



सत्यमेव जयते

# Report of the Comptroller and Auditor General of India

for the year ended March 2015



Union Government  
Department of Revenue  
(Indirect taxes – Central Excise)  
Report No. 2 of 2016

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**Laid on the table of Lok Sabha/Rajya Sabha on \_\_\_\_\_**

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## Preface

This Report for the year ended March 2015 has been prepared for submission to the President of India under Article 151 of the Constitution of India.

The Report contains significant results of the compliance audit of the Central Board of Excise and Customs under the Department of Revenue – Indirect Taxes (Central Excise) of the Union Government.

The instances mentioned in this Report are those, which came to notice in the course of test audit for the period 2014-15; as well as those which came to notice in earlier years but could not be reported in the previous Audit Reports.

The audit has been conducted in conformity with the Auditing Standards issued by the Comptroller and Auditor General of India.

## Executive Summary

The Central Excise collection was ₹ 1,89,038 crore during financial year 2014-15 (FY15) and accounted for 34.61 per cent of Indirect Tax revenue in FY15. Indirect Tax collection has fallen as a ratio of GDP while as a ratio of Gross Tax revenue, it has increased in FY 15 vis-a-vis FY14.

This Report has 64 audit observations on Central Excise duties, having financial implication of ₹ 147.87 crore. The Ministry/Department had, till December 2015, accepted audit observations involving revenue of ₹ 135.85 crore and reported recovery of ₹ 27.95 crore. Some significant findings are as follows:

### Chapter I: Department of Revenue – Central Excise

- Central Excise revenue has shown 11.56 per cent growth in FY15 compared to FY14.

(Paragraphs 1.7)

- During FY15, increase in Central Excise duty on petrol and high speed diesel resulted not only in increase of Central Excise collection from petroleum sector but also lead to overall growth of Central Excise. Except Petroleum products and plastic, revenue growth in other sectors is either stagnant or negative.

(Paragraph 1.8)

- Revenue forgone for FY15 in respect of Excise duties was ₹ 1,84,764 crore (₹ 1,77,680 crore as general exemptions and ₹ 17,284 crore as area based exemptions) which is 97.74 per cent of revenue from Central Excise.

(Paragraph 1.11)

- Huge amount of Central Excise revenue amounting to ₹ 81,538 crore is blocked in appeals. The amount is increasing every year. Despite, a number of measures initiated by the Board, locking up of such a large revenue is a matter of concern.

(Paragraph 1.18)

### Chapter II: Central Excise Exemptions for SSI units

- Less than 50 per cent of the assesseees registered as SSI units in the selected ranges are actually availing the benefit of the SSI exemption. SSI manufacturer of intermediate goods is not benefited out of the scheme.

(Paragraph 2.5)

- In 11 cases, excess availing of SSI exemption amounting to ₹ 1.83 crore was noticed.

(Paragraph 2.7.2)

### **Chapter III : Functioning of Director General of Audit and its zonal units**

- Annual report published by DG (Audit) for the years 2011-12 and 2012-13 had discrepancies in figures compared to Quality Assurance Review (QAR) reports, doubting the correctness of published data.

(Paragraph 3.6.6)

- During 2011-12 and 2012-13, 22 and 29 Commissionerates in respect of Central Excise and 18 and 21 Commissionerates in respect of Service Tax were downgraded vis-a-vis previous year grading, showing drop in performance of internal audit.

(Paragraph 3.6.10)

### **Chapter IV: Tax Accounting and Reconciliation in Central Excise, Service Tax and Customs**

- In 41 Commissionerates (Central Excise), 39 Commissionerates (Service Tax) and nine Commissionerates (Customs), no reconciliation was being done and consequently revenue of ₹ 2,36,295 crore, ₹ 3,01,436 crore and ₹ 82,224 crore respectively, pertaining to these Commissionerate, remained unreconciled for the period 2011-12 to 2013-14.

(Paragraph 4.2.1.1(i), 4.4.1.1(i) and 4.6.1.1)

- Revision of interest rate, at which interest is collected from banks for delayed remittance of Government revenue, was not carried out by Pr CCA, CBEC as and when bank rate was revised by RBI and interest was being calculated by the system from 13 February 2012 onwards at reduced rate.

(Paragraph 4.2.4(a))

### **Chapter V: Issue of Show Cause Notice and Adjudication process**

- SCN invoking extended period on incorrect grounds in contravention of statute resulted in SCNs being time barred in the adjudication in 20 cases involving revenue of ₹ 4.40 crore.

(Paragraph 5.5.1)

- In eight cases involving revenue of ₹ 2.28 crore, SCN were issued late which may lead to demands get time barred.

(Paragraph 5.5.2)

- Cases kept in call book were not being reviewed and 121 cases having monetary implication of ₹ 29.76 crore were kept in Call Book wrongly.

Paragraph (5.9.2)

**Chapter VI: Non-compliance with Rules and Regulations**

- We observed 26 cases of irregular availing and utilisation of Cenvat credit, non/short payment of Central Excise duty involving revenue of ₹ 98.79 crore.

Paragraph (6.1)

**Chapter VII: Effectiveness of Internal Control**

- We observed 34 instances of deficiencies in internal audit carried out by departmental officials and other issues involving revenue of ₹ 32.76 crore.

Paragraph (7.2)

## Chapter I

### Department of Revenue – Central Excise

#### 1.1 Resources of the Union Government

**1.1.1** The Government of India's resources include all revenues received by the Union Government, all loans raised by issue of treasury bills, internal and external loans and all moneys received by the Government in repayment of loans. Tax revenue resources of the Union Government consist of revenue receipts from direct and indirect taxes. Table 1.1 below shows the summary of resources of the Union Government for the Financial Year (FY) 15 and FY14.

**Table 1.1: Resources of the Union Government**

	(₹ in crore)	
	FY 15	FY 14
<b>A. Total Revenue Receipts</b>	<b>16,66,717</b>	<b>15,36,024</b>
<i>i. Direct Taxes Receipts</i>	6,95,792	6,38,596
<i>ii. Indirect Taxes Receipts including other taxes</i>	5,49,343	5,00,400
<i>iii. Non-Tax Receipts</i>	4,19,982	3,93,410
<i>iv. Grants-in-aid and contributions</i>	1,600	3,618
<b>B. Miscellaneous Capital Receipts<sup>1</sup></b>	<b>37,740</b>	<b>29,368</b>
<b>C. Recovery of Loan and Advances<sup>2</sup></b>	<b>26,547</b>	<b>24,549</b>
<b>D. Public Debt Receipts<sup>3</sup></b>	<b>42,18,196</b>	<b>39,94,966</b>
<b>Receipts of Government of India (A+B+C+D)</b>	<b>59,49,200</b>	<b>55,84,907</b>

Source: Union Finance Accounts of respective years. Direct Tax receipts and Indirect tax receipts including other taxes have been worked out from the Union Finance Accounts. Total Revenue Receipts include ₹ 3,37,808 crore in FY15 and ₹ 3,18,230 crore in FY14, share of net proceeds of direct and indirect taxes directly assigned to states.

**1.1.2** The total receipts of the Union Government increased to ₹ 59,49,200 crore in FY15 from ₹ 55,84,907 crore in FY14. In FY15, its own receipts were ₹ 16,66,717 crore including gross tax receipts of ₹ 12,45,135 crore.

#### 1.2 Nature of Indirect Taxes

Indirect Taxes attach themselves to the cost of the supply of goods/services and are, in this sense, transaction-specific rather than person-specific. The major Indirect Taxes/duties levied under Acts of Parliament are:

- a) Central Excise duty:** Central Excise duty is levied on manufacture or production of goods in India. Parliament has powers to levy excise duties on tobacco and other goods manufactured or produced in India except alcoholic liquors for human consumption, opium, Indian hemp

<sup>1</sup> This comprises of value of bonus share, disinvestment of public sector and other undertakings and other receipts

<sup>2</sup> Recovery of loans and advances made by the Union Government

<sup>3</sup> Borrowing by the Government of India internally as well as externally

and other narcotic drugs and narcotics but including medicinal and toilet preparations containing alcohol, opium etc. (Entry 84 of List 1 of the Seventh Schedule of the Constitution).

- b) Service Tax:** Service Tax is levied on services provided within the taxable territory (Entry 97 of List 1 of the Seventh Schedule of the Constitution). Service Tax is a tax on services rendered by one person to another. Section 66B of the Finance Act, 1994 envisages that there shall be a tax levied at the rate of 12 per cent on the value of all services, other than those specified in the negative list, provided or agreed to be provided in the taxable territory by one person to another and collected in such manner as may be prescribed.<sup>4</sup> 'Service' has been defined in section 65B (44) of the Act to mean any activity for consideration (other than the items excluded therein) carried out by a person for another and to include a declared service.<sup>5</sup>
- c) Customs duty:** Customs duty is levied on import of goods into India and on export of certain goods out of India (Entry 83 of List 1 of the Seventh Schedule of the Constitution).

### 1.3 Organisational structure

The Department of Revenue (DoR) of Ministry of Finance (MOF) functions under the overall direction and control of the Secretary (Revenue) and coordinates matters relating to all the Direct and Indirect Union Taxes through two statutory Boards namely, the Central Board of Excise and Customs (CBEC) and the Central Board of Direct Taxes (CBDT) constituted under the Central Board of Revenue Act, 1963. Matters relating to the levy and collection of Service Tax are looked after by the CBEC.

Indirect Tax laws are administered by the CBEC through its field offices, the executive Commissionerates. For this purpose, the country is divided into 23 zones of Central Excise and four zones of Service Tax headed by the Chief Commissioner. In CBEC, restructuring and re-organisation of field formation has taken place in August 2014. Under 23 zones of Central Excise, there are 119 executive Commissionerates and under four zones of Service Tax, there are 22 executive Commissionerates headed by the Commissioner. Division and ranges are the subsequent formations, headed by Deputy/Assistant Commissioner and Superintendents respectively. Apart from these executive Commissionerates, there are eight Large Tax Payer Units (LTU)

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<sup>4</sup> Section 66B was inserted by the Finance Act, 2012 with effect from 1 July 2012; section 66D lists the items the negative list comprises of

<sup>5</sup> Section 66E of the Finance Act lists the declared services

Commissionerates, 60 Appeal Commissionerates, 45 Audit Commissionerates and 20 Directorates General/Directorates dealing with specific function.

The overall sanctioned staff strength of the CBEC is 84,891<sup>6</sup> as on 1 January 2015. The organisational structure of CBEC is shown in Appendix I.

This chapter discusses trends, composition and systemic issues in Central Excise using data from Finance Accounts, departmental accounts and relevant data available in public domain.

#### 1.4 Growth of Indirect Taxes - trends and composition

Table 1.2 depicts the relative growth of Indirect Taxes during FY11 to FY15.

Table 1.2: Growth of Indirect Taxes

(₹ in crore)					
Year	Indirect Tax revenue	GDP	Indirect Taxes as % of GDP	Gross Tax revenue	Indirect Taxes as % of Gross Tax revenue
FY11	3,45,371	77,95,314	4.43	7,93,307	43.54
FY12	3,92,674	90,09,722	4.36	8,89,118	44.16
FY13	4,74,728	99,88,540	4.75	10,36,460	45.80
FY14	4,97,349	1,13,45,056	4.38	11,38,996	43.67
FY15	5,46,214	1,25,41,208	4.36	12,45,135	43.87

Source: Tax revenue - Union Finance Accounts, GDP – Press note of CSO<sup>7</sup>

It is observed that Indirect tax collection have fallen as a ratio of GDP while as a ratio of Gross Tax revenue it has increased in FY15 vis-à-vis FY14.

#### 1.5 Indirect Taxes – relative contribution

Table 1.3 depicts the trajectory of the various Indirect Tax components in GDP terms for the period FY11 to FY15.

Table 1.3: Indirect Taxes – percentage of GDP

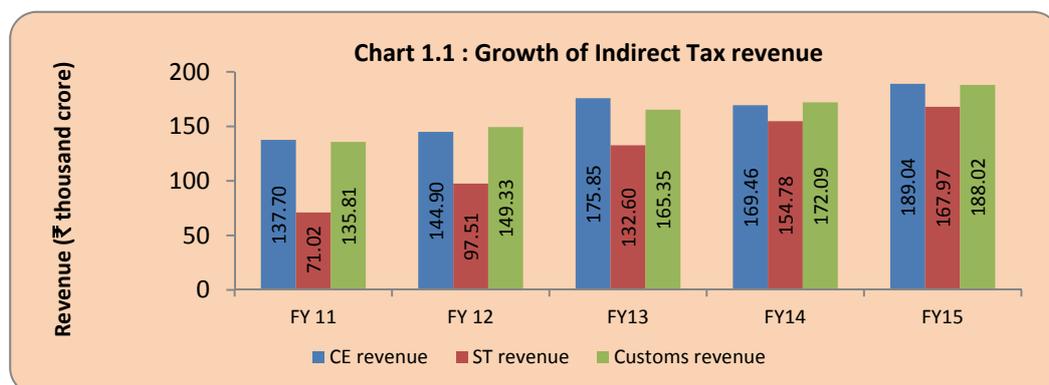
(₹ in crore)							
Year	GDP	CE revenue	CE revenue as % of GDP	ST revenue	ST revenue as % of GDP	Customs revenue	Customs revenue as % of GDP
FY11	77,95,314	1,37,701	1.77	71,016	0.91	1,35,813	1.74
FY12	90,09,722	1,44,901	1.61	97,509	1.08	1,49,328	1.66
FY13	99,88,540	1,75,845	1.76	1,32,601	1.33	1,65,346	1.66
FY14	1,13,45,056	1,69,455	1.49	1,54,780	1.36	1,72,085	1.52
FY15	1,25,41,208	1,89,038	1.51	1,67,969	1.34	1,88,016	1.50

Source: Figures of tax receipts are as per Union Finance Accounts of respective years.

<sup>6</sup> Figures provided by the Ministry

<sup>7</sup> Press note on GDP released on 29 May 2015 by Central Statistical Office (CSO), Ministry of Statistics and Programme Implementation. This indicates that the figures for GDP for FY13 and FY14 are based on New Series Estimates; and figure for FY15 are based on provisional estimates at current prices. The figures of GDP for FY11 and FY12 are based on current market price with base year 2004-05. Figures are being continually revised by CSO and this data is meant for an indicative comparison of fiscal performance with macro economic performance.

The relative revenue contribution of the major Indirect Taxes is depicted in Chart 1.1.



The share of Central Excise revenue as a percentage of GDP has increased while share of Customs and Service Tax has suffered decline during FY15.

### 1.6 Growth of Central Excise receipts - trends and composition

Table 1.4 depicts the trends of Central Excise revenue in absolute and GDP terms during FY11 to FY15.

Table 1.4: Growth of Central Excise revenue

Year	GDP	Gross Tax revenue	Gross Indirect Taxes	Central Excise revenue	₹ in crore)		
					Central Excise Revenue as % of GDP	Central Excise Revenue as % of Gross tax revenue	Central Excise as % of Indirect taxes
FY11	77,95,314	7,93,307	3,45,371	1,37,701	1.77	17.36	39.87
FY12	90,09,722	8,89,118	3,92,674	1,44,901	1.61	16.30	36.90
FY13	99,88,540	10,36,460	4,74,728	1,75,845	1.76	16.97	37.04
FY14	1,13,45,056	11,38,996	4,97,349	1,69,455	1.49	14.88	34.07
FY15	1,25,41,208	12,45,135	5,46,214	1,89,038	1.51	15.18	34.61

Source: Figures of tax receipts are as per Union Finance Accounts of respective years.

It is observed that Central Excise as a ratio of GDP, Gross Tax Revenue and Indirect Taxes has increased during FY15 and it constituted approximately 15 per cent of Gross Tax revenue in FY15.

### 1.7 Central Excise receipts vis-à-vis Cenvat credit utilised

A manufacturer can avail credit of duty of Central Excise paid on inputs or capital goods as well as Service Tax paid on input services related to his manufacturing activity and can utilise credit so availed in payment of Central Excise duty.

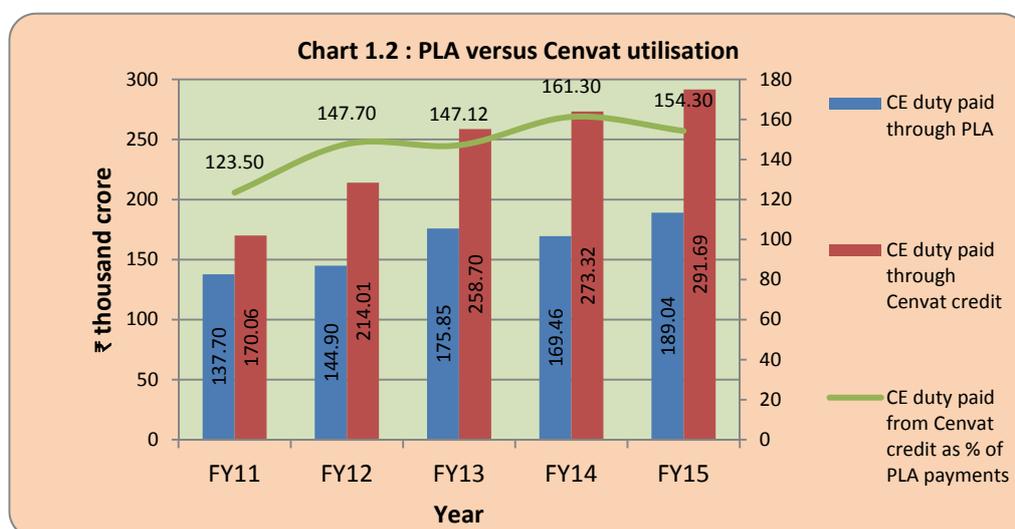
Table 1.5 and chart 1.2 depict growth of Central Excise collections through cash (PLA) and Cenvat credit during FY11 to FY15.

**Table 1.5: Central Excise Receipts: PLA and Cenvat utilisation**

(₹ in crore)

Year	CE duty paid through PLA		CE duty paid through Cenvat credit		CE duty paid from Cenvat credit as % of PLA payments
	Amount#	% increase from previous year	Amount*	% increase from previous year	
FY11	1,37,701	-	1,70,058	-	123.50
FY12	1,44,901	5.23	2,14,014	25.85	147.70
FY13	1,75,845	21.36	2,58,697	20.88	147.12
FY14	1,69,455	-3.63	2,73,323	5.65	161.30
FY15	1,89,038	11.56	2,91,694	6.72	154.30

Source: # Union Finance Accounts, \* Figures furnished by the Ministry

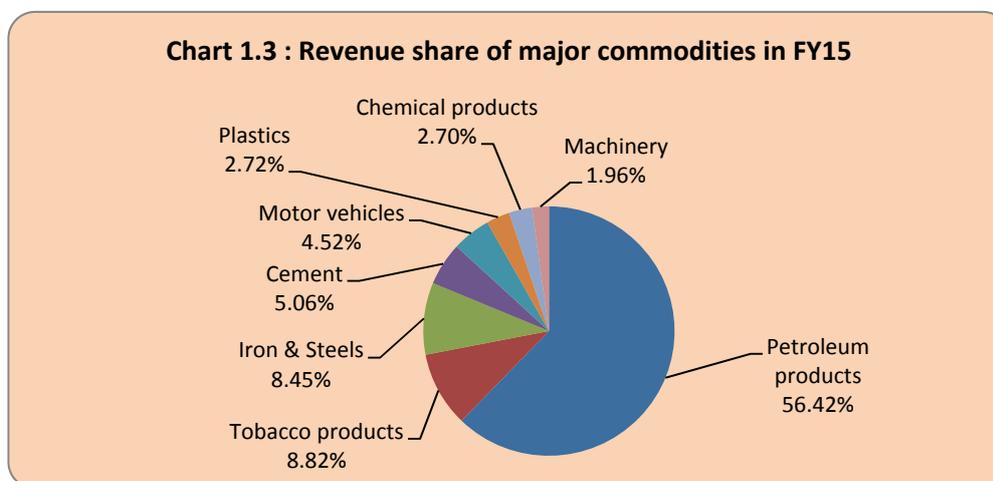


Source: Figures provided by the Ministry

It is observed that Central Excise revenue (PLA) has shown 11.56 per cent growth in FY15 compared to FY14. Payment from Cenvat credit, has increased over last five years from 124 per cent of PLA in FY11 to 154 per cent in FY15. Though, it has decreased marginally in comparison of FY14.

## 1.8 Central Excise revenue from major commodities

Chart 1.3 depicts the share of commodity groups in the Central Excise revenues (FY15).



Source: Figures provided by the Ministry

It is observed that Petroleum (56.42 per cent), Tobacco products (8.82 per cent), Iron and Steel (8.45 per cent), Cement (5.06 per cent), Motor vehicles (4.52 per cent), Plastic (2.72 per cent), Chemical products (2.70 per cent) and Machinery products (1.96 per cent) were the highest revenue earners and altogether, contributed 90.66 per cent of the total Central Excise revenue in FY15.

Table 1.6 depicts revenue from these commodities during last five years.

**Table 1.6 : Revenue from top yielding commodities during last five years**

(₹ in crore)

Commodities	FY11	FY12	FY13	FY14	FY15
Petroleum products	76,023	74,112	84,188	88,065	1,06,653
Tobacco products	13,977	15,682	17,991	16,050	16,676
Iron and Steels	14,483	13,813	17,603	17,342	15,970
Cement	7,458	8,952	10,712	10,308	9,572
Motor vehicles	7,024	7,447	10,038	8,363	8,546
Plastics	2,368	2,931	4,259	4,298	5,150
Chemical products	2,802	3,443	4,872	4,845	5,103
Machinery	2,799	3,452	4,559	3,761	3,707

Source: Figures provided by the Ministry

It is observed that during FY15, the specific Central Excise duty on petrol and high speed diesel increased from ₹ 1.2 per litre and ₹ 1.46 per litre to ₹ 8.95 per litre and ₹ 7.96 per litre respectively which resulted not only in increase

of Central Excise collection from petroleum sector but also lead to overall growth of Central Excise. It is further observed that during FY15 except Petroleum products and plastic, revenue growth is either stagnant or negative.

## 1.9 Tax base

"Assessee" means any person who is liable for payment of duty assessed or a producer or manufacturer of excisable goods or a registered person of a private warehouse in which excisable goods are stored and includes an authorised agent of such person. A single legal entity (company or individual) can have multiple assessee identities depending upon location of manufacturing units. Table 1.7 depicts the number of Central Excise assessees during the last five years:

**Table 1.7: Tax base in Central Excise**

Year	No. of registered assessees	% growth over previous year	No. of assessees who filed return	% age of assessees who filed return
FY11	3,50,257	-	99,399	28
FY12	3,81,439	8.90	1,45,667	38
FY13	4,09,139	7.26	1,61,617	40
FY14	4,35,213	6.37	1,65,755	38
FY15	4,67,286	7.37	1,72,776	37

Source: Figures furnished by the Ministry

It is observed that there is a steady growth in number of registered assessees. However, only around 40 per cent assessees are filing returns. Ministry needs to look into the reasons for the same.

The data furnished by the Ministry this year related to registered assessees does not tally with the data furnished last year by the Ministry and reported in CAG's report no. 7 of 2015.

## 1.10 Budgeting issues in Central Excise

Table 1.8 depicts a comparison of the Budget Estimates and the corresponding actuals for Central Excise receipts.

**Table 1.8: Budget, Revised estimates and Actual receipts**

(₹ in crore)

Year	Budget estimates*	Revised budget estimates*	Actual receipts#	Diff. between actuals and BE	%age variation between actuals and BE	%age variation between actuals and RE
FY11	1,32,000	1,37,778	1,37,701	(+)5,701	(+)4.32	(-)0.06
FY12	1,64,116	1,50,696	1,44,901	(-)19,215	(-)11.71	(-)3.85
FY13	1,94,350	1,71,996	1,75,845	(-)18,505	(-)9.52	(+)2.24
FY14	1,97,554	1,79,537	1,69,455	(-)28,099	(-)14.22	(-)5.62
FY15	2,07,110	1,85,480	1,89,038	(-)18,072	(-)8.73	(-)1.92

Source: \*Union Receipts Budget and # Union Finance Accounts.

It is observed that in FY15, actual receipt of Central Excise have fallen short of Budget estimates by 8.73 per cent though variation reduced to 1.92 per cent in comparison of revised estimate.

## 1.11 Central Excise revenue forgone under Central Excise Act

Central Government has been granted powers under Section 5A(1) of the Central Excise Act, 1944 to issue exemption notifications in public interest so as to prescribe duty rates lower than the tariff rates prescribed in the Schedules. The rates prescribed by exemption notifications are known as the “effective rates”. Revenue forgone is defined to be the difference between the duty that would have been payable but for the exemption notification and the actual duty paid in terms of the said notification –

- In cases where the tariff and effective rates of duty are specified as ad valorem rates - **Revenue forgone= Value of goods X (Tariff rate of duty - Effective rate of duty)**
- In cases where the tariff rate is on ad valorem basis but the effective duty is levied at specific rates in terms of the exemption notification, then – **Revenue forgone = ( Value of goods X Tariff rate of duty) - (Quantity of goods X Effective rate of specific duty)**
- In cases where the tariff rates and effective rates are a combination of ad valorem and specific rates, revenue forgone is calculated accordingly
- In all cases, where the tariff rate of duty equals the effective rate, revenue forgone will be zero.

Besides the powers to issue general exemption notifications under Section 5A(1) *ibid*, the Central Government also has the powers to issue special orders for granting excise duty exemption on a case to case basis under circumstances of an exceptional nature, *vide* Section 5A(2) of the Central Excise Act. However, unlike general exemptions which form part and parcel of fiscal policy of the Central Government, the main object behind issue of exemption orders is to deal with circumstances of exceptional nature. As such, the duty forgone on account of issue of special exemption orders is not being calculated towards revenue forgone figures.

Table 1.9 depicts figures of Central Excise related revenue forgone during last five years as reported in budget documents of the Union Government.

**Table 1.9: Central Excise receipts and total revenue forgone**

(₹ in crore)			
Year	Central Excise receipts#	Revenue forgone*	Revenue forgone as % of Central Excise receipts
FY11	1,37,701	1,92,227	139.60
FY12	1,44,901	1,95,590	134.98
FY13	1,75,845	2,09,940	119.39
FY14	1,69,455	1,96,223	115.80
FY15	1,89,038	1,84,764	97.74

Source: \*Union Receipts Budget and #Union Finance Accounts.

It is observed that the Revenue forgone for FY15 in respect of Excise duties was ₹ 1,84,764 crore (₹ 1,77,680 crore as general exemptions and ₹ 17,284 crore as area based exemptions) which is 97.74 per cent of revenue from Central Excise. It is the first time in five years that revenue forgone is less than the total tax revenue.

## **1.12 Trade facilitation**

### **1.12.1 Creation of Large Taxpayer Units (LTUs)**

For the trade facility LTUs have been set up by the Department. An LTU is self-contained tax office under the Department of Revenue acting as a single window clearance point for all matters relating to Central Excise, Service Tax, Income Tax and Corporate Tax. Eligible Tax Payers who opt for assessment in LTUs shall be able to file their Excise return, Direct Taxes returns and Service Tax return at such LTUs and for all practical purposes will be assessed to all these taxes there under. These units are being equipped with modern facilities and trained manpower to assist the tax payers in all matters relating Direct and Indirect Tax/duty payments, filing of documents and returns, claim of rebates/refunds, settlement of disputes etc. For trade facilitation eight LTUs have been established.

### **1.12.2 Automation of Central Excise and Service Tax**

Automation of Central Excise and Service Tax (ACES) is the e-governance initiative by CBEC, Department of Revenue, Ministry of Finance. It is one of the Mission Mode Projects (MMP) of the Government of India under National e-Governance Plan (NeGP). It is a software application which aims at improving tax-payer services, transparency, accountability and efficiency in the Indirect Tax administration in India. This application is a web-based and workflow-based system that has automated all major procedures in Central Excise and Service Tax.

### **Tax administration in Central Excise**

#### **1.13 Scrutiny of Central Excise returns**

CBEC introduced self-assessment in respect of Central Excise in 1996. With the introduction of self-assessment, the department also provided for a strong compliance verification mechanism with scrutiny of returns. Assessment is the primary function of Central Excise officers who are to scrutinise the Central Excise returns to ensure correctness of duty payment. As per the manual for the Scrutiny of Central Excise Returns, a monthly report is to be submitted by the Range Officer to the jurisdictional Assistant/Deputy Commissioner of the Division regarding the number of returns received and scrutinised. Scrutiny is done in two stages i.e. preliminary scrutiny by ACES and detailed scrutiny, which is carried out manually on the returns marked by ACES or otherwise.

##### **1.13.1 Preliminary scrutiny of returns**

The purpose of preliminary scrutiny is to ensure completeness of information, timely submission of the return, timely payment of duty, arithmetical accuracy of the amount computed as duty and identification of non-filers and stop-filers.

Considering the fact that mandatory electronic filing of Central Excise returns had been introduced with effect from 1 October 2011, returns scrutiny through ACES should have stabilised at least by 2014-15. One of the main intentions behind introducing preliminary scrutiny online was to release manpower for detailed scrutiny, which could then become the core function of the Range/Group.

Table 1.10 depicts the performance of department in respect of preliminary scrutiny of Central Excise returns.

**Table 1.10: Preliminary scrutiny of Central Excise returns**

Year	No of returns filed in ACES	No. of returns marked for *R&C	% of returns marked for R&C	No. of returns cleared after R&C	No. of returns pending for R&C	% of marked returns pending correction
FY13	12,09,197	11,39,968	94.27	9,74,675	1,65,293	14.50
FY14	12,60,659	11,74,911	93.20	8,93,225	2,81,686	23.98
FY15	13,11,127	12,23,006	93.28	6,96,139	5,26,867	43.08

Source : Figures furnished by the Ministry

\*R&C – Review and correction

Data relating to FY13 and FY14 does not tally with similar data provided by the Ministry last year. The very high percentage of scrutinised returns being thrown up for R & C and resultant high number of returns pending corrective action are indicative of deficiencies in the ACES system. Marking so many returns for R&C would increase the workload of departmental officer though online system was aimed to reduce it. This is evident from the pendency of 43 per cent returns at the end of FY15 which is almost double of pendency at FY14. As R&C is carried out at range level and there are 2,518 ranges dealing with Central Excise, on an average, only 446 (FY15) R&C are to be carried out by a range in a year. Instructions may be issued to ranges to carry out R&C in all cases.

### **1.13.2 Detailed scrutiny of returns**

The purpose of detailed scrutiny is to establish the validity of information furnished in the tax return and to ensure correctness of valuation, availing of Cenvat credit, classification and effective rate of tax applied after taking into consideration the admissibility of exemption notification availed etc. Unlike preliminary scrutiny, detailed scrutiny is to cover only certain selected returns, identified on the basis of risk parameters, developed from the information furnished in the returns submitted by the taxpayers.

Table 1.11 depicts the performance of the department in carrying out detailed scrutiny of Central Excise returns.

**Table 1.11: Detailed scrutiny of Central Excise returns**

Year	No. of returns marked for detailed scrutiny	No. of returns where detailed scrutiny was carried out	Number of returns where detailed scrutiny was pending	Age-wise breakup of pendency		
				Returns pending for between 6 months to 1 year	Returns pending for between 1 to 2 year	Returns pending for over 2 years
FY13	50,039	38,900	10,144	8,108	1,684	240
FY14	10,665	6,894	3,771	3,787	796	116
FY15	DNP*	DNP	DNP	DNP	DNP	DNP

Source: Figures furnished by the Ministry

\*DNP - Data for FY15 was not provided

The number of returns marked for detailed scrutiny for FY14 has come down significantly compared to FY12 and FY13. The ministry needs to examine the drastic reduction in number of detailed scrutiny carried out in FY14.

It is further noticed that data for FY14 supplied by the Ministry was not only arithmetically incorrect but was also supplied to audit after obtaining the same from their field formations which led to considerable delays.

Data for FY15 was not provided. During performance audit on Cenvat credit, it has been noticed that out of 41 test checked Commissionerates, no detailed scrutiny was being conducted in 21 Commissionerates and reply of 20 Commissionerates was awaited.

### **1.14 Refunds**

Section 11B of the Central Excise Act, 1944 provides the legal authority for claim and grant of refund of any Central Excise duty. The term refund includes rebate of excise duty paid on excisable goods exported out of India as well as of excise duty paid on material used in the manufacture of goods exported out of India. Further, section 11BB of the Act stipulates that interest is to be paid on refund amount if it is not refunded within three month of the date of application of refund.

Table 1.12 depicts the details of refund related performance of the department during last three years.

**Table 1.12: Refunds in respect of Central Excise during the last three years**

(₹ in crore)

Year	OB plus claims received during the year		Disposals during the Year						Closing Balance	
			Refunds sanctioned during the year		Cases disposed of within 90 days	Delayed disposal	Cases where interest has been paid			
	No. of Cases	Amt.	No. of Cases	Amt.			No. of Cases	No of cases	No. of Cases	Interest paid
FY13	2,15,146	26,873	1,70,797	21,139	1,64,669	6,128	20	15	44,349	5,734
FY14	2,70,321	28,461	2,09,549	11,875	1,98,256	64,215	241	91	60,754	4,714
FY15	2,47,196	DNP*	2,04,353	DNP	DNP	DNP	DNP	DNP	42,843	30,714

Source: Figures furnished by the Ministry

\*DNP - Data not provided

It is observed on the basis of data available that despite the fact that there is a liability on department to pay interest on delayed refunds, department is not paying interest to the assessees in most of the cases. Board must ensure that the provisions regarding payment of interest on delayed refunds are implemented in right earnest.

Despite best pursuance of Audit, Ministry failed to provide certain figures as shown in table above, though same were provided by the Ministry last year. Data provided also does not match with figures provided last year. Data provided also seems incorrect as no of cases in closing balance for FY15 has decreased from FY14 but amount has increased by 600%.

### 1.15 Internal Audit

Modernisation of Indirect Tax administration in India is based on the Canadian model. The new audit system EA 2000 has four distinct features: scientific selection after risk analysis, emphasis on pre-preparation, scrutinising of business records against statutory records and monitoring of audit points.

Audit processes include preliminary review, gathering and documenting systems' information, evaluating internal controls, analysing risks to revenue and trends, developing audit plan, actual audit, preparation of audit findings, reviewing the results with the assessee/Range Officer/Divisional Assistant Commissioner and finalisation of the report.

The Audit framework consists of three parts. Directorate General of Audit and the field Commissionerates share the responsibility of administration of Audit. While the Directorate is responsible for collection, compilation and analysis of audit results and its feedback to CBEC to improve tax compliance and to gauge levels of client satisfaction, audit parties from

Commissionerates undertake audit in terms of EA 2000 audit protocol. In order to improve audit quality, CBEC took the assistance of Asian Development Bank in developing audit manuals, risk management manuals and manuals to train auditors in EA 2000 and CAATs, which prescribe detailed processes for conduct of audit. Table 1.13(a) depicts details of Central Excise units due for audit (during FY15) by audit parties of the Commissionerates vis-à-vis units audited.

**Table 1.13(a): Audits of assesseees conducted during FY15**

Slab of annual duty (PLA+Cenvat)	Periodicity	Number of units due	Number of units audited	Shortfall in audit (%)
Units paying CX duty >₹ 3 crore (Category A)	Annual	12,048	8,550	29.03
Units paying CX duty between ₹ 1 and 3 crore (Category B)	Biennial	6,717	3,888	42.12
Units paying CX duty between ₹ 50 lakh and ₹ 1 crore (Category C)	Once in five years	2,592	1,793	30.83
Units paying CX duty <₹ 50 lakh (Category D)	10 % every year	6,092	3,548	41.76

Source: Figures furnished by the Ministry

It is observed that during FY15, there was a huge shortfall in the Central Excise audits conducted, as compared with audits due, across all categories of units.

The results of the audit, conducted by the department, is tabulated in table 1.13 (b).

**Table 1.13(b): Amount objected and recovered during the year**

Slab of annual duty (PLA+Cenvat)	Amount (₹ in crore)	
	Amount of short levy detected	Amount of total recovery
Category A	2,013	546
Category B	222	113
Category C	198	39
Category D	113	58
<b>Total</b>	<b>2,546</b>	<b>756</b>

Source: Figures furnished by the Ministry

It is observed that amount of short levy detected and recovered in Category A units are significantly large than the non-mandatory units. The Ministry needs to ensure internal audit of all category A (mandatory) units.

### 1.16 Call book

Extant circulars on the subject envisage that cases that cannot be adjudicated due to certain reasons such as the department having gone in appeal, injunction from courts, contesting CAG audit objection etc. may be

entered into the call book. Member (CX), vide his D.O.F.No. 101/2/2003-CX-3, dated 3 January 2005, had emphasised that call book cases should be reviewed every month. Director General of Inspection (Customs and Central Excise) has reiterated the need for monthly review in his letter dated 29 December 2005 stating that review of call book may result in substantial reduction in the number of unconfirmed demands in call book.

Table 1.14 depicts the performance of the department in respect of call book clearance in Central Excise during recent years.

**Table 1.14: Call book cases pending on 31 March**

Year	Opening balance	New Cases transferred to call book during the year	Disposals during the year	Closing balance at the end of year	Revenue involved (₹ in Cr)	Age-wise break up of pendency at the end of the year		
						Less than 6 months	6-12 months	Over 1 year
FY13	30,542	6,753	8,152	29,143	45,267	4,609	2,958	21,576
FY14	30,966	9,624	4,126	36,464	64,356	6,179	3,419	26,866
FY15	35,617	9,552	8,846	36,323	65,765	4,841	2,276	29,206

Source : Figures furnished by the Ministry

It is observed that the pendency of cases in the call book is still very high indicating the need for close monitoring of the process of review of call book items. During FY15, the number of cases pending in call book had reached 36,323 involving revenue of 65,765 crore. It is further observed that the opening balance does not match with closing balance of previous years.

### 1.17 Arrears of Central Excise duties

The law provides for various methods of recovery of revenue demanded but not realised. These include adjusting against amounts, if any, payable to the person from whom revenue is recoverable, recovery by attachment and sale of excisable goods and recovery as arrears of land revenue through the district revenue authority.

Table 1.15 depicts performance of department in respect of recovery of revenue arrears.

**Table 1.15: Arrear realisation in Central Excise**

Year	Amount in arrears at the commencement of the year	Collection during the year	Arrears pending recovery at the end of the year	(₹ in crore)
				Collection as % of arrears at the commencement of the year
FY13	49,654	3,920	50,345	7.89
FY14	58,632	2,882	59,885	4.92
FY15	61,872	1,616	93,925	2.61

Source: Figures furnished by the Ministry

It is matter of concern that the collection as ratio of arrears is falling continuously. In FY15, it has fallen drastically to 2.61 per cent compared to 7.89 per cent in FY13. Although, falling ratio of collection of arrears have been repeatedly pointed out by audit but there is no sign of improvement. There is a need to strengthen the recovery mechanism of the department.

The data furnished by the Ministry related to arrears recovery does not tally with the data furnished last year by the Ministry and reported in CAG's report no. 7 of 2015.

### 1.18 Additional revenue realised because of Anti-evasion measures

Both, Director General of Central Excise Intelligence (DGCEI) as well as the Central Excise and Service Tax Commissionerates have well-defined roles in the task of detection of cases of evasion of Central Excise duty. While the Commissionerates, with their extensive database about units in their jurisdiction and presence in the field, are the first line of defense against duty evasion, DGCEI specialises in collecting specific intelligence about evasion of substantial revenue. The intelligence so collected is shared with the Commissionerates. Investigations are also undertaken by DGCEI in cases having all India ramifications.

Tables 1.16 and 1.17 depict the performance of DGCEI and the Commissionerates pertaining to the past three years.

**Table 1.16: Anti-evasion performance of DGCEI during last three years**

(₹ in crore)

Year	Detection		Voluntary payment during Investigation
	No. of cases	Amount	Amount
FY13	458	2,940	1,019
FY14	384	1,947	363
FY15	388	1,876	240

Source: Figures furnished by the Ministry.

It is observed that number of cases detected by DGCEI in FY15 increased marginally as compared to FY14 but voluntary payment during investigation have fallen. In comparison to FY13 it has reduced drastically.

**Table 1.17 : Anti-evasion performance of Commissionerates during the last three years**

(₹ in crore)

Year	Detection		Voluntary Payment during Investigation
	No. of Cases	Amount	Amount
FY13	2,150	3,415	482
FY14	2,222	2,790	450
FY15	1,750	2,456	300

Source: Figures furnished by the Ministry.

At the Commissionerates level also, number of case, amount involved in them and recovery during investigation has decreased in FY15, compared to FY14.

### 1.19 Revenue collection due to departmental efforts

Besides, the voluntary payment of Central Excise by the tax payers, there are various methods by which the department collects the revenue due but not paid by the taxpayers. These methods include Scrutiny of Returns, Internal Audit, Anti-Evasion, Adjudication etc.

