

## CHAPTER II : COMMERCIAL TAX

### 2.1 Results of audit

Test check of the assessment cases and other records relating to the Commercial Tax Department during the year 2006-07 revealed underassessment, non/short levy of tax and penalty, application of incorrect rate of tax etc., involving Rs. 66.37 crore in 623 cases which fall under the following categories:

Sl. No.	Category	Number of cases	Amount (Rs. in crore)
1.	Non/short levy of tax	184	26.33
2.	Incorrect grant of exemption/deduction/ set off	95	6.28
3.	Application of incorrect rate of tax	91	4.53
4.	Incorrect determination of taxable turnover	40	2.45
5.	Other irregularities	213	26.78
<b>Total</b>		<b>623</b>	<b>66.37</b>

During the year 2006-07, the department accepted underassessment of tax of Rs. 15.33 crore in 149 cases. All these cases pertained to 2006-07. Rs. 95.10 lakh had been recovered in seven cases during the year.

A few illustrative cases involving Rs. 21.20 crore are mentioned in the following paragraphs.

## **2.2 Non-recovery of commercial tax from closed units**

As per the tax exemption scheme of 1994 issued under the Madhya Pradesh *Vanijyik Kar Adhiniyam (Adhiniyam)*, a new industrial unit holding eligibility certificate (EC) shall keep the unit running during the period of eligibility and also for a further period of five years from the date of expiry of the eligibility, failing which the EC shall be cancelled by the DLC/SLC<sup>1</sup> empowered to issue the EC. The amount of tax deferred/exemption availed of by the unit shall also be recovered.

Test check of the records of four offices<sup>2</sup> between April 2006 and January 2007 revealed that two industrial units were allowed deferment of tax of Rs. 4.70 crore and three units were allowed exemption from payment of tax of Rs. 2.07 crore under the 1994 scheme. Of these, four units closed their business during the period of eligibility while one unit closed its business within five years after the expiry of the period of the eligibility. The assessing authorities (AAs) did not take any action to refer the matter to the DLC/SLC for cancellation of EC and recover the amount.

After the cases were pointed out, the Government stated in November 2007 that in two cases action for recovery was in progress. In three cases it was stated that EC cannot be cancelled with retrospective effect. The reply is not tenable as cancellation of EC with retrospective effect is permissible under the provisions of the exemption notification for which action has not been taken.

## **2.3 Incorrect deduction of tax paid sales**

The *Adhiniyam*, Rules and notifications issued thereunder provide deduction of tax paid goods on which tax has been paid within the State to determine the taxable turnover. Where the dealer has furnished false particulars of his sales or purchases in his returns, the Commissioner shall impose a penalty not less than three times the tax payable. Under the *Adhiniyam*, packing material shall be liable to tax at the rate applicable to the goods packed in them.

Test check of the records of four offices between October 2005 and December 2006 revealed that the AAs allowed incorrect deduction of tax paid goods/packing material to five dealers assessed for the period 2000-01 to 2002-03 between July 2003 and January 2006. This resulted in short levy of tax of Rs. 1.17 crore and penalty of Rs. 2.92 crore as mentioned below:

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<sup>1</sup> DLC - District level committee.  
SLC - State level committee.

<sup>2</sup> Regional Assistant Commissioner (RAC): Bhopal, Khandwa and Khargone.  
Commercial Tax Officer (CTO): Indore.

