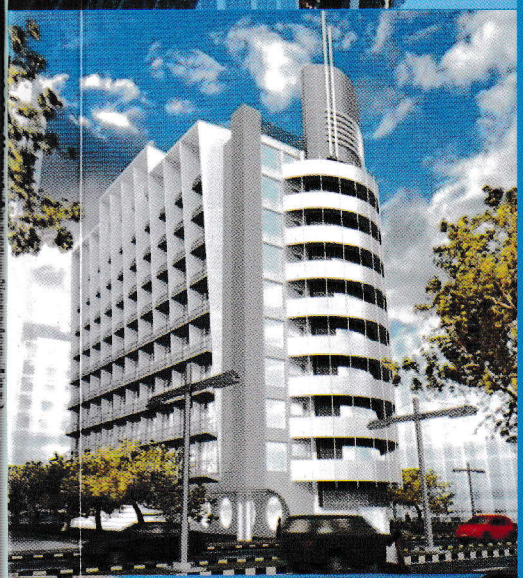

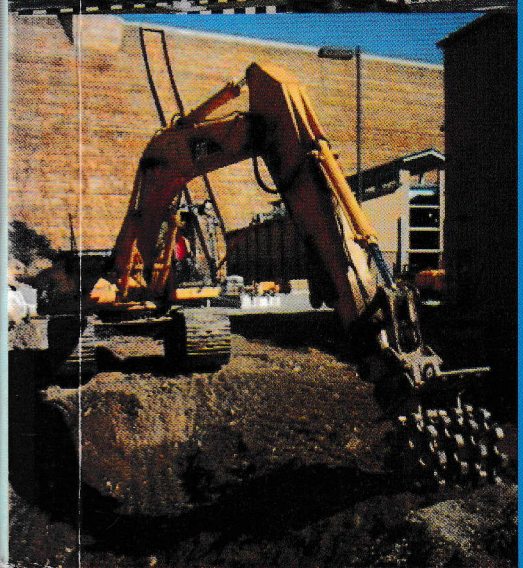

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Report of the Comptroller and Auditor General of India

PERFORMANCE AUDIT OF SERVICE TAX ON CONSTRUCTION SERVICES

Union Government
(Indirect Taxes - Service Tax)
(Performance Audit)
No. 25 of 2010-11

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PREFACE

This Report for the year ended March 2009 has been prepared for submission to the President of India under Article 151(1) of the Constitution of India.

Audit of Revenue Receipts – Indirect Taxes of the Union Government is conducted under the Section 16 of the Comptroller and Auditor General of India (Duties, Powers and Conditions of Service) Act, 1971.

The observations included in this Report have been selected from the findings of a performance audit carried out during the year 2008-09 and covered the collection of revenue during the period 2005-06 to 2007-08.

The results of our audit alongwith recommendations are contained in this Report.

EXECUTIVE SUMMARY

We conducted a performance audit to evaluate the adequacy of provisions of the Finance Act, 1994, Service Tax Rules and related instructions in ensuring proper levy, assessment and collection of service tax on three construction services viz. Commercial or industrial construction services, Construction of complex (residential) services and Works contract services.

We found procedural deficiencies in registration of assessees, receipt of returns, scrutiny of returns, ambiguities/inadequacy in rule provisions and compliance weaknesses. While the total financial implication of this audit intervention was ₹ 1477.19 crore, the direct additional revenue which could come to the Government was ₹ 766.95 crore. Observations with money value of ₹ 66.97 crore had been accepted by the department and ₹ 9.73 crore recovered.

The key findings and related recommendations were: -

- We found that commissionerates had not fixed any target for surveys by its ranges to identify unregistered service providers. Where some surveys had taken place, the outcome was not monitored as prescribed in DGST circular dated 26 May 2003.
- We identified 3535 service providers who had provided these three services and were liable to pay service tax but were not available on the departmental registration lists. We found that 2234 of these potential assessees were liable to pay service tax of ₹ 181.54 crore.
- We recommended that the department needed to take up various measures prescribed by the DGST and work in close liaison with Departments of the State Governments who regularly availed construction services and other services.

(Paragraph 2.1)

- The information furnished by the department showed that 12 per cent of service tax returns were received late and 31 per cent of the returns were not received at all. We found 145 assessees in 10 commissionerates, who had not filed their service tax returns and not paid service tax of ₹ 14.73 crore.

(Paragraphs 2.3.1 and 2.3.2)

- We found 158 cases in 32 commissionerates where the departmental officers had scrutinised the returns but failed to detect irregularities which had led to short levy of service tax totalling ₹ 17.48 crore.

(Paragraph 2.4.2)

- We found, through cross verification of service tax returns with income tax returns and other records maintained by assessees, that 255 assessees had evaded service tax of ₹ 110.08 crore by suppression of assessable value.

(Paragraph 2.4.3)

- We recommended that mechanisms for monitoring the receipt of returns and scrutiny of returns were required to be streamlined so that timely action was taken to pursue and resolve exceptions and deviations.

(Paragraph 2.4)

- We found that very expensive and large residential units were constructed without payment of tax because of the condition that service tax was payable on construction of complex (residential) service only when the construction involved more than 12 residential units.
- We recommended that the Government could consider supplementing the single criterion of 'more than 12 units' with additional criterion so that expensive constructions with less than 12 units were also brought into the service tax net.

(Paragraph 2.6)

- We found that cenvat credit of duty on capital goods and service tax on input services could be availed for WCS composition scheme whereas those were disallowed for CCS/CON abatement scheme.
- We recommended that the Government could consider inserting a clause in the WCS composition scheme to disallow the availing of cenvat credit on capital goods and input services.

(Paragraph 2.7)

- We found instances of non compliance to rules and provisions on irregular availing of abatement and exemption, non-payment of service tax on advance payment, land owner share of the apartment, import of service, incorrect classification, non-remittance of service tax, incorrect/excess availing and utilisation of cenvat credit resulting in revenue impact of ₹ 766.95 crore.

(Chapters III to X)

CHAPTER I
INTRODUCTION

1.1 Construction Services-a brief description

The construction industry is one of the biggest in the world and contributes around ten per cent to the global GDP. It also provides work to almost seven per cent of the total persons employed worldwide. This industry is the cornerstone of industrial and infrastructural development and constructs real estate properties (both residential and commercial), roads, railways, bridges, tunnels, airports, dams, canals etc.

In India, construction has accounted for around 40 per cent of the development investment in the past 50 years. The Indian construction industry employs over three crore people (16 per cent of the nation's working population) and creates assets worth over ₹ 20,000 crore. It contributes more than 5 per cent to the nation's GDP and 78 per cent to the gross capital formation.

Service Tax has been imposed on a total of 108 services through Finance Act, 1994 as amended from time to time upto Finance Act, 2008. Out of these 108 services, three pertain to construction related activities and all of them have been covered in this review. The service tax on construction services had been levied by the Finance Act, 2004, with effect from 10 September 2004. The Finance Act, 2005, enlarged the scope and renamed it as 'commercial or industrial construction services' and introduced another service called construction of complex (residential) services. The service tax on works contract services was introduced by the Finance Act, 2007. The services of commercial or industrial construction services, construction of complex (residential) services and execution of works contract services have been referred to hereafter by the acronyms of 'CCS', 'CON' and 'WCS'. The scope of these services has been expanded from time to time through changes/amendments in the Finance Acts.

1.2 Why we chose the topic

There has been a spurt in construction of commercial, industrial and residential buildings due to a resurgent Indian economy in the last decade. Large constructions are being taken up in urban areas and a large numbers of building firms have mushroomed in the last few years. Therefore, this sector has a rapidly widening tax base with large potential for increasing service tax revenue. We decided to take up a system appraisal of the administration of service tax in this sector in view of the substantial revenue implications.

1.3 Audit objectives

The audit review was conducted to seek assurance that: -

- the mechanism to identify and bring in potential assessees in tax net for levy of service tax was effective;

- tax administration was efficient and effective in ensuring compliance with the applicable legislations and rules; and
- the internal controls were in place and effective.

1.4 Organisational structure

The Central Board of Excise and Customs is the Chief Executive Authority for administering the service tax. It administers service tax through six commissionerates which exclusively deal with service tax and another 66 commissionerates which administer both central excise and service tax.

The Directorate General (Service Tax) is a body constituted by Government of India in 1997 to centralize the work of service tax which was expanding speedily by coverage of more and more services under the service tax net. This body was constituted to ensure that proper establishment and infrastructure could be created under different central excise and service tax commissionerates to monitor the assessment and collection of service tax.