The result of departmental efforts is tabulated in Table 1.18

**Table 1.18: Revenue recovered by departmental efforts**

(₹ in crore)			
Sl. No.	Departmental Action	Recovery during FY14	Recovery during FY15
1	Internal audit	717	411
2	Anti-Evasion	379	288
3	Confirmed Demands	462	1,248
4	Pre Deposit	178	307
5	Scrutiny of Returns	145	478
6	Recovery from Defaulters	709	1,298
7	Provisional Assessment	31	0
8	Others	196	197
	<b>Total</b>	<b>2,816</b>	<b>4,227</b>

Source: Figures furnished by the Ministry

Total Central Excise collection during FY15 is ₹ 1,89,038 crore out of which only ₹ 4,227 crore is collected due to departmental efforts which is only 2.24 per cent of total revenue. Further, it is noticed that revenue collection shown above under Internal Audit (₹ 411 crore) does not tally with amount shown in table 1.13 (b) (₹ 756 crore). Similarly, recovery shown above under anti-evasion (₹ 288 crore) does not tally with amount shown in tables 1.16 and 1.17 (₹ 540 crore).

It is further observed that though, data of detailed scrutiny for FY15 has not been provided and during performance audit on Cenvat credit, it has been noticed that out of 41 test checked Commissionerates, no detailed scrutiny was being conducted in 21 Commissionerates and reply of 20 Commissionerates was awaited, but recovery during FY15 over FY14 due to scrutiny of returns has been increased from ₹ 145 crore to ₹ 478 crore. Ministry needs to ascertain authenticity of all these figures.

## 1.20 Cost of collection

Table below depicts the cost of collection vis-a-vis the revenue collection.

**Table 1.19: Central Excise and Service Tax receipts and cost of collection**

Year	Receipts from Central Excise	Receipts from Service Tax	Total receipts	Cost of collection	(₹ in crore)
					Cost of collection as % of total receipts
FY11	1,37,901	71,016	2,08,917	2,072	0.99
FY12	1,44,540	97,356	2,41,896	2,227	0.92
FY13	1,75,845	1,32,601	3,08,446	2,439	0.79
FY14	1,69,455	1,54,780	3,24,235	2,635	0.81
FY15	1,89,038	1,67,969	3,57,007	2,950	0.83

Source: Union Finance Accounts of respective years

It is observed that despite automation and extensive use of ICT, cost of collection continues to show a rising trend.

## 1.21 Adjudication

Adjudication is the process through which departmental officers determine issues relating to tax liability of assessee. Such process may involve consideration of aspects relating to, inter alia, Cenvat credit, valuation, refund claims, provisional assessment etc. A decision of the adjudicatory authority may be challenged in an appellate forum as per the prescribed procedures.

Table 1.20 depicts an age-wise analysis of Central Excise adjudication.

**Table 1.20: Cases pending for adjudication with departmental authority**

Year	Cases pending as on 31 March		No. of Cases Pending for more than 1 year
	No.	Amount	
	(₹ in crore)		
FY13	16,801	16,020	1,093
FY14	20,428	21,734	3,142
FY15	27,425	23,765	4,984

Source: Figures furnished by the Ministry

It is observed that cases involving duty of ₹ 23,765 crore were pending as on 31 March 2015 for adjudication. It was also observed that 4,984 cases were pending for more than one year. Pendency of cases is increasing over the years. Ministry may initiate measures for adjudication of pending cases as large amount of revenue is blocked.

## 1.22 Appeal cases

Besides the adjudicating authorities, there are several other authorities including departmental appellate authorities, courts of law etc. where issues of law, interpretations etc. are considered. Besides, the department also

resorts to coercive recovery measures in many instances. Huge amounts of revenue thus remain outside the Consolidated Fund of India for substantial periods of time. Based on data furnished by CBEC, we have tabulated the pendency of cases at various forums in Table 1.21 (a).

Table 1.21(a): Pendency of Appeal in CX and ST

Year	Forum	Appeals pending at the end of the year					
		Details of party's appeals		Details of departmental appeals		Total	
		No. of Appeals	Amount Involved (Cr. ₹)	No. of Appeals	Amount Involved (Cr. ₹)	No. of Appeals	Amount Involved (Cr. ₹)
FY13	Supreme Court	760	1,429	1,632	5,743	2,392	7,172
	High Court	5,631	6,844	5,430	5,527	11,061	12,371
	CESTAT	35,964	63,278	15,832	12,010	51,796	75,288
	Settlement Commission	70	103	3	0	73	103
	Commissioner (Appeals)	23,233	7,103	2,965	558	26,198	7,661
	<b>Total</b>	<b>65,658</b>	<b>78,757</b>	<b>25,862</b>	<b>23,838</b>	<b>91,520</b>	<b>1,02,595</b>
FY14	Supreme Court	855	1,835	1,702	6,078	2,557	7,913
	High Court	5,856	9,359	5,505	6,764	11,361	16,123
	CESTAT	41,257	90,447	16,685	14,806	57,942	1,05,253
	Settlement Commission	109	230	4	1	113	231
	Commissioner (Appeals)	23,783	7,054	3,225	669	27,008	7,723
	<b>Total</b>	<b>71,860</b>	<b>108,926</b>	<b>27,121</b>	<b>28,318</b>	<b>98,981</b>	<b>1,37,244</b>
FY15	Supreme Court	815	2,202	1,754	6,428	2,569	8,630
	High Court	5,577	10,206	5,408	9,231	10,985	19,437
	CESTAT	44,710	1,05,905	16,719	14,240	61,429	1,20,145
	Settlement Commission	155	349	2	1	157	350
	Commissioner (Appeals)	25,617	6,272	3,676	655	29,293	6,927
	<b>Total</b>	<b>76,874</b>	<b>1,24,935</b>	<b>27,559</b>	<b>30,554</b>	<b>1,04,433</b>	<b>1,55,489</b>

Source: Figures furnished by the Ministry

It is observed that cases involving revenue of ₹ 1,55,489 crore were pending in appeals at various levels out of which ₹ 81,538 crore pertained to central Excise. The amount is increasing every year. Despite, a number of measures initiated by the Board, locking up of such a large revenue is a matter of concern.

Disposal of appeal cases relating to Central Excise and Service Tax in various forum is depicted below in Table 1.21(b):

**Table No. 1.21 (b): Breakup of cases decided during the year**

Year	Forum	Department's Appeal				Party's Appeal			
		Decided In favour of Deptt.	Decided Against the Deptt.	Remanded	% of Successful appeal of Deptt.	Decided in favour of party	Decided against party	Remanded	% of Successful appeal of party
FY13	Supreme Court	15	75	9	15.15	16	23	7	34.78
	High Court	102	486	97	14.89	473	1,007	269	27.04
	CESTAT	346	955	271	22.01	1,805	2,447	1,380	32.05
	Comm. (Appeals)	1,162	1,198	139	46.50	6,432	13,221	1,575	30.30
	<b>Total</b>	<b>1,625</b>	<b>2,714</b>	<b>516</b>	<b>33.47</b>	<b>8,726</b>	<b>16,698</b>	<b>3,231</b>	<b>30.45</b>
FY14	Supreme Court	21	82	5	19.44	14	33	3	28.00
	High Court	193	355	22	33.86	379	1,247	223	20.50
	CESTAT	248	1,407	151	13.73	2,314	2,125	1,574	38.48
	Comm. (Appeals)	1,141	1,248	31	47.15	7,064	12,888	697	34.21
	<b>Total</b>	<b>1,603</b>	<b>3,092</b>	<b>209</b>	<b>32.69</b>	<b>9,771</b>	<b>16,293</b>	<b>2,497</b>	<b>34.21</b>
FY15	Supreme Court	24	149	16	12.70	16	52	29	16.49
	High Court	230	712	130	21.46	447	1,397	206	21.80
	CESTAT	216	1,121	218	13.89	2,255	1,987	1,874	36.87
	Comm. (Appeals)	717	869	87	42.86	4,202	9,151	931	29.42
	<b>Total</b>	<b>1,187</b>	<b>2,851</b>	<b>451</b>	<b>26.44</b>	<b>6,920</b>	<b>12,587</b>	<b>3,040</b>	<b>30.69</b>

Source: Figures furnished by the Ministry

It is observed that success ratio of department's appeal against adjudication order has decreased from 33.47 per cent in FY13 to 26.44 per cent in FY15. The success ratio of departmental appeals is around 50 per cent when decided by Commissioner (Appeal) but in extra-departmental higher forums, it ranges from 15 per cent to 34 per cent. Appeals filed by the assesseees have better success rate in extra-departmental higher forums. There is a need to analyse the reasons of low success rate and effective measures may be taken to improve the success rate as well as to reduce the pendency of appeals.

### **1.23 Non-furnishing of data and discrepancy in data furnished by the Ministry**

The Ministry could not provide data related to detailed scrutiny of returns (refer paragraph 1.15.2) and disposal of refund cases (paragraph 1.17) for FY15 as format of data and responsibility to maintain the data were revised from November 2014. This indicates that continuity of maintenance of critical data is not ensured during change management in CBEC. Further, we have compiled this chapter based on data mainly obtained through CBEC. It is observed that same data obtained from different sources did not tally (paragraph 1.20) and in some instances, data furnished this year did not tally

with data furnished for last Audit Report no. 7 of 2015 (Para 1.9, 1.13 and 1.15.1). There is a need to improve the quality of data maintenance in respect of Central Excise.

#### **1.24 Audit efforts and Central Excise audit products - Compliance Audit Report**

Compliance audit was managed as per the Comptroller and Auditor General's (CAG) Audit Quality Management Framework, 2014 employing professional auditing standards of the Auditing Standards, 2<sup>nd</sup> Edition, 2002.

#### **1.25 Sources of information and the process of consultation**

Data from the Union Finance Account, along with examination of basic records/documents in DoR, CBEC, and their field formations, MIS, MTRs of CBEC along with other stake holder reports were used. We have nine field offices headed by Directors General (DGs)/Principal Directors (PDs) of audit, who managed audit of 781 (CX and ST) units in FY15.

#### **1.26 Report overview**

The current report has 64 paragraphs involving money value of ₹ 147.87 crore. There were generally four kinds of observations: incorrect availing/utilisation of Cenvat credit, non/short payment of Central Excise duty, effectiveness of internal control and other issues. The department/Ministry admitted audit observations in case of 47 paragraphs involving money value of ₹ 135.85 crore and reported recovery of ₹ 27.95 crore in 30 cases.

#### **1.27 Remedial action taken on the Compliance Audit Report**

Ministry furnished remedial action taken on all paragraphs of the compliance audit report and no ATN pertaining to previous Compliance Audit reports was pending from Ministry.

#### **1.28 Performance Audit Reports**

Performance audit, with the aim to seek an assurance that the systems and procedures were adequate and adhered to by the CBEC, was conducted. This year we have covered Performance audit on 'Working of Automation of Central Excise and Service Tax'. This report was laid in the Parliament on 18 December 2015.

## 1.29 Revenue impact of Audit reports

In the last five audit reports (including current year's report) we had included 440 audit paragraphs (Table 1.22) involving ₹ 683.20 crore.

**Table 1.22: Follow up of Audit Reports**

Year			FY11	FY12	FY13	FY14	FY15	Total
Paragraphs included	No.		159	87	62	68	64	440
	Amt.		158.00	69.32	182.90	125.11	147.87	683.20
Paragraphs accepted	Pre printing	No.	133	85	58	60	47	383
		Amt.	117.64	67.07	179.44	90.71	135.85	590.71
	Post printing	No.	15	2	-	1	-	18
		Amt.	34.76	8.34	-	0.36	-	43.46
	Total	No.	148	87	58	61	47	401
		Amt.	152.40	75.41	179.44	91.07	135.85	634.17
Recoveries effected	Pre printing	No.	67	48	36	28	30	209
		Amt.	46.60	24.72	21.29	27.44	27.95	148.00
	Post printing	No.	3	1	1	3	-	8
		Amt.	0.19	0.04	0.56	3.09	-	3.88
	Total	No.	70	49	37	31	30	217
		Amt.	46.79	24.76	21.85	30.53	27.95	151.88

Source: CAG Audit reports

Ministry had accepted audit observations in 401 audit paragraphs involving ₹ 634.17 crore and had recovered ₹ 151.88 crore.

## Chapter II

### Central Excise exemptions for SSI Units

#### 2 Introduction

##### 2.1 Exemption to Small Scale Industries in Central Excise

SSI units are governed under Notification No. 8/2003 dated 1 March 2003 (as amended from time to time). A unit irrespective of investment whose aggregate value of clearance was less than ₹ 4.00 crore in the previous year is entitled to duty exemption upto ₹ 1.50 crore provided it does not avail Cenvat credit on inputs and not utilize the Cenvat credit of capital goods for payment of duty and the goods manufactured should be covered under the notification.

##### 2.2 Audit objective

We conducted the thematic study to seek assurance that indirect tax administration is adequately placed to safeguard the interests of revenue relating to the small scale industries through:

- a) examination of adequacy of the extant provisions of the Rules, notification(s), Circulars, Manuals and other instructions read with the statutory provisions, in ensuring that the revenue due to the Government does in fact reach the Consolidated Fund without undue delay
- b) whether these provisions help to promote the intention/purpose of the Government in providing the exemption to SSI; and
- c) evaluation of adequacy of the monitoring mechanism in the department to receive and scrutinize returns of SSI units, detect cases of fraud and misuse and issue of 'Show Cause Notices'(SCN) and adjudication without delay.

##### 2.3 Scope and coverage

For conducting audit, we carried out examination of records at 33 selected Commissionerates, 64 Divisions and 134 Ranges. We checked minimum 20 ER-3 Returns in each Range.

The period covered in the study was 2011-12 to 2013-14. However, depending on issues involved, the study was extended to cover previous years wherever it was felt necessary.

##### 2.4 Audit findings

We noticed cases of non-payment/short-payment of duty, irregular availing/utilisation of Cenvat credit etc. Involving revenue of ₹ 9.70 crore.

The department had accepted (March 2015) the audit objections involving revenue of ₹ 3.54 crore and recovered ₹ 1.66 crore.

## 2.5 Revenue foregone and collected

The table below depicts the duty collected and foregone in respect of SSI units during the last three years in selected ranges:

Table 2.1

Year	No. of assesseees in the Ranges	No. of SSI units registered in the Ranges	No. of SSI units availing exemption	Duty foregone	Duty Payment by all units registered as SSI units		CE Duty paid from Cenvat credit as % of PLA payment
					Cenvat	PLA	
2011-12	12,406	5,483	2,355	275.92	419.47	253.76	165.30
2012-13	13,569	5,891	2,565	345.83	520.59	351.65	148.04
2013-14	14,834	6,232	2,739	370.63	611.22	393.57	155.30

The above data shows that less than 50 per cent of the assesseees registered as SSI units in the selected ranges are actually availing the benefit of the SSI exemption. It is noted that eligibility for SSI exemption has been last revised on 1 April 2005 from previous year turnover of ₹ three crore to ₹ four crore and SSI exemption limit has been last revised on 1 April 2007 from first clearance upto ₹ one crore to ₹ 1.5 crore.

It is further observed that SSI manufacturer of intermediate goods is not benefited out of the scheme. As under the present Cenvat credit scheme, the manufacturer paying duty on its clearances is eligible to avail and utilise Cenvat credit on the inputs purchased whereas the SSI manufacturer can not avail the Cenvat credit on its inputs thereby raising its manufacturing cost. An illustrative example depicting the sale of goods is given below:

Table 2.2

1 <sup>st</sup> Stage Manufacturer	Input Cost	Duty	Cenvat credit	Effective Input Cost	Value Addition	Selling Price	Duty	Effective Selling Price
SSI Units	100	10	0	110	20	130	0	130
Non – SSI	100	10	10	100	20	120	12	132
2 <sup>nd</sup> Stage Manufacturer	Input Cost		Cenvat credit		Effective Input Cost			
SSI Units	130		0		130			
Non – SSI	132		12		120			

It is observed that effective selling price of SSI unit is lesser than non SSI unit if the goods are sold to consumers. But if the SSI units are selling its goods to another manufacturer than the effective input cost for second stage manufacturer becomes costlier due to non-availability of Cenvat credit.

The Ministry in its reply stated (September 2015) that it is normal aberration of threshold based exemption. Audit is of the view that the Ministry may take steps to address the aberration.

## **2.6 Inadequacy of monitoring mechanism**

### **2.6.1 Non-registration and non-filing of declaration in Annexure-4 by SSI units**

a) Unit availing SSI benefit has to take Central Excise registration on crossing the specified exemption limit of value of clearance of ₹ 1.50 crore.

Audit examination of details of annual manufacturing accounts furnished in Form 13 to the Commercial Taxes Department and data available with the Industries department revealed non registration by 73 Units on crossing the specified exemption limit in Calicut and Trivandrum Commissionerate. Audit also noticed non-registration by 37 Units engaged in the manufacture of fertilizer (dutiabale since 1 March 2011) in Cochin, Calicut and Trivandrum Commissionerates during 2010-11/2011-12. It was also noticed that 27 units manufacturing plywood in the jurisdiction of Perumbavoor Range in Cochin Commissionerate had not taken registration with the department.

Similarly, Audit examination of details of annual turnover of manufacturers furnished by the Commercial Tax Department with the details furnished by the Ranges selected in Chennai II Commissionerate<sup>8</sup> and Chennai IV Commissionerate<sup>9</sup> and cross verification with the Assessee Master provided by the CBEC in Electronic Accounting System in Excise and Service Tax, revealed that 56, 47 and 40 assesseees for the year 2011-12, 2012-13 and 2013-14 respectively had registered with the Commercial Tax Department but had not registered with the Central Excise Department after crossing the specified exemption limit of value of clearances of ₹ 1.50 crore.

Out of the above, eighteen assesseees had not registered themselves with the Central Excise Department even though their value of clearance had crossed ₹ 1.50 crore for all the three years of 2011-12, 2012-13 and 2013-14 indicating slackness of the Department in widening the tax base.

When we pointed this out (June 2015), the ministry accepted (September 2015) the audit objection in some cases and reported no irregularity in few cases. Investigation is in progress in most of the cases and in the case of M/s Jews Agro Services Centre, Kollam reported recovery of ₹ 14.81 lakh.

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<sup>8</sup> Padi, Ambatur-II, Range IV-A and Range IV-B

<sup>9</sup> Thirumudivakkam-I and II, Perungudi and Palavakkam

b) Notification No.36/2001-CE (NT), dated 26 June 2001 exempted units, having annual turnover below specified limit of ₹ 90 lakh, from registering with the department effective from 1 July 2001. However, such units are required to file a declaration in form Annexure-5, once the value of their clearance reaches the specified limit.

In Audit, as cross-verified from Sales Tax Department, non-filing of declaration in eight cases were noticed in Noida, Lucknow , Belapur Commissionerate and three cases of wrong declaration were noticed in Ahmedabad II Commissionerate.

When we pointed this out (June-July 2014), the ministry accepted (September 2015) the audit objection in eight cases and stated that SCNs are being issued. In three cases no irregularity was found.

### **2.6.2 Filing of Returns**

Rule 12 of the Central Excise Rules, 2002 stipulates filing of returns by every assessee in the form specified by the department. Sub rule 3 of Rule 12 of the Rules *ibid*, prescribes scrutiny of Return by proper officer to ensure correctness of duty assessed by the assessee. Scrutiny of returns, identification of non/belated filers and initiating follow up action is the statutory function of the department. Interest on delayed payment of duty is leviable under Section 11AA of the Central Excise Act, 1944. General penalty up to five thousand rupees is imposable under Rule 27 for non-submission or belated submission of returns.

#### **2.6.2.1 Non/Delayed filing of ER-3 Returns**

Rule 12(1) of the Central Excise Rules 2002, stipulates that every SSI unit availing exemption shall pay the duty by 6<sup>th</sup> in the case of e-payment of the month following the quarter except March (For March by 31<sup>st</sup> March) and file a quarterly return (Form ER-3) within 10 days after the end of the quarter to enable the department to assess levy and collection of duty. As per rule 27 of Central Excise Rules, 2002, a breach of these rules shall, where no other penalty is provided herein or in the Central Excise Act, 1944, be punishable with a penalty which may extend to five thousand rupees.

The details of Non/Stop filers and delayed filers of ER-3 returns obtained from 134 selected Ranges. Audit noticed that there were 527 cases of non-filing and 1,790 cases of late-filing of ER-3 returns by SSI units during the period of our audit. The Department had neither taken any action nor imposed any penalty which could have been upto ₹ 26.35 lakh in case of non-filing and ₹ 89.50 lakh in case of late-filing of returns. The slackness of monitoring mechanism was pointed out (September 2014).

The Ministry in its reply (September 2015) accepted the audit objection in most of the cases and stated that rectificatory action is being initiated and reported recovery of ₹ 4.10 lakh as penalty.

### **2.6.2.2 Non/Delayed filing of ER-7 Returns**

Rule 12(2A) (a) of the Central Excise Rules 2002 stipulates that every SSI unit availing exemption shall submit a statement (Form ER-7) declaring the annual production capacity of the factory by 30th April of the succeeding financial year to enable department to verify correctness as to assessment, production capacity, electrical load utilised, etc. As per rule 27 of Central Excise Rules, 2002, a breach of these rules shall, where no other penalty is provided herein or in the Central Excise Act, 1944 be punishable with a penalty which may extend to five thousand rupees.

The details of Non/Stop filers and delayed filers of ER-7 returns obtained from 134 selected Ranges. Audit noticed that there were 3,282 cases of non-filing and 1,008 cases of late-filing of ER-7 returns by SSI units during the period of thematic study. The Department had neither taken any action nor imposed any penalty which could have been upto ₹ 1.64 crore in case of non-filing and ₹ 50.40 lakh in case of late-filing of returns.

The slackness of monitoring mechanism was pointed out (September 2014). The Ministry in its reply (September 2015) accepted the audit objection in most of the cases and stated that rectificatory action is being initiated and reported recovery of ₹ 6.04 lakh as penalty.

### **2.6.3 Non/Short payment of duty on crossing exemption limit of ₹ 1.50 crore**

Under the SSI scheme, a unit whose aggregate value of clearance was less than ₹ 4.00 crore in the previous year is entitled to duty exemption upto ₹ 1.50 crore provided it does not avail Cenvat credit facility. The manufacturer availing the notification has to satisfy certain conditions for availing the benefit and the goods manufactured should be covered under this notification.

Audit noticed non/short payment of duty in 21 cases in five Commissionerates<sup>10</sup> where clearances crossed the exemption limit. The total duty not paid in such cases amounted to ₹ 1.40 crore which was recoverable with interest of ₹ 27.43 lakh.

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<sup>10</sup> Chennai II, Coimbatore, Cochin, Chandigarh I and Calicut

We have pointed this out in June-September 2014. The Ministry reported (September 2015) recovery of ₹ 18.51 lakh in seven cases. We await the Ministry's response to other cases (December 2015).

Audit is of the opinion that monitoring mechanism must be tightened to bring unregistered SSI units into tax net and also to ensure proper filing of returns.

## **2.7 Non-fulfilment of conditions for exemption**

Under the SSI scheme, the unit whose value of clearance was less than ₹ 4.00 crore in previous year are entitled to full exemption upto ₹ 1.50 crore in current financial year. All clearances from 1<sup>st</sup> April in chronological order have to be considered for the purpose of calculation of exemption limit of ₹ 1.50 crore.

### **2.7.1 Incorrect computation of exemption limit**

The clearances made for export are not included in the turnover of ₹ 4.00 crore for the purpose of deciding the eligibility for SSI exemption for next financial year. In the case of export of goods from the factory, the manufacturer has to file an application in ARE-I form to seek permission to export the goods from the department. Where the manufacturer does not export the goods on its own but through a merchant-exporter, the manufacturer receives a copy of CT-3 certificate from the merchant-exporter indicating the actual removal of the goods for exports.

Instances of incorrect computation of Exemption limit were noticed in three cases in two Commissionerates<sup>11</sup> which resulted in excess availing of exemption amounting to ₹ 20.31 lakh. One illustrative case is discussed below:

M/s Shivnegere Packaging Industries in Bangalore-I Commissionerate claimed exemption on goods cleared to Export Oriented Units during the period 2011-12 to 2013-14. It was noticed in Audit that exemption was claimed without furnishing the prescribed CT-3 certificates. If the exemption is disallowed, the aggregate value of clearances made by the assessee would exceed the exemption limit during the respective years. So, the assessee will not fall under the category of SSI and would be liable to pay duty amounting to ₹ 10.84 lakh along with applicable interest.

When we pointed this out (June-September 2014), the Ministry accepted audit objection in all the cases and initiated rectificatory action in all cases and reported recovery of ₹ 0.73 lakh.

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<sup>11</sup> Delhi I and Bangalore II

## 2.7.2 Incorrect availing of SSI exemption

The exemption contained in the notification shall apply subject to the conditions that the aggregate value of clearances of all excisable goods for home consumption by a manufacturer from one or more factories, or from a factory by one or more manufacturers, does not exceed rupees four hundred lakh in the preceding financial year.

Instances of incorrect availing of exemption were noticed in 11 cases in eight Commissionerates<sup>12</sup> which resulted in excess availing of exemption amounting to ₹ 1.83 crore. Few cases are discussed below:

a) M/s Technico Laboratory Glassworks in Chennai IV Commissionerate, availed duty exemption on first clearances of ₹ 1.50 crore during 2013-14. It was noticed in Audit that total clearances of goods including value of goods cleared with nil rate of duty other than for exports was in excess of ₹ 4.00 crore during the previous year 2012-13. The incorrect availing of duty exemption amounted to ₹ 3.09 lakh.

When we pointed this out (July 2014), the Ministry accepted the audit objection (September 2015) and reported recovery of ₹ 3.65 lakh including interest.

b) M/s B.M. Packaging Machines, Mohali in Chandigarh-I Commissionerate, an SSI unit manufacturing soap packing machines, had two more units at Mohali and Baddi (H.P). The aggregate value of clearances of all three units was ₹ 4.32 crore and ₹ 6.39 crore during 2011-12 and 2012-13 respectively. The assessee however availed SSI exemption during the years 2012-13 and 2013-14. Thus there was incorrect availing of duty exemption amounted to ₹ 37.08 lakh.

When we pointed this out (October 2014), the Ministry accepted the audit objection (September 2015) and stated that SCN for ₹ 88.83 lakh covering the period 2010-11 to 2014-15 has been issued.

c) M/s MJR Components Pvt. Ltd in Faridabad Commissionerate, manufacturing and clearing motor vehicle parts availed SSI exemption of ₹ 15.35 lakh, ₹ 18.04 and ₹ 18.21 lakh during the years 2011-12, 2012-13 and 2013-14 respectively. The assessee had another unit under the same management - M/s Nehra Metal Component Pvt. Ltd at Faridabad. The aggregate value of clearances of both the units exceeded ₹ 4.00 crore during the years 2011-12 to 2013-14. The duty exemption of ₹ 51.60 lakh was therefore not correct.

Reply of the Ministry is awaited (December 2015).

<sup>12</sup> Chandigarh I, Chennai IV, Cochin, Faridabad, Noida, Jaipur I, Thane I and Kolkata II

d) M/s DNV Industrial Systems Pvt. Ltd in Noida Commissionerate, had two units in Noida. The aggregate turnover of both units as per the Balance Sheet for the year 2011-12 was ₹ 4.12 crore. However, the assessee availed SSI exemption for ₹ 18.54 lakh during 2012-13 which was incorrect.

Reply of the Ministry is awaited (December 2015).

When we pointed this out (June-October 2014), the Ministry accepted the audit objection in five cases involving revenue of ₹ 93.80 lakh and reported the recovery of ₹ 4.01 lakh. We await the Ministry's response in remaining six cases (December 2015).

## **2.8 Cenvat credit**

### **2.8.1 Incorrect availing or utilization of Cenvat credit**

We noticed 74 instances in 20 Commissionerates<sup>13</sup> of incorrect availing/utilization of Cenvat credit, non-reversal of Cenvat credit, availing of Cenvat credit on invalid documents etc. amounting to ₹ 1.16 crore. The Ministry accepted the audit objection in 65 cases involving revenue of ₹ 1.02 crore and reported recovery of ₹ 53.26 lakh. A few cases are illustrated below:

In terms of Rule 11(2) of Cenvat Credit Rules, 2004 a manufacturer who opts for exemption from the whole of duty of excise leviable on goods under a notification based on the value or quantity of clearance in a financial year and who availed Cenvat Credit on inputs or input services before such option is exercised, shall be required to pay an amount equivalent to Cenvat credit in respect of inputs lying in stock or in process or contained in final products lying in stock on the date when such option is exercised and after deducting the said amount, the balance, if any, still remaining shall lapse.

a) M/s Western Metaflux Pvt. Ltd. in Thane-I Commissionerate, availed SSI exemption during the year 2012-2013 and 2013-14 and availed Cenvat facility for payment of duty after crossing the threshold exemption limit. It was observed from the input Cenvat credit register and corresponding invoices of 2011-12 that the assessee had availed and utilized the Cenvat credit in respect of inputs lying in the stock as on 31 March 2012. Further, as per Balance sheet, the value of inputs lying in the stock as on 31 March 2012 was ₹ 16.89 lakh. However, the assessee had not paid an amount equivalent to Cenvat credit availed on these inputs. The similar observation was noticed for the year 2013-14.

<sup>13</sup> Bangalore I, Bangalore II, Belapur, Calicut, Chandigarh I, Daman, Delhi I, Guwahati, Kolkata III, Kolkata V, Noida, Pune I, Raipur, Rajkot, Thane I, Ahmedabad II, Cochin, Trivandrum, Coimbatore and Jaipur I

When we pointed this out (May 2014), the Commissionerate accepted the audit objection (May 2014) and reported recovery of ₹ 1.18 lakh for the year 2011-12 and 2012-13.

b) M/s Sathyam NE Wire Products Ltd. in Guwahati Commissionerate, availed SSI exemption during the years 2011-2012 and 2012-2013 and availed Cenvat facility for payment of duty after crossing the threshold exemption ₹ 3.97 lakh and ₹ 8.16 lakh limit. As on 31 March 2012, in respect of inputs, work in progress (WIP) and finished goods lying in stock, Cenvat credit required to be reversed was ₹ 12.36 lakh as against the credit available in Cenvat account of the assessee was ₹ 8.38 lakh. Similarly as on 31 March 2013, the Cenvat credit to be reversed was ₹ 9.02 lakh, whereas the credit available in Cenvat account of the assessee was only ₹ 0.86 lakh. Thus there was short reversal of Cenvat of for the years 2011-2012 and 2012-2013.

When we pointed this out (September 2014), the Ministry stated (September 2015) that a SCN has been issued to the assessee.

c) As per Proviso to Rule 3(5) of the Cenvat Credit Rules, 2004, if capital goods on which Cenvat credit has been taken, are removed after being used, the manufacturer shall pay an amount equal to the Cenvat credit taken on the said Capital Good, reduced by the percentage points calculated by straight line method for each quarter of a year or part thereof from the date of taking the Cenvat credit.

On a scrutiny of Cenvat records of M/s Dobersun Products Pvt. Ltd. in Kochi Commissionerate, manufacturer of cement bricks, audit noticed that the assessee availed Cenvat credit on capital goods of ₹ 48.67 lakh in December 2010. They removed certain capital goods during March and April 2013 and reversed credit of ₹ 16.64 lakh as against the actual amount of ₹ 24.71 lakh. This resulted in short reversal of Cenvat credit of ₹ 8.07 lakh.

When we pointed this out (June 2014), the Ministry intimated (September 2015) the reversal of Cenvat credit of ₹ 8.07 lakh (August 2014).

## **2.9 Other topics**

### **2.9.1 Miscellaneous issues**

We noticed short/non-payment of duty, non-payment of interest in 36 cases in 16 Commissionerates<sup>14</sup>, due to various reasons such as duty assessed but not paid, difference of paid amount detail in ER-3 return and Cenvat

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<sup>14</sup> Ahmedabad II, Daman, Bangalore II, Bangalore III, Chennai II, Chennai IV, Cochin, Calicut, Delhi I, Kolkata V, Guwahati, Kolkata III, Noida, Lucknow, Thane I and Jaipur

accounts/PLA accounts of the assesses, non-availability of challan details on National Securities Depository Limited (NSDL) site, non-fulfilment of specified conditions of exports, incorrect rate of duty, non-inclusion of additional charges in assessable value, under valuation of clearance to related person, non-payment of additional duty on as such clearance of inputs, non-inclusion of debit note values etc. Duty involved in these cases was ₹ 1.21 crore.

We have pointed this out in June-September 2014, the Ministry accepted (September 2015) the audit objection in 24 cases involving revenue of ₹ 91.73 lakh and reported recovery of ₹ 61.35 lakh. We await the Ministry's response in rest of the cases (December 2015).

### 2.9.2 Lacunae in notification

(i) In the SSI scheme, benefit of duty exemption on clearance upto ₹ 1.50 crore is given to rural SSI unit irrespective of the fact whether the clearance is of own/unbranded goods or the goods bearing the brand name or trade name of another person. But for urban SSI unit the duty exemption benefit is given only on clearance of own/unbranded goods. Thus giving boost to SSI unit in rural area. However, for determining the eligibility limit of ₹ 4.00 crore for granting the SSI benefit next year, value of all the clearances made by the rural SSI unit is taken into the account whereas in the case of urban SSI unit only the value of clearance of own/unbranded goods is taken. This puts the rural SSI unit in disadvantage position for being eligible to avail continuous SSI benefits vis-à-vis urban SSI unit.

M/s Tanmed Pharmaceuticals, in Chennai-IV Commissionerate, a SSI unit situated in urban area made clearance of goods bearing own brand name and other's brand name for a value of ₹ 1.01 crore (own brand) and ₹ 27.66 crore (other brand) in 2012-13 and for ₹ 1.26 crore (own brand) and ₹ 31.57 crore (other brand) in the year 2013-14. During 2012-13 and 2013-14 the clearance of own goods was less than ₹ 4.00 crore, the assessee continued to avail SSI exemption in the subsequent year 2013-14 and 2014-15, even though the aggregate value of home clearances was ₹ 28.68 crore and ₹ 32.83 crore in the years 2012-13 and 2013-14 respectively.

However, audit view is that had the SSI unit been in rural area it would not be eligible for SSI exemption during 2013-14, for the reason that the aggregate value in the previous year exceeded ₹ 4.00 crore and duty payable would have worked out to ₹ 15.64 lakh on the total assessable value goods cleared under own brand of ₹ 1.26 crore. By including the value of clearance of branded goods manufactured in rural area for reckoning the threshold limit of ₹ 4.00 crore for availing the benefit of SSI notification, the SSI units in rural

area are placed in a disadvantageous position for they would be losing the SSI status if the value of both branded and un-branded goods exceed ₹ 4.00 crore. There is a need to amend the notification to exclude the value of clearances of branded goods manufactured by SSI manufacturer in a rural area beyond ₹ 1.50 crore on par with the manufacturer in urban area manufacturing branded goods.

When we pointed this out (June 2015), the Ministry in its reply accepted (September 2015) that there is a need to amend the notification to exclude the value of clearance of branded goods manufactured by SSI, manufacturer in rural area beyond ₹ 1.50 crore on par with the manufacturer in urban area manufacturing branded goods.

The Ministry may intimate the steps taken to address the anomaly.

(ii) Under the SSI scheme, an SSI manufacturer is not entitled to credit of duty paid on inputs used in the manufacture and clearance of specified goods up to ₹ 1.50 crore of the first clearance for home consumption. However the notification does not prohibit availing Cenvat credit on input services used in the manufacture of the specified goods till the first clearance of ₹ 1.50 crore. This inconsistency in the Cenvat scheme needs rectification.

Audit observed that 12 assesses in five Commissionerates<sup>15</sup> availed both the Cenvat credit on input service amounting to ₹ 16.50 lakh from 2011-12 to 2013-14 and duty exemption on first clearances up to aggregate value of home consumption of ₹ 1.50 crore, which is an unintended benefit to the SSI manufacturers.

When we pointed this out (June 2015), the Ministry accepted the audit objection in seven cases involving revenue of ₹ 3.34 lakh and reported recovery of ₹ 3.09 lakh. Further, the Ministry did not accept the audit objection in five cases. Thus, the Ministry's reply in different cases on same issue is not consistent. Ministry needs to resolve the inconsistency.

## **2.10 Conclusion**

All registered SSI units are not availing the benefit of SSI exemption, as manufacturers of intermediate goods are not benefited out of the scheme. Rural SSI units are also at disadvantageous position in comparison to urban SSI units. There is a need to resolve the issues by suitable revision in the provisions of the scheme.

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<sup>15</sup> Noida, Ranchi, Guwahati, Pune I and Bangalore II

## Chapter III

### Functioning of Director General of Audit and its zonal units

#### 3.1 Introduction

Internal audit is one of the main compliance verification mechanism in the department, which involves selection of assessee units on the basis of risk parameters and scrutiny of records of the assessee to ascertain the level of compliance with the prescribed rules and regulations. Internal Audit is empowered, under Central Excise and Service Tax Rules, to access the records of the assessees under rule 22 of Central Excise Rules, 2002. Every Commissionerate has an Audit cell, manned by an Assistant/Deputy Commissioner. The audit is done by a set of internal audit parties (IAP) consisting of Superintendents and Inspectors.

In order to monitor, co-ordinate and guide the effective implementation of the new audit system, the CBEC has set up Directorate General of Audit as the nodal agency. Directorate General of Audit and the field Commissionerates share the responsibility of administration and conduct of internal audit of units paying Central Excise duty and Service Tax. While the Directorate is responsible for collection, compilation and analysis of audit findings and its feedback to Central Board of Excise and Customs (CBEC) to improve tax compliance and to gauge levels of client satisfaction, audit parties from Commissionerates undertake audit in terms of internal audit protocol. In order to improve audit quality, CBEC took the assistance of Asian Development Bank in developing audit manuals, risk management manuals and manuals to train auditors in internal audit and Computer Aided Audit Tools (CAATs).

#### 3.2 Organization

The Directorate General of Audit (DGA) headed by Director General was created in July 2000 with headquarters at New Delhi. The Organization was expanded in November 2002 with the implementation of cadre restructuring when seven zonal units were created at Ahmedabad, Bangalore, Chennai, Delhi, Hyderabad, Kolkata and Mumbai each headed by an Additional Director General (ADG). Every zonal unit of DGA has area wise jurisdictional control over zonal units of Chief Commissioner and Commissionerates there under.

After restructuring in 2014, separate Audit Commissionerate have been assigned the work of Internal Audit by taking it out of purview of functional Commissionerates. However, functioning of DG (Audit) to monitor the internal audit function of the department has not been changed.

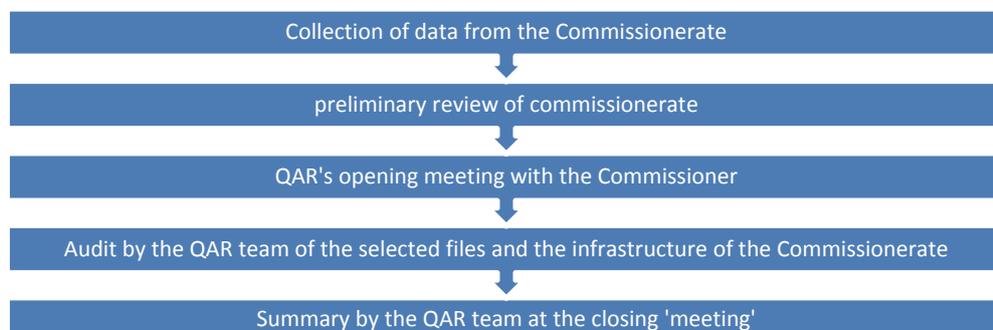
### 3.3 Functions and process:

The functional responsibilities of the Directorate have been delineated in the Charter of Functions approved by the Central Board of Excise and Customs (CBEC) through their letter F.No. 206/13/2000-CX.6 dated 30<sup>th</sup> January 2002. Directorate is to oversee the creation and institutionalization of a credible audit system. On one hand, it aids and advises the Board in policy formulation and on the other hand, it guides and provides functional direction in planning, co-ordination, supervision and conduct of audits to the field formations.

DG (Audit) is entrusted with assessment of quality of audits performed by Central excise and Service tax officers. Zonal Additional Director Generals (ADGs) are responsible for the actual conduct of Quality Assurance Review (QAR) in various Commissionerates in their respective zones. Detailed instructions to conduct QAR are prescribed in 'Manual for Quality Assurance Review' (Manual).

Information regarding audits carried out by Commissionerates by Chief Commissioners is collected from 104<sup>16</sup> Commissionerates across India through an annual proforma. Based on analysis of these proforma, DG (Audit) sends review teams to assess the quality of audit and to prepare Quality assurance report based on their assessment. Based on certain parameters such as selection of units for audit, evaluation of internal controls, audit verification, working papers, audit report preparation and timeliness and follow up, the Commissionerates are assigned grades from A to E (Excellent to Below average).

DG (Audit) then prepares an Annual report which also includes the grading of the assessed Commissionerates on audit performance. The review process is diagrammatically represented as follows:



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<sup>16</sup> 93 central excise, 07 service tax and 04 LTU Commissionerates

### **3.4 Audit Objectives**

This audit on “Functioning of Director General of Audit and its zonal units” was conducted to assess -

- i. Effectiveness of Directorate’s advice to CBEC in policy formation and to provide functional directions in conduct of audits to the field formations.
- ii. Effectiveness in following instructions and procedure framed under manual of QAR.
- iii. Improvements consequent to issue of QAR
- iv. Efficiency of human resources deployed for review of the Commissionerate.
- v. Existence of prompt and adequate follow-up of audit observation of internal audit.

