Report of the Comptroller and Auditor General of India

for the year ended March 2003

Union Government
(Indirect Taxes - Central Excise & Service Tax)
No. 11 of 2004

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PREFACE

This report for the year ended 31 March 2003 has been prepared for submission to the President under Article 151 of the Constitution.

The report presents the observations noticed in test audit of Indirect Taxes (Central Excise and Service Tax) of the Union Government. Section 1 of the report covers matters relating to "central excise" and section 2 covers "service tax".

The cases mentioned in the report are among those which came to notice in the course of audit during the year 2002-03 and early part of the year 2003-04, as well as those which came to notice in earlier years but were not reported.

OVERVIEW

This report is presented in two sections :

Section 1	**Chapters I to XIII**	**Central Excise**
Section 2	**Chapters XIV & XV**	**Service Tax**

Some of the significant findings are highlighted below :-

SECTION 1 - CENTRAL EXCISE

This section contains 166 paragraphs featured individually or grouped together and two reviews with a financial implication of Rs.8485.98 crore. Some of the significant findings included in this section are indicated below :-

A. General

The actual collections fell short of the budget estimates as well as the revised estimates year after year. Despite this, the government continued to make optimistic projections during presentation of the annual budget. The budget estimate 2002-03 was pitched at Rs.91,141 crore, an increase of 11.5 per cent over budget estimates, 22 per cent over revised estimate and 26 per cent over actual collections of 2001-02. The collections in 2002-03 fell short of the budget estimate by Rs.9,100 crore or 9.98 per cent.

(Paragraph 1.1)

A total of 67275 cases involving duty of Rs.36,495.49 crore were pending finalisation on 31 March 2003 with different authorities.

(Paragraph 1.5)

B. Reviews

Determination of assessable value under new section 4 (transaction value)

- **The absence of suitable provisions in the statute helped three oil companies to avoid payment of duty of Rs.713.17 crore on the indirect sale consideration received in the form of subsidy from the government on sale of petroleum products.**

(Paragraph 2.6)

- **Adoption of lower "mutually agreed price" for payment of duty by 12 terminals of three petroleum companies led to a revenue loss of Rs.113.79 crore.**

(Paragraph 2.7)

- **Clearance of goods by job workers manufacturing branded as well as un-branded goods for brand name owners/principal manufacturers, at lower assessable value resulted in a revenue loss of Rs.90.53 crore to the government as the said goods were sold by the brand name owners/principal manufacturers at much higher prices.**

(Paragraph 2.8)

- **Absence of mechanism to verify the correctness of the transaction value of assessee's own manufactured goods as well as the cost of bought out goods and the installation cost forming part of the total value of project installed at site, led to a revenue loss of Rs.90.88 crore in 10 cases where assessees could conveniently suppress value of their own manufactured goods while inflating the value of bought out items.**

(Paragraph 2.9)

- **Lacunae in the valuation rules permitting the assessees to determine the value of goods consumed captively at lower value despite availability of higher value of comparable goods during the relevant period, led to revenue loss of Rs.26.99 crore in seven cases.**

(Paragraph 2.11.1)

- **Irregularities in the valuation of excisable goods due to non-inclusion in the assessable value of various elements such as equalized freight, freight and insurance, dealer's margin, service licence fee, excess freight charges recovered, retail pump outlet charges for petroleum products and pre delivery inspection charges or service charges etc. resulted in short levy of duty of Rs.242.75 crore.**

(Paragraph 2.15 to 2.20)

Call book

- **Intended as an interim arrangement wherein cases could be kept till they were ripe for adjudication, there has been a large increase in the number of cases being retained in the call book in the year 2001-02.**

(Paragraph 3.4)

- **540 cases involving demands for Rs.413.58 crore in 55 Commissionerates were entered in the call book in violation of the prescribed norms.**

(Paragraph 3.6)

- **1512 cases involving demands for Rs.349.38 crore in 31 Commissionerates were kept in the call book even though no appeals were pending in these cases.**

(Paragraph 3.8)

- **4820 cases involving demands for Rs.2622.68 crore in 56 Commissionerates were kept pending in the call book for want of clarifications/decision by the Board.**

(Paragraph 3.9)

- **1655 cases involving demands for Rs.1043.82 crore in 37 Commissionerates continued to be retained in the call book despite these cases no longer being in contest with audit.**

(Paragraph 3.10)

C. Non-levy/short levy of duty

Short levy/under assessment of central excise duty amounting to Rs.1445.59 crore were noticed. The more significant of these findings are as follows :

- **Refund of duty granted on manufacture of petroleum oil based products was withdrawn retrospectively from 8 July 1999. Non recovery of refunds granted alongwith interest from M/s. Numaligarh Refinery amounted to Rs.748.04 crore.**

(Paragraph 4.1)

- **By notifications dated 7 May 1997 and 2 June 1998 as amended, certain exemptions were provided to pan masala which did not contain tobacco in any proportion and containing betel nut more than 10 per cent by weight. In violation of the notifications, exemption was allowed on pan masala containing tobacco thereby resulting in loss of revenue of Rs.81.78 crore.**

(Paragraph 4.2)

- **Additional duty of excise levied on high speed diesel by Finance Act, 1999 was not collected on clearances for export or for consumption on board a ship bound for foreign port in 10 cases amounting to Rs.54.34 crore.**

(Paragraph 4.3)

- **The Central Excise Rules/Cenvat Credit Rules allow Modvat/Cenvat credit of additional duty paid on input goods for utilisation against additional duty leviable on finished products. In contravention of the provisions of these rules, the government has allowed deemed Modvat/Cenvat credit of additional duty for utilisation against final products to manufacturers of processed fabric even though no additional duty was paid on the input goods. This resulted in loss of revenue of Rs.24.72 crore in 27 cases.**

(Paragraph 4.5.1)

- **Incorrect availment of Modvat/Cenvat credit amounted to Rs.319.32 crore.**

(Paragraph 5)

- **Duty amounting to Rs.47.26 crore was short levied because of incorrect application of exemption notifications relating to goods manufactured on job work, intermediate goods, finished goods, goods produced by small scale industry, national calamity contingent duty etc.**

(Paragraph 6)

- **There were instances of incorrect adoption of value of goods sold on maximum retail price or cleared to sister concern; and also non-inclusion of cost of components, packing materials etc., in the assessable value. Duty levied short amounted to Rs.40.76 crore.**

(Paragraph 7)

- **Duty not levied on goods consumed captively, found short in the stock, destroyed by floods and also on goods remade amounted to Rs.23.60 crore.**

(Paragraph 8)

- **Failure to raise demand for duty or to realise confirmed demand caused a loss of revenue of Rs.14.06 crore.**

(Paragraph 9)

- **Incorrect classification of fertilizers, Dabur lal tail etc. resulted in short realisation of duty of Rs.4.21 crore.**

(Paragraph 10)

- **Interest not demanded or realised in cases of delayed payment of excise duty amounted to Rs.2.42 crore.**

(Paragraph 11)

- **Cess amounting to Rs.2.34 crore was not realised from the manufacturers of cement and processed textile fabrics.**

(Paragraph 12)

SECTION 2 - SERVICE TAX

This section contains a review, "Service tax on advertising services and courier services" and 42 paragraphs with revenue implication of Rs.503.00 crore. The significant findings of audit included in this section are mentioned below :-

A. Review

Service tax on advertising services and courier services

- **Instructions issued by the Board for exclusion of charges towards obtaining space and time for publishing and display in the print/electronic media were contrary to the provisions of the Finance Act. Service tax of Rs.74.53 crore was foregone in 18 Commissionerates.**

(Paragraph 14.5)

- **Measures taken by the Department to bring into tax net active service providers were ineffective and inadequate. This resulted in 1408 advertising agencies in 19 Commissionerates remaining un-registered, with loss of revenue estimated to be Rs.160.77 crore.**

(Paragraph 14.7)

- **Due to lack of proper monitoring system, 44 registered advertising agencies in 12 Commissionerates did not file returns thereby evading tax to the extent of Rs.4.62 crore.**

(Paragraph 14.11)

- **Ineffective assessment procedure resulted in short levy of tax to the tune of Rs.8.25 crore and Rs.3.15 crore by 94 advertising agencies in 17 Commissionerates and 14 courier agencies in 5 Commissionerates of Central Excise respectively.**

(Paragraph 14.15)

B. Non-levy/short levy of service tax

Non-levy/short levy of service tax amounting to Rs.42.21 crore were noticed. Some of the significant findings are as follows :-

- **Consulting engineers, clearing and forwarding agents, management consultants, Doordarshan and All India Radio, Chennai did not pay service tax of Rs.12.53 crore.**

(Paragraph 15.1)

- **Service tax of Rs.23.08 crore on the services rendered by foreign consultants providing engineering and management consultancy in India was not collected.**

(Paragraph 15.2)

- **Service tax from the recipients of the services of goods transport operators and clearing and forwarding agents was made recoverable by the Finance Act, 2000 but service tax of Rs.3.97 crore was not realised in 27 cases.**

(Paragraph 15.3)

SECTION 1 - CENTRAL EXCISE

CHAPTER I : CENTRAL EXCISE RECEIPTS

1.1 Budget estimates, revised budget estimates and actual receipts *

The budget estimates, revised budget estimates and actual receipts of central excise duties during the year 1998-99 to 2002-03 are exhibited in the table below:-

(Amount in crore of rupees)

Year	Budget estimates	Revised budget estimates	Actual receipts	Difference between actual receipts and budget estimates	Percentage variation
1998-99	57,690	53,200	53,053	(-) 4637	(-) 8.04
1999-2000	63,565	60,731	61,672	(-) 1893	(-) 2.98
2000-01	70,967	70,399	68,282	(-) 2685	(-) 3.78
2001-02	81,720	74,520	72,306	(-) 9414	(-) 11.52
2002-03	91,141	86,993	82,041	(-) 9100	(-) 9.98

* Figure furnished by Principal Chief Controller of Accounts (Central Board of Excise and Customs).

The actual collections fell short of the budget estimates as well as the revised estimates year after year. Despite this the government continued to make optimistic projections during presentation of the annual budget. The budget estimate 2002-03 was pitched at Rs.91,141 crore, an increase of 11.5 per cent over budget estimates, 22 per cent over revised estimate and 26 per cent over actuals of 2001-02. The collections fell short of the budget estimates by Rs.9,100 crore or 9.98 per cent and short of revised estimates by Rs.4,952 crore or 5.6 per cent in 2002-03.

1.2 Value of output* vis-à-vis central excise receipts

The value of output from the manufacturing sector vis-a-vis receipt of central excise duties through Personal Ledger Account (cash collection) during the years 1992-93 to 2002-03 are as follows:

(Amount in crore of rupees)

Year	Value of output	Central excise	Percentage of central excise receipts to value of production
1992-93	345204	30614	8.87
1993-94	390561	31548	8.08
1994-95	479717	37208	7.76
1995-96	597354	40009	6.70
1996-97	661613	44818	6.77
1997-98	720410	47763	6.63
1998-99	794465	53053	6.68
1999-2000	861200	61672	7.16
2000-01	909427	68282	7.50
2001-02	934891	72306	7.73
2002-03	991919	82041	8.27

* Includes value of all goods produced during the given period including net increase in work-in-progress and products for use on own account. Valuation is, at producers values, that is the market price at the establishment of the producers. As separate figures of value of production by small scale industry units and for export production were not available, these have not been excluded from the

value of output indicated. Value of output for the year 2002-03 is based on estimates. Source : Central Statistical Organisation (Government of India).

The above table reveals that while value of output had increased by a factor of 2.87 during the period 1992-93 to 2002-03, the corresponding increase in the central excise receipts was by a factor of 2.68.

1.3 Central excise receipts vis-a-vis Modvat/Cenvat availed

A comparative statement showing the details of central excise duty paid through Personal Ledger Account (PLA) and the amount of Modvat/Cenvat availed during the year 1992-93 to 2002-03 is given in the following table:

(Amount in crore of rupees)

Year	Central excise duty paid through PLA		Modvat/Cenvat availed		Percentage of Modvat/Cenvat to duty paid through PLA
	Amount	Percentage increase	Amount	Percentage increase	
1992-93	30614	8.91	10840	36.09	35.40
1997-98	47763	6.57	35164	2.75	73.62
1998-99	53053	11.07	35489	0.92	66.89
1999-2000	61672	16.25	41230	16.18	66.85
2000-01	68282	10.72	44986	9.11	65.88
2001-02	72306	5.89	47509	5.61	65.71
2002-03	82041	13.46	53039	11.64	64.65

The above table shows that while the central excise receipts had grown by 2.68 times during the decade 1992-93 to 2002-03, the increase in Modvat/Cenvat availed during the relevant period had been 4.89 times.

1.4 Cost of collection *

The expenditure incurred during the year 2002-03 in collecting central excise duty alongwith the corresponding figure for the preceding four years is given below:-

(Amount in crore of rupees)

Year	Receipts from excise duty		Expenditure on collection		Cost of collection as percentage of receipts
	Amount	Percentage increase over previous year	Amount	Percentage increase over previous year	
1998-99	53053	11.07	547.23	14.10	1.03
1999-2000	61672	16.25	584.82	6.87	0.95
2000-01	68282	10.72	615.84	5.30	0.90
2001-02	72306	5.89	635.79	3.24	0.88
2002-03	82041	13.46	702.55	10.50	0.86

* Figure furnished by Principal Chief Controller of Accounts (Central Board of Excise and Customs).

1.5 Outstanding demands *

The number of cases and amount involved in demands for excise duty outstanding for adjudication/recovery as on 31 March 2002 and 31 March 2003 are as follows :

(Amount in crore of rupees)

		As on 31 March 2002				As on 31 March 2003			
		Number of cases		Amount		Number of cases		Amount	
		More than five years	Less than five years	More than five years	Less than five years	More than five years	Less than five years	More than five years	Less than five years
(a)	**Pending with** Adjudicating officers	1379	25263	600.30	9155.10	1074	22841	265.01	20827.58
(b)	**Pending before**								
(i)	Appellate Commissioners	1457	20034	8420.84	13808.80	1339	19468	414.23	3063.30
(ii)	Board	206	105	18.51	55.00	32	34	0.46	2.65
(iii)	Government	57	30	1.57	19.46	171	97	3.38	17.41
(iv)	Tribunals	2126	6650	8530.25	6426.11	1781	6725	721.36	7429.94
(v)	High Courts	746	1710	1370.08	1184.65	696	1403	916.21	1094.60
(vi)	Supreme Court	136	376	326.73	2399.50	150	333	119.38	420.21
(c)	**Pending for coercive recovery measures**	1946	7181	271.94	2031.44	4449	6682	271.89	927.88
	Total	**8053**	**61349**	**19540.22**	**35080.06**	**9692**	**57583**	**2711.92**	**33783.57**

* Figure furnished by the Ministry of Finance (the Ministry) and relates to 92 Commissionerates

A total of 67275 cases involving duty of Rs.36495.49 crore were pending as on 31 March 2003 with different authorities.

1.6 Fraud/presumptive fraud cases *

The position of fraud/presumptive fraud cases alongwith the action taken by the Department against the defaulting assessees during the period 2000-01 and 2002-03 is depicted in the following table :

(Amount in crore of rupees)

Year	Cases detected		Demand of duty raised	Penalty imposed		Duty collected	Penalty collected	
	Number	Amount	Amount	Number	Amount	Amount	Number	Amount
2000-01	1475	2140.02	1568.90	322	48.40	266.74	89	6.64
2001-02	1454	897.53	306.52	264	33.49	19.48	99	1.47
2002-03	1705	1565.30	513.03	142	476.15	76.28	84	0.24
Total	**4634**	**4602.85**	**2388.45**	**728**	**558.04**	**362.50**	**272**	**8.35**

* Figure furnished by the Ministry and relates to 92 Commissionerates

The above data reveals that while a total of 4634 cases of fraud/presumptive fraud were detected during the years 2000-03 by the Department, involving a duty of Rs.4602.85 crore, the Department raised a demand of Rs.2388.45 crore only and recovered Rs.362.50 crore (15.17 per cent) out of it. Similarly, out of penalty of Rs.558.04 crore imposed, the Department recovered only Rs.8.35 crore (1.49 per cent).

1.7 Commodities contributing major revenue *

Commodities which yielded revenue of more than Rs.1000 crore during 2002-03 alongwith corresponding figures for 2001-02 are as follows :

(Amount in crore of rupees)

Sl. No.	Commodity	2001-02 (Actual)	2002-03 (Actual)	Percentage variation of actual over previous year	Percentage share in total collection
1.	Refined diesel oil	11028.45	10349.86	(-) 6.15	11.90
2.	Motor spirit	8500.87	11566.11	36.05	13.30
3.	Cigarettes and cigarillos of tobacco or tobacco substitutes	5059.51	5049.11	(-) 0.22	5.81
4.	Iron & steel	4665.12	5885.01	26.14	6.77
5.	Cement, clinkers, cement all sorts	3152.56	3440.63	9.13	3.96
6.	All other goods falling under chapter 27 (mineral fuels, oil etc.)	2878.34	3511.92	22.01	4.04
7.	Motor cars and other vehicles	2423.32	2483.66	0.35	2.86
8.	All other goods falling under chapter 84 (machinery, mechanical appliances etc.)	1716.29	1911.70	11.38	2.20
9.	Plastics and article thereof	1650.93	1851.63	12.15	2.13
10.	Petroleum gases and other gaseous hydrocarbons	1542.04	2442.61	58.40	2.81
11.	All other goods falling under chapter 87 (motor vehicles other than at serial no.7)	1533.79	1720.59	15.29	1.98
12.	Pharmaceutical products	1424.60	1418.96	(-) 0.39	1.63
13.	Organic chemical	1309.63	1609.01	22.85	1.85
14.	Synthetic filament yarn	1220.03	1304.49	6.92	1.50
15.	Diesel oil, not elsewhere specified	1178.67	1254.58	6.44	1.44
16.	Cane or beet sugar	1160.02	1275.93	9.99	1.47
17.	Tyres, tubes and flaps	1122.14	1123.38	0.11	1.29
18.	Paper and paper board, articles of paper pulp	1054.75	1173.64	9.46	1.35
19.	Public transport type passenger motor vehicles and motor vehicles for the transport of goods	748.87	1015.52		1.17
20.	Kerosene	699.45	1390.39	98.78	1.60

* Figure furnished by the Ministry.

The above table reveals that there was a shortfall in collection of revenue during 2002-03 in refined diesel oil, cigarettes and cigarillos of tobacco or tobacco substitutes and pharmaceutical products of (-) 6.15, (-) 0.22 and (-) 0.39 per cent respectively over previous year.

1.8 Contents of report

This section contains two reviews 'Call book' and 'Determination of assessable value under new section 4 (transaction value)'. The revenue implication is Rs.7040.39 crore. Besides, there are 166 paragraphs, featured individually or grouped together, arising from test check of records maintained in departmental offices and the premises of the manufacturers pointing out leakage of revenue aggregating Rs.1445.59 crore. Of these the concerned Ministries/Department had (till December 2003) accepted audit observations in 133 paragraphs involving Rs.287.61 crore and recovered Rs.32.82 crore. In 166 cases, based on available information, statutory audit detected objections in 157 units where internal audit had already been done.

CHAPTER II : REVIEW ON DETERMINATION OF ASSESSABLE VALUE UNDER NEW SECTION 4 (TRANSACTION VALUE)

2.1 Highlights

- **The absence of suitable provisions in the statute helped three oil companies to avoid payment of duty of Rs.713.17 crore on the indirect sale consideration received in the form of subsidy from the government on sale of petroleum products.**

(Paragraph 2.6)

- **Adoption of lower "mutually agreed price" for payment of duty by 12 terminals of three petroleum companies led to a revenue loss of Rs.113.79 crore.**

(Paragraph 2.7)

- **Clearance of goods by job workers manufacturing branded as well as un-branded goods for brand name owners/principal manufacturers, at lower assessable value resulted in a revenue loss of Rs.90.53 crore to the government as the said goods were sold by the brand name owners/principal manufacturers at much higher prices.**

(Paragraph 2.8)

- **Absence of mechanism to verify the correctness of the transaction value of assessee's own manufactured goods as well as the cost of bought out goods and the installation cost forming part of the total value of project installed at site, led to a revenue loss of Rs.90.88 crore in 10 cases where assessees could conveniently suppress value of their own manufactured goods while inflating the value of bought out items.**

(Paragraph 2.9)

- **Lacunae in the valuation rules permitting the assessees to determine the value of goods consumed captively at lower value despite availability of higher value of comparable goods during the relevant period, led to revenue loss of Rs.26.99 crore in seven cases.**

(Paragraph 2.11.1)

- **The assessment on transaction value basis has failed to plug leakage in revenue due to lacuna in the provisions and inadequate internal control mechanism.**

(Paragraph 2.14)

- **Irregularities in the valuation of excisable goods due to non-inclusion in the assessable value of various elements such as equalized freight, freight and insurance, dealer's margin, service licence fee, excess freight charges recovered, retail pump outlet charges for petroleum products and pre delivery inspection charges or service charges etc. resulted in short levy of duty of Rs.242.75 crore.**

(Paragraphs 2.15 to 2.20)

2.2 Introduction

Valuation of excisable goods chargeable to duty of excise on ad valorem basis has been laid down in section 4 of the Central Excise Act, 1944. Section 4 was amended to incorporate the concept of 'transaction value' for levy of duty with effect from 1 July 2000.

'Transaction value' means the price actually paid or payable for the goods, when sold, and includes any amount that the buyer is liable to pay to the assessee in connection with the sale whether payable at the time of sale or at any other time, including any amount charged for, or to make provisions for advertising or publicity, marketing and selling and storage etc. but does not include duty of excise, sales tax or any other taxes, if any, actually paid or payable on such goods. Therefore, each removal is a different transaction and duty is charged on the value of each transaction.

The new section 4, therefore, accepts different transaction values which may be charged by the assessee to different customers, for assessment purposes. Where one of the three requirements namely (i) where the goods are sold for delivery at the time and place of delivery; (ii) the assessee and buyers are not related; and (iii) price is sole consideration for sale, is not satisfied, then the transaction value shall not be the assessable value and value in such case has to be arrived at under the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, also made effective from 1 July 2000.

2.3 Audit objectives

A review was conducted in audit to evaluate the adequacy of provisions relating to valuation of excisable goods as substituted with effect from 1 July 2000 at the macro level and to identify weaknesses in the present provisions vis-à-vis the provisions in the old Valuation Rules.

At the micro level, records maintained by the manufacturing units were subjected to detailed scrutiny to seek assurance that the provisions as contained in section 4 of the Act and in the Central Excise Valuation Rules, 2000, effective from 1 July 2000, were being followed correctly and that the functioning of internal control was effective.

2.4 Audit coverage

Administrative control for collection of central excise duty vested with 92 Commissionerates of Central Excise of which 74 were covered in the review. Assessment records of 468 out of 4589 units engaged in the manufacture of excisable goods and paying more than Rs.1 crore duty each from PLA were reviewed in audit covering the period between July 2000 and March 2003.

2.5 Results of audit

During test check of records 360 cases of short collection/loss of revenue/duty forgone to the extent of Rs.1328.18 crore were noticed, in 64 Commissionerates of Central Excise.

Out of the above (i) Rs.1085.43 crore in the cases of 77 assessees, under 49 Commissionerates of Central Excise was due to lacuna in the statute provisions; and (ii) Rs.242.75 crore relating to 283 assessees, in 60 Commissionerates of Central Excise was on account of incorrect determination of transaction value on various grounds. The findings are contained in succeeding paragraphs.

Macro evaluation

➢ Weaknesses in the present system

2.6 Indirect consideration as a result of sale of goods, received from sources other than buyers

Losses suffered by oil companies on account of clearance of kerosene and LPG at lower prices fixed by Oil Co-ordination Committee (OCC) are compensated by government in the form of subsidies. Prior to 1 April 2002 subsidies on the above products, were being credited to the oil pool account. Thereafter, this subsidy is being paid in cash. Audit noticed that in the absence of specific codal provision to charge duty on the full value of consideration (including the part consideration received in the form of subsidy from the government), the additional consideration received from the government is excluded from levy of duty.

Scrutiny of the financial records of M/s. Indian Oil Corporation Limited (IOCL), M/s. Hindustan Petroleum Corporation Limited (HPCL) and M/s. Bharat Petroleum Corporation Limited (BPCL) revealed that the total subsidy claimed by the oil companies on account of sale of kerosene and LPG amounted to Rs.4457.27 crore during the period 1 April 2002 to 31 December 2002. Duty was paid on the controlled price and subsidy received from Petroleum Ministry was excluded from transaction value which resulted in duty amounting to Rs.713.17 crore being lost on clearances during this period.

2.7 Goods cleared at "mutually agreed price"

Audit observed clearances of excisable goods at a lower value on "mutually agreed price" exhibited as "transaction value" even though such a lower "mutually agreed price" did not fall within the definition of transaction value.

2.7.1 Agreed price less than ex-storage sale price

Petroleum products like motor spirit (MS), high speed diesel (HSD), superior kerosene oil (SKO), etc. have been assessed to duty on the basis of ex-storage sale prices that are fixed by the OCC. The assessable value remained the same, irrespective of whether the administered petroleum products were sold at the refineries or through the marketing companies. While introducing the new section 4, the Ministry clarified on 30 June 2000 that there was no essential difference in the scheme of valuation of petroleum products under the old and new section 4.

Though the administered price mechanism (APM) was dismantled with effect from 1 April 2002, prices of petroleum products continued to be monitored and regulated by the OCC.

As a sequel to the dismantling of APM with effect from 1 April 2002, the public sector oil companies entered into Memorandums of Understanding (MOUs) among themselves and inter-alia agreed that the refinery companies and their marketing installations would charge a notional price from 1 June 2002 for the products cleared to depots/terminals (viz. storage point) of other oil companies. Hence, the products (MS, HSD and LPG), falling under chapter 27 were cleared from the terminals of HPCL, IOCL and BPCL to terminals/depots belonging to other oil companies on payment of duty on assessable values which were much lower than the ex-terminal prices fixed for their own outlets/depots. Since terminals of the

latter were treated as independent wholesale buyers such lower price were taken as 'transaction value' for purpose of payment of duty.

Such a "notional price mutually agreed upon" by oil companies cannot be considered as a genuine price since (i) this price is adopted exclusively for oil exchange transactions alone and not for direct sales effected to distributors; (ii) the prices were lowered only for the benefit of each other; and (iii) the product sharing agreement & terms of MOUs also clearly established mutuality of interest among oil companies.

Petroleum products

The adoption of lower assessable values based on mutually agreed price at the time of clearance of the petroleum products from 12 terminals of IOCL, HPCL and BPCL under ten Commissionerates of Central Excise, to the terminals belonging to other oil companies and their depots (storage point) resulted in short collection of duty of Rs.113.79 crore during different periods between April 2002 and March 2003.

The Department stated (September/October 2003) that show cause notices had been issued to three assessees. In two other cases, the Department stated that the matter was already in their knowledge but no demands were raised till audit pointed out the issue.

Liquefied petroleum gas (LPG)

M/s. IOC Limited, in Chennai I Commissionerate of Central Excise, cleared LPG to various oil companies on payment of duty adopting the administered price during the period May 2002 to December 2002 despite realisation of higher value for the transaction from them. As APM was abolished with effect from 1 April 2002, assessment of LPG should have been determined based only on transaction value, non-adoption of which resulted in short levy of duty of Rs.3.53 crore during the period from May 2002 to December 2002.

The Department justified the assessment stating (May 2003) that the difference between transaction value and the price fixed by OCC pertained to budgetary support which could not be construed as additional consideration for inclusion in assessable value.

The reply of the Department is not tenable. Since the assessee recovered full value of the goods cleared to the marketing companies, there was no direct subsidy received by the assessee. The subsidy was received only by the marketing companies. The duty should have been charged on the full value of consideration received by the assessee.

2.7.2 Agreed price less than value based on cost of production

M/s. Indian Oil Petronas Private Limited, Kasberia, Haldia, in Haldia Commissionerate of Central Excise, entered into an agreement with IOC, HPC and BPCL respectively to receive LPG from Reliance Petroleum under bond on their behalf in cryogenic condition in its refrigerated storage tanks which was then to be subjected to different processes conforming to Bureau of Indian Standards (BIS) norms and cleared to different customers as directed by the oil companies at a price fixed by them.

Further scrutiny revealed that the assessee got terminal charges at fixed rates per tonne from the oil companies on account of such loading/handling and processing charges on such LPG. As the assessee was doing job work, the duty in the instant case ought to have been levied on the cost of production i.e. the value of raw materials plus job charges (in terms of judgement of the Apex court in the case of Ujagar Prints and Board's circular dated 1 July 2002) instead

of on the value fixed by the supplier. Adoption of incorrect procedure resulted in undervaluation of such goods and short levy of duty of Rs.61.33 lakh during the period from December 2001 to September 2002.

The Department's contention that the process did not amount to "manufacture" and hence duty as paid by the assessee on dictated price was correct is not acceptable since the assessee received such LPG under bond without payment of duty and goods underwent certain processes to enable them to conform to BIS norms and be made marketable. Since duty was paid from the assessee's premises its value ought to have been the cost of raw material plus processing charges.

