

**CHAPTER V : REVIEW ON SERVICE TAX ON MANAGEMENT CONSULTANT'S SERVICES, SCIENTIFIC OR TECHNICAL CONSULTANCY SERVICES, TECHNICAL TESTING AND ANALYSIS SERVICES & TECHNICAL INSPECTION AND CERTIFICATION SERVICES**

A review in 64 commissionerates was conducted in audit, to evaluate whether service tax administration related to selected services, was effective in identifying and bringing into tax net potential assesseees and was efficient in ensuring regular and correct payment of service tax by registered service providers. Audit review has identified a few unregistered service providers escaping from service tax. Audit has also noticed non-payment/short-payment of service tax by a few registered service providers. 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 are abstracted below: -

**5.1 Highlights**

➤ **Measures taken by the department to bring unregistered service providers into tax net were ineffective and inadequate. Audit identified 777 unregistered service providers in these four services 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.**

(Paragraphs 5.6.1, 5.6.2 and 5.6.3)

➤ **Around twenty two per cent of returns due were not submitted by the registered service providers in these four services, for which no action was initiated by department. 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.**

(Paragraphs 5.7 and 5.7.1)

➤ **Scrutiny of returns was ineffective and policy for scrutinising these was ambiguous.**

(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.**

(Paragraph 5.7.3)

➤ **Provisions to finalise SCNs within a timeframe do not exist for service tax, unlike central excise duties.**

(Paragraph 5.8)

## **5.2 Introduction**

Service tax on the services of '**management consultant's**' (MGC) was levied with effect from 16 October 1998. Section 65(65) of the Finance Act, 1994, defines management consultant as 'any person who is engaged in providing any service either directly or indirectly, in connection with the management of any organisation in any manner and includes any person who renders any advice, consultancy or technical assistance relating to conceptualising, devising, development, modification, rectification or upgradation of any working system of any organisation'.

Service tax on the services of '**scientific or technical consultancy**' (STC) was levied with effect from 16 July 2001. Section 65(92) of the Finance Act, 1994, defines scientific or 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 and technology'.

Service tax on the services of '**technical testing and analysis**' (TTA) was levied with effect from 1 July 2003. Section 65(106) of the Finance Act, 1994, defines technical testing and analysis as 'any service in relation to physical, chemical, biological or any other scientific testing or analysis of goods or material or any immovable property but does not include any testing or analysis service provided in relation to human being or animals'.

Service tax on the services of '**technical inspection and certification**' (TIC) was levied with effect from 1 July 2003. Section 65(108) of the Finance Act, 1994, defines technical inspection and certification as 'inspection or examination of goods or process or material or any immovable property to certify that such goods or process or material or immovable property qualifies or maintains the specified standards, including functionality or utility or quality or safety or any other characteristic or parameters, but does not include any service in relation to inspection and certification of pollution levels'.

Section 69 of the Act *ibid*, read with Rule 4 of the Service Tax Rules, 1994, provides that every person liable to pay service tax shall make an application for registration to the concerned Central Excise officer in form ST-1 within a period of 30 days from the date on which the service tax under Section 66 of the Act, *ibid*, is levied.

## **5.3 Audit objectives**

Review was conducted in audit to seek assurance that: -

- the system to identify and bring in potential assesseees in tax net for new services notified for levy of service tax was effective;
- tax administration was efficient and effective in ensuring compliance to legislations and rules; and
- internal controls were in place and functional.

## **5.4 Scope of audit**

Records of 64 commissionerates out of 71 commissionerates dealing with service tax were test checked. Period covered under audit was from 2000-01 to 2004-05.

## AUDIT FINDINGS AND RECOMMENDATIONS

### 5.5 Trend of revenue

Total service tax collected during the year 2004-05 was Rs.14196.19 crore. The four services viz. MGC, STC and TTA & TIC contributed Rs.208.13 crore, Rs.73.35 crore and Rs.105.96 crore, respectively during 2004-05, which constituted 1.47 per cent, 0.52 per cent and 0.75 per cent, respectively of the total revenue collection from all the services during the year 2004-05.

The tables below indicates trends of revenue in respect of 64 test checked commissionerates.