1.5 Scope of audit and methodology

We test checked the records relating to these selected services in all six exclusive service tax commissionerates and in 55 out of the total of 66 commissionerates dealing with both service tax and central excise. The period covered under audit was from the year 2005-06 to 2007-08. We had also collected some statistical data from the remaining 11 commissionerates where we had not conducted any test check.

1.6 Response of the department

We acknowledge the cooperation extended by the Ministry of Finance and most of the field formations in providing the necessary information and records during the conduct of this audit. However, 12 commissionerates did not provide some items of information to us. The reasons for not being able to furnish the information were also not communicated. These were noticeable aberrations as other commissionerates were able to provide the same information. Details of these commissionerates are given in paragraphs 2.5 and 2.8. The draft report containing the audit findings and recommendations was issued to the Ministry in October 2010. The audit recommendations and some of the audit findings were discussed in an exit conference held on 2 December 2010 with the officers of the Ministry. The responses have been incorporated appropriately in the report. The written reply to the draft report was awaited (December 2010).

CHAPTER II
FINDINGS ON SYSTEMS, RULES, REGULATIONS AND INTERNAL CONTROLS

We have arranged the audit findings in this chapter under two sections. Section A contains findings on procedural deficiencies in registration of assessees, receipt of returns and scrutiny of returns. Section B covers ambiguities and inadequacy in rule provisions which result in foregoing of revenue. The relevant provision of Act/Rules is highlighted in a box at the beginning of the audit observation. Certain illustrative cases have been used to highlight the issues.

SECTION A: PROCEDURAL DEFICIENCIES

2.1 Registration

Every person liable to pay service tax has to apply for registration within a period of 30 days from the date of commencement of his business.

For registration of eligible service providers, the Government has relied largely on 'voluntary compliance' and an entity can evade tax by not applying for a registration. The Director General of Service Tax (DGST), Mumbai had in May 2003, issued a comprehensive action plan to monitor the administration of service tax.

It had identified field survey as one of the important mechanisms in the action plan to identify potential assessees and broaden the tax base. The circular had suggested a performance monitoring system. Every range officer was to be entrusted with the job of doing surveys to identify potential service tax assessees in his jurisdiction and report the outcome every fortnight to their commissionerates through the divisional offices.

In our earlier performance audit reports on Management consultant's services, Scientific or technical consultancy services, technical testing and analysis services and Technical inspection and certification (March 2006), Rent-a-cab scheme operators' services, Photography services and Health club and fitness centre services (March 2007) and Business auxiliary services (March 2008) we had commented on the inadequacy and ineffectiveness of surveys undertaken by the department. Our findings in this review are quite similar.

The 61 commissionerates test checked in audit had not fixed any targets for survey by its ranges during 2006-07 to 2007-08. Where some surveys had taken place, the outcome was not monitored as prescribed in the DGST circular dated 26 May 2003. No surveys were conducted in 29 out of 61 commissionerates, including four out of six exclusive service tax commissionerates. Out of 32 commissionerates where surveys were conducted, 22 commissionerates stated that 583 new service providers (for construction services) were registered through surveys resulting in additional revenue of ₹ 15.05 crore during the year 2006-07 to 2007-08. No new service

providers could be registered through surveys for these services in remaining 11 commissionerates. It was evident that a lot more had to be done by the department in this area.

We attempted, on a limited scale, to identify unregistered service providers who were liable to pay tax. For this purpose, we identified entities who had provided services to various departments of State and Central Government, Nigams/Corporation and PSUs. We also identified service providers by scrutinising returns in the Income Tax department and other secondary records in various Government departments. We found that in 41 out of 61 commissionerates, there were 3535 service providers for these three services, who, though liable to pay service tax, were not available on the departmental registration lists. As already stated in the previous sub-paragraph, 22 commissionerates had registered 583 service providers through surveys conducted in April 2006 to March 2008 and we found 898 unregistered service providers in the same 22 commissionerates during April 2008 to March 2009. This showed that there was ample scope to step up the efforts to identify the assessees.

We attempted to quantify the extent of evasion by these identified potential assesses. We were able to obtain data from various sources such as income tax returns (496 cases), payments made for construction contracts by CPWD (321 cases), various State Housing Boards (328 cases), records of registered contractors who availed services of sub-contractors (372 cases), agriculture marketing board (140 cases) and other sources (577 cases) for 2234 service providers out of 3535 identified by us. We found that these potential assessees had not paid service tax to the extent of ₹ 181.54 crore. This also implied additional penalty upto ₹ 181.54 crore with further interest liability of ₹ 37.10 crore. All these cases require further detailed verification by the department. Some could be cases where the service providers are doing central billing and are, therefore, registered with some other commissionerate. The department had confirmed 27 cases of non registration upto December 2010 which had a revenue implication of ₹ 4.04 crore.

2.2 Creation of database

Under Rule 4(5) of Service Tax Rules, 1994, an application received for registration for service tax should be processed and verified and a certificate of registration should be issued within seven days from the date of receipt of the application by the Superintendent of Range.

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DGST instructed in 2001 that a database of these applications was to be created in each commissionerate wherein the assessee's profile could be comprehensively captured, as it would facilitate cross-referencing.

The information furnished by the department showed that the profiles of 20 per cent registered assessees had not been created in the databases. Therefore the cross linkage of service tax related information furnished by the assessee with records of other Government Departments could not be done for these assessees.

Recommendation Nos. 1 to 2

- *The department needs to take up various measures prescribed by the DGST, including surveys, to identify potential assessees for service tax and get them registered. It should also work in close liaison with Public Works Department, Stamps and Registration Department, Registrar of Companies and Commercial Taxes Department of the State Governments who regularly avail construction services and many other services.*

In the exit conference, the Board stated that surveys were primarily done when a new service was introduced. For construction services, the secondary methods recommended by DGST and audit would be more effective. However, the service tax wing is hampered by severe shortage of staff and the focus is therefore on anti-evasion and internal audit. The Board was considering a cadre restructuring and some of the core issues like identification of assessees would be taken up with greater focus after such re-structuring.

- *The department needs to complete the assessee profile databases to facilitate cross verification.*

In the exit conference, the Board stated that with the introduction of ACES, all new assessees had to mandatorily register through the system and this would automatically capture the complete assessee profiles in future.

2.3 Monitoring of receipt of service tax returns

Every person liable to pay service tax has to assess and pay his own tax. He has to furnish half yearly returns to the department. A person failing to furnish timely returns is liable to pay a penalty subject to a maximum of one thousand rupees.

The scrutiny of returns is one of the critical tools for effective administration of service tax and to guard against risk of evasion by registered service providers. It, therefore, follows that the regular receipt of returns from all service providers is to be monitored by the department.

2.3.1 Receipt of returns

The information furnished by the department showed that a large number of returns were either not received or received late but the department had not taken any corrective action. The position of receipt of returns by the department is shown in the following table: -

Table No. 1

Name of service	No. of returns due	No. of returns received	Returns received by due date	Returns received late	No. of returns not received	Penalty levied for late submission	Penalty not levied @ ₹ 1000/- per return
						(Lakh of rupees)	
CCS	49852[1]	34154	30005	4149	15698	19	179
CON	22175[2]	15802	13849	1953	6373	12	71
WCS	6175[3]	3701	3116	585	2474	3	28
Total	**78202**	**53657**	**46970**	**6687**	**24545**	**34**	**278**
Percentage of returns due				12	31		

The above data relates to 72 commissionerates.

- The table shows that 12 per cent of returns were received late and 31 per cent of the returns were not received at all. We found that the test checked commissionerates had not followed any monitoring mechanism to ascertain the reasons for non-submission of returns.
- The Government had exempted small service providers delivering taxable service upto ₹ 4 lakh from payment of service tax from 1 April 2005. This limit was increased to ₹ 8 lakh from 1 April 2007. Amongst the returns not received, we found 366 service providers, whose annual receipts of CCS and CON had exceeded ₹ four lakh during the year 2005-06, but they had not submitted the returns for the year 2006-07. Similarly, 530 service providers whose annual receipt of CCS and CON had exceeded ₹ eight lakh during the year 2006-07, had not submitted the returns for the year 2007-08. The department had not taken any action to ascertain whether the value of services provided had fallen below exemption limits for these assessees or they had stopped filing returns to evade payment of tax. Thus, it did not know why these service providers had abruptly stopped filing returns.
- The levy of penalty for delayed submission and non submission of returns serves as a deterrent but the department did not impose penalty of ₹ 2.78 crore on defaulting assessees. This amount was 89 per cent of the total amount leviable (₹ 3.12 crore).

