

## CHAPTER-II: TAXES ON SALES, TRADE, ETC.

### 2.1 Results of audit

Test check of records of sales tax offices, conducted during the year 2005-06, disclosed underassessments of tax, non/short levy of interest/penalty, etc., amounting to Rs.52.42 crore in 856 cases, under the following broad categories:

**(Rupees in crore)**

<b>Sl. No.</b>	<b>Category</b>	<b>Number of cases</b>	<b>Amount</b>
1	Non/short levy of tax	357	17.99
2	Non/short levy of tax due to incorrect grant of exemption	116	20.60
3	Non/short levy of turnover tax/resale tax	113	2.26
4	Non levy of interest/penalty	128	6.98
5	Non forfeiture of excess tax collected	50	0.92
6	Non/short levy of additional tax	49	0.63
7	Other irregularities	43	3.04
	<b>Total</b>	<b>856</b>	<b>52.42</b>

During the course of the year 2005-06, the department accepted underassessments of tax amounting to Rs.11.48 crore in 551 cases that were pointed out in audit in earlier years and recovered Rs.9.26 crore in 457 cases.

A few illustrative cases including some cases noticed in earlier years that could not be included in previous Reports involving Rs.25.74 crore are given in the following paragraphs. Of this, Rs.1.67 crore had been recovered.

## 2.2 Incorrect grant of tax incentives to industries

**2.2.1** In accordance with notifications issued from time to time under the Karnataka Sales Tax Act (KST Act) 1957 and the Central Sales Tax Act (CST Act) 1956, exemption from payment of tax is allowed to tiny/small scale/medium and large scale industries based on the fixed assets valuation certificate issued by the Department of Industries and Commerce. In cases of units undertaking expansion schemes, tax exemption was to be limited to the difference between the total tax liability and the average tax liability of three years immediately preceding the year in which investment for expansion took place. Further, if any unit which has opted for tax exemption collects any amount by way of tax or purporting to be by way of tax, it shall forthwith cease to be eligible for tax exemption for the period during which such amounts were collected and subsequently for the remaining prescribed period, such units shall be eligible only for tax deferment.

It was noticed between July 2005 and January 2006, that in four districts while finalising six assessments of four SSI units between January 2004 and March 2005, for the years 2001-02 to 2003-04 sales tax exemption of Rs.10.03 lakh was incorrectly granted as detailed below:

(Rupees in lakh)				
Sl. No.	District (number of cases)	Assessment year (date of assessment)	Nature of irregularity	Tax incorrectly exempted
1	Belgaum (2)	2001-02 and 2002-03 (October 2004 and January 2005)	The dealer opted for sales tax exemption but collected tax on their sales. Therefore the dealer ceased to be eligible for exemption. However, exemption benefit was incorrectly allowed.	3.43
2	Bellary (1) Dakshina Kannada (2)	2002-03 and 2003-04 (January 2004 and February 2005)	The dealers were availing tax exemption under expansion scheme. Therefore tax exemption was to be limited to the difference between total tax liability of Rs.25.29 lakh and the average tax liability of Rs.3.51 lakh. However, exemption benefit was incorrectly allowed on entire amount of tax levied of Rs.25.29 lakh instead of Rs.21.78 lakh. This resulted in excess exemption of Rs.3.51 lakh.	3.51

(Rupees in lakh)				
Sl. No.	District (number of cases)	Assessment year (date of assessment)	Nature of irregularity	Tax incorrectly exempted
3	Shimoga (1)	2002-03 (March 2005)	Against tax exemption of Rs.16.46 lakh admissible to a dealer for the year 2002-03, entire amount of tax levied of Rs.19.55 lakh was exempted. This resulted in excess exemption of Rs.3.09 lakh.	3.09
<b>Total (6)</b>				<b>10.03</b>

These cases were pointed out between July 2005 and January 2006 to the concerned assessing authorities (AAs) and reported between August 2005 and March 2006 to the Commissioner of Commercial Taxes (CCT), but replies have not been received (November 2006).

The matter was referred to Government in May 2006; reply has not been received (November 2006).