### **3.5 Scope and Audit Coverage**

The scope of the audit was to evaluate the performance of the Directorate General of Audit (Headquarters office) and its seven zonal units in respect of the following two areas of its functions-

- (i) Quality Assurance Review of the Commissionerates, and
- (ii) Follow-up action on audit observations.

The office of DG (Audit), its seven zonal units and 57 Commissionerates falling under the jurisdiction of these ADGs were selected for study. The audit examined 25 sample files selected and verified for quality assurance exercise by ADG office. Sample files examined in seven zones were test checked in the selected Commissionerates to assess the authenticity of records maintained by DG audit and its subordinated offices. The period of coverage was from 2011-12 to 2013-14.

### **3.6 Audit findings**

The important audit findings under the two functions of DG Audit vis Quality Assurance Review of the Commissionerate and Follow-up action on audit observations are detailed below:

#### **3.6.1 Recommendation made by DG (Audit) to CBEC and field formation**

As per Board’s letter dated 30th January 2002, DG (Audit) is to oversee the creation and institutionalization of a credible audit system by giving advice to the Board and functional direction to field formations.

A test check of the files at DG (Audit) revealed that the recommendations were being sent to Board regarding audit norms to be followed by Commissionerate, suggestions for revision of CE and ST frequency norms, suggestions regarding improvement in final audit report format and minutes regarding formation of Audit Commissionerates. It was also seen that before finalizing the issues, suggestion/recommendation were also sought from Zonal Additional Director of Audit. After receipt of approval from CBEC the same were being circulated to all ADG office/Commissionerates.

The gist of recommendations was called for from DG (Audit). The department replied (May 2015) that the information will be compiled from the large number of files and will be provided as soon as possible.

Ministry stated (September 2015) that Directorate General is only meant to oversee the creation and institutionalisation of a credible audit system. It aids and advises the Board in policy formulation, guides and provides functional direction in planning, co-ordination, supervision and conduct of audits to the field formations. The gist of all recommendation submitted to the Board could not be prepared as there are voluminous records and there is no system to ascertain each and every letter sent to the Board and field formations. However, all live files were provided to Audit.

Audit is of opinion that Directorate should maintain records of important recommendations made to Board and field formations to evaluate proper follow up of such recommendations.

### **3.6.2 Discrepancies in the Part I of QAR report not pointed out by review teams**

The QAR process starts with collection of information from Commissionerates in Part I of proforma prescribed in Chapter-5 of QAR manual. This data is utilised as the base document to conduct a preliminary review by QAR team. The QAR team is required to verify the authenticity and correctness of the data in proforma provided by Commissionerates and recording the results in QAR report. Para 5.12 (3) of the manual states that data collected in part I of QAR is not only used to create and update national databank but is also used to identify trends of different aspect at national or zonal level.

Audit undertook scrutiny of proforma and compared the differences between Part 1 and the associated QAR reports. Audit observed instances where QAR teams have not pointed out the discrepancies in data submitted by Commissionerates in the QAR reports as detailed overleaf:

In Delhi ZU, in 11 cases there was difference in similar data i.e. number of paras raised and amount as depicted in statement D and statement G of part I of QAR for the period of three years 2011-12 to 2013-14.

Similarly, there was difference in number and amount of paras upheld in Bengaluru (10 cases) and Delhi Zones (5 cases) as depicted in statement G and statement H of part I of QAR during three years.

In Bengaluru zone, there was difference in 8 cases in number of units audited as depicted in statement D (column 8 to 12) and statement E (column 3) of part I of QAR during three years.

When we pointed this out (September 2014 and October 2014), Delhi ZU replied (October 2014) that the disparity was due to paragraphs upheld by Monitoring committee meeting (MCM). The reply is not acceptable as data element i.e. no. of para raised by audit or no. of paras upheld were same, having no relevance of MCMs.

Bengaluru ZU replied (October 2014) that barring few cases, the differences were not significant.

Audit is of the view that discrepancy in data not only affect the ranking of Commissionerates, but also affect the decision making of top management. Board may issue suitable instructions to maintain and monitoring accuracy of data.

Ministry stated (September 2015) that the zonal units were being sensitised to point out the discrepancies in part I of QAR to the field formations.

### **3.6.3 Faulty Selection of assessee files by QAR teams**

One of the most important steps in determining the efficiency of QAR is the selection of files at random from the slab-wise list of assessee units audited by the Commissionerate during the financial year being assessed. The number of files selected should be in line with the number as prescribed in the QAR manual. As per Notes part III (2) of annexure 5.1 of the manual, the QAR team is required to select a minimum of 25 files randomly from 5 slabs<sup>17</sup> with at least 5 files in each of the three revenue slabs.

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<sup>17</sup> (i) Paying total duty (in cash+Cenvat credit)above ₹ 3 crore per annum  
(ii) Paying total duty (in cash+ Cenvat credit)between ₹ 1 crore and ₹ 3 crore per annum  
(iii) Paying total duty (in cash+ Cenvat credit) between ₹ 1 crore to 50 lakh per annum  
(iv) Paying total duty (in cash+ Cenvat credit) less than 50 lakh per annum  
(v) EOU

Audit observed that the file selection norms were not adhered to in QAR process of Kolkata<sup>18</sup> Ahmedabad<sup>19</sup>, Delhi<sup>20</sup> and Mumbai<sup>21</sup> zones by selecting files less than 25 or not selecting minimum five files from three slab.

In Hyderabad zone, ADG asked the Commissionerates to keep 5 files in each category ready for audit before approaching the Commissionerates, thereby undermining the objective of selecting the files randomly giving the Commissionerates opportunity to select files with better work.

When we pointed this out (between October to December 2014), Ahmedabad ZU (December 2014), Hyderabad ZU (December 2014) and Mumbai ZU (February 2015) accepted the audit observations whereas Kolkata ZU replied (December 2014) that the situation depends on the availability of the files in respective Commissionerates.

Reply of Kolkata ZU indicate casual approach in selecting the files, thereby compromising the effectiveness of QAR process.

Ministry stated (September 2015) that the zonal ADsG are being sensitised to be careful in selecting the files for QAR.

### 3.6.4(a) Inordinate delay in issue of QAR Report

As per para 5.11 of chapter 5 of the manual, QAR report should be finalized and communicated to the jurisdictional commissioner and DG (audit) within a month of conduct of review.

Audit observed that there was delay in issuing of QAR for the year 2011-12 to 2013-14 in all zones ranging from 01 to 193 days. Few significant delays are given below:

**Table 3.1 : Delay in issue of QAR reports**

zone	Range of delay	No of QARs where delay was more than two months from scheduled time		
		2011-12	2012-13	2013-14
Delhi	11-177 days	-	6	-
Hyderabad	4-127 days	4	4	4
Chennai	2-155 days	1	-	-
Mumbai	1-87 days	-	-	2
Ahmedabad	5-193 days	4	-	-
Kolkata	24-86 days	1	-	-

In Delhi zone, there was delay ranging from 11 to 177 days in issue of QAR from the stipulated time for the year 2012-13. Further, in respect of six

<sup>18</sup> Kolkata-VI, Kolkata-VII and Kolkata Service Tax Commissionerates

<sup>19</sup> Ahmedabad service tax and Vadodara-I Commissionerates

<sup>20</sup> Chandigarh-I Commissionerate

<sup>21</sup> Pune-I, Belapur and Thane-I Commissionerates

Commissionerates,<sup>22</sup> delay was more than two months from the stipulated time.

In Hyderabad zone, delay was ranging from 4 to 127 days during the period of observation. Further, there was delay of more than two months in respect of 12<sup>23</sup> cases.

In Chennai zone, delay was ranging from 2 to 155 days. In Madurai Commissionerate delay was of 155 days for the year 2011-12.

In Mumbai zone, delay was ranging from 1 to 87 days during three years. QAR for Commissionerate Mumbai-III and Pune-I was issued with delay of more than two months from the stipulated time during the year 2013-14.

In Ahmedabad zone, delay was in the range of 5 to 193 days. QARs in respect of four Commissionerates<sup>24</sup> were issued with delay of more than two months from the stipulated time during the year 2011-12.

When we pointed this out (between September 2014 and January 2015), Delhi ZU stated (October 2014) that there was no inordinate delay except in case of Chandigarh II which was due to inadvertently misplacing QAR file. The reply is not tenable as in other cases also there was inordinate delay.

ADG Mumbai (November 2014), Bengaluru (October 2014). Ahmedabad (November 2014) and Hyderabad (December 2014) replied that due to staff constraints and some additional information required from Commissionerates, there was delay in finalization of QAR. Reply from ADG Kolkata and Chennai was awaited (September 2015).

Audit is of the view that delay of two to six months is a matter of concern as late issuance of QAR further delays its compliance by the Commissionerates affecting the objectives of QAR process.

Ministry stated (September 2015) that due to inadequate manpower in the zonal units coupled with delay in response from the field formations in providing the information called for result in some delay in issuance of QAR report. However, the zonal units are being sensitised to issue the QAR without delay.

Ministry reply indicates that there were manpower constraints in zonal units even prior to restructuring of the department. After restructuring, 45

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<sup>22</sup> Chandigarh-I, II, Allahabad, Delhi-IV, Meerut-II and Ludhiana

<sup>23</sup> Hyderabad I(2012-13 and 2013-14), Hyderabad II (2011-12 and 2012-13), Hyderabad III (2012-13 and 2013-14), Hyderabad IV(2011-12), Viskhapatanam II (2013-14), Guntur(2011-12 and 2012-13), Tirupathi(2011-12 and 2013-14)

<sup>24</sup> Ahmedabad-III (CE), Ahmedabad-III (ST), Ahmedabad Service Tax and Jaipur-I (ST)

dedicated Audit Commissionerates have been formed and it is expected that in future, the QAR reports will be issued in time.

### **3.6.4 (b) Delayed communication of grading**

As per para 5.11 of the manual, quality assurance report along with grading, should be finalized and communicated to the jurisdictional commissioner, jurisdictional chief commissioner, and the Director General (Audit) within a month of conduct of the review. Grades are assigned to Commissionerates, based on audit performance.

Audit observed that in Delhi zone, QARs were finalized and forwarded to the concerned Commissionerate but the grades were forwarded to 19 Commissionerates with delay ranging between 13 days to 249 days for the years 2011-12 and 2012-13.

Though delay in 2013-14 was marginal and in few cases, however, there may be delay in other zones/Commissionerates also. Audit is of the view that grading should mandatorily be issued along with QAR report as a QAR report would not serve its purpose without the final result of the QAR process.

Ministry stated (September 2015) that due to inadequate manpower in the zonal units coupled with delay in response from the field formations in providing the information called for result in some delay in issuance of QAR gradings. However, the zonal units are being sensitised to issue the QAR without delay.

Ministry has not replied on issuing grading separately after QAR report, though as per Manual, it should be a part of QAR report.

### **3.6.5 Delay/non-submission of response to QAR by Commissionerates**

Paragraph 2.6B of the manual prescribes that the findings of QAR are summarized and presented to the commissioner at closing meeting. These are then drafted in the form of prescribed report and forwarded to the concerned commissioner, jurisdictional chief commissioner and the DG (audit). The commissioner is required to communicate his response within a month of receipt of QAR report.

Audit observed that in Delhi, Mumbai, Hyderabad, Bengaluru and Ahmedabad zones compliance reports were not received from many Commissionerates even after one to three years as detailed in table 3.2:

**Table 3.2 : No. of Commissionerates who did not submit compliance report**

Zone	2011-12	2012-13	2013-14
Delhi	9	11	11
Mumbai	13	10	11
Hyderabad	8	10	10
Bengaluru	-	-	2
Ahmedabad	10	10	9
Kolkata	-	-	1

In Delhi zone, out of 19 Commissionerates, 8 Commissionerates had not communicated their response to the findings in 2011-12, 12 Commissionerates failed to send their response in 2012-13 and 13 Commissionerates in the year 2013-14. No action was initiated by Delhi ZU to remind the defaulting Commissionerates of their failure to respond.

In Mumbai zone 13, 10 and 11 Commissionerates did not respond to QAR during the 2011-12 to 2013-14.

In Hyderabad ZU out of 10 Commissionerates, 8 Commissionerates did not respond to QAR Report and no reply on remedial action initiated was sent to ZU.

In Bengaluru zone, reply to QAR of 2012-13 Bengaluru ST Commissionerate had not been furnished and no action was initiated by the zone.

In Ahmedabad zone, 10, 10 and 9 Commissionerates did not responded to QAR during the years 2011-12 to 2013-14.

In Kolkata zone, Patna Commissionerate did not respond to QAR during 2013-14.

Audit also observed that in many cases where compliance reports were sent by the Commissionerates, there was delay in responding to QAR during the years 2011-12 to 2013-14 ranging 03 to 1051 days. Few significant delays are given below:

**Table 3.3 : No. of Commissionerates who submit compliance report with delay**

Zone	Range of delay	No of QARs where delay was more than two months from scheduled time		
		2011-12	2012-13	2013-14
Delhi	03-302 days	03	03	-
Chennai	65-300 days	-	04	09
Mumbai	38-1051 days	08	11	09
Bengaluru	30-569 days	02	02	02
Kolkata	107-285 days	01	01	-

When we pointed this out (between September 2014 and January 2015) Delhi ZU offered no comment on the issue (October 2014), which is indicative of a casual attitude to QAR process.

Chennai ZU (September 2014), Hyderabad ZU (December 2014) and Bengaluru ZU (January 2015) accepted the audit observations. Mumbai ZU replied (October 2014) that the Commissionerates have been repeatedly reminded to send the response. Kolkata ZU confirmed the facts of delayed compliance by the Commissionerate.

Lack of response to QAR reports by Commissionerates implies that remedial measures were not initiated in time to rectify the shortfalls in quality of audits pointed out in QAR, which defeats the objectives of the entire QAR exercise.

Ministry stated (September 2015) that zonal units issue reminders to the Commissionerates to provide response to QAR reports, but shortage of manpower in Commissionerates result in delay. However, the delay is likely to be reduced due to formation of separate Audit Commissionerates with dedicated staff.

### **3.6.6 Non-validation of data published in the Annual Report of DG audit**

As per chapter 1 of QAR manual, it is the primary function of the DG (Audit) to assess the quality of audits performed by central excise and service tax officers, report the findings so that best practices are disseminated and shortcomings come to attention for remedial action such as additional training etc. Based on QAR, DG audit compiles an annual report in which audit performance of the Commissionerates is published.

A test-check of data published in annual report for the years 2011-12 and 2012-13 revealed that there were discrepancies in figures between annual report published and QAR reports as detailed below:

There were differences in the number of mandatory units selected for audited and actually audited in Delhi and Hyderabad zones. For example, in Visakhapatnam Commissionerate, the figures of non-mandatory units selected for audit during 2012-13 and units actually audit had a difference of 587 units and 416 units respectively.

In Chennai Zone, annual reports for the year 2011-12 and 2012-13 with respect to LTU Chennai Commissionerates had difference in data i.e. no. of audits conducted, revenue impact and recovery. Also, in Annual report 2012-13, percentage of parameters of Trichy Commissionerate in respect of Central Excise and Service Tax both were recorded incorrectly and consequently grading of the Commissionerate was downgraded from to C from B in both the cases.

This shows that wrong figures were published in the annual report thereby doubting the correctness of published data.

Audit is of the view that DG Audit may get the draft of annual report verified by zonal ADGs to ensure authenticity of Annual report.

Ministry stated (September 2015) that the observation had been noted for future compliance.

### 3.6.7 Incorrect grading of Commissionerates in QARs

As per chapter 3 of QAR manual, the methodology and procedure of assigning grades to Commissionerates on the basis of QAR has specified 9 audit quality elements<sup>25</sup> for Central Excise and 5 for Service Tax.

Based on the QAR reports, audit performances of the Commissionerates are evaluated and grades based on parameters are assigned.

Audit test checked the grades awarded by ADGs in QARs and verified them with the relevant files in the Commissionerate. It was observed that percentage calculated for quality elements were arrived at incorrectly by ADGs, consequently lower/higher grades were awarded to Commissionerates as detailed below:

**Table 3.4 : Incorrect gradings to Commissionerates**

Zone	No. of Commissionerates	No. of cases where grades were wrongly assigned	Remarks
Chennai	4	9	Grades were downgraded in all cases
Bangaluru	5	18	Grades were upgraded in all cases
Hyderabad	3	18	Grading were upgraded in 12 cases and remained same in 6 cases

In Chennai ZU, in 9 cases QAR review teams had wrongly assigned lower marks against quality elements than was warranted thus downgrading the performance of Commissionerates of Coimbatore, Puducherry, Tirunelveli and Service Tax Commissionerate, Chennai.

On the other hand, in Bangaluru zone, in 18 cases, grades assigned by ADG were unwarrantedly higher because of more marks against quality elements.

<sup>25</sup> **Central Excise** - 1. Selection of units for audit 2.Preliminary/Desk Review 3.Evaluation of Internal Controls 4.Preparation of Audit Plan 5. Audit Verification 6. Technical Issues 7.Working Papers, Audit Reports and Follow up 8. Professional Conduct 9.Timeliness

**Service Tax** - 1. Planning of Audit 2.Conducting of Audit 3.Documentation of Working Papers 4. Finalisation and follow up of audit 5. Other functions

Thus, grades of Bengaluru-I, Belagavi, Thiruvananthapuram, Kochi and Kozhikode Commissionerates were pushed up elevating the performance of these Commissionerates.

In Hyderabad zone, in 12 cases higher grades were awarded while in 6 cases, grades were same though percentage marks awarded were higher.

When we pointed this out (December 2014), Hyderabad ZU replied (December 2014) that-(a) marks are not being awarded for some questions which may not be applicable (b) if detailed process and techniques used in detecting the paragraph were spelt out clearly, then weightage was being given. (c) Most of the queries are subjective in nature; hence interpretation of each officer scrutinizing the file may differ marginally, which in turn affected the marks awarded/grading eventually.

Reply of Hyderabad ZU is not acceptable as the parameters adopted by us as well as the DG(Audit) were the same.

Reply of Chennai and Bengaluru ZUs was awaited (September 2015).

Audit analysis of Commissionerates' performance against the same parameters and incorrect assessment of performance by ADGs indicate casual approach of the DG (Audit) to the whole QAR exercise.

Ministry re-iterated the reply of Hyderabad ZU (September 2015) stating that the main reason for difference in grading could be due to the fact that most of the queries for calculating the gradings are subjective in nature and hence interpretation of each officer scrutinizing the file may differ, which in turn affected the marks awarded/grading eventually. However, the zonal units are being sensitised to be careful/objective in calculating the gradings.

### **3.6.8 Non- publishing of grades of LTU Commissionerates in Annual Reports**

Audit also observed that the grades allotted to LTUs were not being reflected in annual reports, though they were being awarded by respective zones and thus not intimating the same to Board for performance evaluation and rectificatory action. In absence of depiction of grading in annual reports, performance of LTUs could not be commented upon. Analysis of QAR of Delhi LTU for the period 2011-12 and 2012-13 revealed that grading were 4.5 per cent and 7.2 per cent below the conformity level of 60 per cent which may be the reason that grade are not being reflected in annual reports due to poor performance of LTUs.

Ministry stated (September 2015) that LTU Commissionerates did not provide the details of audits conducted and hence same were not reflected in the

report. Two Audit Commissionerates for LTU audits have started functioning from 15.10.2015 and their audit results will be reflected in the annual report.

Ministry reply indicate casual approach of Board in respect of LTU audits despite the fact that LTU Commissionerates are meant for Large Tax Payer units keeping audit of high revenue units out of performance review.

### **3.6.9 Not attending of opening meeting by Additional Directors General of Audit**

As per para 5.4 of the QAR Manual, the review party should fix an opening meeting with the Jurisdictional commissioner at the beginning of the review, and discuss the scope and the expected time frame of the review. It is essential that the Additional Director General attends the opening meeting with the Jurisdictional commissioner.

Examination of relevant records revealed that there was no evidence on record showing that opening meetings had been attended by the Addl. Directors General of Audit of Chennai, Mumbai and Hyderabad zonal units during the period of review covered in audit.

When we pointed this out (between September to December 2014), Ministry stated (September 2015) that in routine course, ADG and in absence of them, the next senior officer attend the opening and closing meetings but no records of meeting are maintained as the same is not instructed in QAR manuals. However, the zonal ADsG are being sensitised in this regard.

Audit is of opinion that opening and closing meeting of QAR process is an important and integral part of the process and the same should be documented.

### **3.6.10 Insignificant improvement consequent to QAR**

Quality Assurance Reviews (QARs) are conducted to ensure full compliance with the standards set for the internal audit process. Based on the extent of the conformity to the process, Commissionerates are graded from A to E categories.<sup>26</sup>

In the comparative scrutiny of QAR gradings reflected in annual reports of DG (Audit) for the years 2010-11 to 2012-13 in respect of the 93 Commissionerates of Central Excise and 73 Commissionerates of Service Tax including composite Commissionerates, Audit observed the following:

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<sup>26</sup> A = Excellent (> 90%), B = Very Good (>80.01 – <90.00%), C = Good (>70.01 – <80.00%), D = Average (>60.01 – <70.00%), E = Below Average <60%

**Table 3.5 : Comparison of grades with previous years**

Duty/ Tax	Year of annual report	Number of Comm. which were downgraded	Number of Comm. whose grade stayed the same	Number of Comm. which showed improvement
Central Excise	2011-12 (comparing with 2010-11)	22	35	36
	2012-13(comparing with 2011-12)	29	39	25
Service Tax	2011-12 (comparing with 2010-11)	18	25	29
	2012-13(comparing with 2011-12)	21	27	25

From the above table, it is clear that during 2011-12 and 2012-13, 22 and 29 Commissionerates in respect of Central Excise and 18 and 21 Commissionerates in respect of Service Tax were downgraded vis-a-vis previous year grading, showing drop in performance of internal audit.

Ministry stated (September 2015) that Directorate General evaluates the qualitative as well as quantitative performance of audits conducted by the field formations. The field formations are not under the administrative control of the Directorate and the results of audit depend on various factors on quarterly basis as well as yearly basis.

Ministry's reply is indicative of casual approach in respect of the whole process. The main function of a performance evaluation is to find shortcomings in the process and suggesting improvement. Non-improvement or down-grading of performance indicates the ineffectiveness of performance evaluation process.

### **3.6.11 Shortfall in achievement of quantitative performance growth**

Effectiveness of internal audit is also reflected in terms of revenue recovered at the instance of internal audit. Audit observed that in many test checked Commissionerates recovery of revenue decreased in comparison of previous year. The details of some of Commissionerate where drastic reductions were noticed are tabled overleaf:

Table 3.6 : Shortfall in recovery

Zone	CX / ST	Year	No. of comm. where recovery increased	Range of increase	No. of comm. where recovery decreased	Range of decrease
Chennai	CX	2011-12	7	5% to 384%	4	18% to 73%
		2012-13	8	23% to 122%	3	6% to 76%
		2013-14	5	7% to 124%	-	-
	ST	2011-12	6	11% to 87%	3	35% to 41%
		2012-13	5	32% to 164%	4	12% to 28%
		2013-14	2	50% to 70%	2	10% to 31%
Hyderabad	CX	2011-12	8	22% to 309%	2	31% to 88%
		2012-13	5	9% to 792%	5	18% to 98%
		2013-14	8	4% to 308%	2	0.4% to 62%
	ST	2011-12	8	5% to 1633%	2	66% to 75%
		2012-13	8	51% to 113%	2	11% to 22%
		2013-14	6	3% to 161%	4	5% to 73%
Ahmedabad	CX	2012-13	2	27% to 35%	1	31%
		2013-14	3	14% to 35%	2	10% to 41%
	ST	2012-13	1	12%	4	26% to 63%
		2013-14	4	47% to 170%	1	40%
Delhi		2012-13	-	-	1	22%
Mumbai	CX	2011-12	3	18% to 135%	4	29% to 86%
		2012-13	5	22% to 740%	2	6% to 22%
		2013-14	5	22% to 1220%	2	1% to 56%
	ST	2011-12	2	73% to 143%	3	4% to 48%
		2012-13	3	18% to 110%	3	23% to 99%
		2013-14	4	37% to 13745%	2	10% to 16%

In 8 Commissionerates, i.e. Chennai III, Puduchery, Vishakhapatnam II, Bhubaneswar I, Hyderabad IV, Guntur and Vadodara, negative growth was more than 50 per cent. Though recovery was being mentioned in QARs, the reasons for decrease in recovery against the amount of the audit objection detected were not analyzed and recorded in QARs.

When we pointed this out (September 2014 to January 2015), Chennai ZU accepted (September 2014) the facts, while Ahmedabad ZU (January 2015) and Hyderabad ZU (December 2014) replied that QAR is assessing the qualitative aspect of audit and not the quantitative performance. The recovery aspect is not at all reflected in grading exercise. Even if, a Commissionerate makes a huge recovery or otherwise, the grading of the Commissionerate will not get affected. Reply from Delhi ZU was awaited (September 2015).

Audit is of the opinion that recovery based on audit observations is an important criteria as it reflect correctness and sustainability of audit

objections. In fact, large number of observations reported in CAG Audit Reports, wherein either the scheduled Internal Audit has not been carried out or if carried out then the lapse is not pointed out by Internal Audit wing of department. Most of such lapses detected by CAG Audit are very general in nature which can be easily identified by Internal Audit. So there is a need of including recovery as a performance evaluation criteria.

Ministry stated (September 2015) that QAR is designed to monitor the maintenance of quality standards and is not aimed at monitoring of amount by Commissionerates. However, the parameters for quantitative and qualitative evaluation of Audit performance are being revised and more weightage will be given to recovery.

### 3.6.12 Outstanding objections not settled

As per item 7 of para 5.8 of chapter 5 of QAR manual, QAR team has to examine the follow up of audit reports as corrective action can be ensured by prompt and adequate follow-up of audit observations. Mere issue of audit report without adequate and periodical follow-up would not serve any purpose.

Audit observed that in 27 Commissionerates, 1,553 paras were outstanding from one to three years as listed below :

**Table 3.7 : Paras outstanding for settlement**

Zone	Commissionerate	No. of paragraphs outstanding	Money value(₹ in lakh)
Hyderabad	Bhubaneswar-I CE	73	1,166.05
	Bhubaneswar-I ST	93	1,952.64
	Visakhapatnam ST	28	492.00
	Guntur ST	2	NA
Ahmedabad	Ahmedabad III CE	10	NA
	Ahmedabad III ST	7	NA
Delhi	Allahabad, Lucknow, Kanpur, Meerut I and II (CE)	534	13,903.06
	Allahabad, Lucknow, Kanpur, Meerut I and II (ST)	521	1,724.40
Kolkata	Patna ST	31	1,287.00
Bengaluru	Bengaluru-I	28	1,390.88
	Bengaluru-III	25	109.54
	Bengaluru ST	7	218.48
	Belagavi-CE	48	3,257.67
	Belagavi-ST	40	693.19
	LTU, Bengaluru-CE	1	-
	LTU, Bengaluru-ST	7	530.46
	Thiruvananthapuram (CE)	3	22.77
	Thiruvananthapuram (ST)	71	1,886.73
	Kochi (CE)	24	139.13
<b>Total</b>		<b>1,553</b>	<b>28,774.00</b>

Table 3.7 indicates that 1,553 paras are pending involving revenue of 287.74 crore.

When we pointed this out (between September 2014 to December 2014). Hyderabad ZU replied (December 2014) that it is not mandated to judge the process of liquidation of pending paras in the Commissionerate, it was impressed upon/advised to do so in general interest. Further, purpose of QAR is to assess as to whether the system are in place or not and nothing else.

The reply is not acceptable as without prompt and adequate follow-up, audit observations does not serve any purpose.

Ahmedabad Zone (September 2014) admitted the observation. The reply of Delhi, Kolkata and Bengaluru ZU was awaited (September 2015).

Ministry stated (September 2015) that details of outstanding objections noticed during QAR are brought to the notice of the field formations. Field formation would be suitably instructed.

### 3.6.13 Non-production of records to Audit

QAR is based on the review of Internal Audit files maintained by the Commissionerates. However, 15 Commissionerates in three zones failed to produced files, reviewed by the QAR teams during the three years, to audit as detailed below:

**Table 3.8 : Non-production of records to Audit**

Zone	Total no. of files demanded by audit	No. of files produced	No. of files not produced to audit
Delhi	597	143	454
Hyderabad	210	63	147
Ahmedabad	706	392	314

Thus, audit could not examine and comment on the efficiency of the QAR process.

Further, Service Tax Delhi Commissionerate failed to provide any record to audit stating that records were not available due to restructuring in the department. Besides the above Cochin (2011-12) Kozhikode (2013-14), Ranchi and Jamshedpur (2011-13) also failed to provide any records to audit.

Ministry stated (September 2015) that Directorate has no role to play in the matter as the Commissionerates are not under its administrative control. However, the observation of Audit will be conveyed to all field formations to produce records to Audit.

### **3.7 Conclusion**

QAR exercise is expected to monitor the performance of Internal Audit and to take necessary action for improvement of performance. Despite the fact that dedicated staff have been deployed for the process under DG (Audit) ,the intended objectives are not being met.

#### ***Recommendation No. 1***

Accuracy of data provided by the Commissionerates need to be ensured as same is utilised by top management for performance evaluation and policy formulation.

Ministry stated (September 2015) that the observation has been noted for future compliance.

#### ***Recommendation No. 2***

Time adherence for the issue of QAR report and compliance report from the Commissionerates should be ensured to avoid delay.

Ministry stated (September 2015) that the observation has been noted for future compliance.

## Chapter IV

### Tax Accounting and Reconciliation in Central Excise, Service Tax and Customs

#### 4.1 Introduction

The Central Board of Excise and Customs (CBEC) working under the Department of Revenue, Ministry of Finance is responsible for collection of Indirect Taxes. Tax Accounting and Reconciliation is a process to ensure that the revenue realised in respect of duty/tax is duly credited to Government Account and properly accounted for without any discrepancy.

##### 4.1.1 Tax Accounting

Union Excise Duties, Service Tax and Customs duties collected by the field formations under CBEC are classified under Major Head '0038-Union Excise Duties', '0044-Service Tax' and '0037-Customs' respectively. Refund and Drawback payments authorized by various departmental authorities are classified under the appropriate sub-heads 'Deduct-Refunds' and 'Deduct-Drawbacks, appearing under the prescribed Major and Minor Heads of accounts as given in the "list of Major and Minor Heads of Accounts of Central Receipts and Disbursements".

Assessees make payments of Central Excise Duty and Service Tax into a branch of nominated bank located within the Commissionerate exercising jurisdiction over it, through GAR-7 challans by means of cash/cheque/pay order etc. or through internet banking. Bank scrolls, containing details of challans are sent by receiving branches concerned to Pay and Accounts Offices (PAO), through their respective Focal Point Branches (FPB).

Customs duties are collected and Duty Drawbacks are paid through electronic mode with the help of Electronic Data Interchange (EDI) system. In some minor ports, Customs Duty is paid through challans in the nominated FPB.

##### 4.1.2 Reconciliation

Reconciliation of receipts is an important process of internal control. In Indirect Taxes, reconciliation of revenue receipts is being done at the following stages:

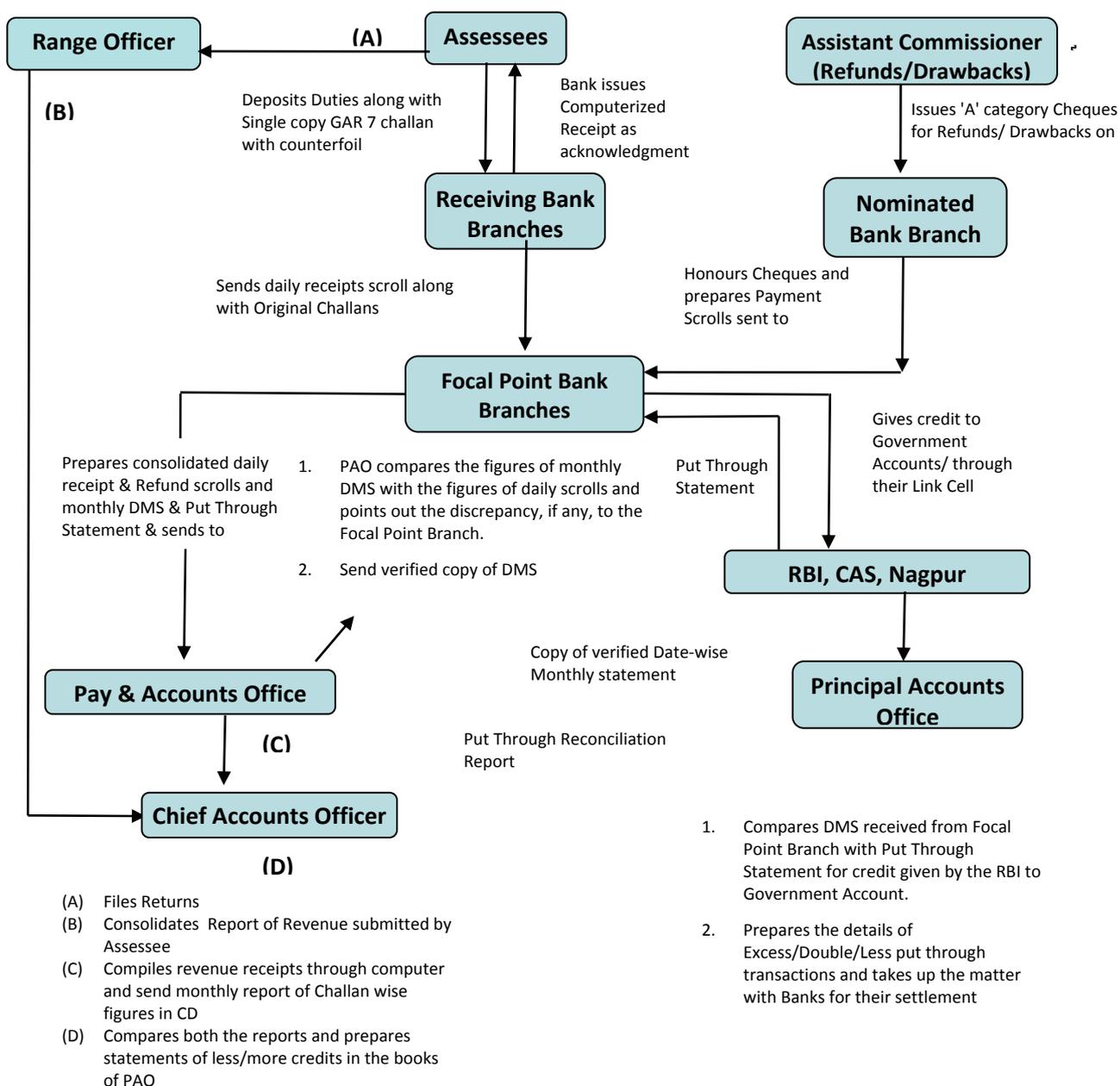
- (i) Reconciliation between the Receiving Bank Branch and FPB<sup>27</sup>
- (ii) FPB and PAO
- (iii) PAO and Chief Accounts Officer (CAO)

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<sup>27</sup> It is carried out by the banks. Department is not undertaking this reconciliation and Audit has also not examined the same

- (iv) FPB and Reserve Bank of India, Central Account Section (CAS), Nagpur
- (v) RBI and Principal Accounts Officer (Pr. AO) in the office of the Principal Chief Controller of Accounts (Pr CCA)
- (vi) Pr.A.O in Pr CCA and PAO

**Flow of accounts and reconciliation of revenue receipts with nominated banks in CBEC**



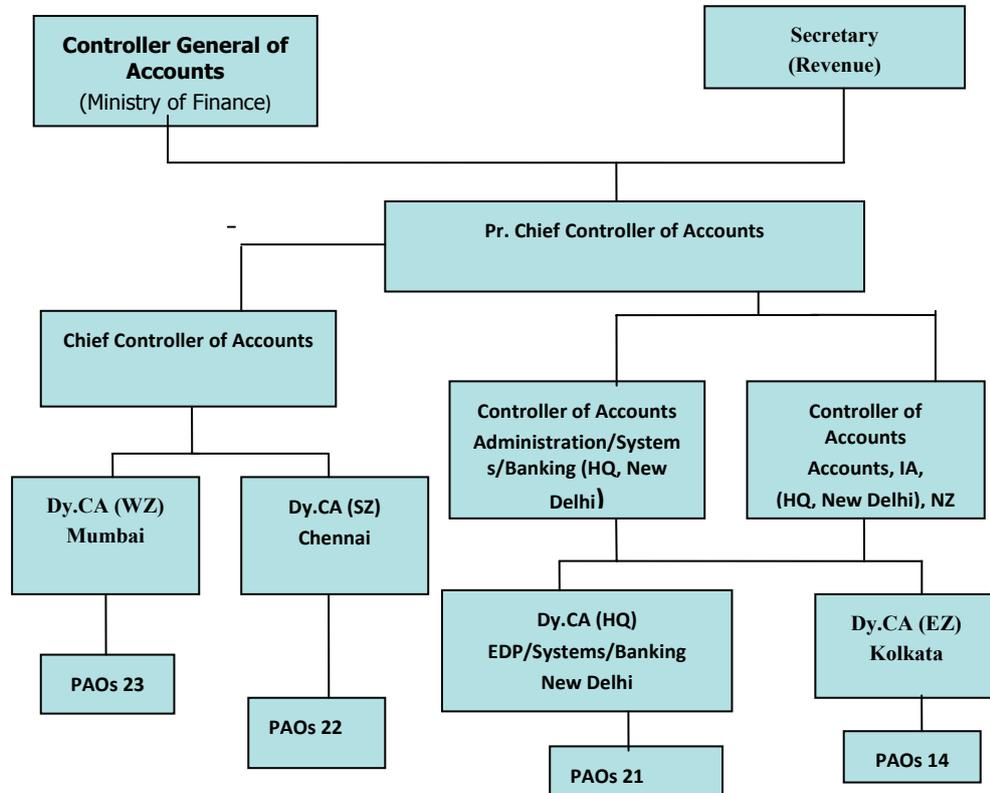
Source: Manual of Accounting of Indirect Taxes

**4.1.3 Organizational setup**

The Office of the Principal Chief Controller of Accounts (Pr CCA) is the head of the Accounting Organization set up in CBEC. It renders financial and

technical advice to CBEC on matters relating to collection of revenues and their accounting, prescribing banking arrangements and is responsible for accurate accounting of both expenditure and revenue (Indirect Taxes) of each Departmental Commissionerate through the PAOs located all over the country. At present there are 80 PAOs to assist Pr CCA. There are 817 Drawing and Disbursing Officers (DDOs) under the payment control of Pr CCA out of which 143 DDOs are having Cheque Drawing Powers and the remaining 674 DDOs are Non-Cheque Drawing and Disbursing Officers (NCDDOs) who submit their bills to Cheque Drawing DDOs or to the PAOs directly.

**Organizational Chart of Accounting Organization, CBEC**



Source: Manual of Accounting of Indirect Taxes

**4.1.4 Software being used by the department**

**EASIEST** - Electronic Accounting System in Excise and Service Tax (EASIEST) is a web based payment gateway launched by CBEC in 2007 enabling assesees to pay Central Excise duties and Service Tax online. It interfaces with the e-payment portals of the tax collecting banks and makes available accurate tax payment data from banks for revenue and tax payer accounting purposes.

**ACES** - Automation of Central Excise and Service Tax (ACES) is a software application which aims at improving tax-payer services, transparency, accountability and efficiency in the indirect tax administration in India. This application is a web-based and workflow-based system that has automated all major procedures in Central Excise and Service Tax.

**ICEGATE** - Indian Customs Electronic Commerce/Electronic Data interchange (EC/EDI) Gateway (ICEGATE) is a portal that provides e-filing services to the trade and cargo carriers and other clients of Customs Department (collectively called Trading Partner).

**P-CBEC** – It is a web-based application, aimed at gathering data from various sources and process it and generate consolidated reports by connecting all the field offices (PAOs) with the Central Server of Pr CCA, CBEC.

**COMPACT (REVACT)** – It is a software meant for receipt accounting in all the PAOs and two e-PAO Offices (one at Chennai for Central Excise and the other at Mumbai for Service Tax). At the PAO level it provides facility for accounting procedure to bring efficiency and accuracy in their functioning and provides information to higher levels of accounting systems for further processing.

#### **4.1.5 Why we chose this topic**

Tax Accounting and reconciliation is a mechanism for duly crediting revenue to Government Account with proper classification. After implementation of EASIEST in 2007, e-PAO was introduced in April 2010 for collection of e-payment of Central Excise Duties. Further e-reconciliation at the level of Range Officer was also introduced. In the light of these developments, we intended to examine the efficacy of the current structure of tax accounting and reconciliation system of CBEC.