#### 5.5.1 MGC

**Table No.1**

(Amount in crore of rupees)

No. of commissionerates	2000-01		2001-02		2002-03		2003-04		2004-05	
	No. of assessees	Amt.	No. of assessees	Amt.	No. of assessees	Amt.	No. of assessees	Amt.	No. of assessees	Amt.
64	1424	27.83	1856	30.35	2557	41.70	4581	65.97	8322	128.20

*Figures furnished by commissionerates.*

**Table No.2**

Percentage growth (+) or (-) over previous year								
No. of commissionerates	2001-02		2002-03		2003-04		2004-05	
	No.	Amt.	No.	Amt.	No.	Amt.	No.	Amt.
64	(+)30.34	(+)9.05	(+)37.77	(+)37.40	(+)79.15	(+)58.20	(+)81.66	(+)94.33

- Above data indicates that the revenue from this service grew at rates varying between 9.05 per cent to 94.33 per cent. The corresponding tax base grew at rates varying between 30.34 per cent to 81.66 per cent.
- Audit noticed that in Cochin commissionerate, there was decline of 4.70 per cent of revenue during the year 2004-05 over the year 2003-04, though the number of service providers increased by 58.14 per cent. In Thirunelveli commissionerate, there was a dip in the revenue collection to the extent of 62.28 per cent during the year 2004-05 over the previous year 2003-04 though the assessee base had remained the same.

#### 5.5.2 STC

**Table No.3**

(Amount in crore of rupees)

No. of commissionerates	2001-02		2002-03		2003-04		2004-05	
	No. of assessees	Amt.	No. of assessees	Amt.	No. of assessees	Amt.	No. of assessees	Amt.
64	238	1.71	530	9.34	1021	18.62	2020	57.66

*Figures furnished by commissionerates.*

**Table No.4**

Percentage growth (+) or (-) over previous year						
No. of commissionerates	2002-03		2003-04		2004-05	
	No.	Amt.	No.	Amt.	No.	Amt.
64	(+)122.69	(+)446.20	(+)92.64	(+)99.36	(+)97.85	(+)209.67

- Above data indicates that the revenue from this service grew at rates varying between 99.36 per cent to 446.20 per cent. The corresponding tax base grew at rates varying between 92.64 per cent to 122.69 per cent.
- Audit noticed that in Bhubaneswar I, Chandigarh and Jaipur I commissionerate, there was a decline of 10.93 per cent, 0.03 per cent and 5.05 per cent of revenue during the year 2004-05 over the year 2003-04, though the service providers had increased significantly by 100 per cent, 64 per cent and 200 per cent, respectively during this period.

### 5.5.3 TTA & TIC

**Table No.5**

(Amount in crore of rupees)

No. of commissionerates	2003-04		2004-05	
	No. of assesseees	Amt.	No. of assesseees	Amt.
64	1516	13.84	2948	53.69

Figures furnished by commissionerates.  
Breakup for TTA & TIC not made available.

**Table No.6**

Percentage growth (+) or (-) over previous year		
No. of commissionerates	2004-05	
	No.	Amt.
64	(+)94.46	(+)287.93

- Above data indicates that during the year 2004-05, revenue from these two services grew by 287.93 per cent over the previous year (2003-04). The corresponding tax base grew by 94.46 per cent over the previous year.

## 5.6 Efforts by department to broaden the tax base were ineffective and inadequate

The growth of revenue is directly linked with the growth of the assessee base. With increasing reliance on voluntary compliance by tax payers, it becomes important for department to put in place an effective mechanism for collecting information from various sources in order to bring unscrupulous assesseees into tax net.

As part of action plan drawn by DGST and circulated to Chief Commissioners on 26 May 2003, the department was to collect intelligence, conduct surveys and to identify unregistered service providers and get them registered. Further, instructions to field formations to carry out 'street to street surveys' to identify tax evaders were issued in August 2004. Position of surveys undertaken by 41 commissionerates during 2004-05 and its impact on revenue, is given in the table 7 below: -

Table No.7

(Amount in crore of rupees)

2003-04				2004-05						
No. of commissionerates	No. of surveys	Total additional revenue realised for all services	No. of persons issued registration from all services	No. of commissionerates	No. of surveys	Total additional revenue realised for all services	No. of persons issued registration			
							For all services	MGC	STC	TTA & TIC
35	2382	3.42	10194	41	3217	2.50	7526	68	11	30

Figures furnished by commissionerates.  
Breakup for TTA & TIC not made available.

Audit noticed that: -

- No target of minimum surveys was fixed for any commissionerate, in the absence of which the performance of commissionerates could not be evaluated against a fixed benchmark.
- Despite conducting street to street surveys during the period 2004-05, number of identified un-registered service providers during the year was less compared to the year 2003-04, when as per the information furnished by 35 commissionerates, 10194 number of such persons were identified and registered (Para 5.6 of the Audit Report No.6 for the period ending March 2005).
- In Bhubaneshwar II commissionerate, 98 surveys were carried out but not a single unregistered service provider was identified.
- In nine commissionerates, prominent among them being Delhi I, Bangalore, Chennai and Chandigarh, no survey was carried out.