**2.2.2** Government of India amended the CST Act from 11 May 2002 according to which production of declaration in form C or certificate in form D was essential to grant exemption from levy of tax under the Act. By a notification dated 31 May 2002 issued under the CST Act, Government of Karnataka directed that tax exemption granted to industrial units under various notifications shall be subject to the condition of furnishing of declaration in form C or certificate in form D issued by the buyer.

In Bangalore (Rural), Bellary, Dakshina Kannada and Gulbarga districts, it was noticed that 17 industrial units covered by various exemption notifications made interstate sales of Rs.81.49 crore. These sales were not supported by prescribed declarations. However, while finalising 21 assessments of these assesseees between November 2003 and February 2005, the AAs incorrectly allowed exemption of Rs.11.40 crore. This resulted in non realisation of Government revenue to that extent.

After these cases were pointed out between December 2005 and February 2006, department accepted audit observations in four cases involving Rs.9.37 crore. Of these, additional demand of Rs.9.30 crore was raised in one case and notices were issued in respect of three cases of two dealers involving Rs.7.26 lakh. In respect of remaining 17 cases, final replies are yet to be received (November 2006).

Government endorsed the reply of the department in September 2006.

### **2.3 Non/short levy of tax, turnover tax and additional tax**

**2.3.1** Under the KST Act, tax was leviable on purchases/sales at the rates mentioned in the relevant schedules to the Act. In addition, cess at the rate of five *per cent* of tax from 1 April 1998 to 31 March 2002 and 15 *per cent* of tax from 1 February 2004 was also leviable.

In nine<sup>2</sup> districts, 30 AAs finalised, between April 2004 and March 2005, 108 assessments of 102 dealers for the years 1996-97, 1999-2000 to 2003-04. It was noticed between July 2005 and February 2006 that in these cases, incorrect rates of tax were applied on turnover of Rs.56.93 crore which resulted in short levy of tax of Rs.1.96 crore. These were due to misclassification of goods and transactions, extending the benefit of concessional rate given under certain notifications to ineligible cases, etc. A few illustrative cases are given below:

(Rupees in lakh)

<b>Sl. No.</b>	<b>District (number of cases)</b>	<b>Assessment year (date of assessment)</b>	<b>Nature of observation</b>	<b>Turnover involved</b>	<b>Tax levied short</b>
1	Bangalore (Rural)(1), Bangalore (Urban)(1) and Dakshina Kannada (3)	2002-03 and 2003-04 (between July 2004 and March 2005)	Concessional rate of tax at five <i>per cent</i> was incorrectly applied on sales made to BESCO <sup>3</sup> , MESCOM <sup>4</sup> and HESCO <sup>5</sup> . In these cases, transformer was liable to tax at 16 <i>per cent</i> and RCC pole was liable to tax at the rate of 12 <i>per cent</i> and 13 <i>per cent</i> respectively during 2002-03 and 2003-04.	253.11	19.80
2	Bangalore (Urban) (1)	2002-03 (July 2004)	Electronic musical instruments were incorrectly classified as Indian musical instruments and tax at four <i>per cent</i> was levied instead of 15 <i>per cent</i> .	91.10	10.02
After this was pointed out, department contended in July 2006 that electronic instruments sold by the assessee were Indian musical instruments. The reply was not tenable as under the Act, electronic musical instruments are not classified as Indian musical instruments.					

<sup>2</sup> Bangalore (Rural), Bangalore (Urban), Belgaum, Bijapur, Dakshina Kannada, Davanagere, Gulbarga, Shimoga, Udupi

<sup>3</sup> Bangalore Electricity Supply Company Limited

<sup>4</sup> Mangalore Electricity Supply Company Limited

<sup>5</sup> Hubli Electricity Supply Company Limited

(Rupees in lakh)

