back without interest after the expiry of the relevant period, in annual instalments, on the due dates specified for repayment. Belated payments attract interest at 21.5 per cent per annum.

During the audit of LTU Nalgonda, it was noticed in February 2006 that a dealer paid deferred sales tax of Rs. 33.76 lakh belatedly. Interest of Rs. 11.85 lakh on belated payments ranging from 18 to 20 months though leviable was not levied by the AA.

⁸ Bhongir, Chilakaluripeta, Hyderabad (IDA Gandhinagar, Nacharam, Rajendranagar), Nandigama, Proddutur-I

⁹ Hyderabad (Nacharam, Rajendranagar), Kakinada

¹⁰ G.O.Ms.No.117 Industries and Commerce (I&R) Department dt.17 March 1993

After the case was pointed out, the Government stated in December 2007 that a demand notice was issued and served to the dealer in December 2006.

2.7 Short levy of tax due to application of incorrect rate

Tax at the rates specified in the Schedules I to VI of the APGST Act, is leviable on the commodities included in these schedules. The commodities not specified in any of these schedules, fall under the VII schedule and are taxable at 12 *per cent* from 1 January 2000.

During the audit of three¹¹ LTUs and 25 circles¹², it was noticed between November 2005 and December 2006 that the AAs while finalising the assessments in 31 cases between June 2004 and March 2006 for the years 2001-02 to 2004-05, levied tax on refrigerators, machinery, glucometers, wrist watches, steel fittings, cables, RCC¹³ spun pipes, tractors and conductors etc., at lower rates than those specified in the Act, resulting in short levy of tax of Rs. 2.06 crore.

After the cases were pointed out, the Government stated between March and December 2007 that the assessments had been revised in 14 cases out of which an amount of Rs. 7.79 lakh was collected/adjusted in six cases. Show cause/revised show cause notices had been issued in eight cases. Revision of assessment was being processed in five cases. Appeal in favour of the assessee was allowed in one case. The replies in respect of the remaining three cases had not been received (December 2007).

2.8 Short levy of tax on inter-State sales

2.8.1 The Central Sales Tax (CST) Act, 1956 provides that inter-State sales not supported by declaration in form 'C' are taxable at twice the rate applicable to sale or purchase of these goods inside the State in respect of declared goods and in respect of other goods at 10 *per cent* or at the rate of tax applicable to sale or purchase of such goods within the State whichever is higher.

During the audit of 12 circles¹⁴, it was noticed between December 2005 and November 2006 that in 12 cases, inter-State sales valued as Rs. 58.43 crore were not supported by declaration in the prescribed forms. The AAs while finalising the assessments for the years 2001-02 to 2004-05, between August

¹¹ Ananthapur, Secunderabad and Vizianagaram

¹² Akiveedu, Chittoor, Eluru, Gudur, Guntur (Eluru Bazaar, Kothapet), Hindupur, Hyderabad (Ashoknagar, Basheerbagh, Hyderguda, Keesara, Nacharam, Rajendranagar, Sanathnagar, Saroornagar), Mangalagiri, Nandyal-II, Nellore-III, Nidadavole, Rajahmundry, Secunderabad (Marredpally, Ranigunj), Tanuku-I, Visakhapatnam (China Waltair, and Dabagardens)

¹³ Reinforced cement concrete

¹⁴ Hyderabad (Agapura, Gandhinagar, Hyderguda, Hydernagar, Keesara, Punjagutta, Rajendranagar) Nalgonda (Miryalaguda), Macherla, Secunderabad (Bowenpally, Marredpally and Ramgopalpet)

2004 and March 2006, either omitted to levy tax or levied tax at lower rate. This resulted in short levy of tax of Rs. 1.33 crore.

After the cases were pointed out, the Government stated between March and October 2007 that the assessments had been revised in four cases and of these, Rs. 2.99 lakh was covered by sales tax deferment in one case. Notices for revision had been issued in two cases and in another two cases revision of assessment was being processed. In one case, it was stated that as per CST Act, if the sale or purchase was generally exempted under the local Sales Tax Act of the State, inter-State sales were to be taxed at “nil” rate. The reply is not tenable since in the instant case, the exemption given under the APGST Act was specific and not general. In another case, it was stated that a revision of assessment was not warranted since the goods were manufactured by the company as per the customer’s specification and tax was leviable under section 5G of the APGST Act. The reply is not tenable as the assessee manufactured packing material within the State and transferred the final product to other State and was liable to be taxed under the CST Act. The replies in respect of the remaining two cases, have not been received (December 2007).