Sl. No.	Name of the unit	Assessment year and month of assessment	Nature of observation
1.	RAC Indore RAC Morena	2002-03 January 2006 2002-03 September 2005	The AAs while finalising the assessments allowed deduction of tax paid sales of Rs. 23.50 crore and Rs. 86.42 lakh treating the transaction of iron & steel and vegetable oil as intra state purchase from registered dealers. Verification of the transactions, however, revealed that the dealers from whom the intra state purchases were made were not in existence. Thus, the deduction of tax paid goods allowed was incorrect which resulted in short levy of tax of Rs. 97.46 lakh with a minimum penalty of Rs. 2.92 crore.
After the cases were pointed out in December 2006, the Government accepted the audit observation in November 2007. However, further action taken has not been reported.			
2.	RAC Indore	2002-03 January 2006	A dealer sold tax paid packing material valued as Rs. 30.37 lakh with taxable medicines. The AA, however, allowed deduction of tax paid packing material which was not correct. This resulted in short levy of tax of Rs. 2.56 lakh.
The Government stated in November 2007 that the deduction allowed was correct in view of the MP High Court <sup>3</sup> decision of 1997 which stipulated that deduction of tax paid packing material used for packing of other goods was admissible. The reply is not tenable as the Supreme Court <sup>4</sup> has held in 1999 that even if packing material used for packing of other goods has been subjected to tax it shall be liable to tax at the rate applicable to the goods packed in them.			
3.	RAC Chhindwara	2001-02 December 2004	A cement dealer of Chhindwara submitted in his accounts incorrect taxable turnover of Rs. 1.16 crore instead of his actual turnover of Rs. 1.36 crore. Thus, the turnover was underassessed by Rs. 20.25 lakh resulting in short levy of tax of Rs. 2.79 lakh.
The Commissioner, Commercial Tax intimated in June 2007 that a demand for Rs. 2.79 lakh had been raised.			
4.	CTO Shajapur	2000-01 2001-02 September 2003 December 2003 March 2004	Intra state sale of cement of Rs. 99.70 lakh which was purchased after 1 November 2000 <sup>5</sup> from a company of Chhattisgarh State was liable to tax but the AA allowed the deduction of tax paid goods incorrectly treating it as the purchase from local registered dealers. This resulted in short levy of tax of Rs. 13.76 lakh at 13.8 per cent.
The Government stated in November 2007 that the cases had been reassessed under section 28 (1) in January 2007 and demand of Rs. 13.69 lakh had been raised.			

<sup>3</sup> Raymond Cement Works V/s STO (1997) 30-VKN-219 (MP)

<sup>4</sup> Supreme Court's decision in the case of M/s Premier Breweries V/s. State of Kerala (1999-32-VKN-317).

<sup>5</sup> Date of bifurcation of Madhya Pradesh.

## **2.4 Incorrect grant of exemption**

**2.4.1** As per the exemption notification dated 6 June 1995 issued under the *Adhiniyam*, a dealer holding EC shall be eligible for exemption to the extent of maximum cumulative quantum of the tax specified therein.

Test check of the records of the RAC, Gwalior in March 2007 revealed that a dealer holding EC was eligible for exemption from tax of Rs. 60.33 lakh, whereas the AA while finalising the assessment in July 2005 for the period 2002-03 allowed exemption of tax to the extent of Rs. 3.90 crore from the date of eligibility. This resulted in grant of exemption in excess of the eligibility with tax effect of Rs. 3.29 crore.

**2.4.2** As per the exemption notification dated 6 October 1994 issued under Madhya Pradesh General Sales Tax (MPGST) Act, a dealer holding EC for exemption from tax in respect of expanded capacity shall be liable to pay tax on the turnover of 100 per cent of its original capacity.

Test check of the records of the RAC, Gwalior in September 2006 revealed that during the year 2002-03 a dealer holding EC for exemption from payment of tax in respect of turnover pertaining to expanded capacity was entitled for exemption for sales valued as Rs. 13.20 crore under the expanded capacity. The AA while finalising the assessment in December 2005 allowed exemption on sales valued as Rs. 25.36 crore out of total turnover of Rs. 44.75 crore. This resulted in incorrect grant of exemption on sales valued as Rs. 12.16 crore with a tax effect of Rs. 46.12 lakh.

After the cases were pointed out (September 2006), the Government accepted the audit observations in November 2007. However, a report on further action taken has not been received (January 2008).

## **2.5 Application of incorrect rate of tax**

The *Adhiniyam* read with the Central Sales Tax Act (CST Act), 1956 and notifications issued thereunder specify the rates of commercial tax leviable on sale of different commodities.

