

OVERVIEW

This report is presented in three sections: -

Section 1	Chapters I and II	Customs
Section 2	Chapters III and IV	Central Excise
Section 3	Chapter V	Service Tax

SECTION 1 - CUSTOMS

This section contains two reviews as under: -

1. Hundred percent export oriented units (EOUs)

Total duty foregone during the period 1997-98 to 2004-05 on EOU Scheme was Rs.37,384 crore. Audit review has identified a few critical risks, which if not mitigated could impact adversely in achieving the mandated goals and objectives of EOUs. Nine constructive and implementable recommendations have been given to remedy the systemic weaknesses noticed by audit. If implemented, these would mitigate the risk of similar irregularities in future. The Ministry of Finance was in agreement (till January 2007) with three recommendations and specific replies to the remaining six recommendations were awaited. The total additional revenue which could come to the Government as a result of this audit intervention (review) is Rs.1,125.29 crore. Some of the major findings and related recommendations are abstracted below:-

➤ Macro data regarding total number of EOUs approved, those functional, duty foregone etc. was inconsistent, incomplete and unreliable. As a result, there was minimal assurance that the units were monitored by the departments to ensure that these met the objectives of their formation and functioned within the existing norms and regulations. There was a need to re-verify/reconcile the number of units approved, functional/closed and that de-bonded as a first step to effectively monitor functioning of these units, so that timely and effective action could be taken for effecting recoveries, wherever due.

(Paragraph 1.6)

➤ Duty amounting to Rs.285.81 crore was not levied/short levied on imports effected, in violation of applicable conditions. As duty free irregular imports made by EOU's are a huge drain on the Government revenue, there is an urgent need to put in place a workable co-ordinated mechanism between Commerce and Finance Ministries, to detect such lapses and recover duty in time.

(Paragraph 1.7)

➤ The department did not recover duty of Rs.284.72 crore and interest of Rs.289.24 crore from 47 EOUs that failed to achieve their prescribed EO/net foreign exchange earning as a percentage of exports (NFEP). There is a need for Ministries of Commerce and Finance to strengthen their internal control mechanism and coordination to monitor that the EOUs achieve their prescribed value addition (VA)/EO, failing which the duty forgone along with interest and penalty leviable should be recovered promptly.

(Paragraph 1.9)

➤ Duty amounting to Rs.84.37 crore was recoverable as 76 EOUs had effected irregular/excess domestic tariff area (DTA) sales, in contravention of Exim Policy/notifications. As EOUs are intended primarily for exports, any DTA sale should only be permissible after the unit has achieved minimum prescribed EO/EP/NFEP etc. Government should strengthen its control mechanism to ensure that DTA sales are effected only after achievement of EO. In audit opinion, use of duty free imports and other concessions in production and diverting the output products in DTA unauthorisedly, is a major risk which needs to be mitigated effectively.

(Paragraph 1.10)

➤ Central sales tax (CST) and drawback amounting to Rs.78.57 crore on DTA sales made by 95 EOUs was reimbursed irregularly, in violation of the Exim Policy and the Handbook of procedures (HBP) Volume-1. There is a need to amend Exim Policy to restrict reimbursement of CST/drawback correctly to duties relating to exported goods only and not for goods sold in DTA.

(Paragraph 1.13)

➤ There was variance between export performance figures as recorded by Revenue Department (Customs) and Development Commissioners (DCs) in Ministry of Commerce. Infact, the performance {free on board (FOB) value of exports} was inflated/over stated in records of DCs which formed the very basis of their evaluation by the DCs. Accordingly, the risk of incorrect decisions based on inflated export performance was left unmitigated. In audit opinion, Government should ensure that export performance evaluation of EOUs is done only on the basis of Customs records and not annual/quarterly performance reports (APRs/QPRs) submitted by the EOUs, as ports are the point of exit of exported goods.