2.3.2 Registered service providers who have stopped filing returns

We did an independent verification, on a limited scale, of income tax returns and other connected records of some of the registered service providers who had stopped filing returns for service tax. We found 145 assessees in 10 commissionerates, who had not filed their service tax returns, but had continued to provide services during the period of non-filing. This resulted in non-payment of service tax of ₹ 14.73 crore. Total interest of ₹ 3.07 crore and

[1] From the date of levy (10 September 2004) to March 2008
[2] From the date of levy (16 June 2005) to March 2008
[3] From the date of levy (1 June 2007) to March 2008

penalty upto ₹ 14.73 crore was also leviable. Some illustrative cases are mentioned in the table below: -

Table No. 2

(Amount in lakh of rupees)

Sl. No.	Commissi-onerate	Name of Assessee	Revenue effect			Source of data
			Tax	Interest	Penalty	
1.	Jaipur II	M/s. Kamal Engineers and Contractor Pvt. Ltd.	62	13	62	IT return
2.	Bhubaneshwar I	M/s Metro Builders Orissa (Pvt.) Ltd	46	18	46	IT return
3.	Nagpur	M/s Gupta Construction	22	5	22	Records of co-contractor

2.4 Scrutiny of returns

The authority to conduct scrutiny of returns is provided in Rule 5A of the Service Tax Rules, 1994 which authorises the Commissioner to empower any officer to carry out 'Scrutiny, verification and checks, as may be necessary to safeguard the interest of revenue'. The Rule also allows such an officer to call for any record maintained by the assessee for scrutinising the return to determine the correctness of the assessments made. The Board has also issued guidelines vide letter F.No.137/27/2007 CX.4, dated 8 February 2007, which makes it mandatory to scrutinise returns on a regular basis. The guidelines clearly envisaged that returns' scrutiny would become the core function of the Service Tax Ranges.

2.4.1 The compiled departmental data for all 72 commissionerates for the year 2007-08 showed that 28 per cent of the returns received for these three services (received: 30090 verified: 21758) were pending preliminary verification/scrutiny.

2.4.2 We also found 158 cases in 32 commissionerates where the departmental officers had scrutinised the returns but failed to detect irregularities like payment of service tax at lower rate, non-levy of interest and penalty, short payment of interest, etc. which had led to short levy of service tax totalling ₹ 17.48 crore. Interest of ₹ 2.38 crore and penalty upto ₹ 6.23 crore was also leviable in these cases. Of these, the department had accepted audit observations involving revenue of ₹ 3.18 crore and had recovered ₹ 2.69 crore and issued SCNs for ₹ 51.94 lakh. Two illustrative cases are given below: -

- Under the WC composition scheme, service tax was payable at the rate of two per cent of the gross amount charged which was enhanced to four per cent from March 2008. M/s. Larsen & Toubro Ltd, in Division-III of Kolkata ST commissionerate, paid service tax at lower rate in respect of WCS for the period from 1 March 2008 to September 2008 although the rate of service tax had been enhanced. This had resulted in short payment

of service tax of ₹ 2.52 crore. The assessee was also liable to pay interest of ₹ 25.42 lakh and penalty of ₹ 46.93 lakh.

This was pointed out in February 2009, the reply of the department was awaited (December 2010).

- Similarly, M/s. Gannon Dunkerlay & Co. Ltd., in Division-I of Kolkata ST commissionerate, paid service tax at the rate of 10 per cent instead of 12 per cent applicable from 18 April 2006. This led to short payment of service tax of ₹ 29.00 lakh for the period from April 2006 to March 2008.The assessee was also liable to pay interest of ₹ 9.82 lakh and penalty of ₹ 19.96 lakh.

This was pointed out in December 2008, the reply of the department was awaited (December 2010).

2.4.3 We did a cross verification of ST returns with income tax returns and other records maintained by assessees. We found that 255 assessees (in 35 commissionerates) had evaded service tax of ₹ 110.08 crore by suppression of value assessable for tax during the period from September 2004 to March 2008. Interest of ₹ 25.97 crore and penalty upto ₹ 109.16 crore was also leviable in these cases:-

Some illustrative cases are mentioned in the following table: -

Table No. 3

(Amount in lakh of rupees)

Sl. No.	Commissi-onerate	Name of Assessee	Revenue effect			Source of detection
			Tax	Interest	Penalty	
1.	Nagpur	M/s. Sunil Hitech Engineers Ltd.	179.32	16.02	179.32	Scrutiny of records of service tax payment
2.	Meerut II	M/s. Alliance Builders	170.24	31.98	170.24	Comparison with IT return
3.	Bangalore ST	M/s IDEB Projects Pvt. Ltd.	162	59.28	162	Scrutiny of ledger account
4.	Delhi ST	M/s B.L. Kashyap & Sons (P) Ltd	724	354	724	Scrutiny of ST-3 return and other financial records

The replies of the department were awaited (December 2010).

2.5 List of books of accounts not filed

Rule 5 (2) of Service Tax Rules, 1994, stipulates that every assessee shall furnish to the superintendent of central excise at the time of filing his return for the first time, a list of books of accounts maintained by the assessee in relation to service tax.

The shortfall in receipt of details of books of accounts for the period from September 2004 to March 2008 in 61 out of all 72 commissionerates, is shown below:-

Table No. 4

Name of service	No. of returns received from service providers for the first time	No. of first returns where details of books of accounts not received	Percentage
CCS	12603	7426	58.92
CON	5796	3871	66.78
WCS	2317	902	38.92
Total	**20716**	**12199**	**58.88**

We observed that fifty nine per cent of service providers had not given the details of books of accounts maintained by them. During the period from September 2004 to March 2008, in 17 commissionerates, not a single assessee had submitted the list of books of accounts at the time of filing of returns for the first time in respect of CCS. The Commissionerates had not pursued these cases to ascertain the reasons for non-submission of these details. Eleven commissionerates[4] did not provide the data relating to accounts details being filed with the first ST return despite repeated pursuance for over six months.

Recommendation No. 3

- *The mechanisms for monitoring the receipt of returns and scrutiny of returns is required to be streamlined so that timely action is taken to pursue and resolve exceptions and deviations.*

During the exit conference, the Board stated that receipt and scrutiny of returns often did not get adequate attention because the officers in ranges were overburdened with multifarious tasks. It was stated that, with the introduction of ACES, these procedures had been automated and could be strengthened further after cadre restructuring.

SECTION B: RULES, REGULATIONS AND SYSTEMS

2.6 Exemption on construction of residential complexes having less than 12 residential units

According to Finance Act, 1994, service tax is leviable for construction of residential complexes comprising a building or buildings, having more than 12 residential units. They must also be located within premises having a common area, facilities such as park, lift, common water supply and the layout of such premises should be approved by appropriate authority.

The condition that service tax is payable only when the construction involves more than 12 residential units, ensures that small housing construction projects remain outside the tax net and only the larger projects are taxed. We found two projects where expensive flats were constructed with large plinth areas but

[4] Hyderabad IV, Raipur, Delhi ST, Rohtak,, Belgaum, Mangalore, Mysore, Bolpur, Haldia, Siliguri, Chennai ST

were not liable to be taxed as they had less than 12 residential units. These are given below:-

2.6.1 M/s Vijay Shanti Builders Ltd., Chennai, in Chennai ST commissionerate, engaged in CON, constructed three residential units with total plinth area of 15000 square feet (5000 sq. ft. per unit) at a cost of ₹ 9.90 crore (₹ 3.30 crore per unit). The assessee availed service tax exemption as the numbers of residential units was less than 12. The revenue foregone was ₹ 40.38 lakh.

2.6.2 M/s Gina Engineering Pvt. Ltd., Bangalore, in Bangalore I commissionerate, had constructed an apartment for M/s Purvankara Projects Pvt. Ltd., 'Purve Grande'. No service tax had been paid on this project as the number of residential units was only eight. However, the floor area of each unit in the apartment ranged from 3339 to 3862 square feet, and the selling price of the units ranged from ₹ 6.34 crore to ₹ 7.34 crore.

Since these expensive projects are staying out of the tax net, we feel that the single criterion of 12 units is not sufficient and other criterion, such as selling price or plinth area per unit should also be specified to ensure that expensive constructions come under the tax net.

This was pointed out in April 2009, in both the cases, the department stated (July 2009) that this was a policy matter.

Recommendation No. 4

- *The Government may consider supplementing the single criterion of 'more than 12 units' with additional criterion so that expensive constructions with less than 12 units are also brought into the service tax net.*

In the exit conference, the Board stated that introduction of value bases criteria would increase subjectivity and interpretation issues would creep in leading to more litigation.

2.7 Variation in admissibility of Cenvat credit in composition/abatement schemes

A service provider delivering WCS has to pay Sales Tax/VAT on the goods components of the contract and service tax on the service components of the contract at the prevailing rate. Under the Composition Scheme for payment of Service Tax on WCS effective from 1 June 2007, he has the option to pay two per cent (effective from 1 June 2007 to 28 February 2008 and revised to four per cent thereafter) of the gross amount charged for the works contract, excluding value added tax/sales tax. Service providers opting for this scheme cannot take cenvat credit on inputs.