Test check of the records of nine RAC<sup>6</sup> and four CTO<sup>7</sup> between May 2005 and March 2007 revealed that tax on the sales turnover of Rs. 49.02 crore in 19 cases assessed between April 2003 and January 2006 for the period April 1999 to March 2003 was levied at incorrect rates. This resulted in short levy of tax amounting to Rs. 2.61 crore. A few instances are mentioned below:

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<sup>6</sup> RAC - Bhopal, Chhindwara, Gwalior (2), Indore (3), Jabalpur & Satna.

<sup>7</sup> CTO - Bhopal (2), Gwalior and Indore.

(Rupees in crore)

Sl. No.	Name of unit and No. of cases	Period and Month of assessment	Name of Commodity	Turn over	Rate of tax applied (per cent)	Rate of tax applicable (per cent)	Short levy of tax
1.	RAC Bhopal, 1	2002-03 November 2005	LAB <sup>8</sup>	28.10	4.6	9.2	1.29
2.	RAC Jabalpur, 3	2001-02 & 2002-03 January 2005 & January 2006	Tower	9.84 0.71	4 8	13.8 13.8	0.97
3.	RAC Gwalior, 1	2002-03 July 2005	Mustard oil cake	2.18	1.15	4.6	0.08
4.	CTO 13 Indore, 1	2002-03, November 2005	Photo copier machine & parts	1.02	9.2	13.8	0.05
5.	RAC Indore, 1	2002-03, January 2006	Industrial solvent	0.35	4.6	13.8	0.03

After the cases were pointed out (March 2007), the Government accepted the audit observations and stated in November 2007 that the department had reassessed the cases of three dealers and raised demands totalling Rs.9.53 lakh out of which Rs. 8.45 lakh was adjusted against the quantum of exemption of tax. In the remaining cases it was stated that action would be taken.

## 2.6 Inadmissible deferment of purchase tax

As per 1986 Deferment Scheme, if a new industrial unit eligible for exemption from payment of tax (i.e. sales tax and purchase tax) under the exemption notification dated 19 February 1991, avails of the facility of deferment in lieu of the exemption, it shall be eligible for deferment of only that amount of tax which is payable by it in respect of the sales of goods manufactured by it.

Test check of the records of the RAC Gwalior in March 2007 revealed that a dealer holding EC for the deferment of tax, purchased raw material valued as Rs. 32.32 crore on which purchase tax was payable. The AA while finalising the assessment for the period 2002-03 in January 2006 levied purchase tax of Rs. 1.49 crore but allowed its deferment, which was not admissible. This resulted in short realisation of tax.

After the case was pointed out (March 2007), the Government replied in November 2007 that deferment allowed was correct in view of the provisions of the notification

<sup>8</sup> Linear Alkyl Benzene.

dated 19 February 1991. The reply is not tenable as the dealer was not entitled to deferment of purchase tax under the deferment scheme.

## **2.7 Non/short levy of entry tax**

Under the Madhya Pradesh *Sthaniya Kshetra Me Mal Ke Pravesh Par Kar Adhiniyam*, 1976 and Rules and notification issued thereunder, entry tax (ET) is leviable on the goods entering into a local area for consumption, use or sale therein at the specified rates. As per notification dated 14 December 2001 billets (a category of iron & steel) if used in the manufacture of steel rods is exempt from ET, but shall be liable to ET if utilised in the manufacture of wire rods.

Test check of the records of five RAC<sup>9</sup> and one CTO<sup>10</sup> between December 2005 and December 2006 revealed that in case of six dealers assessed between December 2004 and January 2006 for the period 2001-02 and 2002-03, ET amounting to Rs. 69.66 lakh was not levied/short levied on cosmetics, iron and steel, staple/viscose fibre, diesel oil, cement etc. valued as Rs. 21.11 crore on their entry into the local area.

After the cases were pointed out (December 2006), the Government accepted (November 2007) the audit observations in five cases involving Rs. 55 lakh and stated that in three cases demands totalling Rs. 9.25 lakh had been raised after reassessment. Report on action taken in two cases has not been received. In one case it was stated that since iron and steel (billets) were used in the manufacture of steel rods, it was exempt from ET under the notification dated 14 December 2001. The reply is not tenable. As the billets were utilised in the manufacture of wire rods, exemption allowed was not correct.