2.7.3 Agreed price less than the cost adopted for captive consumption

M/s. Albright Wilson, in Raigad Commissionerate of Central Excise, arranged for procurement of sulphuric acid for its unit at Ambernath (Thane II Commissionerate) from M/s. Dharmjee Morarjee Chemicals. The price adopted was a mutually acceptable price lesser than the value for captive consumption. Lack of provision in the present rules to value such transaction, at a value at least equal to the value for captive consumption resulted in unintended benefit to the assessee at the cost of the exchequer. The clearance of goods at an agreed price resulted in undervaluation of goods amounting to Rs.77.49 lakh and short levy of duty of Rs.12.40 lakh for the period 1 October 2000 to 31 December 2001.

2.7.4 Agreed price less than cost of inputs

M/s. ITC Bhadrachalam (Paper Board Division), in Hyderabad III Commissionerate of Central Excise, engaged in the manufacture of paper and paper board falling under chapter 48 entered into an agreement with two job workers for converting reels of paper and paper board into sheets/reams. The assessee supplied white duplex board reel to one job worker at an assessable value of Rs.19000 per tonne. The finished sheets, however, were despatched by the job worker to the customer specified by the assessee adopting assessable value of Rs.18000 only per tonne. Thus, the finished product was valued at a price lower by Rs.1000 per tonne compared to the cost of material itself without the addition of job charges. In the case of second job worker it was observed that the assessee as well as the job worker cleared the input goods and finished products respectively adopting the same assessable value of Rs.19995.69 per tonne. In both the cases, conversion charges paid to the job workers were not included in the assessable value. Non-inclusion of conversion charges, of Rs.6.81 lakh and Rs.36.73 lakh respectively paid to the job workers during the period 2000-01 and 2001-02 resulted in short levy of duty of Rs.6.97 lakh, apart from differential duty payable on cost of raw material short adopted by Rs.1000 per tonne in the first case.

The Department's contention (July 2003) that the value at which the goods were cleared by the job worker represented transaction value is not correct, since conversion charges paid to the job worker were not included in the assessable value, and hence, were not subjected to duty.

2.8 Goods cleared by job workers on behalf of principal owners not to be considered as sale

Pursuant to the Supreme Court's decision in the cases of Ujagar Prints Limited {1989(34) ELT 493(SC)} and Pawan Biscuits Company Limited {2000(120) ELT 24(SC)} upholding

valuation of goods in the hands of job workers, certain big brand owners have been resorting to the modus operandi of getting their goods cleared through job workers on payment of duty either on cost of raw materials plus job charges or on an agreed price which are substantially lower than the wholesale prices at which the products are eventually being sold by the brand name owners/principal manufacturers. The lacuna is still not plugged in the new valuation rules.

The cases noticed during test check are discussed below: -

2.8.1 Clearances of branded goods

Test check of records of 26 assessees in 11 Commissionerates of Central Excise, revealed that they were manufacturing different excisable products on job work basis for the brand name owners and clearing the goods at an agreed price which was much lower than the normal price at which the principal manufacturers sold these goods. Job workers got assistance such as personal supervision, help in selection and purchase of raw material and its quality, preparation/formulation, technical knowhow by way of knowledge, training of staff all of which contributed towards the intrinsic value of the goods and were not accounted for. Besides, the principal brand owners incurred expenses on account of marketing, distribution, development of brand also. Since the possession of the goods remained with the brand name owners, the transaction cannot be termed a sale. Absence of provision in the Central Excise Act to charge duty at normal price i.e., the price at which the principal manufacturer/brand name owner sold these goods resulted in undervaluation of goods leading to short collection of duty of Rs.80.51 crore on clearances during the periods between July 2000 and March 2003.

2.8.2 Clearance of unbranded goods

Test check of records of eight assessees in five Commissionerates of Central Excise, engaged in the manufacture of excisable goods on job work basis for the principal manufacturers revealed that the assessees received raw material either from the principal manufacturers, or procured it from other sources as per their directions and cleared the entire processed goods back to them or to another destination on payment of duty on the basis of cost of production determined on the basis of landed cost of material plus processing charges including profit margin. Non adoption of prices charged by principal manufacturers resulted in short realisation of duty of Rs.10.02 crore during the periods between July 2000 and December 2002.

The Department cited the Supreme Court's judgement in the case of Ujagar Prints supra, according to which the duty was to be paid by job worker on the assessable value arrived at after adding the cost of material, processing charges and the profit of the job worker or the processor.

The absence of a suitable provision in the present Valuation Rules to charge duty at normal price (i.e. the sale price charged by the principal owner on the basis of whole sale market) has led to revenue leakage.

2.9 Uniformity of price/genuineness of transaction value not ascertainable - value of bought out items inflated

Under transaction value system, value of goods may vary even for the same buyer for different transactions. The genuineness of the transaction value cannot be scrutinised in the absence of statutory requirements for submission of declaration before the jurisdictional excise authority indicating the elements making up the transaction value.

Test check of records of 10 assessees in five Commissionerates of Central Excise, revealed the absence of any mechanism to verify the actual transaction value of assessee's own manufactured goods, bought out goods and installation charges which led to deliberate undervaluation of the assessee's own manufactured goods by over invoicing bought out goods although the total contract price of the final products remained unchanged. Total duty loss amounted to Rs.90.88 crore in respect of goods cleared during different periods between July 2000 and March 2003.

One of these cases is given below: -

M/s. Alstom Projects India Limited, Durgapur, in Bolpur Commissionerate of Central Excise, engaged in the manufacture of boilers and parts and accessories thereof, procured large lump-sum contracts with different customers for manufacture and supply of on-shore equipment of boilers. The contract included transportation, unloading and storage, erection, testing and commissioning charges of the equipment at site.

Test check of records revealed that while the lumpsum contract for supply of equipment for boilers was in consolidated form, excise duty was not paid on the entire contract value on the plea that a major portion of such equipment consisted of bought out items. Excise duty was, however, paid on such portion of the value that constituted the manufactured goods (ratio of bought-out items to such manufactured goods being 50:50 in most cases.) The assessee devised a billing break-up of numerous equipment both for manufactured goods and bought out items for supply to the customer. Accordingly, the payment was made by the customer on the condition that the break up of such billing did not exceed the total contract price of the goods to be supplied.

Test check of costing records also revealed that the value on which duty was paid (herein referred to as transaction value of manufactured goods) was kept abnormally low while distributing the total contract price between bought out items and own manufactured goods, and compensated such lower value by increasing the price of bought items (although bought out at much lower agreed price) so that it never exceeded the total contract price.

The correctness of the duty paid was not verifiable in the absence of statutory requirement of submission of declaration before the jurisdictional excise authority indicating the elements making up the transaction value. The assessee took advantage of this lacuna in the rule and undervalued own manufactured goods by increasing the price of bought out items. The value ought to have been arrived at as per rule 8 read with rule 11 of the Valuation Rules, 2000 on which basis Rs.1.09 crore during the year 2002-2003 escaped levy.

2.10 No provision for exclusion of cost of durable and returnable container from the transaction value

As per new section 4 cost of all durable and returnable containers shall form part of assessable value even if such packing or containers are supplied by the buyer for repeated use.

M/s. Solaris Chemtech Limited, Karwar in Mangalore Commissionerate of Central Excise, manufacturer of inorganic chemicals falling under chapter 28 cleared the excisable goods, viz., liquid chlorine and caustic soda lye on sale, after packing the goods in cylinders and tankers respectively. Excise duty was paid on the value of the goods, which did not include the cost of cylinders and tankers. In the absence of any exclusion clause, the packing of the said excisable goods in cylinders and tankers would be the essential part of the transaction, without which the goods could not be made marketable. This resulted in undervaluation of excisable goods of Rs.215.83 crore and short levy of duty of Rs.34.53 crore for clearances during the period from July 2000 to March 2003.

2.11 No provision for adoption of comparable goods price

2.11.1 Valuation of goods captively consumed

Before introduction of Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, excisable goods cleared for captive consumption by an assessee for further manufacture of other goods by himself or by his related persons, were to be valued under rule 6(1)(b) of Central Excise Valuation Rules, 1975, on the basis of comparable price of the same goods cleared to others. Under the new Valuation Rules, there is no provision for adoption of comparable price for goods captively consumed. They are to be valued at 115 per cent (110 per cent from 5 August 2003) of the cost of production under rule 8 of the new Valuation Rules, even if the same goods are sold to others at higher prices. The lacuna is leading to undervaluation of goods and short levy of duty.

Seven assessees in seven Commissionerates of Central Excise, engaged in the manufacture of excisable goods like bulk drugs, steel tubes, aluminium rolled products etc. falling under different sub-headings cleared products both for captive consumption within their units as well as to other units. While the products were cleared to others at higher prices during the periods between July 2000 and March 2003, the same were cleared for captive consumption on payment of duty on lower assessable values. Lack of provisions in the new Valuation Rules for adoption of comparable price resulted in short realisation of duty of Rs.26.99 crore during the aforesaid periods.

The Department replied that goods were being cleared as per existing rules.

2.11.2 Clearances of capital goods

As per erstwhile rule 57S of the Central Excise Rules, 1944, where capital goods were removed after being used in the factory, for home consumption on payment of duty of excise as if such goods were manufactured in the assessee's factory, duty was being calculated by allowing deduction of 2.5 per cent of Modvat credit already taken for each quarter of a year of use or fraction thereof from the date of availing credit under rule 57Q. In the absence of a similar provisions in the new Central Excise Rules, duty is being paid on the agreed price which works out to less than the duty payable under the old provisions.

M/s. Philips India Limited, in Pune Commissionerate of Central Excise, cleared capital goods on payment of duty by adopting transaction value. A comparable study of duty paid and duty payable as per old rules revealed that there was short collection of duty of Rs.26.44 lakh on capital goods cleared during August 2001.

2.12 Transaction value lower than price fixed under law

After introduction of the concept of "transaction value" under new section 4, there is no provision where a price fixed under a law (i.e. controlled price, administered price etc) could be taken as the transaction value, as was done under the erstwhile section 4(1)(a)(ii) of the Act.

The Ministry of Finance (the Ministry) had clarified in June 2000 that but for the normal value being replaced by the transaction value, there was no essential difference in the scheme of valuation of petroleum products under the old valuation and new provisions.

2.12.1 Three assessees in Vadodara and Ahmedabad Commissionerates of Central Excise, cleared their manufactured goods "bulk drugs" between July 2000 and October 2001 at a price much lower than those fixed under Drug Price Control Order (DPCO) and paid the duty at lower price. Despite Ministry's clarification (June 2000), the Department admitted these lower prices as assessable value for levy of duty instead of adopting the maximum price fixed under price control order. This resulted in loss of revenue of Rs.10.75 crore.

The Department stated that the Ministrys' clarification relates to products not covered by the DPCO. The reply of the Department is not tenable as in both cases the clarification is with reference to adoption of price fixed under any law. On the same analogy and Ministry's clarification, prices fixed under the DPCO are to be adopted as price of bulk drugs for levy of duty. The Department, however, issued (August 2001 and June 2002) show cause notices for Rs.15.04 crore in two cases. Orders of adjudication were awaited.

2.12.2 Superior kerosene oil (SKO) is cleared under the control of APM as framed/fixed by OCC under Ministry of Petroleum. In the absence of a provision to adopt price fixed by OCC as the transaction value, the assessable value of SKO is being fixed at lower price disregarding the price fixed under APM leading to loss of revenue to the government.

M/s. Indian Oil Corporation Limited, Haldia Refinery, in Haldia Commissionerate of Central Excise, manufacturing different petroleum products falling under chapter 27 of the Central Excise Tariff Act, 1985 cleared SKO (white) to other oil companies at a price which was lower than the price fixed by the OCC. Since the new system does not contemplate that the price fixed under law in respect of any commodity should be the transaction value, the assessee fixed the transaction value different from the administered price fixed for SKO (white). Thus, the product was undervalued and duty short paid by Rs.7.42 crore between March 2002 and April 2003.

2.13 No provision for differential duty on account of upward revision of prices

Unlike under the old section 4, there is no provision in the new section 4, effective from 1 July 2000, to re-determine the assessable value of excisable goods lying in stock at depot and charge differential duty on the basis of upward revision of price from a particular date.

M/s. Indian Oil Corporation Limited, in Chennai I Commissionerate of Central Excise, engaged in warehousing of petroleum products, sold the goods through depots also. The assessee made an upward revision of price on 1 March 2001 and 12 January 2002 which was given effect to simultaneously at factory gate as well as at depots. Since the assessee is not liable to pay differential duty on the stock lying at depot on account of price rise, loss of revenue of Rs.11.39 lakh had arisen which was reckoned with reference to the quantity of stock transfer made to depots on the day preceding the day of upward revision of price. The exact quantum of loss of revenue could not be ascertained in audit in the absence of correct stock position held at depot on the date of upward revision.

The Department stated that the assessee had already been addressed to furnish stock position at depots. The fact, however, remained that the Department had not pursued the issue further and hence their contention that they were seized of the issue is not acceptable.

Micro evaluation

2.14 Lack of control mechanism

2.14.1 Definition of "related person" more complex

Under the erstwhile system of valuation the concept of related person was defined in a very simple manner i.e. mutuality of interest must exist. Under the present system of valuation a more elaborate definition of "inter-connected undertaking" under the Monopolies and Restricted Trade Practice Act, 1969 (MRTP) has been adopted. The term "inter connected undertakings" comprehends three basic tests for inter connection viz. management, ownership and control of one undertaking by another. While the ownership test can be established/proved by verifiable evidence, the control and management aspect requires considerable investigation and collection of facts as to determine who really controls or manages an undertaking. This may lead to avoidance of in-depth scrutiny and attempt to prove the fact of related person by the Department especially in cases where goods are cleared to thousands of customers. Identification of relationship between the assessee and the customers may not be established as required in the statute.

2.14.2 Scrutiny of invoices not possible in normal course

In the absence of provision for submission of copy of invoice with the monthly/quarterly return, there is no possibility of its scrutiny in the normal course unless records are specifically called for from the assessee.

2.14.3 No provision for initiating action at the Department's level for determination of value of excisable goods on provisional basis

Rule 7 of the Central Excise Rule 2002, permits the assessee to make payment of duty on provisional basis where he is not able to determine the value of the excisable goods or rate of duty applicable thereon.

But, there is no provision in the new rules corresponding to the erstwhile rule 9B whereby the Department could initiate suo-moto action for resorting to provisional determination of value in cases where the value determined by the assessee was not accepted as correct.

2.14.4 Possibility of misuse of invoice by unscrupulous assessee not ruled out

There is no in-built system devised by the Department at range level to check misuse of invoices cancelled after the clearance of goods by unscrupulous assessees whereas under the earlier system assessee was required to submit copy of the cancelled invoice to the range officer within 24 hours of its cancellation.

2.14.5 Use of valuation cells not made mandatory

There is no statutory provision for creation of valuation cells to which doubtful cases of valuation could be referred for correct and final determination of value. The lack of control mechanism also contributed to incorrect determination of transaction values in some cases resulting in short payment of duty. The cases noticed in audit are discussed in the succeeding paragraphs.

2.15 Undervaluation of goods due to non inclusion of various charges in the assessable value

The Board vide its circular dated 30 June 2000 clarified that transaction value includes all elements which add value to the goods before they are marketed. Where the assessee charges an amount as price for the goods, the amount so charged and paid or payable for the goods will form part of the assessable value. If, however, in addition to the amount charged as price from the buyer, the assessee also recovers any other amount by reason of or in connection with sale, then such amount shall also form part of the assessable/transaction value.

Some of the important cases noticed in audit are highlighted below: -

2.15.1 Non inclusion of equalised freight/insurance

A test check of records of 22 assessees in 15 Commissionerates of Central Excise, engaged in manufacture of different excisable products revealed that the manufacturers inter-alia collected equalised freight/insurance for transportation of goods to the place of delivery. The amount so collected was abated from the total assessable value for purpose of levy of duty. Since under rule 5 of Central Excise Valuation Rules, 2000 abatement from assessable value of the amount of equalised freight/insurance is not a permissible deduction, duty ought to have been paid on the entire value including equalised freight/insurance. Duty of Rs.16.52 crore was levied short during different periods between July 2000 and March 2003.

The Department while confirming the facts in one case stated that the contention of audit would be considered at the time of finalisation of assessment. Reply is not specific, since equalised freight is not an eligible abatement and the same should have been disallowed by the Department without postponing the issue to the time of finalisation of assessment. In another case the Department stated (December 2002 – February 2003) that the matter was already in their notice and show cause notices had already been issued. Reply of the Department is not specific to the issue at hand. Scrutiny of the said show cause notices revealed that the notices issued were based on the Tribunal's decision in Escorts JCB Limited case, which had already been decided (October 2002) by the Supreme Court in favour of the assessee, whereas the audit objection was based on the non-implementation of Board's clarification dated 30 June 2000.

2.15.2 Non inclusion of dealers' margin on goods cleared through company owned and company operated (COCO) outlets

As per rule 9 of Central Excise Valuation Rules, 2000, where the assessee so arranges that the excisable goods are not sold by an assessee except through related person the value of such goods shall be the normal transaction value at which it is sold by the related person at the time of its removal.

Eighteen terminals of petroleum companies, in 14 Commissionerates of Central Excise, engaged in the manufacture and sale of petroleum products cleared MS and HSD through dealers and also through their own outlet viz., COCO in different zones. The assessable value of the products cleared through dealers and COCO outlets remained the same. But in cases of goods cleared to COCO outlets, dealer's margin was retained by the assessees who owned such outlets. Non-inclusion of dealers' margin in respect of goods sold through COCO outlets has resulted in short payment of duty of Rs.9.69 crore during the periods between July 2000 and March 2003.

The Department in two cases issued show cause notice covering the period from July 2000 to January 2002. No recovery of differential duty in respect of other assessees in other Commissionerates of Central Excise was started. It was also seen in audit that some of the assessees (in Commissionerates Chennai I & Coimbatore) had begun including the dealer's margin in transaction value from April 2002 onwards in respect of sale through COCO as a result of audit pointing it out.

2.15.3 Storage service licence fee (SSLF)

Oil companies recover licence fee from dealers for using the company's assets for dispensing their products like MS, HSD and SKO which is based on the quantity of oil uplifted by the dealers. The recovery of licence fee being an indirect consideration having direct nexus with the sale of product, is includible in assessable value.

Test check of records of oil companies at 22 terminals, in 15 Commissionerates of Central Excise, revealed that these oil companies recovered SSLF totalling Rs.31.88 crore (approximately) from the dealers during the periods between July 2000 and March 2003 but did not include the amount so recovered in the assessable value. This resulted in undervaluation of excisable products with short recovery of duty of Rs.5.36 crore during the aforesaid period.

The Department in five cases reported issue of show cause notices and in three other cases stated that they were under issue. In another case (Rajkot CCE) though the Department claimed knowledge of the issue, it in fact issued show cause notice after audit pointed out the irregularity.

2.15.4 Non inclusion of freight charges collected in excess of expenditure

In the case of 14 assessees, in 11 Commissionerates of Central Excise, it was noticed that the assessees collected freight and insurance in excess of what was actually paid to the transporters. Since only the actual cost of transportation including insurance was allowed to be deducted under rule 5 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, such excess realisation of freight from the buyers was required to be included in the 'transaction value'. Non-inclusion of such freight element in

the 'transaction value' resulted in undervaluation of excisable goods and short levy of duty of Rs.3.66 crore during the periods between July 2000 and March 2003.

The Department in two cases admitted the objections (with recovery of Rs.2.14 lakh in one case) but stated in the third case that the assessee had excluded the total cost of transportation from the total invoice price which he had collected from the customer. The fact, however, remained that the assessee despatched his own manufactured goods as well as other goods in the same vehicle and availed abatement of the entire amount of freight charges instead of the prorata cost of transportation on account of his own manufactured goods.

2.15.5 Retail pump outlet (RPO) charges for petroleum products

M/s. IOC Limited, Haldia Refinery, in Haldia Commissionerate of Central Excise, and six other assessees, in four Commissionerates of Central Excise, engaged in manufacture of petroleum products under chapter 27, separately collected RPO surcharge and RPO charges over and above the permissible limit prescribed by the Board on the clearances of HSD sold to retail pump outlets on the sale of HSD and MS to them which ought to have been included in transaction value. Non inclusion of such charges resulted in short recovery of duty of Rs.3.01 crore on clearances during the period from July 2000 to April 2002.

The Department stated that these were only delivery charges and hence not includible in the assessable value. The reply is not acceptable as the assessee was collecting delivery charges separately over and above the RPO charges.

2.15.6 Cost of transportation not shown separately in the invoice but excluded from the transaction value

Scrutiny of records of 17 assessees, in 13 Commissionerates of Central Excise, revealed that although they had recovered transportation cost they did not show such charges separately in the invoice in contravention of rule 5 of the Valuation Rules, 2000. The transportation charges so recovered from the buyers after the sale of excisable goods were, thus, liable to be included in the assessable value. The Board vide circular dated 30 June 2000 clarified that exclusion of cost of transportation from the value is allowed only if the assessee has shown them separately in the invoice for such excisable goods and the exclusion is permissible only for the actual cost so charged from his buyers. Non inclusion of such charges, therefore, resulted in undervaluation of excisable goods with subsequent short-levy of duty of Rs.18.76 crore during the periods between July 2000 and March 2003.

The Department in one case stated that the matter would be examined and in another two cases claimed that action was initiated prior to visit of CERA whereas the fact remains that the show cause notices were issued after the audit objections were raised.

2.15.7 Pre-delivery inspection and testing charges

The Board clarified on 1 July 2002 that after sales service and pre-delivery inspection charges (PDI) provided free by the dealers to the customers on behalf of the assessee, would be included in transaction value.

M/S. Hindustan Motors Limited, Hooghly and three other assessees, in four Commissionerates of Central Excise, engaged in manufacture of motor vehicles and parts and other excisable products had cleared their products to various dealers and government customers under DGSD rate contract. Scrutiny of records revealed that in case of sales to

customers, other than sales to government, central excise duty was calculated only on basic price of vehicle excluding the cost of pre delivery inspection charges and testing charges. Non adoption of such charges resulted in short-levy of duty of Rs.1.95 crore (including Rs.1.55 crore in case of Hindustan Motors) on the clearances made during the period between July 2000 and March 2003.

The Department admitted the objection in Hindustan Motors case and agreed to examine the other.

2.15.8 After sales service charges

The Board vide circulars dated 19 November 1997 and 12 January 1999 clarified that the cost towards free after sales service provided by the dealers out of their margin was includible in the assessable value. Based on an Apex court ruling to the contrary on 27 January 2000, the above circulars were withdrawn. The Board, however, subsequently clarified (July2000/December 2002) that after-sales service charges are includible in transaction value and also that earlier circulars would apply to past cases only as provisions of new section 4 introduced from 1 July 2000 were not subject matter of dispute before the Apex court.

M/s. Tractor and Farm Equipment Limited, Sembium, in Chennai II Commissionerate of Central Excise, engaged in manufacture of tractors cleared the product through dealers network who were entrusted with four free after sales services of tractors during warranty period. The cost of four free after sales service was met by dealers out of their margin and, therefore, such charges were includible in the transaction value. Non-inclusion of the same resulted in short levy of duty of Rs.15.66 lakh for the period from July 2000 to December 2002.

The Department stated (May 2003) that it would be taken care of at the time of finalisation of assessment for the period upto June 2002 and show cause notice would be served on the assessee for the later period i.e., July 2002 to December 2002. The Department's reply for the period from 1 July 2000 to June 2002 is not acceptable since Board's references cited were explicit on the issue and remedial action did not warrant postponement to the time of finalisation of provisional assessment.

2.15.9 Other charges over and above 'transaction value'

Test check of records of 22 assessees, in 17 Commissionerates of Central Excise, manufacturing different excisable goods revealed that the assessees did not include various "other charges"(including free supply of inputs or packing material in certain cases) collected over and above the declared transaction value. Since such charges were collected from the customers, as an indirect consideration in relation to the sale of goods, these charges ought to have been included in the transaction value. Non inclusion of these charges resulted in short levy of duty of Rs.5.97 crore during the period between July 2000 and March 2003.

The Department in three cases confirmed the demand of Rs.58.59 lakh; booked offence case for Rs.11.65 lakh in one case and issued show cause notice for Rs.12.34 lakh in another case. In one case the Department justified the amortisation of value of crates because of their repeated use. The reply is contrary to the Valuation Rules since crates are not used in the factory.

2.16 Incorrect deductions from the assessable value

Test check of records of 20 assessees, in 17 Commissionerates of Central Excise, revealed short levy of duty of Rs.10.50 crore due to incorrect deductions from the assessable value. Some of the interesting cases are given below: -

2.16.1 Commission paid for procuring orders

Two assessees, in Jalandhar and Coimbatore Commissionerates of Central Excise, engaged in the manufacture of nylon/polyester yarn (chapters 54 and 55) and chains (chapter 84) claimed trade discount at 2 per cent and 30 per cent respectively for arriving at the assessable value while transferring goods to their depots, consignment agents and dealers. As per the marketing pattern adopted by the first assessee, dealers were required to procure orders and arrange payments to the assessee alongwith interest wherever the payment was not made by due date. Since trade discount was not allowed on commercial invoices when the goods were invoiced by the assessee to the customers, credit notes were issued to the appointed dealers for 2 per cent of amount of invoice as "commission". In the second case the assessee passed on discount of 29 per cent and the balance 1 per cent was passed on to the whole sale dealers who acted as agents. This was contrary to the Apex court's judgement in the case of M/s. Coromondal Fertilizers Limited {1984(17) ELT 607} which had held that the commission paid to selling agents is not a trade discount and hence did not qualify for deduction.

Since relation between the assessees and dealers and consignment agents was that of principal and agents, trade discount at 2 per cent and 1 per cent deducted from transaction value at factory gate on the transfer of goods to consignment agents and dealers was in the nature of a commission paid to them for services rendered which was not admissible. This resulted in short levy of duty of Rs.6.37 crore on clearances during the periods between September 1997 and July 2002.

The Department in one case reported issue of show cause notice for recovery of excise duty of Rs.6.18 crore for the period May 1997 to August 2002 by invoking the extended period clause on the incorrect allowance of deduction of discount.

2.16.2 Incorrect deduction of freight collected for both ways under round trip kilo metre (RTKM) system

Test check of records of 11 terminals of oil companies, in nine Commissionerates of Central Excise, engaged in the manufacturing and marketing of various petroleum products like MS, HSD and SKO etc., revealed that the oil companies while clearing the products to various distribution outlets on payment of duty on ex-terminal prices through hired tankers at the distribution points, collected delivery charges for both ways in the name of RTKM charges from the dealers. The entire amount collected on account of transportation both ways was claimed whereas deduction for only onward freight would be eligible for deduction under rule 5 of the Valuation Rules. Incorrect deduction of two ways freight resulted in undervaluation of excisable products with short levy of duty of Rs.1.40 crore for the period from July 2000 to March 2003.

The Department in five cases promised to examine the issue.

2.16.3 Purchase tax on raw materials

Since only the duties and taxes paid/payable on finished products are eligible abatements to arrive at the transaction value of excisable goods manufactured, purchase tax paid on raw materials is not an allowable deduction. Mention was, therefore, made in Para 10.2 of CAG's Audit Report for the year ended 31 March 1999 regarding irregular abatement of purchase tax on raw material by M/s. TVS Suzuki Limited in December 1997 which the Ministry had admitted. However, test check of records of the same assessee in March 2003 revealed that such abatement continued upto 2001-02. This resulted in short levy of duty of Rs.1.02 crore for the period July 2000 to March 2002 viz. after the introduction of transaction value.

The Department admitted the objection and intimated issue of show cause notice for Rs.67.80 lakh for the period 2001-02 stating that for the earlier period, action would be taken at the time of finalisation of assessment.

2.16.4 Inadmissible discount

Under amended section 4 of the Central Excise Act, 1944, all types of discounts allowed on declared price and actually passed on to the buyer are permissible as deductions from transaction value.

Three assessees in three Commissionerates of Central Excise, claimed cash turnover discounts from the assessable value, but did not pass on the discount to the buyers on the aggregate quantity of goods sold from depots etc. Such discounts were, however, adjusted separately with the discounts passed on at a later date. Such an adjustment was not admissible after 1 July 2000, being contrary to provision pertaining to transaction value. This resulted in short levy of duty of Rs.62.14 lakh on clearances during the periods between July 2000 and March 2003.

The Department reported recovery of Rs.11.60 lakh in one case but in another case stated that discounts which are known later are also eligible for deduction from assessable value in terms of Board's circular dated 30 June 2000. The reply is not tenable since in view of rule 7 of the Valuation Rules, 2000 each transaction is treated as a separate transaction, and the amount of discount passed on in one transaction cannot be adjusted against the other.

2.16.5 Average/equalized turn over tax (TOT)

Test check of records of two assessees, in Vadodara and Noida Commissionerates of Central Excise, revealed short levy of duty of Rs.84.79 lakh on account of inadmissible deduction of average/equalised TOT. As per the rules all taxes and levies such as duty of excise, sales tax and other taxes are not included in transaction value provided they are actually paid or actually payable. As per para 8 of Board's circular of July 2002 transaction value does not allow deduction towards such taxes and levies if they are calculated on average/equalized basis.