Sl. No.	District (number of cases)	Assessment year (date of assessment)	Nature of observation	Turnover involved	Tax levied short
3	Bangalore (Urban) (1)	2002-03 and 2003-04 (July/August 2004)	A dealer sold bread using the name "Good bread" and had turnover exceeding Rs.1 crore during each assessment year. This was to be treated as branded bread. It was liable to tax at 4 <i>per cent</i> from 1 April 2002 to 31 May 2003, five <i>per cent</i> from 1 June 2003 to 31 January 2004 and 5.6 <i>per cent</i> from 1 February 2004 to 31 March 2004. However, tax was levied at one <i>per cent</i> and two <i>per cent</i> as unbranded goods.	607.12	15.35
4	Bangalore (Urban) (1)	2001-02 (September 2004)	Sweets sold in sealed containers were taxable at 12.6 <i>per cent</i> . However, tax was levied at 10.5 <i>per cent</i> .	304.93	6.40

After these cases were pointed out between July 2005 and February 2006, department accepted in July 2006 audit observations in 68 cases involving Rs.1.02 crore. Of these, in 15 cases additional demand of Rs.28.14 lakh was raised and recovered Rs.13.63 lakh. Notice for revision of assessments was issued in 53 cases involving Rs.73.47 lakh. In respect of remaining cases, final replies have not been received (November 2006).

Government endorsed the reply of the department in September 2006.

**2.3.2** Under the CST Act, tax leviable on interstate sale of goods shall be at the rate of 10 *per cent* or at the rate applicable for sale or purchase of such goods inside the State whichever is higher. In case of declared goods, tax shall be calculated at twice the rate applicable to the sale of such goods inside the State. However, in case of interstate sale supported by declaration in form C or certificate in form D, tax leviable shall be at the rate of four *per cent* or the rate applicable to the sale or purchase of such goods inside the State which ever is lower.

In eight<sup>6</sup> districts, while finalising 59 assessments between May 2002 and March 2005 of 55 dealers for the years 1998-99 and 2000-01 to 2003-04, tax amounting to Rs.1.49 crore was levied short by 21 AAs due to application of incorrect rates of tax on turnover of Rs.130.68 crore. A few illustrative cases

<sup>6</sup> Bangalore (Rural), Bangalore (Urban), Belgaum, Chitradurga, Dakshina Kannada, Dharwad, Gulbarga, Raichur

are given below:

**(Rupees in lakh)**

Sl. No.	District (number of cases)	Assessment year (date of assessment)	Nature of observation	Turnover involved	Tax levied short
1	Bangalore (Rural)(1), Bangalore (Urban)(3) and Dakshina Kannada (1)	2000-01, 2002-03 and 2003-04 (between May 2004 and March 2005)	Tax on interstate sales not supported by C form was levied at the rate of four <i>per cent</i> instead of 10 <i>per cent</i> .	263.68	15.82
2	Bangalore (Urban) (3) Belgaum (1) Dakshina Kannada (1)	2002-03 (between May 2004 and March 2005)	Tax on interstate sales not supported by C form was levied at the rate of two <i>per cent</i> instead of 10 <i>per cent</i> .	474.76	37.98

After these cases were pointed out between July 2005 and February 2006, department accepted audit observations in 39 cases involving Rs.99.30 lakh. Of these, additional demand of Rs.29.93 lakh was raised in 13 cases and Rs.6.12 lakh recovered. Notices for revision of assessment were issued in 26 cases involving Rs.69.37 lakh. In respect of remaining 20 cases, final replies have not been received (November 2006).

Government endorsed the reply of the department in September 2006.

**2.3.3** Under the KST Act every registered dealer, whose total turnover in a year exceeds the prescribed monetary limit, was liable to pay turnover tax (TOT) at the prescribed rate(s) on his total turnover, after such deductions as were admissible under the Act upto March 2002.

In six<sup>7</sup> districts, while finalising 45 assessments of 44 assesseees between April 2004 and March 2005, for the years 1995-96 to 1997-98 and 1999-2000 to 2001-02, TOT was either not levied or levied short on turnover of Rs.80.87 crore by 23 AAs due to incorrect exemptions, application of incorrect rate, etc. This resulted in non/short levy of TOT of Rs.1.27 crore. A few instances are

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<sup>7</sup> Bangalore (Rural), Bangalore (Urban), Belgaum, Chitradurga, Dakshina Kannada, Shimoga

given below:

