CHAPTER IX
SERVICE TAX RECEIPTS

9.1 Tax administration

Service tax was introduced from 1 July 1994 through the Finance Act, 1994. Administration of service tax has been vested with the central excise department under the Ministry of Finance (the Ministry). The Central Board of Excise and Customs (the Board) has set up a separate apex authority headed by the Director General Service Tax (DGST) at Mumbai for its administration. Commissioners of central excise/service tax have been authorised to collect service tax within their jurisdiction. The number of services under the tax net had increased from 51 in 2002-03 to 97 in 2006-07.

9.2 Trend of receipts

Revenue projected through annual budget and actual receipts from service tax during the years 2002-03 to 2006-07 is exhibited in the following table:-

Table no. 1

(Amounts in crore of rupees)

Year	No. of services covered by tax	Budget estimates	Revised budget estimates	Actual receipts*	Difference between actual receipts and budget estimates	Percentage variation
2002-03	51	6026	5000	4122	(-) 1904	(-) 31.60
2003-04	58	8000	8300	7890	(-) 110	(-) 1.38
2004-05	71	14150	14150	14199	49	0.35
2005-06	81	17500	23000	23055	5555	31.73
2006-07	97	34500	38169	37598	3098	8.98

* Figures as per Finance Accounts

In 2004-05, 2005-06 and 2006-07, actual collections had been higher than the budget estimates by 0.35, 31.73 and 8.98 per cent respectively. In 2006-07 there was a short fall of Rs. 571 crore in actual receipts against the revised budget estimates.

9.3 Outstanding demands *

The number of cases and amount involved in demands for service tax outstanding for adjudication/recovery as on 31 March 2007 are mentioned in the following table:-

Table no. 2

(Amounts in crore of rupees)

Pending decision with	As on 31 March 2006				As on 31 March 2007			
	Number of cases		Amount		Number of cases		Amount	
	More than five years	Less than five years	More than five years	Less than five years	More than five years	Less than five years	More than five years	Less than five years
Adjudicating officers	35	11378	0.01	358.45	74	10478	0.11	709.51
Appellate Commissioners	0	197	0.00	82.46	7	732	0.20	173.50
Board	2	17	0.08	0.91	1	0	0.01	0.00
Government	0	1	0.00	0.06	0	8	0.00	0.81
Tribunals	5	221	1.32	73.49	5	471	0.89	570.33
High Courts	6	48	0.01	5.49	15	87	15.87	30.03
Supreme Court	0	0	0.00	0.00	2	4	0.69	3.65
Pending for coercive recovery measures	2	2552	0.01	53.39	94	5448	45.74	228.70
Total	**50**	**14414**	**1.43**	**574.25**	**198**	**17228**	**63.51**	**1716.53**

***** Figures furnished by the Ministry and relates to 40 commissionerates of central excise and three commissionerates of service tax.

A total of 17,426 cases involving tax of Rs. 1,780.04 crore were pending as on 31 March 2007 with different authorities, of which 61 per cent in terms of number were with the adjudicating officers of the department. Pendency for recovery of demands had increased from 2,554 in 2005-06 to 5,542 cases in 2006-07 i.e. an increase of 116.99 per cent.

9.4 Fraud/presumptive fraud cases *

The position of fraud/presumptive fraud cases alongwith the action taken by the department against defaulting assessees during the period 2004-05 to 2006-07 is depicted in the following table:-

Table no. 3

(Amounts in crore of rupees)

Year	Cases detected		Demand of duty raised	Penalty imposed		Duty collected	Penalty collected	
	Number	Amount	Amount	Number	Amount	Amount	Number	Amount
2004-05	571	142.03	55.64	228	20.62	7.79	128	0.05
2005-06	564	187.21	60.04	41	1.58	59.72	14	0.02
2006-07	616	208.27	95.47	62	16.53	78.50	4	0.02
Total	**1751**	**537.51**	**211.15**	**331**	**38.73**	**146.01**	**146**	**0.09**

***** Figures furnished by the Ministry and relates to 40 commissionerates of central excise and three commissionerates of service tax.

The above data reveals that while a total of 1,751 cases of fraud/presumptive fraud were detected during the years 2004-07 by the department involving tax of Rs. 537.51 crore, it raised demand of Rs. 211.15 crore only and recovered Rs. 146.01 crore (69.15 per cent). Similarly, out of the penalty of Rs. 38.73 crore that was imposed, the department could recover only rupees nine lakh (0.23 per cent).

9.5 Provisional assessments

The number of cases of provisional assessments and the amount involved therein as on 31 March 2006 and 31 March 2007 is exhibited in the following table:-

Table no. 4

(Amounts in crore of rupees)

Pending decision with	As on 31 March 2006		As on 31 March 2007*	
	Number of cases	Duty involved	Number of cases	Duty involved
Court of law	0	0.00	0	0.00
Government of India or Board	0	0.00	0	0.00
Commissioners	1	8.54	0	0.00
Total	**1**	**8.54**	**0**	**0.00**

***** Figures furnished by the Ministry and relates to 40 commissionerates of central excise and three commissionerates of service tax.

9.6 Contents

This section contains 125 paragraphs featured individually or grouped together with a revenue implication of Rs. 79.02 crore directly attributable to audit pointing out non-compliance with rules/regulations. The Ministry/department have accepted (till November 2007) audit observations in 117 paragraphs involving Rs. 65.49 crore and have recovered Rs. 18.19 crore.