A service provider delivering CCS and CON services has to pay service tax on the gross value of services provided if he avails cenvat credit of duty on inputs, capital goods and input services. He also has the option to avail abatement of 67 per cent and pay tax on 33 per cent of gross value if he does not take any cenvat credit on inputs or capital goods or input services. This translates to an effective rate of 3.96 per cent of the gross value.

A comparison of the optional composition/abatement schemes shows that the effective rate of service tax is almost the same for WCS (4 per cent) and CCS/CON (3.96 per cent) as percentage of gross value. However there is a significant difference between the two because cenvat credit of duty on capital goods and service tax on input services can be availed for WCS whereas these are disallowed for CCS/CON. This has introduced some degree of inequity between services within the construction sector.

We found that M/s Ahluwalia Contracts (India) Ltd and M/s Aksava Infrastructure Private Ltd, in Service Tax division, Gurgaon (Delhi III) commissionerate, realised an amount of ₹ 98.94 crore and paid service tax of ₹ 2.18 crore under composition scheme for various projects during 2007-08. They also availed Cenvat credit of ₹ 29.78 lakh on input services which would not have been available for services under CCS/CON while availing abatement scheme. Therefore, the effective revenue collection was lower in WCS by ₹ 29.78 lakh as compared to similar CCS/CON service.

This was pointed out in March 2009, the reply of the department was awaited (December 2010).

Recommendation No. 5

- *The Government may consider inserting a clause in the WCS composition scheme to disallow the availing of Cenvat credit on capital goods and input services.*

During the exit conference, the Board stated that the effective rate for CCS/CON had reduced further as the service tax rate had reduced to 10 per cent from 12 per cent while the WCS composition rate had remained at 4 per cent. This had brought parity between the two schemes even though the conditions for allowing cenvat credit were different.

2.8 Time limit for adjudicating service tax cases not prescribed

Section 73 of Finance Act, 1994, through which service tax was introduced, provides that SCNs in normal/fraud cases must be issued within one/five years for recovery of service tax short levied. These provisions are similar to section 11A of Central Excise Act.

Section 11A also prescribes a time-limit of six months/one year, where it is possible to do so, for finalisation of adjudication cases relating to central excise receipts, whereas time limit for adjudication of service tax cases has not been incorporated in section 73 or in any other rules. Therefore, the adjudication officers are not obliged to finalise SCNs relating to service tax within a prescribed time frame. This contributes to delays in finalisation of cases and recovery of service tax.

The information furnished by the department showed that there was no pendency in adjudication of SCNs in 34 commissionerates. However, in 30 commissionerates, 1744 SCNs relating to service tax on CCS and CON, involving revenue of ₹ 54.74 crore, were pending (as on 30 September 2008) for adjudication. Of these, 137 SCNs involving revenue of ₹ 3.27 crore were

pending for more than two years. Eight commissionerates[5] did not provide data relating to pendency of adjudication of SCNs.

Recommendation No. 6

- *The Government should prescribe a time-limit for adjudicating SCNs alongwith suitable mechanism to monitor the time limit.*

During the exit conference, the Board stated that the time limit in central excise was only recommendatory and the real problem was the large number of adjudications which could not be handled by the existing set up. This was sought to be addressed through the cadre restructuring which would enhance the number of exclusive service tax commissionerates and separate formations were also being contemplated exclusively for doing adjudications.

[5]Patna, Rohtak, Belgaum, Mangalore, Mysore, Bolpur, Haldia and Siliguri

CHAPTER III
ABATEMENT

3.1 Abatement

As per departmental notifications for CON/CCS, the service provider has the option to claim abatement of 67 per cent of the gross amount charged and pay tax on the balance, provided he has not availed cenvat credit for inputs or capital goods or input services.

We observed irregular availing of abatement resulting in short payment of service tax of ₹ 170.44 crore in 127 cases. Interest of ₹ 13.53 crore and penalty upto ₹ 170.34 crore is also leviable in these cases. Some of the cases are cited by way of illustrations.

3.1.1 Simultaneous availing of cenvat credit and abatement

3.1.1.1 M/s Della Technica & Interior Designers Construction Pvt Ltd., in Division I of Mumbai commissionerate, had availed the benefit of 67 per cent abatement as per the above notification in respect of all projects while simultaneously availing cenvat credit of service tax paid on input services, during the period from March 2006 to March 2008. In view of the proviso to the notification, the benefit of abatement was not available to the assessee and tax was payable on the gross value of the contracts. This resulted in short payment of service tax by ₹ 7.59 crore, including interest.

On this being pointed out by us, the department accepted the audit observation and intimated that SCN for ₹ 6.36 crore had been issued and the assessee had agreed to pay the balance of ₹ 30.38 lakh.

3.1.1.2 Similarly in another case M/s Shapoorji Pallonji & Co. Ltd, in Delhi ST commissionerate, availed abatement as well as cenvat credit on inputs during the period April 2006 to March 2007. This resulted in short payment of service tax of ₹ 1.75 crore. Besides, interest of ₹ 45.47 lakh and penalty upto ₹ 1.75 crore were also leviable.

When we pointed this out in August 2008, the department replied (April 2010) that assessee had stated that in projects where abatement was taken, cenvat credit had not been taken. The department did not verify the reply of assessee before replying to the audit observation. This reply could not be verified by us as the project wise details of cases wherein abatement was taken was not furnished.

Details of some more cases are tabulated below: -

Table No. 5

(Amount in lakh of rupees)

Sl. No.	Name of Assessee & Commissionerate	Period during which abatement taken	Also availed cenvat credit on	Short payment of service tax	Interest	Penalty
1.	M/s ALSTOM Projects India Pvt. Ltd. in Delhi ST	04/2006 to 03/2007	Input Service	329.76	60.73	329.76
2.	M/s B L Kashyap & Sons in Delhi ST	04/2006 to 10/2007	Input Service	226.10	58.79	226.10
3.	M/s Larsen & Toubro Ltd. (ECC Division) in Chennai ST	10/2005 to 03/2006	Input Service	361.70	141.06	361.70
Total				**866.36**	**247.29**	**866.36**

Replies of the department in respect of cases at Sl. No. 1 and 2 were awaited (December 2010). In respect of the case at Sl. No. 3 on being pointed out (May 2009), the department replied that upto February 2006, the assessee availed and utilised cenvat credit under notification dated 10 September 2004 and utilised the balance cenvat credit during March 2006.

The reply of department was not acceptable for the reasons (i) abatement was available to the assessee if no cenvat credit is availed on inputs, capital goods or input services; (ii) the assessee had no unutilised/accumulated credit at the end of February 2006, and (iii) the condition for availing abatement notification was not fulfilled.

3.1.2 Value of goods and material not included in gross value of service

When service tax is paid on abated value, the quantum of abatement is calculated on the gross amount charged which has to include the value of goods and material supplied or provided or used for providing the taxable service by the service provider.

3.1.2.1 M/s B.P. Construction, Bhiwadi in Jaipur I commissionerate provided CCS services to M/s. Gems Cab Industrial, Bhiwadi, a manufacturer engaged in manufacture of insulated wire and cable and paid service tax of ₹ 6.94 lakh on abated value of service charges of ₹ 212.41 lakh. Scrutiny of records revealed that the cost of materials supplied by the manufacturer amounting to ₹ 255.03 lakh was not included into the gross receipt for charging service tax which led short payment of service tax ₹ 9.90 lakh. Interest of ₹ 4.28 lakh is also leviable under section 75 of Finance Act.

On this being pointed out (July 2009), the department reported (March 2010) recovery of service tax of ₹ 9.90 lakh and interest of ₹ 3 lakh. It was also intimated that efforts are being made to recover the balance interest of ₹ 1.28 lakh.

3.1.2.2 M/s. Kunnel Engineers and Contractors, Ernakulam, in Cochin commissionerate, provider of CCS, CON and WCS had also provided services as sub contractor. As a sub contactor, the assessee availed abatement but did not add the value of raw material provided free of cost by main contractor/builder. This resulted in reduction of the gross amount charged and

consequent reduction in abated value on which tax was paid. Therefore, the assessee was liable to pay additional service tax after adding the value of free goods and re-working the abatement and tax payable.

In other similar cases involving M/s. National Building Construction Ltd. (site office at Kohra) and M/s Kirloskar Brothers Ltd. both in Raipur commissionerate and M/s L&T Limited (ECC Division), M/s B R Kohli Construction Pvt. Ltd. and M/s Toyota Construction Company in Hyderabad II, Delhi ST and Nagpur commissionerates respectively, abatement was taken without adding value of material received free of cost.