One of the cases is given below: -

M/s. Apollo Tyres Limited, in Vadodara II Commissionerate of Central Excise, engaged in manufacture of tyres, determined the assessable value of their products for stock transfer to their depots after deducting government levies at the rate of 0.50 per cent from April 1999 to September 2001 and 0.35 per cent thereafter from the assessable value on account of

averaged/equalized payment and octroi charges based on payments on this account made during the previous years. Since deduction of government levies on account of TOT and octroi on averaged/equalized basis was not permissible, deduction of Rs.4.21 crore claimed towards such levies escaped payment of duty of Rs.67.29 lakh during the period from July 2000 to March 2002.

The Department accepted the objection and issued show cause notice in August 2002 and February 2003. Later it stated that the actual TOT was to be ascertained later on and was an admissible deduction. The fact, however, remains that equalised/average TOT was not a permissible deduction during the relevant period.

2.16.6 Abatement towards distress sale

The Supreme Court in the case of M/s. MRF Limited {1995 (77) ELT 433}, held that the abatement of discount claimed on the clearance of new tyres with reference to loss suffered by the dealers on account of defective nature of tyres cleared earlier is inadmissible.

M/s. TVS Motors, Hosur in Chennai III Commissionerate of Central Excise, manufacturing two wheeler motor vehicles directed their dealers to sell the stock held by them as on 1 March 2001 at reduced prices promising to compensate them for the loss suffered by way of 'special trade discount' on future clearances. The assessee in fact extended the above scheme in a phased manner to all his dealers in India restricting the 'special trade discount' to the actual loss suffered. On the analogy of the decision of the Apex court, such a deduction was not an eligible abatement. Incorrect abatement allowed to dealers in Tamilnadu, Pondicherry, Uttar Pradesh, and Karnataka amounted to Rs.1.55 crore resulting in short levy of duty of Rs.24.77 lakh during the period March and June 2001. Department was requested to ascertain the details for differential duty relating to dealers in other States.

The Department stated that a show cause notice had been issued to the assessee. But later stated that the judgement of MRF case would not be applicable in the instant case.

The assessee's letter dated 14 June 2001 addressed to the Department, however, revealed that 'special trade discount' claimed by the assessee and allowed by the Department was only to compensate the loss suffered by dealers and hence, it could not be treated as normal trade discount.

2.17 Under valuation of goods consumed captively

Test check of records revealed that 83 assessees in 37 Commissionerates of Central Excise, cleared excisable goods to their other units/related persons/inter-connected undertakings for captive consumption on payment of duty on basis of transaction value or the value determined under rule 4 instead of under rule 8 of the Valuation Rules. Scrutiny of records revealed that even in these cases, the assessees committed irregularities in working out cost of production, thus undervaluing the goods which resulted in short payment of duty of Rs.145.48 crore on clearance during different periods between July 2000 and March 2003.

One of the interesting cases is given below: -

M/s. Reliance Industries Limited (RIL), Jamnagar, in Rajkot Commissionerate of Central Excise, cleared the goods on payment of duty based on transaction value to its four major complexes viz. RIL, Patalganga Complex, RIL, Naroda Complex, RIL, Hazira Complex and RIL, Jamnagar Complex, for manufacturing different products. A consolidated balance

sheet/annual report was prepared showing therein inter divisional transfer of goods separately. On scrutiny of excise records it was noticed that inter divisional transfer of goods were valued at lower rate based on "transaction value" method instead of cost construction method i.e. 115 per cent of cost of production. Since the assessee did not provide the details of cost of production, same was worked out on the data available in the balance sheet for the year 2001-2002 on the line of Board's instructions issued in October 1996. Between July 2000 and February 2003, the assessee had transferred 45.12 lakh tonne of their products (paraxylene and naptha) at an aggregate value of Rs.7391.36 crore instead of an aggregate value of Rs.7688.30 crore computed at 115 per cent of cost of production. This resulted in under valuation of goods by Rs.296.95 crore with short payment of duty of Rs.47.51 crore.

The Department stated that in case of inter unit transfers, valuation will have to be done under rule 4 and not under rule 8 of Valuation Rules, and the sale at normal price at factory gate including to their other unit was in accordance with the rules. The Department's reply is neither relevant nor tenable as rule 4 of Valuation Rules, 2000 merely provides for adjustment of price at the time of delivery, if it is later than the time of removal.

2.18 Short levy of duty due to undervaluation of goods cleared to or through interconnected undertakings

Test check of records of four assessees in three Commissionerates of Central Excise, revealed that incorrect determination of the assessable value of excisable goods cleared to the subsidiary/interconnected undertakings resulted in short levy of duty of Rs.48.52 lakh during the periods between July 2000 and March 2003. Valuation of excisable goods was not made as per rule 10 of the Valuation Rules.

The Department in one case admitted the irregularities and intimated recovery of Rs.3.38 lakh.

2.19 Short levy of duty on goods sold through depots/consignment agents

Test check of records of excisable goods transferred to depots/premises of consignment agents in the case of six assessees, in five Commissionerates of Central Excise, revealed that the transaction value of goods determined in many cases was lower than the normal transaction value. As per rule 7 of the Central Excise Valuation Rules, 2000 where the excisable goods are not sold by the assessee at the time and place of removal but are transferred to a depot, premises of a consignment agent or any other place, from where goods are to be sold, the value shall be the normal transaction value i.e., the value at which the greatest aggregate quantity of such goods were sold from the depots/premises of consignment agents at or about the same time or at the time nearest to the time of removal of goods. Non following of the rules resulted in incorrect valuation of goods with consequent short levy of duty of Rs.23.96 lakh for the periods between July 2000 and March 2003.

The Department, therefore, was requested to verify the necessary details in respect of all the depots for the period from July 2000 onwards and raise demands wherever warranted for differential duty based on the analogy of irregularities that came to light during test check. So, in September 2001 and February 2003, Rs.16.24 lakh was debited/paid by two assessees.

2.20 Other interesting cases

During test check of records of 43 assessees, in 25 Commissionerates of Central Excise, various other cases of short levy of duty of Rs.20.98 crore were noticed as discussed below: -

2.20.1 Undervaluation of inputs cleared as such

Thirty seven assessees in 21 Commissionerates of Central Excise, cleared inputs as such to their other units, under the same management, for further use in manufacture of excisable goods. The assessees discharged duty liability equivalent to credit taken which was contrary to rules 57AB(4) of the Central Excise Rules, 1944, as applicable for the period 1 July 2000 to 28 February 2001 and rule 3(4) of Cenvat Credit Rules, 2001 for the period from 1 July 2001 to 28 February 2003. Fifteen per cent was required to be added to the landed cost of inputs cleared as such for purpose of determining the value for payment of duty. Non-adoption of the value equivalent to 115 per cent of the total landed cost of these inputs resulted in undervaluation of goods involving short levy of duty of Rs.10.24 crore during different periods between July 2000 and February 2003.

The Department stated that the removal of inputs and payment of duty was in accordance with the Board's circular. The reply is not tenable since the Board's instructions were not in conformity with the rules and hence the amendment was introduced with effect from 1 March 2003 which established the fact that valuation was required to be done at 115 per cent of the cost of production till 28 February 2003.

2.20.2 Incorrect valuation of goods by adopting value under rule 8 instead of transaction value

M/s. Bharat Bijlee and M/s. Aluflex, in Belapur Commissionerate of Central Excise, inter alia manufactured lifts and curtain wall which were, after installation, declared to be immovable and non-excisable goods. Accordingly, both the assessees paid duty on their components and parts cleared to the site for commissioning of the said goods. The duty on these components and parts was paid at 115 per cent of the cost of production under rule 8, considering clearance to their own site as captive consumption. This was incorrect as there was no captive consumption as envisaged in rule 8 and also when the "transaction value" i.e. the price actually charged of the goods was available. The incorrect adoption of "value" under rule 8 (115 per cent of cost of production), instead of the "transaction value" under section 4(1)(a), resulted in short levy of duty of Rs.5.79 crore on clearances during the different periods between July 2000 and March 2003.

➢ Delayed/non-withdrawal of notifications

2.20.3 Iron and steel products

With the introduction of new section 4 of the Central Excise Act, 1944, and allied Valuation Rules thereon with effect from 1 July 2000, the transaction value for each removal should be the basis for assessment of central excise duty. In the case of stock transfer of iron and steel products from integrated steel plants to their stockyard, the valuation at factory gate is to be governed by rule 7 of Central Excise Valuation Rules, 2000. However, notification No.13/2000 CE dated 1 March 2000 which exempts iron and steel products cleared from the steel plants for further sale at stockyards, from so much of the duty of excise as was more than the duty leviable at the factory gate, remained operative till 28 February 2003. The said

notification was, however, withdrawn vide notification 17/2003 CE dated 1 March 2003. As such during the period 1 July 2000 to 28 February 2003, due to overlapping of the provisions there was unintended benefit to the integrated steel plants selling their goods at stockyards.

M/s. Durgapur Steel Plant (a unit of Steel Authority of India Limited), at Durgapur, in Bolpur Commissionerate of Central Excise, engaged in manufacture of iron and steel products under chapter 72, while clearing the manufactured goods to its stockyards had charged "distribution charges" separately at Rs.400/Rs.200 per tonne but did not include the same in the value for the purpose of levy of excise duty availing exemption under notification No.13/2000 dated 1 March 2000. Due to non withdrawal of the notification, there was short-collection of duty of Rs.2.29 crore during the period from April 2001 and March 2002 (short levy relating to the period 1 July 2000 to March 2001 could not be calculated for want of details of clearances).

2.20.4 Motor vehicle parts

M/s. Ashok Leyland Limited, Ennore, in Chennai I Commissionerate of Central Excise, engaged in manufacture of motor vehicle components including internal combustion engines consumed the products captively in their factory and also stock transferred the goods to their other units. The assessee adopted either 115 per cent of cost of production or 60 per cent of spare parts price in terms of notification No.6/2000-CE dated 1 March 2000 and No.3/2001 CE (NT) dated 1 March 2001 for valuation of stock transferred goods whichever was found to be beneficial. Not rescinding the notification even after withdrawal of the concept of comparable price with effect from 1 July 2000 resulted in short levy of duty of Rs.2.09 crore for the period from December 2001 to December 2002.

The Department admitted that the observation pertained to policy decision of the government.

2.20.5 Incorrect valuation of goods based on MRP (section 4A) instead of transaction value (section 4)

Air conditioners of capacity upto 3 tonne falling under heading 84.15 are assessed to duty on the basis of maximum retail price (MRP) under section 4A. However, in case of supply of air conditioners against rate contract to the DGSD or government departments etc. where MRP is not required to be printed on the item, valuation is required to be done under section 4 (transaction value) and not under section 4A (MRP).

Two assessees in Delhi III and Delhi IV Commissionerates of Central Excise, sold air conditioners of 3 tonne capacity to various government departments/corporations and industrial customers etc. at prices as per rate contract/agreed price. The assessee, however, contrary to the Board's clarification dated 28 February 2002 paid duty on the basis of MRP under section 4A as against the contract/agreed price (actually charged) which was more than the value on which duty was paid. Thus, incorrect valuation of goods resulted in short payment of duty of Rs.57.32 lakh.

2.21 Conclusion

The assessment on transaction value basis has failed to plug leakage in revenue due to lacunae in the provisions and inadequate internal control mechanism. Provisions need to take into consideration the subsidies received from the government by petroleum companies as indirect consideration. The practice of assessees entering into mutually

agreed lower prices must be countered to protect revenue. Similarly, undervaluation by job workers and in case of contract agreements over invoicing of bought out items have a negative impact on revenue and suitable measures need to be taken to counter the same. Review revealed several instances of undervaluation due to non inclusion of various charges in assessable value as also incorrect deductions indicating weaknesses in administration. There is an urgent need to impose effective internal controls to check gross undervaluation of the excisable products and avoid leakage of revenue.

The above observations were pointed out in October 2003; reply of the Ministry had not been received (February 2004).

CHAPTER III : REVIEW ON CALL BOOK

3.1 Highlights

- **Intended as an interim arrangement wherein cases could be kept till they were ripe for adjudication, there has been a large increase in the number of cases retained in the call book in the year 2001-02.**

(Paragraph 3.4)

- **540 cases involving demands for Rs.413.58 crore in 55 Commissionerates were entered in the call book in violation of the prescribed norms.**

(Paragraph 3.6)

- **1512 cases involving demands for Rs.349.38 crore in 31 Commissionerates were kept in the call book even though no appeals were pending in these cases.**

(Paragraph 3.8)

- **4820 cases involving demands for Rs.2622.68 crore in 56 Commissionerates were kept pending in the call book for want of clarifications/decision by the Board.**

(Paragraph 3.9)

- **1655 cases involving demands for Rs.1043.82 crore in 37 Commissionerates continued to be retained in the call book despite these cases no longer being in contest with audit.**

(Paragraph 3.10)

- **Ineffective internal control mechanism coupled with non-adherence to the instructions of the Board regarding monthly review of the cases at Commissionerate level was largely responsible for accumulation of cases in the call book.**

(Paragraph 3.12)

3.2 Introduction

According to the Manual of Office Procedure brought out by the Department of Administrative Reforms and Public Grievances, a call book was required to be maintained by it in which a case which had reached a stage where no action could, or needed to be taken to expedite its disposal for at least 6 months (e.g. cases held up in the law courts) could be transferred with the approval of a competent authority. Cases transferred to the call book are not included in the monthly statement of pending cases.

The Central Board of Excise and Customs (Board) through their instructions dated 14 December 1995 enlarged the scope for inclusion of cases in the call book by clarifying that the following category of cases could be transferred to call books.

(i) Cases in which the Department had gone in appeal to the appropriate authority.

(ii) Cases where injunctions had been issued by Supreme Court/High Court/CEGAT, etc.

(iii) Cases where audit objections were contested.

(iv) Cases where the Board had specifically ordered the same to be kept pending and to be entered into the call book

In their 14th Report (May 1997) the Public Accounts Committee (11th Lok Sabha), expressed their concern over the manner of transfer of cases to call book and desired that the Ministry of Finance (the Ministry) review the system of transfer of cases and ensure that these were done strictly in terms of the instructions and were properly subjected to the prescribed periodical review both by the Commissioners as well as by the Board. In their 39th Report (13th Lok Sabha), Committee further desired that Commissioners of Central Excise should examine and approve the cases before their transfer to the call book and that such cases should be scrupulously reviewed regularly and the progress of linked cases in litigation also monitored.

3.3 Audit objectives

A comprehensive appraisal of the system of maintenance of call book was carried out to seek assurance that:

(i) only authorised cases were entered in the call book,

(ii) cases already entered were regularly reviewed and re-opened when ripe for adjudication.

For this purpose, records of 162 divisions/adjudicating sections in 56 Commissionerates of Central Excise out of 61 Commissionerates were checked. The audit findings are contained in the succeeding paragraphs.

Macro analysis

3.4 Increase in the cases transferred to call book

The pendency position of cases transferred to call book during the past 2 years (position as on 30 September 2002) in respect of 54 Commissionerates according to information furnished by them is given below: -

(Amount in crore of rupees)

Period	Cases		Percentage increase/decrease	
	No.	Amount	No.	Amount
Upto 2000-01	21925	8841.01	--	--
Upto 2001-02 (Position as on 30.09.2002)	29251	12313.74	33	39

From the table above it is evident that during the period 2001-02 there was a large increase of 33 per cent in terms of number and 39 per cent in terms of amount compared to the pendency upto 2000-01.

- An analysis of the rise in the quantum of cases transferred to the call book during the year 2001-02, revealed that there was a significant increase of 40 per cent in terms of numbers and 106 per cent in terms of amount in the category 'pending decision of the Board' over the previous year.
- Amongst the 11 Chief Commissionerates, the Chief Commissionerate, Delhi recorded an increase of 59 per cent in terms of number and 106 per cent in terms of the amount in cases transferred to call book during the year 2001-02 over the previous year.

3.5 Age-wise pendency

The age wise pendency of the cases in the call book in respect of 55 Commissionerates was as under :-

(Amount in crore of rupees)

	No.	Amount
More than 10 years old	1028	194.32
Between 6 and 10 years	3197	855.06
Between 3 and 6 years	8622	2891.33
Less than 3 years old	16404	8373.03
Total	**29251**	**12313.74**

The cases pending in the call book for more than 3 years was 44 per cent in terms of number and 32 per cent in terms of value.

Micro analysis

The number of demand cases transferred by the Department to call book being large, an effort was made in audit to identify the factors responsible for the pendency through a test check of the records of selected divisions.

3.6 Cases entered in violation of prescribed norms

The Board vide their instructions dated 14 December 1995 specified the category of cases which could be transferred to the call book. From a test check of records, it was revealed that 540 cases involving demand of Rs.413.58 crore in 68 divisions/adjudication cells in 55 Commissionerates had been kept in the call book, even though they did not fall under any of the categories specified for this purpose. The details are as under: -

(Amount in crore of rupees)

Sl. no.	Period	Ordered by the courts for denovo adjudication		Pending for want of chemical examiner's report		Pending with settlement commissioner		Transferred to call book without specific approval of Commissioner/Board		Provisional assessment cases	
		No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
1.	Cases more than 5 years old	59	12.06	8	0.16	--	--	91	10.23	7	97.89
2.	More than 2 years old	24	2.84	3	1.15	--	--	121	98.16	1	24.95
3.	Less than 2 years old	25	1.74	19	1.08	10	2.87	168	152.61	4	7.84
	Total	108	16.64	30	2.39	10	2.87	380	261.00	12	130.68
								Grand Total		**540**	**413.58**

Unauthorised transfer of these cases to the call book had resulted in locking up of large amount of potential revenue.

Some illustrative cases are given below :-

3.6.1 Nine cases involving revenue of Rs.3.80 crore in respect of M/s. Chittaranjan Locomotives, Asansol in Bolpur Commissionerate of Central Excise, were transferred to call book even though they were remanded by CEGAT and the Commissioner of Central Excise (Appeal) for denovo adjudication in 1991 and 1994 respectively. No action was taken by the Department to remove the cases from the call book and adjudicate the same for over 10 years.

On this being pointed out (September 2002), the Commissionerate replied (March 2003) that the cases had now been removed from call book and denovo adjudication done.

3.6.2 In Surat I Commissionerate of Central Excise, a case involving revenue of Rs.12.85 crore on account of wrong availment of Modvat credit on false documents against M/s. Rama Newsprint and Paper Limited Surat was irregularly transferred to call book in July 1999 without approval of the Commissioner because it was also being investigated by the CBI.

3.6.3 A provisional assessment order involving an amount of Rs.24.95 crore in respect of M/s. VICCO Laboratories was issued by Goa Commissionerate in September 1997. The case was transferred to call book in 1999. Despite the amendment in Central Excise Rules with effect from 1 July 2001, requiring the competent authority to finalise the assessment within six months, the case continued to be kept in call book. Thus, potential revenue of Rs.24.95 crore remained blocked due to unauthorised transfer of provisional assessment case to call book.

3.6.4 Demand notices involving excise duty of Rs.18.12 crore were issued to M/s. Indian Oil Corporation and M/s. Hindustan Petroleum Corporation in April 2000 and June 2000 respectively in Delhi I Commissionerate of Central Excise, at the instance of central excise intelligence. After a period of more than a year, the Board vide their orders dated 8 June 2001 assigned these cases to the Commissioner of Central Excise (Adjudication), Delhi by name for adjudication. Despite the appointment of adjudicating authority by the Board, the Commissioner of Central Excise, Delhi I, wrote to Director General, Central Excise Intelligence, Delhi in November 2001 requesting him to take up the matter with the Board for appointing an appropriate adjudicating authority, as he could not adjudicate due to jurisdictional problem. The case was unauthorisedly transferred to call book by the Delhi I Commissionerate thereby locking up potential revenue of Rs.18.12 crore.

3.7 Non-vacation of stay orders

The Public Accounts Committee in their 53rd Report (10th Lok Sabha) while discussing audit para 3.66 of Report of the Comptroller and Auditor General on Central Excise for the year 1990-91 expressed concern over the alarming situation of pendency of cases in the court and, cautioned both the Ministry of Finance and Law that 'there should be no let up in securing early vacation of stay orders and collection of substantial revenue that have been blocked'.

A test check of records revealed that 2106 cases involving revenue of Rs.1052.17 crore in 34 Commissionerates, were kept in call book for more than one year as on 30 September 2002

due to non-vacation of stay orders by the courts. The age-wise pendency of these cases was as follows:-

(Amount in crore of rupees)

More than 10 years old		More than 5 years old		More than 3 years old		1 to 3 years		Total	
No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
215	45.06	375	417.92	850	258.02	666	331.17	2106	1052.17

- Cases pending for more than 5 years constituted 28 per cent of the total cases pending in the call book for more than a year. Such prolonged delays betray lack of concerted effort to get the stay vacated as also non-existence of effective internal mechanism to cope with cases of litigation.
- Concerned over the heavy pendency of excise litigation cases, the Public Accounts Committee (1984-85) in their 9th Report (8th Lok Sabha) recommended creation of a separate Directorate in the Board for effective pursuance of the cases in litigation. The Ministry, however, created special cell (litigation) in the Board instead, which, Public Accounts Committee (2002-03) in their 39th Report (13th Lok Sabha) observed, had failed to cope with the cases of litigation. It was only after the Committee drew attention to their earlier recommendations that the Ministry created a Directorate of Legal Affairs under the Board in June 2002 after a lapse of more than 16 years.

Some illustrative cases are given below:

3.7.1 A show cause notice for Rs.10.60 crore for clearances between 1986 and 1989 was issued to M/s. Maruti Udyog Limited, Gurgaon in Delhi III Commissionerate in April 1990. The case was transferred to call book in 1991, when the assessee filed a writ petition in Delhi High Court and obtained stay orders in February 1991. Even after a lapse of more than 12 years, the stay has not been got vacated. On this being pointed out (September 2002), the Commissioner of Central Excise, Delhi III wrote to the central government standing counsel in September 2002 for taking necessary action for early listing of the case.

3.7.2 Demands for duty of Rs.3.02 crore and Rs.1.11 crore against M/s. Mayil Mark Nilayam Chennai I and M/s. Palanganatham Rice and Oil Mills, Madurai were issued by Chennai I and Madurai Commissionerates respectively on account of clearance of shikakai powder without payment of duty in 1998. The assessees filed a writ petition in Madras High Court and obtained stay orders in 1998, citing a judgement of Karnataka High Court that shikakai was not dutiable. However this judgement was struck down by the same High Court and classification of shikakai under chapter 33 upheld by the Supreme Court (January 2000). Despite judgements favourable to revenue and instructions by the Board (February 2002), the Department did not get the stay vacated.

3.7.3 Three show cause notices involving demand for Rs.4.64 crore for the period from April 1986 to June 1999 on account of dutiability of teleprinter rolls were issued to M/s Delhi Paper Products Co. (P) Limited, in Delhi I Commissionerate of Central Excise. The show cause notices were transferred to the call book on the plea that the assessee had obtained a stay in September 1982, in an earlier case. No efforts was made by the senior central government counsel to either seek an opinion from the legal department on the applicability of the earlier stay order to the present case or to get the stay vacated from the High Court. Even after the request by the concerned Deputy Commissioner, the anti evasion branch took

no action to book a case or seize goods. The Department also failed to issue further demand notices for the period from July 1999 onwards. The non-issue of demand notices could result in the demands for the period after July 1999 becoming time barred.

3.7.4 M/s. Bajaj Auto Limited was served with 40 demand notices for Rs.2.25 crore during the period October 1986 to March 2002. The notices were transferred to the call book during the period from December 1987 to May 2002 based on a stay order from Mumbai High Court. A civil appeal was filed for vacation of stay. No follow up action was taken by the Department on two interim orders passed by High Court in December 1994. The case is pending for over 14 years.

3.8 Cases where no appeal is pending

A scrutiny of records revealed that 1512 cases out of 29251 cases pending as on 30 September 2002 involving demand for Rs.349.38 crore in 34 divisions/adjudication branches in 31 Commissionerates, were being kept in the call book despite existing judgements by courts in these cases/similar cases.

Some illustrative cases are given below :-

3.8.1 The validity of section 3A of the Central Excise Act, 1944 was challenged by iron and steel manufacturers in the case of Government of India vs. Supreme Steels Private Limited and others, before the Apex court. The Supreme Court passed interim orders in April 1998 barring the Department from taking penal or coercive measures. The Ministry of Law opined on 9 August 2000 that the Department could, however, adjudicate cases in respect of duty alone. The case was finally decided in favour of revenue and the Board issued instructions on 21 January 2002 to finalise all pending assessments.

Audit observed during test check of records that despite the above orders, 759 cases involving Rs.105.90 crore in 22 Commissionerates both on account of duty and penalty and interest, continued to be kept in the call book.

3.8.2 A case involving revenue of Rs.4.87 crore in respect of M/s. Bhushan Processors Private Limited in Ahmedabad I Commissionerate was transferred to call book in January 2000, as the assesseee filed special leave application in both Gujarat High Court and Supreme Court. Even though the case was dismissed by Gujarat High court on 22 February 2000 and Supreme Court on 31 October 2000, the same was not removed from the call book till the date of audit (December 2002).

3.9 Clarification awaited from the Board

A scrutiny of records in 56 Commissionerates revealed that 4820 cases involving an amount of Rs.2622.68 crore were kept pending under the category 'for want of clarifications from the Board'. The age-wise pendency of the cases was as under:-

(Amount in crore of rupees)

Cases more than 5 years old		More than 3 years old		Less than 3 years old		Total	
No.	Amount	No.	Amount	No.	Amount	No.	Amount
278	25.35	455	458.86	4087	2138.47	4820	2622.68

There was an alarming increase (40 per cent in terms of number and 106 per cent in terms of the amount) in this category during the year 2001-02, which is indicative of a reluctance by the Board to take a final view on issues ordered by it to be kept pending.

Some illustrative cases are given below :-

3.9.1 Twelve show cause notices for Rs.96.21 crore for the period from June 1996 to February 2002 on account of misclassification of bathing bars were issued to M/s. Hindustan Lever Limited in Pondicherry Commissionerate. Due to Board's instructions dated 16 November 1999, the case was transferred to call book in 1999. The issue was kept pending for 6 years and in the call book for more than three years for want of a decision by the Board.

3.9.2 On a demand raised by Mumbai VI Commissionerate against M/s. Amardeo Plastics for Rs.52.82 crore, the assessee made a representation to the Board on 26 October 1998. The Board did not specifically order the case to be kept pending and the Commissioner of Central Excise intimated the Board that the case was under the process of adjudication. Despite this, the case was irregularly transferred to call book on 29 January 1999. Interestingly, there was no further communication from the Board. Thus adjudication in this case has been postponed and the case transferred to call book.

3.10 Cases where audit objections were already accepted/settled

As per the orders of the Board dated 14 December 1995 only those cases relating to audit objections were to be transferred to call book which were contested by the Department. A scrutiny of records revealed that 1655 cases in 37 Commissionerates involving demands for Rs.1043.82 crore continued to be retained in the call book even though in these cases either the objections were already admitted by the Ministry or settled in audit on furnishing of necessary clarification by the Department. These cases being no longer in contest, ought to have been recalled from call book.

A few illustrative cases are given below :-

3.10.1 On an objection raised in audit in 1995, show cause notices involving an amount of Rs.3.80 crore were issued on account of mis-classification of carton boxes to M/s VFC Limited, Halol in Vadodara Commissionerate. All these cases were transferred to call book in 1996 pending decision of the Commissioner (Appeal), who in his orders dated 26 May 1998 decided the case in favour of revenue thus upholding the contention of audit. Since the objection was no longer in contest, the show cause notices ought to have been removed from call book and adjudicated upon.

3.10.2 Even after the objections raised by Audit were admitted by the government, the following cases continued to be kept in the call book.

(Amount in crore of rupees)

Commissi-onerate	Name of the assessee	Audit para no. and period of the audit report	Amount
Bolpur	IISCO, Burnpur	2.17(iii)(b) of 1992-93	0.28
Kolkata I	India Foils	3.19 of 93-94	1.69
Kolkata IV	Dankuni Coal Complex	8.2 of 2001-02	3.57
Kolkata II	Hindustan Lever Chemicals Limited	8.11 of 2001-02	0.82
		Total	**6.36**

3.11 Loss of revenue due to closure of units

A test check revealed that in 36 Commissionerates, 1106 units against whom demands for Rs.178.12 crore were kept pending in the call book were already closed as per details given below: -

(Amount in crore of rupees)

	No.	Amount
Units closed for more than 5 years	721	104.68
Units closed for more than 3 years	154	41.76
Units closed since less than 3 years	231	31.68
Total	**1106**	**178.12**

The prospects for recovery in the event of finalisation of adjudications proceedings in these cases appear to be bleak.

A case is illustrated below: -

A demand case involving an amount of Rs.2.05 crore in respect of M/s. Ishar Alloy Steels Limited in Indore Commissionerate was unauthorisedly transferred to call book in November 1997 in violation of norms prescribed by the Board. While the unit was closed by the assessee in 2000, the case was not adjudicated as it had been transferred to the call book unauthorisedly.

3.12 Ineffective internal control mechanism

An appraisal of the internal control mechanism conducted in audit revealed the following: -

3.12.1 Review at range/divisional offices

As per the Manual of Office Procedure for central government offices, the range officer/divisional officer is required to review the call book cases on a monthly basis so that the cases which have become ripe for action are removed from it before preparation of monthly technical report. It was noticed that in 65 test checked divisions/adjudication branches of 26 Commissionerates, no such review was undertaken.