9.7 Impact of audit reports

9.7.1 Revenue impact

During the last five years (including the current years' report), audit through its audit reports had pointed out short levy and other deficiencies with revenue impact of Rs. 491.83 crore in 318 audit paragraphs. Of these, the Government had accepted audit observations in 256 audit paragraphs involving Rs. 188.32 crore and had since recovered Rs. 38.60 crore. The details are shown in the following table:-

Table no. 5

(Amounts in crore of rupees)

Year of Audit Report	Paragraphs included		Paragraphs accepted						Recoveries effected					
			Pre printing		Post printing		Total		Pre printing		Post printing		Total	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
2002-03	42	42.21	35	40.43	5	1.16	40	41.59	2	2.04	2	1.79	4	3.83
2003-04	20	17.56	19	17.25	Nil	Nil	19	17.25	2	0.33	5	0.41	7	0.74
2004-05	48	86.57	42	35.59	Nil	Nil	42	35.59	8	5.41	12	2.90	20	8.31
2005-06	83	266.47	38	28.40	--	--	38	28.40	20	7.38	1	0.15	21	7.53
2006-07	125	79.02	117	65.49	--	--	117	65.49	60	18.19	--	--	60	18.19
Grand Total	**318**	**491.83**	**251**	**187.16**	**5**	**1.16**	**256**	**188.32**	**92**	**33.35**	**20**	**5.25**	**112**	**38.60**

9.7.2 Amendment to Act/Rules

During the years 2004 to 2007 (up to March 2007), the Government had amended Act/Rules addressing the concerns raised by audit through audit reports. These changes are shown in the following table:-

Table no. 6

Reference of audit report (AR) paragraph	Related issue raised in audit	Amendment to Act/Rules etc.
Paragraphs 15.6 of AR no. 11 of 2005 and 20.5 of AR no. 7 of 2006	Incorrect/unauthorised adjustment of service tax paid in excess.	Sub- rules (4A) and (4B) of rule 6 of the Service Tax Rules, 1994 had been amended by notification no. 1/2007-ST dated 1 March 2007 which enables the assessees to make adjustment of the amount paid in excess from the amount of service tax liability to be discharged in succeeding month/quarter.
Paragraphs 14.5 of AR no. 11 of 2003 and 15.2 of AR no. 11 of 2005	Service tax collected but not paid to the Government.	Section 87 of the Finance Act, 1994 had been amended by the Finance Act, 2006 providing more comprehensive recovery procedure including coercive recovery mechanism for recovery of tax from person not registered.
Paragraphs 15.2 of AR no. 11 of 2004, 15.3 of AR no. 11 of 2005	Non-levy of service tax on services provided from outside India and received in India.	Section 66A had been inserted under the Finance Act, 1994 by the Finance Act, 2006 making the services taxable if provided from outside India.
Paragraph 12.7.2 of AR no. 11 of 2000	Service tax rate of five per cent fixed under the Finance Act, 1994 had been viewed lower and audit had suggested the rate of twelve per cent.	Service tax rates adopted at eight per cent with effect from 14 May 2003 by the Finance Act, 2003, ten per cent from 10 September 2004 by the Finance Act, 2004 and twelve per cent from 18 April 2006 by the Finance Act, 2006.

CHAPTER X
INCORRECT ASSESSMENT OF SERVICE TAX

Rule 6 of the Service Tax Rules, 1994, prescribes that service tax shall be paid to the credit of the Central Government by the 5th of the month immediately following the calendar month in which the payments for services are received. Further, where the assessee is an individual or proprietary firm or partnership firm, the tax is required to be paid by the 5th of the month immediately following the quarter in which payment for services are received. Where any service tax has not been paid or has been short paid, the person chargeable with service tax, will, in addition to the tax, be liable to pay interest notified under section 75 of the Finance Act, 1994 and penalty prescribed under section 76 of the said Act. A few illustrative cases of non-levy or incorrect assessment of service tax totalling Rs. 50.30 crore noticed in test check, are mentioned in the following paragraphs.

10.1 Service tax not levied on services rendered by indigenous service providers

10.1.1 Consulting engineers

Service tax on consulting engineer's service has been imposed with effect from 7 July 1997. Section 65(31) of the Finance Act, 1994, defines consulting engineers to mean any professionally qualified engineer or an engineering firm who, either directly or indirectly, renders any advice, consultancy or technical assistance in any manner to a client in one or more disciplines of engineering.

10.1.1.1 M/s Mc Nally Bharat Engineering Company Ltd., Dhanbad, in Ranchi commissionerate, engaged in the manufacture of plant, machinery, etc. carried out turnkey project business which involved consultancy services in the field of engineering, electrical, mechanical, drawing and engineering, etc. to its clients. The assessee collected service charges of Rs. 214.28 crore during the period April 2003 to March 2005 but service tax of Rs. 19.60 crore leviable thereon was not paid.

On this being pointed out (June 2006), the department stated (January 2007) that the issue in question was being examined to ascertain and recover the amount of service tax. Reply of the Ministry has not been received (November 2007).

10.1.1.2 M/s Central Electricity Authority, in Delhi commissionerate of service tax, provided consultancy services in design and engineering of power projects to its clients and collected consultancy fee of Rs. 9.63 crore during the period from October 1999 to February 2005. Service tax of Rs. 62.10 lakh leviable on the said consultancy fee was neither collected from the clients nor was it paid to the Government. Assessee also did not obtain registration certificate from the department. Service tax of Rs. 62.10 lakh was recoverable with interest of Rs. 29.04 lakh till March 2007. The department did not take any action to realise the service tax.