#### **4.1.6 Audit Objectives**

Audit aimed to assess:

- i. Adequacy of rules, circulars, instructions and procedures in relation to tax accounting and reconciliation of Central Excise, Service Tax and Customs Duty
- ii. Compliance of statutory provisions and procedures in accounting and reconciliation of Central Excise Duty, Service Tax and Customs Duty
- iii. Effectiveness of monitoring and control mechanism.

#### **4.1.7 Scope and coverage of audit**

We selected 46 PAOs, 63 Commissionerates working under these PAOs and four Ranges under each selected Commissionerate for coverage under Audit

of Tax Accounting and Reconciliation. The period of coverage was 2011-12 to 2013-14 and the field audit was conducted between July and November 2014.

Audit observations contained in this chapter related to PAOs as well as Commissionerates. Ministry furnished its reply in respect of Commissionerates of Central Excise, Service Tax and Customs. Reply in respect of observation relating to PAO was awaited from Pr CCA (December 2015).

#### **4.1.8 Audit Criteria**

Audit criteria was based on the functions and responsibilities depicted in the following Acts, Rules, Manuals and Instructions:

- i) Manual of Accounting of Indirect Taxes of CBEC, 2013
- ii) Suspense Manual of Controller General of Accounts (CGA)
- iii) Civil Accounts Manual issued by the Ministry of Finance, CGA, 2007
- iv) Central Excise Rules, 2002
- v) General Financial Rules, 2005
- vi) Receipt and payment Rules, 1983
- vii) Finance Act, 1994
- viii) Customs Act, 1962
- ix) Notifications, Circulars, Instructions, Guidelines, etc. issued by the CBEC from time to time

**PART - A**  
**Central Excise**

**4.2 Accounting of Central Excise Duty**

Proper accounting of Central Excise duty is necessary to have fair picture of duty collection. We observed the following inconsistencies in this regard.

**4.2.1 Reconciliation of Revenue Receipts**

Proper reconciliation of revenue receipts with well defined procedures is necessary for ensuring that revenue is duly credited to Government Account. On review of reconciliation procedure, certain lacunae in the system as well as inconsistencies in procedures were observed which are discussed in the following paragraphs.

**4.2.1.1 Reconciliation of Central Excise revenue by Commissionerates of Central Excise with that booked by PAOs**

As per Para 12.10.1 of the Manual, the PAOs will provide an assessee-wise collection report to the CAO of the Commissionerate concerned. The CAO will distribute the same to the concerned Division/Range Officers. The Range Officers in turn compare it with the returns submitted by the assessees and prepare a monthly statement for submission to CAO as directed vide CBEC's instruction No. 224/37/2005-EX-6 dated 24 December 2008. The CAO notes down the discrepancies as 'Less Credit' and 'More Credit' and forwards a copy to PAO. The CAO undertakes the necessary correspondence with the Range Officers concerned in case of 'More Credit' and PAO interacts with the FPB in case of 'Less Credit'.

We observed the following irregularities in this regard:

(i) Out of the selected 49 Commissionerates, no reconciliation was being done in 41 Commissionerates and consequently Central Excise receipts of ₹ 2,36,295 crore were not reconciled for the period 2011-12 to 2013-14.

Audit collected data in ten Commissionerates<sup>28</sup> where reconciliation was not conducted and comparison of the revenue receipt figures of PAO/e-PAO with departmental figures revealed 'Less credit' of ₹ 512.07 crore and 'More credit' of ₹ 1,230.02 crore.

We pointed this out (June to October 2014) and 41 Commissionerates responded (June to December) as follows:

Nine Commissionerates<sup>29</sup> admitted the fact of non-reconciliation.

<sup>28</sup> Mumbai-I, Raigad, Thane-I, II, Belapur, Nasik, Tirupathi, Dibrugarh, Ahmedabad II and Rajkot

<sup>29</sup> Thane I, Nasik, Bhubaneswar I, II, Raigad, Kolkata VI, Madurai, Calicut and Allahabad

Six Commissionerates<sup>30</sup> stated that reconciliation could not be completed due to non-receipt of assessee-wise collection reports from PAO and e-PAO.

Three Commissionerates<sup>31</sup> stated that on receipt of data from PAO/e-PAO, same was sent to ranges/divisions but reconciliation reports were not received till date.

Nine Commissionerates<sup>32</sup> replied that reconciliation was under process. While five Commissionerates<sup>33</sup> replied that reconciliation was not done due to non-sanctioning/non-functioning of CAO at Commissionerates.

Four Commissionerates<sup>34</sup> replied that after introduction of e-payment system, entire process of reconciliation is automated and there was no need to verify CAO/PAO data.

The reply is not acceptable as para 12.3.4 of the manual clearly states that e-PAOs (in case of online payment) would also send assessee-wise payment/challan details to the Commissionerate every month for departmental reconciliation and as per para 12.10.1, Commissionerates have to reconcile the revenue with PAO. Reconciliation carried out by Audit in nine Commissionerates and the discrepancies in form of less/more credit indicate the need for reconciliation process.

Reply from five Commissionerates<sup>35</sup> was awaited (December 2015).

Different replies from the Commissionerates indicate that field formations have different views for reconciliation and the work is not being carried out.

Audit recommended that Board may clarify the issue with suitable instructions and make arrangements for proper implementation and monitoring of reconciliation process.

Ministry admitted (October 2015) that after implementation of ACES, procedure of revenue reconciliation prescribed in Board instructions' dated 24 December 2008 is not being followed and stated that these instructions needs to be followed timely and regularly. It also stated that reconciliation system between EASIEST software and PAOs have some discrepancies due to difference in consideration of reporting date of revenue which are being addressed and a number of measures are being initiated as follows:

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<sup>30</sup> Chandigarh I, Raipur, Haldia, Panchkula, Dibrugarh and Thane II

<sup>31</sup> Chandigarh II, Mumbai I and Belapur

<sup>32</sup> Puducherry, Chennai IV, Tirunelveli, Coimbatore, Ghaziabad, Jaipur I,II, Vapi and Daman

<sup>33</sup> Bhopal, Delhi II, Delhi LTU, Indore and Meerut I

<sup>34</sup> Delhi I, Ahmedabad II, Rajkot, Cochin

<sup>35</sup> Bengaluru II, III, Mysore, Ranchi and Jamshedpur

- (a) Pr CCA has been requested to update assessee details in synchronisation with ACES/EASIEST
- (b) NSDL has been asked to provide revenue reporting date on the basis of challan realisation date.
- (c) Pr CCA has been asked to import challan data from EASIEST and take action for proper reconciliation of revenue by sharing information between PAOs and banks.
- (ii) Audit also observed that where reconciliation was being done, it was done for past years only and up to date reconciliation was not completed. Thus there was delay in reconciliation ranging from 12 to 66 months in six Commissionerates as detailed in Table 4.1:

**Table 4.1 : Statement showing the delays in reconciliation**

Sl. No	Commissionerate	Reconciliation completed upto	Delay in Months (as on December 2014)
1	Hyderabad –I	August 2013	16
2	Hyderabad-II	December 2013	12
3	Hyderabad-III	May 2013	19
4	Chennai-II	March 2012	33
5	Tirupathi	February 2011*	46
6	Bolpur	June 2009	66

\* In Tirupathi Commissionerate, revenue realised through e-payment was not taken into account for reconciliation

When we pointed this out (between August to November 2014), Ministry intimated (October 2015) that in Hyderabad I and III Commissionerate, reconciliation was completed upto November and September 2013 respectively and further information was awaited from e-PAO. In Hyderabad II, reconciliation would be completed in two months. In Chennai II, reconciliation was completed upto December 2014 and no discrepancy was found. In Bolpur Commissionerate, data was not received from PAO in proper form earlier, it was received recently and reconciliation was being done. In case of Tirupathi Commissionerate, Ministry replied that reconciliation was not required due to same being verified from ACES and NSDL.

Ministry seems to have forwarded replies obtained from various Commissionerate without analyzing and taking a final view. Ministry opinion in case of Tirupathi Commissionerate is not correct as reconciliation between PAO and Commissionerates is required to ascertain that amount booked by Commissionerates is properly deposited in Government account. Ministry

may issue instruction to such Commissionerate and also ensure that data from e-PAO/PAO is sent to Commissionerates regularly.

Audit is of the view that Ministry needs to take a final view and issue instructions to field formations accordingly.

**(iii)** In Kolkata II and Kolkata V Commissionerates, reconciliation was initiated from July 2012 and November 2012 respectively but no reconciliation was taken up for the earlier period.

When we pointed this out (July 2014 and October 2014), Kolkata II Commissionerate replied that reconciliation reports from Ranges was not received for the period from April 2011 to June 2012, and reconciliation was done for the later period i.e. July 2012 to February 2013. Reports for the period from March 2013 to December 2013 were received in July 2014 and same were under scrutiny.

Kolkata V Commissionerate replied (October 2014) that no record was available for the year 2011-12. For 2012-13, reconciliation was done only for the months of July 2012 and November 2012 to March 2013. For 2013-14, reconciliation was done upto March 2014.

Ministry stated (October 2014) that further report for Kolkata II Commissionerate will follow.

For Kolkata V Commissionerate, Ministry on one hand stated that comparison of return with NSDL by range officer serve the purpose, on other hand it stated that instruction are being issued to the Commissionerate to follow the procedure.

Ministry's reply is contradictory which needs to be resolved and suitable instruction to be issued to field formation for consistency.

**(iv)** Audit observed that four Commissionerates detected 'Less credit' and 'More credit' as detailed in Table 4.2. However, no follow up action was taken for rectification of these discrepancies.

**Table 4.2 : Discrepancies found during reconciliation of figures between concerned Range and PAO**

(₹ in crore)

S. No.	Commissionerate	Reconciliation done up to	More Credits	Less Credits
1	Hyderabad-I	August 2013	703.55	42,357.34
2	Hyderabad-II	December 2013	4293.00	1275.00
3	Tirupathi	February 2011	54.46	35.06
4	Bolpur	June 2009	3.68	6.73

When we pointed this out (August to November 2014), Ministry intimated (October 2015) that in Hyderabad I, II and Bolpur Commissionerate reconciliation had been initiated. For Tirupathi Commissionerate, it stated that reconciliation was not required which is not acceptable for the reasons stated in previous paragraph.

**(v)** In Hyderabad III Commissionerate the closing balances of 'Less Credits' amounting to ₹ 406.00 crore and 'More Credits' amounting to ₹ 599.31 crore for the month of May 2012 were not carried forward as opening balance for the month of June 2012 which resulted in incorrect depiction of 'Less Credit' and 'More Credit'.

When we pointed this out (November 2014), Ministry stated (October 2015) that amount was reconciled in May 2012 and hence was not carried forward in June 2012.

**(vi)** During the scrutiny of the monthly accounts of e-PAO, Central Excise, Chennai for the year 2012-13 Audit observed that receipts of ₹ 198.86 crore and ₹ 202.22 crore were accounted for in the months of September and October 2012 respectively under Chennai I Commissionerate which was not consistent with normal monthly receipts trend of not more than ₹ 24 crore.

When we pointed this out (August 2014) the Deputy Controller of Accounts (DCA), Chennai replied (August 2014) that actual revenue collection for September and October 2012 was only ₹ 17.91 crore and ₹ 24.92 crore respectively and the difference in revenue collection was due to wrong location code used by some banks in the respective months. DCA further replied that due to non-reconciliation of revenue figures by the Commissionerates, these could not be rectified earlier.

Non-reconciliation of revenue by PAO and Commissionerates thus resulted in inflated booking of ₹ 180.95 crore in September 2012 and ₹ 177.30 crore in October 2012. Reconciliation system failed to notice even the cases of abnormal increase/decrease in revenue realization indicating the lack of seriousness being given to the process.

Ministry stated (October 2015) that reply will follow.

From the observations above it is clear that reconciliation is not being done at most of the places and wherever it is being done, rectification of discrepancies was not being carried out. Thus, accuracy of the revenue credited into Government account could not be ensured.

#### 4.2.1.2 Discrepancies between Date-wise Monthly Statements (DMS) and Put-Through Statements (PTS)

As per para 6.12.3 of the Manual, the FPB will prepare DMS on a monthly basis at the end of every month for submission to the concerned PAO. Para 6.15 of the manual states that CAS, RBI, Nagpur will generate a statement showing Bank-wise, PAO-wise and Major Head-wise amount put through in Government Account and furnish the same to PAO and link cell of the concerned bank. As per para 6.10 of the Manual the PAO and FPB concerned are responsible for reconciliation between DMS and PTS.

(i) Audit observed that Out of 46 test checked PAOs, in four PAOs<sup>36</sup> reconciliation of PTS and DMS was not conducted. In PAO Bhopal, reconciliation was not conducted during the period 2006-07 to 2012-13 and was started from 2013-14 with 'Nil' opening balance.

When we pointed this out (August to October 2014), Ministry intimated (October 2015) that in Bolpur PAO, efforts were being made for reconciliation. For Calicut, Delhi, Raipur and Bhopal Commissionerates, it stated that observation related to PAO and reply of Pr CCA may be considered. Reply of Pr CCA was awaited (December 2015).

(ii) Audit further observed that in 13 PAOs<sup>37</sup> where reconciliation was done, there was difference between DMS of FPBs and PTS prepared by CAS, RBI, Nagpur amounting to ₹ 38.78 crore in Central Excise receipts and ₹ 141.17 crore in Central Excise Refunds at the end of March 2014. The difference was pending rectification.

Out of this, in receipt side, amount in DMS was more by ₹ 23.24 crore as compared to PTS, indicating that amount was paid to bank but not credited to Government Account. In payment side, amount of ₹ 118.41 crore was more in PTS which indicates that more money was claimed by banks from Government Account than actually paid by them.

When we pointed this out (between August to October 2014), DCA Chennai stated (May 2015) that matter was taken up with banks by PAOs to rectify discrepancy.

Ministry stated (October 2015) that efforts were being made at Hyderabad, Ahmedabad I, Vapi-Daman, Puducherry and Bhopal PAOs. For Nasik, Kolkata, Physical PAO Chennai, e-PAO Chennai, Kochi, Jaipur and Bhubaneswar I PAOs, it offered no comments stating that observation pertained to PAO. For

<sup>36</sup> Calicut, Bolpur, Delhi and Raipur

<sup>37</sup> Hyderabad, Tirupathi, Bhubaneswar I, Ahmedabad, Vapi-Daman, Nasik, Kolkata, Physical PAO Chennai, e-PAO Chennai, Puducherry, cochin, Bhopal, Jaipur

Tirupathi PAO, it again stated that reconciliation was not required as field formations were verifying it with ACES and NSDL.

Ministry's reply is not consistent as all the observation pertained to PAOs only. Ministry needs to take a final view and instructions may be issued to all PAOs for consistency. Reply of the Pr CCA was awaited (December 2015).

#### **4.2.1.3 Challans not found on NSDL website resulting in non-reconciliation of duty**

As per the procedure laid down in annexure 6.3 of para No. 6.5.4 of the Manual, banks would upload challan data of taxes collected on EASIEST system on daily basis. The central system at NSDL would check the file structure of data files uploaded by banks and if found correct send the consolidated data to CBEC daily on the next working day. CBEC NSDL website provides Challan Identification Number based view to track the online status of Challans deposited in Bank.

During test check of challan details in ranges, we observed that in four ranges under four Commissionerates, eight challans involving an amount of ₹ 21.74 lakh were shown as remitted to Government as per details provided in returns of the assesseees but the challans were not found on NSDL website.

Further examination revealed that in respect of one challan of M/s Flora Art amounting to ₹ 1.55 lakh in Delhi Commissionerate, discrepancy was detected by ACES and review was also carried out. However, this Challan could not be traced on NSDL website. In case of three challans amounting to Rs 16.99 lakh pertaining to Allahabad Commissionerate, ACES did not detect discrepancy.

In Central Excise Commissionerate Vapi, we observed that M/s Aniket Metals Pvt. Ltd. paid Central excise duty of ₹ 0.93 lakh through cheque No. 960418 dated 01 October 2011. But, the challan was not available on NSDL. On verifying the same with PAO records, it was observed that the amount was not credited to the Government account.

When we pointed this out (between July to October 2014), Ministry stated (October 2015) that in the case of M/s Flora art, the duty amount of ₹ 1.55 lakh was paid by the assessee and same was verified, however challan could not be found on NSDL website due to mistake of challan no. Similarly challans relating to JS Industries were verified and found correct but were not available on NSDL and bank was requested to take action. In case of M/s Champion Cibee and Co, Ministry stated that reply will follow. In case of M/s Aniket Metals Pvt. Ltd., it stated that case was adjudicated and recoveries effected.

Audit is of the view that Ministry needs to take requisite steps to address the issue.

#### **4.2.2 Classification of Central Excise Duty**

Central Excise Duties collected by field formations of CBEC are accounted for under the Major Head 0038 Union Excise Duty. Education Cess (EC) and Secondary and Higher Education Cess (SHEC) are levied for specific purposes by Central Government and are not part of shareable duty. Proceeds under EC and SHEC are to be transferred to the Ministry of Human Resource Development. Hence, correct classification of Cess is necessary not only for correct presentation of accounts but also for allotment of amount to such intended purposes.

We observed following misclassifications of Duty/Cess as detailed in the succeeding paras:

##### **4.2.2.1 Classification of EC/ SHEC**

As per Pr CCA's instructions<sup>38</sup>, Central Excise duty, EC and SHEC are to be paid under accounting codes 00380003, 00380111 and 00380115 respectively.

Initially, after introduction of SHEC on Excise Duty from 01 March 2007, CBEC notified accounting codes 00380086 as 'Minor Head - Receipt Awaiting Transfer (RAT)' on temporary basis. This accounting code was subsequently modified to the new accounting code 00380115 vide the instruction *ibid*.

As per Para 5.3 of Civil Accounts Manual, to correct an error of classification in original accounts, transfer entries are required. If the accounts of the year in which errors take place are closed, such entry may be passed with the approval of Pr CCA.

We observed that 266 assesseees in four Commissionerates of Gujarat involving three PAOs, remitted SHEC of ₹ 47.85 lakh in temporary accounting code 00380086 during 2012-13 to 2013-14. Further, the PAOs incorrectly accounted such SHEC amount in 'Other Receipts Head-00380087' instead of correct Accounting Head -00380115.

Audit also noticed that department did not take any action to disable the temporary accounting code 00380086 from the directory of EASIEST software, after the new accounting code 00380115 was allotted to SHEC in October 2007 which led to misclassification of SHEC.

When we pointed this out (July to September 2014), ministry stated (October 2015) that in Rajkot and Ahmedabad II PAOs, assessee mentioned temporary accounting code which was not available in REVACT software,

<sup>38</sup> No. Co-Ord/13-6/98-99/ Vol. IV/454 dated 4 October 2007

hence, the amount was booked under Head 00380087 so that Challans may be compiled in the monthly accounts. In Vapi-Daman PAO, assesseees were requested to pay under proper head and to submit request for rectification of wrong accounting codes.

Audit recommended that Board may take action to carry out necessary updation in all relevant software and issue instruction for proper follow-up of accounting of various cess in proper head as improper accounting of cess impacts transfer to respective heads.

Ministry admitted the recommendation and stated that necessary updation will be made in software and fresh instruction will be issued for proper accounting of EC and SHEC.

#### **4.2.2.2 Rectification of error in accounting head**

As per Pr CCA instructions<sup>39</sup> for correction of Accounting Head, the PAO should get approval from the concerned Commissioner confirming that necessary changes have been made or being made in the Personal Ledger Account (PLA) of that year maintained at their end and after getting the approval from the Commissioner, necessary correction shall be made through the COMPACT (REVACT). If the amount involved is above ₹ 50 lakh in each case, further approval from the Pr CCA should be obtained.

During the audit of PAOs/Commissionerates, we observed the following irregularities:

(i) Six assesseees under Bhubaneswar I and II Commissionerates requested the PAO Bhubaneswar for rectification of error in accounting head, involving ₹ 3.10 crore and PAO forwarded such requests to the concerned Commissionerates. But, no approval from the concerned Commissionerates was received in all these cases.

When we pointed this out (July 2014), the PAO replied (July 2014) that further information is awaited from the Commissionerates.

Ministry stated (October 2015) that in Bhubaneswar I Commissionerate, no compliance was received from PAO but steps were being taken by the Commissionerate, for rectification in accounting code. In respect of Bhubaneswar II Commissionerate, it stated that reply would follow.

Ministry's reply indicates lack of coordination between PAO and Commissionerates to carry out the rectification.

(ii) M/s Aastha Alloycorp (P) Limited under Kurnool Range of Tirupathi Commissionerate incorrectly remitted (July 2013) Central Excise Duty

<sup>39</sup> OM No Coord/i(S)/R.II/9-10/23 dated 27 May 2009

amounting to ₹ 8.59 lakh under Accounting Code 00380031 (Others) instead of 0038003 (BED). The assessee applied (August 2013) for correction of Accounting Code to CAO which was forwarded to e-PAO, Chennai for rectification in accounts and e-PAO referred the case to Commissionerate for their approval. CAO then asked the range Kurnool I to make necessary changes in the PLA of the assessee. However, the rectification was not carried out till October 2014.

When we pointed this out (October 2014), Ministry stated (October 2015) that the unit was closed, however, action was being taken to rectify the error and forward the same to PAO.

#### **4.2.3 Outstanding balances under Suspense and Remittance heads**

Both Suspense and Remittance heads are intermediary and their clearance through per contra debit/credit to the final head should be ensured.

##### **4.2.3.1 Outstanding Balances under the Head of Suspense Account in respect of Central Excise, Service Tax and Customs**

As per Para 1.1 of Suspense Manual, Suspense heads are operated in Government Accounts to reflect transactions of receipts and payments which cannot be taken to final head of receipts or expenditure owing to lack of information as to the nature or for any other reason.

Suspense heads are also used to book temporarily, transactions of receipts and payments carried out by different entities i.e. banks, DDO etc. and then amount is transferred from suspense account to relevant head in the Government accounts which cannot be taken to final head of receipts or expenditure owing to lack of information as to the nature or for any other reason. They are finally cleared by minus debit or minus credit when the amount is taken to the final head of account. If amount under suspense head remained unadjusted, the balances under these heads get accumulated resulting in understatement of Government's receipts and refunds.

As per para 12.11.4 of Manual of Accounting of Indirect Taxes (Manual), on receipt of PTS from RBI Nagpur in Pr CCA, a transfer entry should be passed to transfer the total amount debited/credited by RBI to the account of CBEC, from the major head "8658-Suspense Account-Public Sector Bank Suspense" by minus debit or minus credit, as the case may be, to the major head "8675-Deposit with Reserve Bank". Similarly, other suspense heads are to be cleared by minus debit/credit entries.

Audit observed from the records of Pr CCA, New Delhi that there were outstanding balances under the major head "8658-Suspense Account" during last five years as detailed in Table 4.3.

**Table 4.3 : Outstanding balances under the major head “8658 – Suspense Account”  
– as on 31 March**

Head	2009-10		2010-11		2011-12		2012-13		2013-14	
101 - PAO Suspense	58.41	Cr	31.80	Cr	19.67	Cr	18.60	Cr	21.90	Cr
102 - Suspense Account Civil	1.22	Dr	1.51	Dr	2.31	Dr	1.55	Dr	0.39	Dr
108 - PSB suspense	209.36	Dr	504.54	Dr	784.12	Dr	517.42	Dr	433.46	Dr
138 - Other nominated Bank suspense	1.00	Dr	1.26	Dr	1.16	Dr	1.38	Dr	1.47	Dr

(₹ in crore)

Pr CCA was asked to provide the details of the outstanding balances, but the same was not provided and it could not be ascertained for how long the balances are pending in suspense accounts. Reconciliation is also not possible without item wise details.

When we pointed this out (October 2014) the Pr CCA office replied (October 2014) that efforts were being made to clear the balance from suspense head.

Ministry stated (October 2015) that operation of suspense account is an ongoing process as suspense balances under various heads keeps added and getting cleared. However, efforts will be made to clear old suspense balances in coordination between banks and Commissionerates.

Audit is of the view that item-wise details should be available to clear pending suspense balances in time.

#### **4.2.3.2 Outstanding amount under Major Head 8670-Cheques and Bills**

As per para 9.8.2 of the Manual, the Divisional Officer shall prepare a List of Payments (LOPs) on weekly basis i.e. 7th, 14th, 21st and 30th of every month and send it to the PAO along with paid refund vouchers.

As per para 2.3 and 2.4 of Suspense Manual (issued by CGA), the total amount of cheques issued by PAO and cheques issued by cheque drawing DDO during the month as verified from list of payment (LOP) will be credited to the minor head ‘102 - PAO cheques’ and ‘103 - Departmental cheques’ respectively under major head ‘8670 - Cheque and Bills’. Similarly payments made through electronic advices will be credited to ‘110- Electronic advices’ and ‘111 - PAO’s electronic advices’. Further as per Para 2.6 of the manual, on receiving ‘Date-wise monthly statement (DMS) from FPB, the PAO, after reconciliation, pass a transfer entry to transfer the amount under 8670 to 8658-Suspense Account.

During the scrutiny of records of Pr CCA New Delhi, Audit observed that there were outstanding balances under the major head “8670-Cheques and Bills” as detailed in Table 4.4.

**Table 4.4 : Outstanding balance under the major head "8670-Cheques and Bills" – as on 31 March**

Head	(₹ in crore)									
	2009-10		2010-11		2011-12		2012-13		2013-14	
102 - PAO Cheques	497.16	Cr	544.63	Cr	432.38	Cr	372.84	Cr	350.32	Cr
103 - Deptt. Cheques	-1,776.98	Cr	-1,033.25	Cr	-131.55	Cr	-144.16	Cr	133.17	Cr
110 - Electronic Advices	-40.91	Cr	35.20	Cr	-114.93	Cr	13.10	Cr	-4.44	Cr

There was a minus bookings under the head Electronic Advices – 8670 110 for an amount of ₹ 4.44 crore in 2013-14. This minus booking indicated payment in excess of advices issued. When we pointed this out (October 2014), the Pr CCA office replied that minus booking under the heads was due to delay in receipt of List of Payments (LOP) from the Commissionerates.

During the Audit, we also observed delays in receipt of LOPs in 5 PAOs<sup>40</sup>.

Credit balance in 102-PAO Cheques and 103-Deptt. Cheques above indicate that refund is being paid by the department through cheques and large number of cheques is pending credit in account of assesseees. Instructions of the Board for online payment of refund are not being followed by the department as depicted in paragraph 2.1.3 and 2.1.4.

Audit is of the view that payment of refund through cheques should be stopped to avoid delayed refund and interaction with the assesseees.

When we pointed this out (July to October 2014), Ministry stated (October 2015) that refund through online payment by RTGS had already been introduced. Chandigarh and Rajkot Commissionerates had also issued trade notices in this regard and steps were being taken to expand the system further.

#### **4.2.4 (a) Updation of interest rate in software for delayed remittance of revenue by banks to Government account**

As per Para 12.11.9 of the Manual, settlement of transactions of revenue remittances with CAS, RBI, Nagpur is required to be completed within T<sup>41</sup>+3 working days, in case of local transactions where the collecting branch and the FPB are in the same city/agglomeration and within T+5 working days in the case of outstation transactions.

Reserve Bank of India notified<sup>42</sup> interest rate on delayed credit of revenue receipt into Government Account as bank rate +2%. Para 12.11.14 of Manual prescribes rate of interest on delayed credit of revenue receipt into

<sup>40</sup> Mumbai II, Mumbai III, Cochin, Calicut and Vapi

<sup>41</sup> T is the day when money is available to the branch

<sup>42</sup> Notification No. RBI/2006-2007/235 DGBA.GAD.No.H-11763 / 42.01.011 /2006-07 dated 24 January 2007

Government Account as 8% (i.e. then bank rate of 6% +2%) with effect from 1 January 2007.

Audit observed that bank rate was revised by RBI from time to time after 1 January 2007 as depicted in table 4.5.

**Table 4.5 : Revision of bank rate by RBI**

Date	Bank rate	Date	Bank rate
09-Apr-03	6	20-Sep-13	9.5
13-Feb-12	9.5	07-Oct-13	9
17-Apr-12	9	29-Oct-13	8.75
29-Jan-13	8.75	28-Jan-14	9
19-Mar-13	8.5	15-Jan-15	8.75
03-May-13	8.25	04-Mar-15	8.5
15-Jul-13	10.25	02-Jun-15	8.25

However, no revision of interest rate was carried out by Pr CCA, CBEC as and when bank rate was revised and interest was being calculated by the system at the rate of 8% (6+2). Thus, interest from 13 February 2012 onwards was being calculated at reduced rate.

It was also observed that no instruction was issued by CGA for revision of interest in the system after January 2007.

#### **4.2.4 (b) Recovery of interest on delayed credit of revenue receipts into Government account**

Para 12.11.15 stipulates that the Delay Monitoring Module of P-CBEC software calculates automatically the delay in remitting revenue receipts by collecting banks to RBI, and penal interest to be levied thereon. From this system, bank-wise and branch-wise reports, relating to delay in remittance of revenue receipts, can be generated. Para 12.11.7 of the Manual provides that the Pr AO of Pr CCA office, New Delhi monitors the delays in remittances of Revenue Receipts to Government Account by authorized Banks and recovery of interest on such delayed remittances.

During the Audit of Pr CCA it was observed that Pr CCA calculated (April 2014) and demanded (August 2014) penal interest of ₹ 59.84 crore through P-CBEC on delayed remittances in respect of 29 banks. No recovery of the interest was reported till (October 2014).

When we pointed this out (October 2014), Pr CCA replied (May 2015) that interest of ₹ 16.60 crore was recovered from 27 banks and it was also intimated that four banks requested for waiving of interest as they remitted the amount to government in time. The claim of the banks was found correct by Pr CCA as interest was calculated wrongly due to wrong scroll dates

provided by the banks and same was entered in the software resulting in erroneous calculation of interest.

Further, due to non-updation of interest rate in the system, interest was being calculated at reduced rate. Though audit could not quantify the differential interest, Pr CCA may quantify and recover the differential interest from the banks from 13 February 2012 onward.

Audit recommended that Board should issue instructions for updation of interest rate in the system and recovery of balance interest from banks for previous period due to revision of interest rate from time to time.

Ministry stated (October 2015) Software used for monitoring the delay was being reviewed for making modification to incorporate for applicable bank rate as revised by RBI periodically. It further stated that representation made by the bank to justify delay, were under examination and recovery would be affected accordingly.

Audit will watch the progress.

### **4.3 Effectiveness of Monitoring and Internal Control**

Monitoring and Internal Control is an integral process which addresses risk and provides reasonable assurance about effectiveness and adequacy of system and procedures. We noticed the following inadequacies in this regard.

#### **4.3.1 Conduct of Internal Audit**

As per Para 3.2.2 (vi) of the manual, Pr CCA is responsible for conducting Internal Audit of Customs, Service Tax and Central Excise Commissionerates at the Headquarters, Division and Range levels, and subordinate authorities including Pay and Accounts Offices (PAO).

Audit observed that out of 46 PAOs selected by Audit, no internal audit was conducted by Pr CCA at 20 PAOs<sup>43</sup> for the years 2011-12 to 2013-14. Further, in North and west zones, nine Commissionerates<sup>44</sup> were also not audited during the three years. Details of Commissionerates audited by Dy. Controller of Accounts (South Zone), Chennai was not furnished. It was also observed that Range Offices were not considered for internal audit at all.

Internal audit is an important tool of internal control. Non-conducting of internal audit may result in irregularities, inconsistencies and systemic lapses remaining unnoticed.

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<sup>43</sup> Bhubaneswar, Allahabad, Ghaziabad, Ahmedabad, Vapi, Jaipur, Bhopal, Rajkot, Delhi, Hyderabad, Chandigarh I, Chandigarh II, Mumbai-II, Mumbai-III, Nasik, Raipur, Kolkata, Dibrugarh, Jamshedpur, Ranchi

<sup>44</sup> West Zone (Thane-I, Thane-II, Belapur, Raigarh, Mumbai-I, Nasik), North zone (Allahabad, Ghaziabad, Meerut)

When we pointed this out (July 2014 to April 2015), Ministry stated (October 2015) that due to limited resources, internal audit of all Commissionerates was not possible. As more Commissionerates had been created recently, proposal to augment resources would be sent to Board and Department of revenue and internal audit would be conducted on regular basis.

The efforts made by Board in this regard would be examined in subsequent audit.

#### **4.3.2 Payment of Central Excise duty through physical mode**

As per Rule 8 (1) of Central Excise Rules 2002, an assessee who had paid total duty of ₹ 10 lakh<sup>45</sup> or more including the amount of duty paid by utilization of Cenvat credit in the preceding financial year, shall thereafter, mandatorily deposit the duty electronically through internet banking. The total duty paid amount was further reduced to ₹ one lakh with effect from 1 January 2014<sup>46</sup>. From October 2014, electronic payment was made compulsory for all assesseees irrespective of amount of duty payment.

Test check in selected Commissionerates revealed that 219 assesseees in 22 Commissionerates<sup>47</sup> made central excise duty payments through physical mode instead of depositing the same electronically and Department did not initiate any steps for enforcing this mandatory provision. It is also observed that there is no provision to levy penalty for non-compliance in Central Excise, as exists in Service Tax<sup>48</sup>.

We pointed this out between August to October 2014.

Rajkot Commissionerate replied (February 2015) that the assesseees have been suitably guided to pay the duty through electronic mode and that since then all assesseees are paying duty through e-payment.

Daman Commissionerate replied (February 2015) that show cause notices had been served to assesseees for paying duty through physical payment.

Vapi Commissionerate replied (December 2014) that assesseees had then started paying duty through electronic mode, however, necessary action would be taken for earlier period.

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<sup>45</sup> With effect from 01 April 2010 vide Notification No.04/2010-Central Excise (NT), dated 19 February 2010

<sup>46</sup> Vide Notification no 15/2013-CE (NT) dated 22 November 2013

<sup>47</sup> Hyderabad I, Hyderabad III, Tirupathi, Bolpur, Kolkata-VI, Kolkata-II, Kolkata-V, Thane-I, Raigad, Allahabad, Rajkot, Ahmedabad-II, Vapi, Daman, Jaipur-I, Jaipur-II, Bhubaneswar I, Bhubaneswar II, Delhi, Bhopal, Indore, Raipur

<sup>48</sup> Penalty of ₹ 10,000 vide section 77(1)(d) of Finance Act, 1994

Jaipur I and II Commissionerates replied (November 2014) that concerned officers would be directed to take necessary action in this regard.

Delhi Commissionerate replied that assesseees could not pay duty through e-payment because of non-availability of net banking facility. Reply of the Department is not tenable as it was department's responsibility to educate the assesseees about making necessary arrangement for mandatory payment of the duty through electronic mode.

Ministry stated further (October 2015) that in Ahmedabad II Commissionerate, M/s Vital Technoplast paid the duty through physical mode but same was reflected in ACES as online payment and hence, ACES needs modification to rectify the error. It also stated that in Vapi, Daman, Hyderabad I and III Commissionerates, SCNs were issued against the assesseees and they started paying duty electronically.

Audit recommended that Board may consider inclusion of penalty clause for failure of payment of Central Excise Duty electronically in the lines of provision under section 77(1)(d) of Finance Act, 1994 in respect of Service Tax.

On the recommendation, Ministry stated that rule 27 of Central Excise Rules, 2002 already have a general penalty of ₹ 5,000 which could also be invoked in such cases and no fresh penalty was required.

Ministry's reply is not tenable as general penalty is also available in Service Tax but there is specific penalty in case of failing in online payment. Further, in practice, neither the assesseees are aware that general penalty may be invoked for not making online payment nor departmental officers invoke general penalty in case of such default. Ministry either needs to impose specific penalty or instruct department to invoke general penalty in such defaults.

#### **4.3.3 Payment of Refund claim through cheques instead of directly to the Assesseees/ Exporters Bank Account**

CBEC advised<sup>49</sup> that the practice of payment of refunds to the assessee through A/c payee cheques is outdated and entails a lot of paper work besides causing undue hardship to the assesseees and to put in place a system and mechanism for transfer of Refund claim amount directly to the bank account of the respective assesseees/ exporters.

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<sup>49</sup> Vide letter FTS No. 171722/2012 dated 09 October 2012

Audit observed that the payments of refund claims amounting to ₹ 2.43 crore were made through A/c payee cheques in Kadapa division of Tirupathi Commissionerate contrary to the aforesaid instructions of the Board.

When we pointed this out (February 2014), the department accepted the observation (February 2014) and intimated that the procedure would be followed in future.

Ministry stated (October 2015) that proposal to create e-PAO (refunds) is being considered for electronic payment of refund and correct and timely accounting.

#### **4.3.4 Issue of refunds cheques of ten lakh and above with single signature**

According to para 3.5.1 (viii) of CAM, all cheques drawn for ₹ 10 lakh and above shall bear two signatures. For this purpose the Head of the accounting organization shall nominate another gazetted officer/senior most non-gazetted officer, as second signatory<sup>50</sup>.

Further, para 9.4.2 of the Manual clearly stipulates that instructions contained in Central Government Accounts (Receipts and Payments) Rules, 1983 and para 3.5.1 of CAM should be carefully observed by the departmental authorized officer in relation to issue of cheques of payment of refunds.

Audit observed that in PAO Bhopal, all cheques drawn for ₹ 10 lakh and above were issued with single signature instead of two signatures contrary to the provisions, *ibid*.

When we pointed this out (July 2014), PAO Bhopal accepted the observation (July 2014) and intimated that the audit observation was forwarded to the Commissionerate for making necessary arrangements by nominating one more gazetted officer as second signatory.

Ministry stated (October 2015) that matter had been taken up with check signing authority and banks to follow the procedure of two signatures on cheques amounting ₹ 10 lakh and above.

#### **4.3.5 Supply of list of outstanding cheques**

As per Para 10.17 of the Manual, a cheque writer prepares a list of outstanding cheques at the end of each month from the Cheque Payment Register. A daily statement of cheques encashed is received from the Bank

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<sup>50</sup> O.M. No. 1(3)/95/TA/Pt.File/578 dated 27 July 1998

and the details are posted against the relevant columns of the Cheque Payment Register. Items against which no entries have been made become outstanding and such items are picked up and brought together in the form of a statement and a total is struck, which is verified with the figures already worked out separately in the Cheque Payment Register itself. After agreement the list is put up to CAO for signature and after its approval, the same should be attached to the monthly Cash Accounts to be sent to the PAO.

We observed that the list of outstanding cheques was not received in 15 PAOs<sup>51</sup> from the department and no action was taken for obtaining the same.

When we pointed this out (August 2014 to April 2015), the PAO, Tirupathi and Hyderabad intimated (October 2014) that issue would be taken up with department for providing list of outstanding cheques at the end of each month. Replies from other PAOs were awaited (May 2015).

Ministry stated (October 2015) that instructions are being issued by the Commissionerates to concerned DDOs to send list of outstanding cheques to PAOs. It further stated that it had no comments to offer on observations relating to PAOs. Reply from Pr CCA was awaited (December 2015).

#### **4.3.6 Obtaining of 'Nil' pendency certificates from FPBs**

As per Para 6.11.1 (j) of the Manual, the FPB should furnish a monthly certificate on the last working day of the following month to the concerned PAO certifying that 'nil' amounts of Central Excise, Service Tax, Customs collected are lying with the collecting branches under its control or in the pipeline somewhere between itself and the collecting branch.

We observed in 20 PAOs<sup>52</sup> that FPBs had not submitted such pendency certificate along with monthly scroll.

When we pointed this out (July to October 2014), 16 PAOs intimated (July 2014 to January 2015) that matter would be taken up with FPBs concerned to send the statement regularly. Replies from the PAOs of Bolpur, Dibrugarh, Ranchi and Jamshedpur were awaited (May 2015).

Ministry also stated (October 2015) that PAOs are taking action to obtain the certificates from the banks.

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<sup>51</sup> Hyderabad, Tirupathi, Kochi, Coimbatore, PAO(Revenue) Kolkata, Vapi-Daman, Ahmedabad, Rajkot, Jaipur, Delhi, Ghaziabad, Meerut, Allahabad, Jamshedpur, Ranchi

<sup>52</sup> Hyderabad, Tirupathi, Bhubaneswar, Delhi, Bhopal, Cochin, Calicut, Chandigarh-I, Chandigarh-II, Bolpur, Dibrugarh, Allahabad, Ghaziabad, Meerut, Ranchi, Jamshedpur, Ahmedabad, Rajkot, Vapi and Jaipur

#### **4.3.7 Delayed submission of Branch scrolls**

As per Para 6.8 of the Manual, the receiving Bank Branch should identify all those challans against which payment had been received in cash for the day, or for which payment by Cheque/ Draft have been realized, the electronic file containing all the Challan data for which payment have been realized for that day are transmitted electronically to FPB. However, the physical scroll and the underlying challans are forwarded to FPB for preparation of main scroll. At the start of the next working day, the receiving branch will forward two copies of the branch scroll along with the concerned challans to the designated FPB with a forwarding memo. Further, the FPB should furnish the Branch Scrolls along with challans to PAO on the next working day.

Audit observed that in PAO Tirupathi, Branch scrolls from Corporation Bank were received at the end of the month for the transactions during the month. Similarly, in PAO Bhubaneswar, we observed delay in submission of Branch scrolls by UCO bank on 62 occasions.