3.12.2 Non-maintenance of call book register/non-preparation of monthly abstract

In 8 test checked divisions/adjudication branches, it was noticed that call book registers were not being maintained in the format as prescribed in the manual of office procedure. In 24 test checked divisions, call book registers were not found closed every month. No monthly abstract showing opening balance, receipt, disposal, closing balance etc. was drawn at the end of each month in these divisions.

3.12.3 Incorrect reporting in monthly technical report

It was noticed in 44 test checked divisions that no proper checks were exercised at the time of incorporation of the information in the monthly technical reports. This resulted in incorrect/suppressed data of pendency being reported therein.

Some of the cases of discrepancies are illustrated as follows: -

(Amount in crore of rupees)

Commisionerates/ Divisions	Period	Call book of adjudication branch/division		As per technical report of adjudication branch/ division		Difference	
		No. of cases	Amount involved	No.	Amount	No.	Amount
Vadodara (Division IV)	30.6.02	81	112.61	81	668.27	--	555.66
Delhi III (Gurgaon I)	30.9.02	173	368.18	173	169.59	--	198.60
Vishakhapatnam	30.9.02	74	145.62	65	284.20	9	138.58
Delhi I (All divisions)	30.9.02	174	303.71	165	425.69	9	121.98
Delhi III (Gurgaon II)	30.9.02	159	94.40	165	104.03	6	9.63
Kolkata III (Adjudication Cell)	30.9.02	65	106.36	54	99.22	11	7.14
Bolpur (Adjudication Cell)	30.9.02	92	258.10	221	264.92	129	6.82
Delhi III (Ambala)	30.9.02	245	39.24	175	33.90	70	5.35
Guntur (All divisions)	30.9.02	141	65.00	138	69.63	3	4.63
Mumbai VI (Adjudication Cell)	30.6.02	131	160.38	68	155.79	63	4.59

The fact that discrepancies existed in reporting was also highlighted by the Board which issued instructions on 23 May 2003 to all the Commissioners to take utmost care in compiling vital data.

3.12.4 Review at commissionerate level

The Board vide their letters dated 6 September 1990, 4 March 1992 and 30 March 1998 directed the Commissionerates to review the pending cases every month. Audit scrutiny revealed that in 30 test checked Commissionerates, the monthly technical reports received from divisions were compiled and furnished to the Chief Commissioners without proper review of the cases shown as pending in the call book.

On this being pointed out (February 2003), the Bolpur Commissionerate replied (March 2003) that due to frequent transfers at the level of the Commissioner/Additional Commissioner and Joint Commissioner, such review could not be done.

3.13 Action by the Department on audit findings

On audit pointing out irregular transfer of cases to the call book, 258 cases involving an amount of Rs.52.46 crore which were ripe for adjudication were removed from the call book.

A few illustrative cases are given below: -

3.13.1 The demand case involving Rs.4.18 crore relating to M/s. Richardson and Cruddas, Nagpur in Nagpur Commissionerate of Central Excise, was taken out of call book by the

Department for adjudication (February 2003) when it was pointed out in audit (July 2002) that following a ruling of the Supreme Court in M/s. Elecon Engineering Company Limited Vs. Commissioner of Central Excise, Chandigarh, a similar case had been decided by the CEGAT in favour of revenue.

3.13.2 Three cases of provisional assessment involving demand for Rs.1.16 crore in respect of M/s. CIMMCO, Gwalior, in Indore Commissionerate of Central Excise were removed from call book in August 2002 on being pointed out by Audit that these cases were kept in the call book in violation of the prescribed norms.

3.14 Recommendations

In view of the increase in the number of demand cases transferred to call book, there is an urgent need for streamlining the monitoring system by effective monthly review both at divisional and Commissionerate level. Proper co-ordination between Commissioners and newly formed Directorate of Legal Affairs, Customs and Central Excise is required to cope with litigation cases effectively. Besides, it is recommended that time limit be stipulated for decision by the Board on cases transferred to call book on its specific orders.

The above observations were pointed out in August 2003; reply of the Ministry had not been received (February 2004).

CHAPTER IV : TOPICS OF SPECIAL IMPORTANCE

4.1 Duty not realised in compliance of Finance Act, 2002

By notification dated 8 July 1999 as amended on 9 February 2000, Numaligarh Refinery was entitled to get refund of duty paid on mineral based goods. This refund has been withdrawn by notification dated 1 March 2002 with retrospective effect.

Section 142 of the Finance Act, 2002 (enacted on 11 May 2002) further provides that the amendment withdrawing the grant of refund, shall be deemed to have been made on and from 8 July 1999 to 28 February 2002 retrospectively as if the notification as amended had been in force at all material times and recovery shall be made of all amounts which have been refunded before amendment of the notification on 1 March 2002, within thirty days from the date on which the Finance Bill, 2002 receives the assent of the President, and in the event of non-payment, interest at the rate of fifteen per cent per annum shall be payable from the date immediately after the expiry of the said thirty days till the date of payment.

Test check of records of M/s. Numaligarh Refinery in Shillong Commissionerate of Central Excise, revealed that an amount of Rs.667.16 crore was refunded to the assessee on clearances of petroleum products like high speed diesel (HSD), superior kerosene oil, naptha etc. between February 2000 and February 2002. This amount was recoverable by 9 June 2002 i.e., within thirty days from the date of assent of the President to the Finance Bill, 2002. No action was taken by the Department to recover the amount. The total amount recoverable worked out to Rs.748.04 crore including interest of Rs.80.88 crore due upto 31 March 2003.

On this being pointed out (March 2003), the Ministry of Finance (the Ministry) stated (January 2004) that the retrospective amendment of the notification dated 8 July 1999 had been done only in relation to the goods mentioned in schedule to the notification and since the refinery was granted refund under amendment dated 9 February 2000 and not on the basis of the schedule to the subject notification, refund granted to the unit was not attracted for recovery.

Reply of the Ministry is not tenable as M/s. Numaligarh Refinery is the only mineral oil based unit which had availed benefit under notification dated 8 July 1999 as amended on 9 February 2000 and since this notification has been withdrawn with retrospective effect by section 142 (1) of the Finance Act, 2002, the amount is recoverable with interest.

4.2 Exemption allowed in violation of notification

Under notification dated 7 May 1997, pan masala in retail packages upto 4 grams was exempt from fifty per cent of the maximum retail price declared on the package in which such goods are sold in retail. By another notification dated 2 June 1998 pan masala packed and sold in retail packages upto 10 grams was notified for assessment of duty on the basis of tariff values which ranged from Re.1 to Rs.6 per pack depending upon the weight of the contents in the packages. By an amendment dated 8 June 1999, a sub-clause was added in both these notifications stipulating that "this notification shall not be applicable to goods containing not more than 10 per cent betel nut by weight and not containing tobacco in any

proportion". As per the amended version, these notifications were not to be applied if pan masala contained tobacco in any proportion and consequently duty was payable on them on the basis of normal price/transaction value under section 4 of Central Excise Act, 1944.

Test check of records of ten assessees in Hyderabad III, Kanpur, Lucknow, Vadodra and Valsad Commissionerates of Central Excise, revealed that these assessees manufactured pan masala which contained tobacco. They cleared their products availing benefit under the notifications ibid. Since their pan masala contained tobacco, they were not entitled to the benefit of the said notifications and were liable to pay duty under section 4 on the basis of normal prices upto 30 June 2000 and transaction values thereafter. This resulted in incorrect grant of exemption of Rs.81.78 crore between June 1999 and March 2003.

On this being pointed out (March and May 2003), the Ministry while admitting objection in principle from 1 March 2001 stated (January 2004) that for period prior to 1 March 2001 pan masala containing tobacco was eligible for exemption as it was classifiable under heading 21.06.

Reply of the Ministry is not tenable as pan masala containing tobacco was not eligible for exemption even under heading 21.06 in view of the specific restriction imposed by amending notification dated 8 June 1999 cited in sub para 1 supra.

4.3 Exemption from additional duty allowed without exemption notification

By section 133 of the Finance Act, 1999, additional duty of excise at the rate of one rupee per litre on HSD oil has been levied with effect from 28 February 1999. This rate has been increased to one rupee fifty paise per litre from 1 March 2003.

Under rule 13 of the Central Excise Rules, 1944, read with notification dated 22 September 1994 as amended, excisable goods meant for export outside India may be cleared from the factory of a manufacturer or from a warehouse without payment of duty under bond. In the new Central Excise Rules, 2002, similar provision for duty free clearance of export goods is provided under rule 19 read with notification dated 26 June 2001 issued thereunder. In rule 2(7) of the Central Excise Rules, 1944/rule 2(e) of the Central Excise Rules, 2002, the term 'duty' means duty payable under section 3 of the Central Excise Act. Additional duty leviable under Finance Act, is not exempt from payment on goods cleared for export under said notification/rule 13, since this duty is distinct and different from those leviable under section 3 of the Central Excise Act.

The Supreme Court in the case of M/s. Modi Rubber Limited {1986(25) ELT 849 SC} held that "where a notification granting exemption is issued only under sub rule 1 of rule 8 of the Central Excise Rules, 1944, without reference to any other statute making the provisions of the Central Excise Act, 1944 and the rules made there under applicable to the levy and collection of special, auxiliary or any other kind of excise duty levied under such statute, the exemption must be read as limited to the duty of excise payable under the Central Excise Act, 1944 and cannot cover such special, auxiliary or other kind of duty of excise".

Test check of records revealed that 10 assessees in 7 Commissionerates of Central Excise, engaged in the manufacturing/marketing of petroleum products, cleared under bond 543286.265 kilo litres of HSD and low sulphur heavy flash (LSHF) for export or for consumption on board a ship bound for foreign port during the period from May 1999 to

March 2003 without payment of additional duty leviable under the Finance Act. Since additional duty leviable under the Finance Act was not covered under rebate/exemption, clearance of HSD and LSHF without payment of duty was incorrect. This resulted in non-payment of duty of Rs.54.34 crore. It was also noticed in audit that show cause notices for Rs.46.70 lakh issued by Mangalore and Tirunelveli Commissionerates of Central Excise in November 2000, May and September 2002 were dropped in adjudication as the cases were decided in favour of the assessees, in January 2001, September and November 2002 respectively. No appeal was filed in these cases as the Department was of the view that notification dated 22 September 1994 would apply in relation to levy and collection of additional duty of excise leviable under Finance Act. Audit also noticed that in the case of M/s. Indian Oil Corporation, Korukkupet, the Chennai I Commissionerate of Central Excise confirmed the demand of Rs.3.12 lakh in February 2000, deciding that the additional duty leviable under the Finance Act was not covered by said notification. The Commissioner (Appeals) had also upheld the decision of Chennai I Commissionerate in January 2001. Revenue not realised in 10 cases alone amounted to Rs.54.34 crore.

The Ministry stated (December 2003) that the provisions relating to rebate of central excise duty were applicable to additional duty also as section 133 (3) of the Finance Act, 1999 extended the applicability of the provisions of Central Excise Act and the Rules for the levy and collection of additional duty of excise.

Reply of the Ministry is not tenable as Central Excise Act and Rules stipulate that rebate of duty may be granted by issue of notification. In the absence of such a notification, rebate of additional duty was not admissible. The government specifically provided for rebate of additional duty of excise as levied under section 157 of the Finance Act, in 2003. Similar provision should have been inserted in the notification for grant of rebate of additional duty of excise on HSD oil.

4.4 Loss of revenue due to delay in amendment of rules

Under rule 57A of the Central Excise Rules, 1944, (rule 57AB(2) from 1 April 2000 and rule 3(6) of the Cenvat Credit Rules, 2001, as it stood before 1 March 2002), Cenvat credit in respect of inputs or capital goods produced and cleared to a domestic tariff area by a hundred per cent export oriented unit (EOU), shall be restricted to the amount which is equal to the additional duty as leviable on like goods under section 3 of the Customs Tariff Act, 1975, paid on such inputs.

While interpreting the above rule, the Tribunal, in the case of M/s. Vikram Ispat {2000 (120) ELT 800 (Trib – LB}, had held on 9 August 2000 that if additional duty was less than the actual duty paid on the inputs cleared from hundred per cent EOUs, the manufacturer in India would be eligible for credit equivalent to additional customs duty leviable on such goods.

The relevant amendment in rule 3 (6) of Cenvat Credit Rules was brought out later on 1 March 2002 through the Finance Act, 2002 so as to allow credit of additional customs duty actually paid by hundred per cent EOU.

Three assessees, in Mumbai VII and Aurangabad Commissionerates of Central Excise, engaged in the manufacture of iron and steel products and capacitors were receiving certain inputs from hundred per cent EOUs. Assessees availed credit of additional duty payable on such goods even though additional duty actually paid was only 50 per cent. During the period

from September 2000 to February 2002, assessees availed credit of Rs.25.27 crore as against Rs.13.24 crore actually paid by them. Delay by 17 months in amending the rule, even after the issue had been raised in the Tribunal, resulted in loss of revenue of Rs.12.03 crore in three cases alone.

The Ministry while admitting the objection in principle stated (December 2003) that an appeal had been filed in Mumbai High Court against the Tribunal's decision in the case of M/s. Vikram Ispat, ibid.

4.5 Grant of deemed credit of duty in contravention of rules

4.5.1 Rule 57AB of the Central Excise Rules, 1944, and rule 3 of the Cenvat Credit Rules, 2002, prescribes that credit in respect of the additional duty of excise leviable under section 3 of the Additional Duties of Excise (Goods of Special Importance) Act, 1957 shall be utilized only towards payment of excise duty leviable under the Additional Duties of Excise (Goods of Special Importance) Act, 1957, on any final product manufactured.

By issue of notification dated 1 March 2001 (as amended on 29 June 2001) and 1 March 2002, the Government allowed deemed credit ranging from 20 per cent to 66 2/3 per cent of the aggregate of duty of excise leviable under the Central Excise Act, 1944 and the additional duty of excise leviable under the Additional Duties of Excise (Goods of Special Importance) Act, 1957, on the final products declared therein.

Test check of records of 27 assessees in Chandigarh I & II, Jaipur II and Surat I Commissionerates of Central Excise, engaged in production of processed fabrics, revealed that credit of additional duty of Rs.24.72 crore had been availed between March 2001 and November 2002. The credit so availed was utilized for payment of additional duty on final products though no additional duty was paid on inputs used in their manufacture. Inclusion of additional duty payable under the Additional Duties of Excise (Goods of Special Importance) Act, 1957, in the said notification, for grant of deemed credit, was not correct as this duty was not leviable on the declared inputs (viz. yarn). Additional duty was also exempt on the intermediate product – grey fabrics. Therefore, as no additional duty was payable on the inputs, the grant of credit of the same was incorrect in the light of the restrictions in the Cenvat Credit Rules.

On this being pointed out (between April 2002 and February 2003), the Ministry stated (December 2003) that deemed credit scheme was introduced to complete the Modvat chain and in no way provided credit where no duty incidence had been suffered on the inputs. It was further stated that this issue had recently been taken up in litigation and the CEGAT, New Delhi had held (November 2002) that the assessee was entitled to deemed credit.

Reply of the Ministry does not address the points raised in audit.

4.5.2 By notifications dated 1 March 2001 and 29 June 2001 issued under rule 11 of the Cenvat Credit Rules (erstwhile rule 57G(2) of the Central Excise Rules), deemed credit to fabric processors from 25 per cent to 50 per cent of duty paid on final product has been allowed. Yarn, dyes, chemicals, consumables and packing material were declared inputs in these notifications. Grey fabrics have not been declared as eligible inputs in these notifications.

While interpreting rule 57G(2), the Tribunal in the case of M/s. Machine Builders {1996 (83) ELT 576} held that 'the intention is not to deem that the inputs which actually did not suffer duty are inputs which suffered duty. The purpose is to ensure the benefit to those who use inputs in the manufacture of which, duty has actually been paid, but it might not be possible to produce duty paying documents'.

Test check of records of 16 assessees in Chandigarh I & II and Jaipur II Commissionerates of Central Excise, engaged in the manufacture of processed fabrics revealed that the assessees purchased and used grey fabric which was exempt from duty. Deemed credit of basic excise duty of Rs.24.95 crore between March 2001 to November 2002 was availed and utilized despite the exclusion of grey fabrics as an eligible input. Hence, allowing of deemed credit in these cases was not correct.

On this being pointed out (between April 2002 and February 2003), the Ministry stated (December 2003) that deemed credit was admissible even though the declared inputs were not directly used by the manufacturers of declared final products. It was introduced to complete the Modvat chain and in no way provided credit where no duty incidence had been suffered on the inputs. As such Tribunal's ruling in M/s. Machine Builders case had no bearing on this matter. It was further stated that this issue had recently been taken up in litigation and Tribunal New Delhi had held (November 2002) that the assessee was entitled to deemed credit.

Reply of the Ministry is not tenable as the declared inputs were not procured by the assessee. The question of direct or indirect use of declared inputs would not arise. The ratio of the Tribunal's judgement is also relevant as it relates to the allowance of deemed credit on inputs which did not suffer duty. The purpose of deemed credit would be to reimburse the duty paid on inputs, and the amount of deemed credit allowed has far exceeded the amount of duty paid on the minor inputs.

CHAPTER V : GRANT OF MODVAT/CENVAT CREDIT

Under Modvat/Cenvat scheme, credit is allowed for duty paid on 'specified inputs' and 'specified capital goods' used in manufacture of finished goods. The credit can be utilised towards payment of duty on finished goods subject to the fulfilment of certain conditions. Some cases of incorrect availment of Modvat/Cenvat credit, noticed in test audit are elucidated in the following paragraphs :-

5.1 Incorrect availing of credit on inputs not involving purchase and sale

Rule 57AE(3) of the Central Excise Rules, 1944, prescribes that the manufacturer of final products shall maintain proper records for the receipt, disposal, consumption and inventory of the inputs and capital goods in which the relevant information regarding the value, duty paid, the person from whom the inputs or capital goods have been purchased is recorded. The burden of proof regarding the admissibility of the Cenvat credit shall lie upon the manufacturer taking such credit. Similar provision has also been made in rule 7(4) of the Cenvat Credit Rules, 2001 effective from 1 July 2001. The Ministry of Finance (the Ministry) circular dated 3 April 2000 also clarified that the basic responsibility lies upon the manufacturer to prove that inputs or capital goods were purchased and used by him for the intended purpose.

Eighteen assessees, in Bolpur, Kolkata I, II, III and IV Commissionerates of Central Excise, manufacturing excisable goods got inputs from their sister units on stock transfer basis. The invoices indicated that the goods sent were not a sale and the valuation of such inputs by the sender unit was made under rule 8 of the Valuation Rules, 2000. Sales tax was not paid on such goods as the transaction was not a sale. Since the assessee did not purchase the inputs, the availment of Cenvat credit of Rs.114.65 crore from 1 April 2000 to 27 December 2001 was not correct.

On this being pointed out (October 2000/February 2002), the Ministry stated (January 2003) that Cenvat credit was admissible as stock transfer of such inputs satisfied the definition of sale and purchase under section 2(h) of the Central Excise Act, 1944 and that rule 57AE (3) only clarifies maintenance of records and does not impose a condition regarding admissibility of credit on purchase of inputs by the manufacturer. The Ministry further stated (December 2003) that transaction between sister units are treated as separate entities.

Reply of the Ministry is not tenable since stock transfer does not satisfy the definition of 'sale and purchase' under section 2(h). Transfer of the possession of goods from one person to another was not involved as both parties belonged to the same company. The contention that rule 57AE(3) is only a clarification is also not correct as each rule is a separate entity and has to be followed mandatorily. The Supreme Court in case of A.N. Sehgal Vs. Raje Ram Sheoram (AIR 1991 SC 1406} held that effect should be given to both provisions of an enactment which cannot be reconciled with each other. The Ministry remained silent on its own circular dated 3 April 2000 where it was clarified that the basic responsibility is upon the manufacturer to prove that inputs or capital goods were purchased and used for the intended purpose. Moreover, rule 57AE(3) has been amended by a notification dated 1 March 2003 in which the word 'purchased' in rule 7 (4) (identical to rule 57AE (3)) of

Cenvat Credit Rules, 2001 has been substituted by the word 'procured' prospectively. This lends credence to the stand taken by Audit. Hence, credit availed was recoverable for the period before 1 March 2003.

5.2 Simultaneous availing of Cenvat/Modvat credit on capital goods and depreciation under Income Tax Act.

5.2.1 Rule 4(4) of the Cenvat Credit Rules, 2002, prescribes that credit in respect of capital goods shall not be allowed in respect of that part of the value of capital goods which represents the amount of duty on such capital goods, which the manufacturer claims as depreciation under section 32 of the Income Tax Act, 1961.

M/s. Numaligarh Refinery Limited, in Shillong Commissionerate of Central Excise, availed Cenvat credit of Rs.51.67 crore between June and August 2002, The balance sheets as on 31 March 2001 and 2002 and other records disclosed that fixed assets were exhibited at their cost inclusive of duty. The company was paying minimum alternative tax (i.e. income tax) on the basis of its book profit which was arrived at after charging depreciation on capital goods. As depreciation was charged on the capitalized value of capital goods which was inclusive of duty of excise, availment of credit was incorrect.

On this being pointed out (November 2002), the Ministry admitted the objection (December 2003).

5.2.2 Under rule 57R(8) of the Central Excise Rules, 1944, as effective before 1 April 2000, no credit of specified duty paid on capital goods was allowed if a manufacturer claims depreciation under section 32 of the Income Tax Act, 1961 or as revenue expenditure under any other provisions of the said Income Tax Act, in respect of that part of the value of capital goods which represents the amount of specified duty paid on such capital goods.

M/s. Honda Siel Cars India Limited, in Noida Commissionerate of Central Excise, availed of and utilized Modvat credit of Rs.14.79 crore on capital goods during 1998-99 and 1999-2000. The Annual Report of 1999-2000 revealed that the assessee claimed a revenue expenditure of Rs.354.33 crore during 1998-99 and 1999-2000 in the profit and loss account for the year ended March 2000 which included the amount of Modvat credit taken on capital goods. Availing Modvat credit of Rs.14.79 crore was, therefore, incorrect. Further, as the assessee had suppressed the facts, he was liable to pay penalty of Rs.14.79 crore and interest of Rs.10.72 crore upto January 2003 under rule 57U in addition to duty of Rs.14.79 crore.

On this being pointed out (July 2001 and August 2002), the Ministry while admitting the objection in principle stated (October 2003) that demand of Rs.14.79 crore had been confirmed and penalty of Rs.14.79 crore imposed in January 2003.

5.3 Short levy or non levy of duty on removal of inputs as such

Rule 57AB of the Central Excise Rules, 1944, and rule 3 of the Cenvat Credit Rules, 2001, prescribes that when inputs or capital goods, on which Cenvat credit has been taken, are removed as such from the factory, the manufacturer of the final products shall pay an amount equal to the duty of excise which is leviable on such goods at the rate applicable to such goods on the date of such removal and on the value determined for such goods under section 4 of the Act.

5.3.1 M/s. Ispat Industries Limited and M/s. Ispat Metallics India Limited, in Raigad Commissionerate of Central Excise, cleared inputs on which Cenvat credit was availed on payment of duty. Scrutiny of financial records revealed that the value shown in the excise invoices for payment of duty of excise was lesser than the value actually realised from the buyer. This resulted in short payment of duty of Rs.7.43 crore during the period 1 April 2000 to 30 September 2002.

On this being pointed out (November 2002), the Ministry while admitting the objection intimated (December 2003) that show cause notices demanding duty of Rs.13.67 crore along with interest and for imposition of penalty had been issued.

5.3.2 M/s. Ispat Metallics India Limited and M/s. Ispat Industries Limited, in Raigad Commissionerate of Central Excise, bought iron ore pellets (input) and availed Cenvat credit on them. Thereafter, in March and July 2001, the iron ore pellets were cleared without payment of duty. This resulted in non levy of duty of Rs.69.48 lakh.

On this being pointed out (October 2002), the Ministry admitted the objection (December 2003)

5.4. Modvat/Cenvat credit availed but duty not paid on final goods

Under rule 57CC of the Central Excise Rules, 1944, where a manufacturer is engaged in the manufacture of any final product which is chargeable to duty as well as any other final product which is exempt or is chargeable to 'nil' rate of duty and the manufacturer takes credit of specified duty on any input for the manufacture of both categories of final products without maintaining separate account, the manufacturer shall pay an amount equal to 8 per cent of price of second category of final product charged by the manufacturer for the sale of such goods, at the time of clearance from the factory.

5.4.1 M/s Jayaswals Neco Limited and M/s. Chhattisgarh Electricity Company Limited, in Raipur Commissionerate of Central Excise, engaged in the manufacture of pig iron and ferro alloy also produced electricity which was partly used in the production of final products and partly sold outside the factory to Madhya Pradesh Electricity Board, M/s Monnet Ispat Limited and M/s. Raipur Alloys and Steel Limited, Raipur. The assessees had availed of credit on inputs such as furnace oil, caustic soda, hydrochloric acid, clean flo etc. for generation of electricity (non excisable). Modvat/Cenvat credit so availed was utilised for payment of duty on final products. No separate accounts of inputs used in the generation of electricity cleared for sale were maintained. Electricity valuing Rs.52.26 crore between January 1998 to April 2003 was sold on which an amount of Rs.4.18 crore being 8 per cent of the price of electricity was recoverable.

On this being pointed out (between December 2000 and July 2003), the Ministry stated (November 2003) that electricity being non-excisable, the provisions of rule 57CC/57AD(2) were not applicable for recovery of 8 per cent. However, reversal of credit of Rs.3.73 lakh on inputs used in manufacture of electricity sold was intimated. In case of M/s. Jaiswal Neco Limited, it stated that the assessee did not claim Cenvat credit on disputed inputs since January 2002.

Reply of the Ministry is not tenable as no separate records were maintained for use of inputs in manufacture of dutiable and non-dutiable goods, and hence 8 per cent of the value of non-

dutiable final products was recoverable under the Cenvat Credit Rules. Further the rules do not provide for reversal of Cenvat credit on proportionate basis in such a situation. Verification of ER1 of December 2002 and March 2003 of the assessee also revealed that the Cenvat credit was availed on disputed inputs even after January 2002.

5.4.2 M/s. Crompton Greaves Limited, in Mumbai IV Commissionerate of Central Excise, manufactured electric motors and power driven pumps (exempted goods) using common inputs. No separate inventory was maintained for inputs used in their manufacture. The assessee cleared power driven pumps valuing Rs.19.35 crore without payment of duty during the period from April 2000 to March 2001. The assessee paid an amount of Rs.37.40 lakh only instead of Rs.1.55 crore (being 8 per cent of the price of power driven pumps) required to be paid. The amount of Rs.1.17 crore short paid was therefore recoverable.

On this being pointed out (June 2001), the Ministry accepted the objection (August 2003).

5.4.3 M/s. Indian Iron and Steel Company Limited, Burnpur, in Bolpur Commissionerate of Central Excise, manufactured raw coal gas by destructive distillation process and then sent the same to its purification unit within the premises for purification and manufacture of coal gas. A portion of pure coal gas (sub-heading 2705.00) was used within the factory as fuel for manufacture of final products and another portion was cleared outside the factory without payment of duty. The assessee used common inputs like sulphuric acid, wash oil etc. and did not maintain any separate accounts of inputs for such exempted category of excisable goods. The Modvat credit on inputs so availed was utilised towards the payment of other dutiable products. Therefore an amount equivalent to eight per cent of the value of such exempted final products was required to be paid. This resulted in non-payment of Rs.54.46 lakh for the period from August 1996 to March 2000.

On this being pointed out (January 2000), the Ministry admitted the objection (October 2003).

5.4.4 M/s. A.P. Paper Mills Limited, Rajahmundry, in Visakhapatnam II Commissionerate of Central Excise, engaged in the manufacture of both dutiable and exempted paper products, availed Cenvat credit on certain common inputs. No separate accounts were maintained for the inputs used in the exempted final products. The assessee cleared exempted goods valuing Rs.7.48 crore from July 2000 to January 2001, but did not pay an amount of Rs.59.81 lakh which was payable.

On this being pointed out (March 2001), the Ministry admitted the objection and intimated (October 2003) confirmation of demand of Rs.2.57 crore in July 2003.

5.4.5 M/s. Maize Products, in Ahmedabad II Commissionerate of Central Excise, manufactured and cleared maize starch, sorbitol and modified starches on payment of duty and byproducts (maize gluton, wet bran, corn S liquid etc.) at nil rate of duty. Separate inventory of common inputs, used in the above two streams of manufacture, was not maintained. Therefore the amount of Rs.2.30 crore was recoverable on products cleared at nil rate of duty during the period from April 2000 to June 2001 since byproduct was a final product as per rule 57AA(C) of Central Excise Rules, 1944.

On this being pointed out (February 2002), the Ministry admitted the objection and intimated (December 2003) that six show cause notices demanding duty of Rs.5.12 crore for the period from April 2000 to December 2002 had been issued.

5.5 Incorrect availing of Cenvat credit on inputs used in exempted final products

Rules 57C and 57AD(1) of the Central Excise Rules, 1944, prescribe that Modvat/Cenvat credit shall not be allowed on such quantity of inputs which are used in the manufacture of exempted goods.