On this being pointed out (December 2005), the Ministry accepted the audit observation and stated (October 2007) that show cause notice was being issued.

10.1.2 Port services

Port services were brought under the purview of service tax with effect from 16 July 2001. Port services means any service rendered by a port or other port or any person authorised by such port or other port, in any manner, in relation to a vessel or goods. The Board clarified on 9 July 2001 that wharfage on general cargo and wharfage on petroleum products is includible in the taxable value.

The Oil & Natural Gas Corporation Ltd. (ONGC) laid pipelines for the transportation of crude oil through Mumbai Port Trust area. The ONGC was required to pay compensation at half the rate of wharfage charges of crude oil imported through the said pipeline. The port received Rs. 85.01 crore for the period from April 2001 to March 2007 towards compensation but did not pay service tax which worked out to Rs. 5.70 crore.

On this being pointed out (February 2006), the Ministry admitted the audit observation and stated (July 2007) that show cause notice for Rs. 5.99 crore had been issued and it was under adjudication process.

10.1.3 Production or processing of goods

Services relating to production or processing of goods for or on behalf of a client were brought under the service tax net with effect from 10 September 2004, provided such production or processing did not amount to manufacture within the meaning of section 2(f) of the Central Excise Act, 1944.

10.1.3.1 M/s Ordnance Factory, in Hyderabad I commissionerate, obtained base vehicles of different makes from customers and processed them to make the vehicles bullet/mine proof as per the requirements of police units, ministries, army, navy, para-military and other defence establishments and collected conversion charges of Rs. 32.38 crore from the customers during the period from July 2005 to June 2006. Since the work done did not come within the ambit of manufacture, service tax of Rs. 3.31 crore was leviable thereon. Neither did the department demand service tax on the conversion charges nor did the assessee pay any service tax.

On this being pointed out (October 2006), the Ministry while admitting the audit observation stated (November 2007) that the irregularity was already noticed by the departmental officers in August 2006. It also reported issue of a show cause notice for Rs. 12.24 crore covering the period from 10 September 2004 to June 2006 to the assessee in May 2007 and recovery of tax of Rs. 1.75 crore in February 2007.

The fact remains that the action to recover tax was taken by the department after the irregularity was pointed out in audit.

10.1.3.2 M/s Nicco Corporation Ltd., in Kolkata-III commissionerate, engaged in the manufacture of insulated wires and cables, provided certain services to their customer by using a new technology known as “electron beam irradiation (EBI) technology”. The process undertaken included sterilisation of petri dish, dental powder and medical equipment, colouration of diamond,

irradiation of 'O' ring and similar jobs by using the above EBI technology. Such services related to the processing of goods and were chargeable to service tax. However, service tax of Rs. 39.78 lakh was not paid during the year 2005-06 which was recoverable with interest.

On this being pointed out (July 2006), the Ministry admitted the audit observation and reported (September 2007) the issue of show cause notice for Rs. 54.01 lakh for the period from 10 September 2004 to 31 March 2006.

10.1.4 Goods transport service

A factory registered under the Factories Act or a company established under the Companies Act, which receives the services of an agency providing services in relation to transport of goods by road, is liable to pay service tax with effect from 3 December 2004.

Sixteen manufacturers, in Bolpur (2), Guntur (3), Hyderabad III (1), Hyderabad IV (1), Kolkata III (1), Kolkata V (1), Meerut I (1). II (1), Noida (1), Pune III (3) and Visakhapatnam II (1) commissionerates, availed goods transport services and paid transportation charges to goods transport agencies. Though these manufacturers were registered under the Factories Act or were established under the Companies Act, yet they did not pay service tax of Rs. 1.07 crore payable on the transportation charges paid between January 2005 and October 2006.

On this being pointed out (March and August 2006), the Ministry accepted the audit observations and reported (between September and November 2007) recovery of Rs. 71.54 lakh from fourteen assessees in Bolpur (2), Guntur (3), Hyderabad III (1), Hyderabad V (1), Kolkata III (1), Kolkata V (1), Meerut II (1), Noida (1), and Pune III (3) and issue of show cause notices for Rs. 56.51 lakh to two assessees in Meerut I and Visakhapatnam commissionerates.

10.1.5 Business auxiliary service

Business auxiliary service is chargeable to service tax with effect from 1 July 2003 and includes, inter alia, any service in relation to promotion or marketing or sale of goods produced or provided by or belonging to the client.

The Board clarified on 20 June 2003 that any incidental or auxiliary market support service provided in relation to evaluation of prospective customer, managing distribution, getting a customer, verification of prospective customer, operational assistance for marketing, formulation of customer service and the like would also be covered under the business auxiliary service.

M/s Ford India Private Ltd. and M/s Veljan Hydrair Private Ltd., in Chennai III and Hyderabad I commissionerates respectively, engaged in the manufacture of passenger cars and hydraulic air cylinders also rendered incidental or auxiliary market support service by way of introducing various sales promotion schemes in the market/or provided the services relating to promotion of products in the market. These services rendered by the assessees fell under the category of business auxiliary services. The assessees collected charges of Rs. 5.80 crore during the period March 2003 and March 2006 but service tax of Rs. 56.02 lakh leviable thereon was not paid.