(Paragraph 1.20)

2. Adjudication and appeal cases

The review of adjudication and appeal cases revealed several instances of abnormal delays, non adjudication, lapses, inadequate response and monitoring leading to loss as well as risk to revenue. Audit has given nine implementable recommendations, which

would lead to substantive reduction in pendency and safeguarding of Government revenue apart from addressing systemic weaknesses and mitigating the associated risks. The Ministry of Finance had till January 2007 accepted eight of these recommendations. Final reply on the remaining one recommendation, in consultation with Ministry of Commerce, had not been received. Some of the major findings and recommendations are abstracted below:-

➤ The data provided/maintained by the department regarding adjudication cases and revenue involved therein was incomplete, inconsistent, inaccurate, un-reconciled and hence unreliable. In the absence of accurate data regarding the numbers and revenue involved, the assurance that the Board is monitoring these cases effectively is minimal. The Board, as a first step, should verify and reconcile the number and amount involved in pending SCNs to effectively monitor the disposal of these cases.

(Paragraph 2.5)

➤ Cases pending adjudication increased by 89 per cent as on 31 March 2005 compared to 1 April 2002 when a time limit of six months/one year for completing adjudication was brought in. During 2002-03 to 2004-05, only 24 to 57 percent cases were finalised within six month or one year. Government may consider reviewing the time limit of six months/one year for disposing SCNs and fix a realistic time frame. Recording and/or justifying reasons for going beyond prescribed time limit and obtaining orders from superior authorities to do so, should be made mandatory.

(Paragraph 2.5)

➤ Revenue of Rs.448.67 crore was locked up in 1,173 pending adjudication cases for period ranging between one to 46 years. Of these, 17 cases each having revenue implication of Rupees one crore and above were awaiting adjudication from two to eight years. Board should issue instructions to its field formations to take old cases involving substantial revenue for priority adjudication.

(Paragraph 2.6.1)

➤ Files in 165 cases involving demand of duty of Rs.26.48 crore apart from interest and penalty of Rs.89.81 lakh were reported missing in four commissionerates. Board should investigate the reasons for which these files went missing and based on the result of probe, fix responsibility and initiate appropriate action.

(Paragraph 2.6.2)

➤ Appeals filed by the department in 33 cases were either dismissed on grounds of delay or the department could not stake its claim owing to belated action/non submission of proper evidence, leading to non realisation/loss of revenue of Rs.160.38 crore.

(Paragraph 2.7.2)

- In ten cases, department failed to initiate recovery action in spite of non compliance of pre-deposit orders of the Courts/dismissal of appeals, leading to non realisation of revenue of Rs.23.33 crore, even after delay of eight months to nine years. Further, confirmed demands of Rs.240.59 crore were pending realisation as on 31 December 2005 in 1,467 cases. Government should consider fixing time limit for paying duty on confirmation of demand, beyond which coercive action should be initiated.

(Paragraphs 2.8.1 and 2.8)

SECTION 2 - CENTRAL EXCISE

This section contains two reviews as under: -

3. Review on provisional assessment

The review has identified certain compliance issues like non-determination of differential duty in large number of cases and non-finalisation of provisional assessment cases within the prescribed time limit. Ten constructive and implementable recommendations have been given to remedy the systemic weaknesses identified by audit. Of these, nine recommendations have been accepted by the Ministry. Some of the major findings and related recommendations are abstracted below: -

- In 2087 pending provisional assessment cases, the differential duty was not quantified. The adequacy and sufficiency of the amount of bond/security required to be obtained in these cases could not, therefore, be evaluated in audit. There was a need to ensure that the differential duty was worked out as per the standard methods prescribed in 'provisional assessment monitoring system' and the amount of bond/security was obtained/reviewed from time to time as per the estimated differential duty to safeguard the revenue.

(Paragraphs 3.5, 3.9 and 3.10.6.1)

- In spite of incorporation of normal time limit of six months in the Rules, 2260 provisional assessment cases were pending for more than six months and upto 25 years. There is, therefore, urgent need for fixation of realistic time limit without the provisions for extension, for recovering differential duty in time.

(Paragraph 3.6)

- Revenue of Rs.133.23 crore was at risk for want of administrative action in three provisional assessment cases, which were not finalised. The Board should issue suitable instructions for finalisation of provisional assessment cases involving substantial amount, on a priority basis.