5.5.1 M/s. Gujarat Narmada Valley Fertilisers Company Limited, in Vadodara II Commissionerate of Central Excise, availed Cenvat credit on Low Sulphur Heavy Stock (LSHS) used for generation of steam. Though a part quantity of steam so generated was sold outside the factory without payment of duty, the assessee did not reverse the credit attributable to the quantity of LSHS used as inputs in the manufacture of steam cleared outside the factory.

On this being pointed out (April 2002), the Department admitted the objection and stated (October 2002) that a show cause notice for Rs.3.45 crore from 27 September 1997 to 31 March 2002 had been issued (September 2002).

The Ministry admitted the objection (November 2003).

5.5.2 M/s. Ispat Industries Limited, in Raigad Commissionerate of Central Excise, availed Cenvat credit on iron ore pellets which was used in the manufacture of iron oxide fines. Since iron oxide fines (heading 26.01) were cleared without payment of duty during the period from April 2000 to March 2001, availment of credit of Rs.1.01 crore was not correct.

On this being pointed out (November 2002), the Ministry stated (December 2003) that the matter was being examined and steps taken to safeguard the interest of revenue.

5.5.3 M/s Chhattisgarh Electricity Company Limited, in Raipur Commissionerate of Central Excise, engaged in the manufacture of ferro alloy and electricity, availed Cenvat credit of Rs.75.10 lakh on inputs during the period June 2000 to May 2001. These inputs were used in the manufacture of electrostatic precipitators, raw material handling plant, copper tube and pipes which were consumed captively without payment of duty, availing exemption under notification dated 16 March 1995. As no duty was paid on the goods captively consumed, Cenvat credit availed thereon was not correct.

On this being pointed out (June 2003), the Ministry stated (November 2003) that the credit availed of was correct as inputs were used in the manufacture of capital goods which were further used in the factory of the manufacturer.

Reply of the Ministry is not tenable as the final goods manufactured from inputs did not suffer any duty and Cenvat credit availed on such inputs was not permissible under rule 57AD.

5.5.4 M/s. Aurobindo Pharma Limited, Unit IV, in Hyderabad I Commissionerate of Central Excise, engaged in the manufacture of bulk drugs, availed of Cenvat credit on selinium metal powder, ethylene diamine and propylene glycol which was exclusively used in the manufacture of pyrazynamide, an exempted product. Assessee paid eight per cent of the value of the said product under rule 57AD (2). This was not correct as the above rule is attracted only if the inputs are used in the manufacture of exempted and dutiable goods. The

entire credit of Rs.67.03 lakh availed on these inputs during the period between June 2001 and April 2002 required recovery.

On this being pointed out (April 2002), the Ministry while admitting objection stated (October 2003) that a show cause notice demanding Rs.67.03 lakh had been issued besides demanding interest and proposing imposition of penalty.

5.6 Cenvat credit not reversed on raw materials written off

The Board clarified in February 1995 that where Modvat credit is availed on inputs, but later on inputs are not used in the manufacture and its value is written off from stock accounts for any reason, the Modvat credit should be reversed. The Board further clarified on 16 July 2002 that credit of duty availed on inputs is to be reversed only in cases where unused inputs are fully written off.

5.6.1 M/s. Electronics Corporation of India Limited, in Hyderabad III Commissionerate of Central Excise, availed Cenvat credit on different inputs received in their factory. Verification of their annual accounts revealed that during the year 2000-01, the assessee had written off full value of some of the raw materials and components declaring them as obsolete. The value of such materials written off amounted to Rs.10.55 crore. The corresponding credit of duty of Rs.1.69 crore on such inputs was however, not paid back.

On this being pointed out (May 2002), the Ministry stated (November 2003) that only the value of inputs was reduced and the quantity of inputs was not written off from the records for which provisions to restrict credit did not exist in the rules.

Reply of the Ministry is not tenable as the assessee had written off obsolete stores from materials stock account (Schedule N-2) for the year 2000-01 and hence those goods ceased to be inputs for availing credit under rule 57A.

5.6.2 M/s. Hindustan Petroleum Corporation Limited, in Mumbai II Commissionerate of Central Excise, engaged in the manufacture of petroleum products, had written off stores and spares, on which Cenvat credit was taken, valued at Rs.2.49 crore and Rs.5.12 crore during the years 2000-01 and 2001-02 respectively. Cenvat credit on these written off inputs was not reversed. Considering the credit amount as 8 per cent of value of inputs, the amount to be reversed worked out to Rs.60.88 lakh approximately.

On this being pointed out (June 2002), the Ministry stated (December 2003) that the spares were usable and write off in respect of these goods was done as an accounting entry to spread the cost of spares over a period.

Reply of the Ministry is not tenable as the value of inputs had been fully written off and hence credit was to be paid back as per Board's circular cited above irrespective of whether or not such inputs were capable of being used.

5.7 Non-reversal of credit on inputs found short

Rules 57A and 57F of the Central Excise Rules, 1944, provided that credit of specified duty paid on inputs was available to a manufacturer to the extent it was used in or in relation to the manufacture of final products.

5.7.1 M/s. Mahindra and Mahindra Limited, in Mumbai V Commissionerate of Central Excise, engaged in the manufacture of motor vehicles, noticed shortage of inputs worth Rs.50.80 lakh at the time of stock taking for the year ended March 2000. As Modvat credit had been availed, credit was required to be reversed since the inputs were not used in the manufacture of final products.

On this being pointed out (March 2001), the Department stated (July 2003) that a show cause notice demanding duty of Rs.1.53 crore was issued on 31 March 2003 of which Rs.1.38 crore had been recovered. Department further stated that the point was under consideration and it could not have remained unnoticed.

Reply of the Department is not tenable as the stock taking for the year 1999-2000 was completed in March 2000 and show cause notice issued only in March 2003 which indicated that action was initiated after pointing out in audit.

The Ministry admitted the objection in principle (November 2003).

5.7.2 M/s. Philips Carbon Black Limited, Durgapur, in Bolpur Commissionerate of Central Excise, imported carbon black feed stock as the main input for manufacture of carbon black and availed of Modvat credit. Records of daily receipt and consumption of such inputs disclosed that the said materials were stored in the storage tank and at the end of every month actual quantity of stock in hand was ascertained physically by dip measurement of tanks. The shortage so found in stock was adjusted by reducing the book balance. Since the materials found short were not used in the final products, corresponding Modvat/Cenvat credit of Rs.98.59 lakh for the period from April 1999 to October 2001 ought to have been reversed.

On this being pointed out (January 2002), the Ministry admitted the objection and intimated (December 2003) that show cause notices demanding Cenvat credit of Rs.1.09 crore from April 1999 to January 2003 had been issued.

5.7.3 Physical verification of stores of M/s. Bharat Heavy Electrical Limited, in Hyderabad I Commissionerate of Central Excise, revealed shortage of stock of stores (inputs) of 324 spares and component items pertaining to the years 1991-92 to 2000-01 on which Modvat/Cenvat was availed of by them. The corresponding Modvat/Cenvat credit amounting to Rs.50.10 lakh relating to the said shortages was not, reversed by the assessee.

On this being pointed out (January 2003), the Department accepted the objection and stated (May 2003) that a show cause notice was being issued.

The Ministry stated (October 2003) that audit had taken into account only shortages and surplus had been ignored. It was further stated that there was shortage of filter assembly during the year 1990-91 and the same was in excess in the year 1997-98. During the process of reconciliation, the said shortages had been set off.

Reply of the Ministry is not tenable as such a set off is not allowed under the rules.

5.8 Incorrect availing of credit on the basis of improper duty paying document

Under notification issued in August 1997, deemed credit at the rate of 12 per cent of the invoice price of re-rolled products on which duty had been paid under section 3A was

allowed to the manufacturer provided the said re-rolled products were received directly from their manufacturer.

M/s. K.E.C. International Limited, Butibori, in Nagpur Commissionerate of Central Excise, availed credit on M.S. angles received from M/s. Sunrise Structurals and Engineering Limited, Nagpur. These M.S. angles had been originally purchased from hot re-rollers who cleared the products under section 3A. M/s. Sunrise Structurals & Engineering Limited availed deemed credit and sold the M.S. angles to the assessee without mentioning clearance of 'input as such' on the invoice and paid excise duty at the rate of 16 per cent. This facilitated the assessee in availing Modvat credit of Rs.1.48 crore from May 1998 to January 2000, which was not admissible as the assessee had not purchased the inputs from the original manufacturer.

On this being pointed out (February 2000), the Ministry admitted the objection and intimated (October 2003) that demand of Rs.5.12 crore had been confirmed in July 2002 and penalties equal to duty were also imposed on both the parties. On appeal, the Tribunal had granted stay.

5.9 Utilisation of Cenvat credit more than the balance available

Under rule 57AB of the Central Excise Rules, 1944 read with notification dated 18 August 2000, while paying duty, the Cenvat credit shall be utilized only to the extent such credit is available on the fifteenth day of a month for payment of duty relating to the first fortnight of the month, and the last day of the month for payment of duty relating to the second fortnight of the month.

M/s.Kirpa Industries, Pithampur, M/s. Hotline Teletube and Components Limited and M/s.Hotline Glass Limited, Malanpur, in Indore Commissionerate of Central Excise, engaged in the manufacture of various excisable goods paid duty on finished goods from Cenvat credit account more than the balance available on the fifteenth and last day of the month during the period from August 2000 to February 2001. This resulted in excess utilisation of credit of Rs.63.37 lakh which tantamounts to clearance of goods without payment of duty.

On this being pointed out (May and June 2001), the Ministry while admitting the objection intimated (December 2003) recovery of Rs.11.23 lakh from M/s. Kripa Industries between September and December 2001 and confirmation of demand of Rs.54.25 lakh against M/s. Hotline Teletube and M/s. Hotline Glass Limited.

5.10 Availing of Cenvat credit of non specified duty

Cenvat credit is admissible on duties specified in rule 3 of the Cenvat Credit Rules, 2001.

M/s. Mandovi Pellets Limited, in Goa Commissionerate of Central Excise, availed Cenvat credit of Rs.54.45 lakh on iron oxide fines received from M/s. Ispat Industries Limited during the period from October 2001 to June 2002. Availing of credit was not correct because iron oxide fines were exempt from duty and M/s. Ispat Industries Limited had paid the amount of eight per cent under rule 6 of the Cenvat Credit Rules since common inputs were used for manufacture of dutiable as well as non-dutiable final goods. Payment of eight per cent did not represent duty, and hence availing of credit was not correct.

On this being pointed out (January 2003), the Ministry stated (November 2003) that M/s. Ispat Industries Limited had cleared the broken iron ore pellets on payment of appropriate duty.

Reply of the Ministry is not tenable as the relevant invoices clearly indicated that M/s. Ispat Industries had cleared iron oxide fines.

5.11 Incorrect availing of Cenvat credit on capital goods before use

Rules 57AC and 4(2)(a) and (b) of the Cenvat Credit Rules provide that Cenvat credit on capital goods received in a factory during a financial year shall be taken only for an amount not exceeding fifty per cent of the duty paid on such capital goods in the same financial year. The balance fifty per cent credit may be taken in subsequent financial years provided the capital goods are still in possession and use of the manufacturer of final products in such subsequent years. The Ministry clarified on 5 May 2000 that balance credit may be taken in a subsequent financial year subject to the capital goods still being in the use and possession of the assessee.

5.11.1 In M/s. National Aluminium Company Limited, (refinery division and smelter plant) in Bhubaneswar I Commissionerate of Central Excise, it was revealed that the assessee availed balance fifty per cent Cenvat credit of Rs.36.56 crore in April 2002 on capital goods received during 2001-02 for expansion programme out of which Rs.21.02 crore was utilized by them (by June 2002 and August 2002) before installation and actual use of the said capital goods which were either lying in the central store, or with the co-ordinator of expansion programmes. Expansion programme was yet to be completed and production thereof not started. The availing of balance Cenvat credit and utilisation thereof was incorrect.

On this being pointed out (June 2002), the Ministry admitted the objection (December 2003).

5.11.2 M/s. Kalyani Brakes Limited and M/s. Ispat Industries Limited, in Aurangabad and Raigad Commissionerates of Central Excise, availed balance 50 per cent of Cenvat credit amounting to Rs.15.87 crore during April 2001 and utilized the same even though the said capital goods were not put to use. This resulted in incorrect availment of Cenvat credit amounting to Rs.15.87 crore.

On this being pointed out (November 2002), the Ministry stated (October 2003) that installation or use of the capital goods was not a precondition for taking Cenvat credit.

Reply of the Ministry is not tenable in view of specific inclusion of the phrase, 'possession and use of' capital goods in rule 57AC ibid and Ministry's own clarification of 5 May 2000.

5.11.3 M/s. Indian Oil Corporation Limited, Haldia, in Kolkata II Commissionerate of Central Excise, availed of fifty per cent Cenvat credit of Rs.5.87 crore during 2001-02 and balance Rs.5.87 crore in April 2002 and thereupon utilized the same. Audit scrutiny revealed that the new plant was still under construction and was not commissioned/installed to make it operational till May 2002. Availment/utilisation of credit of Rs.5.87 crore was incorrect.

On this being pointed out (July 2002), the Ministry stated (October 2003) that installation or use of the capital goods was not a precondition for taking Cenvat credit.

Reply of the Ministry is not tenable in view of specific inclusion of the phrase 'possession and use of' capital goods in rule 57AC ibid and Ministry's own clarification of 5 May 2000.

5.12 Excess availing of Modvat credit on capital goods

5.12.1 Rule 57Q(3) of the Central Excise Rules, 1944, as it stood before 1 April 2000, allowed credit of additional duty leviable under section 3 of the Customs Tariff Act, 1975, on goods falling under heading 98.01 of the Customs Tariff, to the extent of 75 per cent of the said additional duty paid on such goods.

M/s. Tata Iron and Steel Company Limited, in Jamshedpur Commissionerate of Central Excise, received capital goods in 1999 falling under heading 98.01 of the Customs Tariff. The assessee availed full Modvat credit of Rs.6.56 crore on such capital goods in two spells i.e. 50 per cent in April 2000 and balance in April 2001 instead of 75 per cent of duty paid. This resulted in excess availment of credit of Rs.1.64 crore.

On this being pointed out (August 2001), the Ministry admitted the objection and intimated (October 2003) recovery of Rs.5.02 crore including interest.

5.12.2 M/s. Tamil Nadu Petro Products Limited, Manali, in Chennai I Commissionerate of Central Excise, availed (May 2002) Cenvat credit of Rs.3.13 crore being 50 per cent balance credit pertaining to capital goods received during the period 2001-02. While reckoning the credit of Rs.3.13 crore, the assessee incorrectly included an amount of Rs.75.03 lakh being the 50 per cent balance credit already availed (January 2002) pertaining to the period 2000-01. This resulted in excess availment of credit of Rs.75.03 lakh.

On this being pointed out (November 2002), the Ministry admitted the objection and intimated (July 2003) recovery of duty of Rs.75.03 lakh and interest of Rs.5.09 lakh in November 2002.

5.13 Other cases

In 593 other cases of grant of Modvat/Cenvat credit, the Ministry/the Department had accepted objections involving duty of Rs.17.84 crore and reported recovery of Rs.8.33 crore in 536 cases till February 2004.

CHAPTER VI : EXEMPTIONS

Under section 5A(1) of the Central Excise Act, 1944, government is empowered to exempt excisable goods from the whole or any part of the duty leviable thereon either absolutely or subject to such conditions as may be specified in the notification granting the exemption. Some of the major cases of incorrect allowance of exemption noticed in audit are detailed in the following paragraphs:

6.1 Incorrect grant of exemption on goods manufactured on job work

By notification dated 25 March 1986, as amended, specified goods manufactured in the factory on job work basis and used in relation to the manufacture of final products falling under Central Excise Tariff, are exempt from the whole of the duty leviable thereon. Electricity does not fall under Central Excise Tariff. However, rule 2 of the Cenvat Credit Rules, provides Cenvat credit facility to inputs used for generation of electricity which in turn is used for manufacture of final products, within the factory of production.

M/s. Haldia Petrochemicals Limited, in Kolkata II Commissionerate of Central Excise, manufactured naptha returned stream/pyrolysis gas, C6 raffinate, cyclopentane and cleared them outside the factory without payment of duty for generation of electricity on job work basis, and a major portion of such electricity was returned to the assessee who used the same in the manufacture of final products. Clearance of goods without payment of duty was not correct as electricity was not specified as excisable good in the Tariff. This resulted in evasion of duty of Rs.21.89 crore from November 2000 to October 2002.

On this being pointed out (November 2002), the Ministry admitted the objection (December 2003).

6.2 Incorrect grant of exemption on intermediate goods

6.2.1 By notification dated 2 June 1998 as amended on 1 March 2000, processed tyre cord fabrics (heading 59.02) are exempted from additional duty under Additional Duties of Excise (Goods of Special Importance) Act, 1957, if manufactured out of unprocessed tyre cord fabrics on which the appropriate duty or as the case may be, the additional duty leviable under the Customs Tariff act, 1975 has already been paid.

Test check of records of M/s. Birla Tyres, in Bhubaneswar I Commissionerate of Central Excise, revealed that the assessee purchased grey (unprocessed) tyre cord fabrics (TCF) which were dipped in a chemical to produce dipped (processed) tyre cord fabrics. This dipped TCF was being cleared for rubberisation without payment of duty under notifications dated 16 March 1995 and 2 June 1998 as it was manufactured from unprocessed tyre cord fabric. Later on, the dipped TCF was coated with rubber on a calendering machine to produce rubberised tyre cord fabrics, which was again being cleared for manufacture of tyres without payment of excise duty as well as additional excise duty. Since the rubberised (processed) tyre cord fabric was produced from dipped (processed) tyre cord fabric, exemption under notification dated 2 June 1998 was not available. This resulted in non-levy of duty of Rs.14.33 crore during the period from April 2000 to November 2002.

On this being pointed out (January 2003), the Ministry stated (December 2003) that the assessments were provisional in view of the fact that the department had filed appeals against the Tribunal's decisions with regard to the classification of rubberised tyre cord fabrics under heading 59.05.

6.2.2 By notification dated 16 March 1995, specified excisable goods manufactured in a factory and used within the factory for the manufacture of final products are exempt provided that the final products are not exempt from whole of the duty or chargeable to nil rate of duty.

M/s. Niphad SSK Limited, in Nasik Commissionerate of Central Excise, manufactured and cleared 8320.27 tonne of molasses for captive consumption without payment of duty during the period from March 2002 to January 2003 for manufacture of ethyl alcohol (sub-heading 2204.90) which was chargeable to nil rate of duty. Since the final product was chargeable to nil rate of duty, exemption from duty on molasses was not applicable. This resulted in incorrect availment of exemption of Rs.51.90 lakh.

On this being pointed out (January 2003), the Ministry admitted the objection (November 2003).

6.3 Incorrect grant of exemption on final products

6.3.1 By notification dated 1 March 2000, excisable goods specified in chapters 72 and 73 which are manufactured in and cleared from an integrated steel plant and are intended to be sold at a place other than the said integrated steel plant are exempt from so much of the duty of excise leviable thereon under the Central Excise Act, 1944, as is in excess of the duty leviable on such goods as if they were sold and delivered to a buyer in the course of whole sale trade at the integrated steel plant. Explanation in this notification states that "integrated steel plant means a manufacturer or a producer who starting from the stage of iron ore, manufactures or produces within the same premises the excisable goods specified in chapter 72 or chapter 73".

M/s Monnet Ispat Limited, Raipur, in Raipur Commissionerate of Central Excise, manufactured M.S. ingots using 14000 tonne pig iron, 1000 tonne M.S. scrap, 4800 tonne of C.I. scrap/skull, 29 tonne of sponge iron and 1200 tonne of ferro alloys. These input materials were purchased from the market. The final product was cleared to the depots on payment of duty on assessable value which excluded the freight charges from factory gate to the depots under notification dated 1 March 2000. Exclusion of the freight charges was not correct since the final product was not manufactured starting from the stage of iron ore within the same premises. Moreover, the assessee did not have a plant to produce pig iron. Thus, availing of exemption of Rs.54.43 lakh between the period January 2001 and October 2002 was incorrect.

On this being pointed out (December 2002), the Ministry admitted the objection in principle (December 2003).

6.3.2 By notifications dated 7 May 1997 and 16 March 1995 (as amended), goods supplied as stores for consumption on board a vessel of the Indian Navy are exempt from payment of the whole of the duty leviable thereon.

The Tribunal in the case of M/s. Moosa Haji Patrawala Private Limited {1999 (114) ELT 620} held that if the goods are not supplied as stores for consumption on board a vessel directly to the Indian Navy, then the benefit of exemption is not applicable on such goods. The Supreme Court also upheld the judgement on 3 March 2000.

M/s. Nicco Corporation Limited, 24 Parganas, in Kolkata III Commissionerate of Central Excise, manufactured 'insulated wires and cables' and cleared the goods without payment of duty availing exemption under the aforesaid notification. Test check of records revealed that these goods were not supplied to the Indian Navy for consumption as stores on board a vessel but were cleared to ship builders like M/s Garden Reach Ship Builders and Engineers Limited directly. Hence, exemption availed was incorrect. This resulted in short levy of duty of Rs.20.93 lakh between April 1999 and March 2002.

On this being pointed out (October 2002), the Ministry while admitting the objection stated (October 2003) that central excise duty involved was Rs.1.51 crore from April 1999 to March 2002 and the Department had initiated enquiry on September 2001.

The fact remains that no show cause notice has been issued to protect government revenue.

6.4 Incorrect grant of exemption of national calamity contingent duty

By section 136 of the Finance Act, 2001, as effective from 1 March 2001, a surcharge by way of duty of excise called the national calamity contingent duty (NCCD) has been levied on goods specified under heading 21.06 (pan masala) and heading 24.04 (other manufactured tobacco products).

Under notification dated 16 March 1995 and 11 August 1994, specified intermediate goods, if captively consumed in the manufacture of specified final products, are exempt from (i) duty of excise leviable under the Central Excise Tariff Act, 1985, and (ii) Additional Duty of Excise leviable under the Additional duties of Excise (Goods of Special Importance) Act, 1957.

Six assessees in Chandigarh I Commissionerate of Central Excise, manufactured 'additive mixture' viz., tobacco essence (heading 24.04) and 'unbranded pan masala' (heading 21.06) and used them captively in the manufacture of final product viz., zarda, gutka etc. and branded pan masala, without payment of duty, after availing exemption under notifications ibid. Since NCCD was not specified under the aforesaid notification, exemption availed was incorrect. This resulted in short levy of duty of Rs.7.76 crore during 1 March 2001 to 16 October 2002.

On this being pointed out (January 2002), the Ministry admitted the objection in principle (December 2003).

6.5 Incorrect grant of small scale industry exemption

Under notification dated 28 February 1993, specified goods are not eligible for exemption if they bear a brand name or trade name (registered or not) of another person, who himself is not eligible for grant of exemption, under the notification ibid.

M/s. Mehak Chemicals (P) Limited, in Chandigarh I Commissionerate of Central Excise, manufactured bleaching powder (heading 28.28) and cleared it by affixing brand name 'Shri

Ram' as per instructions from their customer. Since the brand name belonged to another person who was not eligible for grant of exemption, availment of exemption by the assessee was incorrect and resulted in short levy of Rs.18.30 lakh during the period from October 1996 to March 1998.

On this being pointed out (March 2001), the Ministry admitted the objection (November 2003).

6.6 Other cases

In 50 other cases of exemptions, the Ministry/the Department had accepted objections involving duty of Rs.53 lakh and reported recovery of Rs.22 lakh in 46 cases till February 2004.

CHAPTER VII : VALUATION OF EXCISABLE GOODS

Ad valorem rates of duty are charged on a wide range of excisable commodities. The valuation of such goods is governed by section 4 of the Central Excise Act, 1944, read with the Central Excise (Valuation) Rules, 1975 and Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000. The valuation of excisable goods introduced with effect from 14 May 1997 with reference to retail sale price is governed by section 4A. Some illustrative cases of short levy due to incorrect valuation pertaining to the period before 1 July 2000 or cases covered under section 4A are narrated in the following paragraphs :

7.1 Incorrect adoption of value cleared in multi piece packages

The Board clarified in November 1999 that multi piece packages containing individual pieces of less than 10 grams/10 ml by weight or measure would be assessed to duty under section 4A of the Central Excise Act, 1944, as the exemption contemplated in rule 34(b) of the Standards of Weight and Measures (Packaged Commodities) Rules, 1977 was applicable to a package containing a commodity and not to multi piece packages. Moreover, under rule 17 (1) of the Rules ibid, the assessee is statutorily required to declare the retail sale price of multi piece packages and individual pieces contained in such multi piece packages. The Board further clarified (October 2002) that if individual items were capable of being sold separately at the maximum retail price (MRP) printed on them, then the aggregate of MRP's of the items comprising the multi pack could be considered for the purpose of levy of duty under section 4A of the Central Excise Act, 1944.

M/s. Mul DentPro Limited and M/s. Alfa Packaging Silvassa, in Daman and Valsad Commissionerates of Central Excise, manufactured shampoo, ayush hair oil, fal cos, etc., and cleared them in multi piece packages containing pouches/strips/sachets each having less than 10 grams/10 ml by weight or measure. MRP was also printed on individual piece/pouch. Duty on these packages was paid on assessable value arrived at under section 4 instead of on the basis of MRP under section 4A. This resulted in short levy of duty of Rs.21.78 crore between April 2001 and October 2002.

On this being pointed out (November and December 2002), the Ministry of Finance (the Ministry) stated (January 2004) that the Board's clarifications of November 1999 and October 2002 would not be relevant as the products under reference were not statutorily required to be affixed with MRP.

Reply of the Ministry is not tenable as the products under reference were multi piece packages and were statutorily required to be affixed with the MRP under rule 17(1) of the Standards of Weight and Measures (Packaged Commodities) Rules, 1977 and exemption under rule 34 of these rules was not applicable to multi piece packages.

7.2 Incorrect valuation of goods cleared to sister concerns

Under section 4(1)(b) of the Central Excise Act, 1944, read with rule 6(b) of the Central Excise (Valuation) Rules, 1975, the assessable value of excisable goods consumed within the

factory of production or in any other factory of the same manufacturer had to be determined on the basis of cost data if value of comparable goods was not ascertainable.

7.2.1 M/s. Raymonds Limited, in Mumbai VI Commissionerate of Central Excise, engaged in the manufacture of 'woollen products' cleared goods to its sister concern during the period from April 1997 to June 2000. Scrutiny of records revealed that value adopted for payment of duty was less than the value arrived at on the basis of cost data for the relevant period. Non-adoption of correct value resulted in undervaluation of goods and consequent short levy of duty of Rs.3.41 crore during the period from April 1997 to June 2000.

On this being pointed out (May 2001), the Ministry admitted the objection (October 2003).

7.2.2 M/s. Hindustan Lever Limited, in Kolkata I Commissionerate of Central Excise, manufacturing soap noodles cleared some of its products to another unit of the assessee on payment of duty on the basis of cost of production since the value of comparable goods was not ascertainable. Scrutiny of the cost statement revealed that the assessee did not include elements like overhead expenses on actual basis, depreciation, interest as per annual accounts in the cost of production of such goods. Non-inclusion of these elements in the cost of production resulted in undervaluation with short levy of duty of Rs.1.86 crore during the period from November 1996 to December 1998.

On this being pointed out (June 2001), the Ministry admitted the objection and stated (October 2003) that the assessee voluntarily paid duty of Rs.5.06 crore for the years 1996 to 1998.

7.2.3 M/s. Shivaji Works Limited, a Kirloskar group company, in Pune II Commissionerate of Central Excise, engaged in the manufacture of C.I. castings (sub-heading 7325.10), cleared 16937.37 tonne of C.I. castings to M/s. Kirloskar Oil Engines Limited at a price lower than the assessable value arrived at on the basis of cost of production during the period from April 1998 to June 2000. As both the companies were related, the assessee was required to clear the goods adopting cost of production as the basis for valuation in the absence of a comparable price. This resulted in undervaluation of goods amounting to Rs.9.33 crore with short levy of duty of Rs.1.46 crore.

On this being pointed out (March 1999), the Ministry admitted the objection (September 2003).

7.3 Additional consideration not included in the value

Section 4(1)(a)of the Central Excise Act, 1944, read with rule 5 of the Central Excise (Valuation) Rules, 1975, prescribe that where the price charged for excisable goods sold in wholesale trade is not the sole consideration for the sale, the assessable value of such goods shall be determined based on the aggregate of the price and money value of additional consideration flowing directly or indirectly from the buyer to the assessee. In the case of Bombay Tyre International {1983 (14) ELT (1896)}, the Supreme Court held that the value of the article for the purpose of levy of excise duty shall include all costs and expenses which have given the article its marketability.

7.3.1 *Cost of bought out components*

The Tribunal in the case of M/s. Baroda Machinery Manufacturers held that cost of bought out items being an integral part of a final product is to be included in assessable value {1997 (91) ELT 88 CT}.

M/s. KEC International Limited, in Nagpur Commissionerate of Central Excise, fabricated galvanized steel parts with holes for tightening bolts and nuts as per approved design for erection of transmission line towers and cleared these parts on payment of duty under sub-heading 7308.90 to customer's site for erection of transmission line tower as per agreement. For erection of tower, assessee had bought out nuts and bolts from market and sent them directly to site. The value of nuts and bolts was not included in the assessable value for the purpose of determining duty. As nuts and bolts were an integral part of the tower, the value should have been included in the assessable value. This resulted in undervaluation with short levy of duty of Rs.72.69 lakh from April 1999 to March 2000.