When we pointed this out (July and October 2014), both the PAOs replied (July and October 2014) that the matter was taken up number of times with bank branches and also reported to Pr CCA, New Delhi. However, banks continued delayed furnishing of scrolls. PAOs stated that further steps would be taken for timely furnishing of scrolls.

Ministry stated (October 2015) that in PAO Tirupathi scrolls were being received on daily basis. For other PAOs, it stated that detailed comments would be submitted by Pr CCA.

#### **4.3.8 Maintenance of Register of Bank Scrolls and Register of Lost Challans**

As per Para 12.2 of the Manual, in order to watch timely receipt and disposal of Bank Scrolls a Register of Bank Scrolls shall be maintained in the office of PAO. This register should be closed monthly and a report indicating the date for which daily scrolls have not been received from the Bank and action taken in this regard shall be put up to the PAO. Similarly Register for Lost or Misplaced Challans also needs to be maintained in specified format and should be closed by 10<sup>th</sup> of following month.

We observed in four PAOs<sup>53</sup> that both the Register of Bank Scrolls and Register of Lost Challans were not maintained. In five PAOs<sup>54</sup> Register of Bank Scrolls was maintained but Register of lost challans was not maintained. Non

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<sup>53</sup> Delhi, Bhopal, Jamshedpur, Ranchi

<sup>54</sup> Vapi-Daman Ahmedabad, Raipur, Hyderabad, Mumbai II (Revenue)

maintenance of such register indicates deficiency in internal control mechanism.

When we pointed this out (July 2014 to April 2015), Ministry stated (October 2015) that registers were not maintained in some PAOs due to shortage of staff and they were being maintained now.

#### **4.3.9 (i) Compilation of Revenue Receipts and Refund Payments by Single Data Entry Operator**

As per para 12.7.1 of the Manual, the Branch Scrolls received along with the challans will be compiled by the PAO in his computer system using revenue accounting software "COMPACT (REVACT)". According to para 12.7.2 of the Manual, the Main Scroll (FPB), branch scroll and underlying challans are entered into "COMPACT (REVACT)" software by two separate Data Entry Operators (DEOs) as Set I and Set II to ensure correct capture of challan data. Unless these two sets of documents are tallied, the system does not allow the DEOs to consolidate the main scroll and forward it to the Set II DEO. Further, if there is a difference between data entered by Set I and Set II, the system sends it to the AAO/PAO for physical verification of documents. After identifying the error, the data is again sent back to the DEO for making necessary changes before it is accepted by the AAO/PAO for final compilation.

We observed in five PAOs (Bhopal, Bolpur, Raipur, Ranchi and Jamshedpur) that the data was entered only through Set-I client. As the data was not entered through Set-II client also verification by Set-II client does not happen thereby affecting the reliability of the Monthly Account.

When we pointed this out (July to August 2014), the PAOs accepted (July to August 2014) the observation.

Ministry stated (October 2015) that points raised by Audit would be looked into for making suitable changes in revenue accounting system.

#### **4.3.9 (ii) Conduct of test-check of data entered in software**

As per Para No. 12.8.1 of the Manual, the compilation sheets of revenue receipts and refunds shall be test checked at the time of acceptance of data entered by the Data Entry Operators (DEOs) through COMPACT (REVACT) software by the Assistant Accounts Officer / Pay and Accounts Officer in accordance with the procedure laid down in Para 5.4.6 of CAM. Pr CCA, CBEC vide letter No. Co-ord/1(5)/Gen. Policy/93/532, dated 3 September 2002, prescribed the limits for test check which are as follows:

- Assistant Accounts Officer – All challans amounting to ₹ 25,000 and above.
- Senior Accounts Officer/Account Officer – All challans amounting to ₹ 1,00,000 and above.

Audit observed in PAO Raipur that no such test check was done either by Assistant Accounts Officer or by Account Officer before entry of data into COMPACT (REVACT).

It was also observed that there is no provision in COMPACT (REVACT) software for test check at Senior Accounts Officer/PAO level for all challans amounting to ₹ 1,00,000 and above. In the absence of provision in the software for electronic test check by the Senior Accounts Officer/Account Officer, the compliance of the instructions of Pr CCA, CBEC was not feasible.

When we pointed this out (August 2014), PAO Raipur replied (August 2014) that the staff was over burdened with office work and could not exercise such test check. PAO Mumbai replied (August 2014) that COMPACT (REVACT) software provided for acceptance of data at Assistant Accounts Officer level only and not at PAO level.

However, in view of online payment of duties and transfer of data between banks and department, Board may analyse whether these instructions are still relevant. Penalty provisions for assessee may also be made and enforced to eliminate physical payment by the assessees.

Ministry stated (October 2015) that due to heavy work load, test check of revenue receipts and refund could not be conducted. However, arrangements were being made to facilitate such tests.

Audit is of the view that Ministry should examine whether these instructions are still relevant.

#### **4.3.10 Mismatch of total revenue and assessee-wise details in PAO**

As per Para 12.1 of the Manual, each PAO is responsible for the accounting of revenue receipts and payments on account of refunds, rebates and drawbacks for Commissionerates under its accounting jurisdiction using the software package COMPACT (REVACT). Further, as per Para 12.10.1 of the Manual, the PAOs will provide an assessee-wise collection report to the CAOs of the Commissionerates concerned. Thus, it is necessary that REVACT software shows the correct information of assessee-wise revenue collection for reconciliation purpose.

Audit observed that in PAO Ahmedabad, the assessee-wise ledger generated an amount of ₹ 1,538.04 crore as against the gross receipt of Excise/Service

Tax of ₹ 1,556.38 crore for the period 2011-12 to 2013-14 resulting in short exhibition of ₹ 18.34 crore in assessee-wise ledger.

Similarly, in PAO Vapi, it was observed that the assessee-wise ledger generated an amount of ₹ 514.38 crore as against the gross receipt of Excise/Service Tax of ₹ 523.64 crore for the period 2011-12 to 2013-14 resulting in short exhibition of ₹ 9.26 crore in assessee-wise ledger.

The difference between actual receipts and assessee-wise ledger receipts was needed to be reconciled as assessee-wise figures are sent to Commissionerates for reconciliation. Analysis of the error revealed that error was due to non-updation of assessee's master data in COMPACT (REVACT) software in line with ACES/NSDL, due to which the payments of the assesseees which are not found in master data of COMPACT (REVACT), were not reflected in assessee's ledger.

When we pointed this out (September to October 2014), Ministry stated (October 2015) that the problem is related to COMPACT (REVACT) software and competent authority would be approached for the said correction in the COMPACT (REVACT) software. It further stated that in respect of PAO Vapi, reply will be submitted by Pr CCA.

## PART - B

### Service Tax

#### 4.4 Accounting of Service Tax

Proper Accounting of Service Tax is necessary to have fair picture of duty collection. We observed following inconsistencies in accounting of Service Tax.

##### 4.4.1 Reconciliation of Service Tax Receipts

Proper reconciliation of Revenue Receipts is necessary for ensuring that revenue is duly credited to Government Account. On review of reconciliation procedure, certain lacunae in the system as well as inconsistencies in procedures were observed as detailed below.

##### 4.4.1.1 Reconciliation of Service Tax by Commissionerates

As per Para 12.10.1 of the Manual, the PAO will provide an assessee-wise collection report to the CAO of the Commissionerate concerned. The CAO will distribute the same to the concerned Division/Range officers. The Range Officers in turn compare it with the returns submitted by the Assessee and prepare a monthly statement for submission to CAO. The CAO notes down discrepancies as 'Less Credit' and 'More Credit' and forwards a copy to PAO. The CAO undertakes the necessary correspondence with the Range Officers concerned in case of 'More Credit' and PAO interacts with the Focal Point Branch in case of 'Less Credit'.

As per CBEC's instruction<sup>55</sup>, the Range Officer has to prepare monthly statements of TR-6/GAR-7 challans received from assessees and reconcile the same with copies of challans received from Banks and send reports to CAO.

We observed the following irregularities in this regard:

(i) In 39 Commissionerates, reconciliation of Service Tax revenue with PAO figures was not done for the period from 2011-12 to 2013-14. Consequently Service Tax receipts of ₹ 3,01,436 crore remained unreconciled.

Audit collected data in seven Commissionerates where reconciliation was not conducted and comparison of the revenue receipt of PAO/e-PAO with that of departmental figures revealed 'Less Credit' of ₹ 1,088.89 crore and 'More Credit' of ₹ 37.74 crore.

We pointed this out (June to October 2014) and 39 Commissionerates responded (June to December 2014) as follows :

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<sup>55</sup> Serial no. 14.1 of instruction No. 224/37/2005-EX-6 dated 24 December 2008

Ten Commissionerates<sup>56</sup> admitted the fact of non-reconciliation.

Five Commissionerates<sup>57</sup> stated that reconciliation could not be completed due to non-receipt of assessee-wise collection reports from PAO and e-PAO.

Kolkata ST Commissionerate replied (September 2014) that assessee-wise collection reports were received from PAO but not forwarded to range offices.

Chandigarh II Commissionerate replied (July 2014) that on receipt of data from PAO/e-PAO, same was sent to ranges/divisions but reconciliation reports were not received till date.

Nine Commissionerates<sup>58</sup> replied that reconciliation was under process.

Four Commissionerates<sup>59</sup> replied that reconciliation was not done due to non-sanctioning/non-functioning of CAO at Commissionerates.

Bengaluru ST Commissionerate replied (August 2014) that after introduction of ACES, the reconciliation was being carried by the PAO with bank and no separate reconciliation had been carried out by the Commissionerate. Rajkot Commissionerates replied (February 2015) that Range Officers were reconciling returns with data available in ACES and verification of challans from CAO/PAO is not required. It further stated that data from PAO/e-PAO was not available with CAO and data received from e-PAO Chennai for the month of August 2014 was sent to field formations for verification.

The reply is not acceptable as para 12.3.4 of the manual clearly states that e-PAOs (in case of online payment) would also send assessee-wise payment/challan details to the Commissionerate every month for departmental reconciliation and as per para 12.10.1, Commissionerates have to reconcile the revenue with PAO. Reconciliation carried out by Audit in 7 Commissionerates and the discrepancies in form of less/more credit indicate the need of reconciliation process.

Tirupathi Commissionerate replied (October 2014) that though field formations were instructed to reconcile revenue statement with PAO for Central Excise but very few ranges were responding. No instructions were issued in respect of Service Tax.

Ahmedabad ST Commissionerate replied (February 2015) that reconciliation was conducted by Range Officers and no discrepancy was reported to CAO.

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<sup>56</sup> Mumbai ST I, ST II, Allahabad, Cochin, Bhubaneswar I, II, Nasik, Raigad, Madurai and Calicut

<sup>57</sup> Chandigarh I, Raipur, Haldia, Panchkula and Dibrugarh

<sup>58</sup> Puducherry, Tirunelveli, Coimbatore, Chennai ST, Ghaziabad, Jaipur I, II, Vapi and Daman

<sup>59</sup> Bhopal, Delhi LTU, Indore, and Meerut I

However, Ranges examined by Audit stated that there was no mechanism/system available with Range office to get any separate compiled details of challans paid by the assessee which indicates that PAO/e-PAO data was not sent to Range offices for reconciliation.

Reply from Five Commissionerates was<sup>60</sup> awaited (May 2015).

Different replies from the Commissionerates indicate that field formations have different views for reconciliation and the work is not being carried out.

Audit recommended that Board may clarify the issue with suitable instructions and make arrangements for proper monitoring of reconciliation process.

Ministry stated (October 2015), that present system of reconciliation involve manual intervention and in built delays and can not be monitored and tracked from the headquarter and needed to be reviewed for improvement. It also admitted that reconciliation of Service Tax as envisaged in Board's instructions dated 24 December 2008 and in Manual is to be done timely and regularly. It further stated that the system will be reviewed and time limit would be fixed to complete the reconciliation. Instructions will also be issued for proper implementation and monitoring of reconciliation process.

(ii) We observed delays in reconciliation of PAO figures with that of Commissionerate. In Hyderabad I, III and Bolpur Commissionerates ranging from 16 to 66 months as detailed in table below :

**Table 4.6 : Statement showing the delays in reconciliation**

Sl. No	Commissionerate	Reconciliation completed upto	Delay in Months (as on December 2014)
1	Hyderabad –I	August 2013	16
2	Hyderabad-III	May 2013	19
3	Bolpur	June 2009	66

When we pointed this out (between August to November 2014), Ministry replied (October 2015) that In Hyderabad I and III Commissionerates reconciliation was completed upto November 2013 and August 2013 respectively and it was being done for further period. In Bolpur Commissionerate, reconciliation had been started on receipts of data from PAO.

<sup>60</sup> Hyderabad II, Ranchi, Jamshedpur, Delhi ST and Mysore

#### 4.4.1.2 Discrepancies between Date-wise Monthly Statements (DMS) and Put-through Statements (PTS)

As per para 6.12.3 of the Manual, the FPB will prepare DMS on a monthly basis at the end of every month for submission to the concerned PAO. Para 6.15 of the manual states that CAS, RBI, Nagpur will generate a statement showing Bank-wise, PAO-wise and Major Head-wise amount put through in Government Account and furnish the same to PAO and link cell of the concerned bank. As per para 6.10 of the Manual the PAO and FPB concerned are responsible for reconciliation between DMS and PTS.

Audit observed non rectification of discrepancies detected in reconciliation of DMS with PTS in Mumbai e-PAO and Tirupathi PAO, as tabled below :

**Table 4.7 : Discrepancies between DMS and PTS as on 31.03.2014**

Commissionerate/ PAO	Receipts		Payment	
	More in DMS	More in PTS	More in DMS	More in PTS
e-PAO, Mumbai	573.87	0	0	0
Tirupathi	12.24	16.68	9.97	0
<b>Total</b>	<b>586.11</b>	<b>16.68</b>	<b>9.97</b>	<b>0</b>

(₹ in lakh)

In receipts side, more amount in DMS indicates possibility of payment of Service Tax amounting to ₹ 586.11 lakh by the assesseees to the authorised banks, but the same was not credited to the Government Account.

When we pointed this out (July 2014 and October 2014), e-PAO (Service Tax), Navi Mumbai accepted the observation (July 2014) and intimated that the matter was under correspondence with the banks. PAO Tirupathi replied (October 2014) that necessary steps would be taken to settle the differences.

Ministry stated (October 2015) that reconciliation between DMS and PTS requires better coordination between PAOs and banks and the system will be strengthened by issuing fresh instructions to banks.

#### 4.4.1.3 Challans not found on NSDL website

As per Annexure 6.3 under Para 6.5.4 of the Manual, banks would upload challan data of taxes collected under EASIEST system on daily basis. The central system at NSDL would check the file structure uploaded by banks and if found correct send consolidated data to CBEC on the next day. CBEC NSDL website provides Challan Identification Number based view to track the online status of challans deposited in bank.

During test check of challan details in range, Audit observed that in four Ranges under two Commissionerates<sup>61</sup>, 13 challans involving amount of ₹ 5.49 crore shown realized as per departmental records but the challans were not found on NSDL website.

On further scrutiny, it was observed that in respect of six challans amounting to ₹ 1.57 crore, discrepancies were detected by ACES and review was also carried out. However, these Challans could not be traced (May 2015) on NSDL website. In case of seven challans amounting to ₹ 392.23 lakh, ACES did not detect the discrepancy.

When we pointed this out between August to October 2014, Ministry stated (October 2015) that the issue needs to be taken up by the system team of CBEC and Pr CCA with banks involving NSDL. Reply in respect of Delhi ST and Kolkata ST Commissionerates would follow.

#### 4.4.2 Classification of Service Tax

Service Tax collected by field formations of CBEC is accounted for under the Major Head 0044 Service Tax.

As per Board's instructions<sup>62</sup>, EC is to be paid and accounted for under specific head '00440298' whereas SHEC is to be paid and accounted for under specific code '00440426'.

Further, as per Para 5.3 of Civil Accounts Manual, to correct an error of classification in original accounts Transfer Entries are required. If the accounts of the year in which errors take place are closed such entry may be passed with the approval of Pr CCA.

We observed the following cases of misclassification of Tax/ Cess as detailed in the succeeding paras.

##### 4.4.2.1 Accounting of Service Tax/EC/SHEC

M/s Vodafone Infrastructure Limited in Service Tax Commissionerate, Ahmedabad remitted Service Tax of ₹ 5.42 crore (accounting code 00440366), EC of ₹ 10.84 lakh (accounting code 00440298) and SHEC of ₹ 5.42 lakh (accounting code 00440426) through physical payment by challan dated 6 January 2012. The PAO incorrectly accounted for the amounts as detailed in Table 4.8:

<sup>61</sup> Delhi ST and Kolkata ST

<sup>62</sup> Circular No. 161/2012-ST dated 06 July 2012 and 165/16/2012- dated 20 November 2012 issued by CBEC read with Pr CCA's letter No. CO-ORD/13-6/98-99/Vol. IV/454 dated 04 October 2007

Table 4.8 : Incorrect accounting of Remittance

			(₹ in lakh)
A/c Head	Amount remitted by assessee as per challan	Amount booked in REVACT by PAO	Excess (+)/Less (-)
00440366	542.09 (Service Tax)	5.42	-536.67
00440298	10.84 (2% E cess)	542.09	+531.25
00440426	5.42 (1% SHE cess)	10.84	+5.42

When we pointed this out (September 2014), the PAO intimated (September 2014) that the matter would be taken up with Pr CCA for further necessary action. The Service Tax Commissionerate, Ahmedabad replied (February 2015) that the assessee had been directed to deposit the Service Tax in the appropriate head.

Ministry stated (October 2015) that instruction had been issued by the Commissionerates to the assesseees to deposit Service Tax in appropriate heads. It further stated that necessary updation will be carried out in software being used by PAOs and fresh instructions would be issued in that regard.

#### 4.4.2.2 Classification of Education Cess (EC)/ Secondary Higher Education Cess (SHEC)

Service Tax collected by field formations of CBEC is accounted for under the Major Head 0044 Service Tax. Education Cess (EC) and Secondary and Higher Education Cess (SHEC) are levied for specific purposes by Central Government and are not part of shareable duty. Proceeds under EC and SHEC are to be transferred to the Ministry of Human Resource Development. Hence, correct classification of Cess is necessary not only for correct presentation of accounts but also for allotment of amount to such intended purposes.

Audit observed that in 12 cases pertaining to ranges Group I and II of Hyderabad II Commissionerate, EC and SHEC amounting to ₹ 53.87 lakh was not accounted for properly and misclassified the amounts to improper revenue accounting code.

When we pointed this out in (December 2014), Ministry stated (October 2015) that field formations are advised to bring instances of misclassification to the notice of PAO for rectification.

#### 4.4.2.3 Rectification of error in Accounting Head

As per Pr CCA instruction<sup>63</sup> for correction of Accounting Head, the PAO should get approval from the Commissioner concerned, confirming that necessary changes have been made or being made in the Personal Ledger Account (PLA)

<sup>63</sup> Notification No Coord/i(S)/R.II/9-10/23 dated 27 May 2009

of that year maintained at their end. Necessary correction shall be made through the COMPACT (REACT). If the amount involved is more than ₹ 50 lakh in each case, approval from Headquarters should be obtained.

Audit observed that in PAO Bhubaneswar, in 19 cases the assessee requested PAO for rectification of the error in Accounting Head. The PAO forwarded all such requests for rectification of error in Accounting Head to the Commissionerates concerned but no such approvals were received. Total tax misclassified was ₹ 75.88 lakh (₹ 50.09 lakh in Bhubaneswar I Commissionerate and ₹ 25.79 lakh in Bhubaneswar II Commissionerate).

When we pointed this out (July 2014), the PAO stated (July 2014) that approval was awaited from Bhubaneswar-I and II Commissionerates.

Ministry stated (October 2015) that in Bhubaneswar I Commissionerate necessary direction would be made to concerned section to carry out rectification and in Bhubaneswar II, rectification was under process.

#### **4.4.2.4 Classification of Service Tax in residuary head**

As per the Board's instructions<sup>64</sup> for payment of Service Tax in the Negative List regime, a new accounting code '00441089-All Taxable Services Other Than in Negative List' (residuary accounting code) was notified by the CBEC and simultaneously service specific codes prevailing at that time were discontinued. Later, through circular No. 165/16/2012-ST dated 20 November 2012, different accounting codes for 120 services, interest penalty etc. were notified. This included replacement of residuary accounting code from '00441089' to '00441480- Other Taxable Services'. Assessee were required to make payment of Service Tax in the accounting head notified for each of the services.

With a view to remove this discrepancy, instruction<sup>65</sup> were issued by Director General of Service Tax, Mumbai to all the Chief Commissionerates instructing them to persuade the assessee for payment of tax under appropriate head instead of residuary accounting head 00441089.

Audit observed that assessee continued to misclassify Service Tax in residuary heads and no action was taken by the PAO/Commissionerates as depicted in following cases:

(i) In PAO Hyderabad, Service Tax receipts continued to be posted under residuary head '00441089' instead of appropriate service-wise heads, even

<sup>64</sup> Circular No. 161/12/2012-ST dated 6 July 2012

<sup>65</sup> Circular No F.NO.V/ DGST/Rev.Misc/ 98/ 2012/3517 dated 25 September 2013

after November 2012. In 2013-14, total Service Tax of ₹ 696.30 crore was misclassified under residuary head '00441089'.

When we pointed this out (December 2014), the PAO intimated (January 2015) that posting under Service-wise head would be undertaken after receipt of necessary instructions from Pr CCA.

Reply of the Ministry was awaited (December 2015).

(ii) Test check in six Commissionerates<sup>66</sup> also revealed that 6,858 assesseees paid Service Tax amounting to ₹ 335.64 crore in residuary head instead of proper service-wise heads. No action was taken by the Commissionerates to instruct assesseees in compliance of the instructions issued in November 2012 and September 2013.

We pointed this out (July to October 2014).

Service Tax Commissionerate, Ahmedabad accepted the observation (February 2015) and intimated that Range Offices had initiated action to educate the assesseees for payment of tax in correct head and issued instructions to that effect.

Daman Commissionerate intimated (January 2015) that assesseees were asked to either pay the Service Tax under correct head or submit request to this office regarding change of Accounting Code.

Division I, Silvassa of Vapi Commissionerate intimated (December 2014) that the assessee had paid Service Tax under residuary head due to lack of information and requested the Commissionerate for issue of suitable trade notice in this regard.

Rajkot Commissionerate replied (July and September 2014) that instructions to the authorized signatory of assessee had already been issued orally/telephonically.

Jaipur I and II Commissionerates replied (November 2014) that concerned officers were being directed to take necessary action in this regard.

Ministry confirmed the reply of the Commissionerates (October 2015). In case of Rajkot Commissionerate it also stated that it was only a technical error and there was no revenue impact.

Though the issue has no revenue impact, however, mis-classification of Tax in wrong heads defeat the purpose of revenue allocation service category wise for budgetary and financial analysis.

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<sup>66</sup> Rajkot, Ahmedabad ST, Vapi, Daman, Jaipur I and Jaipur II

Audit recommended that Board may instruct Pr CCA to issue necessary instruction to PAOs for proper classification and Commissionerates to instruct assesseees for making payment under proper heads.

Ministry admitted the recommendation partly stating that audit observation was conveyed to Pr CCA to issue instructions to PAOs. However, for issuing instructions to assesseees for proper classification under proper service heads, it stated that as definition of different services no longer exists, assessee could not be compelled to pay tax under proper service code.

Ministry replies is not correct as circular dated 20 November 2012 require assesseees to pay Service Tax in the accounting head notified for each service. Further, it would not be possible for PAOs to classify tax service-wise if same is not classified by the assesseees.

Ministry need to examine the issue and issue consistent instructions to assesseees and PAOs.

#### **4.4.2.5 Classification of Service Tax refund**

As per Para 9.8.4 of Manual of accounting of indirect taxes (Manual), in the case of refund of revenue there is no budgetary allocation and the total monthly payments on account of refunds are booked in the accounts as "Deduct Refunds" below the relevant revenue receipt major head of Account.

Audit observed lapses of misclassifications as follows:

(i) In PAO Meerut, during 2013-14, FPB booked refund of Service Tax and Customs as Central Excise and sent the refund payment scroll to PAO. However, PAO did not verify scroll details with cheques and consequently, booked the amount under Head of Account 0038 (Central Excise) instead of 0037 (Customs) and 0044 (Service Tax) as mentioned in refund cheques attached with scrolls. This resulted in misclassification of Service Tax and Customs refunds amounting to ₹ 134.63 lakh as Central Excise refunds.

When we pointed this out (November 2014), the PAO intimated (November 2014) that as per scrolls generated by the FPBs the booking was done. Reply of the PAO is not acceptable as PAO has to verify all refund payments along with the list of payments and refund cheques as per Rule *ibid*. It also indicates that PAO did not exercise proper checks in respect of such refunds.

Ministry stated (October 2015) that reconciliation could not be done due to non-receipt of assessee-wise collection report from the PAO.

(ii) In PAO, Jamshedpur payment of refund claim amounting to ₹ 42.91 lakh was made to M/s Rungta Mines Ltd, Chaibasa and ₹ 0.52 lakh to M/s Quality Steel Product, Jamshedpur, which were to be debited under Head of Account

0044 (Service Tax) on duty deduct refund, but it was erroneously debited to 0038 (Central Excise) by the FPB, Jamshedpur.

When we pointed this out (in September 2014), Ministry stated (October 2015) that bank was asked to carry out necessary correction.

(iii) In PAO (Customs), New Delhi, refund claim of Service Tax was included in scrolls of Central Excise and Customs by FPB erroneously between January and November 2013. However, PAO did not verify the scrolls and Service Tax refund was booked under head 0037-Customs instead of 0044-Service Tax resulting in misclassification of Service Tax refund amounting to ₹ 139.18 lakh.

When we pointed this out (September 2014), PAO intimated (December 2014) that Commissionerates while sending List of Payments (LOPs) did not indicate Service Tax refund and proforma for submission of LOP was revised.

Reply of the Ministry was awaited (December 2015).

#### **4.5 Effectiveness of Monitoring and Internal Control**

Monitoring and Internal Control is an integral process which addresses risk and provides reasonable assurance about effectiveness and adequateness of system and procedures. We noticed the following inadequacies in this regard.

##### **4.5.1 Payment of Service Tax through electronic mode**

As per Rule 6(2) of Service tax Rules, 1994, read with notification No. 01/2010 ST dated 19 February 2010, effective from 1 April 2010 assessee who paid total duty of ₹ 10 lakh or more including the amount of duty paid by utilization of Cenvat credit in the preceding financial year, shall mandatorily deposit the duty electronically through internet banking. This limit was reduced to ₹ 1 lakh with effect from 1 January 2014 through CBEC circular No. 16/2013 ST dated 22 November 2013. From October 2014, electronic payment was made compulsory for all assessees irrespective of amount of duty payment.

Further, As per Section 77(1)(d) of the Finance Act 1994, a person who is required to pay tax electronically through internet banking fails to pay the tax electronically, shall be liable to pay ₹ 10,000 as penalty.

Audit observed that in 16 Commissionerates, 1,765 assessees made payment through physical mode in-stead of electronic mode. Despite the provision in section 77(1)(d) of the Finance Act 1994, no penalty was imposed by the department to stop the assessees from paying duty by physical mode. Amount of penalty leviable on these assessees, amounted to ₹ 1.77 crore, considering single default by each assessee.

We pointed this out between August 2014 to October 2014.

Service tax Commissionerate, Ahmedabad intimated (February 2015) that the concerned range offices had directed the assesseees to deposit service tax through e-payment.

Vapi Commissionerate (December 2014) replied that assesseees had now started paying duty through electronic mode, however, necessary action would be taken for earlier period.

Jaipur I and II Commissionerates replied (November 2014) that Concerned Officers would be directed to take necessary action in this regard.

Rajkot Commissionerate replied (July and September 2014) that assesseees were suitably guided to adhere the Board's instructions on the subject matter and point was noted for further compliance.

Cochin Commissionerate replied (July 2014) that both the assesseees were informed to use electronic payment and they were complying with since then.

Delhi Commissionerate replied that there was no mechanism on the ACES system to ascertain the mode of payment.

Reply of the department is not tenable as there is separate column for payment mode in ACES for challan particulars.

Reply from remaining 11 Commissionerates was awaited (May 2015).

Ministry stated (October 2015) that all the assesseees had been suitably guided to pay duty through electronic mode. Ministry was silent on imposing penalty for violation of the instructions.

#### **4.5.2 Payment of Rebate/ Refund claims to the Assesseees' Bank Account**

CBEC through letter FTS No. 171722/2012 dated 9 October 2012 instructed to put in place a system/mechanism for transfer of refund claim amount directly to the bank account of the respective assesseees/exporters.

Audit observed that payments of rebate/ refund claims of ₹ 34.19 crore for the year 2013-14 were made through A/c payee cheques in CAO, Hyderabad II Commissionerate, contrary to the instructions.

When we pointed this out (December 2014), CAO intimated (December 2014) that instructions would be complied in future.

On one hand, department has provision of penalty of ₹ 10,000 for assessee in case of physical payment to discourage assessee but department itself is not paying refund through electronic mode.

Audit recommended that Board may issue instruction to monitor the compliance of its instructions by field formations to avoid hardship to the assesseees.

Ministry admitted the recommendation (October 2015) and stated that the issue of direct payment of refund/rebate to the bank accounts was being considered and detailed procedure would be laid down.

#### **4.5.3 Sanction of Refund from the Consumer Welfare Fund (CWF)**

Consumer Welfare Fund (CWF) was established in accordance with Section 12 C of Central Excise Act, 1944. As per Section 73A(6) of Finance Act, 1994 any surplus amount left as a result of unjust enrichment shall be credited to CWF. As per rule 3 of Consumer Welfare Fund rules 1992, any amount having been credited to CWF is ordered or directed as payable to any claimant by orders of proper officer, appellate authority or court shall be paid from the fund.

As per Para 8.7.1 (vi) and (vii) of the Manual, PAO attached to each Commissionerate will be designated to handle the transactions relating to refund from CWF on the "Department of Revenue" side. Pr CCA will issue cheque to PAO concerned for payment of refund out of CWF. Initially, PAO is required to deposit the cheque into Government account and subsequently refund amount would be debited to Government account.

Audit observed that in PAO Ahmedabad, refund of ₹ 4.72 lakh was sanctioned to M/s Karnawati Club Ltd. out of CWF and Pr CCA issued cheque to PAO for remitting the amount in Government account and pay the refund claim to the assessee. However, PAO Ahmedabad, instead of remitting the cheque to Government account and then issue a refund cheque to the assessee, remitted the cheque in bank as a payment by the assessee for tax liability. Thus, the amount was not included in refund figures and same were understated.

When we pointed this out (September 2014), PAO Ahmedabad admitted (November 2014) that the amount was erroneously deposited in bank account and also intimated that Service Tax Division concerned was advised not to allow refund to the party to avoid double claim.

Ministry confirmed the reply of the PAO (October 2015).

## PART - C

### Customs

#### 4.6 Accounting of Customs Duty

Proper Accounting of Customs Duty is necessary to present fair picture of duty collection. We noticed the following inconsistencies in accounting of Customs Duty:

##### 4.6.1 Reconciliation of Customs revenue receipts

Proper reconciliation of revenue receipts with well defined procedures is necessary for ensuring that revenue is duly credited to Government account. On review of reconciliation procedure, we observed lacunae in the system as well as inconsistencies in procedures which are discussed in the following Paragraphs.

##### 4.6.1.1 Reconciliation of Customs revenue by the Commissionerates

As per Para 10.3.1 and 10.4.1 of the Manual, in the manual payment, the importer/exporter is required to fill in the Bill of Entry (BE)/Shipping Bills (SB) as prescribed by the department for import or export of goods. On the basis of details provided in the BE/SB the designated officer does the appraisal/item-wise calculation of various duties and prepares four copies of challans manually or through ICEGATE for tendering duty payment at the counter of the authorised banks. One copy of the challan is sent to the PAO along with the receipt scrolls for detailed accounting and reconciliation. Para 10.3.2 of the Manual stipulates that the revenue account compiled by the PAOs is also reconciled with the challan information collected by the departmental officer viz. CAO.

We observed that in nine Commissionerates<sup>67</sup>, reconciliation of customs revenue figures of Commissionerate with those of PAO figures was not carried out for the period 2011-12 to 2013-14. Thus, total Customs Duty receipt of ₹ 82,224 crore pertaining to these Commissionerate remained unreconciled. It was also observed that Refund/drawback in respect of two Commissionerates<sup>68</sup> amounting to ₹ 3,947 crore was not reconciled.

Audit conducted reconciliation of CAO data with PAO data in Customs(Preventive) Kolkata and Customs Cochin Commissionerates and detected the following discrepancies:

<sup>67</sup> Kandla, Kolkata (Preventive Customs), Kolkata (Port ), Kolkata ( Airport), Amritsar, Chennai Customs, Cochin(Customs), Trichy and Tuticorin

<sup>68</sup> Kolkata (Preventive Customs) and Kandla

(i) In Commissionerate of Custom (Preventive), Kolkata and Customs Cochin, reconciliation of Customs revenue with PAO(Revenue) Kolkata revealed difference of Customs duty during the years 2011-12 to 2013-14 as detailed in Table 4.9.

**Table 4.9 : Differences of Customs Duties between PAO and CAO**

(₹ in lakh)

Name of the Commissionerate of Customs	Year	Customs receipts of CAO	Customs Receipts PAO	Difference due to non-reconciliation by the Commissionerate
Commissionerate of Customs (Preventive), Kolkata	2011-12	20,814	40,882	(-)20,068
	2012-13	40,943	46,200	(-)5,257
	2013-14	36,582	32,564	4,018
Commissionerate of Custom, Cochin	2011-12	1,89,514	1,90,454	(-)940
	2012-13	59,655	59,755	(-)100
	2013-14	18,085	17,999	86

It is observed from above table that there was difference in CAO and PAO figures in all the years. Thus, accuracy of revenue credited into Government account could not be ensured.

(ii) There was also difference in Refund/Drawback figures of Commissionerate of Customs (Preventive) Kolkata with figures booked by PAO as detailed in Table 10:

**Table 4.10: Differences in drawback/refund between PAO and CAO**

(₹ in lakh)

Name of the Commissionerate of Custom	Year	Drawback/Refund as per Commissionerate	Drawback/Refund as per PAO(Revenue) Kolkata	Difference
Commissionerate of Custom (Preventive), Kolkata	2011-12	5,977	2,651	3,326
	2012-13	17,038	19,946	(-)2,908
	2013-14	19,447	9,857	9,590

Difference of ₹ 95.90 crore in 2013-14 indicated that though the refund was sanction by the Commissionerate, same was not credited to the accounts of the assesseees in time.

We pointed this out (July to November 2014).

CAO Commissionerate of Customs (Preventive), Kolkata replied (September 2014) that PAO was sending customs receipt data at three or four months interval which could not be reconciled in the absence of major or minor head wise segregation. Further PAO (Revenue), Kolkata intimated that CD on monthly basis would henceforth be sent to CAO.

CAO (Port and Airport), Kolkata confirmed (September 2014) that reconciliation was not conducted.

Customs Commissionerate, Amritsar intimated (December 2014) that reconciliation could not be conducted in the absence of proper data from PAO and PAO was requested to provide party wise report.

Reply from Chennai Customs, Tuticorin, Kandla, Kochi customs and Trichy Commissionerate was awaited (May 2015).

PAO Kandla intimated (October 2014) that as accounts of financial year 2011-12 to 2013-14 had been closed there was no possibility to amend them and figures intimated to the Government by PAO had been accepted by department. PAO however agreed that from current financial year (2014-15) reconciliation work would be started.

Reply is not acceptable as reconciliation of monthly figures was necessary to ascertain the accuracy of accounting of Customs duty. Further Paragraph 5.3.3 of the Civil Accounts Manual has provision of transfer entries, if error was detected within existing financial year. In case, accounts have been closed, there is provision to make entry below specific wrong entry. Reply of Kandla Commissionerates was awaited.

PAO Customs house, Chennai confirmed (August 2014) the non-reconciliation.

PAO (Tuticorin) stated (August 2014) that the reconciliation by CAO was carried out up to the period October 2012 and the reconciliation from November 2012 onwards was yet to be taken up.

PAO (Customs), Cochin intimated that matter would be taken up with the department to reconcile these figures.

Ministry stated (December 2015) that in Kandla and Cochin Commissionerates, reconciliation had been initiated. In Amritsar Commissionerate, assessee-wise revenue report was not received from PAO despite repeated requests due to which no reconciliation was done. After restructuring in CBEC in October 2014, revenue collection and reconciliation work has been shifted to Ludhiana Commissionerate. In Chennai Commissionerate, revenue figures will be obtained monthly henceforth. In Tuticorin and Trichy Commissionerates, reconciliation for the years 2011-12 to 2013-14 was completed. In Kolkata (Preventive), Kolkata (Port) and Kolkata (Airport) Commissionerates, audit observation was noted and officers were instructed for necessary action. Further progress would follow.

#### 4.6.1.2 Discrepancies between Date-wise Monthly Statements (DMS) and Put-Through Statements (PTS)

As per Para 6.12.3 of the Manual, the FPB will prepare DMS on monthly basis for submission to the concerned PAO. Para 6.15 of the Manual states that CAS, RBI, Nagpur will generate a PTS statement showing Bank-wise, PAO-wise and Major Head-wise amount in Government account.

Para 6.10 of the Manual provides that PAO and FPB concerned are responsible for reconciliation between DMS and PTS.

Audit observed that in PAO Amritsar reconciliation of PTS and DMS was not conducted. It was also observed that in three PAOs/e-PAOs<sup>69</sup> difference between DMS of FPBs and PTS prepared by CAS, RBI, Nagpur was detected for the years 2011-12 to 2013-14 as tabled below but same was not rectified.

**Table 4.11 : Difference in DMS and PTS (for the period 2011-12 to 2013-14)**

Commissionerate/PAO	Receipts		Payments	
	More in DMS	More in PTS	More in DMS	More in PTS
Kolkata		23.06		19.61
Tirupathi		4.69		52.07
e-PAO <sup>70</sup> (Customs) Delhi	476.00	658.00		
<b>Total</b>	<b>476.00</b>	<b>685.75</b>		<b>71.68</b>

In receipt side amount of ₹ 4.76 crore was more in DMS indicating that amount was paid to bank but not credited to Government Account. In payment side, amount of ₹ 71.68 lakh was more in PTS which indicate that more money was claimed by banks from Government Account then actual paid by them.

When we pointed this out (July to October 2014), e-PAO Customs, New Delhi intimated that matter had been taken up with the banks. PAO, Tirupathi intimated (October 2014) that necessary steps would be taken to settle the differences. PAO, Kolkata intimated that discrepancies were pending with SBI and several reminders had been issued in this regard to the bank.

Ministry stated (December 2015) that in Kolkata Commissionerate audit observation was noted and officers were instructed for necessary action. Further progress would follow. For e-PAO (Customs) Delhi, it stated that matter pertains to PAO and reply will follow. Reply for Amritsar and Tirupathi Commissionerates was awaited.

<sup>69</sup> Kolkata, Tirupathi and e-PAO(Customs) Delhi

<sup>70</sup> e-PAO (Customs) deals with electronic payment at all India level

#### 4.6.1.3 Mismatch in ICEGATE and Bank data for Customs Duty

As per para 10.9 of the Manual, e-PAO (Customs) receives Customs Duty collection data from authorised banks receiving Customs Duty through e-payments on day-to-day basis. Further, e-PAO also receives Customs Duty data from ICEGATE on daily basis. Both the data are uploaded in the system COMPACT-REVACT and accounts are compiled on daily basis.

Test check of e-PAO (Customs), Delhi data for March 2014 revealed that there were 7,853 cases amounting to ₹ 538.16 crore in ICEGATE which did not match with bank data. Similarly, there were 8464 cases amounting to ₹ 628.37 crore in bank data which did not match with ICEGATE data.

When we pointed this out (October 2014), the e-PAO intimated (December 2015), that it did not have structural data of the database hence it would approach NIC for difference in ICEGATE data and clarification in difference of bank data.

Ministry stated (December 2015) that reply will follow.

#### 4.6.2 Classification of Customs Duty

Education Cess (EC) and Secondary Higher Education Cess (SHEC) are being levied for specific purposes by the Government of India and are not part of shareable Customs Duty. Proceeds under EC and SHEC are to be transferred to the Ministry of Human Resource Development. Hence correct classification of this Cess is necessary for proper presentation of accounts and for allotment of the amount for such intended purposes.

##### 4.6.2.1 Classification of EC/SHEC

As per Pr CCA's instructions<sup>71</sup>, Education Cess on Customs duty is to be paid under accounting head 00370066 and SHEC is to be paid under accounting head 00370068. Deputy Controller of Accounts (WZ), Mumbai instructed<sup>72</sup> to all the PAOs to check the discrepancies in challans and book the figures of EC/SHEC properly so that the revenue under these heads remains equal to three per cent of Customs Duty realized.