On this being pointed out (between June 2006 and February 2007), the Ministry admitted the audit observation in the case of M/s Veljan Hydrair Private Ltd. and reported (September 2007) recovery of Rs. 40.49 lakh. In the case of M/s Ford India Private Ltd., it stated (October 2007) that the matter was noticed by the internal audit in September 2006 and a show cause notice for Rs. 76.69 lakh was issued on 5 July 2007.

The reply of the Ministry is not tenable as the action to raise demand was taken by the department only after the issue was raised by central excise receipt audit party in February 2007.

10.1.6 Machinery/equipment leasing services

Financial leasing services including equipment leasing and hire purchase fall under 'banking and financial services' and are liable to tax with effect from 16 July 2001.

M/s Ajara SSSK Ltd., in Pune II commissionerate of central excise and M/s Bombay Dyeing and Manufacturing Company Ltd., in Mumbai commissionerate of service tax, provided leasing of plant and machinery, supplementary equipment and other ancillary assets during the years 2003-04 and 2004-05. The assessees received Rs. three crore as hire charges/lease rent but did not pay the service tax of Rs. 27.90 lakh leviable thereon. The department also did not demand it.

On this being pointed out (April 2004 and June 2005), the Ministry while admitting the audit observations, reported (September and November 2007) issue of show cause notices for Rs. 94.56 lakh to both the assessees.

10.1.7 Technical testing and analysis services

Technical testing and analysis services have been brought under the service tax net from 1 July 2003.

M/s Mishra Dhatu Nigam Ltd., in Hyderabad II commissionerate, performed activities of operation and maintenance of aeronautical metallurgical testing laboratory building, equipment and machinery, testing and analysis of components required for the Kaveri Engineering Project etc. These activities were connected with testing and evaluation of aero engine material/components and fell within the ambit of technical testing and analysis services. During the period from 2003-04 to 2005-06, the assessee received Rs. 3.12 crore as cost of services on which service tax of Rs. 29.68 lakh was not paid.

On this being pointed out (January 2006/July 2006), the Ministry admitted the audit observation and reported (July 2007) issue of a show cause notice.

10.2 Non-payment of service tax on services obtained from foreign service providers

By rule 2 (d) (iv) of the Service Tax Rules, 1994 inserted with effect from 16 August 2002, a person receiving taxable services in India has been made liable for payment of service tax on services provided by a person who is a non-resident or is from outside India and does not have any office in India.

10.2.1 Business auxiliary services

Business auxiliary services have been bought under the service tax net with effect from 1 July 2003. Section 65 (19) of the Finance Act, 1994 envisages that "business auxiliary services" means any commercial concern which is engaged in providing any service to any client for promotion or marketing or sale of goods, promotion or marketing of services or any customer care service or any incidental or auxiliary support service such as billing, collection or recovery of cheques, etc.

Twenty nine assessees, in Chandigarh (6), Chennai III (1), Coimbatore (2), Faridabad (2), Gurgaon (3), Hyderabad (1), Indore (1), Jalandhar (1), Kolkata III (1), Kolkata IV (1), Ludhiana (3), Noida (1) and Tirupathi (3) commissionerates of central excise and three in Chennai commissionerate of service tax, entered into agreement with foreign service providers for promotion or marketing of goods, production or processing of goods, procurement of orders or any customer care services, etc. The assessees paid commission amounting to Rs. 41.32 crore to various foreign service providers towards rendering business auxiliary services during the period between July 2003 and March 2007. However, service tax of Rs. 4.28 crore leviable thereon was not paid by the service provider/service receiver which should be recovered with interest and penalty.

On this being pointed out (between February 2006 and May 2007), the Ministry while admitting the audit observations in twenty four cases, reported (between July and November 2007) recovery of Rs. 1.25 crore from ten assessees and issue of show cause notices for Rs. 1.18 crore in nine cases. It further stated that action was being taken to recover the service tax in five cases. Replies in the remaining cases have not been received (November 2007).

10.2.2 Consulting engineer services

In terms of section 65 (31) of the Finance Act, 1994, consulting engineer means any professionally qualified engineer or an engineering firm who either directly or indirectly, renders any advice, consultancy or technical assistance in any manner to a client in one or more disciplines of engineering.

M/s Phoenix Yule Ltd., M/s Ondeo Nalco Ltd., M/s Landis and Gyr Ltd., M/s Moser Baer Ltd. and M/s Pricol Ltd. in Kolkata III, IV, V, Noida and Salem commissionerates respectively engaged in the manufacture of excisable goods, received technical consultancy, technical know how, technical assistance, etc. from foreign consultants and paid service charges aggregating Rs. 29.95 crore between 16 August 2002 and 31 December 2005. However, service tax of Rs. 1.45 crore leviable thereon was neither paid by the foreign service provider nor by the recipient of services.

On this being pointed out (between July 2005 and November 2006), the Ministry admitted the audit observations and reported (between July and December 2007) that show cause notices for Rs. 1.51 crore had been issued or were being issued to the assessees in Kolkata IV, V, Noida and Salem commissionerates and recovery of tax of Rs. 73,125 from M/s Phoenix Yule Ltd.

10.2.3 Intellectual property right services

Intellectual property right services involving transfer of right to use intangible property were brought under the ambit of service tax with effect from 10 September 2004. The term 'intangible property' means trade marks, designs, patents or any other similar intangible property under any law for the time being in force and includes the right to use technical know-how belonging to another person.