(Rupees in lakh)				
Sl. No.	District (number of cases)	Period (date) of assessment	Turnover involved	Tax effect
1	Bangalore (Urban) (5)	2000-01 and 2001-02 (between May 2004 and September 2004)	836.39	13.57
Total turnover of the assesseees in the assessment years as well as in the respective preceding years was more than Rs.10 crore and TOT was leviable at three <i>per cent</i> . However, it was levied at 1.5 <i>per cent</i> on turnover of Rs.6.31 crore and at one <i>per cent</i> on turnover of Rs.2.02 crore by the concerned AAs.				
2	Bangalore (Urban) (1)	2001-02 (August 2004)	319.42	9.58
Sale turnover of 'combined harvester' was liable to TOT at the rate of three <i>per cent</i> . However, AA incorrectly exempted TOT.				
3	Bangalore (Urban) (1)	2001-02 (January 2005)	128.43	3.85
Sale made by any dealer to M/s. Toyota Kriloskar Motors Ltd., was exempted from levy of sales tax but TOT was leviable. However, while finalising the assessment TOT was also exempted by the AA.				
4	Bangalore (Urban) (1)	1999-2000 (October 2004)	1,238.38	17.48
TOT was incorrectly levied at one <i>per cent</i> (on Rs.5 crore) and at two <i>per cent</i> (on Rs.7.33 crore) instead of three <i>per cent</i> on entire turnover.				

After these cases were pointed out between July 2005 and February 2006, department accepted in July 2006 audit observations in 35 cases involving Rs.114.46 lakh. Of these, additional demand of Rs.86.21 lakh was raised in 20 cases and Rs.36.54 lakh recovered in six of them. Notice for revision of assessments was issued in 15 cases involving Rs.28.25 lakh. In respect of remaining 10 cases, final replies are yet to be received (November 2006).

Government endorsed the reply of the department in September 2006.

**2.3.4** Under the KST Act, from 1 June 2003 every registered dealer was liable to pay additional tax (AT) at the rate of one *per cent* of the taxable turnover.

In six<sup>8</sup> districts, while finalising between August 2004 and March 2005, 40 assessments of 40 assesseees for the year 2003-04, 14 AAs either omitted to levy AT or incorrectly exempted turnover of Rs.44.17 crore. This resulted in non levy of AT of Rs.44.17 lakh.

<sup>8</sup> Bangalore (Rural), Bangalore (Urban), Dakshina Kannada, Gulbarga, Mysore, Shimoga

After these cases were pointed out between July 2005 and February 2006, department accepted audit observation in all the cases. Of these, in 13 cases additional demand of Rs.8.67 lakh was raised by revision of assessments and Rs.7.44 lakh recovered in 11 of them. Notice for revision of assessments was issued in 24 cases. In respect of the remaining three cases, report on action taken has not been received (November 2006).

Government endorsed the reply of the department in September 2006.

## **2.4 Incorrect grant of exemption**

Under the KST Act and CST Act, taxable turnover of every dealer shall be determined in accordance with relevant provisions of the Act and Rules made thereunder after allowing prescribed deductions from the total turnover. Tax is leviable on the taxable turnover determined at the rates mentioned in the relevant schedules to the Act. In addition, cess at the rate of five *per cent* of tax upto 31 March 2002 and 15 *per cent* after 1 February 2004, TOT at prescribed rate upto 31 March 2002 and AT at the rate of one *per cent* with effect from 1 June 2003 were also leviable. Under the CST Act, tax at specified rates is levied on interstate sale of goods.

In nine<sup>9</sup> districts, it was noticed between July 2005 and February 2006 that while finalising between May 2002 and March 2005, 47 assessments of 44 dealers for the years 1998-99 and 2000-01 to 2003-04, turnover aggregating Rs.44.18 crore was incorrectly exempted by 21AAs resulting in non levy of tax of Rs.2.92 crore. A few instances are given below:

**(Rupees in lakh)**

<b>Sl. No.</b>	<b>District (number of cases)</b>	<b>Period (date) of assessment</b>	<b>Turnover involved</b>	<b>Tax effect</b>
1	Bangalore (Urban) (1)	2003-04 (March 2005)	385.72	108.00
Aviation turbine fuel sold to aircrafts registered in any foreign country which is party to the Convention on International Civil Aviation was exempted by a notification effective from 3 December 2003. However, in the assessment concluded, exemption was incorrectly allowed even on the sales made between 1 April 2003 and 2 December 2003.				
2	Bangalore (Rural) (3) Bangalore(Urban) (4) Shimoga (1)	2001-02 and 2002-03 (between April 2004 and February 2005)	628.83	66.85
Notification exempting tax on raw materials, component parts and packing materials sold to 100 <i>per cent</i> export oriented units (EOUs) was effective from 14 September 2001. However, in the assessments concluded, exemption was incorrectly allowed on sales of such goods between 1 April 2001 and 13 September 2001 and also on sale of furniture.				

<sup>9</sup> Bangalore (Rural), Bangalore (Urban), Belgaum, Bidar, Chitradurga, Dharwad, Shimoga, Tumkur, Udupi



(Rupees in lakh)

Sl. No.	District (number of cases)	Period (date) of assessment	Turnover involved	Tax effect
3	Belgaum (1)	2001-02 (October 2004)	2,087.38	41.75
By a notification issued on 14 September 2001 tax on sales to 100 <i>per cent</i> EOUs in the State was exempted. However, tax was exempted on sales made to 100 <i>per cent</i> EOUs situated outside the State.				

After these cases were pointed out between July 2005 and February 2006, department accepted in July 2006 audit observations in 27 cases involving Rs.2.13 crore. Of these, in nine cases additional demand of Rs.1.42 crore was raised and Rs.58.21 lakh recovered. Notices for revision of assessments were issued in 18 cases involving Rs.70.91 lakh. In respect of the remaining cases, final replies have not been received (November 2006).

Government endorsed the reply of the department in September 2006.

## 2.5 Non levy of tax on branded goods

Under the KST Act, from 1 April 2000, every registered dealer who purchases goods without a brand name and sells such goods after assigning a brand name, shall be liable to pay tax at rates prescribed under the Act. However, the tax so payable shall be reduced by an amount of tax which was already paid at the time of purchase. Under the Act, chemical fertilizer was taxable at the rate of four *per cent* during 2002-03.

In Dakshina Kannada district, during the year 2002-03 an assessee purchased chemical fertilizer for Rs.23.08 crore and sold the same for Rs.27.67 crore after assigning brand name "Mangala brand". Tax leviable on sales turnover was Rs. 1.11 crore from which tax paid on purchases amounting to Rs.0.89 crore was deductible. The differential amount of Rs.0.22 crore was required to be demanded. However, the Deputy Commissioner of Commercial Taxes (Transition)-I, Mangalore, while finalising the assessment of the assessee for the year 2002-03 in February 2005, exempted the entire sale turnover as second sales. This resulted in non levy of tax of Rs.0.22 crore.

After this was pointed out in December 2005, department accepted audit observation and issued notice for revision of assessment.

Government endorsed the reply of the department in September 2006.

## **2.6 Non levy of purchase tax**

Under the KST Act, a dealer, who purchases any taxable goods which have not suffered tax and consumes them in the manufacture of other goods for sale or disposes of goods in any manner other than by way of sale in the State, was liable to pay tax on the purchase price of such goods at the same rate at which it would have been leviable on the sale of such goods inside the State.

In Bangalore (Urban), during 2000-01 to 2002-03, two dealers purchased sand, jelly, stone, stone dust and vetiver (a grass) root from unregistered dealers for use in construction of apartments and for manufacture of aroma respectively. The purchase turnover in these cases aggregated Rs.50.96 lakh. The AA, while finalising three assessments between May and September 2004 of these two dealers for the years 2000-01 to 2002-03, failed to levy tax on purchase turnovers. This resulted in non levy of purchase tax of Rs.5.37 lakh.

After these cases were pointed out in August and September 2005, department accepted audit observation in July 2006 and raised additional demand of Rs.5.37 lakh.

Government endorsed the reply of the department in September 2006.

## **2.7 Non levy of resale<sup>10</sup> tax**

Under the KST Act, from 1 April 2002, every registered dealer is liable to pay resale tax (RST) at the rate of 1.5 *per cent* on such portion of the total turnover which is not liable to tax under other provisions of the Act, after allowing such deductions as are admissible under the Act. However, RST was leviable at 0.3 *per cent* on sale of iron and steel.