(Paragraph 3.8)

- In 171 provisional assessment cases, deficiency in bond value and bank guarantee was Rs.819.80 crore and Rs.212.29 crore respectively. In addition there was undue financial benefit derived by the assesses as they could save Rs.16.05 crore by way of bank commission. There is a need to strengthen internal control mechanism so as to ensure that bonds/bank guarantees of appropriate amount are obtained and the amount of bonds/bank guarantees so obtained are reviewed periodically to keep pace with the increase in estimated differential amount of duty.

(Paragraph 3.9)

4. Review on excise duty on plastic and articles thereof

A review of 235 units manufacturing plastic and articles has revealed excessive availment of cenvat credit by this sector, few compliance issues and inadequate controls. Two constructive and implementable recommendations have been given to remedy the weaknesses noticed by audit. The total additional revenue which could come to the government as a result of this audit intervention (review) is Rs.18.24 crore. Some of the major findings and related recommendations are abstracted below: -

- The percentage of Cenvat to duty paid in cash was exceptionally high in plastic industry. The Government should ascertain the exact reasons and plug the loopholes to avoid possible misuse of Cenvat by plastic sector.

(Paragraph 4.5)

- Undervaluation of goods consumed captively resulted in revenue loss of Rs.64.88 lakh.

(Paragraph 4.7.3)

- Irregular availment of Cenvat credit resulted in revenue loss of Rs.9.07 crore.

(Paragraph 4.8)

- Non-payment of service tax on the services rendered by foreign consultants resulted in revenue loss of Rs.2.98 crore. Non-payment of service tax on various services rendered by manufacturers of plastic and articles thereof, resulted in revenue loss of Rs.1.24 crore. There is a need for making necessary changes in the format of excise assessment returns to include information relating to taxable services to prevent escapement of service tax by manufacturers.

(Paragraphs 4.9.1 to 4.9.6)

SECTION 3 - SERVICE TAX

This section contains a review as under: -

5. Review on service tax on management consultant's services, scientific or technical consultancy services, technical testing and analysis services & technical inspection and certification services

Audit review has highlighted ineffective and inadequate efforts to increase the tax base in addition to certain compliance issues and inadequate internal controls. Seven constructive and implementable recommendations have been given to remedy the systemic weaknesses noticed by audit. Of these, six recommendations have been accepted by the Ministry. The total additional revenue which could come to the Government as a result of this audit intervention (review) is Rs.216.92 crore. Some of the major findings and related recommendations are abstracted below: -

➤ Measures taken by the department to bring unregistered service providers into tax net were ineffective and inadequate. Audit identified 777 unregistered service providers with estimated loss of revenue of Rs.86.96 crore. Penalty of Rs.86.96 crore and interest of Rs.15.12 crore was also leviable. The Board should establish Key Performance Indicators (KPIs) for commissionerates, to enable the Board to monitor and evaluate their performances in an effective and scientific manner. The procedure for conducting survey needs to be streamlined so that these are conducted after collection, collation and risk analysis of information gathered.

(Paragraphs 5.6.1, 5.6.2 and 5.6.3)

➤ Service tax of Rs.6.12 crore was evaded by 105 registered service providers during the period when they did not file returns. Penalty and interest amounting to Rs.8.09 crore was also leviable. There is a need to devise an appropriate and effective mechanism to detect 'stop filers' in time and prevent them from evading service tax.

(Paragraphs 5.7 and 5.7.1)

➤ Scrutiny of returns was ineffective and policy for scrutinising these was ambiguous. There is a need to adopt risk based selection of returns for detailed scrutiny.

(Paragraph 5.7.2)

➤ Service tax of Rs.5.66 crore was short paid by the 116 registered service providers on account of suppression of taxable value. Penalty and interest amounting to Rs.7.05 crore was also leviable. There is a need for an effective mechanism to check the returns as also making it mandatory for service providers to submit income tax returns and annual financial statement alongwith ST returns to mitigate the risk of undervaluation and resultant evasion of tax.

(Paragraph 5.7.3)

- **Provisions to finalise SCNs within a timeframe do not exist for service tax, unlike central excise duties. There is a need for the Government to prescribe timeframe for adjudication of SCNs relating to service tax.**

(Paragraph 5.8)