### **Recommendation No.1**

*The Board should establish Key Performance Indicators (KPIs) for a commissionerate which should include minimum number of surveys conducted to identify/register assesseees and results thereof (increased revenue). This would facilitate monitoring and evaluation of performance of a commissionerate in an effective and scientific manner.*

Responding to the recommendation, the Ministry stated (January 2007), that the Board prescribes KPIs from time to time such as revenue collection, recovery of arrears, disposal of pending adjudication, performance in audit and any anti-evasion work, etc. They further stated that the jurisdictional Commissioner, instead of the Board, would be in the best position to decide the optimal number of surveys keeping in view the available resources.

### 5.6.1 Escapement from tax net by unregistered service providers

The department launched various schemes to bring into tax net, active but unregistered service providers. These included 'street to street survey' and 'extraordinary taxpayers' friendly scheme for instant registration without any penalty' during the year 2004-05. The results of such schemes in terms of widening of tax base and yielding of extra revenue was, however, not significant as mentioned in the preceding para. An effort was, therefore, made by audit on a limited scale to gauge the extent of escapement by active though unregistered service providers from tax net, in the backdrop of various measures taken by department to widen assessee base. For this purpose, information from various sources such as yellow pages, newspapers, websites, income tax returns, various Government departments of State as well as Central Government and other secondary records etc. was collected and analysed by audit. Preliminary findings by audit revealed that, prima facie, 777 service providers (MGC - 518, STC - 79 and TTA & TIC - 180) in 35 commissionerates had not registered themselves with central excise department. Audit estimated that revenue not realised by Government due to these unregistered service providers was Rs.86.96 crore as pointed out in the succeeding paragraphs.

### 5.6.2 Loss of service tax due to unregistered service providers

In order to firm up findings of audit, income tax records and other connected secondary records, wherever possible were cross verified. Audit was able to verify income tax records and other related records (like annual financial statements, departmental receipts, and contracts) of 247 service providers out of 777 such identified unregistered service providers. The service tax evaded by them was to the extent of Rs.78.23 crore, besides interest of Rs.15.12 crore and penalty payable under Section 76 of the Finance Act, 1994 (equal to service tax payable) upto 2004-05. This represents nearly one third of the total collection from these services from 64 commissionerates during the year 2004-05. The details are given in table 8 below: -

**Table No.8**

(Amount in crore of rupees)

Name of the service	No. of commissionerates	No. of service providers	Gross value of service provided	Amount of service tax leviable but not paid	Interest payable	Penalty
<b>MGC</b>	16	71	82.43	4.64	2.25	4.64
<b>STC</b>	19	46	167.41	13.00	3.88	13.00
<b>TTA &amp; TIC</b>	24	130	789.25	60.59	8.99	60.59
<b>Total</b>	<b>35</b>	<b>247</b>	<b>1039.09</b>	<b>78.23</b>	<b>15.12</b>	<b>78.23</b>

- Furthermore, the amount of service tax evaded under TTA & TIC from 24 commissionerates alone (Rs.60.59 crore) was more than half of the total collection during the year 2004-05 (Rs.105.96 crore) under these two services from all the commissionerates.
- The amount of service tax evaded by unregistered service providers in 'STC' in 19 commissionerates (Rs.13.00 crore) was almost one fifth of the total revenue from all the 71 commissionerates (Rs.73.35 crore).

Some illustrative cases are mentioned in the succeeding paragraphs: -

- (i) M/s. Schbumberger Asia Services Limited, in Chennai I commissionerate, were engaged by M/s. Oil and Natural Gas Corporation, for providing well logging, perforating

and other wire line services. Their services were in the nature of technical consultancy and falling under 'STC'. They had realized Rs.62.33 crore from Oil and Natural Gas Corporation during the period from April 2001 to March 2005 on account of technical consultancy. They, however, did not register themselves with the department and had not paid service tax of Rs.3.83 crore. The company was also liable to pay interest of Rs.2.09 crore besides penalty of Rs.3.83 crore.

(ii) Scrutiny of income tax returns, of M/s. Hospitech Management Consultants (P) Limited, in Delhi I commissionerate, revealed that they had realised Rs.2.01 crore from their clients on account of management consultancy during the period April 2003 to March 2005. They, however, did not register themselves with the department thereby evading service tax to the extent of Rs.17.25 lakh. The company was also liable to pay interest of Rs.3.28 lakh besides penalty of Rs.17.25 lakh.