Two assessees in Bangalore and Chennai commissionerates of service tax, two in Hyderabad I and one each in Cochin, Kolkata III, IV, Meerut I and Pondicherry commissionerates of central excise, engaged in the manufacture of various excisable products acquired technical know-how/technology, trade marks, etc. from different foreign companies. The assessees paid royalty aggregating to Rs. 22.17 crore during the period between 10 September 2004 and 31 March 2006 to the foreign companies but did not discharge service tax liability of Rs. 1.43 crore.

On this being pointed out (between November 2005 and May 2007), the Ministry admitted the audit observations and reported (between July and October 2007) recovery of tax of Rs. 1.36 crore from seven assessees. Report on the recovery of tax from assessees in Kolkata III and Meerut I commissionerates has not been received (November 2007).

10.2.4 Online information service

Online information and database access or retrieval service through computer network was brought into the ambit of service tax from 16 July 2001. Section 65(75) of the Finance act, 1994, defines the "online information and database access or retrieval" to mean any service provided to a customer by a commercial concern, in relation to online information and database access or retrieval or both in electronic form through computer network.

M/s Bosch Rexroth (India) Ltd. and M/s Flakt (India) Ltd., in Ahmedabad and Kolkata commissionerates of service tax and M/s Aventis Pharma Ltd., in Surat II commissionerate of central excise, availed online information services, mailing services, etc through computer network from foreign companies. They paid Rs. 4.41 crore during the period between November 2002 and December 2005 to the service providers in foreign currency. However, service tax of Rs. 35.64 lakh payable thereon was neither paid by the service provider nor service receiver. The department also did not demand it.

On this being pointed out (August and September 2005), the Ministry while accepting the audit observations, reported (November 2007) that service tax of Rs. 1.23 lakh with interest of Rs. 27,269 had been recovered from M/s Bosch Rexroth (India) Ltd. and two show cause notices demanding service tax of Rs. 40.98 lakh had been issued to M/s Flakt (India) Ltd. and M/s Aventis Pharma Ltd.

10.2.5 Scientific and technical consultancy service

Scientific and technical consultancy services were brought under the ambit of service tax with effect from 16 July 2001. Section 65 of the Finance Act, 1994 defines scientific and technical consultancy as any advice, consultancy

or scientific or technical assistance rendered in any manner either directly or indirectly by a scientist or a technocrat or any science or technology institution or organisation to a client in one or more disciplines of science or technology.

M/s Bharat Electronics Ltd. (BEL), in Hyderabad III commissionerate, engaged in the manufacture of electronic systems, paid (between November 2002 and September 2005) Rs. 2.15 crore to M/s Elta Electronics Industries Ltd., Israel for providing of technical know-how/technical information, practical application of the state-of-the-art, industrial techniques relating to manufacture, documentation of data, technical and manufacturing assistance in India, training of BEL personnel besides granting exclusive patent rights for five years to the assessee for manufacture and sale of products in India. Though the services fell within the ambit of scientific and technical consultancy services, service tax of Rs. 20.34 lakh was not paid which was recoverable with interest.

On this being pointed out (July 2006), the Ministry stated (December 2007) that providing technical know-how, technical information, training licence to sell licenced products, etc. did not constitute an agreement for scientific or technical consultancy. It also stated that a show cause notice demanding tax of Rs. 20.33 lakh had been issued to the assessee in November 2007.

The reply of the Ministry is not tenable as the definition of scientific and technical consultancy services encompasses all the activities mentioned in the agreement. The CESTAT in the case of M/s MRF Ltd. has also held {(2005 (179) ELT 472)} that the aforementioned activities fell within the scope of scientific and technical consultancy services.

10.3 Incorrect grant of exemption of service tax

By a notification dated 3 December 2004, seventy five per cent value of the taxable service provided by a goods transport agency (GTA) to a customer is exempt from the levy of service tax, subject to the conditions that cenvat credit on inputs or capital goods used for providing such taxable service is not taken and exemption under notification dated 20 June 2003 is not availed of by the GTA.

The Board clarified on 27 July 2005 that the person availing of exemption under the notification dated 3 December 2004, will have to obtain a declaration from the GTA on the consignment note to the effect that the conditions of the aforesaid notification have been satisfied. The Board again examined the issue in consultation with the Ministry of Law and issued order on 12 March 2007 under section 37B reiterating that earlier instructions of 27 July 2005 must be followed.

10.3.1 Twelve assessees, in Vadodara II, Surat I, Vapi, Daman, Rajkot and Ahmedabad III commissionerates, engaged in the manufacture of various excisable goods, availed of the services of GTA. These assessees paid service tax after availing of exemption of seventy five per cent on the gross freight charges paid to the GTA during the period between January 2005 and March 2006. The declarations as required under the Board's instructions cited above for satisfying the conditions of the notifications, were not obtained in any of the consignment notes issued by the GTA. Exemption of service tax

amounting to Rs. 2.42 crore availed of by the assessees was, therefore, incorrect.

On this being pointed out (between March 2006 and January 2007), the department admitted the audit observations in two cases and intimated (September 2006) recovery of tax of Rs. 4.62 lakh in a case. In the other two cases, it stated (April and May 2007) that show cause notices for Rs. 25.43 lakh were being issued. In two cases relating to Vapi commissionerate, it contended that the exemption availed of was correct as the assessees had declared that credit had not been availed. The reply is not tenable as declaration was required to be given on each consignment note by the GTA in terms of notification dated 3 December 2004 read with Board's clarification dated 27 July 2005 and hence exemption availed of was not correct. Reply of the Ministry has not been received (November 2007).