Audit observed instances of misclassification due to wrong information from bank as detailed below:

(i) In PAO Ahmedabad, Customs duty of ₹ 2,792.95 crore (which included Import Duty and EC/SHEC) was booked during the years 2011-12 to 2013-14 under Import Duty Head 00370002/00370005, instead of booking the

<sup>71</sup> Letter No. Co-ord/13-6/98-99/Vol.IV/454 dated 4 October 2007

<sup>72</sup> Vide circular No. DCA/WZ/Circular/2012-13/744 dated 13 December 2012 read with Pr CCA's OMs dated 24 July 2012 and 16 November 2012

EC/SHEC amount in respective heads. Thus, EC amounting to ₹ 54.23 crore and SHEC amounting to ₹ 27.11 crore were misclassified as Customs Duty.

When we pointed this out (September 2014), PAO Ahmedabad intimated (October 2014) that posting was done on the basis of physical challans received from Banks and as the assessee did not classify the amount in any sub-head, the challans were posted in the same way as received.

The reply is not acceptable because Audit scrutiny revealed that in some challans, the assessee had shown EC/SHEC amount separately. Further, the PAO did not take up the matter with Customs Commissionerate for rectification of challan data as directed in aforesaid instructions.

Ministry stated (December 2015) that revenue pertaining to the years 2011-12 to 2013-14 was already accounted for, however, matter was being taken up with higher authorities for making necessary correction. Reconciliation of Customs revenue is now being done regularly.

(ii) In PAO Central Excise Cochin, Audit observed that entire Customs receipts of ₹ 4.31 crore was booked under 'Other Receipts-Customs' head for the years 2011-12 to 2013-14. Thus, EC/SHEC amounting to ₹ 12.56 lakh was misclassified as Customs Duty.

We pointed this out in July 2014. Reply from PAO was awaited (December 2015).

Ministry stated (December 2015) that para pertained to PAO and reply was required to be furnished by them.

(iii) In PAO (Customs) Cochin, total receipts inclusive of Cess for the period 2011-12 to 2013-14 were ₹ 2,682.08 crore and EC/SHEC cess at the rate of three per cent on the above amount worked out to ₹ 78.12 crore. However, Cess booked in the classified abstract for the above period was ₹ 11.84 crore resulting in short accounting of EC and SHEC to the tune of ₹ 66.28 crore as detailed in Table 4.12.

**Table 4.12 : Difference in Cess collection**

Year	Receipts as per Consolidated Abstract	Admissible Cess [col.(2)*3/103]	Amount shown in consolidated abstract figure			Difference
			EC	SHEC	Total	
			(4)	(5)	(6)	
(1)	(2)	(3)	(4)	(5)	(6)	(7)= (3-6)
2011-12	1,90,453.66	5,547.19	514.74	246.41	761.15	4,786.04
2012-13	59,754.88	1,740.43	116.93	56.45	173.37	1,567.06
2013-14	17,998.99	524.24	167.70	81.81	249.51	274.73
<b>Total</b>	<b>2,68,207.53</b>	<b>7,811.87</b>	<b>799.37</b>	<b>384.67</b>	<b>1,184.04</b>	<b>6,627.83</b>

(₹ in lakh)

When we pointed this out (September 2014), the PAO Cochin intimated (September 2014) that consolidated abstract was prepared on the basis of the monthly account figures of CAO and that the matter would be taken up with the Commissionerate to review the figures and to ascertain the actual amount of Cess.

The reply is not acceptable as PAO has to classify the duty based on information provided by banks in challans/bank scroll and RBI.

DCA, Chennai stated (May 2015) that accounting by PAO would be done properly and that department has to take up the matter and issue necessary instructions.

#### **4.6.2.2 Posting of Challan-wise entry of Customs Duty Receipts in COMPACT (REVACT)**

As per Para 12.1 of the Manual, each PAO is responsible for the accounting of revenue receipts and payments on account of refunds and drawbacks for Commissionerates under its accounting jurisdiction using the software package COMPACT (REVACT). Pr CCA office instructed<sup>73</sup> all the PAO offices to carry out posting of challan-wise entries.

Audit observed the lapses in posting of challans as detailed below:

(i) In PAO Kandla, challan-wise entries of Customs receipts were not carried out in REVACT Software prior to October 2013 and figures as submitted by FPB in their Date-wise Monthly Statement (DMS) were entered in accounts. Test check of challans of February-March, 2014 revealed that in 17 cases, EC, SHE and Clean Energy Cess were wrongly booked in single head of Customs Duty (00370005), instead of the respective heads. This resulted in misclassification of amount of ₹ 66.08 lakh, ₹ 33.04 lakh and ₹ 8.91 crore respectively in 17 cases, test checked.

Further, it was also observed that the PAO did not account for certain Cess such as Rubber Cess, Clean Energy Cess etc. which are collected for specific purposes. In the absence of proper accounting, the correctness of amount of these Cess, collected for intended purpose could not be ensured.

When we pointed this out (October 2014), the PAO Kandla intimated (October 2014) that the amounts were classified correctly and also submitted copy of year-wise figures of Customs receipts. The reply was not acceptable as in cases test checked by Audit, entries in the REVACT software were erroneously accounted for in single head. The reply was silent regarding the

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<sup>73</sup> Vide letters dated 14 February 2012, 21 December 2012 and Circular No. DCA/WZ/Circular/2012-13 dated 31 December 2012

mechanism for ensuring proper accounting of other Cess in the absence of Challan-wise entry.

Ministry stated (December 2015) that from November 2013, challan-wise entry in REVACT had been started and amount of cess was being entered under proper accounting head.

(ii) At PAO Delhi, we observed that there was no regular feeding of each challan. However, the figures of Date-wise Monthly Statement (DMS) of receipts and refunds were entered in the system through transfer entries most of the time. Posting made through transfer entries during 2011-12 to 2013-14 is tabled below :

**Table 4.13 : Customs duty receipt not entered challan-wise**

(₹ in crore)			
Year	Figures as per revenue accounts compiled by PAO(Customs)	Figures of Transfer entries made during the period	Percentage of figures entered through transfer entries
2011-12	17,446.04	17,218.85	98.70
2012-13	8,070.15	7,796.24	96.60
2013-14	2,159.99	885.55	41.00
Total	27,676.18	25,900.64	93.58

During 2011-12 to 2013-14, out of ₹ 27,676.18 crore, ₹ 25,900.64 crore (93.58%) was entered into the system through transfer entries. Percentage of figures entered through transfer entries were 98.7%, 96.6% and 41% in 2011-12, 2012-13 and 2013-14 respectively. Further we noticed that all Customs Duty on imports was classified under '0037001010201-All Other Articles' and there were no bookings under EC/ SHEC in the months of April 2011, August 2011, January 2012, April 2012, December 2012, February 2013, August 2013 and January 2014.

When we pointed this out (October 2014), the PAO accepted the observation and intimated (December 2014) that because of non-availability of staff, feeding of challans could not be done and now the Challan-wise feeding had been started.

Audit is of the view that in absence of challan-wise entry, entry of the EC, SHEC and other cess could not be accounted for correctly and due to non-accounting of cess, transferring of the correct amount of cess to respective heads could not be ensured, defeating the purpose of imposing the cess.

Reply of the Ministry was awaited (December 2015).

(iii) In PAO Kolkata also, it was observed that instead of challan-wise entry, postings were made in the system through transfer entries on the basis of DMS received from banks.

When we pointed this out (October 2014), the PAO admitted (October 2014) the observation.

Ministry stated (December 2015) that audit observation was noted and officers were instructed for necessary action. Further progress would follow.

Board may take appropriate action for proper entries of challans to ensure correct accounting of duty and cess.

#### 4.6.3 Outstanding Balances under the Head of Suspense Account

Suspense heads are operated in Government Account to reflect transactions that cannot be booked initially to their final head of account for some reason or the other. They are finally cleared by minus debit or minus credit when the amount is taken to the final head of account. If amount under suspense head remains unadjusted, the balances under these heads get accumulated resulting in understatement of Government's receipts and payments. Minor Head 136 under Major Head 8658 are operated for booking Customs receipts under suspense.

Audit observed from the records of Pr CCA, New Delhi that there were outstanding balances under the major head "8658 – Suspense Account" during the period 2009-10 to 2013-14 as detailed in Table 4.14.

**Table 4.14 : Outstanding balances under the major head "8658 – Suspense Account"**  
(₹ in crore)

Accounting head	2009-10		2010-11		2011-12		2012-13		2013-14	
136 - Customs receipts awaiting transfer	145.47	Cr	252.28	Cr	249.50	Cr	222.56	Cr	223.26	Cr

When we pointed this out (October 2014), the Pr CCA stated (October 2014) that the amount included receipt of advance payments of ₹ 144.13 crore of the current financial year 2014-15. Thus, the balance of ₹ 79.13 crore pertained to previous years awaiting clearance. Further progress was awaited (December 2015).

Ministry stated (December 2015) that para pertained to Pr CCA. Reply of Pr CCA was awaited (December 2015).

#### 4.6.4 Arbitrary transfer of amounts of Receipts Awaiting Transfers (RAT) to different head of account of Customs Duty

Para 12.7.7 of the manual stipulates that in case of missing/lost challan, the certificate in lieu of lost or misplaced challan containing all details including account classification available electronically with the bank is to be obtained from the bank by the PAO. Till the certificate is obtained, the total amount of the missing challan is booked under relevant head of account namely, 0044(ST)/0038(CX) or 0037(Cus.)-RAT. On receipt of certificate in lieu of

lost/misplaced challans on a subsequent day, the booking under 0044/0038 or 0037-RAT is reversed by booking the amount under the appropriate head of accounts as provided in the certificate in lieu of the missing challan.

Audit observed that in e-PAO Customs Delhi, during the period January 2012 to March 2014 the figures under the head “00370080001 – Receipt Awaiting Transfer (RAT) to other minor heads etc”, were reflected in the accounts every month except for the month of December 2012 and March 2014. The consolidated figures reflected under this head in the monthly accounts for the period 16.1.2012 to 28.02.2014 are detailed in table 4.15:

**Table 4.15 : Amount under Receipts Awaiting Transfer (Customs)**

(₹ in crore )		
Sl.No.	Period	Figures under the head RAT
1.	16.01.2012 to 31.03.2012	89.10
2.	01.04.2012 to 31.10.2012	744.61
3.	01.11.2012 to 30.11.2012	(-)744.61
4.	01.01.2013 to 28.02.2013	655.83
5.	01.03.2013 to 31.03.2013	(-)655.83
6.	01.04.2013 to 31.01.2014	2,622.30
7.	01.02.2014 to 28.02.2014	(-)2,622.30

Audit further observed that amount booked under the head was being arbitrarily transferred to other Minor Heads.

When we pointed this out (October 2014) e-PAO intimated (December 2014) that since their office was not in a position to know the exact classification of the amounts appearing under RAT, the amount from RAT was cleared to different heads of account of Customs Duty collection and the matter had been taken up with Pr CCA for clarification.

The reply indicated that PAO did not follow the Accounting Manual procedures/instructions for adjustment of RAT figures.

Ministry stated (December 2015) that para pertained to Pr CCA. Reply of Pr CCA was awaited (December 2015).

#### **4.6.5 Recovery of interest from banks on delayed credit of revenue receipts into Government Account**

As per Para 12.11.9 of the Manual, settlement of transactions of revenue remittances with CAS, RBI, Nagpur is required to be completed within T+3 working days in the case of local transactions where the collecting branch and the FPB are in the same city/agglomeration and within T+5 working days in the case of outstation transactions.

Para 12.11.7 of the Manual provides that the Pr.A.O. of Pr CCA office, New Delhi monitors the delays in remittances of Revenue Receipts to Government

Account by authorized Banks and recovery of interests on such delayed remittances.

Audit observed in PAO, Hyderabad that though there were delays ranging from 11 days to 385 days in crediting of revenue receipts into Government Account, interest amounting to ₹ 3.15 crore on such delayed credit was not recovered.

Audit also observed that this delay was not included in the interest calculated by Pr CCA for all banks (refer para 4.2.4 (b) – CX).

Further, it was observed that rate of interest was not updated in the software at the time of change in base rate of RBI as detailed in para 4.2.4 (a).

When we pointed this out (October 2014), Ministry stated that recovery of interest would be taken up with Pr CCA.

#### **4.6.6 Delayed remittance of revenue to the bank**

In terms of Rule 6(1) of Receipts and Payment Rules 1983, all moneys received by or tendered to Government Officers on account of revenue or receipts or dues of the Government shall, without undue delay, be paid in full into the accredited bank for inclusion in Government account.

Audit observed that in Commissionerate of Customs (Preventive) Kolkata, and Customs House Treasury Kolkata Port Commissionerate there was delay in remittance of cash receipts. In test checked cases, we observed delays ranging from 6-32 days in remitting the receipts amounting to ₹ 1.03 crore into Government account.

When we pointed this out (September 2014), Superintendent Customs of Petrapole Customs Circle admitted the delayed remittance (September 2014) in respect of Bagda Preventive Unit and assured that the prescribed norms would be strictly followed in future.

Range Officers of Ghojadanga LCS and PU and Tentulia Customs Preventive Unit intimated (September 2014) that due to non-availability of suitable transport/government vehicle for carrying cash to the bank and due to intervening holidays the cash could not be deposited in time. CAO Customs House Kolkata stated (September 2014) that due to non-availability of armed guards, there were such delays and cash receipts are being deposited currently to RBI once or twice a week.

Ministry stated (December 2015) that audit observation was noted and officers were instructed for necessary action. Further progress would follow.

Board may take steps to provide necessary facilities for timely remittance of cash receipts into Government account.

#### 4.6.7 Non/Delayed payment of Drawback

As per Para 11.5.2 of the Manual, on receipt of “Monthly Reconciliation Statement of Drawback Disbursement” from the Customs Department (Drawback/Refund), the PAO will reconcile the figures of drawback/refund payments authorised during the month and payment made by the bank shown in reconciliation statement, with figures as per his accounts. Any discrepancy shall be brought to notice by PAO to the Customs Department (Drawback) for rectification.

As per the Memorandum of Understanding between Banks and RBI, the Banks have to first make payments of drawback and then make claim for reimbursement from RBI.

Audit observed the following inadequacies in this regard.

In PAO Hyderabad, in respect of drawback relating to Inland Container Depot, Hyderabad and Air Cargo Complex, Shamshabad, the banks had drawn the amount from Government Account before making payment to exporters. The gap between period of drawal of amount and actual payment ranged from 1 to 185 days. Further, the bank had not made payment of Drawback amounting to ₹ 35.09 lakh due to transaction failure after drawing the amount from Government Account. Out of this amount, the bank refunded ₹ 10.21 lakh to the government but remaining amount of ₹ 24.88 lakh was not refunded till October 2014.

Similarly in Ghaziabad Commissionerate , 79 Drawback payments amounting to ₹ 64.65 lakh for the year 2013-14, relating to Inland Container Depot, Loni were not paid to the assesseees due to failed transactions but the amount was subsequently withdrawn from Government account.

In Customs Commissionerate Kandla, in 66 cases involving drawback amount of ₹ 48.35 lakh, bank returned the unpaid amount through Banker’s cheques to Customs department. The validity of banker’s cheques got expired and same were revalidated by bank at later dates with delay ranging 40 to 1,568 days. Thus the drawback amounts were kept pending with department and not paid back to the Government. In 29 other cases, amount returned by the bank was not remitted to the Government account but paid to the exporters with delay ranging from 172 to 1,204 days.

In PAO Cochin, drawback payments were transferred electronically to the Bank. In 153 cases amounting to ₹ 33.38 lakh pertaining to the Custom Commissionerate Cochin, amounts were neither paid due to non availability of exporters nor credited back to Government Account.

When we pointed this out (between August 2014 to October 2014), PAO Hyderabad intimated (August 2014) that the matter had been taken up with concerned bank.

PAO Kandla stated (October 2014) that matter was taken up in workshop on audit of bank held at Pr CCA office in August 2012 and again by Zonal DCA, Mumbai with SBI, Kandla.

PAO Cochin intimated (September 2014) that Pr CCA had instructed department to transfer such amount to the Government Account.

DCA, Chennai stated (May 2015) that Pr CCA undertook audit of duty drawback payment by banks and payment have been streamlined. All the banks have deposited the unsettled payments to department which have been credited to government accounts by respective PAOs.

The reply indicates that government revenue was blocked by banks which gave financial advantage to them and loss of interest to the government due to non-reconciliation of drawback payment.

Ministry stated (December 2015) that in Hyderabad, DD of ₹ 38.95 lakh received from the bank on 11.09.2014 got expired which was revalidated on 24.02.2015 and sent to PAO. In respect of objection pertaining to Ghaziabad Commissionerate, it stated that amount of ₹ 42.76 lakh was received from the bank on account of failed transaction of drawback disbursement which had been deposited to Government account. In Kandla Commissionerate, amount of ₹ 48.35 lakh had been deposited in Government account as per direction of PR CCA. In Cochin Commissionerate, all drawback amount returned by bank had been credited to Government account.

Board needs to examine flouting of MOU clauses by banks in claiming drawback re-imburements from Government before actual payments.

#### **4.7 Effectiveness of Monitoring and Internal Control**

Monitoring and Internal Control is an integral process which addresses risk and provides reasonable assurance about effectiveness and adequateness of system and procedures. We noticed the following inadequacies in this regard.

##### **4.7.1 Conduct of Internal Audit**

As per Para 3.2.2 (vi) of the manual, Pr CCA is responsible for conducting Internal Audit of Customs, Service Tax and Central Excise Commissionerates at the Headquarters, Division and Range levels, and subordinate authorities including Pay and Accounts Offices (PAO).

Audit observed that internal audit had not been conducted at e-PAO (Customs) New Delhi, PAO (Customs) New Delhi, Amritsar, Kolkata, Kandla, Tiruchirapalli, Chennai and Tuticorin for the years 2011-12 to 2013-14.

All PAOs confirmed (July to April 2015) the non-conduct of internal audit.

Ministry stated (December 2015) that internal audit of Tuticorin had been conducted upto June 2013 and audit of PAO Trichy was scheduled in November 2015. It also stated that no audit was conducted by Pr CCA in Kandla during the period July 2014 to April 2015, though the audit observation pertained to the period 2011-12 to 2013-14. Reply in respect of remaining PAO was awaited.

#### 4.7.2 Maintenance of Cash Book

As per Rule 13 read with Rule 21 of Central Government Account (Receipt and Payment) Rules, 1983, every officer who is authorised to receive cash on behalf of Government, should maintain cash book in Form G.A.R.3 and issue the payee a receipt duly signed by him after he has satisfied himself, before signing the receipt and initialising its counterfoil.

Audit observed that in Petrapole Preventive Unit under Customs Commissionerate (Preventive) Kolkata, no cash book was maintained. Scrutiny of Monthly Technical Report (MTR) for the months of January and February 2014 revealed difference in the amount actually collected through TR-5 Challans and the figure reported to Customs Commissionerate (P) Kolkata as shown in Table 4.16.

**Table 4.16 : Mismatch between TR-5 Challans and MTR figures**

Month	Total of TR-5 Challans	MTR figure	(₹ in lakh)
			Excess/Less
Jan-2014	151.65	149.91	1.74
Feb-2014	158.28	177.13	(-) 18.85

When we pointed this out (September 2014), the Superintendent, Petrapole Preventive Unit admitted (September 2014) the discrepancies and confirmed that the figures shown in TR-5 were correct.

As the cash book was not maintained, there was no scope for cross verification of actual realization with remittances and cash balance. Incorrect reporting of revenue collection would consequently result in incorrect accounting by CAO.

Ministry stated (December 2015) that report will follow.

#### 4.7.3 Obtaining of 'Nil' pendency certificates from FPBs

As per Para 6.11.1 (j) of the Manual issued by Pr CCA, the FPB should furnish a monthly certificate on the last working day of the following month to the concerned PAO certifying that 'nil' amounts collected of Central Excise, Service Tax, Customs are lying with the collecting branches under its control, or in the pipeline somewhere between itself and the collecting branch (RBI's No.358/41.04.001/97-98 of 29 May 1995).

Audit observed that in six PAOs<sup>74</sup>, FPBs had not submitted 'nil' pendency certificate along with monthly scroll. In the absence of this certificate, possibility of retaining Government revenue with FPB could not be ruled out.

When we pointed this out (August to October 2014), all the concerned PAOs admitted the observation and intimated (August to October 2014) that matter would be taken up with FPBs to send the said certificates regularly.

Ministry stated (December 2015) that in Gujarat zone, before closing the accounts for the financial year, it is ensured that no scroll from the bank is pending.

The reply is not tenable as the procedure requires 'Nil' pendency certificates from the banks.

For Cochin Commissionerate, it stated that reply is to be furnished by PAO. Reply for remaining PAOs was awaited.

#### 4.7.4 Maintenance of Register of Bank Scrolls and Register of Lost Challans

As per Para 12.2 of the Manual, a Register of Bank Scrolls shall be maintained by PAO in order to watch timely receipt and disposal of Bank Scrolls. This register should be closed monthly and a report indicating the date for which daily scrolls have not been received from the Bank and action taken in this regard shall be put up to the PAO. Similarly Register for Lost/Misplaced Challans needs to be maintained in specified format and should be closed by 10<sup>th</sup> of the following month.

Audit observed that in PAO Kandla, Delhi, Amritsar and Kolkata register of bank scrolls was not maintained. Further, in PAO Delhi neither certificate in respect of lost challans was obtained from concerned banks nor any register to watch over lost Challans was maintained for the years 2011-12 to 2013-14. As these registers are essential for effective monitoring of receipt and disposal of Bank scrolls, non-maintenance of the same indicates lapse in internal control mechanism.

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<sup>74</sup> PAO(Customs) Kolkata, Kolkata Customs(Preventive), Kandla, Delhi, Cochin and Amritsar

When we pointed this out (September 2014 to October 2014), all the PAOs admitted (September to October 2014) the observation. PAO Amritsar further intimated that points were noted for future compliance.

Ministry stated (December 2015) that observation pertained to PAO. Reply of the Pr CCA was awaited (December 2015).

#### **4.8 Conclusion**

Tax Accounting and Reconciliation process in CBEC needs revision due to change in mode of duty payment and electronic exchange of data. Existing manual/instructions to be followed by the field formation also need to be revised. Better monitoring of compliance of the instruction by field formation is required to ensure proper accounting and reconciliation of revenue.

##### ***Recommendation no. 3***

Board may analyse the extant Manuals/instructions in view of electronic payment and transfer of data and revise them accordingly.

Ministry stated (October 2015) that discrepancies in reconciliation between EASIEST and PAOs are being examine and measures are being initiated to address the issue.

##### ***Recommendation no. 4***

Necessary updation may be carried out in software for rate of interest as and when revised by RBI and ensure recovery of differential interest from banks for prior period.

Ministry admitted and stated (October 2015) that Software used for monitoring the delay was being reviewed for timely updation of interest rate.

##### ***Recommendation no. 5***

Online payment of refund and drawback to the assesseees instead of by cheque may be ensured.

Ministry stated (October 2015) that efforts are underway to pay refund and drawback online and proposal to create e-PAO (refunds) is being considered for electronic payment of refund.

## Chapter V

### Issue of Show Cause Notice and Adjudication process

#### 5.1 Introduction

Adjudication is a quasi-judicial function of the officers of the Central Excise and Service Tax Department. Through imposition of an appropriate penalty after adjudication it seeks to ensure that no revenue loss is caused by the contravention of applicable laws/rules/regulations etc. However, if an innocent person is punished or the punishment is more than warranted by the nature of offence, it may undermine the trust between the Government and the tax payer. If, on the other hand, a real offender escapes the punishment provided by law, it may encourage commission of offences to the detriment of both, the Government and the honest taxpayers.

There may be situations relating to the demand of duty not paid, short paid or erroneously refunded, misclassification, Cenvat credit wrongly availed, imposition of penalty etc. It is mandatory that a show cause notice (SCN) is issued if the department contemplates any action prejudicial to the assessee. The SCN would detail the provisions of law allegedly violated and ask the noticee to show cause why action should not be initiated against him under the relevant provisions of the Act/Rules. Thus, an SCN gives the noticee the opportunity to present his case.

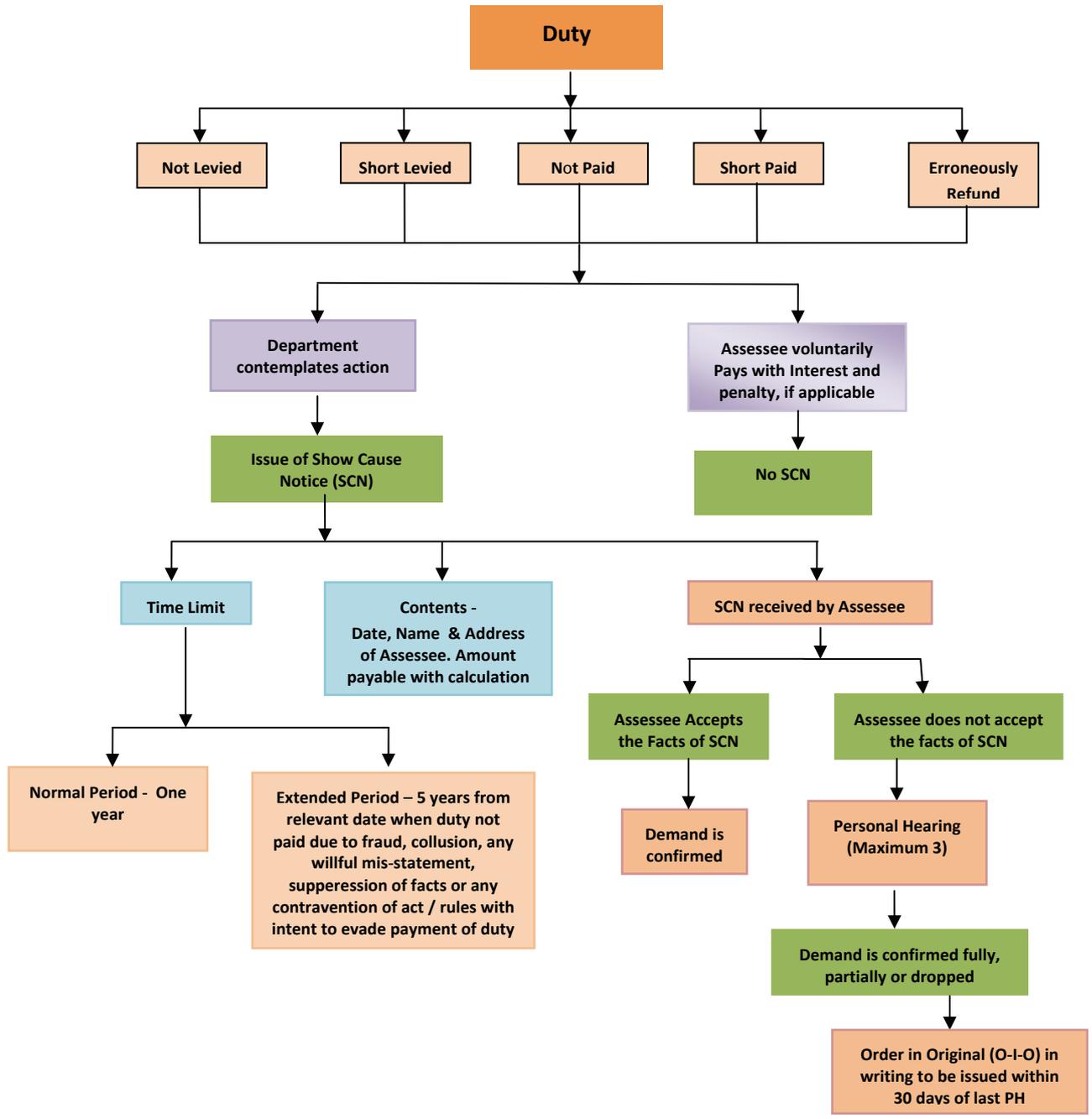
In the cases where duty has not been paid or short paid or erroneously refunded, SCN is to be served within one year from the relevant date in normal case and within five years from the relevant date in case of fraud, collusion, wilful suppression of facts, etc., with the intent to evade payment of duty or to get erroneous refund.

Further, it is provided in the Central Excise Act, 1944 that where it is possible to do so, the SCNs should be adjudicated within six month in normal cases and within one year in extended period cases, from the date of service of the notice to the person.

Adjudication proceedings shall be conducted by observing principles of natural justice. The noticee shall be given a personal hearing (PH) before deciding the case. There shall be a written Order in original (OIO) after the completion of adjudication process detailing facts of the case and justification of the adjudication order.

Thus the idea is to ensure prompt initiation and speedy disposal of the adjudication cases. The process of adjudication is shown in the chart overleaf:

**Chart 5.1: SCN & Adjudication Process under Section 11A of Central Excise Act, 1944**



## 5.2 Audit objectives

The objectives of this audit were to examine:

- a) the adequacy of rules, regulations, notifications, circulars/instructions etc. issued from time to time in relation to adjudication process;
- b) whether the extant provisions of law are being complied with adequately;
- c) whether there was an effective monitoring and internal control mechanism.

## 5.3 Scope of Audit and coverage

In this audit we covered 40 Commissionerates along with 84 Divisions and 70 Ranges falling under these Commissionerates. Further, we checked 1,737 adjudication cases yet to be finalized, 4,816 adjudicated cases, 320 draft SCNs pending for issue, 2,255 call book cases and 1,995 cases decided against revenue in adjudication stage. The period covered was 2011-12 to 2013-14.

## 5.4 Audit findings

We noticed irregularities in 809 cases involving revenue of ₹ 345.75 crore. The major findings are as under:

- (i) In 20 cases involving revenue of ₹ 4.40 crore, demands were concluded as time barred in adjudication due to late issue of SCN.
- (ii) In eight cases involving revenue of ₹ 2.28 crore, demands may get time barred due to late issuance of SCN.
- (iii) 196 cases involving revenue of ₹ 289.67 crore were pending for adjudication for more than one year as on 31 March 2014.
- (iv) 121 cases involving revenue of ₹ 29.76 crore were irregularly kept in call book.

The findings are discussed in subsequent paragraphs.

## 5.5 Issue of SCN

### 5.5.1 Invocation of extended period of time for issue of SCN

As per section 11A of the Central Excise Act, 1944 where any duty of excise has not been levied or has been short-levied or short-paid or erroneously refunded, central excise officer may, within one year from the relevant date, serve notice on the person chargeable with duty which has not been levied or paid or which has been short-levied or short-paid or erroneously refunded, requiring him to show cause why he should not pay the amount specified in the notice. Period of one year stands extended to five years where duty has been short-paid due to fraud, collusion, wilful mis-statement or suppression of facts with the intention to evade duty.

Test check of seven Commissionerates<sup>75</sup> revealed that issue of SCN invoking extended period on incorrect grounds in contravention of statute resulted in SCNs being time barred in the adjudication. We noticed 20 cases involving revenue of ₹ 4.40 crore. The Ministry accepted (November 2015) the facts in 17 cases and did not furnish reply in three cases. Two cases are illustrated below:

**5.5.1.1** We noticed in Rajkot Commissionerate that a SCN dated 21 September 2004 was issued to M/s Reliance Industries Ltd. for short payment of duty of ₹ 1.18 crore. Assessee had transferred various excisable goods to their inter divisional units by adopting the value of comparable goods instead of adopting the value at the rate of 115 per cent of the cost of production. Assessee had submitted a duly acknowledged copy of letter dated 21 September 2000 addressed to the department based on which it was claimed that department was duly informed about the practice adopted by them.

The Commissioner adjudicated the above SCN vide OIO 04 February 2013 and dropped the demand and noted that, "it is seen that the present SCN demanding duty for the period from July 2000 to August 2003 was issued on 21 September 2004. Therefore, SCN is time barred and cannot be sustained on the point of limitation". Therefore, not issuing SCN within time resulted in loss of revenue of ₹ 1.18 crore.

When we pointed this out (September 2014), the Ministry accepted the facts (November 2015) and stated that appeal filed by the department in CESTAT had also been rejected.

**5.5.1.2** In Thane-I Commissionerate, it was noticed that two units of M/s Omkar Speciality Chemicals Ltd. (OSCPL) were found evading payment of Central Excise duty on their finished product by misclassifying Potassium Iodide and Sodium Selenite as feed grade and classified under chapter heading 2309 attracting nil rate of duty, though these products were correctly classifiable under chapter 28 attracting duty at rate of 16 per cent. As per SCN issued (March 2011) by DGCEI, Zonal unit Mumbai, the assessee cleared excisable goods valued at ₹ 7.71 crore evading duty of ₹ 98.17 lakh from Unit-I and goods valued at ₹ 1.03 crore evading duty of ₹ 8.45 lakh from Unit-II during the period from 1 April 2007 to 22 February 2010 and 20 June 2009 to 13 February 2010 respectively. Accordingly the assessee paid (January/ February 2010) ₹ 24.21 lakh and ₹ 7.35 lakh in respect of Unit-I and Unit-II respectively at the time of investigation towards Central Excise Duty liability against the clearance of above said products.

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<sup>75</sup> Kolkata III, Kolkata V, Bolpur, Shillong, Delhi I, Rajkot & Thane I

Based on the judgment of CESTAT, Mumbai in the case of M/s SMZS Chemicals Ltd, {2006 (1193) ELT 46 (Tri-Mumbai)} and finding the case to be at par with their products, the assessee again started classifying the products under chapter 23.09 after issuing advance intimation (November 2006) to the jurisdictional Assistant Commissioner of Central Excise. The assessee had also sent three reminders to the department for verification and obtaining response from the department. However the department failed to give any response on this issue.

Commissioner of Central Excise, Thane-1 issued (June 2011) OIO concluding that the extended period under proviso to Section 11A (1) of the Central Excise Act, 1944 was not invocable in the instant case as there was no suppression of facts involved. It was further stated in OIO that in fact, the department was well aware of the facts since many years through intimations, communications, documents and technical literature as well as flow chart of manufacturing process, list of raw materials, list of actual users, audit reports, ER-1 returns, etc. and dropped the SCN as time barred. This resulted in loss of revenue to the extent of ₹ 75.06 lakh (excluding excise duty of ₹ 31.56 lakh paid by the assessee during investigation).

In reply, the Ministry stated (November 2015) that the department had filed an appeal in CESTAT which is pending for decision. Hence, at this stage it can not be concluded that there is a potential loss in Government revenue.

Therefore, had the Department been vigilant enough to issue Show Cause cum Demand Notices within the prescribed time frame as per extant statute, potential losses to the Government Exchequer as highlighted above could have been avoided.

### **5.5.2 Issue of Show Cause Notice**

One of the reasons for issue of SCN is the Audit Para raised during Internal Audit /CAG audit. The scrutiny of audit paras is done in the Monitoring Committee Meeting at Commissionerate level and these audit paras are deleted only after the issue of SCN. In this regard, Board has issued instruction dated 22 April 2013<sup>76</sup> that the audit objections should be settled within one year by issuing SCN.

Test check of six Commissionerates<sup>77</sup> revealed that non-issuance of SCN in contravention of statute which might result in these Show Cause cum Demand Notices being time barred. We noticed eight cases involving revenue

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<sup>76</sup> F. No. 208/04/2013/CX-6 dated 22 April 2013

<sup>77</sup> Kolkata V, Ranchi, Jaipur I, Bengaluru LTU, Thane I & Ahmedabad II

of ₹ 2.28 crore. The Ministry's reply (November 2015) had been received in two cases only and the cases are illustrated below:

**5.5.2.1** Kengeri Division of Bengaluru LTU Commissionerate confirmed a demand of ₹ 65.21 lakh along with interest for the period from 01 July 2000 to 31 March 2003 against M/s Toyota Kirloskar Motors Pvt. Ltd, for non-inclusion of promotional expenses incurred by their dealers in the transaction value of the products (multi utility vehicles, Passenger cars and parts thereof). The assessee preferred an appeal with Higher Authorities. The CESTAT in its final order dated 25 June 2007 allowed the appeal filed by the assessee. Against this final order, the department then preferred a Civil Appeal No.1389-1392/2008 before the Honorable Supreme Court of India, which was pending (August 2014). It was observed in audit that the department had not issued any SCN for the period from January 2004 to March 2006.

Scrutiny further revealed that the department issued periodical SCN on 6 April 2011 for the period from April 2006 to September 2010 for an amount of ₹ 21.19 crore. Since the extended Period cannot be invoked while issuing subsequent notices on the same or similar facts the demand raised for the period from April 2006 to March 2010 involving an amount of ₹ 18.47 crore would become time barred.

When we pointed this out (August 2014), the Ministry replied (November 2015) that the assessee furnished the details required for the period from August 2007 onwards, reluctantly and belatedly on 9 August 2010 after an inordinate delay of nearly three years from the date of first letter (31 August 2007), consequent to relentless persuasions and innumerable reminders. Hence, there was suppression of facts with the intent to evade duty and there was nothing wrong in invocation of extended period for issuing subsequent SCN. As regards, non-issue of SCN for the period mentioned in audit objection, the matter is under enquiry.

The reply of the Ministry is not acceptable because the extended period to issue the SCN is to be used in exceptional cases only and not in a matter of routine.

**5.5.2.2** M/s Hindustan Coca Cola Beverages Pvt. Ltd in Range III of Kalyan I Division under Thane I Commissionerate engaged in manufacture of goods under Chapter 22 availed Service tax credit on Goods Transport Agency Service (GTA) for outward transportation of finished goods, Catering Services and other ineligible credits during the period April 2006 to March 2011. The SCN issued in this regard in May 2011 for ₹ 1.75 crore was confirmed by the Commissioner (August 2011) and a penalty of ₹ 1.75 crore was imposed. The

issue is since pending in CESTAT. We noticed that during the period April 2011 to March 2014, the assessee availed service tax credit of ₹ 1.45 crore on GTA Services for outward transportation and Catering Services. To safeguard loss of revenue, Department should have issued periodical SCN for the aforesaid period also but no such SCN had been issued (December 2014).

When we pointed this out (May 2014), the Ministry accepted (November 2015) the facts and stated that combined SCN including the said availment of Cenvat credit for period April 2011 to March 2014 has been issued by CCE- Thane-I on 20 June 2014 for the amount of ₹ 1.74 crore. Further, the department has issued periodical SCN dated 30 April 2015 for the period April 2014 to November 2014 for ₹ 5.29 lakh.

## 5.6 Completeness of Show Cause Notices

SCN is the foundation on which the demand is based and it is a pre-requisite for any demand under indirect taxes. Principles of natural justice fully apply to SCN e.g. all evidence on which department wants reply should be disclosed. SCN should give all essential particulars. Amount demanded must be indicated in the SCN. The notice should state nature of contravention and provisions contravened. Charges should be informed. Grounds should be mentioned. If penalty is proposed to be imposed, this should be mentioned in the notice. Above all, the SCN should not be vague, confusing or self-contradictory. If SCN is based on one ground, demand cannot be confirmed on other ground.

During scrutiny it was revealed that five SCNs in three Commissionerates<sup>78</sup> were found to be erroneous. Ministry accepted (November 2015) the facts in one case. The Ministry did not furnish reply in rest of the cases (December 2015).

## 5.7 Procedure of Adjudication

Sub-section (2A) of section 11A of Central Excise Act, 1944 provides that in case any duty of Excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded, by reason of fraud, collusion or any willful mis-statement or suppression of facts, or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty, where it is possible to do so, the adjudicating authority shall determine the amount of such duty, within a period of one year; and, in any other case, where it is possible to do so, he shall determine the amount of duty of Excise which has not been levied or paid or has been short-levied or

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<sup>78</sup> Kolkata III, Kolkata V & Shillong

short-paid or erroneously refunded, within a period of six months, from the date of service of the notice on the person under sub-section 11A(1).

### 5.7.1 Pending Adjudication cases

Scrutiny of records in 16 Commissionerates<sup>79</sup>, Division and Ranges revealed that in 196 cases, the department failed to adjudicate the cases upto 31 March 2014 resulting in blockage of revenue of ₹ 289.67 crore. The pendency ranges between six months to ten years beyond one year of issue of SCN.

The issue was pointed out to the Department (July to November 2014). In most of the cases the Ministry accepted the facts and stated (November 2015) that the main reason for non-adjudication of cases was due to absence/frequent transfer of regular adjudicating officers.

A few interesting cases are illustrated below:

**5.7.1.1** In Ranchi Commissionerate a SCN was issued to M/s SAIL, Bokaro in May 2011 for contravention of provision of Section 4(1)(b) of Central Excise Act and Valuation Rule 2000 for evading payment of ₹ 5.32 lakh for the period 2006-07. In response to the SCN, M/s SAIL Bokaro had submitted its reply on 14 May 2012 with request to give personal hearing before the final decision. But no date was granted to the assessee by the department nor any other action has been taken in this case. The case has not been adjudicated even after a lapse of more than two years.

When we pointed this out (September 2014), the Ministry stated (November 2015) that the case will be adjudicated soon.