(iii) M/s. Indo National Limited, Nellore and M/s. Panasonic Carbon India Tada, in Guntur commissionerate, made payment of Rs.9.44 crore and Rs.4.73 crore respectively to their foreign consultants viz. M/s. Matsushita Battery Industrial Co. Limited Osaka Japan on account of scientific and technical consultancy for the period April 2001 to March 2005. Under notification dated 1 August 2002, they were required to pay service tax on taxable services provided by a person who is a non-resident or is from outside India. They, however, did not obtain registration, nor did they pay service tax on account of STC to the extent of Rs.60.98 lakh and Rs.32.36 lakh, respectively. Besides, interest of Rs.23.38 lakh and penalty of Rs.93.34 lakh was also payable by them.

(iv) Scrutiny of records of Chief Electrical Inspector, Gandhinagar, in Ahmedabad commissionerate, revealed that they had collected Rs.15.28 crore towards electrical installation inspection fee and lift inspection fee, during the period from July 2003 to March 2005. These services were in the nature of 'technical inspection and certification services'. The Chief Electrical Inspector, however, did not register himself with the department nor did he pay the service tax. This resulted in escapement of service tax of Rs.1.39 crore, besides interest of Rs.17.95 lakh and penalty of Rs.1.39 crore.

### **5.6.3 Estimation of service tax loss in respect of other unregistered service providers identified by audit**

In the absence of related records, audit estimated quantum of service tax evaded by 530 out of 777 unregistered service providers identified by audit, by applying average revenue yield from registered assesseees of these services. Service tax to the extent of Rs.8.73 crore has been estimated to have been evaded by these unregistered service providers during the year 2004-05 alone, besides penalty of Rs.8.73 crore, as per the details given in the table 9 below:-

**Table No.9**

(Amount in crore of rupees)

Name of service	No. of commissionerates	No. of other unregistered service providers identified by audit	No. of registered service providers	Total revenue	Revenue yield per service provider	Estimated revenue loss	Penalty
MGC	17	447	8322	128.20	0.0154	6.88	6.88
STC	03	33	2020	57.66	0.0285	0.94	0.94
TTA & TIC	04	50	2948	53.69	0.0182	0.91	0.91
<b>Total</b>	<b>18</b>	<b>530</b>				<b>8.73</b>	<b>8.73</b>

- If the projections were to be made on what audit had actually worked out as average yield on test checked cases, the estimated revenue loss would be much higher.

### **Recommendation No.2**

*The procedure for conducting survey needs to be streamlined 'Survey, intelligence and verification cells' as suggested by Director General of Service Tax (DGST) should be created/activated and strengthened in the commissionerates to collect information from various sources including from income tax department. The survey should be conducted in a professional manner after collection, collation and analysis of information. Suitable changes in the format of excise assessment returns may also be made requiring manufacturers to indicate details of taxable services provided by them.*

Responding to the recommendation, the Ministry accepted (January 2007) the recommendation and stated that the department continues to make surveys more scientific and professional including collection of information from third parties.

### **5.7 Ineffective monitoring of service tax returns**

Section 70 of Finance Act, 1994, read with Rule 7(1) and (2) of Service Tax Rules, 1994, provided that every person liable to pay service tax shall himself assess the tax, furnish half yearly return in Form ST-3 or ST-3A by 25<sup>th</sup> of the month following the half year. Under amended Section 77 of Finance Act, a person failing to furnish the returns in due time was liable to a penalty subject to a maximum of one thousand rupees.

The return is one of the crucial tools with the department for effective administration of service tax and to combat escapement from service tax by registered service providers. It is the responsibility of the department to watch and ensure that the returns are regularly submitted in time, by active registered service providers.

Position of submission of returns by registered service providers during the period from date of levy of service tax till 2004-05 is given in the table 10 below: -

**Table No.10**

(Amount in lakh of rupees)

Name of the service	No. of commissionerates	No. of returns due	No. of returns received	Returns received by due date	Returns received late	No. of returns not received	Penalty levied	Penalty not levied
<b>MGC</b>	49	28921	22062	18479	3583	6859	0.57	45.39
<b>STC</b>		3306	2575	2139	436	731	0.01	2.54
<b>TTA &amp; TIC</b>		5412	4860	4365	495	552	0.06	3.88
<b>Total</b>		<b>37639</b>	<b>29497</b>	<b>24983</b>	<b>4514</b>	<b>8142</b>	<b>0.64</b>	<b>51.81</b>

*Figures furnished by commissionerates.*

Audit noticed that: -

- Penalty leviable on defaulters to the extent of Rs.51.81 lakh was not levied.
- Twenty two per cent of the returns due were not received in respect of these four services.
- Fifteen per cent of the returns were received late.