3.1.3 Incorrect availing of abatement on completion and finishing service

The abatement of 67 per cent cannot be taken if the taxable services provided are of the nature of completion and finishing service in relation to building, civil structure or residential complex.

In the following case, the assessee availed the benefit of abatement, which was inadmissible.

M/s Nitson & Amitsu Pvt Ltd, in Division-III of Kolkata ST commissionerate, engaged in providing CCS as well as CON, had provided 'completion and finishing' job viz. glazing, metal joinery & carpentry, painting, wall covering etc. of buildings or civil structures and residential complex. The assessee availed the benefit of abatement which was not admissible. This resulted in short payment of service tax ₹ 2.98 crore during the period from April 2006 to March 2008. The assessee was also liable to pay interest of ₹ 32.75 lakh and penalty of ₹ 2.98 crore.

This was pointed out in December 2008, the reply of the department was awaited (December 2010).

Other cases are tabulated below where abatement was taken on similar completion and finishing services.

Table No. 6

(Amount in lakh of rupees)

Name of Assessee & Commissionerate	**Period during which abatement taken**	**Short payment of service tax**	**Interest**	**Penalty**
M/s Likproof in Mumbai ST	04/2005 to 03/2008	265.30	34.49	265.30
M/s Lloyds Insulations India Ltd. In Mumbai III	04/2005 to 03/2008	114.42	14.87	114.42
M./s Jayant Furnishers in Mumbai III	04/2005 to 03/2008	88.82	11.55	88.82
M/s Aline Curtain Walls Pvt. Ltd. In Kolkata ST	04/2005 to 03/2008	151.45	39.80	151.45
M/s Millennium Constructions Pvt. Ltd. In Delhi ST	04/2006 to 03/2008	98.72	12.83	98.72
Total		**718.71**	**113.54**	**718.71**

When we pointed this out, in the case of M/s. Likproof, the department accepted the audit observation and intimated that SCN has been issued to both the assessees.

The replies of the department in the remaining three cases were awaited (December 2010).

3.1.4 Incorrect availing of abatement on site formation and clearance service

The abatement of 67 per cent is applicable only to CCS and CON and not to "site formation and clearance, excavation and earthmoving and demolition services."

3.1.4.1 M/s Inkor Auto Tech India (P) Ltd., in Chennai (Service Tax) commissionerate, had executed exclusive site preparation work during April 2007 to March 2008 and classified the works under CCS and availed of abatement which was inadmissible. This resulted in short payment of tax of ₹ 71.69 lakh.

This observation was pointed out to the department in May 2009. The reply was awaited (December 2010).

3.1.4.2 Similarly M/s Subrahamanyan Construction Co (P) Ltd. (B-Division), in Chennai commissionerate, also executed exclusive site preparation work during April 2007 to March 2008 and classified the works under CCS and availed the abatement which was not in order. This resulted in short payment of tax of ₹ 14.07 lakh.

On this being pointed out (May 2009), the department replied (July 2009), that the assessee had carried out work in stages. As per Board's clarification in paragraph 3.2 of the letter dated 28 February 2006, a composite service even if it consists of more than one service should be treated as single service based on the main or principle service.

The reply of the department was not acceptable because the clarification mentioned by the department was only applicable for Composite work order. In the instant case the assessee received work orders for different works and one among those orders was 'site formation and clearance'. Hence Board's clarification could not be applied in the instant case.

3.2 Ambiguity on availing of cenvat credit on capital goods under abatement scheme

As per departmental notifications for CON/CCS, a service provider has the option to claim abatement of 67 per cent of the gross amount charged and pay tax on the balance, provided he has not availed cenvat credit for inputs or capital goods or input services.

M/s. Consolidated Construction Consortium Ltd., in Chennai ST commissionerate, paid tax on gross value for some contracts and availed cenvat credit. For other contracts, it paid tax on abated value. For these

contracts it did not avail cenvat credit on input/input services. However, it availed cenvat credit of ₹ 51.69 lakh on capital goods which were used for both kinds of contracts i.e. those with ST paid on full value as well as contracts under abatement scheme and cenvat credit of ₹ 129.90 lakh on capital goods used exclusively in abatement contracts. Since Cenvat credit had been availed, the benefit of abatement was not admissible. This resulted in non-payment of ST of ₹ 55.93 crore on the abated value. Interest of ₹ 13.45 crore and penalty of ₹ 55.93 crore were also payable.

The department stated in reply that since the assessee had neither availed nor utilised the cenvat credit in respect of contracts in which they had discharged duty under the abatement scheme, the credit availed by the assessee in respect of contracts where they had paid tax at full rate was in order. Therefore, the question of demanding tax did not arise.

The reply of the department was factually incorrect, because the assessee had himself intimated the department through letter dated 21 June 2007 that it had availed cenvat credit of ₹ 51.69 lakh on capital goods used for both abatement and gross value contracts and availed credit of ₹ 129.90 lakh on capital goods used exclusively for abatement contracts.

CHAPTER IV
EXEMPTION

4.1 Exemption

The services provided for construction of roads, airport, railways, transport terminals, bridges, tunnel and dam are not included in any of three construction services i.e. WCS, CCS and CON.

We observed irregular availing of exemption resulting in short payment of service tax of ₹ 19.24 crore in 15 cases. Interest of ₹ 3.11 crore and penalty of ₹ 19.24 crore is also leviable in these cases.

4.1.1 EPC project relating to canal work

Works contract services includes engineering, procurement and construction or commissioning (EPC) projects and the services rendered in connection with such projects are liable for service tax. M/s Lanco Infratech Ltd and M/s Larsen & Toubro Ltd (ECC Division), in Hyderabad II Commissionerate, executed EPC projects relating to canal works for irrigation projects undertaken by Government of Andhra Pradesh but these assessees did not discharge service tax liability on gross consideration of ₹ 62.61 crore and ₹ 272.66 crore respectively received by them during the period July 2007 to March 2008 treating the project exempted from levy of service tax. The service tax payable under composite scheme was not paid by M/s Lanco Infratech Ltd and M/s Larsen & Toubro Ltd was of ₹ 1.65 crore and ₹ 5.62 crore respectively. These assessees were also liable to pay interest of ₹ 94.45 lakh and penalty of ₹ 7.27 crore.

On this being pointed out by us (September 2008 and February 2009), the department accepted the audit observation and reported (December 2008) that SCN for ₹ 1.93 crore had been issued to M/s Lanco Infratech Ltd. The action taken in the case of M/s Larsen & Toubro Ltd had not been reported (December 2010).

4.1.2 M/s Lanco Infratech Ltd, in Hyderabad II Commissionerate, entered into contracts for construction of power projects and did not discharge service tax liability on the works relating to roads, dams, dam facilities, associated works, tunnels, bridges, etc. being constructed for the power project on the ground that they fall outside the scope of definition of CCS. This is incorrect as these works were undertaken in relation to setting up of power projects. Service tax of ₹ 7.73 crore was not paid during the period 2005-06 to 2007-08. The assessee was also liable to pay interest of ₹ 1.70 crore and penalty upto ₹ 7.73 crore. The observation was pointed out to the department in September 2008. The reply was awaited (December 2010).

4.2 Road works

The Board has clarified that if a contract for the construction of a commercial complex is a single contract and the construction of road is not recognised as a separate activity as per the contract, then the Service Tax would be leviable on gross amount charged for construction including the value of construction of roads.

Scrutiny of the contract agreement entered between M/s Jai Prakash Enterprises, assessee in Delhi ST commissionerate, and M/s Jay Pee Greens Limited in August 2004 revealed that the assessee had entered into a comprehensive agreement for development of nine Hole Golf Course and public park at Greater Noida at a total contract price of ₹ 76.72 crore and the construction of road was not recognised as a separate activity. The assessee, however, availed irregular exemption of ₹ 24.40 crore on account of construction of road during the period September 2004 to March 2008. This resulted in short payment of Service Tax of ₹ 99.53 lakh. Interest of ₹ 12.94 lakh and penalty upto ₹ 99.53 lakh were also leviable.

This was pointed out in March 2009, the reply of the department was awaited (December 2010).

4.3 Misclassification of components

Similarly, M/s Ramky Infrastructure Limited (Pharma city), in Visakhapatnam II commissionerate, entered into an agreement with M/s Ramky Pharma City (India) Limited, for construction of Pharma City and did not pay service tax on value of consideration of ₹ 61.14 crore received during the period September 2004 to March 2008 on certain components such as landscaping and arboriculture, roads and site grading etc. relating to the same work. As these components were executed in connection with construction of the single complex i.e. Pharma City, the entire work as a whole was taxable and tax exemption was not available on the components. Hence, service tax of ₹ 2.30 crore was payable. The assessee was also liable to pay interest of ₹ 29.91 lakh and penalty of ₹ 2.30 crore.