**5.7.1.2** M/s Ramsarup Industrial Corporation in Kolkata-III Commissionerate was issued a SCN dated 30 April 2010 for ₹ 1.68 crore based on our observation. The issue was transferred to Call Book on 06 May 2010 on being contested by the Department. The case had been brought out from Call Book on 27 July 2011 for adjudication. We further observed that during process of adjudication, the Department had adjourned Personal Hearing six times on assessee's request (6<sup>th</sup> PH being on 12 April 2012) in place of statutory three times. The assessee appeared before the adjudicating authority (i.e., Commissioner of Central Excise, Kolkata-III Commissionerate) on 21 June 2012 and requested for verification of invoice by the concerned Range Officer. But the said verification was not done and consequently, the issue remained pending for adjudication till 31 October 2014.

When we pointed this out (November 2014), the Ministry stated (November 2015) all efforts are being made to issue the adjudication orders in the

<sup>79</sup> Kolkata III, Kolkata V, Delhi I, Delhi II, Delhi LTU, Shillong, Bolpur, Guwahati, Raigad, Kanpur, Bhopal, Jaipur I, Jaipur II, Puducherry, Chandigarh I & Ranchi

suggested time limit after personal hearing. But due to the unavoidable circumstances, such as time bound work pending with adjudicating authority, further documents/verification of documents submission by the party, the adjudicating authority has not been able to issue the orders in time. However, the audit objection has been taken note for compliance.

Thus, the department failed to comply with the provisions of the extant statutes to adjudicate the said cases within the prescribed time frame in these cases.

### **5.7.2 Fixing of personal hearing**

As per Section 11A of the Central Excise Act, 1944 the SCN should be adjudicated within six months/one year from the date of SCN as far as possible.

On scrutiny of the SCNs and Adjudication files in five Commissionerates<sup>80</sup>, it was noticed that the first Personal Hearing was fixed after inordinate delay in 20 cases. We observed that there was delay ranging between 371 days and 4,641 days which resulted in adjudication process getting delayed.

When we pointed this out (June 2014), the Ministry accepted (November 2015) the facts in most of the cases and stated that reason for delay is due to change of adjudication authorities and time taken in verification of facts mentioned in the SCN for following the principal of natural justice.

### **5.7.3 Grant of personal hearing**

Section 33A (1) of Central Excise Act, 1944 provides that the Adjudicating Authority may, if sufficient cause is shown, at any stage of proceedings grant time, from time to time, to the parties or any of them and adjourn the hearing for reasons to be recorded in writing, provided that no such adjournment shall be granted more than three times to a party during the proceeding.

Scrutiny of records revealed that in 49 cases in nine Commissionerates<sup>81</sup> the department, while adjudicating the demand cases, granted more than three adjournment to the assesseees in contravention of the above statutory provision.

The number of adjournment ranges from 4 to 9.

When we pointed this out (May to November 2014), the Ministry accepted the facts in most of the cases and stated (November 2015) that the reasons for giving more PH was change of adjudication authorities, due to the fact

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<sup>80</sup> Ahmedabad II, Rajkot, Alwar, Jaipur I & Jaipur II

<sup>81</sup> Kolkata III, Guwahati, Ahmedabad II, Jaipur I, Jaipur II, Chandigarh I, Delhi I, Belapur & Kanpur

that to deliver natural justice effective hearing was necessary and hence more PH was given and in most of the cases assessee asked for the same.

The reply of the Ministry is not acceptable as the Section 33(A) *ibid* categorically provides for maximum three adjournments of hearing.

#### **5.7.4 Issuance of adjudication orders within stipulated period after completion of personal hearings**

As per Board's Circular dated 5 August 2003<sup>82</sup> in all cases where personal hearing have been concluded it is necessary to communicate the decision immediately or within a reasonable time of 5 days. Where for certain reasons, the above time limit cannot be adhered to in a particular case, the order should be issued within 15 days or at most one month from the date of conclusion of personal hearing.

Scrutiny of records in 23 Commissionerates<sup>83</sup> and Divisions revealed that the department failed to adjudicate in 342 cases within the prescribed time frame of one month from the date of conclusion of personal hearing. The delay ranges between 2 days to 333 days (in excess of 30 days from the date of completion of last personal hearing granted to the parties.

When we pointed this out (between June 2014 and November 2014), the Ministry while admitting the facts (November 2015) stated that in most of the cases the delay was due to seeking comments from division office in respect of reply filed by noticee, non- submission of additional documents timely by the assessees. Further, it was reiterated that the Adjudication authority always try to dispose of the cases within prescribed time limit in most of cases but in certain cases where some difficult question of law crops up and where the case law and defence require detailed examination vis-a-vis the allegations of SCN, strict adherence to time limit prescribed is not feasible.

The reply of the Ministry is not acceptable as the Board had fixed the maximum limit at one month after last PH hence either the departmental officers shall adhere to this timeline or the Board may revise the time limit suitably for exceptional cases.

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<sup>82</sup> Circular No. 732/48/2003-CX dated 5 August 2003

<sup>83</sup> Kolkata III, Kolkata V, Bolpur, Guwahati, Noida, Kanpur, Delhi I, Delhi II, Indore, Bhopal, Mumbai LTU, Belapur, Aurangabad, Raigad, Coimbatore, Chennai II, Cochin, Vadodara I, Jaipur I, Jaipur II, Hyderabad II, Chandigarh I & Panchkula

## 5.8 Adjudication of remanded cases

**5.8.1** Sub-section (1) of section 11A of Central Excise Act, 1944 provides that Central Excise Officer shall determine amount of duty of excise within six months from the date of notice where it is possible to do so in normal case and within one year from the date of notice, where it is possible to do so in case of any duty of Excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded, by reason of fraud, collusion or any wilful mis-statement or suppression of facts, or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty. In de-novo cases, when case is remanded to original authority, the case should be taken as afresh case and decided accordingly.

Scrutiny of records in five Commissionerates<sup>84</sup> revealed that the department in eight cases failed to adjudicate the de-novo cases in time. Delay ranges between 2 to 10 years. Ministry accepted (November 2015) the facts in all but one case. Two interesting cases are narrated below:

**5.8.1.1** In Guwahati Commissionerate, we observed that in case of M/s Assam Asbestos Ltd. [SCN dated 13 July 2001] the department confirmed demand of ₹ 12.02 lakh vide Order dated 25 July 2002. Being aggrieved the assessee preferred an appeal to CESTAT against the impugned order. CESTAT in its Order dated 27 May 2005 remanded the case for de novo adjudication. Audit observed that the case was personally heard on 12 November 2010 after a lapse of more than five years but was not decided by the then Commissioner. Again the case was heard on 26 November 2012 and finally De novo adjudication order was issued on 11 March 2013. Thus, the department took more than seven years to complete the adjudication process afresh in the instant case.

In reply (November 2015) the Ministry accepted the facts and regretted the delay. It further, stated that due care will be taken to finalize the remand cases within prescribed time.

**5.8.1.2** In Raigad Commissionerate, the SCN issued to M/s Nippon Denro Ispat Ltd. was initially adjudicated (February 1997) by Commissionerate Mumbai III. However, this case was remanded for de-novo adjudication (November 2003) by CESTAT. Though the file was submitted for deciding the adjudicating authority during 2004 and 2005, no further action was taken till 2013 and Personal hearing was conducted (August 2013) and the case adjudicated (November 2013) after 10 years of CESTAT order for de-novo

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<sup>84</sup> Vadodara I, Noida, Kanpur, Guwahati & Raigad

adjudication. The adjudication of the case was delayed due to insufficient monitoring of the cases pending for adjudication.

In reply (November 2015) the Ministry accepted the facts and stated that delay was due to re-organisation of the Commissionerate and for following the principals of natural justice.

Audit noticed that there was inordinate delay in adjudicating the remand cases contravening the codal provisions cited supra.

### **5.8.2 Cases remanded by Commissioner (Appeals)**

As per Section 35A(3) of Central Excise Act, 1944, the Commissioner (Appeals) shall, after making such further inquiry as may be necessary, pass such order, as he thinks just and proper, confirming, modifying or annulling the decision or order appealed against.

Further, Board's Circular dated 18 February 2010<sup>85</sup> clarified that the power of remand by the Commissioner (Appeals) has been taken away by amending section 35A with effect from 11 May 2001 under the Finance Bill, 2001.

Scrutiny of records in four Commissionerates<sup>86</sup> revealed that in seven cases the Commissioner (Appeals) remanded the cases contravening the statutory provisions cited supra.

Remand of the cases by the Commissioner (Appeals) was, thus, in contravention of the statutory provisions read with Board's clarification cited supra.

When we pointed this out (November 2014), the Ministry stated (November 2015) that Commissioner (Appeal) still has power to remand matter as also held by Honorable CESTAT in the case law reported at {2014(302) ELT 244 (Tribunal Delhi)}. The said judgment of CESTAT was passed by placing reliance on the judgment passed by the Honorable Supreme Court in the case of UOI vs Umesh Dhaimode {1998 (98) ELT 584(S.C.)}. The Honorable High court of Gujarat's judgment reported {2004(173)ELT 117(Gujarat)} has also confirmed this views.

The reply of the Ministry is not acceptable as Honorable Supreme Court in its judgment dated 1 March 2007<sup>87</sup> has observed that power of remand by the Commissioner (Appeal) has been taken away by amending Section 35A with effect from 11 May 2001. Subsequent to which the Board issued above mentioned clarification asking its field formation to strictly follow the judgment.

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<sup>85</sup> F.No.275/34/2006-CX.8A dated 18 February 2010

<sup>86</sup> Jaipur I, Kolkata III, Noida & Belapur

<sup>87</sup> MIL India Ltd. [2007(210)ELT 188 (SC)]

## 5.9 Effectiveness of monitoring and Internal Control

Monitoring and Internal Control is an integral process which addresses risk and provides reasonable assurance about effectiveness and adequateness of system and procedures. We noticed the following inadequacies in this regard.

### 5.9.1 Adjudication of call book cases

As per Board's Circular dated 14 December 1995<sup>88</sup>, the following categories of cases may be transferred to Call Book with the approval of the Competent Authority:

- (i) Cases in which the Department has gone in appeal to the appropriate authority.
- (ii) Cases where injunction has been issued by Supreme Court/ High Court/ CEGAT, etc.
- (iii) Cases where audit objections are contested.
- (iv) Cases where the Board has specifically ordered the same to be kept pending and to be entered into the call book.

Again, the Board had emphasized<sup>89</sup> that Call Book cases should be reviewed every month. The Director General of Inspection (Customs and Central Excise) had reiterated (December 2005) the need for monthly review stating that review of Call Book cases may result in substantial reduction in the number of unconfirmed demands in call book.

During test check we noticed 30 cases having monetary implication of ₹ 18.20 crore kept in Call Book as on 31 March 2014 in Kolkata V Commissionerate, where periodical review of the cases was not done.

Scrutiny of files revealed that four cases amounting to ₹ 5.34 crore and 10 cases amounting to ₹ 3.29 crore were pending for more than five years and three years respectively.

A case in point is narrated below:

The case of M/s Flakt India Ltd. involving revenue of ₹ 1.23 crore [SCN dated 25 April 1986] was pending for more than ten years from the date of entry in the call book and twenty five years from issue of SCN. The case was transferred to call book on the grounds of Writ Petition (W. P. No. 5086 of 1987) in Kolkata High Court filed by the assessee. The department approached Sr. Central Government Advocate to make necessary

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<sup>88</sup> Circular No. 162/73/95-CX dated 14 December 1995

<sup>89</sup> DO F No. 101/2/2003-CX-3 dated. 03 January 2005

arrangement for early listing and hearing of the case in July 2004 since then no further progress was made till the date of audit. All this indicates lackadaisical approach on the part of the department to dispose of the case pending for a very long time in Call Book.

When we pointed this out (July 2014), the Ministry stated (November 2015) that cases have been kept in call book as department has gone in appealing similar cases. But the fact remains that these cases are pending for very long time and no proactive action has been taken by the department to clear the pendency.

### **5.9.2 Monitoring of Call Book cases**

Scrutiny of records in 14 Commissionerates<sup>90</sup> for the period 2011-12, 2012-13 and 2013-14 revealed that the call book register was not maintained properly and not reviewed on regular basis. DGICCE also pointed out the irregularity in their report. Despite this, 121 cases having monetary implication of ₹ 29.76 crore were found to be kept in Call Book irregularly. Some of the reasons for this error were, non-approval of the competent authority to transfer the case to Call Book, paras kept pending in Call Book although decisions in similar cases was given by higher authorities and paras kept pending in Call Book on the ground of contesting CAG para although either no SOF/DP issued by CAG in these cases or paras closed by CAG etc. Ministry accepted the facts (November 2015) and stated that remedial action is being taken now.

Some interesting cases are narrated below:

**5.9.2.1** The Board in its Circular dated 12 January 2005<sup>91</sup> categorically clarified that where the cases remanded back for de-novo adjudication, it should be decided by an authority which pass the said remanded order i.e the original adjudicating authority.

Scrutiny of records of Kolkata-V Commissionerate revealed that in a case of M/s Jay Engineering Works Ltd. which was remanded back for De-novo adjudication by CESTAT Kolkata. The Department filed Miscellaneous Application vide appeal No. 198/2008 to ascertain the adjudication authority for such De-novo adjudication. Despite there being categorical instructions from Board, the department still made a miscellaneous application to CESTAT in 2008 to ascertain the adjudicating authority. As such, the case was transferred to the call book on account of the case lying in the appellate forum, though the case could have been adjudicated following the Board's clarification *ibid*.

<sup>90</sup> Jaipur I, Jaipur II, Delhi I, Delhi II, Noida, Calicut, Cochin, Bhopal, Chennai II, Vadodara I, Chandigarh I, Guwahati, Kolkata V & Bolpur

<sup>91</sup> Board's circular no. 806/3/2005-CX dated 12 January 2005

In a similar case under Bolpur Commissionerate, an issue relating to the period 24 November 1980 to 08 October 1985 against M/s Eastern Biscuits Company Ltd., had been retained in Call Book since 21 October 2008 citing CESTAT, Kolkata Order dated 07 July 2006 in which CESTAT remanded the case for re-adjudication after finalization of provisional assessment by the proper officer. We also observed that during periodical review of Call Book cases in December 2011, the Commissioner of said Commissionerate opined in the Review Sheet that no reason persisted to keep the case in Call Book. However, the case remained in the Call Book till 21 August 2014. Though the case did not fall into any category as cited supra for keeping a case in Call Book, yet the Department kept the case irregularly in the Call Book.

When we pointed this out (July to August 2014), the Ministry (November 2015) in case of M/s Jay Engineering Works Ltd stated that concerned adjudicating authority has been advised for De-novo adjudication of the case as per Board's Circular. In case of M/s Eastern Biscuits Co Ltd stated that De-novo adjudication could not be submitted due to non-finalization of provisional assessment by the Divisional Deputy Commissioner. Subsequently, the case was transferred to Durgapur Commissionerate.

**5.9.2.2** In Noida Commissionerate, a SCN was issued on 05 November 2001 to M/s Hongo India (P) Ltd demanding Modvat credit of ₹ 8.43 crore wrongly availed during the period 10 March 1999 to 15 November 2000 on which the department filed Special Leave Petition, which was dismissed by Honourable Supreme Court on 27 March 2009. Despite the order of Honourable Supreme Court, these cases along with five other cases of similar nature were irregularly retained in call book even after the lapse of five years.

When we pointed this out (September 2014), the Ministry accepted the facts and stated (November 2015) that the case of M/s Hongo India Pvt Ltd has been taken out from the call book in March 2015 in view of the dismissal of the departmental appeal by the Apex court.

**5.9.2.3** According to Board's circular dated 3 February 2010<sup>92</sup>, the cases of CAG audit objections where contested and not received any reply from the CAG even after one year and also where no SOF and DAP are pending have to be taken from Call Book and to be adjudicated on merit of the case.

In Bolpur and Vadodara-I Commissionerate, it was noticed that the following cases were transferred to Call Book in respect of contested CAG audit objection but irregularly retained in Call Book even after the closure of Para raised by CAG:

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<sup>92</sup> F. No. 206/02/2010-CX-6 dated 03 February 2010

Table 5.1

Assessee	Commissionerate	Entry in Call Book	CAG audit objection status	Closure by CAG
M/s Durgapur Steel Plant	Bolpur	July 2005	SF No. 102/99-2000 DAP No.63/99-2000	September 2005
M/s Durgapur Steel Plant	Bolpur	June 2006	SF No. 105/99-2000	September 2005
M/s Sri Vasavi Industries Ltd.	Vadodara I	March 2012	IR No. CERA/IR/Bol/10-11/921	October 2012
M/s Gujarat Alkalies and Chemicals Limited	Vadodara I	April 2003	DAP-64/2005-06.	May 2008

This implies lack of proper monitoring of Call Book.

When we pointed this out (June to August 2014), the Ministry stated (November 2015) that all these three cases have been taken out of Call Book during October 2014.

Despite the continuing concern of the Board regarding periodical review and disposal of call book cases by the department, lapses on the part of the department still persist.

### 5.9.3 Monitoring mechanism of reporting through MTR

The Board vide letter dated 23 May 2003<sup>93</sup> had instructed the Commissioners and Chief Commissioners to analyze the reasons of pendency of adjudication cases and strengthen the monitoring system. Annexure-IV and IVA of the Monthly Technical Reports (MTR) incorporate information relating to adjudications and their disposals.

There are certain annexure on MTR relating to adjudications and their disposals, reasons for pendency, unconfirmed demands, call book cases pending etc. Some of these are monitored by DGICCE. The Chief Commissionerates forward the same to the monitoring authorities. The relevant annexure include Annexure II, IV, IVA, VII and XI.

Scrutiny of records in seven Commissionerates<sup>94</sup> revealed that there was discrepancies in figures between MTR and other records (335J Register / adjudication Register) maintained in the department. The Ministry accepted the facts (November 2015) in most of the cases and stated that due care is taken now.

<sup>93</sup> Letter No. 296/2/2003-CX dated 23 May 2003

<sup>94</sup> Delhi I, Kolkata III, Bolpur, Bhopal, Indore, Raipur & Rajkot

A case in point is narrated below:

In Bolpur Commissionerate, Audit scrutiny revealed that the Call Book cases were not reviewed on monthly basis. Reconciliation of call book register with MTR revealed that although there were 114 cases as on 31 March 2014 of more than 2 years old but in the MTR no case was shown as above 2 years old. Moreover, there were 5 cases in the call book which were more than 8 years old.

When we pointed this out (August 2014), the Ministry stated (November 2015) that proper records are being maintained now.

#### **5.9.4 Maintenance of registers**

The Board in its Circular dated 24 December 2008<sup>95</sup> envisaged the functions, responsibilities and duties to be performed by Range Officers and Sector officers under the Central Excise Act, 1944 and the rules made there under for maintenance of proper records/ registers and timely review and prepare monthly abstract.

Scrutiny of records in 10 Commissionerates<sup>96</sup> revealed that there was lack of proper monitoring in respect of preparation and maintenance of 335J, Confirmed/Unconfirmed Demand; Adjudication, Call Book registers etc.

The issues were pointed out to the Department (July to November 2014). In reply, the Ministry accepted the facts (November 2015) in most of the cases and stated that registers are being maintained properly now.

#### **5.9.5 Internal control in respect of preparation and issuance of SCN**

The Board vide letter dated 23 May 2003<sup>97</sup>, had instructed the Commissioners and Chief Commissioners to do the analysis of the reasons of pendency of adjudication cases and strengthen the monitoring system.

Scrutiny of records in nine Commissionerates<sup>98</sup> revealed that there was lack of proper monitoring in respect of preparation and issue of SCN, analysis of the reasons of pendency of SCNs for adjudication, review of call book etc.). Ministry accepted (November 2015) the facts in most of the cases.

Some interesting cases are cited overleaf:

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<sup>95</sup> Circular No. F. No. 224/37/2005-CX-6 dated 24 December 2008

<sup>96</sup> Delhi II, Bhopal, Mumbai LTU, Raigad, Jaipur I, Noida, Kanpur, Ranchi, Jamshdepur & Cochin

<sup>97</sup> Letter No. 296/2/2003-CX.9 dated 23 May 2003

<sup>98</sup> Delhi V, Kolkata V, Indore, Bhopal, Jamshedpur, Ranchi, Bolpur, Rajkot & Noida

**5.9.5.1** As per Board's instructions dated 29 April 1965<sup>99</sup>, Adjudicating officers should guard against passing two formal adjudication orders on the same case. The legal position in this respect is that, where a matter has already been adjudicated by the competent authority and another order of adjudication is passed relating to the same transaction subsequently, the second order is a nullity. The authority who undertakes the enquiry resulting in the second adjudication acts without jurisdiction. The second order being a nullity, it should be taken as not to exist at all. When the fact of such an order having been passed is brought to light, the records should be corrected, the order deleted from the record and the party affected informed accordingly.

(i) In Kolkata V Commissionerate, in the case of M/s Design Era Pvt. Ltd., it was noticed that a demand of ₹ 10.91 lakh was raised under violation of Rule 4, 5, 6, 8, 10, 11 and 12 of the Central Excise Rules, 2002 covering the period 2006-07 to 2009-10 vide SCN dated 02 May 2011. Further, on 24 May 2011, another show cause cum demand notice of ₹ 49.13 lakh was issued to the assessee under the same ground covering same period vide SCN dated 24 May 2011. Both SCNs were adjudicated vide OIO dated 20 February 2012 confirming the two demand cases for the same period and same issue. Audit scrutiny further revealed that no corrigendum was issued on this account. Thus, issuance of two show cause cum demand notices for two different amounts covering the same period and for same grounds of allegations seems irregular in light of the extant statutes.

In reply, the Ministry accepted (November 2015) the facts and stated that mistake is regretted and observation of the audit has been noted for future reference.

(ii) In a similar case of M/s Sreeleathers, in Kolkata V Commissionerate issued Two SCNs dated 05 March 2012 demanding duty of ₹ 19.20 lakh and ₹ 23.55 lakh respectively for same issue and for the same period from 01 February 2011 to 30 June 2011 for violation of Section 6 of the Central Excise Act, 1944 read with Rule 9 of Central Excise Rules, 2002.

In reply, the Ministry accepted (November 2015) the facts and stated that mistake is regretted and observation of the audit has been noted for future reference.

(iii) Similarly, Bolpur Commissionerate issued a demand of ₹ 9.60 crore (SCN dated 16 June 2011) to M/s Durgapur Steel Plant for irregularly availing of Cenvat credit during the period from June 2006 to March 2011. In the process of adjudication the department found that two other SCNs, dated 03 February 2010 and dated 20 December 2010 were issued to the assessee

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<sup>99</sup> F. No. 18/18/65-CXIV dated 29 April 1965

already included a portion of the demand amount raised in the SCN dated 16 June 2011. Thus there was duplication of demands as observed by the department while passing the adjudication order [Order dated 13 December 2011] of the demand notice dated 16 June 2011. The department had no option but to drop an amount of ₹ 37.82 lakh which was demanded through SCN dated 03 February 2010 [amounting to ₹ 31.01 lakh confirmed on 10 August 2010] and SCN dated 20.12.2010 [amounting to ₹ 6.81 lakh confirmed on 20 July 2011]. This duplication of demands for the same period indicates poor control mechanism persisting in the department for issue of show cause cum demand notices.

In reply, the Ministry accepted (November 2015) the facts and stated that mistake is regretted and the officers have been sensitized to prevent recurrence of such lapses.

**(iv)** In Division-I under Rajkot Commissionerate we observed that a SCN dated 26 July 2011 for ₹ 0.52 lakh was issued to M/s Star Industries which was adjudicated and dropped by the Assistant Commissioners of Central Excise vide OIO dated 16 January 2012. Audit further noticed that the Assistant Commissioner of Service Tax Division had also issued another SCN to same assessee for same transaction and amount. (SCN dated 30 September 2009), which was subsequently confirmed by the same authority vide OIO dated 16 August 2010, against which assessee preferred an appeal before the Commissioner (A), Rajkot. The Commissioner (A) vide OIA dated 14 December 2010 stated that the instant case might be pertaining to wrong availing of Cenvat credit by the appellant in the capacity of manufacturer for which the demand, if any, should have been made by the jurisdictional Central Excise Assistant Commissioner.

This shows that two different adjudicating authorities had adjudicated the same issue in different way. While one had confirmed the demand, the other had dropped the same.

When we pointed this out (July to October 2014), the Ministry stated (November 2015) M/s Star Industries is a case of suppression of fact and hence it does not fall within the criteria of case to be adjudicated by the jurisdictional range superintendent and falls within exclusion category-B.

The reply of the Ministry is not correct as the audit objection was related to issuance and adjudication of two SCN in one case.

This implies that there was lack of proper monitoring in respect of preparation and issue of SCN.

## **5.10 Conclusion**

It was noticed during audit that the journey of SCN right from the first step of issue of SCN till its adjudication was fraught with delays and shortcomings. Administrative efficiency requires that the work is done in minimum possible time. The maximum time limits define the outer boundaries for completion of tasks. The time limit prescribed for issue of SCN was one year with provision to invoke extended period of five year for specific circumstances. But instead, it was seen that the extended period was used as a routine provision rather than a rare exception. Thus there is a need to reduce delays in various stages of issue and processing of SCN by systematic monitoring so that interests of both the government revenue and the assessee are protected.

## Chapter VI

### Non-Compliance with Rules and Regulations

#### 6.1 Introduction

We examined the records maintained by the assesseees in relation to the payment of Central Excise duty and checked the correctness of duty payment and availing of Cenvat credit. We noticed cases of incorrect availing/utilisation of Cenvat credit, non/short payment of Central Excise duty and other issues involving revenue of ₹ 98.79 crore. We communicated these observations to the Ministry through 26 draft audit paragraphs. The Ministry/Commissionerate accepted (December 2015) the audit observations in 25 draft audit paragraphs and initiated/completed corrective action in 22 cases involving revenue of ₹ 95.94 crore which are listed in Appendix II. The Ministry is yet to respond to one draft paragraphs (December 2015). The objections are covered under three major headings :

Non-payment / Short payment of Central Excise duty

Cenvat credit

Other issues

#### 6.2 Non-payment / Short payment of Central Excise duty

We noticed nine cases where duty was not paid/short paid. Ministry/department admitted observation in eight cases and initiated/taken corrective action in seven cases. These seven cases are detailed in appendix II. Remaining two cases are illustrated in following paragraphs:

##### 6.2.1 Non-levy of duty on additional consideration as Sales Tax remission

As per Section 4(1)(a) of the Central Excise Act, 1944, when the duty of excise is chargeable on any excisable goods with reference to their value, then such value shall be the transaction value. Transaction value means the price actually paid or payable for the goods when sold, and includes in addition to the amount charged as price, any amount that the buyer is liable to pay to or on behalf of, the assessee, by reason of, or in connection with the sale whether payable at the time of the sale or at any other time, including, but not limited to, any amount charged for, or to make provision for, advertising or publicity, marketing etc or any other matter, but does not include the amount of duty of excise, sales tax and other taxes, if any, actually paid or actually payable on such goods.

The Government of Maharashtra introduced the Package Incentive Scheme for deferred payment of Sales Tax whereby the assessee was allowed to collect Sales Tax from the buyer and retain 75 per cent and repay it after prescribed period. The Government of Maharashtra thereupon amended the provisions of Sales Tax Act and issued a Notification in November 2002 providing further incentive for premature repayment of Sales Tax liability.

Supreme Court in its judgment dated 28 February 2014 in case of M/s Super Synotex (India) Ltd. (2014-TIOL-19-SC) on similar issue already made it clear that the 75 per cent of Sales Tax retained by the assessee would form part of Assessable value and Excise duty is payable. Board also issued instructions vide F.No.6/8/2014-CX.1 dated 17 September 2014 on similar lines in light of above judgment and instructed that similar cases may be finalized on this ground.

M/s Garodiya Special Steel Ltd. in Raigad Commissionerate, engaged in the manufacture of Steel Bar, Billets, Ingots etc had opted for premature repayment of Sales Tax deferred liability during the year 2010-11 and 2011-12 under the above mentioned scheme. Scrutiny of the financial records of the assessee revealed that he had received discount of ₹ 5.26 crore due to premature prepayment of sales tax liability accrued at Net Present Value (NPV). The difference between the actual sales tax collected from customers and the payment made at NPV was shown as income in the accounts. Non-inclusion of sales tax amount collected but not paid to the Government in the assessable value resulted in undervaluation of goods to the extent of ₹ 5.26 crore with consequential short levy of ₹ 54.18 lakh which was recoverable with interest.

When we pointed this out (August 2012), department did not admit the objection and stated (March 2015) that SCN amounting to ₹ 85.99 lakh was under process of issue. However, department did not furnish reason for not accepting the objection.

Reply is not tenable as similar issues were reported in Audit Report No. 7 of 2015 (para 5.2.3) and Board issued specific instructions dated 17 September 2014 to deal such cases on the basis of Supreme Court judgment cited supra. Further, similar issue in Nasik Commissionerate (refer para 7.3.2.9 ) has been accepted by the department.

Reply of the Ministry was awaited (December 2015).

### **6.2.2 Short payment of duty due to adoption of incorrect value by Job Worker**

As per Rule 17 of the Central Excise Rules, 2002, removal of goods from Export Oriented Unit (EOU) to Domestic Tariff Area (DTA) shall be made under an invoice and on payment of appropriate duty. Such unit shall maintain proper account relating to production, description of goods, quantity removed, duty paid and each removal made on an invoice. The unit shall also submit monthly Return form ER-2 to the Excise department. Rule 10-A of Central Excise Valuation (determination of price of excisable goods) Rules, 2000, prescribes that for goods manufactured on job work basis on behalf of a person (commonly known as principal manufacturer), the value for payment of excise duty would be based on the sale value at which the principal manufacturer sells the goods, subject to the condition that the buyer and seller are unrelated and the price being the sole consideration for sale. As per Rule 9 of Central Excise Rules, 2002, every person who manufactures or deals in excisable goods shall get himself registered with the Central Excise department and non-compliance would be liable for penal action.

M/s Tamil Nadu Minerals Limited (TAMIN), Chennai (not registered with Central Excise department) entrusted the job work of manufacture of Granite/Skirting slabs and Pillars to M/s PRP Exports, a 100 percent EOU by supplying rough blocks (Non excisable item). After processing the Rough Blocks, M/s PRP Exports cleared the goods (Polished slabs) to TAMIN, by delivering the goods at the agreed place (construction site) through Excise invoice, on payment of excise duty worked out on the agreed processing charges (November 2009 to February 2010). The goods were ultimately sold (November 2009 to January 2011) by TAMIN to M/s East Coast Construction and Industries Limited (ECCIL), Chennai.

On scrutiny of the sale invoices of TAMIN raised on M/s ECCIL, Chennai, audit noticed that TAMIN had realized ₹ 15.66 crore towards sale of said goods on which the duty liability worked out to ₹ 2.42 crore. However, the duty paid for the clearances of the above goods by M/s PRP Exports on behalf of TAMIN was only ₹ 1.21 crore which was worked out on the basis of job charges collected by M/s PRP Exports from TAMIN, which resulted in short levy of duty of ₹ 1.20 crore.

The objection was communicated to the Central Excise Commissionerate, Madurai (September 2011) and also to the Development Commissioner, MEPZ (October 2011). Development Commissioner forwarded (June 2012) a copy of the reply received from M/s PRP Exports, EOU wherein it was stated

that the transaction were over as soon as the goods were delivered to TAMIN through their sale bills and also there were no express or implied terms in the contract with regard to further sale by TAMIN and the transaction value entered in to by TAMIN with the third parties. However, as per terms of agreement TAMIN had entrusted to M/s PRP Exports, the entire activity of manufacture and transport of finished goods to the delivery point and payments are to be made at three stages – 70 per cent on sending bill to TAMIN, 25 per cent on receipt of slabs at construction site and balance after satisfactory laying in the building. As M/s PRP Exports, manufactured and delivered excisable goods on job work basis on behalf of the Principal manufacturer, the value of excisable goods was the transaction value of the said goods sold by TAMIN in terms of valuation rules cited above. Hence, Ms/ PRP Exports is liable to pay the differential duty arising due to incorrect valuation of cleared goods. Further, TAMIN being the person dealing in excisable goods, must have registered with the Central Excise department. Penalty is leviable on TAMIN for failure to obtain registration and non-compliance of central excise rule provisions to ensure procedural formalities as regards valuation of excisable goods by the job worker.

The Assistant commissioner of Central Excise, Madurai, replied (January 2015) that a show cause notice was issued to M/s PRP granites demanding duty of ₹ 3.93 crore without appropriating duty of ₹ 1.21 crore already paid besides appropriate interest and penalty in respect of clearances made to four parties for the period from November 2009 to March 2010, July 2010 to January 2011 and May 2011. In the same SCN, TAMIN was required to show cause why penalty should not be levied for non-registration and/or non disclosing to M/s PRP Exports, the value of finished goods which resulted in short payment of duty.

Audit is of the view that TAMIN evaded Central Excise duty fraudulently by not registering himself with department and making arrangement to clear goods from job worker at reduced price. Issue may be examined in details for earlier period and other clearances made by it.

Ministry re-iterated (October 2015) that SCN for ₹ 3.93 crore was issued to the job worker and ₹ 1.21 crore had already been paid by him. Ministry further stated that the job work done by the assessee was one time activity and not recurrent in nature and there was no similar activity by job worker till closure of unit in August 2012.

### 6.3 Cenvat credit

We noticed 14 cases of incorrect availing/utilization of Cenvat Credit by the assessees. Ministry/department admitted observation in all cases and initiated/taken corrective action in 13 cases. These 13 cases are detailed in appendix II. Remaining one case where action is under process, is illustrated in following paragraphs :

#### 6.3.1 Non-reversal of input service credit attributable to Trading Activity

As per Rule 2 (e) of Cenvat Credit Rules 2004, "Exempted Service" means taxable service which is exempt from the whole of the Service Tax leviable thereon; or service, on which no Service Tax is leviable under Section 66B of the Finance Act 1994; or taxable service whose part of value is exempted on the condition that no credit of inputs and input services, used for providing such taxable service, shall be taken. Board, vide Notification No. 3/2011-CE (NT) dated 01 March 2011, clarified that exempted service includes trading. Therefore, trading of goods is exempted service and no Service Tax is payable on this activity. Further, as per Rule 6 (3) of the said Rules, where the manufacturer of goods or the provider of output service, opts not to maintain separate accounts, shall (i) pay an amount equal to six per cent (five percent upto 31.03.2012) of the value of the exempted goods and exempted services or (ii) pay an amount proportionate to credit pertaining to exempted goods as determined under sub-rule (3A).

M/s Aurobindo Pharma Limited (U-I), Medak District under Hyderabad-II Commissionerate, engaged in the manufacture of Bulk Drugs falling under Chapter-29 of Central Excise Tariff Act 1985, used some inputs in manufacture of final products. However, some inputs were sold to outside customers during 2011-12 and 2012-13 which falls under 'Trading Activity'. As Trading Activity is an exempted service, the assessee was required to pay an amount equivalent to five or six per cent (as applicable) of value of exempted service which worked out to ₹ 64.61 lakh, as the assessee did not exercise any option under Rule 6(3) (ii) and did not follow the procedure specified under sub-rule (3A) *ibid*.

When we pointed this out (November 2013), Ministry admitted the objection (November 2015) and stated that Service Tax of ₹ 31.96 lakh along with interest of ₹ 8.93 lakh was recovered from the assessee and for balance amount, SCN was being issued to the assessee.

## 6.4 Other issues

We noticed three other observations relating to exemption, interest and cess. Ministry/department admitted observation in all cases and initiated/taken corrective action in two cases. These two cases are detailed in appendix II. Remaining one case where action is under process, is illustrated in following paragraphs :

### 6.4.1 Non-payment of Cess on Cement

Section 9(1) of the industries (Development and Regulation) Act, 1951 read with Cement Cess Rules, 1993 made there under, stipulates that every manufacturer producing cement in cement plants of capacity not lower than 99,000 tonne per annum based on rotary kiln and 66,000 tonne per annum based on vertical shaft kiln, shall pay cess at the rate of ₹ 0.75 per tonne of cement manufactured and removed from the factory. Rule 3 and Rule 4 of the said rules further stipulate that every manufacturer of cement, who is liable to pay cess shall submit to the Development Commissioner for cement industry, a monthly return relating to stocks of cement produced and removed during the preceding month and shall remit the amount of cess to the said authority by 15th of the following month.

M/s Cement Corporation of India, Tandur under the jurisdiction of Hyderabad-I Commissionerate, engaged in the manufacture of cement falling under Chapter-25 Central Excise Tariff Act 1985, was liable to pay cess amounting to ₹ 50.50 lakh on cement cleared during the period from 1999-2000 to 2012-13. However, the assessee paid only ₹ 4.58 lakh which resulted in short payment of cess to the tune of ₹ 45.92 lakh.

When we pointed this out (May 2014), the Ministry of Commerce and Industry intimated (September 2014) that department was instructed to take action for recovery of cess from the assessee.

## **Chapter VII**

### **Effectiveness of Internal Controls**

#### **7.1 Introduction**

Internal control is an integral process carried out by an entity's management and personnel which is designed to address risks and provides reasonable assurance that in pursuit of the entity's mission, the entity is achieving the following general objectives:

- executing orderly, ethical, economical, efficient and effective operations;
- fulfilling accountability obligations;
- complying with applicable laws and regulations;
- safeguarding resources against loss, misuse and damage.<sup>100</sup>

#### **7.2 Audit findings**

During the course of examination of records, we observed certain cases where due processes were not followed by departmental officers. We communicated these observations to the Ministry through 34 audit paragraphs involving revenue of ₹ 32.76 crore. The Ministry accepted (December 2015) the audit observations in 22 audit paragraphs and initiated/completed corrective action in 18 cases involving revenue of ₹ 25.51 crore which are listed in Appendix III. The Ministry did not agree with 10 audit observations and yet to respond to two observations (December 2015). These 16 observations are covered under two major headings i.e. Internal Audit and other lapses.

#### **7.3 Internal Audit**

Internal audit is one of the main compliance verification mechanisms in the department. Internal audit teams carry out audit at assessee premises by following prescribed procedures for examination of records of the assessee to ascertain the level of compliance with the prescribed rules and regulations. Internal audit is authorised under the Central Excise Rules, 2002 to access the records of assessees at their registered premises. The Directorate General of Audit with its seven zonal units at Ahmedabad, Mumbai, Delhi, Bangalore, Kolkata, Chennai and Hyderabad is to provide a focal link between the Commissionerates (who actually implement the audit process) and the Board on all audit-related matters. On the one hand, it aids and advises the Board in policy formulation and on the other, it guides and provides functional direction in planning, co-ordination, supervision and conduct of audits at the

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<sup>100</sup> INTOSAI GOV 9100 – Guidelines for Internal Control Standard for Public Sector

local level. Earlier, audit work was carried out by Commissionerate through audit cells, manned by an Assistant/ Deputy Commissioner and auditors and headed by an Additional/Joint Commissioner. Internal audit parties consisting of Superintendents and Inspectors carry out the audits. After restructuring of the department (August 2014), 45 exclusive Audit Commissionerates have been created to look after the audit work.

We sought to get an assurance whether internal audit of the assessee, due for audit was conducted by Commissionerates as per frequency norms prescribed by the Board.<sup>101</sup> We also tried to assess the quality of actual audit done by internal audit parties by verifying some assessee records already audited by internal audit parties. We came across certain instances of non-detection assessee's lapses by internal audit parties.

### **7.3.1 Non-conducting of internal audit resulting in lapse committed by the assessee remained unnoticed**

We noticed 10 cases where internal audit was due but not conducted by the department. Ministry/department admitted observation in all cases and initiated/taken action in eight cases. These eight cases are detailed in appendix III. Remaining two cases are illustrated in following paragraphs :

#### **7.3.1.1 Non-detection of non-reversal of Cenvat credit in consequence to refund order**

Rule 5 of Cenvat Credit Rules, 2004, allows refund of Cenvat credit of inputs and input services used in the manufacture of exported goods, if the adjustment of such credit is not possible for payment of Central Excise Duty or Service Tax by the manufacturer or the provider of output service.

M/s Lakshminarayana Mining Company, Siddapur Village, Bellary, a 100% Export Oriented Undertaking, in Belgaum Commissionerate had filed refund claim of ₹ 162.12 lakh during the period from April 2009 to June 2010 in respect of unutilized Cenvat credit on input services consumed for manufacture of exported goods. The department sanctioned (March 2010 and November 2012) refund of ₹ 86.81 lakh vide three different OIOs and rejected the remaining amount of ₹ 75.31 lakh, on the grounds that the assessee was not eligible to avail Cenvat credit of such services. On receipt of the said refund orders the assessee should have reversed the Cenvat credit in lieu of which refund was sanctioned. The assessee should also have reversed the Cenvat credit for the amount where refund order held credits as ineligible. However, verification of ER-2 returns revealed that the assessee did not reverse Cenvat credit of ₹ 162.12 lakh mentioned above. Though the

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<sup>101</sup> Refer table 1.9 of chapter 1 of this report

statutory returns were filed regularly, the department did not take any action to ensure that the Cenvat credit had been reversed by the assessee.

It was also observed that no internal audit of the assessee was conducted by the department during 2010-11 to 2012-13.

When we pointed this out (March 2013), the department stated (June 2014) that the assessee reversed Cenvat credit of ₹ 86.81 lakh and exhibited the same in ER-2 returns for the month of April 2013. Department further stated (February 2015) that the assessee reversed the balance amount of ₹ 75.31 lakh and exhibited the same in ER-2 returns for the month of June 2013.