On this being pointed out (November 2000 and January 2002), the Ministry stated (December 2003) that the value was not includible, since nuts and bolts were procured outside the factory and sent directly to site. It was further stated that the Supreme Court in case of M/s. Triveni Engineering and Industries held that, structures assembled and erected at site by rigid foundation which could not be dismantled without substantial damage to their components and could not be reassembled at any site after dismantling, were not excisable being immovable property.

Reply of the Ministry is not tenable as nuts and bolts are integral parts of the structure without which the tower cannot be erected. The Supreme Court judgement quoted by the Ministry is not applicable in this case as the towers can be erected at another site after dismantling with the help of nuts and bolts without substantial damage to the components. Therefore, towers do not become immovable property and fail the test of permanency, hence are excisable as per Supreme Court judgement in the case of M/s. Triveni Engineering {2000 (120) ELT 273 (SC)} and M/s. Sirpur Paper Mills Limited {1998 (97) ELT 3 (SC)}. It was noticed that the same assessee had included value of nuts and bolts in the assessable value of towers cleared from July 2000 onwards lending credence to the audit stand. Moreover, another assessee viz., M/s. Hundai Unitech Limited in the same Commissionerate had included the value of nuts and bolts in the assessable value of towers for payment of duty.

7.3.2 *Cost of packing materials*

Section 4(4)(d)(i) of the Central Excise Act, 1944, provides that where goods are delivered at the time of removal in a packed condition, the assessable value includes cost of such packing except the cost of packing, which is of durable nature and is returnable by the buyer to the assessee. The Tribunal in the case of M/s. Jauss Polymers Limited {2002 (132) ELT 675 (Trib – Del} held that cost of packing material supplied by the buyer is includible in the assessable value.

M/s. Pearl Polymers Limited, in Mumbai VII Commissionerate of Central Excise, engaged in the manufacture of plastic goods, had not included the cost of cartons supplied by the buyer while determining the assessable value. Non-inclusion of cost of packing material, resulted in short levy of duty of Rs.17.42 lakh from April 1998 to September 1999.

On this being pointed out (November 1999), the Ministry while admitting audit objection stated (October 2003) that the demand of Rs.48.77 lakh had been confirmed and penalties of Rs.49.77 lakh imposed under section 11AC and rule 173Q.

7.3.3 Research and development charges

M/s. Madhushilica Private Limited, in Bhavnagar Commissionerate of Central Excise, engaged in the manufacture of various grades of silica, had recovered an amount of Rs.3.33 crore towards research and development charges from various parties between April 1997 and March 2001. Although, these charges were recovered for the use of the Research and Development Centre run by the assessee for the development of various grades of silica, the same were not included in the assessable value. Omission to include this additional consideration resulted in short levy of duty of Rs.53.28 lakh.

On this being pointed out (February 2002), the Ministry admitted the objection (December 2003).

7.3.4 Escalation charges

M/s. Southern Structurals Limited, Chennai and M/s. Burn Standard Company Limited, Salem, in Chennai and Coimbatore Commissionerates of Central Excise, respectively manufactured railway wagons and refractory materials/bricks and cleared the goods to Railway Board and steel plants on payment of duty on contract value of the goods. The contract provided for reimbursement of escalation charges towards materials and wages. Accordingly the assessees were reimbursed Rs.1.69 crore and Rs.0.81 crore (respectively) by their customers towards escalation charges on account of revision of cost of raw materials and wages. These escalation charges were not included in the assessable value which resulted in short collection of duty of Rs.37.53 lakh between February 1998 and January 2000.

On this being pointed out (between February 2000 and October 2001), the Ministry admitted the objection in one case and intimated (November 2003) confirmation of demand of Rs.69.77 lakh with imposition of penalty of Rs.69.77 lakh on the assessee. In the second case it stated that provisional assessments were made and exact amount of differential duty would be known on finalisation.

7.4 Other cases

In 133 other cases of valuation of excisable goods, the Ministry/the Department had accepted objections involving duty of Rs.6.25 crore and reported recovery of Rs.4.04 crore in 116 cases till February 2004.

CHAPTER VIII : NON-LEVY OF DUTY

Rules 9 and 49 read with rule 173G of the Central Excise Rules, 1944, prescribe that excisable goods shall not be removed from the place of manufacture or storage unless the excise duty leviable thereon has been paid. If any manufacturer, producer or licencee of a warehouse, removes excisable goods in contravention of these rules or does not account for them, then besides such goods becoming liable for confiscation, a penalty not exceeding the duty on such excisable goods or ten thousand rupees, whichever is greater, is also leviable under rule 173Q. Similar provisions exists in rules 4 and 25 of the Central Excise Rules, 2002 which came into force from 1 March 2002 in place of Central Excise Rules, 1944. Some illustrative cases of non-levy of duty are given in the following paragraphs :

8.1 Non-levy of additional duty of excise

Section 3 of the Additional Duties of Excise (Textiles and Textile Articles) Act, 1978, levies additional excise duty at the rate of 15 per cent of the amount of basic excise duty chargeable. For the purpose of determining additional excise duty, the basic excise duty chargeable is to be calculated after excluding any exemption for giving credit or for reduction of duty already paid on raw material used in the production or manufacture of such goods.

M/s. Birla VXL Limited (OCM Woollen Mills), in Amritsar Commissionerate of Central Excise, manufactured woollen yarn, artificial synthetic fibre and synthetic fibres and used them captively in the manufacture of woollen fabrics without payment of basic excise duty by availing exemption under notifications dated 16 March 1995 and 23 July 1996. The assessee also did not pay additional excise duty, which was leviable by working out quantum of basic excise duty chargeable after excluding the benefit availed through the above exemption notifications. This resulted in non-levy of additional excise duty of Rs.7.89 crore for the period April 1997 to June 2002.

Similar objection was featured in para 6.3 (i) of Audit Report 1996-97. The Ministry of Finance (the Ministry) stated (February 1998) that notification dated 16 March 1995 did not belong to the excluded category. Reply of the Ministry was not tenable since these notifications provided exemption if duty was already paid on raw material used in the production of finished goods thereby nullifying the cascading effect of duties. Hence these would fall under excluded category. The Ministry was requested (November 1999) to obtain the opinion of the Ministry of Law. The Ministry reiterated (November 2003) its earlier stand without obtaining the opinion of the Ministry of Law.

8.2 Duty not levied on excisable goods found short or destroyed

Rule 49(1) of the Central Excise Rules, 1944, prescribes that a manufacturer shall, on demand, pay the duty leviable on any goods which are not shown to the satisfaction of the proper officer to have been lost or destroyed by natural cause or by unavoidable accident.

8.2.1 Scrutiny of central excise records of M/s Steel Authority of India Limited, Bhillai, in Raipur Commissionerate of Central Excise, revealed that shortage of wire rods of 28.927 tonne for the years 1998-1999 and 1999-2000 noticed by the assessee during physical

verification was adjusted in the month of April 2001 by reducing the balances in daily stock account (RG1) from 46215.724 tonne to 17288.724 tonne. Such a reduction in RG1 without payment of duty was in contravention of the rules and resulted in evasion of duty of Rs.5.55 crore.

On this being pointed out (January 2002), the Ministry stated (November 2003) that variation in stock between recorded quantity and on actual physical weighment in integrated steel plants was a common occurrence.

Reply of the Ministry is not tenable as such a reduction in production records by the assessee is not permissible under the rules.

8.2.2 M/s. Indian Iron and Steel Company, Burnpur, in Bolpur, Commissionerate of Central Excise, was permitted to account for the manufactured goods in their daily stock account (RG 1) register on the estimated weight of goods. On the other hand, the assessee used to maintain their clearances on the basis of actual weight. Due to adoption of two different models of weighment at two different stages, a wide variation occurred between the quantity of pig iron and semi flats recorded in the RG-1 register and the quantity finally cleared. Scrutiny of the report of annual stock verification for the year 1997-98 conducted jointly by the Department and the assessee revealed that the shortages were adjusted by reducing the closing balances of the products in the succeeding year 1998-99 without assigning any reason and without demanding any duty. This resulted in evasion of duty of Rs.1.73 crore.

On this being pointed out (August 2000), the Ministry while admitting the objection stated (August 2003) that two show cause cum demand notices for Rs.1.77 crore had been issued.

8.3 Non-levy of special excise duty

Special excise duty at the rate of 16 per cent ad valorem is leviable on all petroleum products falling under sub-heading 2710.19 with effect from 1 March 2002.

M/s. Haldia Petrochemicals Limited, Midnapore, in Haldia Commissionerate of Central Excise, manufacturing different excisable products cleared C6 raffinate under sub-heading 2710.19 without payment of special excise duty at the rate of 16 per cent ad valorem. This resulted in non-payment of duty of Rs.1.26 crore during the period from March to October 2002.

On this being pointed out (November 2002), the Ministry admitted the objection (October 2003).

8.4 Duty not levied on goods remade

Rule 173-H of the Central Excise Rules, 1944, states that an assessee may, subject to such conditions as may be specified by the Commissioner, retain in, or bring into, his factory or ware-house, excisable goods or parts thereof, accompanied by duty paying document, within a period of one year from the date of their initial removal from the factory or warehouse or within the period of warranty or guarantee which ever is more if such goods or parts thereof need to be re-made, refined, reconditioned, repaired or subjected to any similar process in the factory. Such goods and parts thereof if not subjected to any process amounting to

manufacture, can be removed from the factory or warehouse without payment of duty subject to such conditions as may be specified by the Commissioner.

M/s. Glass Equipment (India) Limited, Bahadurgarh, in Rohtak Commissionerate of Central Excise, engaged in the manufacture of glass forming machineries and parts thereof, received back machines sold by him to M/s. Hindustan National Glass Industries Limited during the past period ranging from 5 to 15 years, for overhauling, reconditioning, repairing etc. under rule 173-H. These goods were cleared after repairing, overhauling and reconditioning involving manufacturing process. Assessee also received Rs.54.98 lakh for the said work undertaken in 1996-97 and 1997-98 but excise duty leviable thereon was not paid. As the goods were received back after the expiry of prescribed period and were not accompanied by duty paying documents, duty was recoverable on those goods.

On this being pointed out (February 1999), the Ministry admitted the objection and stated (October 2003) that demand of Rs.97.17 lakh for the period from April 1996 to January 2001 had been confirmed, besides imposing penalties of Rs.89.95 lakh under section 11AC and Rs.7.33 lakh under rule 173Q.

8.5 Non-levy of duty on excisable goods used captively

Under procedure set-out in chapter X of the Central Excise Rules, 1944, an assessee can procure raw materials on the strength of a certificate (CT-2) without payment of duty for utilization only for the purpose specified in the said certificate failing which the duty at the appropriate rate would become payable.

M/s. Krishak Bharati Co-operative Limited, in Surat I Commissionerate of Central Excise, manufacturing fertilisers falling under chapter 28 had procured aromatic rich naptha and natural gasoline liquid under chapter X procedure without payment of duty for use in the manufacture of fertilisers. Out of those inputs, the assessee manufactured steam, de-mineralised water and treated water and cleared them to Hazira Ammonia Extension Plant without payment of duty to manufacture products other than fertilisers during the period between December 1998 and March 2002. As the said goods were used for other than the purpose for which they were procured, duty was leviable thereon.

On this being pointed out (August 2002), the Ministry admitted the objection and stated (October 2003) that two show cause notices for Rs.63.48 lakh for the period from September 1997 to March 2003 had been issued.

8.6 Non-levy of duty on excisable goods cleared

Under rule 4 of the Central Excise Rules, 2002, every person who produces or manufactures any excisable goods shall pay duty leviable on such goods in the manner provided in rule 8, and no excisable goods shall be removed without payment of duty from any place where they are produced or manufactured. On failing to do so, the person shall be liable to a penalty not exceeding the duty on such goods or ten thousand rupees whichever is greater under rule 25 of the said rules.

M/s. U.P. State Sugar Corporation, in Allahabad Commissionerate of Central Excise, manufactured sugar falling under heading 17.01 and cleared 100303 quintals sugar (free sale) during April 2002 and May 2002 and paid duty on 27208 quintals only. This resulted in non-

levy of duty of Rs.62.13 lakh on 13095 quintals of sugar. The assessee was also liable to pay penalty of Rs.62.13 lakh for contravening the provisions of the rules and interest of Rs.9.86 lakh upto May 2003 under section 11AB of the Act.

On this being pointed out (March 2003), the Ministry while admitting the objection stated (October 2003) that the matter was noticed by range officer in September 2002 and a show cause notice for Rs.62.13 lakh had been issued in May 2003.

The fact remains that the show cause notice was issued only after being pointed out in audit.

8.7 Other cases

In 159 other cases of non-levy of duty, the Ministry/the Department had accepted objections involving duty of Rs.3.26 crore and reported recovery of Rs.2.04 crore in 142 cases till February 2004.

CHAPTER IX : DEMANDS NOT RAISED OR DELAYED

Short payment or non-payment of duty on any excisable goods is to be recovered by issuing a show cause notice under section 11A to be followed up with its adjudication and recovery proceedings. The period of limitation for issue of show cause notice is one year (six months upto 11 May 2000) in normal cases of non-levy/short levy of duty. In case of short levy/non-levy due to fraud, collusion etc. the limitation period stands extended to five years. Some illustrative cases of demands raised with delay or not raised are given in the following paragraphs: -

9.1 Non raising of demand

The Supreme Court in the case of Union of India and others Vs. Madhumilan Syntex Private Limited {1988 (35) ELT 349 (SC)} held that unless a show cause notice was issued under section 11A of the Central Excise Act, 1944, the Department was not entitled to recover any dues.

9.1.1 Test check of records of M/s Jaiswal Neco Limited, in Raipur Commissionerate of Central Excise, engaged in manufacture of pig iron (chapter 72), revealed that they had been procuring iron ore (heading 26.01) from M/s Tisco Limited on payment of duty though the same was chargeable to nil rate of duty and had been availing Modvat/Cenvat credit of duty paid on inputs. Availing of such credit was not correct as duty paid on such inputs was not duty but deposit for which credit was not admissible as clarified by the Board on 4 January 1991. Internal audit in January 2002 had also pointed out incorrect availing of Rs.3.06 crore for the period April 2000 to December 2001. Inspite of this, the Department did not take action to protect revenue by issue of timely show cause notices. Demands for Rs.83.71 lakh for the period from February 2002 to May 2002 were issued only in March 2003. The demands hit by time bar resulted in loss of revenue of Rs.4.39 crore for the period April 1997 to January 2002 and revenue of Rs.2.05 crore for the period from June 2002 to May 2003 remained un-protected due to non-issue of show cause notice.

On this being pointed out in June 2003; the Ministry of Finance (the Ministry) admitted the objection (November 2003).

9.1.2 M/s. Modern Petrofils, in Vadodara II Commissionerate of Central Excise, manufacturing 'partially oriented yarn' cleared goods worth Rs.4.32 crore against AR 3As (bearing numbers 132 to 305) between 1 June and 8 June 2000. The range officer issued in September 2000 a simple letter to the assessee demanding duty of Rs.69.11 lakh for non-submission of re-warehousing certificates for AR3As bearing numbers 257 to 305 within 90 days. The range officer also issued another simple letter in December 2000 demanding duty of Rs.85.15 lakh for AR3As bearing numbers 132 to 256 having been found fake and fabricated. Against these, the assessee appealed to the High Court. Assessee's appeal against the September 2000 demand was pending decision. However, the High Court set aside (June 2001) the demand of December 2000 directing the Department to give sufficient opportunity to the assessee by issue of show cause notice as required under the law which had still not been done. Thus, due to non-initiation of proper action, government dues of Rs.154.26 lakh

(Rs.69.11 lakh for non receipt of re-warehousing certificates and Rs.85.15 lakh on account of fake and fabricated AR 3A) remained unprotected.

On this being pointed out (August 2002), the Ministry admitted the objection (December 2003).

9.1.3 Section 11D of the Central Excise Act, 1944, prescribes that every person who is liable to pay duty under this Act and has collected any amount in excess of the duty paid on any excisable goods, shall pay the amount so collected, to the credit of central government. Where the amount has not been so paid, the central excise officer may serve show cause notices on the person liable to pay such amount.

Four units of M/s. Indian Oil Corporation Limited and M/s. Bharat Petroleum Corporation Limited, in Bolpur and Shillong Commissionerates of Central Excise, received motor spirit, high speed diesel and kerosene on payment of duty at the appropriate rate prevalent at that point of time. The materials were stored in separate duty paid tanks from where the same were sold and central excise duty was collected at the higher rate applicable at the time of sale. The extra duty of Rs.1.11 crore so collected between March 2001 and July 2002 was not remitted to the government exchequer by the assessee. The Department also did not take any action to realise it from the assessees by issuing demand notices.

On this being pointed out (between June and October 2002), the Ministry admitted the objection in two cases and intimated (August 2003) recovery of Rs.16.62 lakh and issue of show cause notices for Rs.11.62 lakh in February 2003. In the remaining two cases the Ministry stated (October 2003) that the assessees purchased duty paid goods and sold them at a profit like any other wholesaler and therefore, there was no obligation to pay the difference.

Reply of the Ministry is not tenable as the assessees had collected more duty than actually paid and hence it was recoverable under section 11D of the Act.

9.2 Short raising of demand

Test check of records of M/s. Tamil Nadu Petroproducts Limited, Manali, in Chennai I Commissionerate of Central Excise, revealed that in September 2002, the Department had issued a show cause notice to the assessee demanding differential duty of Rs.37.37 lakh for epichlorohydrin supplied to M/s. Petro Araldite Private Limited during September 2001 to February 2002 by treating M/s. Petro Araldite Private Limited as a related person and by reworking the value adopted by the assessee at 115 per cent of cost of production. However, the demand was raised on the profit margin element (Rs.23,632 per tonne) alone omitting the raw material cost and overheads (Rs.1,12,100 per tonne). So, the demand was raised short by Rs.1.40 crore.

On this being pointed out (November 2002 and January 2003), the Ministry admitted the objection (October 2003).

9.3 Delay in raising demand

M/s. Ind Swift Limited, Parwanoo, in Chandigarh I Commissionerate of Central Excise, manufactured 'chloroquin phosphate tablets' (sub-heading 3003.20) by using inputs which were common for dutiable and exempted category of final products. The assessee cleared chloroquin phosphate tablets after availing exemption but without payment of Rs.56.62 lakh

being 8 per cent of the price of exempted final goods leviable under rule 57CC during January 1998 to February 2000. The internal audit had also pointed out the non-levy in August 1998. However, no demand was raised till date of audit (November 1999).

On this being pointed out (November 1999), the Ministry stated (November 2003) that show cause notice for Rs.56.62 lakh for the period June 1997 to December 1997 had been issued in July 2002. Details of the show cause notice issued for the period from January 1998 to February 2000 had not been intimated.

9.4 Non realisation of confirmed demand

Section 11 of the Central Excise Act, 1944, provides that if any duty and any other sum of any kind is payable to government under the provisions of Act or rules made thereunder, the officer empowered to levy such duty or require the payment of such sums may deduct the amount so payable from any amount payable or due to the assessee, and if the amount payable is not so recovered, he may prepare a certificate signed by him specifying the amount due from the person liable to pay the same and send it to the Collector of the district in which such person resides or conducts his business and the said Collector, on receipt of such certificate, shall proceed to recover from the said person the amount specified therein as if it were an arrear of land revenue. Further, rule 230 of the Central Excise Rules, 1944, also provides for the recovery of dues. For late payment of revenue, interest is also leviable under the Act/Rules.

Test check of records of PBC Range, Mukerian in Jalandhar Commissionerate of Central Excise, revealed that a demand of Rs.28.83 lakh was confirmed by the Commissioner vide his orders dated 23 September 1988 and a personal penalty of Rs.25,000 was also imposed in the case of M/s. Northern India Rubber Limited, Dina Nagar, but the same had not yet been realised despite a lapse of 14 years. Besides, interest of Rs.86.43 lakh (notional Rs.38.92 lakh from 23 September 1988 to 25 May 1995 and thereafter actual Rs.47.51 lakh till June 2003) was also leviable for delayed payment.

On this being pointed out (April 2002 and March 2003), the Department stated (July 2003) that the party had obtained (September 1988) stay of recovery from Tribunal until the case was finally decided. The case was decided in November 1999 in favour of revenue but during the interim period the factory had been closed and property with plant and machinery disposed of.

Inaction on the part of the Department to attach the properties pending decision of Tribunal or to obtain a stay on the disposal of properties enabled the assessee to dispose of the properties. The Department's lapse in protecting government revenue led to it becoming irrecoverable.

The Ministry admitted the facts of the audit objection (November 2003).

9.5 Other cases

In 4 other cases of demands, the Ministry/the Department had accepted objections involving duty of Rs.1.03 crore till February 2004.

CHAPTER X : CLASSIFICATION OF EXCISABLE GOODS

The rates of duty leviable on excisable goods are prescribed under various headings in the Central Excise Tariff. Some illustrative cases of incorrect classification of goods resulting in short levy of duty are given in the following paragraphs:

10.1 Fertilisers

Harmonized Commodity Description and Coding System specifies that, heading 31.01 excludes mixtures of natural fertilisers with chemical fertilisers. Mixtures of animal or vegetable fertilisers with chemical or mineral fertilisers are, thus appropriately covered under heading 31.05.

M/s. Krishi Rasayan Export Private Limited, Baddi, in Chandigarh I Commissionerate of Central Excise, manufactured 'Kri Kelp (Cytozyme/sea weed) and classified it as vegetable bio-fertiliser under heading 31.01 carrying nil rate of duty. Scrutiny of the manufacturing process revealed that cytozyme was a micro-nutrient i.e. mixture of soluble salts which assist in growth of plants and was thus correctly classifiable under heading 31.05. Incorrect classification of the product, resulted in non-levy of duty amounting to Rs.1.72 crore from April 1996 to March 2001.

On this being pointed out (March 2001), the Ministry of Finance (the Ministry) while admitting the objection stated (November 2003) that the matter was in their knowledge and was under investigation since July 2000.

Reply of the Ministry is not tenable as action to safeguard revenue was taken only after it was pointed out in audit (March 2001). Two show cause notices for Rs.20.06 lakh and Rs.133.27 lakh were issued in May and December 2001.

10.2 Dabur lal tail

Note 5 of chapter 33, clarifies that heading 33.04 applies to skin foods, skin tonics, cuticle removers and other preparations for use in manicure or chiropody and barrier creams to give protection against skin irritants. The Supreme Court in the case of M/s. Shree Baidyanath Ayurved Bhawan Limited {1996 (83) ELT 492 (SC)} had held that medicine is ordinarily prescribed by a medical practitioner and it is used for limited time and not every day unless it is so prescribed to deal with a specific disease like diabetes. The Tribunal in the case of M/s. Sunny Industries (P) Limited {1995 (75) ELT 677 (T)} held that 'Ad – vitamin massage oil fortex' being a massage oil intended for care of skin is classifiable under heading 33.04.

M/s. Burman Laboratories (P) Limited, Maksi, in Indore Commissionerate of Central Excise, manufactured 'Dabur lal tail' – baby massage oil for the care of skin and classified the product under sub-heading 3003.39 as other medicament. As per the product literature, it was a baby massage oil for the care of skin, intended for strengthening muscles and nourishing baby's tender skin to keep it soft and supple. It was, therefore, correctly classifiable under heading 33.04 as per note 5 of chapter 33 and judgements ibid. Incorrect classification of the product, resulted in short levy of duty of Rs.1.42 crore from June 2001 to January 2002.

On this being pointed out (March 2002), the Ministry admitted the objection (October 2003).

10.3 Other cases

In 19 other cases of classification, the Ministry/the Department accepted objections involving duty of Rs.1.07 crore and reported recovery of Rs.20 lakh till February 2004.

CHAPTER XI : INTEREST NOT DEMANDED OR REALISED

Section 11AA of the Central Excise Act, 1944, prescribes that where a person chargeable with duty determined under sub section (2) of section 11A, fails to pay such duty within three months from the date of such determination, he shall pay in addition to duty, interest at the rate of 20 per cent per annum (24 per cent with effect from 12 May 2000 and 15 per cent with effect from 13 May 2002) on such duty from the date immediately after the expiry of the said period of three months till the date of payment. Some illustrative cases of interest not demanded or realised are mentioned below:

11.1 Non-realisation of interest

Non-payment of confirmed demands of Rs.92.31 lakh alongwith interest of Rs.33.18 lakh by M/s. Jenson and Nicholson (I) Limited in Kolkata III Commissionerate of Central Excise, for the period from 13 September 1997 to 30 June 1999 had been pointed out in Para 9.3 of the Audit Report 1999-2000. The Ministry of Finance (the Ministry) while admitting the case, reported (October 2001) that an amount of Rs.18.50 lakh had been recovered and the balance amount with interest was being pursued for recovery.

Subsequent audit of the unit revealed that the assessee paid the outstanding demand in installments alongwith an amount of Rs.2 lakh as interest on his own but did not pay the accrued interest of Rs.64.13 lakh (upto September 2001). The Department did not take any action to realise such interest either.

On this being pointed out (April 2002), the Ministry admitted the audit objection (November 2003).

11.2 Interest not demanded

Test check of records of the range offices under Jaipur I and II Commissionerates of Central Excise, revealed that demands for duty of Rs.1.40 crore were confirmed against nine assessees between May 1997 and November 2000. Duty was deposited after delay ranging from 21 to 40 months. Interest of Rs.18.78 lakh payable on account of delay was neither paid by the assessees nor demanded by the Department.

On this being pointed out (January 2003), the Ministry admitted the objection and intimated (December 2003) recovery of Rs.13.80 lakh in five cases. In the remaining four cases, it intimated that the matter was sub-judice.

11.3 Interest lost due to non determination of duty

Section 11A(2B) of the Central Excise Act, 1944 (with effect from 11 May 2001), prescribes that where any duty of excise has not been levied or short levied, the person chargeable with duty may pay the amount of duty before service of notice under sub section (1), and inform the Central Excise Officer of such payment in writing, who, on receipt of such information shall not serve any notice. As per explanation 2 below sub section 2(B), interest under section 11AB shall be payable on the amount paid under this sub section. Section 11AB provides for charging interest at the rate of 24 per cent per annum (15 per cent with effect

from 13 May 2002) from the first day of the month succeeding the month in which duty ought to have been paid under the Act.

11.3.1 M/s. Ispat Metallics India Limited, in Raigad Commissionerate of Central Excise, engaged in the manufacture of iron and steel products, did not pay differential duty on due dates on hot metal cleared to M/s. Ispat Industries Limited during the period from May 2001 to March 2002. The delay in payment of differential duty ranged from15 days to 127 days. Interest amounting to Rs.47.04 lakh leviable for delayed payment as per provisions cited above was not paid by the assessee.

On this being pointed out (November 2002), the Ministry admitted the objection (December 2003).

11.3.2 Test check of records of M/s. Indian Oil Corporation, Sangrur, in Ludhiana Commissionerate of Central Excise, revealed that the rate of excise duty leviable on motor spirit was revised from 20 per cent to 32 per cent ad valorem with effect from 3 June 1998. The assessee cleared 3490.383 kilo litre of motor spirit on 3 June 1998 at the enhanced duty rate. The differential duty amounting to Rs.55.23 lakh collected from the customers was remitted after a delay of 37 months. Failure of the Department to demand duty on its becoming due resulted in notional loss of interest of Rs.34.76 lakh for the period from 3 September 1998 to 16 July 2001.

On this being pointed out (November 2002), the Ministry stated (October 2003) that the assessee had collected higher rate of duty in its capacity as a trader and hence party was not liable to pay differential duty and therefore question of payment of interest did not arise.

Reply of the Ministry is not tenable as the excise duty was collected from the customers at the higher rate. The assessee had remitted the excise duty so collected, thus acknowledging its liability to pay. Delayed payment of this duty had resulted in loss of interest of Rs.34.76 lakh.

11.4 Other cases

In 10 other cases of interest not demanded or realised, the Ministry/the Department accepted the objections involving duty of Rs.76.81 lakh and reported recovery of Rs.42.62 lakh in 8 cases till February 2004.

CHAPTER XII : CESS NOT LEVIED OR DEMANDED

Cess is levied and collected in the same manner as excise duty under the various Acts of Parliament.

Some of the cases in which cess was not levied or demanded are mentioned below:

12.1 Non-levy of cess on cement

Rule 2 of Cement Cess Rules, 1993, read with Ministry of Industry's (Department of Industrial Development) standing orders 125(E) dated 24 February 1993, prescribes 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 based on vertical shaft kiln is to pay a cess of seventy five paise on every tonne of cement manufactured and removed from his factory. Rules 3 and 4 of Cement Cess Rules further stipulate that every manufacturer of cement who is liable to pay cess shall submit to the Development Commissioner for Cement Industry, Government of India, 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 demand draft by 15th of the following month.

Twelve manufacturers of cement, in four Commissionerates of Andhra Pradesh, cleared 159.57 lakh tonne of cement produced in their factories during the years from 1995-96 to 2002-03 without payment of cess amounting to Rs.1.20 crore even though the installed capacity of their factories operating on rotary kilns was far in excess of 99,000 tonne per annum.