CHAPTER V
ADVANCE

5. Service tax on advance payments

As per amended rule provisions applicable from 16 June 2005 when payment relatable to taxable services are received during the course of provision of service, service tax is liable to be paid to the extent of receipt of payment. In other words, a person is liable to pay service tax as soon as the consideration towards the taxable services is received.

5.1 We found instances where service tax was not paid on advances received.

- During 2005-06 to 2007-08 M/s Larsen and Toubro Ltd., in Kolkata ST commissionerate, received advance payment for CCS from M/s Bhusan Steel & Strips Ltd., M/s Tata Steel Ltd. and M/s NTPC etc. It did not pay applicable service tax of ₹ 18.13 crore on receiving the advances.
- During April 2007 to February 2008 M/s. Larsen & Toubro Ltd. in Ahmedabad ST commissionerate, received advances of ₹ 35.01 crore for CCS and ₹ 160.80 crore for WCS. It did not pay applicable service tax of ₹ 7.63 crore on receiving the advances.

  When we pointed this out (April 2009), the department (Ahmedabad ST commissionerate) reported (August 2009) that two SCNs for non payment of service tax of ₹ 16.72 crore and ₹ 6.88 crore had been issued.
- M/s Tarapore and Company, in Jamshedpur commissionerate, received advances of ₹ 1.05 crore and ₹ 95.70 lakh in November 2006 and February 2007 respectively for providing CCS. It did not pay service tax of ₹ 24.78 lakh.
- M/s Anant Raj Construction & Developers Pvt. Ltd., registered under WCS, in Delhi commissionerate, formed on 4 October 2007, with a paid up capital of ₹ 50 lakh, as a wholly owned subsidiary company of M/s Anant Raj Industries Ltd for the purpose of providing WCS to their holding company for construction of various Building/civil structures. The assessee received amounts from its holding company and accounted for them under the head 'Loan', which amounted to ₹ 57.11 crore as on 31 March 2008. These "loans" were actually advances received from holding company because as per contract the assessee was provided advances for supply of goods and construction work. By treating the advances as loans, they did not pay service tax of ₹ 2.33 crore.

The department replied (February, 2009) in respect of the second case that the assessee had stated that he was discharging his service tax liability on the adjustment bills issued after executing the work. The reply of the assessee confirmed that it was not complying with the provisions of the Act on the advances received. In respect of the fourth case, department replied (April 2010) that SCN had been issued to the assessee.

In all the above cases, the department had to ascertain the time period between the receipt of the advance and dates when the service tax was paid against these amounts. This represented the delay in payment for which interest had to be charged. In case some part of tax had not been paid, it had to be recovered with appropriate interest and penalty.

5.2 Short payment of Service tax on advance as a result of change in rate of duty

The Board clarified in July 2005 that, when advance payment is received for a service which is non-taxable at the time of receipt of payment but becomes taxable during the course of provision of service, such payment would have to be apportioned appropriately between the two periods and that part of service provided on or after the service becomes taxable services, is only liable for service tax. Similarly, when payment is received in advance for services to be provided but subsequently the services are not actually provided, then in such cases service tax paid is liable to be refunded.

It follows that such apportioning has also to be done in case of advance payments received for a taxable service on which service tax has been paid at the prevailing rate and the rate of service tax is enhanced subsequently, while the services being provided. Service tax is payable at enhanced rates on the amount of advance payment which relates to the service provided after date of enhancement.

We found from the ST-3 returns of two service providers of CCS and WCS, M/s Bharat Heavy Electrical Ltd (BHEL) (PSWR), Nagpur and M/s Sunil Hitech Engineers Ltd, in Nagpur commissionerate, that they had received advance payment of ₹ 72.01 crore and ₹ 34.97 crore during the periods June 2005 to April 2006 and September 2007 to February 2008 respectively for services to be provided. Out of these amounts, ₹ 4.03 crore and ₹ 34.18 crore respectively could be adjusted till the date of enhancement of rate of service tax under CCS (18.4.2006) and WCS (1.3.2008) respectively. The balance of advance of ₹ 68.77 crore, service was rendered by the assessees after the date of enhancement of rate of service tax. However the assessees paid the service tax on the entire advance at pre-revised rates and did not pay the differential service tax after date of enhancement of rates. This resulted in short payment of service tax of ₹ 1.40 crore (₹ 1.39 crore and ₹ 1.62 lakh). Interest of ₹ 54.09 lakh was also payable.

On this being pointed out by us (March 2008 and February 2009), the department replied (July 2008 and February 2009) in the case of M/s Bharat Heavy Electrical Ltd (BHEL) that there was no provision to demand service tax at enhanced rate, for which service was rendered after the date from which the rate of tax was enhanced.

Reply of the department was not tenable in view of Board's clarification of July 2005.

CHAPTER VI
LAND OWNER'S SHARE

6. Service tax liability on the land owner's share of apartment

Section 67(ii) of the Finance Act, 1994 (as amended) provides for payment of service tax on money or "consideration" received for providing the service. Explanation below the section provides that "consideration" includes any amount that is payable for the taxable services provided or to be provided. Rule 3(a) of the Service Tax (Determination of Value) Rules defines criteria for determining the equivalent money value of such consideration received, where the value cannot be determined otherwise.

We have studied the category of construction where a developer constructs buildings and transfers them free of cost because he receives a consideration in return. This is the form of a right to construct more buildings on same tract of land which does not belong to him and thereafter he sells the constructed property. As per definition in the Finance Act, this consideration is liable to service tax as it is received by the person providing taxable services of CON/CCS to the person who receives the cost free constructed premises.

We found several cases where contractors received considerations in the form of right to use land and sell but did not pay service tax on these considerations.

6.1 We observed that M/s Gopalan Enterprises Pvt. Ltd., in Bangalore ST commissionerate, engaged in CCS, was paying service tax on the consideration on land usage received from the land owner. While calculating the amount of consideration, the assessee had considered only the proportionate built up area pertaining to land owner's portion. However, the remaining portion of the land on which the assessee had constructed flats and the portion which had been developed as common area were also a part of the project. Therefore, that land was also a part of the consideration but the assessee did not add the value of that portion of land. Consequently, the assessee paid service tax of ₹ 13.55 lakh against ₹ 1.33 crore payable. This resulted in short payment of ₹ 1.19 crore. The assessee was also liable to pay interest of ₹ 15.47 lakh and penalty of ₹ 1.19 crore.

6.2 M/s Shyamaraju & Co. Pvt. Ltd in Bangalore ST commissionerate, had not paid service tax of ₹ 51.39 lakh on the consideration received towards the land valued at ₹ 12.47 crore. The assessee was also liable to pay interest of ₹ 6.68 lakh and penalty upto ₹ 51.39 lakh.

6.3 M/s. Almark Housing Co. (P) Ltd. Ernakulam, in Cochin commissionerate, engaged in developing properties and constructing multi storied buildings entered into agreements with the land owners, where the properties of land owner were developed and multi storied buildings for residential as well as commercial complexes were constructed by the company. In consideration, a specified portion of the constructed building

was to be handed over to the land owner. Thus, the company was providing services to independent customers as well as the land owner by constructing commercial or residential complexes in the properties of the land owner. However, the assessee paid service tax only on the amount received from the customers. The gross value of the buildings handed over to the land owner amounted to ₹ 36.40 crore during 2007-08 and the non-payment of service tax amounted to ₹ 1.48 crore on the net taxable value of ₹ 12.01 crore after allowing abatement of 67 per cent on the gross value. The assessee was also liable to pay interest of ₹ 19.41 lakh and penalty upto ₹ 1.48 crore.

6.4 In Mumbai, Slum Rehabilitation Authority (SRA) was set up in 1995 to rehabilitate the 'slums' as identified by the State Government. To rehabilitate the slums, an agreement is signed by the builder/contractor with each slum dweller authorising the builder to develop the said slum plot where the builder/contractor constructs a building in the said plot and after its completion, dwelling units of specific carpet areas are allocated free of cost to each slum dweller.

In return, the builder/contractor gets the right to develop dwelling units at the same plot and sell them in open market or he gets the Transfer Development Right (TDR) in another area, which can be consumed by the builder himself or could be sold to another builder.

Details were obtained from SRA in respect of TDR of 563912 sq. mtrs. recommended for 94 builders/contractors during the year 2006-07 and 2007-08. The TDR rate in Mumbai during December 2007 was around ₹ 2500/- per sq. ft. Thus the value of such TDR worked out to ₹ 1517.47 crore, on which service tax of ₹ 60.09 crore was payable after allowing the admissible abatement, which was not paid by the builders/contractors.