## **2.8 Non-levy of tax**

**2.8.1** A new unit holding EC under exemption scheme of 1994 is liable to tax in respect of the sale of manufactured goods which is adjustable against the quantum of exemption of tax as specified in the EC.

Test check of the records of RAC, Morena revealed that a dealer assessed in January 2006 holding EC under the 1994 scheme manufactured and sold goods valued as Rs. 11.32 crore but the AA while finalising the assessment did not levy tax thereon amounting to Rs. 45.29 lakh. This resulted in incorrect grant of tax benefit to that extent.

After the case was pointed out in March 2007, RAC Morena reassessed the case in June 2007 and raised a demand of Rs. 45.29 lakh which was adjusted against the quantum of exemption of tax.

**2.8.2** The *Adhiniyam*, Rules and notification issued thereunder, provide levy of tax on purchase value of raw material, incidental goods and packing material when purchased without payment of tax and used or consumed in the manufacture of

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<sup>9</sup> RAC: Guna, Indore (2), Jabalpur and Morena.

<sup>10</sup> CTO: Bhopal.

finished goods. If goods so purchased or the finished goods manufactured from such goods are transferred out of the state, purchase tax is leviable.

Test check of the records of two RAC at Indore and Gwalior and one CTO at Indore between November 2006 and March 2007 revealed that three dealers holding ECs for exemption under 1994 scheme assessed between November 2005 and January 2006 for the period 2002-03, purchased raw material valued as Rs. 4.12 crore on declarations without payment of tax for use in the manufacture of other goods. The AAs while finalising the assessment did not levy purchase tax. This resulted in non-levy of purchase tax of Rs. 18.96 lakh.

After the cases were pointed out (March 2007), the Government accepted the audit observations in November 2007 and stated that additional demands totalling Rs. 8.14 lakh had been raised and adjusted against the quantum of exemption in two cases. Further, report on action taken in the remaining case has not been received (January 2008).

## **2.9 Non-levy of interest**

Under Section 26 (4) (a) of the *Adhiniyam*, if a dealer liable to file return fails without sufficient cause to pay the amount of tax as per the return, he shall be liable to pay interest in respect of the tax payable by him.

Test check of the records of the RAC, Guna in October 2006 revealed that a dealer assessed in January 2006 for the period 2002-03 did not pay tax aggregating Rs. 1.15 crore on the taxable turnover as shown in the returns filed for the relevant period in anticipation of issue of EC by the Department of Industries for exemption from payment of tax. The dealer who had solvent extraction plant was not eligible for exemption after 22 August 1998<sup>11</sup> and was liable to pay interest on the amount of tax payable by him. But the AA while finalising the assessment, exempted the dealer from the payment of interest. This resulted in non-levy of interest of Rs. 63.19 lakh.

After the case was pointed out (October 2006), the Government stated in November 2007 that the liability to pay interest did not arise as the amount of tax payable according to returns was nil. The reply is not tenable because the sales of goods shown in the returns were liable to tax and hence interest was leviable under the *Adhiniyam*.

## **2.10 Non-levy of tax on sales incorrectly treated as tax free**

Under the *Adhiniyam* read with the CST Act, Rules and notifications issued thereunder, commercial tax is leviable on the sale of goods except those specified in schedule I of the *Adhiniyam* or exempted by the Government by issue of notification.

Test check of the records of three RAC at Gwalior and Indore and two CTOs at Indore between September 2006 and January 2007 revealed that in case of five dealers assessed between October 2005 and January 2006 for the period 2002-03,

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<sup>11</sup> Notification No. A-3-96-95-ST-V(54)/(55) dated 22.8.1998.

HDPE/PP<sup>12</sup> fabrics valued as Rs. 3.34 crore, though taxable under the *Adhyniam*, were incorrectly treated as tax free goods. This resulted in short levy of tax of Rs. 16.41 lakh.