On this being pointed out (January 2003), the Development Commissioner/Ministry of Commerce and Industry intimated (January 2003 and August 2003) recovery of Rs.9.28 lakh from an assessee and issue of demand notices to five others. In the remaining six cases, the Ministry intimated that the matter was under consideration for grant of exemption in response to Cement Manufacturers Association's demand for exemption to mini cement plants.

12.2 Non-levy of cess on textiles

Under section 5A(1) of the Textile Committee Act, 1963 and the notification issued (June 1997) by the Ministry of Commerce, cess at 0.05 per cent ad valorem is leviable on textiles manufactured in India. For this purpose textiles interalia includes fabrics made wholly or partly of cotton, wool, silk, artificial silk or other fabric. The authority to collect such cess is vested with the Textile Committee constituted under the Act.

12.2.1 Test check of records of eleven assessees, engaged in manufacture of processed textile fabrics in Gujarat and Haryana, revealed (January and November 2002) that the assessees did not pay textile cess amounting to Rs.60.63 lakh between the period April 1998 and September 2002. The Textile Committee also did not demand cess.

On this being pointed out (between February and December 2002), the Ministry of Textiles intimated (August 2003) recovery of Rs.4.70 lakh from two assessees and issue of demand

notices to five others one of whom had gone in appeal. Reply in the remaining cases had not been received (February 2004).

12.2.2 Another two manufacturers of yarn, collected cess from their customers/ buyers on the clearance of yarn, but did not deposit it with the Textile Committee on the ground that stay had been granted by the High Court of Rajasthan. Scrutiny of records revealed that stay was granted against demand pertaining to the year 1995-96 in one case and pertaining to the period from July 1991 to June 1993 in the other. Stay was granted on the ground that appeals of assessees were pending before Tribunal. The two assessees had collected a total amount of Rs.51.90 lakh on account of cess, which had not been remitted into Government account. Audit scrutiny further revealed that the committee did not raise demands for the subsequent period by obtaining value of clearance of yarn from Central Excise Department. Further, in the absence of provisions for charging interest on delayed payment of cess in the Textile Committee (Cess) Rules, 1975, the assessees enjoyed financial accommodation of Rs.51.99 lakh being the amount of cess collected but not paid along with interest thereon.

On this being pointed out (March 2003), the Ministry of Textiles stated (August 2003) that demand notices for the period upto June 2003 had also been issued but the assessees had not responded as their appeals were pending decision with the Tribunal.

12.3 Other cases

In 3 other cases of cess, the Department had accepted the objections involving cess of Rs.1 lakh and reported recovery of Rs.1 lakh till February 2004.

CHAPTER XIII : MISCELLANEOUS TOPICS OF INTEREST

13.1 Incorrect payment of duty on the basis of production capacity

Explanation III under rule 5 of Hot Air Stenter Independent Textile Processor Annual Capacity Determination Rules, 1998 as amended, prescribes that if the processor of specified fabrics has proprietary interest in any other factory engaged in the spinning of yarn or weaving of fabrics, he cannot be treated as an independent processor for the purpose of levy of duty under section 3A of Central Excise Act. Since the term 'proprietary interest' has not been defined in the Act, the related provisions in the Companies Act (section 370 sub section I B) and in the Monopolies and Restrictive Trade Practices Act {section 2(g) and explanation thereto} have to be applied for interpretation of this term. As per the explanatory note to section 2(g) of the MRTP Act, two undertakings shall be deemed to be inter-connected if one owns, manages and controls the other. The Ministry of Law opined on 28 June 2001 that two companies can be considered as undertakings under the same management if they are owned, managed or controlled by the other.

M/s. Sangam Processors Limited, Bhilwara, in Jaipur II Commissionerate of Central Excise, engaged in processing of fabrics cleared its finished product on payment of duty on the basis of production capacity. Scrutiny of the balance sheet for the year 1999-2000 revealed that the assessee company and the other unit viz. M/s. Sangam India Limited, Bhilwara had a common Chairman and a common Director. Therefore in terms of explanation in MRTP Act, these two companies were under the same management. As the latter company was primarily and substantially engaged in the spinning of yarn and weaving of fabrics, the assessee was not eligible to pay duty under section 3A of the Central Excise Act. Duty was required to be paid under section 4 of the Central Excise Act. This resulted in short payment of excise duty of Rs.27.24 crore during the period from 16 December 1998 to 31 October 2000.

On this being pointed out (February 2001), the Ministry of Finance (the Ministry) stated (December 2003) that the Supreme Court in the case of M/s. Alembic Glass Industries Limited {2002 (143) ELT 244} had held that two limited companies having common Directors did not mean that one company had interest in the business of the other.

Reply of the Ministry is not relevant as the question involved in this case is of proprietary interest and not of the business interest. The absence of explanation of the term 'proprietary interest' in the Act, facilitated the units to avail benefit under the said Act though they were not otherwise entitled to the concessions.

13.2 Default in payment of duty attracting penalty and forfeiture of fortnightly payment facility

Rule 8 of the Central Excise Rules, 2001, prescribes that duty on goods removed from a factory or a warehouse during the first fortnight of the month shall be paid by the 20th of that month and duty on the goods removed from the factory or the warehouse during the second fortnight of the month shall be paid by the 5th of the following month. If the assessee fails to pay any one instalment within 30 days from the due date or the instalment by the due dates for the 3rd time in a financial year, the assessee shall forfeit the facility for a period of 2

months from the date of communication of orders or till such date on which all the dues were paid, whichever was later. During this period the assessee is required to pay duty for each clearance through the PLA. In the event of any failure, it shall be deemed that such goods have been cleared without payment of duty and he shall be liable to penalty not exceeding the amount of duty leviable or ten thousand rupees, whichever is greater.

13.2.1 M/s. Priyadarshini Cement Limited and M/s. India Cements Limited, in Hyderabad III Commissionerate of Central Excise, defaulted in payment of central excise duty on more than 3 occasions during the fortnights ending 30 April 2002 to 30 June 2002. The jurisdictional Deputy Commissioner passed forfeiture orders (May and July 2002) withdrawing the fortnightly payment facility in these cases for two months or till the date of clearance of dues whichever was later. Though the assessees cleared the goods for the subsequent period on payment of duty on consignment basis, they did not pay the outstanding dues relating to the said fortnights together with interest. The Department did not initiate any steps for recovery of duty and so government revenue of Rs.6.99 crore and interest thereon amounting to Rs.0.16 crore remained unrecovered.

On this being pointed out (July/September 2002), the Department in the first case reported (May 2003) that the assessee had not cleared the dues yet and that the outstanding amount with interest was recoverable as arrears of revenue under section 11 of Central Excise Act, 1944. In the second case the Department reported (May 2003) that the dues payable amounting to Rs.4.23 crore with interest of Rs.0.48 crore were paid by the assessee in 15 instalments between 23 January 2003 and 4 April 2003.

Inaction by the Department in initiating recovery action had resulted in non-remittance of excise duty inclusive of interest of Rs.3.08 crore in the case of M/s. Priyadarshini Cements (March 2003) and delayed remittances of Rs.4.23 crore by M/s. India Cements.

The Ministry confirmed the facts (December 2003).

13.2.2 M/s Gabriel India Limited, in Indore Commissionerate of Central Excise, defaulted in payment of duty on due dates on ten occasions in succession between May 2001 and March 2002. Therefore, the facility of fortnightly payment was to be forfeited with immediate effect and the assessee was required to pay duty in cash on consignment basis. The Department did not take action to forfeit the facility. The assessee continued to pay duty from Cenvat account and utilized the Cenvat credit of Rs.1.38 crore between August 2001 and March 2002 in contravention of rule 8 of the Central Excise Rules, 2001. Therefore, clearances of goods on payment of duty of Rs.1.38 crore from Cenvat account was to be treated as clearance of goods without payment of duty. An equal amount of penalty of Rs.1.38 crore was also leviable under the rules. Interest was also recoverable for delayed payment of duty.

On this being pointed out (April 2002), the Ministry admitted the audit objection (December 2003).

13.2.3 M/s. Hindusthan Engineering and Industries Limited, Santragachi, in Kolkata II Commissionerate of Central Excise, defaulted thrice in payment of duty on due dates in 2000-2001. Accordingly, the forfeiture order was passed in March 2001, directing the assessee to clear excisable goods on payment of duty from account current on consignment basis for two months. The assessee however paid duty both from the account current and

Cenvat account in the months of March 2001, April 2001 and June 2001. All the dues for the defaulting period including interest were cleared in the month of July 2001. Since the assessee paid duty through the Cenvat account during the said period in contravention of rule 8, it resulted in clearances of goods without payment of duty of Rs.66.59 lakh as per said sub-rule. An equal amount of penalty was also leviable under the rules.

On this being pointed out (July 2002), the Ministry while admitting the audit objection in principle stated (December 2003) that a show cause notice demanding Rs.45.08 lakh and also proposing imposition of penalty had been issued to the assessee.

13.2.4 M/s. Kalinga Iron Works and M/s. Orissa Sponge Iron Limited, in Bhubaneswar II Commissionerate of Central Excise, defaulted in payment of duty of Rs.125.31 lakh pertaining to January and February 2002 and August 2001. Both the assessees paid Rs.65.39 lakh during the months of April 2002 to August 2002 leaving a balance of Rs.59.92 lakh still unpaid. No action was taken by the Department to recover duty of Rs.59.92 lakh alongwith interest of Rs.17.80 lakh due till the end of August 2002. Penalty of equal amount of duty of Rs.59.92 lakh was also leviable.

On this being pointed out (January 2003), the Ministry admitted the objection and intimated (October 2003) recovery of Rs.81.76 lakh including interest.

13.3 Undue financial accommodation due to non recovery of duty short paid

Under notification dated 4 January 1995, all excisable goods manufactured by a hundred per cent Export Oriented Undertaking (EOU) and allowed to be sold in India i.e. sale in Domestic Tariff Area (DTA) are to be charged to excise duty at a concessional rate of 50 per cent of aggregate of the duties of customs. The Board while clarifying the method of calculation of duty leviable under said notification directed the Department on 6 February 2001 that the duty on goods cleared in DTA should be calculated in the manner as given in circular dated 24 September 1999 and differential duty on or after 16 September 1999 should be recovered by 15 February 2001.

Test check of records of M/s. Ferro Alloys Corporation (EOU), in Bhubaneswar Commissionerate of Central Excise, revealed that the assessee manufactured charge chrome and cleared the goods in DTA on payment of duty. The duty was calculated in a manner different from the manner prescribed by the Board thereby resulting in short payment of duty of Rs.76.44 lakh from 16 September 1999 to 16 March 2001. The Department did not finalise the assessments despite Board's order of February 2001 ibid. This resulted in financial accommodation to the assessee by way of non-realisation of duty of Rs.76.44 lakh besides interest.

On this being pointed out (April 2002), the Ministry while confirming the facts intimated (October 2003) that demand of Rs.78.93 lakh had been confirmed and penalty of Rs.8 lakh imposed.

13.4 Other cases

In 436 other cases of miscellaneous topics of interest, the Ministry/the Department had accepted objections involving duty of Rs.6.21 crore and reported recovery of Rs.3.83 crore in 396 cases till February 2004.

SECTION 2 - SERVICE TAX

SECTION 2: SERVICE TAX

General

Service tax was introduced from 1 July 1994 through the Finance Act, 1994. Administration of service tax has been vested with the central excise department under the Ministry of Finance (the Ministry). The Board has set up a separate apex authority headed by Director General Service Tax (DGST) at Mumbai for its administration. Commissioners of Central Excise have been authorised to collect service tax within their jurisdiction. This section features a review "Service tax on advertising services and courier services" with financial implication of Rs.460.79 crore and contains 42 paragraphs featured individually or grouped together with a revenue implication of Rs.42.21 crore. The Ministry/the Department had accepted audit observations in 35 paragraphs involving Rs.40.43 crore and recovered Rs.2.04 crore till February 2004. The significant findings of audit included in this section are mentioned in the following chapters:-

CHAPTER XIV : REVIEW ON SERVICE TAX ON ADVERTISING SERVICES AND COURIER SERVICES

14.1 Highlights

- **Instructions issued by the Board for exclusion of charges towards obtaining space and time for publishing and display in the print/electronic media were contrary to the provisions of the Finance Act. Service tax of Rs.74.53 crore was forgone in 18 Commissionerates of Central Excise.**

(Paragraph 14.5)

- **Measures taken by the Department to bring into tax net active service providers were ineffective and inadequate. This resulted in 1408 advertising agencies in 19 Commissionerates of Central Excise remaining un-registered, with loss of revenue estimated to be Rs.160.77 crore.**

(Paragraph 14.7)

- **Due to lack of proper monitoring system, 44 registered advertising agencies in 12 Commissionerates of Central Excise did not file returns thereby evading tax to the extent of Rs.4.62 crore.**

(Paragraph 14.11)

- **Ineffective assessment procedure resulted in short levy of tax to the tune of Rs.8.25 crore and Rs.3.15 crore by 94 advertising agencies in 17 Commissionerates of Central Excise and 14 courier agencies in 5 Commissionerates of Central Excise respectively.**

(Paragraph 14.15)

- **Agencies which were engaged in providing celebrities for advertising purposes and fell within the definition of 'advertising agency' did not pay tax of Rs.1.68 crore.**

(Paragraph 14.16)

14.2 Introduction

Service tax on 'advertising services' was levied with effect from 1 November 1996. For the purpose of this levy, the term 'advertising agency' means any commercial concern engaged in providing any service connected with the making, preparation, display or exhibition of advertisement and includes an advertisement consultant. Further, advertisement has been defined to include any notice, circular, label, wrapper, document, hoarding or any other audio/visual representation made by means of light, sound, smoke or gas. Every advertising agency which raises a bill on a client is liable to pay service tax at 5 per cent (8 per cent with effect from 14 May 2003) on the gross amount charged from the client for services related to the advertisement.

Service tax on 'courier services' was also levied with effect from 1 November 1996. Courier agency refers to a commercial concern engaged in the door to door transportation of sensitive documents, goods and articles utilising the services of a person either directly or indirectly to carry or accompany such documents, goods or articles. This also includes 'express cargo services' provided by some transporters. Every courier agency raising the bill for services rendered to a client is liable to pay service tax at 5 per cent (8 per cent with effect from 14 May 2003) on the gross amount charged from the customer.

14.3 Audit objectives

A review was undertaken to seek assurance on: -

(i) the adequacy of the mechanism to ensure that potential assessees providing advertising and courier services had been brought into the service tax net; and
(ii) the adequacy and effectiveness of the rules framed and procedures prescribed to ensure tax compliance by service providers.

For this purpose, records of 41 major service tax earning Commissionerates in these two services covering 8 States were checked. The period covered under audit was from 1996-97 to 2001-02. The findings are contained in the succeeding paragraphs.

Macro issues

14.4 Trend of revenue

The table below gives an indication of trend of revenue in respect of 41 Commissionerates test checked.

14.4.1 Advertising services

(Amount in crore of rupees)

No. of Commiss-ionerates	1997-98		1998-99		1999-2000		2000-2001		2001-2002	
	No. of assessees	Revenue	No. of assessees	Revenue	No. of assessees	Revenue	No. of assessees	Revenue	No. of assessees	Revenue
41	8941	44.15	10402	47.59	12625	68.66	13637	110.98	14859	87.79

- Despite an increase of 9 per cent in the number of assessees during the year 2001-02 over the year 2000-01, there was an overall decline in revenue to the extent of 21 per cent, which was particularly noticeable in Mumbai V, Pune II, Kolkata I, Bolpur, Ahmedabad I and Bangalore I Commissionerates of Central Excise.
- The increase in number of assessees which was 16 and 21 per cent in the years 1998-99 and 1999-2000 compared to each of the immediately preceding years came down to 8 and 9 per cent in 2000-01 and 2001-02 respectively.

14.4.2 Courier services

(Amount in crore of rupees)

No. of Commiss-ionerates	1997-98		1998-99		1999-2000		2000-2001		2001-2002	
	No. of assessees	Revenue	No. of assessees	Revenue	No. of assessees	Revenue	No. of assessees	Revenue	No. of assessees	Revenue
39	9106	19.90	10594	18.80	12659	45.01	15169	54.64	16875	59.50

- Despite an increase of 11 per cent in the number of courier service providers during the year 2001-02 compared to 2000-01, there was only 9 per cent increase in revenue. In fact, Pune II, Kolkata I, Ahmedabad I, Belgaon and Mangalore Commissionerates of Central Excise recorded a decline in revenue during 2001-02 despite addition of new service providers in these Commissionerates in the range of 3-38 per cent.
- The rate of increase in assessees which was around 16-20 per cent in the first 4 years came down to 11 per cent in 2001-02.

14.5 Inconsistency between Finance Act and Board's instructions on the value to be taxed on advertising agency

According to section 67 of the Finance Act, 1994, as amended, value of any taxable service shall be the gross amount charged by the service provider for such service rendered by him. While imposing service tax on advertising agency vide the Finance Act, 1996, the value of taxable service was defined as 'the gross amount charged by such agency from the client for services rendered in relation to the advertisement'. This would, therefore, include the entire gamut of services rendered by the agency in connection with display or exhibition in the print or electronic media. Contrary to the provisions of the Act, the Board in their circular dated 31 October 1996 clarified that the amount paid by advertising agency towards obtaining space and time in getting their advertisement published/displayed in the print/electronic media was not to be included in the value of taxable service. Service tax was to be levied only on the amount representing commission of 15 per cent given by the media to the accredited agencies and commission of 10 per cent given to the non-accredited agencies. The tax research unit (TRU) of the Board had estimated the turnover of advertising agencies to be in the order of Rs.3000 crore out of which advertisement through print media and electronic media account for roughly 60 per cent and 30 per cent respectively. Due to exclusion of the component of expenses towards space and time in the print and electronic media against the expressed intention of the government in the Act, almost 85 per cent of the

90 per cent of total turnover of the advertising agency would remain outside the ambit of service tax.

Examination of relevant files revealed that Board's executive instructions, finally issued in October 1996, were not in conformity with either TRU's opinion or the opinion of Ministry of Law.

Exclusion of these advertisement expenses on the basis of executive instructions which were not in consonance with the Finance Act, resulted in less revenue being realised to the extent of Rs.74.53 crore for the period from 1996-97 to 2001-02 in respect of 18 Commissionerates of Central Excise alone as per the details given below: -

(Amount in crore of rupees)

No. of Commissionerates	No. of assessees	Gross amount of the bills	Amount of tax payable	Amount of tax paid	Amount of tax less realised
18	132	1765.37	88.28	13.75	74.53

Micro issues

14.6 Inadequate efforts by the Department to bring unregistered service providers into the tax net

According to section 69 of the Finance Act, 1994 read with rule 4 of the Service Tax Rules, 1994, every person liable to pay service tax shall make an application for registration to the Superintendent of Central Excise in form ST-I within a period of 30 days of the service tax becoming leviable. Penal provisions for levy of penalty under section 75A for failure of registration were made only with effect from 16 July 2001 in the Finance Act, 2001. Penalty for failure to pay service tax was leviable which would not exceed the amount of service tax that a person failed to pay under the section.

Prevention of tax evasion and widening of the tax base are two of the important functions of tax administration for optimum tax realisation. With increasing reliance on voluntary compliance by the tax payers at large, it becomes necessary for the Department to collect and utilise information from various sources to curb evasion of tax by unscrupulous assessees. While expressing concern over the lackadaisical approach of the Department towards the administration of service tax, the Board vide their instructions dated 5 November, 1999 issued directions to undertake survey and intelligence collection to identify potential tax evaders. Various measures undertaken by the Department to bring into the tax net unregistered service providers, and their impact on realisation of revenue, was examined in audit in the selected major tax earning Commissionerates in these two services. It was seen that apart from giving advertisements through print media enjoining on the agencies to register themselves, some Commissionerates conducted surveys and raids to tap potential assessees. The position of these surveys and raids conducted by some Commissionerates for the period from 1996-97 to 2001-02 and its impact on revenue is given below: -

14.6.1 Advertising services

(Amount in crore of rupees)

No. of Commissionerates	No. of surveys	No. of raids	No. of persons evading service tax identified	No. of persons issued registration	Additional revenue realised upto 31.12.2002
17	512	75	274	236	0.41

- 587 raids and surveys over a six year period could yield only 236 fresh assessees from whom a meagre Rs.0.41 crore was realised.
- It was noticed that some of the major earning Commissionerates of Central Excise such as Mumbai IV, Kolkata I, Ahmedabad I and Bangalore I had not conducted any raid/survey at all.

14.6.2 Courier services

(Amount in crore of rupees)

No. of Commissionerates	No. of surveys	No. of raids	No. of persons evading service tax identified	No. of persons issued registration	Additional revenue realised upto 31.12.2002
16	611	77	337	319	0.90

- A total of 688 raids and surveys over a period of six years brought into the tax net 319 service providers from whom Rs.0.90 crore was collected.
- Major earning Commissionerates of Central Excise, such as Mumbai IV, Kolkata I, Ahmedabad I and Bangalore I had not undertaken any raid or survey.

Audit noted that no target was fixed for any Commissionerate of Central Excise regarding minimum number of surveys or raids.

On this being pointed out (April 2003), Pune III Commissionerate of Central Excise replied (August 2003) that they had set up a survey intelligence verification cell within the service tax cell in June 2003, which resulted in unearthing 153 number of unregistered service providers till August 2003.

14.7 Audit scrutiny revealed that large number of advertisement service providers escaped from the tax net

The measures taken by the Department to widen the assessee base in these services being considered inadequate and ineffective, an effort was made in audit on a limited scale in the selected Commissionerates of Central Excise to gauge the extent of the evasion of tax by active service providers. In this connection, secondary records such as those of Doordarshan, All India Radio, Indian Newspaper Society, Yellow Pages, Municipal authorities as also income tax returns were verified.

It was revealed that these service providers had received gross amount of Rs.3215.77 crore for advertising services rendered during the period 1997-98 to 2001-02. None of these service providers were found registered with the central excise department. Service tax evaded by these agencies was to the tune of Rs.160.77 crore, besides interest of Rs.5.45 crore and penalty of Rs.160.77 crore under section 76 ibid as per the table given below: -

(i) As per secondary records other than income tax returns

(Amount in crore of rupees)

No. of Commissionerates	No. of service providers	Gross value of service provided	Amount of service tax not paid	Interest payable	Penalty
19	1334	2983.34	149.15	1.72	149.15

(ii) As per verification of income tax returns

(Amount in crore of rupees)

No. of Commissionerates	No. of service providers	Gross value of service provided	Amount of service tax not paid	Interest payable	Penalty
8	74	232.43	11.62	3.73	11.62

Some illustrative cases are given below: -

14.7.1 Scrutiny of income tax returns of M/s. Vantage Advertising Limited, Kolkata and M/s. Selvel Media Service, Kolkata revealed that these agencies realised a gross amount of Rs.96.00 crore from customers on account of advertisements for the period from April 1998 to March 2001. They did not register themselves with the Department and thus evaded payment of service tax to the extent of Rs.4.80 crore.

This was pointed out in March 2003; the reply of the Department had not been received (September 2003).

14.7.2 Investigation of monthly electricity bills sent by M/s. Calcutta Electric Supply Corporation (CESC) to its consumers in Kolkata I Commissionerate of Central Excise showed that it was also engaged in providing advertisement services to manufacturers of Fast Moving Consumer Goods (FMCG) printed on the body of the electricity bill. Discount coupons in a separate envelope were attached with the electricity bills in some cases. The company, being a commercial concern, satisfied the definition of advertising agency. Scrutiny of departmental records revealed that M/s. CESC was not registered with the Department and accordingly no service tax was paid. Verification of income tax returns, revealed that it had realised Rs.10.03 crore during the year 2001-02 on account of advertisements from FMCG. An estimated amount of Rs.50 lakh thus escaped taxation.

The Department has reported the issue of show cause notice for Rs.50.15 lakh covering the period 2001-02.

14.8 Failure of the Department to bring into tax net unregistered courier agencies even after their identification

Courier agencies, apart from providing courier services also undertake to transport documents, goods or articles on behalf of other courier agencies as a 'co-loader', and charge the other courier agencies for such services.

According to Board's circular dated 31 October 1996, service provided by co-loaders to the other courier agency is not chargeable to service tax as they do not provide any service directly to customers. This exemption to co-loader is based on the assumption that charges of co-loaders are ultimately recovered by the other courier agency from customers and service tax is paid on such gross charges by the other agency.

A scrutiny of service tax records of M/s. DHL World Wide Express and M/s. Blaze Flash Courier, Ahmedabad in Mumbai II and Ahmedabad I Commissionerates of Central Excise respectively revealed that they also acted as 'co-loader' for a number of unregistered courier agencies. These agencies paid service tax on the amount earned as co-loader because the unregistered courier agencies were not paying any service tax. The Department failed to act and register these unregistered courier agencies on the basis of details already available with co-loaders. This resulted in non realisation of tax on the actual amount charged by unregistered courier agencies from clients. Assuming the amount collected from customers to be double the amount paid to co-loaders, service tax on a conservative basis not paid worked out to Rs.31 lakh for the period 1997-98 and 2001-02 as per the details given below apart from interest due: -

(Amount in crore of rupees)

No. of Commissionerates	No. of unregistered courier agencies	Estimated gross receipt	Service tax payable	Penalty
2	94	6.19	0.31	0.31

On this being pointed out (January 2003), Mumbai IV Commissionerate of Central Excise admitted the objection (July 2003).

14.9 Large number of cinema theatres and cable operators providing advertising services outside the tax net

According to clause (3) of section 65 of the Act, advertising agency refers to any commercial concern engaged in providing any service connected with the making, preparation, display or exhibition of advertisement and includes an advertising consultant. The Department of Revenue vide their circular dated 31 October 1996 also clarified that the scope of the service which is included in the tax net extends not only to any service connected with making and preparation of advertisement but also includes any service connected with display or exhibition of advertisement. A cinema theatre or a cable operator, being commercial concern, exhibiting advertisements through his local channel would, therefore, also be required to pay service tax on the income earned by display or exhibition of advertisements in accordance with the definition of 'advertising agency'. On verification of income tax returns of some of the theatres and cable operators, it was revealed that although they had earned income from advertising business, they did not get themselves registered with the Department. The Department also did not make any effort to get this category of advertising agencies under the tax net. This has resulted in evasion of service tax to the extent of Rs.3.85 crore during the period from 1 April 1997 to 31 March 2002 as per details given in the table below: -

(Amount in crore of rupees)

No. of Commissionerates	No. of unregistered cinema owners and cable operators	Gross amount earned through advertising	Service tax payable	Interest	Penalty
11	155	77.09	3.85	0.48	3.85

14.10 Ineffective monitoring of returns required to be furnished by registered service providers

According to the provisions of section 70 of the Finance Act, every person liable to pay service tax was required to file a quarterly return in form ST3 by 15th of the month following the quarter upto October 1998 and thereafter half yearly by 25th of the month following the half year, failure to do so attracting penalty under section 77 subject to a maximum of Rs.1,000 after 16 July 2001.

The position of submission of returns by registered service providers during the period from 1996-97 to 2001-02 is given below in the table: -

14.10.1 Advertising services

(Amount in crore of rupees)

No. of Commis-sionerates	No. of assessees registered	No. of returns due	No. of returns received	No. of returns received by due date	Returns received late	Returns not received	Penalty levied	Amount of penalty not levied
37	19274	39284	32091	28810	3281	7193	0.002	5.14

- 18 per cent of the returns were not received by the Department.
- Penalty was levied only in 3 cases amounting to Rs.20000. Non-levy of penalty amounted to Rs.5.14 crore.
- Test check revealed that in Chandigarh I, Chandigarh II, Bangalore I, Bangalore II, Hyderabad II, Delhi I, Chennai II and Coimbatore Commissionerates of Central Excise, 243 registered service providers did not furnish any return after their registration.

14.10.2 Courier services

(Amount in crore of rupees)

No. of Commis-sionerates	No. of assessees registered	No. of returns due	No. of returns received	No. of returns received by due date	Returns received late	Returns not received	Penalty levied	Amount of penalty not levied
38	19905	45005	36829	32926	3903	8176	0.51	3.57

- 18 per cent of the returns due were not submitted by the registered service providers.
- The deterrent provision of levy of penalty was invoked only in 3 cases for an amount of Rs.51 lakh.
- A test check of the records revealed that in Bangalore I and II and Delhi Commissionerates of Central Excise alone, 718 registered courier agencies did not file any return.

14.11 Escape from payment of tax by non filers

Since the position of non-filers was high, an independent verification of income tax returns of 44 such advertising agencies was made in audit. It was revealed that they had been carrying out advertising activities and received charges for services rendered. Though registered with central excise department for service tax purpose, these assessees did not file their periodical return and evaded tax to the extent of Rs.4.62 crore, besides interest of

Rs.2.61 crore and penalty of Rs.4.62 crore for the period from 1997-98 to 2001-02 as per details given below: -

(Amount in crore of rupees)

No. of Commissionerates	No. of assessees	Gross amount as per IT returns	Service tax payable	Interest	Penalty leviable
12	44	92.38	4.62	2.61	4.62

Some cases are narrated below as illustrations: -

14.11.1 M/s. MCS Communication (P) Limited, in Chennai II Commissionerate of Central Excise, registered as advertising agency did not file any return after registration. Income tax returns of this agency revealed that Rs.32.77 crore was shown as income from advertising for the period from 1996-97 to 2000-01. Service tax to the extent of Rs.1.64 crore was thus evaded by this agency.