### 5.7.1 No mechanism to detect and take proactive action for 'stop filers', leading to evasion

In audit's opinion, the number of service providers not filing returns was significantly high for want of proper watch by department over the submission of returns and inaction by department by way of imposition of penalty in cases of default. Audit attempted to ascertain whether the active service providers had actually rendered services during the period when they did not furnish the returns. An independent verification of income tax returns and other connected records of a few of such defaulters, on a very limited scale, revealed that 105 assesseees (53 of MGC, 20 of STC and 32 of TTA & TIC) in 26 commissionerates had continued providing services attracting tax during the period, when they had deliberately not filed returns. Service tax due was also not paid. Department did not take any action for non-submission of returns by these defaulters, nor did it verify whether the defaulters were actively engaged in providing services during the period of default. This resulted in evasion of service tax to the extent of Rs.6.12 crore, besides interest of Rs.1.97 crore and penalty of Rs.6.12 crore, during the period from 1998-99 to 2004-05. The details of such cases are given in the table 11 below: -

Table No.11

(Amount in crore of rupees)

Name of the service	No. of commissionerates	No. of service providers	Gross value of services	Service tax payable	Interest payable	Penalty payable
<b>MGC</b>	17	53	53.73	3.02	1.33	3.02
<b>STC</b>	8	20	7.08	0.57	0.14	0.57
<b>TTA &amp; TIC</b>	16	32	28.58	2.53	0.50	2.53
<b>Total</b>	<b>26</b>	<b>105</b>	<b>89.39</b>	<b>6.12</b>	<b>1.97</b>	<b>6.12</b>

Figures furnished by commissionerates.

Some illustrative cases are mentioned in the succeeding paragraphs: -

(i) Verification of income tax returns of M/s. Xavier Institute of Management, in Bhubaneswar I commissionerate, revealed that the assessee had realised Rs.15.03 crore for rendering MGC during the period from 1998-99 to 2002-03. However, no returns were filed by the assessee, during this period. Leviable service tax was also neither paid nor was it demanded by the department. This resulted in non-payment of service tax to the extent of Rs.75.13 lakh, besides interest of Rs.47.72 lakh and penalty of Rs.75.13 lakh.

(ii) M/s. Appollo Hospital Enterprises Limited, in Chennai commissionerate, engaged in providing management consultancy for setting up new hospitals paid service tax from April 2001 onwards. A verification of their profit and loss account for the year 1999-2000, however, revealed they had realised Rs.5.28 crore as management consultant's fee on which no service tax was paid. This resulted in evasion of service tax to the extent of Rs.26.37 lakh besides interest of Rs.31.34 lakh and penalty of Rs.26.37 lakh.

(iii) Indian Registrar of Shipping, Kolkata, in Kolkata commissionerate, engaged in providing 'technical inspection and certification services', was registered with the department. During the period from 2003-04 to 2004-05, they did not submit any returns. Cross verification with annual financial statements, however, revealed that they had realised Rs.1.99 crore and Rs.2.88 crore respectively, during this period for providing the 'TIC' on

which service tax to the extent of Rs.45.31 lakh was not paid. Besides, interest of Rs.6.39 lakh and penalty of Rs.45.31 lakh was also payable.

### **Recommendation No.3**

*The Ministry should devise an appropriate and effective mechanism to detect 'stop filers' in time and collect Government revenue wherever due from these assesseees.*

Responding to the recommendation, the Ministry informed (January 2007), that the project of ACES is already in the advance stage of preparation. Implementation of ACES will provide an appropriate and effective mechanism to identify 'stop filers' in an automated environment.

### **5.7.2 Scrutiny of returns was ineffective**

The scrutiny of returns is the most important element of the enforcement strategy of tax administration. The overriding aim of such scrutiny/verification is to provide a creditable deterrence to wilful suppression of actual assessable value as well as to realise correct Government revenues.

Prior to 10 September 2004, Section 71 of the Finance Act, 1994, provided for verification of the correctness of the tax assessed by the assessee, on the basis of information contained in the returns filed by the assessee. But this Section has been omitted with effect from 10 September 2004. Afterwards, no departmental instructions for scrutiny of ST-3 returns have been issued. While superintendent of Central Excise need not verify the return after 10 September 2004, the DGST in his Performance Report for the year 2005-06 spoke of the need to streamline the scrutiny of the returns. There is, therefore, contradiction in the policy of the Board/Government and perception of the DGST on the issue of scrutiny/verification of returns.