After the cases were pointed out (January 2007), the Government stated in November 2007 that the benefit of exemption was allowed on the basis of the notification dated 24 August 2000. The reply is not tenable as the said notification exempts all type of cloth only and not HDPE/PP fabrics which is taxable under entry no. 28 of part V of schedule II of the *Adhinyam*.

## **2.11 Non-payment/levy of surcharge**

Under section 10A of the *Adhinyam* and notification issued thereunder, surcharge is leviable on the amount of tax at the rate of 15 *per cent*. Under the *Adhinyam*, any registered dealer who carries on wholly or partly the business of supplying goods in the course of execution of works contract entered into by him, may be permitted to pay in lieu of tax payable by him under the Act a lumpsum at such rate as may be prescribed.

**2.11.1** Test check of the records of three RAC at Gwalior, Morena and Sendhwa between March 2005 and March 2007 revealed that five works contract dealers assessed for the period 1999-2000 to 2002-2003 between January 2002 and January 2006, paid Rs. 78.04 lakh in lieu of tax at the prescribed lumpsum rate. However, they did not pay surcharge at 15 *per cent*, resulting in non-realisation of surcharge of Rs. 11.71 lakh.

After the cases were pointed out (March 2007), the Government stated in November 2007 that the prescribed lumpsum rate was inclusive of surcharge. The reply is not tenable since surcharge is payable in addition to the tax paid.

**2.11.2** Test check of the records of the regional office Morena in May 2003 and April 2004 revealed that in two cases of two dealers assessed for the period 2000-01 in November and December 2003, surcharge at 15 *per cent* on tax amount of Rs. 25.11 lakh payable on the sale of tractors was not levied. This resulted in non-levy of surcharge of Rs. 3.77 lakh.

After the case was pointed out (April 2004) the AA accepted the audit observation and raised the demand in May 2005.

The cases were forwarded to the department in May 2007 and to the Government in November 2007; their reply has not been received (January 2008).

## **2.12 Non/short levy of value added tax**

Under section 9-B of the *Adhinyam*, value added tax (VAT) is leviable at the prescribed rates on the added value of resale of goods specified in Part II to VI of schedule II of the *Adhinyam*.

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<sup>12</sup> HDPE - High density poly ethylene.  
PP - Poly Propylene.



Test check of the records of two RAC at Dewas and Indore between October 2004 and September 2006 revealed that in case of two dealers assessed for the period 1999-2000 and 2002-03 in December 2002 and December 2005, VAT amounting to Rs. 10.90 lakh was not/short levied on added value of Rs.1.29 crore on the resale of goods.

After the cases were pointed out the Government accepted the audit observation in November 2007 and stated that in one case demand of Rs. 2.81 lakh had been raised. Further, action taken in the other case has not been reported (January 2008).

### **2.13 Short levy of tax due to allowing incorrect deduction**

Section 2(w)(v) of the *Adhiniyam* prescribes a formula<sup>13</sup> to arrive at the amount of taxable turnover. It also provides that deduction on the basis of the formula shall not be made if the amount by way of tax collected by the registered dealer had been otherwise deducted from the aggregate of sale prices or not included in the sale price.

Test check of the records of two RAC at Indore and Morena and one CTO at Gwalior in November 2006 and February 2007 revealed that in four cases of three dealers assessed for the period 2001-02 and 2002-03 between January 2005 and January 2007, deduction of tax of Rs. 9.39 lakh was allowed in accordance with the prescribed formula. Since the dealers were holding EC for exemption from tax and had not collected tax, the deduction allowed was not correct. This resulted in short levy of tax of Rs. 9.39 lakh.

After the cases were pointed out (February 2007), the Government accepted the audit observations in November 2007 and stated that in case of one dealer demand of Rs. 1.25 lakh had been raised. Report on the action taken in the other cases has not been received (January 2008).

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<sup>13</sup> 
$$\frac{\text{Rate of tax} \times \text{aggregate of sale prices}}{100 + \text{rate of tax}}$$