In eight<sup>11</sup> districts, while finalising 23 assessments of 18 assesseees between April 2004 and March 2005, for the years 2002-03 and 2003-04, RST was not levied on turnover of Rs.17.92 crore by 15 AAs due to incorrect allowance of exemption. This resulted in non levy of RST of Rs.17.23 lakh.

After these cases were pointed out between July 2005 and February 2006, the department accepted audit observations in 15 cases involving Rs.10.76 lakh. Of these, in 11 cases additional demand of Rs.7.18 lakh was raised and Rs.3.35 lakh recovered in four of them. Notice for revision of assessment was

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<sup>10</sup> Sale of tax suffered goods

<sup>11</sup> Bangalore (Urban), Bijapur, Dakshina Kannada, Davanagere, Dharwad, Gulbarga, Shimoga, Tumkur

issued in four other cases involving Rs.3.58 lakh. In respect of remaining eight cases, final replies are yet to be received (November 2006).

Government endorsed the reply of the department in September 2006.

## **2.8 Incorrect grant of refund**

In terms of a notification issued under CST Act, in March 2002, from 1 April 2002, the tax payable by a dealer under the Act on oil and oil cake manufactured in the State out of the seeds which have suffered tax under the KST Act, shall be reduced by an amount equal to the tax paid on such oil seeds. No refund was admissible if tax payable on oil and oil cake was less than tax paid on oil seeds.

In Chitradurga district while finalising seven assessments of seven dealers between April 2004 and March 2005 for the years 2002-03 and 2003-04, tax levied under CST Act on oil and oil cake was Rs.15.26 lakh. The tax paid under the KST Act on corresponding oil seeds consumed in the manufacture of oil and oil cake was Rs.30.01 lakh. After reducing the tax paid on oil seed from the tax levied on oil and oil cake there was a balance of Rs.14.75 lakh. Of this, Rs.11.73 lakh was incorrectly adjusted towards tax payable by the respective dealers under the KST Act. This resulted in incorrect grant of refund of Rs.11.73 lakh in the form of adjustment of tax due under KST Act.

After these cases were pointed out in July 2005, department accepted audit observations in six cases and raised additional demand of Rs.10.80 lakh. In respect of the remaining case, final reply has not been received (November 2006).

Government endorsed the reply of the department in September 2006.

## **2.9 Non forfeiture of tax collected in excess**

Under the KST Act, a registered dealer is prohibited from collecting any amount by way of tax in excess of that specified in the Act. Where any collection is made in contravention thereof, the AA is required to forfeit the tax collected in excess.

It was noticed in four<sup>12</sup> districts while finalising 34 assessments of 33 dealers between November 2003 and March 2005, for the years 2000-01 to 2003-04, 16 AAs levied tax of Rs.17.95 crore. Against this, the dealers collected tax of Rs.18.45 crore. No action was initiated to forfeit excess collection of tax amounting to Rs.0.50 crore.

After these cases were pointed out between July 2005 and February 2006, the department accepted audit observations in 30 cases involving Rs.44.29 lakh. Of these in 21 cases additional demand of Rs.27.22 lakh was raised and Rs.14.62 lakh recovered. Notice for revision of assessments was issued in nine cases involving Rs.17.07 lakh. In respect of remaining four cases final replies have not been received (November 2006).

Government endorsed the reply of the department in September 2006.

## **2.10 Incorrect determination of taxable turnover**

Under the KST Act, a dealer is liable to pay tax on his taxable turnover, determined after allowing prescribed deductions from the total turnover of transfer of property in goods (whether as goods or in some other form) involved in the execution of works contracts at rates specified in the sixth schedule to the Act. However, dealers executing works contract have the option to pay tax for any year at four *per cent* on the total consideration. Where such option for payment of tax by composition is exercised, no deduction is admissible from the total consideration except for amounts paid to sub contractor as consideration for execution of works, subject to production of proof that such sub contractor is a registered dealer liable to tax under the Act and turnover of such amounts is included in the monthly returns filed by him.