The information furnished by 46 commissionerates, however, revealed that the commissionerates continued to check returns as before although the pendency of the returns remaining unchecked increased considerably after 10 September 2004. The position of verification/checking of ST-3 returns for the period from 2002-03 to 2004-05 is given in the table 12 below: -

**Table No.12**

(Amount in lakh of rupees)

No. of commissionerate	Period	Name of the service	No. of returns received	No. of returns checked	Pending verification	Additional demands raised		Recovery	
						No.	Amt.	No.	Amt.
46	2002-03 to 2003-04	MGC	9103	8412	691	30	58.07	9	0.88
		STC	5899	5305	594	3	9.57	1	0.31
		TTA & TIC	1323	1297	26	14	3.41	6	0.10
		<b>Total</b>	16325	15014	1311	47	71.05	16	1.29
46	2004-05	MGC	10150	6965	3185	91	21.45	15	3.86
		STC	6143	4871	1272	5	0.85	0	0.00
		TTA & TIC	2718	2381	337	21	1.37	2	0.15
		<b>Total</b>	19011	14217	4794	117	23.67	17	4.01
		<b>Grand total</b>	<b>35336</b>	<b>29231</b>	<b>6105</b>	<b>164</b>	<b>94.72</b>	<b>33</b>	<b>5.30</b>

Figures furnished by commissionerates.

- Eight per cent of returns for the period upto 2003-04 were pending for verification in these four services.
- Twenty five per cent of returns for the period 2004-05 were not checked after 10 September 2004.
- Rs.5.30 lakh was recovered as a result of scrutiny of 29,231 returns for the period from 2002-03 to 2004-05.

Some ST-3 returns duly verified/checked by department were scrutinised in audit. Cases of short payment of service tax on the basis of information contained in ST-3 returns which had escaped notice of department came to light indicating that even basic checks with reference to the rate of service tax and interest payable for delayed payment, etc. were not exercised. Some of these cases are illustrated in succeeding paragraphs: -

(i) Rate of service tax was revised upward from eight per cent to 10 per cent with effect from 10 September 2004. Education cess was also levied with effect from 10 September 2004 at the rate of 2 per cent on service tax payable. However, in 16 cases, assessee continued to calculate service tax at lower rate. This resulted in short payment of service tax to the tune of Rs.20.42 lakh besides interest of Rs.2.98 lakh.

(ii) Nine other cases of non-payment of service tax/interest to the extent of Rs.30.81 lakh for various reasons such as interest on delayed payment, service tax not paid on gross amount, incorrect assessment of service tax etc were noticed by audit.

#### **Recommendation No.4**

*Board may consider putting in place a mechanism for checking/verification of returns on regular basis. This checking may be reinforced by detailed scrutiny of selected cases on scientific representative sample basis after proper risk analysis.*

Responding to the recommendation, the Ministry stated (January 2007), that it was working on the issue and once ACES is implemented, the risk management system in service tax will be implemented alongwith the selection on scientific basis for detailed scrutiny.

#### **5.7.3 Suppression of taxable value**

The power vested in Superintendent of Central Excise to call for any records from the assessee for verification was withdrawn, when Section 71 of Finance Act, 1994 was omitted with effect from 10 September 2004. This power was, however, seldom exercised by the department for verification purpose even prior to 10 September 2004, as had been pointed out in the reviews on various services contained in Audit Reports of earlier years. Since no mechanism to check the correctness of the assessment made by the service providers as a deterrent has been put in place, the risk of suppression of assessable value in ST-3 returns to evade payment of service tax, remains unmitigated. Attempt was, therefore, made by audit to ascertain extent of correctness of tax paid by assessee by cross verification of ST-3 returns with income tax returns and other related records of a few assessee. Audit noticed deliberate attempts by assessee to suppress value of services and consequently evade service tax, in few cases. The service tax evaded by 116 assessee by suppression of their assessable value was Rs.5.66 crore during the period from 2000-01 to 2004-05. Besides interest of Rs.1.39

crore and penalty of Rs.5.66 crore was also payable, as per details given in the table 13 below: -

**Table No.13**

(Amount in crore of rupees)

Name of the service	No. of commissionerate	No. of assesseees	Value of service not shown in ST-3 returns	Service tax payable	Interest	Penalty
<b>MGC</b>	21	67	35.70	2.25	0.70	2.25
<b>STC</b>	11	30	21.41	1.76	0.36	1.76
<b>TTA &amp; TIC</b>	8	19	18.18	1.65	0.33	1.65
<b>Total</b>	<b>24</b>	<b>116</b>	<b>75.29</b>	<b>5.66</b>	<b>1.39</b>	<b>5.66</b>

Figures furnished by commissionerates.