CHAPTER VII
INCORRECT CLASSIFICATION OF SERVICE

7.1 Switchover to WCS composition scheme

While introducing the new service WCS through the Finance Act, with effect from 1 June 2007, the Government also introduced a composite scheme from the same date. It provided an option to service provider to pay service tax at the rate of two per cent (raised to four per cent with effect from 1 March 2008) on the gross amount charged for the works contract.

The Board clarified in January 2008 that a service provider who had paid service tax prior to 1 June 2007 for the taxable services provided on contracts for erection, commissioning or installation services, CCS or CON, as the case may be, was not entitled to change the classification of the same contract on or after 1 June 2007 and were not entitled to avail the composition scheme under WCS.

We identified 60 cases where the service providers had paid service tax under CCS and CON contracts before 1 June 2007. After 1 June 2007, they treated all these ongoing contracts as WCS and paid tax @ 2 per cent under composition scheme. This kind of switchover was irregular. This resulted in short payment of service tax of ₹ 95.74 crore, interest of ₹ 14.56 crore and penalty upto ₹ 95.74 crore could be levied.

In one such case, M/s Lanco Infratech Ltd, in Hyderabad II commissionerate, engaged in providing CCS paid service tax under this service up to May 2007 but started paying service tax at 2 per cent under WCS for the ongoing works with effect from 1 June 2007 even though such change over was not permissible. The assessee provided CCS of ₹ 229.99 crore during the period July 2007 to March 2008 and was liable to pay service tax of ₹ 9.34 crore on ₹ 75.57 crore i.e. 33 per cent of the amount of service provided but paid service tax of ₹ 1.56 crore only. Thus, there was short payment of ₹ 7.78 crore due to the incorrect classification.

On this being pointed out by us (March 2008), the department accepted (November 2008) the observation and stated that SCN for ₹ 7.78 crore along with interest and penalty had been issued.

Some other similar cases are tabulated below:-

Table No. 7

(Amount in lakh of rupees)

Assessee and commissionerate	Total value of service provided after 1 June 2007	Tax payable under CCS/CON	Tax actually paid by treating under WCS	Short payment		
				ST	Interest	Penalty
M/s. Ahluwalia Contract (India) Ltd. In Noida	5929	733	122	611	79	611
M/s. JMC Projects India Ltd. in Ahmedabad ST	17448	712	360	352	46	352
M/s. Millenium Construction (Private) Limited in Gurgaon	6036	246	187	59	8	59
M/s. Jayant Furnishers in Mumbai ST	2124	263	44	219	28	219
M/s. Subhash Project and Marketing in Kolkata ST	216	87	44	43	13	43
M/s Essar Construction India Ltd, in Rajkot	15463	1893	319	1574	409	1574

7.2 Input credit taken under composition scheme

A service provider who opts for the Works' Contract Composition Scheme is not permitted to take cenvat credit of duties or cess paid on any inputs used in contract.

M/s. Rohan Builders (India) Pvt. Ltd, in Pune III commissionerate, paid service tax of ₹ 26.67 lakh under Works Contract Composition Scheme for a project of M/s Suessen Asia, Satara. We, found that the assessee had availed cenvat credit on inputs used for project and was ineligible for the composition scheme. He was liable to pay service tax of ₹ 1.60 crore at the rate applicable for CCS on the total receipt of ₹ 12.95 crore.

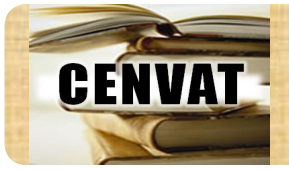
This resulted in short payment of ₹ 1.33 crore and interest of ₹ 13.48 lakh.

7.3 Evasion of service tax due to treating of service as sale

A works contract consists of two components, transfer of property in goods and works contract services provided. Where VAT or Sales Tax has been paid on the actual value of transfer of property in goods, this actual value shall be deducted from the total amount of the works contract to determine the value of services provided under the contract.

M/s Anant Raj Construction & Development Pvt. Ltd., was registered under WCS in Delhi ST commissionerate, for the period 2007-08. We found that it got some items of work done by sub contractors such as providing & laying of cement concrete of specified strength prepared through batch plant and providing of centring and shuttering done by sub-contractors. The sub-contractors charged works contract tax from the assessee in lieu of VAT/Sales Tax under composition scheme of VAT/Sales Tax. The assessee took cenvat credit of input service for the tax paid to the sub-contractors. Thereafter, the assessee treated these works as a sale of material to the final users and did not pay any service tax. The total value of such works aggregated to ₹ 6.94 crore. It was clear that this work done by the sub contractors included goods and services and could not be treated as a sale by the assessee. Since the sub contractors had charged the assessee under composite scheme of VAT/Sales Tax, the value of goods and the services had not been segregated and the assessee had to pay service tax of ₹ 29.74 lakh under WCS. This resulted in short payment of service tax of ₹ 29.74 lakh. Besides, interest of ₹ 11.72 lakh and penalty were also recoverable.

When we pointed this out (March 2009), the department replied (April 2010) that SCN had been issued.



CHAPTER VIII
CENVAT CREDIT

8. Cenvat credit

A provider of taxable services can, in terms of rule 4 of the Cenvat Credit Rules, 2004, avail credit of excise duty paid on inputs and capital goods and service tax paid on any input service. The credit can be utilised towards payment of service tax subject to the fulfillment of certain conditions.

We observed incorrect and excess availing and utilisation of cenvat credit totalling ₹ 26.46 crore, by providers of CCS, CON and WCS in 41 cases. Interest of ₹ 90.80 lakh and penalty of ₹ 5.75 crore was also leviable in these cases. The department has accepted audit observations involving revenue of ₹ 6.77 crore, recovered ₹ 90.70 lakh and issued SCNs for ₹ 6.32 crore.

A few cases are illustrated in the following paragraphs: -

8.1 Ineligible input services

As per Rule 2(l) of Cenvat Credit Rules, 2004, the term 'input service' includes services used in relation to setting up, modernisation, renovation or repairs of the premises of provider of output service, advertisement or sales promotion, market research, storage up to the place of removal, procurement of inputs, activities relation to business, such as accounting, auditing, financing, recruitment and quality control, coaching and training, computer networking, credit rating, share registry, and security, inward transportation of inputs, or capital goods and outward transportation upto the place of removal.

M/s. Consolidated Construction Consortium Ltd., in Chennai ST commissionerate, availed cenvat credit on input services relating to issue of initial public offering (IPO) during the period April 2007 to March 2008. This service did not fall under the definition of input service and hence did not qualify for credit under 'input service'. This resulted in irregular availing of cenvat credit of ₹ 87.91 lakh.

8.2 Excess cenvat credit availed on capital goods

Rule 4 (2) (a) of the Cenvat Credit Rules, 2004, stipulates that maximum of 50 per cent of the cenvat credit can be taken for duty paid on capital goods in the relevant financial year and the balance 50 per cent in the subsequent financial year. Rule 14 provides that where the cenvat credit has been availed or utilised wrongly, it will be recovered with interest.

M/s Shapoorji Pallonji & Co. and M/s Tirath Ram Ahuja Pvt. Ltd., in Delhi commissionerate, registered under WCS, availed the full credit of ₹ 3.30 crore for duty paid on capital goods procured during the year 2007-08 as against the admissible credit of ₹ 1.65 crore. This resulted in excess availing of credit of ₹ 1.65 crore which was recoverable with interest.

On this being pointed out by us (August 2008), the Department stated (February 2009) that M/s Shapoorji Pallonji & Co was entitled to avail the cenvat credit in next financial year 2008-09. Therefore, no such demand could be made from the assessee. The reply was not acceptable. According to provisions stated, the excess had to be recovered with interest and could be credited thereafter in the next financial year. In case of M/s Tirath Ram Ahuja it was stated in August 2010 that the assessee had been asked to comply with the audit objection.

8.3 Credit availed on input services not used for output service

A service provider can avail Cenvat credit on the basis of documents listed under Rule 9 of the Cenvat Credit Rules.

Scrutiny of records of M/s. NITCO Paints, in Mumbai ST commissionerate, revealed that the assessee had availed Cenvat credit of ₹ 367.86 lakh during the period from 2005-06 to 2006-07, whereas as per the documents of duty paid on inputs during the said period, the total cenvat credit available to the assessee was ₹ 289.25 lakh. This resulted in excess availing of Cenvat credit amounting to ₹ 78.61 lakh.

On this being pointed out by us (August 2009), the department intimated (June 2010) that a show cause notice of ₹ 78.61 lakh had been issued in February 2010.