**2.10.1** It was noticed between August 2004 and February 2006, that in Bangalore (Urban), Dakshina Kannada and Raichur districts while finalising 11 assessments between July 2002 and March 2005 for the years 1999-2000 to 2003-04 in respect of 10 dealers who were engaged in execution of works contracts, deduction aggregating Rs.2.70 crore was incorrectly allowed towards royalty, income tax and commissions paid, deposits made for obtaining electricity supply, gross profit on amounts paid to subcontractors, etc., by nine AAs. This resulted in short levy of tax of Rs.33.61 lakh.

After these cases were pointed out between August 2004 and February 2006, department accepted audit observations in 10 cases involving Rs.32.19 lakh. Of these, in seven cases additional demand of Rs.27.69 lakh was raised and Rs.2.86 lakh recovered. Notice for revision of assessment was issued in three

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<sup>12</sup> Bangalore (Urban), Belgaum, Dharwad, Gulbarga

cases involving Rs.4.49 lakh. Final reply in respect of a remaining case has not been received (November 2006).

Government endorsed the reply of the department in September 2006.

**2.10.2** It was noticed between August and September 2005 in Bangalore (Urban) and Dharwad districts that while finalising three assessments between January and March 2005 for the years 2001-02 and 2003-04 in respect of three dealers who were engaged in execution of works contracts and had opted for composition, taxable turnover was either incorrectly computed or deductions on account of labour and like charges were allowed incorrectly. This resulted in short levy of tax of Rs.10.10 lakh on a turnover of Rs.2.52 crore.

After this was pointed out between August and September 2005, department accepted audit observations in two cases involving Rs.2.69 lakh and issued notices for revision of assessments. In respect of the remaining case, final reply has not been received (November 2006).

Government endorsed the reply of the department in September 2006.

### **2.11 Short levy of penalty on misuse of concession to industrial inputs**

Under the provisions of the KST Act, tax payable by a registered dealer in respect of sale of any industrial inputs to another registered dealer for use as a component part, raw material, packing material or consumables in the manufacture of other goods inside the State for sale, shall be at the specified concessional rate on the turnover relating to such sale, on furnishing prescribed declarations. However, if any person sells such inputs contrary to such declaration, the AA shall impose upon him a minimum penalty equal to twice the amount of tax leviable on those goods. Chemicals and dyes were liable to tax at the rate of four *per cent*.

In Bangalore (Urban), it was noticed in August 2005 that a dealer purchased chemicals and dyes valued at Rs.1.21 crore during 2000-01 and 2001-02 after furnishing a declaration for use in manufacture of ready made garments but used the same in job works. As this was contrary to the declaration furnished, minimum penalty of Rs.9.66 lakh was leviable. However, while finalising the assessments in June and October 2004, the AA levied penalty of Rs.3.76 lakh only. This resulted in short levy of penalty of Rs.5.90 lakh.

After these cases were pointed out in August 2005, department accepted audit observation and issued notice for revision of assessments.

Government endorsed the reply of the department in September 2006.

## **2.12 Short levy of penalty on suppression of turnover**

Under the KST Act, if the return submitted by any dealer appears to be incorrect or incomplete, AA shall assess such dealer to the best of his judgement, recording the reason for such assessment. Further, while making such assessment, the assessing officer may also direct the dealer to pay in addition to the tax so assessed, a penalty not exceeding one and half times but not less than one half of the amount of tax due on the turnover that was not disclosed by the dealer in his return.

In Bangalore (Urban) and Chitradurga districts, while finalising in April 2004, four assessments of two dealers for the years 1999-2000 to 2001-02, two AAs levied tax of Rs.53.13 lakh on turnover of Rs.5.22 crore which was not disclosed by the dealers but was detected by investigating authorities. However, penalty of only Rs.0.72 lakh was levied for suppression of turnover as against the minimum penalty leviable of Rs.26.56 lakh. This resulted in short levy of penalty of Rs.25.84 lakh.

After these cases were pointed out between July and November 2005, department contended that levy of penalty under the said provision of the Act is not mandatory and that there were no adequate grounds to treat the non disclosure of turnover by the assessee as suppression and hence a small amount was levied as penalty. The reply was not tenable as the amount of penalty, once the provision is invoked, shall not be less than one half times the tax assessed on such turnover.