10.3.2 Notification dated 16 December 2002, exempts taxable services provided by a consulting engineer to a client on the transfer of technology from so much of the service tax leviable thereon which is equivalent to the amount of cess paid on the said transfer of technology under the Research and Development Cess Act, 1986.

M/s J.C.B. India Ltd., Ballabhgarh, in Faridabad commissionerate, paid Rs. 6.17 crore to a foreign service provider for the services provided for transfer of technology between July 2004 and April 2005. The assessee paid cess under Research and Development Cess Act but did not pay service tax of Rs. 31.36 lakh which was leviable thereon after deducting the amount of cess already paid.

On this being pointed out (August 2005), the Ministry admitted the audit observation and intimated (September 2007) that show cause notice was being issued.

10.4 Short payment of service tax due to undervaluation

Section 67 of the Finance Act, 1994, envisages that the value of any taxable service shall be the gross amount charged by the service provider.

10.4.1 M/s Hwashin Automotive India Private Ltd. and M/s Hanil Lear India Ltd., in Chennai commissionerate of service tax and M/s TVS Motor Company in Chennai III commissionerate of central excise, engaged in the manufacture of motor cycles, automobile components, etc. received consulting engineer services or technical consultancy services from foreign service providers and paid Rs. 67.79 crore to them. The assessees paid service tax at the applicable rates on the value of services after excluding the amount of tax deducted at source from the value of services which was not correct. Incorrect adoption of value, resulted in short payment of service tax of Rs. 1.16 crore between January 2004 and March 2006.

On this being pointed out (between December 2006 and March 2007), the Ministry while accepting the audit observations intimated (September 2007) that the demand of Rs. 13.06 lakh has been confirmed against M/s Hanil Lear India Ltd. and show cause notices to the other two assessees are issued or are under process of issue.

10.4.2 Another assessee viz., M/s Decisioncraft Analytics Ltd., in Ahmedabad commissionerate of service tax, engaged in providing management consultancy services, declared gross receipt of Rs. 1.39 crore for the years 2001-02 to 2003-04 and paid service tax accordingly. Verification of records revealed that the gross receipts for that period was in fact Rs. 2.50 crore which was also declared by the asssessee in the income tax returns for the years 2001-02 to 2003-04. Incorrect declaration of value of services, resulted in service tax of Rs. 9.05 lakh being paid short. This was recoverable with interest of Rs. 3.02 lakh.

On this being pointed out (August 2005), the Ministry accepted the audit observation and stated (October 2007) that the demand of Rs. 6.03 lakh had been confirmed in September 2006 but the Commissioner (Appeals) had remanded the case for de novo adjudication. Further developments in the case have not been received (November 2007).

10.5 Loss of revenue due to non-issue of demand notice

Short payment or non-payment of service tax is to be recovered by issuing show cause notice under section 73 of the Finance Act, 1994 within a period of one year in normal cases. In case of short levy/non-levy due to fraud, collusion, etc. limitation of this period stands extended to five years.

M/s Tamilnadu Ex-Servicemen's Corporation, in Chennai commissionerate of service tax, provided security service to various clients. The assessee realised service charges from the clients but did not pay service tax of Rs. 73.96 lakh for the period from 16 October 1998 to 31 March 2000. While the department demanded service tax from 1 April 2000 onwards which was also paid by the assessee, it did not demand service tax for the earlier period. This resulted in loss of revenue of Rs. 73.96 lakh to the Government.

On this being pointed out (January 2007), the Ministry accepted the audit observation and stated (October 2007) that the chief commissioner had been directed to fix responsibility for not issuing the demand notice in time.

10.6 Non-recovery of service tax from goods transport operators

By a notification dated 5 November 1997 effective from 16 November 1997, the recipient of the services of goods transport operators was made liable to pay service tax at the rate of five per cent of the freight charges paid to goods transport operators. The Supreme Court in the case of Laghu Udyog Bharti {1999 (112) ELT 365} held that the recipients of services cannot be made liable to pay service tax and the rules in this regard were ultravires of the Finance Act, 1994. In order to validate the recovery of service tax from the recipients, the Finance Act, 1994 was amended with retrospective effect vide section 117 of the Finance Act, 2000.

By the Finance Act, 2003, a new section 71A was introduced requiring service receiver/user of transport operator to file return for the relevant period (i.e. 16 November 1997 to 1 June 1998) within six months from 14 May 2003.

Six assessees, in Vadodara II, Bhavnagar and Daman commissionerates of central excise and one in Ahmedabad commissionerate of service tax, availed of services of goods transport operators during the period from 16 November 1997 to 2 June 1998 but did not pay service tax of Rs. 38.47 lakh on the freight charges of Rs. 7.69 crore paid to the service providers. The assessees also did not submit returns as required under the Finance Act, 2003. The department also did not take any action to recover the service tax with applicable interest.

On this being pointed out (between March 2005 and January 2006), the Ministry accepted the audit observation and stated (October 2007) that show cause notices had been issued to all assessees.

10.7 Incorrect issue of show cause notice

Intellectual property services have been brought under the service tax net with effect from 10 September 2004. Section 65(55a) of the Finance Act, 1994, defines 'intellectual property' to mean any right to intangible property, trade mark, design, patents or any other similar intangible property under any law for the time being in force, but does not include copyright.

CESTAT in the case of M/s Araco Corporation, Bangalore held that transferring of technical know-how in terms of licence, fell within the category of intellectual property services {2005 (180) ELT 91 (Tri – Bang)}.