14.11.2 M/s. Incoda, Kolkata, in Kolkata-II Commissionerate of Central Excise, though registered with the Department, did not file returns. The examination of the income tax returns revealed that they realised Rs.4.79 crore from their clients on account of advertising charges for the period from April 1997 to March 2001. Service tax of Rs.0.24 crore due thereon was, however, not paid by the agency, nor did the Department take any action for non-submission of return or recovery of tax.

14.12 Assessment procedure not effective to check underassessment

Prior to 16 July 2001, on filing of a quarterly return (form ST3) by the assessee, the central excise officer was required to pass an order in writing assessing the taxable value of service and determining the amount of service tax payable under section 71 ibid. From 16 July 2001 onwards, however, the scheme of self-assessment procedure was introduced under which every person liable for service tax himself assessed the tax and furnished to the superintendent of central excise a half yearly return in form ST3. For the purpose of verification, the superintendent of central excise was empowered to call for any accounts, documents or other evidence from the assessee, as he may deem necessary. Under section 72, the Assistant/Deputy Commissioner was vested with powers to make best judgement assessment after taking into account all the material documents which had been gathered. Section 78 provided for penalty for suppressing value of taxable service.

The position of the assessments finalised by the Department for 1996-97 to 2001-02 in respect of 40 Commissionerates of Central Excise test checked in audit are given below: -

14.12.1 Advertising services

No. of Commissionerates	1.11.1996 to 16.07.2001			After 16.07.2001		
	No. of returns received	Assessed	Pending assessment	No. of returns received	Verified	Pending verification
40	26257	23955	2302	9946	6182	3764

- 9 per cent of the returns prior to 16 July 2001 were still to be assessed by the Department. In Mumbai I Commissionerate of Central Excise in particular 68 per cent were pending.

- After the self assessment procedure with effect from 16 July 2001, there was a marked slackness in the matter of verification, as 38 per cent of the returns were yet to be verified as to the correctness of the amount paid.
- Exercise of assessment/verification by the Department resulted in additional demand for Rs.0.07 crore in 9 cases in Guntur, Trichy, Belgaum, Mangalore and Tirupati Commissionerates of Central Excise, out of which only Rs.31000 was recovered.

14.12.2 Courier services

No. of Commissionerates	1.11.1996 to 16.07.2001			After 16.07.2001		
	No. of returns received	Assessed	Pending assessment	No. of returns received	Verified	Pending verification
38	31507	30374	1133	8943	7882	1061

- 4 per cent of the returns (prior to 16 July 2001) were yet to be assessed by the Department. In Mumbai I Commissionerate of Central Excise 68 per cent (267 out of 390) were pending.
- 12 per cent of the returns (after 16 July 2001) were yet to be verified by the Department as to the correctness of the amount.
- On the basis of assessment/verification additional demand for Rs.17 lakh was raised only in Surat I Commissionerate of Central Excise which was as yet unrecovered.

14.13 Inadequate information in return (ST3) for assessment

In terms of section 70(1) of the Finance Act, 1994 and rule 7 of the Service Tax Rules, 1994, the assessees were required to submit quarterly (half yearly from 16 October 1998) return in form ST3 along with copy of treasury challans (form TR6) in support of service tax paid. As per the proforma of the return, the assessee is only required to give details of value of taxable service charged, value of taxable service realised, amount of service tax payable alongwith the details of payment made to the government credit. The return was not accompanied by any other supporting document like invoices billed to the customers for services rendered or other documents like balance sheet, trading and profit and loss account from which the value of taxable services declared in the form could be cross checked and co-related. Before 16 July 2001, the assessing officer assessed these returns through an assessment memorandum printed in the form itself. The assessment was with reference to arithmetical accuracy for want of any other supporting documents. From 16 July 2001, the Department was to only verify the correctness of the amount self assessed by the service provider on the basis of scant information contained in form ST3.

14.14 Assessment finalized/verification made in a routine manner

Section 71(1) of the Finance Act, 1994, as amended authorised the superintendent to call for additional information/documents and section 72 empowered the Assistant Commissioner/Deputy Commissioner to make best judgement assessment after taking into account all the material documents. These powers were seldom exercised. Additional information was called for only in 426 cases in respect of advertising services in Mumbai III,

Pune I, Pune II, Tirupathi, Guntur, Belgaum and Vishakhapatnam Commissionerates of Central Excise. Additional demands in respect of advertising services under the best judgement assessment was raised only in 5 cases amounting to Rs.0.04 crore in Vishakhapatnam, Guntur and Tirupathi Commissionerates of Central Excise of which no recovery had been made. It was observed that assessments/verification were completed in a routine manner, by accepting whatever the assessee had declared. For instance, four assessees in Hyderabad I Commissionerate of Central Excise paid Rs.0.29 crore less as tax even on the declared gross value of Rs.15.14 crore (Rs.0.76 crore as tax due and Rs.0.47 crore tax paid). The Department did not notice this lapse which came to light during audit.

14.15 Suppression of taxable value by assessees

Sample cross verification of income tax returns and commercial records of 94 advertising agencies and 14 courier agencies was carried out in audit to ascertain the extent of the correctness of the tax paid by the assessees. It was revealed that the assessees were taking recourse to suppressing their taxable value by taking advantage of voluntary compliance and ineffective assessment procedure. The trend of avoidance of tax was further aided by the unwillingness of the assessing officers to make use of the powers vested in them under sections 71(1) and 72. The short payment detected in audit was Rs.8.25 crore in respect of advertising services and Rs.3.15 crore in courier services in addition to interest and penalty leviable as per details given below: -

➢ As per income tax returns

(i) Advertising services

(Amount in crore of rupees)

No. of Commissionerates	No. of service providers	Gross value on which tax not paid	Tax payable	Penalty
17	68	143.19	7.16	7.16

(ii) Courier services

(Amount in crore of rupees)

No. of Commissionerates	No. of service providers	Gross value on which tax not paid as per income tax returns	Tax payable	Penalty
4	8	2.40	0.11	0.11

➢ As per commercial records

(i) Advertising services

(Amount in crore of rupees)

No. of Commissionerates	No. of service providers	Gross value on which tax not paid	Tax payable	Penalty
9	26	21.72	1.09	1.09

(ii) Courier services

(Amount in crore of rupees)

No. of Commissionerates	No. of service providers	Gross value on which tax not paid	Tax payable	Penalty
1	6	60.87	3.04	3.04

Some of the cases are illustrated below: -

14.15.1 M/s. Selvel Advertising (P) Limited, in Kolkata-I Commissionerate of Central Excise, paid service tax of Rs.0.95 crore by showing gross value of the taxable amount as Rs.18.80 crore during the period 1999-2000 and 2000-01 in his ST3 return. A scrutiny of the income tax returns revealed that the assessee had realised an amount of Rs.33.70 crore from his clients on which service tax of Rs.1.69 crore was payable. A sum of Rs.0.74 crore was thus evaded by suppressing the value of taxable amount.

This was pointed out in March 2003, the reply was awaited.

14.15.2 M/s. Hindustan Thompson Limited, an advertising agency in Mumbai I Commissionerate of Central Excise did not pay tax on expenses towards travel and stay in hotel for its employees in connection with advertising although these out of pocket expenses separately recovered from the client were includible in taxable service in terms of the circular dated 31 October 1996. The suppression of gross value of Rs.4.04 crore for the period from April 2000 to March 2002 on this account resulted in short levy of service tax of Rs.0.20 crore. The interest worked out to Rs.0.04 crore.

On this being pointed out (May 2003), the Department replied (August 2003) that it was impracticable for it to obtain the financial accounts of the asssessee for income tax purposes for finalising the assessment of service tax return. It was relying on voluntary compliance by the assessee and assessees follow self assessment procedure. The volume of work with departmental staff was tremendous and written permission had to be obtained each time for issue of notice under section 71 ibid to obtain accounts. Department also stated that the Board and DGST had not suggested that such a course should be adopted in all cases before finalising the assessment.

The reply of the Department is not tenable because the notion of 'voluntary compliance' cannot be allowed by the tax administration to degenerate into a situation whereby tax is evaded/short paid by service providers with impunity. As per the amendments made in the statutory provisions with effect from 16 July 2001, the superintendent of central excise has been empowered to call for any of the documents from the assessee. There is thus no bar on the Department to verify the correctness of tax by scrutiny of other relevant records. Even the DGST in his annual performance report 2001-02 had pointed out that the Commissionerates of Central Excise had shown little interest in cross checking with the income tax returns and assessee's own annual reports/balance sheet.

14.16 Non payment of service tax on the charges received for providing celebrities for advertising

As per section 65(3) of the Finance Act, 1944, advertising agency means any commercial concern engaged in providing any service connected with making preparation, display or exhibition of advertisement and included an advertising consultant.

It was noticed in audit that M/s. Worldtel Sports India and M/s. A B Corporation Limited were engaged by the client companies, including Indian and multinational companies, for providing celebrities as models. As per the conditions of the tripartite agreement between client companies, agencies and the celebrities, the models were to act as brand ambassadors, assist and aid in the advertisement and marketing of products of the client company. The charges for providing celebrities as models for advertising purposes were to be paid by the client companies to these agencies. The agencies, however, did not pay any service tax on the taxable amount received by them as charges from the client companies even though they were engaged in providing services connected with advertising, nor did the Department take any action for recovery of service tax from these agencies.

The non-payment of service tax by the agencies resulted in loss of revenue of Rs.1.68 crore as tax and Rs.1.68 crore as penalty apart from interest as per details given below: -

(Amount in crore of rupees)

Commissi-onerate	Name of the agencies	Gross amount received from client	Service tax payable	Penalty
2	M/s. WorldTel Sports India	9.50	0.48	0.48
	M/s. A B Corporation Limited	24.00	1.20	1.20
	Total	**33.50**	**1.68**	**1.68**

14.17 Lacunae in the instructions of the Board resulting in a class of service providers escaping from the purview of service tax

On obtaining a contract from an advertiser (client) for preparation and exhibition of a film, the job of an advertising agency, inter-alia, consists of preparation of blue print for the film, engagement of a film producer who in turn would engage a model for acting in the film as also the technicians, booking of time and space in a television network and release of a film for exhibition. Though actual 'service' is provided by various persons, for the purpose of levy of service tax all services are to be treated as having been rendered by the advertising agency, as it would have recovered the gross amount from the client.

The Board in their circular dated 31 October 1996 addressed the issue of levy of service tax when a film producer chooses to charge the client directly for the film or documentary. The Board clarified that in such a case the film producer would be liable to pay tax accordingly as he had provided services relating to the advertisement.

It was noticed in audit that although advertising agencies were engaged by client companies, which included multinational companies such as M/s. Pepsi Foods Limited and M/s. Cadbury India for the purpose of preparation of advertisement, celebrities were engaged by these companies separately. The payments were also made by these companies to the celebrities directly as per mutual agreement, the terms of which, inter-alia, included that the celebrity would act as a model for all promotional and advertising material including posing for photographs, tapes, films, etc. and that the models photograph/live shows/illustrations could be utilized in all advertising campaigns and sales promotions material in connection with the product in India or abroad.

The casting of a celebrity as a model in any film is central to the advertisement. The significance of a celebrity in the ad campaign can be gauged from the fact that whereas M/s.

Alliance Media & Entertainment, Mumbai, an advertising agency was paid only Rs.4 lakh towards consultancy fee, the celebrity actress employed for the advertisement was paid Rs.40 lakh for the period from 1 January 1998 to 30 September 2000 by Pepsi Foods Limited directly.

Since their case was akin to that of a film producer charging a client directly for services rendered in relation to advertisement, the Board should have extended such provisions to the celebrities as well.

Such lacunae has resulted in large amount of advertising charges escaping tax net. A test check of the records of only six client companies revealed these companies had made payment directly to celebrities for Rs.19.37 crore. The tax forgone was Rs.0.96 crore as per details given below: -

(Amount in crore of rupees)

No. of Commissionerates	No. of celebrities	Gross amount paid by client to celebrities	Service tax forgone
4	11	19.37	0.96

14.18 Non payment of interest on delayed payment of service tax by courier agency

As per section 75 of the Finance Act, 1994, if a person liable to pay service tax in accordance with section 68 or rules made thereunder fails to credit the tax or any part thereof to the account of central government within the prescribed period, he shall pay simple interest by which such crediting of the tax or any part thereof is delayed.

M/s. Sky Pak Services Limited (courier services) was initially registered in Mumbai I Commissionerate of Central Excise in May 1998 but did not file the service tax returns from 1998 onwards nor did they pay any service tax. The Service Tax Cell of Mumbai I Commissionerate of Central Excise also did not issue any notice. The company paid service tax from April 1998 onwards in August, 2002 when it applied for fresh registration with Mumbai IV Commissionerate of Central Excise. However the interest from May 1998 to August 2002 on account of delay in crediting tax to government, which worked out to Rs.14 lakh, was not recovered by the Department.

On being pointed out (April 2003), the Department admitted the objection and reported recovery of Rs.7 lakh.

14.19 Non payment of service tax on the services provided to Centre/State government

The Board vide their notifications dated 22 January, 1998 (as amended) and 24 April 1998 exempted advertising agencies from payment of service tax in respect of service rendered to diplomatic missions, United Nations or an International Organisation.

Nine advertising agencies, in Ahmedabad I Commissionerate of Central Excise, did not pay service tax on the amount of Rs.18.35 crore towards services rendered to various central/state government treating their cases as eligible for exemption. The Department did not take any

action for recovery of service tax. Service tax and penalty of Rs.92 lakh each was forgone apart from interest of Rs.52 lakh.

On this being pointed out (April 2003), the Department stated (April 2003) that show cause notice to all the assessees for the period from 1997-98 to 2001-02 had been issued.

14.20 Conclusion

Given the magnitude of tax escaping the net a proactive and vigorous approach needs to be adopted to widen the tax base. The ineffieient internal control mechanism for monitoring of the submission of returns by registered assessees and near complete reliance on the returns filed by the assessee, has encouraged wilful evasion of tax. In order to make the verification meaningful and effective, the assessing officers need to take frequent recourse to the powers vested in them under sections 71(1) and 72 of Finance Act. Ineffective administration in these two services has thus resulted in realisation of only a small proportion of the gross value of the services actually provided. The underlying ethos of voluntary compliance has, therefore, to be reviewed.

The above observations were pointed out in October 2003; reply of the Ministry had not been received (February 2004).

CHAPTER XV : NON LEVY/SHORT LEVY OF SERVICE TAX

15.1 Non payment of service tax

15.1.1 Consulting engineers

Under section 66 of the Finance Act, 1994 read with notification dated 2 July 1997, service tax is leviable with effect from 7 July 1997 on the gross amount charged by consulting engineers on services rendered by them to their customers. Clause 13 of section 65 ibid defines a consulting engineer as any professionally qualified engineer or an engineering firm who either directly or indirectly renders any advice, consultancy or technical assistance in any manner to a client in one or more disciplines of engineering.

(a) M/s. Electronic Corporation of India Limited, in Hyderabad III Commissionerate of Central Excise, engaged in the manufacture of electronic systems/goods and parts thereof in various divisions also rendered engineering services which inter alia covered, technical assistance with regard to feasibility study, pre design and preparation of project reports, basic engineering design, detailed design engineering, supervision, commissioning, initial operation and integration of systems, trouble shooting and other technical services including establishing systems and procedures, maintenance of various project systems etc. Though these activities fell within the ambit of the definition of consulting engineers services, the assessees had neither got themselves registered with the Department as required under rule 4(1) of Service Tax Rules, 1994 nor paid service tax or filed periodical returns as laid down under rules 6 and 7 of Service Tax Rules. The assessee realised Rs.140.72 crore during the years 1997-98 to 1999-2000 but service tax of Rs.7.04 crore payable thereon was not paid.

On this being pointed out (August 1999 and January 2001), the Ministry of Finance (the Ministry) admitted the objection and intimated (December 2003) issue of a show cause notice for Rs.9.77 crore for the period from 7 July 1997 to March 2002.

(b) M/s. Flex Engineering Limited, in Noida Commissionerate of Central Excise, received an amount of Rs.9.25 crore during the year 2000-01 towards technical services rendered by them. Service tax of Rs.46.25 lakh leviable on such technical service charges was not levied.

On this being pointed out (December 2002 and March 2003), the Ministry admitted the objection (October 2003).

(c) Test check of records of M/s. V.A. Tech Escher Wyes Florel Limited, M/s. Escorts Limited and M/s. Fib Com India Limited, in Delhi III and IV Commissionerates of Central Excise, engaged in manufacture of plant and machineries revealed that the assessees realised an amount of Rs.9.12 crore between January and March 2003 from various customers on account of erection and commissioning of plants and machineries including maintenance. Though such services were liable to service tax under the heading 'consulting engineer', service tax of Rs.45.60 lakh due thereon was not levied.

On this being pointed out (March 2003), the Ministry admitted the objection and intimated (December 2003) issue of show cause notices amounting to Rs.16.11 lakh in 2 cases.

(d) Test check of records of fifteen assessees in eleven Commissionerates of Central Excise, revealed that these assessees received an amount of Rs.43.33 crore between July 1997 and March 2002 towards advice, consultancy, erection, testing and technical services rendered by them. Service tax of Rs.2.17 crore was not levied.

On this being pointed out (December 2001 and May 2002), the Ministry while accepting the objection in thirteen cases (between July and November 2003) intimated issue of show cause notices for Rs.1.76 crore. In one case the Ministry stated (January 2004) that a show cause notice demanding Rs.37.86 lakh had been issued in April 2003 but the matter was under review in consultation with the Ministry of Law, in the light of the Tribunal's ruling regarding leviability of tax on works contracts under engineering projects. Reply in the remaining case had not been received (February 2004).

15.1.2 Clearing and forwarding agents

According to sections 65(12), 65(41), 66 and 67 of the Finance Act, 1994 (as amended by subsequent Finance Acts) read with notification dated 11 July 1997, service provided by a clearing and forwarding agent is chargeable to service tax. Clearing and forwarding agent has been defined as any person who is engaged in providing any service, either directly or indirectly, connected with the clearing and forwarding operations in any manner to any other person and includes consignment agent. Service tax on the value of services was payable by the recipients of such services till 31 August 1999. Thereafter it was payable by the service providers.

(a) Test check of records revealed that M/s. Ford India Limited, in Chennai III Commissionerate of Central Excise, manufacturing passenger cars (heading 8703.90), engaged the services of a company to undertake on their behalf the entire activity of export viz., receipt of materials, inventory control, sequence packing and stuffing into container for shipping from the packing plant of the assessee. Similarly, another company was entrusted with the distribution of spare parts i.e. order processing, packing, handling, shipping, invoicing etc. from the spare parts warehouse of the assessee. Audit pointed out (November 2001, January and April 2002) that as all these activities constitute service under the category of clearing and forwarding agents, service tax of Rs.66.45 lakh for the period from June 2000 to October 2001 was payable by such service providers.

The Ministry admitted the objection (December 2003).

(b) M/s. Ram Shree Steels Private Limited, Orai, in Kanpur Commissionerate of Central Excise, collected an amount of Rs.3.99 crore as commission from customers for providing services on account of procurement of orders/raw materials, arranging sales, etc., during the period 1999-2000 to 2000-01. Though, such services were liable to tax under heading 'clearing and forwarding agents', service tax of Rs.19.95 lakh due thereon was not levied.

This was pointed out in May 2002 and April 2003; reply of the Ministry/the Department had not been received (February 2004).

15.1.3 Management consultant

Services of management consultants has been brought under service tax net with effect from 16 October 1998. As per section 65(21) of the Finance Act 1994, 'management consultant' means any person who is engaged in providing any service, either directly or indirectly, in

connection with the management of any organisation in any manner and includes any person who renders any advice, consultancy or technical assistance relating to conceptualising, devising, development, modification, rectification or upgradation of any working system of any organisation.

M/s. Sterlite Optical Technologies Limited, in Daman Commissionerate of Central Excise and M/s. Telephone Cables Limited, in Chandigarh Commissionerate of Central Excise, collected Rs.9.93 crore as fee for providing management services/rendering services for the development of export activity between April 1999 and March 2002. Though such services were covered under the ambit of management consultancy, service tax of Rs.49.62 lakh leviable thereon was not paid.

On this being pointed out (September 2002), the Ministry admitted the objection (August and November 2003) and intimated issue of show cause notice for Rs.42.48 lakh to M/s. Sterlite Optical Technologies Limited.

15.1.4 Doordarshan and All India Radio

Test check of records of Doordarshan Kendra, Chennai, in Chennai II Commissionerate of Central Excise, revealed that the assessee rendered broadcasting service for the period from 16 July 2001 to March 2003. The assessee collected service tax for the services rendered from September 2002 to March 2003 and forwarded the amount to Doordarshan Kendra, New Delhi for depositing to Government account. The assessee however, had not paid service tax of Rs.51.53 lakh on the value of taxable service of Rs.10.30 crore for the period 16 July 2001 to August 2002.

Similarly, All India Radio, Chennai in the same Commissionerate had rendered broadcasting services for a value of Rs.10.57 crore during the period from July 2001 to March 2003. Though they were registered with the central excise department, they had not paid service tax of Rs.52.83 lakh due and had also not filed the periodical returns to the Department.

On the non-raising of demand of service tax from the two service providers being pointed out (May 2003), the Ministry stated (December 2003) that as per Board's letter dated 27 March 2003, Prasar Bharati Corporation (Doordarshan and All India Radio) was not liable to pay service tax.

Reply of the Ministry is not tenable as the Board in its earlier circular dated 9 July 2001 had clarified that Prasar Bharati Corporation (Doordarshan and All India Radio) was liable to pay service tax. The clarification of the Board dated 27 March 2003 was not retrospective. Further, the Board in its circular dated 14 July 2003 withdrew its instructions of 27 March 2003 and reverted to the earlier position of 9 July 2001. Since no specific exemption vide any notification was available for the broadcasting service provided by these organizations during the period in question, service tax was recoverable with interest. Further, Doordarshan Kendra, New Delhi stated (October 2003) that they had not collected service tax on broadcasting services till March 2003. Hence, the actual remittances to government account of the amount collected by Doordarshan Kendra, Chennai could not be confirmed.

15.2 Non-levy of service tax on services rendered by foreign service providers

The Finance Act, 1994 and the Service Tax Rules, 1994 framed thereunder did not provide for a mechanism for collection of service tax on taxable service rendered in India by a person

who is a non resident or is from outside India who does not have any office in India. Rule 6 of the Service Tax Rules, 1994 as amended with effect from 28 February 1999 provides that where a person liable to service tax is a non-resident or is from outside India, such a person shall pay service tax by demand draft alongwith the return prescribed within 30 days from the date of raising the bill on the client for taxable service rendered.

15.2.1 Consulting engineers

Service tax has been imposed on services rendered by consulting engineers with effect from 7 July 1997.

Test check of records of 51 assessees in 18 Commissionerates of Central Excise, revealed that they availed services falling under the category of 'consulting engineers' from foreign consultants and paid service charges of Rs.217.75 crore between July 1997 and November 2002. Since service had been rendered in India service tax of Rs.10.87 crore was payable but had not been demanded by the Department. In the case of 26 assessees, it was seen that income tax had, in fact, been deducted at source before releasing payment to foreign consultants.

The Ministry admitted the objection in forty five cases and stated (between September and December 2003) that show cause notices demanding tax of Rs.5.93 crore had been issued to ten assessees of which Rs.1.23 lakh had been recovered. Reply in the remaining cases had not been received (February 2004).

15.2.2 Management consultants

Service tax on services provided by management consultants has been imposed with effect from 16 October 1998.

A test check of records of eleven assessees in Delhi, Pune I and Noida Commissionerates of Central Excise, revealed that service charges of Rs.185.78 crore were paid to foreign consultants for services of 'management consultancy' between October 1998 and March 2003. Since, the said services were rendered in India, service tax amounting to Rs.9.29 crore was leviable on such services, which was not paid.

The Ministry admitted the objection (between August and December 2003).

15.2.3 Eight assessees in Goa and Trivandrum Commissionerates of Central Excise, received services of 'engineering consultancy' and 'management consultancy' from foreign consultants and paid service charges of Rs.58.39 crore in foreign currency between July 1997 and December 2002. As the services were rendered in India, tax amounting to Rs.2.92 crore was leviable on such services. Although income tax and other taxes were deducted at source before releasing payment to the foreign consultants, service tax was not recovered and paid to the government.

On this being pointed out (between September 2002 and March 2003), the Ministry admitted the objection (October and December 2003).

15.3 Non-recovery of service tax

Under the Finance Act, 1994, service tax is payable by the service provider. Service tax on services rendered by 'clearing and forwarding agents' and 'transport operators' has been levied with effect from 11 July 1997 and 16 November 1997 respectively. Service Tax Rules

provided for recovery of service tax in these cases from the recipients of services. The Supreme Court in case of Laghu Udyog Bharti {1999 (112) ELT 365 (SC)} ruled that the recipients of services cannot be made liable to pay service tax and that the Service Tax Rules made in this regard are ultra vires the Finance Act, 1994. The Finance Act, 1994, was amended with retrospective effect vide section 117 of the Finance Act, 2000 to provide service tax recovery from the recipient of the service in case of clearing and forwarding agents for the period from 16 July 1997 to 31 August 1999 and in the case of goods transport operators from 16 November 1997 to 1 June 1998.

15.3.1 Goods transport operators

(a) Test check of records of twenty assessees in eight Commissionerates of Central Excise, revealed that they did not pay service tax of Rs.3.08 crore on freight charges paid to goods transport operators, during the period 16 November 1997 to 1 June 1998. No action was taken by the Department for recovery of service tax.

The Ministry admitted (between May and December 2003) the objection in all cases and reported issue of show cause notices for Rs.2.13 crore in seventeen cases out of which demand of Rs.80.10 lakh was confirmed and Rs.0.52 lakh recovered.

(b) M/s. Dalmia Cement, in Tiruchirapalli Commissionerate of Central Excise, had availed the services of goods transport operators but did not pay tax of Rs.36.15 lakh for the period from March 1998 to May 1998. Service tax of Rs.15.88 lakh paid for the period from November 1997 to February 1998 was refunded by transferring the amount and crediting it to Consumer Welfare Fund. This was not credited to government account even after enactment of the Finance Act, 2000.

On this being pointed out (January 2001), the Ministry admitted the objection and intimated issue of show cause notice for Rs.36.15 lakh.

15.3.2 Clearing and forwarding agents

Test check of records of six assessees in Aurangabad, Mumbai VI, Pune I and II and Trichirapalli Commissionerates of Central Excise, revealed that though these assessees engaged the services of clearing and forwarding agents and paid service charges of Rs.8.49 crore to them, they did not pay service tax on the service charges so paid. The Department did not take action to recover service tax of Rs.42.49 lakh during the period between 16 July 1997 and 31 August 1999.

The Ministry admitted the objection in all cases (between September and December 2003).

15.4 Short payment of service tax

M/s. Bharti Cellular Limited, New Delhi, in Delhi I Commissionerate of Central Excise, engaged in providing cellular phone services to its subscribers and in selling SIM cards to activate the device, realised an amount of Rs.337.04 crore for rendering services to subscribers as shown in the profit and loss account of the company for the year 1999-2000. Test check revealed that the assessee paid service tax of only Rs.16.50 crore as against Rs.16.85 crore payable thereon. Service tax short paid amounting to Rs.35 lakh was not demanded by the Department.

On this being pointed out (November 2002), the Ministry admitted the objection (December 2003).

15.5 Non-realisation of interest on delayed payment of service tax

Service rendered by goods transport operators was made liable to service tax vide Finance Act, 1997. The Supreme Court in the case of M/s. Laghu Udyog Bharti held that the provisions of rule 2(1)(d)(ii) and (xvii) making the user of the goods transport service responsible for payment of service tax, were ultra vires of the Finance Act. By section 116 and 117 of the Finance Act, 2000, users of services of goods transport operators were made responsible for recovery of service tax retrospectively from 16 November 1997. The Tribunal in the cases of M/s. Ruby Woollen (P) Limited {2002 (103) ECR 323(T)} and M/s. Shree Ganapati Synthetics and others {2002 (103) ECR 176 (T)} held that service tax along with interest became payable retrospectively as per section 116 and 117 of the Finance Act, 2000.

M/s. Century Cement, Baikunth, in Raipur Commissionerate of Central Excise, engaged in the manufacture of cement clinker and cement used the services of goods transport operators during the period 16 November 1997 to 1 June 1998. Service tax amounting to Rs.23.66 lakh due on these services was paid on 9 June 2000. Interest of Rs.9.52 lakh for delayed payment of service tax was not paid.

On this being pointed out (September 2001), the Ministry stated (September 2003) that interest was not recoverable till enactment of the Finance Act, 2000 on 12 May 2000. The reply of the Ministry is not tenable as payment of interest for the relevant period was obligatory under section 75 of the Finance Act, 1994 read with section 117 of the Finance Act, 2000 as held in the judgements cited supra.

15.6 Other cases

In 9 other cases of non-levy of service tax, the Ministry/the Department had accepted objections involving duty of Rs.2.06 crore and reported recovery of Rs.2.06 crore till February 2004.

Minakshi Ghose

New Delhi
Dated : 1 April 2004

(MINAKSHI GHOSE)
Principal Director (Indirect Taxes)

Countersigned

New Delhi
Dated : 1 April 2004

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