Some illustrative cases are mentioned in the succeeding paragraphs: -

(i) Scrutiny of income tax returns of M/s. Zaiden Leeng SDN BHD Artefact Project (JV), in Nagpur commissionerate, revealed that they had shown receipt of Rs.6.91 crore on account of MGC in their income tax returns during the period from 2003-04 to 2005-06. But in ST-3 returns gross receipt was shown as Rs.3.03 crore. This resulted in undervaluation of taxable amount and short payment of service tax to the extent of Rs.34.83 lakh, besides interest of Rs.2.53 lakh and penalty of Rs.34.83 lakh during the period from 2003-04 to 2005-06.

(ii) Comparison of the income tax returns, of M/s. Oriental Infrastructure Consultancy Research Private Limited, in Bhubaneswar I commissionerate, with ST-3 return showed that assessee had undervalued receipt on account of STC to the extent of Rs.2.82 crore. This resulted in short payment of Rs.19.81 lakh, besides interest of Rs.5.64 lakh and penalty of Rs.19.81 lakh.

(iii) Verification of income tax returns of M/s. Aurigene Discovery Tech. Limited, in Bangalore commissionerate providing STC, revealed that assessee had undervalued services to the extent of Rs.7.31 crore in ST-3 returns. This resulted in short payment of Rs.58.48 lakh, besides interest of Rs.17.07 lakh and penalty of Rs.58.48 lakh.

#### **Recommendation No.5**

*Government may consider amending the Act/Rules to require mandatory submission of IT returns, annual financial statements alongwith ST return, to enable detection of undervaluation. If need be, periodicity of ST returns could be aligned with IT returns.*

Responding to the recommendation, the Ministry did not accept it and stated (January 2007) that it was a conscious decision to keep the process of filing of return simple so that no undue hardship is caused to the tax payer. They further stated that detection of short payment on basis of IT returns or other financial records is being carried out by the department through audit.

#### **5.7.4 Service tax on the other services rendered prior to registration not paid**

M/s. Escon Technical Services, M/s. Quality Cert (India) Limited, M/s. Nautilus Services, in Coimbatore and Chennai commissionerates, registered themselves under technical testing &

analysis and technical inspection & certification services respectively, in July 2003, and M/s. Cholamandalam, in Chennai commissionerate, registered itself under 'STC' in August 2001. A scrutiny of their annual financial accounts, however, revealed that they had been providing services which were in the nature of STC (M/s. Escon Technical Services and M/s. Nautilus Services) and MGC (M/s. Quality Cert (India) Limited and M/s. Cholamandlam AXE Risk) on which no service tax was paid. This resulted in non-payment of service tax to the extent of Rs.16.30 lakh. Besides interest of Rs.10.03 lakh and penalty of Rs.16.30 lakh was also payable.

## **5.8 Delay in adjudication**

In 27 commissionerates, adjudication of 477 show cause notices issued to MGC, STC, TTA & TIC involving revenue of Rs.17.04 crore was pending as on 30 September 2005, of which, 44 SCNs involving revenue of Rs.8.55 crore were pending for more than two years. In Mumbai commissionerate alone 28 show cause notices involving Rs.6.61 crore were pending for more than two years.

Section 73 of Finance Act, 1994, relates to issue of SCN and recovery of service tax short levied. These provisions are on lines of Section 11A of Central Excise Act. However, the provision of Section 11A prescribing time-limit for finalisation of adjudication process were not incorporated in Section 73. The adjudication officer is thus not required to finalise a demand case within a prescribed time frame, which could lead to delays in finalisation of cases and recovery of service tax.

### ***Recommendation No.6***

*A time-limit for finalisation of adjudication involving technical infractions and those involving service tax revenue may be prescribed so as to avoid pendency of adjudication cases and consequential risk to revenue.*

Responding to the recommendation, the Ministry stated (January 2007), that a time limit for finalisation of adjudication of pending cases was being prescribed from time to time through executive instructions.

## **5.9 Service tax code number based on permanent account number (PAN) not allotted**

Board in their letter dated 27 August 2001 issued instructions for allotment of service tax code numbers based on PAN allotted by income tax department to all service providers. The work was to be completed latest by 15 November 2001. The progress was to be monitored by DGST on a weekly basis. Board vide circular dated 21 February 2002 issued further instruction for allotment of PAN based service tax code numbers. Audit found that the progress made in this regard was not encouraging and was indicative of lack of monitoring and appropriate corrective action by the department.