M/s Inductotherm (India) Private Ltd., in Ahmedabad commissionerate of service tax, engaged in the manufacture of furnaces of different capacities, paid royalty of Rs. 4.60 crore to Inductotherm Industries Inc. USA during 1 October 2004 to 30 September 2005 for providing technical know-how and transfer of technology. Though this service fell under the definition of intellectual property service, the department issued a show cause notice on 2 August 2005 demanding service tax of Rs. 20.17 lakh for the period from 1 April 2004 to 31 March 2005 under the head 'consulting engineer services' which was incorrect and was not maintainable. The service receiver was liable to pay service tax of Rs. 23.45 lakh under intellectual property services.

On this being pointed out (December 2005), the Ministry accepted the audit observation and stated (October 2007) that the demand of Rs. 23.45 lakh had been confirmed under intellectual property service, and intimated that the assessee had filed an appeal against the demand before the Commissioner (Appeals) which was pending.

10.8 Other cases

In 147 other cases of incorrect assessment of service tax, the Ministry/department have accepted the audit observations involving duty of Rs. 5.08 crore and have reported recovery of Rs. 3.23 crore in 130 cases till November 2007.

CHAPTER XI
GRANT OF CENVAT CREDIT

Cenvat credit of service tax paid on specified input services is admissible with effect from 10 September 2004. Credit availed can be utilised for payment of central excise duty on finished goods or service tax payable on output services subject to fulfilment of certain conditions. A few cases of incorrect grant of cenvat credit involving tax of Rs. 28.72 crore, noticed in test audit are described in the following paragraphs.

11.1 Utilisation of cenvat credit in excess of the admissible limit

Rule 3 of the Cenvat Credit Rules, 2004 allows that a provider of taxable service to take the credit of specified duties and service tax paid on any input goods, input services or capital goods received in the premises of the provider of output service on or after 10th day of September 2004. Further, rule 6(3) of the Cenvat Credit Rules provides that where a provider of output service avails of cenvat credit in respect of any inputs or input services and provides output services which are chargeable to tax as well as exempt, and does not maintain separate accounts in respect of both category of services, then the provider of output service will utilise credit only to the extent of an amount not exceeding twenty per cent of the service tax payable on the output service.

11.1.1 M/s Bharti Hexacom Ltd., in Jaipur I commissionerate, engaged in providing both taxable and exempted cellular phone services availed of cenvat credit on inputs, input services and capital goods. While utilising credit, the assessee restricted utilisation of cenvat credit availed on inputs and input services only. Cenvat credit availed of on capital goods was utilised without any restriction. This was irregular in terms of the provisions cited. This resulted in excess utilisation of cenvat credit of Rs. 12.21 crore during the year 2005-06 which was required to be recovered.

On this being pointed out (August 2006), the Ministry stated (September 2007) that rule 6 imposed restriction for availing and utilisation of cenvat credit on inputs and input services only and not on capital goods. The reply is not tenable as rule 6(3)(c) of the Rules restricts utilisation of credit upto 20 per cent of the amount of service tax payable on output service. This means that the remaining eighty per cent of tax is to be paid from PLA or in cash. Further, the Ministry's reply in this paragraph contradicts its reply given in paragraph 11.1.2 of this report where it has admitted a similar audit observation.

11.1.2 M/s Mahindra Steel Service Centre Ltd., M/s Bharat Sanchar Nigam Ltd. (BSNL), Kollam and M/s NCS Industries Ltd., in Pune I, Thiruvananthapuram and Visakhapatnam II commissionerates respectively, engaged in providing of taxable as well as exempted services, had availed of credit on common input services. The assessees did not maintain separate accounts for taxable and non-taxable services. The credit was, therefore, required to be utilised to the extent of 20 per cent of service tax payable on output service. However, the assessees utilised input service credit without

applying the aforesaid restriction. This resulted in excess utilisation of credit of Rs. 1.20 crore during the period between March 2005 and December 2006.

On this being pointed out (between December 2005 and March 2007), the Ministry admitted the audit observation and intimated (September and October 2007) that while credit of Rs. 31.50 lakh and interest of Rs. 3.31 lakh had been recovered from the first assessee, demand of Rs. 86.80 lakh had been confirmed against the second assessee and show cause notice had been issued for Rs. 14.95 lakh to the third assessee.

11.2 Cenvat credit availed of in excess on capital goods

Rule 4 of the Cenvat Credit Rules, 2004, provides that credit in respect of capital goods received in the premises of the provider of output service at any time in a given financial year, will be taken only for an amount not exceeding fifty per cent of the duty paid on such capital goods in the same financial year. Rule 14, of the same- Rules provides that where the cenvat credit has been taken or utilised wrongly, it will be recovered with applicable interest.

M/s Bharat Sanchar Nigam Ltd., in Thiruvanathapuram commissionerate, engaged in providing cellular phone service, procured capital goods in July and August 2005. The assessee availed of the full credit of Rs. 6.40 crore as against the admissible credit of Rs. 3.20 crore (i.e 50 per cent of the duty paid during the year 2005-06). The excess credit of Rs. 3.20 crore availed of was recoverable with interest.

On this being pointed out (July 2006), the Ministry admitted the audit observation and stated (November 2007) that a show cause notice has been issued which is pending.

11.3 Incorrect utilisation of cenvat credit for payment of service tax on input services

Credit availed of under the Cenvat Credit Rules can be utilised for payment of central excise duty on finished goods or for service tax leviable on output service. There is no provision for its utilisation for payment of service tax on any input service. Wrong utilisation of cenvat credit is recoverable with interest.