This non-reversal of ₹ 162.12 lakh would have gone unnoticed, had it not been pointed out by audit.

Ministry confirmed the reversal of credit of ₹ 162.12 lakh. For not conducting internal audit, it stated that audit could not be conducted due to manpower constraints.

Audit is of the opinion that Board should issue suitable instruction to field formations to ensure reversal of credit in such cases.

### **7.3.1.2 Non- detection of short levy of Central Excise duty**

As per extant rules 9 and 10 of the Central Excise (Valuation) Rules 2000 (existed upto 30.11.2013), where excisable goods are not sold by an assessee except or through a related person which inter alia includes interconnected undertaking, the value of goods shall be the normal transaction value at which these are sold by the related person at the time of removal, to buyers (not being related person). Thereby, meaning that these rules were not applicable in case assessee sold goods partly to related buyers and partly to unrelated buyers.

Further, as per Clause (1) below section 4 (3) (b) of Central Excise Act 1944, interconnected undertaking are related for the purpose of valuation of Excisable goods. As per explanation 1 (ii) below section 4 (3) (b) of the Act, if Managing Director of one body corporate is Managing Director of the other, than both are deemed to be under same management and thereby they are interconnected.

The Tribunal in the case of Ispat Industries Limited Vs Commissioner of Central Excise, Raigarh, {2007 (209) ELT 185 (TriLB)} and Hon'ble Supreme Court in the case of Aquamall Water Solutions limited Vs Commissioner of Central Excise, [{006 (193) ELT A 197 (S.C.)} have also upheld that where goods are sold to a related person and partly to independent third parties, assessment should be on the basis of sale made to third party.

Rule 9 has been revised w.e.f. 1 April 2012 inserting 'where whole or part of excisable goods are sold by the assessee to or through a person who is related'.

M/s G R Multiflex Packaging Pvt Ltd. in Kolkata V Commissionerate, engaged in the manufacture of Plain Plastic Film etc. under Chapter 39 of Central Excise Tariff Act 1985, cleared Plain Plastic Film to related party M/s G R Poly Film Pvt Ltd., both having a common Managing Director during the period 2011-12 and 2012-13. Further verification revealed that in some cases the price of the products transferred to related units, was lower than the price at which it was sold to other parties. This resulted in undervaluation of the products cleared to their related units and consequent short-levy of duty of ₹ 46.05 lakh (including cess) for the period 2011-12 and 2012-13 which was recoverable along with applicable interest.

Though the unit was a mandatory unit for internal audit, it was not audited since December 2010. Hence the assessee's lapse remained undetected until pointed out by us.

When we pointed this out (August 2013), the Assistant Commissioner (October 2014) intimated that Show Cause cum Demand Notice for ₹ 46.05 lakh covering the period of 2011-12 to 2012-13 along with applicable interest and penalty had been issued to the assessee.

Reply of the Ministry was awaited (December 2015).

### **7.3.2 Lapses not detected by Internal Audit**

We detected 23 cases where audit of the assessee was conducted by the department but it failed to detect the defaults committed by the assessee. In 10 cases, Ministry admitted the lapses of internal audit and stated that instructions are being issued to the department to sensitise the audit parties. These cases are detailed in appendix III. Remaining 13 cases are illustrated in following paragraphs.

#### **7.3.2.1 Non-detection of irregular availing of Cenvat credit on Works Contract**

As per Rule 2(l) of Cenvat Credit Rules 2004 "input service" means any services used by the manufacturer, whether directly or indirectly, in or in relation to the manufacture of final products and clearance of final products up to the place of removal but excludes services as specified in Rule 2(l)(ii)(A),(B) and (C) viz. construction or execution of works contract of a building or a civil structure or a part thereof with effect from 1 April 2011.

M/s Fresenius KABI Oncology Ltd. under Kolkata III Commissionerate, engaged in the manufacture of Bulk drug viz. Irinotecan, aclitaxel, etc. under

chapter 29 of Central Excise Tariff Act 1985, availed input service credit of ₹ 23.26 lakh (including cess) for service tax paid on civil construction services rendered by M/s Power Max (India) Pvt. Ltd., Kolkata during the period 2011-12 and 2012-13 for civil structural and infrastructural works at Kalyani. Out of this total irregularly availed service credit, the assessee had already reversed ₹ 5.63 lakh (including cess) in February 2013, though such reversal was not shown in the ER-1 of the respective month. Thus, the remaining irregularly availed input service credit of ₹ 17.63 lakh (including cess) during the period 2011-12 and 2012-13 was recoverable from the assessee.

Though internal audit was carried out by the department in November 2013 covering the period August 2012 to July 2013, the lapse remained undetected until pointed out by CAG.

When we pointed this out (March 2014), Ministry stated (September 2015) that the assessee has reversed the amount of ₹ 17.63 lakh from their Cenvat account. On lapse of internal audit, Ministry stated that the issue was detected by internal audit in November 2013 and amount of ₹ 4.26 lakh was realised from the assessee.

Department, though detected lapse committed during August 2012 to July 2013 but failed to detect lapse for the prior period.

### **7.3.2.2 Non-detection of non-reversal of Cenvat credit on account of trading**

According to Rule 6 (2) of Cenvat Credit Rules 2004, manufacturers or providers of output service availing Cenvat credit of any inputs or input services, and manufactures such final products or providing such output services which are chargeable to duty or tax as well as exempted goods or services, shall maintain separate accounts for receipt, consumption and inventory of inputs and input services and take Cenvat credit only on that quantity of input or input service which are intended for use in the manufacture of dutiable goods or in providing output service on which service tax is payable. Rule 6(3) states that the manufacturer or provider of output service, opting not to maintain separate accounts shall either pay an amount equal to five per cent (6 per cent up to 6 July 2009) of value of exempted goods and services; or pay an amount as determined under sub-rule (3A). As per explanation under Clause 2(iii) of Notification No.3/2011/CE dated 1 March 2011, exempted services include trading.

M/s Delphi Connection Systems Pvt. Ltd. Mulanthuruthy, in Cochin Commissionerate, was engaged in trading of goods in addition to manufacturing activity. The assessee had trading income of ₹ 7.14 crore and ₹ 17.93 crore during the years 2011-12 and 2012-13 respectively. The

assessee availed credit of inputs and input services but separate accounts were not maintained for receipt, issue and inventory of inputs and input services relating to exempted services. The assessee was liable to pay an amount of ₹ 34.69 lakh payable as per Rule 6(3).

Internal audit of the assessee was carried out in July 2013 covering the period up to June 2013, but the lapse detected by us was not pointed out.

When we pointed this out (January 2014), department replied (February 2015) that the assessee reversed amount of ₹ 34.73 lakh for the period April 2011 to March 2014 with interest of ₹ 16.35 lakh and penalty of ₹ 8.03 lakh.

Ministry also confirmed (October 2015) that assessee had reversed the credit. On lapse of internal audit, it stated that during preliminary walk through of the unit, the audit team understood that trading and manufacturing activities were dealt by the unit separately and the team centered on manufacturing activity only.

The reply is not tenable, as no verification of assessee's wrong claim was done by internal audit which resulted in non-detection of the lapse.

### **7.3.2.3 Non-detection of incorrect adoption of assessable value resulting in short payment of duty**

Central Excise (Valuation) Rules, 2000 vide Rule 10 read with rule 8 and 9 stipulates that where excisable goods are sold by an assessee to an inter-connected undertaking for use or consumption of such goods in the production or manufacture of articles, the value shall be hundred and ten percent of the cost of production or manufacture of such goods as calculated in CAS-4 certificate. On belated payments if any, interest is payable as per section 11AA of Central Excise Act 1944.

M/s Lucas Indian Service Ltd., falling under Chennai II Commissionerate had adopted Purchase Order rate on the clearance of goods made during the years 2011-2014 to its holding company M/s Lucas TVS Ltd. The purchase order rate was less than one hundred and ten percent of the cost of production or manufacture of such goods. The non-adoption of correct assessable value on the clearances made to another inter-connected undertaking resulted in short payment of duty.

The internal audit of the unit was conducted in September 2013 but this aspect was not pointed out by them.

When we pointed this out (May 2014), the department replied (December 2014) that the assessee had paid the differential duty for the three years amounting to ₹ 17.55 lakh with interest of ₹ 5.90 lakh.

Ministry also confirmed (November 2015) the payment made by the assessee. It further stated that CAS-4 was not prepared for three years by the assessee at the time of internal audit and therefore, it could not calculate the differential duty.

The reply is not tenable as, even if CAS-4 certificate was not prepared by the assessee, the issue of non-preparation of CAS-4 certificate should have been raised by internal audit.

#### **7.3.2.4 Non-detection of short payment of duty in respect of clearance made to related party**

Rule 8 of Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 stipulates that where the excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in the production or manufacture of other articles, the value shall be one hundred and ten per cent of the cost of production or manufacture of such goods.

Further, Rule 9 stipulates that "When the assessee so arranges that the excisable goods are not sold by an assessee except to or through a person who is related in the manner specified in either of sub clause (ii), (iii) or (iv) of clause (b) of sub section (3) of section 4 of the Act, the value of the goods shall be normal transaction value at which these are sold by the related person at the time of removal, to buyers (not being related); or where such goods are not sold to such buyers, to buyers (being related person) who sells such goods in retail, provided that in a case where the related person does not sell the goods but use or consumes such goods in the production or manufacture of articles, the value shall be determined in the manner specified in Rule 8 *ibid*, that is one hundred ten per cent of the cost of production of such goods.

M/s Sunshine Steel Industries, Jodhpur in Jodhpur Commissionerate (erstwhile Commissionerate Jaipur II), engaged in manufacture of SS Utensils and SS Cold Rolled Patta/Patti, cleared manufactured quantity 18.36 lakh Kgs of SS cold rolled Patta/Patti having assessable value of ₹ 12.24 crore to a related party M/s Ramdev Stainless Strips Pvt. Ltd., Jodhpur during 2012-13 and this manufactured product was not sold to any other party. The value of SS cold rolled Patta/Patti should have been determined at 110 per cent of the cost of production in terms of rules *ibid*. Since the assessee did not provide the cost of production i.e. CAS-4 certificate in respect of clearance made to sister concerned/related person Audit worked out the Short payment considering the invoice values to related party as cost of production amounted to ₹ 15.13 lakh which was required to be recovered along with interest.

Internal audit of the assessee was carried out by the department in October 2012 covering the period upto September 2012 but the lapse was not detected by it.

When we pointed this out (October 2014), the Commissionerate admitted the objection and stated (June 2015) that a Show Cause Notice was under process of issuance.

Ministry stated (December 2015) that the fact of partners being related to other firms/companies could not be ascertained from the documents provided to internal audit party. However, officials of audit party had been warned to be more cautious to examine this aspect.

### **7.3.2.5 Non-detection of irregular utilization of Cenvat credit on old capital goods**

As per Rule 3(5A) (b) of Cenvat credit Rules (CCR) 2004, if capital goods on which Cenvat credit have been taken are removed after being used, whether as capital goods or as scrap or waste, the manufacturer or provider of output service shall pay an amount equal to the Cenvat credit taken on the said capital goods reduced by 2.5 per cent calculated by straight line method for each quarter or part thereof from the date of taking the Cenvat credit. Rule 14 of CCR 2004 states that where Cenvat credit has been taken and utilized wrongly, the same along with interest shall be recovered from the manufacturer or provider of output service.

M/s OEN India Ltd., Mulanthuruthy, in Cochin Commissionerate transferred its Capital goods procured in 1995, 1997 and 2000 to Tripunithura unit in January 2005. These goods were again transferred back to Mulanthuruthy unit in March 2013 and the Mulanthuruthy unit availed the credit which was reversed at the time of transferring the said capital goods to Tripunithura unit during January 2005, on the basis of old invoices. Since the original invoices pertained to 1995, 1997 and 2000, on transfer of these capital goods to Mulanthuruthy unit in March 2013, there was no credit left to be availed applying the formula for proportionate reduction at the rate of 2.5 per cent per quarter, as per sub-rule 3 (5A)(b). However, the transfer of the capital goods was made on the basis of the old original invoices without making the proportionate reduction as stipulated in sub-rule 3(5A)(b) and full Cenvat credit ₹ 8.25 lakh was availed and utilized by Mulanthuruthy unit in March 2013, which was irregular and required to be reversed with interest from the assessee.

Internal audit of the assessee covering the period upto March 2013 was conducted in December 2013, but the irregular utilization of credit was not detected.

When we pointed this out (January 2014), the department replied (November 2014) that Show Cause Notice demanding Cenvat credit of ₹ 8.25 lakh, with interest and equal penalty had been issued to the assessee.

Ministry stated (November 2015) that credit reversal at time of transferring capital goods to other unit and credit taken again at the time of receiving back the capital goods was in order.

Reply is not tenable as rule 3(5A) cited supra, specifically require reversal of credit at reduced rate according to depreciated value of capital goods.

### **7.3.2.6 Short payment of duty due to misclassification**

According to Rule 4 (1) of Central Excise Rules, 2002, every person manufacturing excisable goods shall pay duty in the manner provided in Rule 8 and Rule 6 states that, the assessee shall himself assess the duty payable on excisable goods. Chapter 90 of Central Excise Tariff Act 1985 covers medical or surgical instruments and apparatus. General Exemption No. 50 provides for payment of reduced rate of duty at the rate of 4 per cent upto February 2011 and at the rate of 5 per cent from March 2011 for goods covered under Chapter heading 9018. As per Harmonised System of Nomenclature (HSN) 2002 and 2012, chapter heading 9018 does not cover instruments and appliances used in laboratories to test blood, tissue, urine, fluid etc. and should be classified under Chapter heading 9027. Chapter heading 9027 is for instruments and apparatus for physical or chemical analysis, instruments or apparatus for measuring or checking viscosity, porosity, expansion, surface tension or the like, instruments and apparatus for measuring or checking quantities of heat, sound or light (including exposure meters), microtomes etc.

M/s Agappe Diagnostics Ltd, in Cochin Commissionerate, manufacturing diagnostic equipments, incorrectly classified medical diagnostic equipments viz. MISPA Plus Analyzer, MISPA-1 and MISPA Uno which were clinical chemistry analyzers, under chapter heading 90189019 instead of under Chapter heading 9027. The assessee paid duty for the equipments at reduced rate of 4 per cent/ 5 per cent under General Exemption No. 50 during the period April 2010 to May 2011. The assessee reclassified the equipments correctly under Chapter heading 90278090 and paid duty at normal rate of 10 per cent from June 2011, since Customs authorities issued demand notice in June 2011 classifying similar equipments imported by the assessee under heading 90278090 on the basis of HSN notes. However, assessee did not rectify the mistake for period prior to June 2011. Misclassification of diagnostic equipments during the period April 2010 to May 2011 resulted in short payment of duty of ₹ 22.21 lakh.

Internal audit carried out in July 2011 covering the period upto June 2011 had not pointed out the lapse detected by us.

When we pointed this out (September 2012), the Commissionerate stated (July 2013) that the demand of duty of ₹ 24.07 lakh was issued to the assessee which was confirmed in adjudication (December 2014) alongwith interest and equivalent penalty.

Ministry also confirmed (November 2015) that SCN issued to the assessee was adjudicated, confirming the demand. On lapse of internal audit, it stated that classification of goods was changed by the assessee on the basis of demand notice issued by the Customs authority and the fact was not brought to their notice by the assessee, therefore internal audit was not able to detect it.

Reply is not tenable as not only the department failed to detect the wrong classification, as detected by Customs authorities, internal audit also failed to take cognizance of the demand notice of Customs authority and incorrect classification by the assessee.

Audit is also of the view that Board needs to devise a mechanism for exchange of information in such cases between different wings of the Board i.e. Customs, Central Excise and Service Tax.

### **7.3.2.7 Non-detection of irregular availing of Cenvat credit on civil construction service**

Rule 2(1) (A) of Central Credit Rules, 2004 provides that service portion in the execution of a works contract and construction services in so far as they are used for construction or execution of works contract of a building or a civil structure or a part thereof or laying of foundation or making of structures for support of capital goods, except for the provision of one or more of the specified services that are not included in input services for availment of Cenvat credit.

M/s Kudos Chemie Ltd., Derabassi in Chandigarh II Commissionerate, engaged in manufacturing of bulk drugs under chapter 29 of Central Excise Tariff Act, 1985, availed Cenvat credit amounting to ₹ 92.50 lakh on civil construction during the period 2011-12 to 2013-14 in contravention of the Rules *ibid*. This resulted into irregular availment of Cenvat credit amounting to ₹ 92.50 lakh which was recoverable alongwith interest.

The Internal Audit of the assessee was carried out by the department upto April, 2014, but the irregularity was not pointed out.

When we pointed this out (August 2014), the department intimated (November 2014) that an amount of ₹ 92.50 lakh had been reversed by the assessee and interest of ₹ 0.68 Lakh was also paid.

Ministry also confirmed the credit reversal by the assessee (September 2015). On lapse of internal audit, it stated that the matter was under examination.

### **7.3.2.8 Non-detection of wrong availing of credit on same invoice and utilization of the same**

Rule 4 (2)(a) of Cenvat Credit Rules, 2004 stipulates that the Cenvat credit in respect of capital goods received in a factory at any point of time in a given financial year shall be taken only for an amount not exceeding 50 per cent of the duty paid on such capital goods in the same financial year. Rule 14 of the said rules stipulates that irregularly availed and utilized Cenvat credit shall be recovered along with interest.

Audit of M/s Shri Badrinarain Alloys and Steel Ltd. in Haldia Commissionerate, engaged in manufacturing of TMT bars, revealed that the assessee purchased three capital goods from M/s Shailja Engineering Works in the month of October 2013 and availed Cenvat credit of ₹ 28.43 lakh (including Cess) being 50 per cent of the total duty paid on Capital Goods. Subsequently, the remaining 50 per cent credit of ₹ 28.43 lakh was availed in April 2014. Further verification revealed that the assessee in the month of November 2013 had also availed Cenvat credit of ₹ 28.43 lakh based on same sets of invoices. Thus, assessee availed 150 per cent credit out of which 100 per cent was availed in the same year. The credit availed by the assessee in the month of November 2013 was irregular. The assessee had also utilised whole of irregularly availed credit. This resulted in irregular availing and utilization of Cenvat credit of ₹ 28.43 lakh during the period 2013-14 which was recoverable along with interest.

The unit was audited by Internal Audit (May 2013) but it didn't detect the lapse pointed out by us.

When we pointed this out (August 2014), department intimated (October 2014) that the assessee had reversed the credit of ₹ 28.43 lakh along with interest of ₹ 10.58 lakh.

Ministry also confirmed the reversal of credit by the assessee (December 2015). On lapse of internal audit, it stated that audit for the period of 2011-12 was completed in January 2014, hence there was no lapse by the internal audit in 2013-14.

Reply is not tenable, as provision of Central Excise Audit Manual 2008 stipulates that audit should extend upto one completed month preceding the date of current audit. Thus, even if audit was completed in January 2014, it should have covered the period upto December 2013.

### **7.3.2.9 Non-detection of non-payment of duty on additional consideration as Sales Tax remission**

As per Section 4(1)(a) of the Central Excise Act, 1944, when the duty of excise is chargeable on any excisable goods with reference to their value, then such value shall be the transaction value. Transaction value means the price actually paid or payable for the goods when sold, and includes in addition to the amount charged as price, any amount that the buyer is liable to pay to or on behalf of, the assessee, by reason of, or in connection with the sale whether payable at the time of the sale or at any other time, including, but not limited to, any amount charged for, or to make provision for, advertising or publicity, marketing etc or any other matter, but does not include the amount of duty of excise, sales tax and other taxes, if any, actually paid or actually payable on such goods.

The Government of Maharashtra introduced the Package Incentive Scheme for deferred payment of Sales Tax whereby the assessee was allowed to collect Sales Tax from the buyer and retain 75 per cent and repay it after prescribed period. The Government of Maharashtra thereupon amended the provisions of Sales Tax Act and issued a Notification in November 2002 providing further incentive for premature repayment of Sales Tax liability.

Supreme Court in its judgment in case of M/s Super Synotex India dated 28 February 2014 (2014-TIOL-19-SC-CX) on similar issue made it clear that the 75 per cent of Sales Tax retained by the assessee would form part of Assessable value and Excise duty is payable. Further Board has also issued a circular vide F.No.6/8/2014-CX.1 dated 17 September 2014 on similar lines in light of above judgment and instructed that similar cases may be finalized on this ground.

M/s Perfect Circle India Ltd in Nashik Commissionerate, engaged in the manufacture of the goods (chapter 84) had prepaid the amount of deferred taxes (Sales Tax) at Net Present Value (NPV) on 29 June 2013 under Package Scheme of incentive. Thus benefit availed by the assessee for ₹ 1.34 crore was includible in the assessable value. Non-inclusion of Sales Tax amount in the assessable value resulted in short levy of duty of ₹ 16.58 lakh with interest of ₹ 2.68 lakh (upto 23 May 2014).

Internal Audit of the assessee was conducted in November 2013 but the lapse was not detected by them.

When we pointed this out (May 2014), department admitted the objection (June 2015) and stated that show cause notice was being issued.

Ministry stated (December 2015) that SCN was issued to the assessee. On lapse of internal audit, it stated that the fact of deferred sales tax payment was not informed to the audit officer and the assessee suppressed the facts from the department.

Reply is not tenable as if the facts are not reported by the assessee, internal audit should be able to detect such evasion and in the instant case, internal audit failed to detect the lapse.

### **7.3.2.10 Non-detection of irregular availing of Cenvat credit**

Rule 3 (1) of Cenvat Credit Rules, 2004 provides that a manufacturer of final products shall be allowed to take credit of specified duties paid on any input or capital goods received in factory of manufacturer of final products on or after 10 September 2004.

Govt. of India vide notification numbers 13/2012-Customs and 14/2012-Customs dated 17 March 2012 exempted the imported goods from payment of Education cess and Secondary and Higher education cess leviable under sub-section (1) of section 3 of the Customs Tariff Act, 1975.

M/s Somi Conveyer Belting Ltd and M/s Prem Cables Pvt. Ltd in Jodhpur Commissionerate availed Cenvat credit of Education cess and Secondary and Higher Education cess on imported goods during 2012-13 and 2013-14 which was not levied in Bill of Entries as the same was exempted vide notifications ibid. This resulted in irregular availing of Cenvat credit of ₹ 11.67 lakh which is recoverable from the assessee alongwith applicable interest of ₹ 3.65 lakh.

Though internal audit of the assessee was conducted for the period included in the para, the irregularity was not pointed out until detected by us.

We pointed this out in December 2014. Reply from the Ministry/Commissionerate was awaited (December 2015).

## **7.4 Other Lapses**

### **7.4.1 Non-conducting of detailed scrutiny resulted in non-detection of irregular availing of Cenvat credit**

Rule 2(l) of Cenvat Credit Rules, 2004, specifically excluded architect services, construction services and works contract services from the definition of 'input service', if these services are utilized for construction of a building or civil structure or for laying foundation or making structures for support of capital goods and Cenvat credit of the same is not admissible.

Audit of the records pertaining to Nippani II Range under Belgaum Commissionerate, for the period 2009-10 to 2011-12 revealed that no detailed scrutiny was conducted by the Range. Audit selected a few assesseees for detailed assessment to verify the impact of not conducting of detailed scrutiny of returns and observed that, M/s Shivshakti Sugars Ltd., Soudatti had availed Cenvat credit of ₹ 11.39 lakh on architect services, construction services and works contract services utilized for construction of factory building and M/s Krishna SSKN, Athani had availed Cenvat credit of ₹ 3.66 lakh on works contract services and club membership services during 2011-12. These services were not eligible input services for the manufacturers for availing Cenvat credit. The Cenvat credit availed was irregular and had to be reversed, along with interest and penalty, as applicable.

When we pointed this out (January 2013), the department replied (April 2015) that scrutiny of returns were not conducted initially due to various operational issues faced during the implementation of ACES and that scrutiny was being conducted regularly after these problems have been solved. The department further replied (October 2013) that M/s Shivshakti Sugars Ltd. had paid (April 2013) ₹ 11.39 lakh and M/s Krishna SSKN had paid ₹ 3.24 lakh for ineligible Cenvat credit. Department also replied (June 2014) that the assessee had not reversed Cenvat credit of ₹ 0.42 lakh, hence, a Show Cause Notice (SCN) was issued to M/s Krishna SSKN on the grounds that the same was not an eligible credit as it pertained to membership of Federation of Co-operative Sugar Mills.

Ministry also confirmed (December 2015) the payment made by both the assesseees. On departmental lapse, it also stated that department could not conduct scrutiny due to operation issues in ACES.

Though Commissionerate stated that detailed scrutiny is being conducted now, however, during performance audit on Cenvat credit, it has been noticed that out of 41 test checked Commissionerates, no detailed scrutiny was being conducted in 21 Commissionerates and reply of 20 Commissionerates was awaited. Ministry need to ascertain the claim of Belgaum Commissionerate for conducting detailed scrutiny.

#### **7.4.2 Delay in issuing SCNs by the department**

CBEC circular No. 5/83-CX.6 dated 10 March 1983 as amended vide instruction F No. 206/2/2010-CX.6 dated 03 February provided that instructions should be issued to issue show cause notice immediately on receipt of an audit objection from CAG, even if the objection is not admitted.

Section 11A of Central Excise Act, 1944 stipulated that a show cause notice shall be issued within one year (for Service Tax, 18 months, with effect from

28 May 2012) in normal course and in case of fraud, collusion, wilful misstatement, suppression of facts etc. with intent to evade duty, within a period of five years from the relevant date. Further as per section 73(6)(b) of the Act, relevant date inter alia means where no periodical returns as aforesaid filed, the last date on which such returns to be filed under the said rules.

Supreme Court in the case of M/s Nizam Sugar Ltd. Vs Commissioner of Central Excise {2006(197) ELT 465(SC)} has held that the extended period of five years was not available to the department for the subsequent show cause notice which was issued based on the same set of facts of the earlier show cause notice as the full facts were known to the department and hence suppression cannot be alleged.

Audit pointed out five cases relating to four assesseees under the Allahabad Commissionerate, during June 2010 to March 2011. However, department took action by issuing SCN in January 2013 (one case) and April 2014 (four cases). Thus, department took action after more than four years, resulting in realisation of revenue to the tune of ₹ 1.29 crore doubtful, as these cases may have become time-barred.

When we pointed this out (May 2015), Ministry did not admit the objection stating that there was no violation of Board's instruction as protective SCNs were issued in all these cases.

Reply is not tenable as CBEC instruction dated 3 February 2010 clearly states that show cause notices should be issued immediately on receipt of an Audit observation of CAG, even if the objection is not admitted. The audit observations were issued during 2010-11 (June 2010 to April 2011) but the department did not furnish any reply to these paras till the year 2014. The department intimated Audit in the Audit Committee Meeting held with the department in 2014 about issuance of SCNs in respect of these cases during January 2013 and April 2014 respectively i.e. after more than four years.

Further, an SCN can be issued after one year only in cases where there is suppression of facts or fraud by the assessee. However, department in all delayed cases use the suppression of facts clause which many times are not admitted by tribunal/courts and SCN are time barred.

#### **7.4.3 Non-issuance of show cause notice to recover Central Excise duty**

Rule-6(3) of Cenvat Credit Rules, 2004 provides that if Cenvat credit is availed on common inputs/input services which are used in manufacture of exempted goods as well as in dutiable goods and separate accounts for inputs are not maintained, then the manufacturer shall either pay an amount equivalent to six per cent (five percent upto 31.03.2012) of value of the

exempted goods or pay an amount equivalent to the Cenvat credit attributable to inputs and input services used in or in relation to the manufacture of exempted goods or provision of exempted services.

Section 11A of Central Excise Act, 1944, provides that when any duty of excise has not been levied or has been short-levied or short-paid or erroneously refunded, Central excise officer may, within one year from the relevant date, serve notice on the person. The period of one year stands extended to five years where duty has been short-paid due to fraud, collusion, willful mis-statement or suppression of facts with the intention to evade duty.

M/s Canton Laboratories Ltd. in Vadodara-II Commissionerate cleared the exempted goods – Sodium chloride (NaCl) amounting to ₹ 524.18 lakh during April 2009 to June 2012 using common inputs and input services for the manufacture of said exempted goods. However, the assessee neither maintained separate accounts for inputs and/or input services nor paid amount equivalent to six/five per cent of the value of the exempted goods.

Audit further noticed that internal audit raised this issue in March 2014 and the assessee paid amount equivalent to six percent of value of exempted goods for the period July 2012 to February 2014. However, department did not initiate any action to recover the amount for the period April 2009 to June 2012 from the assessee. This resulted in non-recovery of Central Excise duty of ₹ 28.24 lakh.

When we pointed this out (May 2014), the Commissionerate stated (March 2015) that objection was acceptable and Show cause notice for ₹ 25.45 lakh had been issued to the assessee covering the period from July 2009 to June 2012.

Ministry stated (October 2015) that SCN was adjudicated, confirming the demand. Reply was silent on departmental lapse.

#### **7.4.4 Ineffective Review of Call Book**

As per CBEC Circular No.162/73/95-CX dated 14.12.1995, the Show Cause Notices (SCNs) which has reached a stage when no action can or need to be taken to expedite its disposal for at least 6 months might be transferred to the Call Book with the approval of the Competent Authority. Cases held up in law courts, cases in which the department has gone in appeal to the appropriate authority, cases where injunction has been issued by Supreme Court/High Court/CESTAT etc., cases where audit objections are contested and cases where the Board has specifically ordered the same to be kept pending and to be entered into the Call Book, can be transferred to the Call Book. Further, extant instructions to the Commissionerates require monthly review of pending Call Book items.

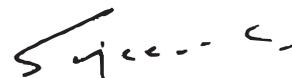
During the verification of cases pending in the Call Book at Belgaum Commissionerate, we noticed that 28 SCNs in respect of 13 cases/assesseees were kept pending in the Call Book even though the cases were fit for adjudication. In one such case SCN dated 26 July 2010 issued to M/s JSW Cement Ltd., Bellary, demanding ₹ 97.06 lakh of irregular Cenvat credit availed on MS Plates, TMT Bars, Angles etc. as capital goods. Though the SCN was liable to be adjudicated in February 2011, as similar cases were adjudicated by the department, it took more than three years to adjudicate the case.

When we pointed this out (April 2013), the department intimated (November 2013) that 22 SCNs, including SCN issued to M/s JSW, were taken out of call book. Department further intimated (March 2015) that 22 cases were adjudicated and three more cases were to be taken out, and continued to keep the remaining two SCNs in Call Book.

Retaining the two cases in Call Book was not accepted by Audit as the reasons furnished by the department were not correct.

Ministry stated (December 2015), that remaining two cases had also been taken out from call book and adjudication was underway.

New Delhi  
Dated: 10 February 2016



(SANJEEV GOYAL)  
Principal Director (Central Excise)

Countersigned

New Delhi  
Dated: 10 February 2016



(SHASHI KANT SHARMA)  
Comptroller and Auditor General of India

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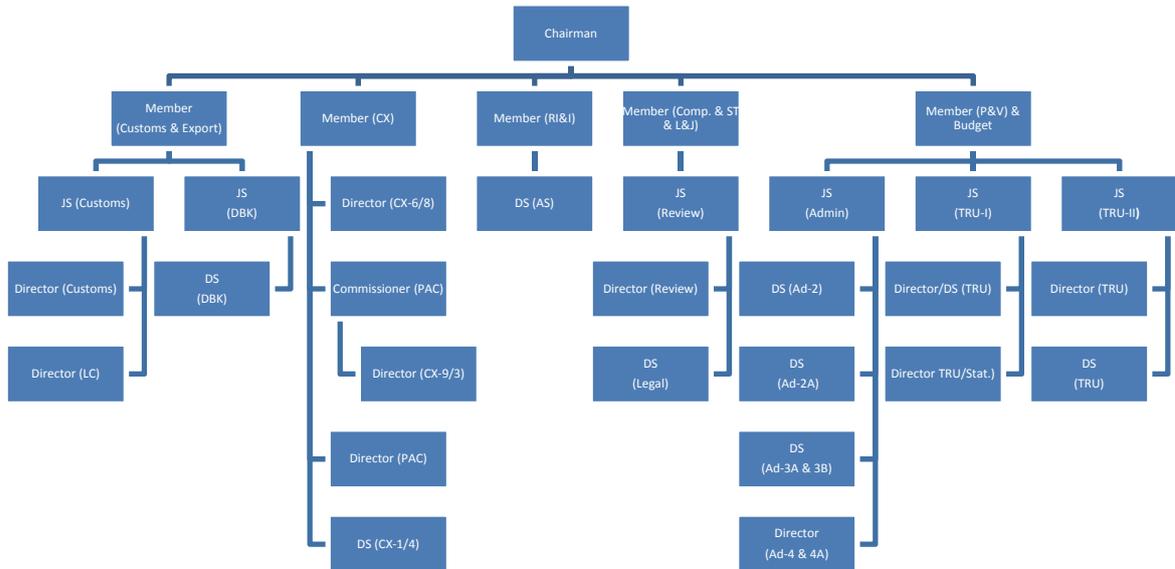
# APPENDICES

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## Appendix I

### Organisational structure of CBEC



## Appendix II

(₹ in lakh)

Sl. No.	DAP No.	Brief Subject	Amount objected	Amt Admitted	Amt recovered	Commissionerate
1	1B	Incorrect availing of Cenvat credit	19.54	19.54	NIL	Madurai
2	2B	Short payment of Excise duty	30.87	30.87	30.87	Allahabad
3	3B	Ineligible utilization of Cenvat credit	17.11	17.11	17.11	Trivandrum
4	4B	Non-payment of amount on clearances of exempted goods	1,781.45	1,781.45	78.37	Kolkata li
5	5B	Non payment of duty on clearance of exempted goods	114.34	114.34	51.87	Ahmedabad I
6	6B	Irregular availment and utilization of Cenvat credit	47.84	47.84	NIL	Kolkata I
7	7B	Short payment of Central Excise duty and interest	21.63	21.63	21.63	Alwar
8	8B	Short Reversal of Cenvat Credit	18.35	18.35	NIL	Ahmedabad I
9	9B	Short Reversal of Cenvat Credit	50.85	50.85	50.85	Bharuch
10	10B	Wrong availment of Cenvat credit	23.94	23.94	NIL	Meerut
11	11B	Short Reversal of Cenvat Credit	32.64	32.64	32.64	Bharuch
12	12B	Incorrect availing of exemption resulting in non-payment of duty	80.24	80.24	NIL	Chennai III
13	13B	Incorrect payment of differential duty through Cenvat account	23.07	23.07	23.07	Puducherry
14	14B	Non-conduct of detailed scrutiny of returns, resulting in non-recovery of Excise duty	88.90	88.90	88.90	Silvassa (Vapi)
15	16B	Non-payment of amount under Rule 6 of Cenvat Credit Rules	47.74	47.74	NIL	Bengaluru I
16	17B	Non-payment of Central Excise duty and violation of the provision of Rule 8 of Central Excise Rules	42.94	42.94	42.94	Belgaum
17	4A	Incorrect availment of Cenvat on ineligible services	292.67	292.67	NIL	Tirunelveli
18	6A	Non-payment of interest on belated payment of differential duty	23.05	23.05	23.05	chennai III
19	9A	Wrong availment of credit of service tax by taking credit twice on the basis of same bills/ invoices	24.43	24.43	24.43	Raipur
20	11D	Non-reversal of input service credit attributable to Trading Activity	30.09	30.09	30.09	Visakhapatnam-I
21	25D	Non-reversal of Cenvat Credit on input and input credit service	958.85	958.85	NIL	Bhubaneswar-I

Sl. No.	DAP No.	Brief Subject	Amount objected	Amt Admitted	Amt recovered	Commissionerate
22	38D	Non-reversal of Cenvat credit on provision made for obsolete stock	21.84	21.84	NIL	Belapur
		Small money value observations which were accepted by the department and rectificatory action taken but not converted into Draft Audit Paragraphs	5,801.59	5,801.59	833.02	
		<b>Total</b>	<b>9,593.97</b>	<b>9,593.97</b>	<b>1,348.84</b>	

## Appendix III

(₹ in lakh)

Sl. No.	DAP No.	Brief Subject	Amount objected	Amt Admitted	Amt recovered	Commissionerate
1	2D	Irregular availment of Cenvat credit on outward freight	21.06	21.06	NIL	Meerut
2	3D	Simultaneous availing of Cenvat Credit on Capital goods and depreciation under Income Tax Act	34.69	34.69	NIL	Bharuch
3	5D	Non-reversal of Cenvat Credit	68.07	68.07	NIL	Gurgaon II
4	6D	Irregular availment of Cenvat credit	47.46	47.46	47.46	Ahmedabad III
5	9D	Non-payment of amount	860.60	860.60	NIL	Bolpur
6	10D	Short levy of duty due to undervaluation	109.84	109.84	109.84	Haldia
7	12D	Non-payment of interest on differential duty	94.04	94.04	94.04	Durgapur
8	14D	Short payment of duty due to non-inclusion of freight charges to Assessable Value	160.53	160.53	NIL	Hyderabad III
9	15D	Short payment of duty due to non-inclusion of freight charges to Assessable Value	47.82	47.82	0.46	Hyderabad III
10	18D	Non-reversal of Cenvat credit on provision made for obsolete stock	17.03	17.03	17.03	Pondicherry
11	21D	Short payment of duty due to non-inclusion of freight charges to Assessable Value	253.58	253.58	NIL	Hyderabad III
12	22D	Irregular availment of Cenvat credit	18.54	18.54	NIL	Vadodara II
13	23D	Non-realisation of interest	45.83	45.83	45.83	Bolpur
14	26D	Non-levy of interest	76.05	76.05	76.05	Jamshedpur
15	27D	Irregular availing of Cenvat credit	209.67	209.67	NIL	Jamshedpur
16	31D	Non-reversal of Additional Excise Duty on 'as such clearance' of imported material.	421.97	421.97	317.54	Jaipur I
17	34D	Non-conduct of internal audit leading to irregular availing of cess credit	25.93	25.93	25.93	Bolpur
18	35D	Irregular availment of Cenvat credit	37.84	37.84	NIL	Durgapur
		<b>Total</b>	<b>2,550.55</b>	<b>2,550.55</b>	<b>734.18</b>	

## Glossary

AC	Assistant Commissioner
ACES	Automation of Central Excise and Service Tax
ADG	Additional Director General
BE	Budget Estimate
Board	Central Board of Excise and Customs
CAAT	Computer Assisted Audit Techniques
CAG	Comptroller and Auditor General of India
CAO	Chief Accounts Officer
CAS	Cost Accounting Standards
CBDT	Central Board of Direct Taxes
CBEC	Central Board of Excise and Customs
CE/CX	Central Excise
CD	Compact Disk
Cenvat	Central Value Added Tax
CERA	Central Excise Receipts Audit
CESTAT	Customs, Excise and Service Tax Appellate Tribunal
CGA	Controller General of Accounts
CSO	Central Statistical Office
CWF	Consumer Welfare Fund
DC	Deputy Commissioner
DCA	Deputy Controller of Accounts
DD	Demand Draft
DDO	Drawing and disbursing officer

DG	Director General
DGA	Director General of Audit
DGCEI	Directorate General of Central Excise Intelligence
DMS	Date-wise Monthly Statement
DoR	Department of Revenue
EA 2000	Excise Audit 2000
EASIEST	Electronic Accounting System in Excise and Service Tax
EC	Education Cess
e-PAO	Electronic Pay and Accounts Officer
ELT	Excise Law Times
EOU	Export Oriented Unit
ER	Excise Return
FPB	Focal Point Bank
FY	Financial Year
GAR	Government Accounting Rules
GDP	Gross Domestic Product
HSN	Harmonic System of Nomenclature
IAP	Internal Audit Party
ICEGATE	Indian Customs Electronic Gateway
ICT	Information and Communication Technology
INTOSAI	International Organisation of Supreme Audit Institution
INTOSAI GOV	INTOSAI Guidance of Good Governance
LTU	Large Taxpayer Unit
MIS	Management Information System

MMP	Mission Mode Projects
MOF	Ministry of Finance
MTR	Monthly Technical Report
NCDDO	Non-Cheque Drawing and Disbursing Officer
NeGP	National e-Governance Plan
NSDL	National Securities Depository Limited
OIO	Order in Original
PAO	Pay and Accounts Officer
PD	Principal Director
PLA	Personal Ledger Account
Pr CCA	Principal Chief Controller of Accounts
PTS	Put Through Statement
QAR	Quality Assurance Review
R&C	Review and Correction
RAT	Receipts Awaiting Transfer
RBI	Reserve Bank of India
RE	Revised Estimates
RTGS	Real Time Gross Settlement
SB	Shipping Bill
SC	Supreme Court
SCN	Show Cause Notice
SHEC	Secondary and Higher Education Cess
SSI	Small Scale Industries
ST	Service Tax

TIOL Tax India Online

TMT Thermo-Mechanical Treatment

TR Treasury Rules

UOI Union of India

ZU Zonal Unit

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