Position of allotment of PAN based service tax code number as on 30 September 2005 in 49 commissionerates (where information was made available) is given in the following table 14:-

**Table No.14**

Name of service	No. of commissionerates	No. of service providers	No. of service tax providers not allotted STCNs	Percentage
MGC	43	5791	1991	34
STC	36	1403	346	25
TTA & TIC	38	2415	415	17
<b>Total</b>	49	9609	2752	29

- Furthermore, the DGST in its performance report for the year 2004-05 stated that the programme of generation of PAN based registration numbers and allotment of ST codes to service tax assesseees have been properly implemented in most of the commissionerates. Contrary to this assertion, audit verified that work of allotment of service tax code numbers, which is crucial from the point of view of cross verification of value of services shown in the returns with the income tax returns, was yet to be completed even after a lapse of more than four years.
- Information received from Visakhapatnam I commissionerate, revealed that no service provider in these services was allotted service tax code number.
- In Lucknow commissionerate, no service provider was allotted service tax code number in 'MGC'.
- In Delhi I commissionerate, the percentage of person not allotted PAN based service tax code numbers, was as high as 73 per cent in MGC and 77 per cent in STC.

**Recommendation No.7**

*As commented upon earlier in this report, in audit's opinion, correlation of income tax data and service tax data is an important key factor for correct evaluation of service tax liability. Allotment of PAN based ST codes is a step in right direction. However, this aspect of implementation of this scheme has been slow and non-exhaustive, which needs to be corrected.*

The Ministry accepted (January 2007) the recommendation.

**5.10 Records not transferred to newly created six exclusive service tax commissionerates**

At the behest of DGST, the Board vide circular dated 18 May 2004 notified the creation of six commissionerates of service tax at Mumbai, Delhi, Chennai, Kolkata, Bangalore and Ahmedabad. The purpose of creation of exclusive service tax commissionerates was to bring about more efficiency in administration of service tax. The newly created commissionerates, however, started functioning from September 2004 onwards.

A test check of the records of these commissionerates, relating to the four services under review, revealed the following: -

- (i) After the re-organisation of commissionerates of service tax, no instructions for transfer of records within a time bound programme were issued either by the Board or by the DGST. Nor did the Board/DGST monitor the progress of the transfer of records.

(ii) In the absence of such instruction, records prior to September 2004 were not transferred by the other concerned commissionerates till the date of audit (December 2005). The newly formed commissionerates, therefore, could not produce the requisite records to audit.

(iii) For want of transfer of all the connected records, audit could not evaluate the performances of the newly created service tax commissionerates in terms of widening of service tax base or generation of additional revenues.

### 5.11 Search and seizure

Amendment in Section 82 of Finance Act, 1994, with effect from 16 August 2002, vests powers with commissioner of central excise to search premises and seize documents, where necessary. DGST vide communication of 27 June 2003 instructed commissioners to exercise this power in an effective and meaningful manner. From information furnished by 41 commissionerates, it was noticed that only 20 searches and 8 seizures were made during the period 2004-05, that too, on a very limited scale. The position is given in table 15 below: -

Table No.15

(Amount in crore of rupees)

No. of commissionerates	Period	No. of searches	No. of seizure	MGC		STC		TTA & TIC	
				No. of SCN	Service tax involved	No. of SCN	Service tax involved	No. of SCN	Service tax involved
41	2004-05	20	8	3	4.67	2	0.17	4	2.85

Figures furnished by commissionerates

- Audit noticed that, in 37 commissionerates, including Mumbai, Hyderabad II, Delhi (Gurgaon) and Ahmedabad, where there is a large base of these services, no searches and seizures were conducted.

### 5.12 Internal audit of service tax assesseees

Board vide circular dated 7 February 2002 extended the coverage of internal audit to service tax and issued guidelines for the internal audit parties. The audit was on the pattern of Excise Audit-2000 in Central Excise.

The details of internal audit coverage of the services under review, are given in the table 16 below: -

Table No.16

(Amount in crore of rupees)

Name of service	No. of commissionerates	No. of assesseees covered	Amount of demand raised as a result of internal audit	Amount of demands dropped	Latest position of demand cases		
					Amount recovered	Adjudication pending	In appeal
MGC	8	31	6.18	0.97	0.84	1.75	2.62
STC	3	4	0.89	0.00	0.00	0.89	0.00
TTA & TIC	4	7	0.01	0.00	0.01	0.00	0.00
<b>Total</b>	<b>11</b>	<b>42</b>	<b>7.08</b>	<b>0.97</b>	<b>0.85</b>	<b>2.64</b>	<b>2.62</b>

- The internal audit in STC and TTA & TIC was not effective in terms of detection of evasion/short payment of service tax.

This could be due to the fact that units in these services were not selected after gathering specific information and on the basis of proper risk analysis.

**New Delhi**  
**Dated :**

**(JAYANTI PRASAD)**  
**Principal Director (Indirect Taxes)**

**Countersigned**

**New Delhi**  
**Dated :**

**(VIJAYENDRA N. KAUL)**  
**Comptroller and Auditor General of India**