Government endorsed the reply of the department in September 2006.

## **2.13 Non levy of interest**

**2.13.1** Under the KST Act, every dealer is required to pay the full amount of tax payable on the basis of the turnover computed by him for the preceding month within 30 days of close of that month. Further, the full amount of tax payable by a dealer in advance for the year as reduced by the amount of tax already paid is to be paid within 30 days after the close of the year to which such tax relates. In case of default, the assessee is liable to pay interest at the rate of two *per cent* per month.

In 14 districts, though 162 dealers delayed payment of monthly/annual taxes amounting to Rs.8.50 crore by one to 47 months relating to the years 1999-2000 to 2003-04, interest of Rs.3.82 crore was not levied by 31 AAs, as detailed below:

(Rupees in lakh)					
Sl. No.	District (number of assesseees)	Period of assessment/ Date of assessment	Amount of tax involved	Delay in payment of tax (months)	Interest due
1	Bangalore (Rural) (19)	1999-2000 to 2003-04 (between January 2004 and February 2005)	74.95	2 to 47	30.94
2	Bangalore (Urban) (61)	1999-2000 to 2003-04 (between February 2004 and March 2005)	324.96	10 to 47	138.51
3	Belgaum (4)	2000-01 and 2002-03 (between April 2004 and February 2005)	20.93	1 to 40	14.51
4	Bellary (1)	1999-2000 (July 2003)	1.49	39	1.17
5	Bijapur (5)	2000-01 to 2003-04 (between March 2004 and January 2005)	17.26	2 to 41	8.49
6	Chitradurga (1)	1999-2000 and 2001-02 (November 2001 and October 2003)	11.77	17 to 19	4.30
7	Dakshina Kannada (35)	2000-01 to 2003-04 (between July 2003 and March 2005)	180.75	7 to 45	71.99
8	Davanagere (2)	2000-01 (May 2004)	2.50	37	1.83
9	Dharwad (19)	2000-01 and 2002-03 (between April 2004 and March 2005)	172.65	15 to 46	97.95
10	Gulbarga (6)	2002-03 and 2003-04 (between June 2004 and March 2005)	16.46	9 to 20	3.38
11	Hassan (2)	2002-03 and 2003-04 (May 2004 and March 2005)	4.45	9 to 14	0.97
12	Shimoga (2)	2003-04 (November 2004)	9.74	7 to 14	1.61
13	Tumkur (1)	2000-01 (May 2004)	3.25	37	2.40
14	Udupi (4)	2000-01 to 2002-03 (between May 2004 and February 2005)	8.78	14 to 26	4.09
	<b>Total (162)</b>		<b>849.94</b>		<b>382.14</b>

After these cases were pointed out between July 2005 and January 2006, department accepted audit observations in 89 cases involving Rs.2.23 crore. Of these, in 36 cases demand was raised for interest of Rs.52.78 lakh and Rs.22.07 lakh recovered. In 53 other cases, notices were served on the

concerned assesseees. In respect of remaining 73 cases, replies have not been received (November 2006).

Government endorsed the reply of the department in September 2006.

**2.13.2** Under the KST Act, tax or any other amount due is required to be paid within the prescribed time which, in the case of final assessments, is 21 days from the date of service of demand notice. In case of default in making payments, the assessee is liable to pay interest at the rate of two *per cent* per month.

In Bangalore (Urban) and Dakshina Kannada districts, it was noticed between August and December 2005 that 22 dealers paid between January 2003 and March 2005 the sums specified in the demand notices issued for the years 1995-96 to 2002-03 between August 1998 and September 2004. In these cases, the delay ranged between one to 69 months and interest of Rs.51.42 lakh was leviable. However, concerned AAs failed to levy interest to that extent.

After this was pointed out between August and December 2005, department accepted audit observations in 11 cases and raised demand of Rs.15.77 lakh of which Rs.1.71 lakh was recovered. In respect of remaining cases, replies have not been received (November 2006).

Government endorsed the reply of the department in September 2006.