2.8.2 Under Section 6-A of CST Act, read with Rule 9A(2) of CST (AP) Rules, each declaration in form ‘F’ shall cover transactions effected during a period of one calendar month. Therefore, a single declaration issued to cover transfer of goods for more than one month is to be treated as invalid and the turnover has to be brought to tax treating it as inter-state sales not covered by proper declarations.

During the audit of three¹⁵ circles, it was noticed between January and June 2006 that in three cases of branch transfer of goods, valued as Rs. 2.50 crore were supported by ‘F’ forms. As each ‘F’ form contained transactions of more than one month, these were liable to be treated as invalid. But the AAs while finalising the assessments between July 2004 and February 2006 for the years 2001-02 to 2002-03, incorrectly exempted the turnover from levy of tax. This resulted in short-levy of tax of Rs. 25.01 lakh.

After the cases were pointed out, the Government stated in September 2007 that show cause notices had been issued in all the three cases.

2.9 Non-levy of interest for belated payment of tax

The APGST Act provides that interest is leviable on tax, if such dues are not paid within the time specified for payment.

During the audit of Somajiguda circle in November 2006, it was observed that a dealer failed to pay tax of Rs. 3.59 crore along with his monthly returns of June, July, August and September 2002. It was paid after a delay ranging between 10 and 328 days. The AA while finalising the assessment relating to the year 2002-03 in March 2006 did not levy interest of Rs. 99.08 lakh on

¹⁵ Anakapalli, Hyderabad (Hydernagar), Karimnagar

belated payment of tax. This resulted in short realisation of revenue. After the case was pointed out, the Commissioner stated in October 2007 that the assessment had been revised in August 2007 levying interest of Rs. 99.08 lakh.

The matter was referred to the Government in May 2007; their reply had not been received (December 2007).

2.10 Non-levy of penalty

Under Section 5-B of the APGST Act, purchases of a dealer for use in manufacture attract a concessional rate of tax at four *per cent* on the production of form 'G'. Under sub section 2(ii), misuse of form 'G' attracts penalty of not less than three times which may extend up to five times the tax leviable on the sale of goods so purchased.

During the audit of the Ongole circle, it was noticed (May 2005) that an assessee had purchased C.I. pipes valued as Rs. 72.71 lakh against form 'G' and consumed these in the construction of buildings instead of utilising them in manufacturing activity. Thus, minimum penalty amounting to Rs. 17.45 lakh was leviable on tax of Rs. 5.82 lakh for misutilisation of 'G' form.

The matter was referred to the department in January 2007 and the Government in May 2007; their reply has not been received (December 2007).

2.11 Incorrect allowance of set-off of taxes

Under the provisions of the APGST Act and the notifications issued thereunder, set-off can be allowed on the sale of finished goods for tax paid on purchase of raw material and used in the manufacture of goods, provided transactions at both the ends take place within the State.

During the audit of five circles¹⁶, it was noticed between May and September 2006 that set-off of Rs. 5.16 crore was allowed between April 2005 and March 2006 against the admissible set-off of Rs. 5.08 crore during the assessment years 2002-03 to 2004-05 in six cases relating to jute, iron and steel, paper and plastics. Set-off was either allowed in excess of tax already paid or was incorrectly determined. Excess grant of set-off resulted in short levy of tax of Rs. 8.32 lakh.

After the cases were pointed out, the Government stated in September 2007 that assessments had been revised in four cases; while revision of assessment was being processed in two cases.

¹⁶ Hyderabad (Rajendranagar, Saroornagar), Nandyal-II, Sattenapalli, Visakhapatnam (Gajuwaka)

2.12 Misclassification of sale as works contract

Under Schedule I to the APGST Act, RCC sleepers are taxable at the rate of eight *per cent* from 1 January 2000 at the point of first sale in the State. It was judicially held¹⁷ that manufacture and supply of goods according to the specifications given by the contractee constitutes sale and not works contract.

During the audit of Tuni circle (June/July 2006), it was noticed that a manufacturer supplied pre-cast concrete blocks valued as Rs. 1.77 crore to another registered dealer as per his specifications. The sale was to be taxed at the rate of eight *per cent*. The AA, however, treated the supply as works contract and levied tax at the rate of four *per cent*. This resulted in short levy of tax of Rs. 7.09 lakh.

After the case was pointed out, the Commissioner stated in October 2007 that the assessments had been revised.

The matter was referred to the Government in May 2007; their reply has not been received (December 2007).

¹⁷ M/s Suman Engineering Company Vs State of Andhra Pradesh (30 STJ P.78)