Thirty four assessees, in thirteen commissionerates, availed of cenvat credit and utilised it for payment of service tax leviable on services obtained from goods transport agencies or on intellectual property right services. As the assessees were not providing output services, the utilisation of cenvat credit for payment of service tax on input services was not correct. The assessees ought to have paid the service tax relating to the said services through cash only. The credit incorrectly utilised for payment of service tax amounted to Rs. 3.08 crore between September 2004 and March 2007, which was recoverable with interest.

On this being pointed out (between September 2005 and April 2007), the Ministry while accepting the audit observations reported (between July and November 2007) recovery of Rs. 1.30 crore in twelve cases. Report on

recovery of tax in the remaining cases has not been received (November 2007).

11.4 Availing and utilisation of non-permissible cenvat credit

Under the provisions of rule 3 of the Cenvat Credit Rules, 2004, a manufacturer is allowed to take credit of service tax paid on any 'input service' used in the manufacture of final goods. Service tax paid by the manufacturer for outward transportation of final products beyond the place of removal is not an 'input service' and credit of tax paid on such services is not admissible in terms of explanation 2(l) below rule 2(K) of the Rules mentioned above.

11.4.1 M/s Godrej & Boyce Manufacturing Company Ltd. and M/s Hyva India Private Ltd., in Mumbai commissionerate of service tax, availed credit of Rs. 2.69 crore representing service tax paid on outward transport services beyond the place of removal during the period between January 2005 and March 2007. As the credit was admissible for outward transport upto the place of removal only, the credit availed of was not correct and was recoverable with interest.

On this being pointed out (August 2006 and April 2007), the Ministry while accepting the audit observations reported (November 2007) that the tax of Rs. 31.59 lakh had been paid by one assessee and show cause notice for Rs. 2.37 crore had been issued to the other assessee.

11.4.2 Fifteen units in Bolpur (2), Haldia (2) Hyderabad I (1), Kolkatta III (2), Ludhiana (1), Pune III (1), Salem (1), Surat II (1), Thane II (1), Trichirapalli (1), Vapi (2) commissionerates of central excise and one in Kolkatta commissionerate of service tax, engaged in the manufacture of various excisable goods, availed of credit of service tax paid on freight for outward transportation of finished goods by road from factory/depot to the buyer's premises. Since credit of service tax paid on such services was not permissible to the manufacturers, credit of Rs. 5.16 crore availed of during the period between the years 2004-05 and 2006-07 was incorrect and was recoverable with interest.

On this being pointed out (between February 2006 and June 2007), the Ministry while admitting the audit observations, intimated (between July and December 2007) that tax of Rs. 72.25 lakh had been recovered from three assessees in Kolkatta III, Ludhiana and Surat II commissionerates and demands totalling Rs. 11.78 lakh had been confirmed against the assessees in Pune III and Trichirapalli commissionerates. It also intimated that show cause notices for tax of Rs. 9.91 crore had been issued or were being issued to the remaining eleven assessees.

11.5 Incorrect utilisation of service tax credit on ineligible services

Rule 3 of the Cenvat Credit Rules, 2004, allows the manufacturer or producer of final products to take credit of service tax paid on any input service received by him, if such service is used in the manufacture of final products.

M/s Hindustan Petroleum Corporation Ltd., M/s Rashtriya Ispat Nigam Ltd. and M/s GMR Industries Ltd., in Visakhapatnam I commissionerate, engaged in the manufacture of various excisable goods, availed of cenvat credit of service tax of Rs. 49.97 lakh during the period between April 2005 and December 2006 on services not used in the manufacture of final products. The first assessee obtained health insurance policies during 2005-06 for the benefit/welfare of the employees of the company. The second assessee had hired a number of private cabs on a regular basis for meeting their day to day administrative requirements in connection with transportation of their own officials as well as outside personnel visiting the plant. The third assessee had obtained financial advisory services of a bank for disposal of company's shareholding. The service tax totalling Rs. 49.97 lakh paid by them was availed of as cenvat credit and utilised for payment of duty on final products. Since service so received did not have any nexus with the manufacturing activity, it fell outside the scope of input service. Accordingly, credit of Rs. 49.97 lakh was recoverable with interest.

On this being pointed out (November 2006 and February 2007), the Ministry while accepting the audit observations reported (October and November 2007) that the show cause notice has been issued to an assessee and it was under issue to other two assessees.

11.6 Credit availed of wrongly on services received prior to 10 September 2004

Rule 3(iv) of the Cenvat Credit Rules, 2004, allows taking of credit of input service by the manufacturer of final product or by the provider of output services on or after 10 September 2004.

M/s IBP Company Ltd., M/s Smita Steel Ltd. and M/s Elecon Engineering Ltd. in Nasik, Thane I and Vadodara I commissionerates of central excise respectively, availed of cenvat credit of Rs. 20.91 lakh relating to services which were received prior to 10 September 2004. This was not correct and the credit availed of was recoverable with interest.

On this being pointed out (between December 2005 and April 2007), the Ministry admitted the audit observation and intimated (October 2007) that Rs. 20.40 lakh had been recovered and efforts were being made for recovery of the remaining amount with interest.

11.7 Other cases

In five other cases of incorrect use of cenvat credit, the Ministry/department have accepted the audit observations involving tax of Rs. 47.13 lakh and reported recovery of Rs. 13.19 lakh in two cases till November 2007.