8.4 Interest on delayed payments

Section 75 of the Finance Act, 1994, stipulates that if a person fails to credit the tax due or any part thereof within the prescribed period, it shall have to pay simple interest at prevalent rate. Section 76 of Finance Act, 1994, provides for levy of penalty for failure to pay service tax.

Scrutiny of records of M/s BHEL, in Kolkata ST commissionerate, revealed that it paid service tax of ₹ 2.50 crore on services received from NBCC Ltd. It took cenvat credit of input service for this amount twice in the months of October 2007 and December 2007. The tax paid for December 2007 was adjusted from the second irregular credit. This resulted in short payment of service tax of ₹ 2.50 crore in December 2007. This short payment was detected later and adjusted in the month of March 2008. However, no interest was paid for the delay in payment of service tax from December 2007 to March 2008. Interest of ₹ 7.66 lakh and penalty upto ₹ 14.34 lakh were leviable.

8.5 Excess utilisation of Cenvat credit beyond the admissible limit

The Cenvat Credit Rules, 2004, provides that a service provider who avails of Cenvat credit on input or input services and provides both exempted and taxable output services, has to maintain separate accounts in respect of both category of services. If he does not do so, then he can utilise credit only to the extent of an amount not exceeding twenty per cent of the service tax payable on the output services.

8.5.1 M/s Consolidated Construction Consortium. Ltd., in Chennai ST commissionerate, availed cenvat credit on input services. It provided both taxable and exempted output services but did not maintain separate accounts for the year 2007-08. It did not restrict utilisation of cenvat credit to 20 per cent of applicable service tax on output services and this resulted in excess utilisation of cenvat credit by ₹ 5.49 crore. The assessee was also liable to pay interest of ₹ 71.42 lakh and penalty upto ₹ 5.49 crore.

8.5.2 M/s Rajdeep Buildcon Pvt. Ltd, in Ahmednagar commissionerate, had provided taxable as well as exempted services during 2006-07 and 2007-08. It had wrongly availed cenvat credit of service tax on input services, such as telephone services, courier service, legal and professional services, authorised service station services, rent a cab service, advertising service etc., which were not valid input services as per rules. The total amount of such inadmissible credit was required to be ascertained and reversed. Moreover, the assessee was providing taxable as well as exempted services but did not maintain separate accounts of input services. Therefore, the assessee was eligible to utilise service tax credit to the extent of ₹ 3.06 crore against the total liability of service tax of ₹ 15.31 crore on output service during April 2005 to March 2008. The assessee utilised service tax credit amounting to ₹ 8.43 crore which resulted in excess utilisation of credit of ₹ 5.37 crore. The assessee was liable to pay service tax of ₹ 5.37 crore and interest of ₹ 69.84 lakh.

On this being pointed out by us (January 2009), the department replied (September 2009) that the audit observation was accepted and SCN for ₹ 5.37 crore plus interest and penalty applicable under the provisions had been issued in August 2009.

8.6 Mis-statement of balance of cenvat credit

M/s. SPACE, Ernakulam, in Cochin commissionerate, engaged in providing CON switched over to WCS and started availing cenvat credit on input services from June 2007. We found that it availed cenvat credit of ₹ 23.83 lakh on input services and utilised the same during the period June 2007 to September 2007. Consequently, there was nil credit of input service as on 30 September 2007. However, the assessee showed an opening balance of ₹ 11.58 lakh as on 1 October 2007 and utilised this amount during October 2007 to December 2007. This mis-statement resulted in irregular utilisation of credit of

₹ 11.58 lakh which was recoverable. The company was also liable to pay interest of ₹ 2.25 lakh, and penalty upto ₹ 11.58 lakh.

CHAPTER IX
SERVICE TAX COLLECTED BUT NOT REMITTED

9. Service tax collected but not remitted to the Government

Section 73 A of the Finance Act, 1994 (as amended from 18 April 2006), provides that any person, who is liable to pay service tax and has collected any amount in excess of the service tax assessed, shall forthwith pay the amount so collected to the credit of the Central Government.

We noticed that in 14 cases, service providers of CCS, CON and WCS had collected service tax of ₹ 3.87 crore but did not remit it to the Government account. They were also liable to pay interest of ₹ 60.74 lakh and penalty upto ₹ 3.87 crore. Three cases with a financial implication of ₹ 53.80 lakh were accepted and excess service tax recovered by the department.

A few illustrative cases are mentioned below: -

9.1 M/s Hindustan Steelworks and Construction Ltd., in Raipur Commissionerate, provided CCS to Bhilai Steel Plant and charged service tax at the rate of 12 per cent on gross amount but paid service tax after claiming abatement. During the period 2005-06 to 2006-07 the assessee charged service tax of ₹ 1.07 crore against construction service of ₹ 7.80 crore provided but remitted only ₹ 29.48 lakh. This led to short remittal of ₹ 77.32 lakh (excluding education cess). The assessee was also liable to pay interest of ₹ 20.10 lakh and penalty up to ₹ 77.32 lakh.

9.2 M/s Ahluwalia Contracts Ltd, in Ludhiana Commissionerate, was engaged in providing taxable services under CCS. We found that the assessee had provided taxable service of ₹ 34.79 crore and charged service tax of ₹ 1.42 crore (at the rate of 12.36 per cent on abated value) from August 2007 to March 2008. However, it had deposited service tax of ₹ 71.57 lakh (at the rate of 2.06 per cent up to February 2008 and at the rate of 4.12 per cent for March 2008) during the above said period. This resulted in undue retention of service tax of ₹ 70.35 lakh which was required to be recovered along with interest of ₹ 9.15 lakh and penalty upto ₹ 70.35 lakh.

9.3 M/s. BHEL, in Kolkata ST Commissionerate, engaged in providing CCS, had entered into a contract with West Bengal Power Development Corporation Ltd. In the letter of intent (March 2007) it was fixed that all applicable taxes and duties should be as per prevailing rates on date of offer (27 October 2006) and in case of any decrease in rate of taxes and duties, the excess amount of such duties and taxes shall be refunded by the assessee. We found that the total contract price was ₹ 197.07 crore including applicable service tax at the rate of 12.24 per cent when the contract was signed. Subsequently, the particular project was converted into WCS and service tax was paid by the assessee under composition scheme at the rate of 2.06 per cent on gross amount received. The excess service tax collected was neither refunded to the West Bengal Power Development Corporation Ltd nor

deposited with the Government exchequer. This resulted in short payment of service tax of ₹ 39 lakh. The assessee was also liable to pay interest of ₹ 10.15 lakh and penalty up to ₹ 39 lakh.

9.4 M/s Vijaynath Interiors and Exteriors Pvt. Ltd, in Mumbai I division under Mumbai ST commissionerate, had, paid service tax of ₹ 74.46 lakh for the half year ending March 2008. ST-3 return for the said half year was not filed by the assessee. On reconciliation with the bank statements and the details of the receipts during the said period, it was seen that the assessee had collected an amount of ₹ 2.77 crore during the month of March 2008 which included service tax of ₹ 34.18 lakh. This was over and above the tax paid of ₹ 74.46 lakh. The service tax of ₹ 34.18 lakh was collected but not paid till the date of audit (August 2008).

On this being pointed out by us (August 2008), the assessee paid service tax of ₹ 34.18 lakh and interest of ₹ 0.89 lakh (August 2008).

CHAPTER X
MISCELLANEOUS TOPICS OF INTEREST

10.1 Non payment of service tax on CCS by sub contractor

The Board's Circular No.96/7/2007-ST dated 23 August 2007 stipulates that where a taxable service provider outsources a part of the work by engaging another service provider (sub-contractor), the sub-contractor has to pay service tax on services provided by him.

As per Section 65(25b) of Finance Act, 1994, CCS includes construction of a pipe line or conduit used or intended for commerce or industry.

10.1.1 M/s Dharti Dredging and Infrastructure Ltd, in Hyderabad-II commissionerate, was awarded a sub contract valued at ₹ 32 crore by M/s Punj Lloyd Ltd. for execution of pipeline trenching and back filling work. This was a part of the main contract of laying of 20 gas pipelines from Uran to Trombay. The assessee received payment during the period April 2005 to March 2008 for execution of work but did not pay service tax of ₹ 3.85 crore. The assessee was also liable to pay interest of ₹ 83.74 lakh and penalty upto ₹ 3.85 crore.

On this being pointed out by us (September 2008), the department accepted the observation (April 2009) and intimated that SCN for ₹ 3.85 crore had been issued (March 2009).

10.1.2 During the test check of records of M/s Hindustan Steelworks and Construction Ltd. in Raipur commissionerate, we observed that M/s Sunil Hi Tech Engineers Ltd. provided services as subcontractor of M/s Hindustan Steelworks for which they received ₹ 7.65 crore during the year 2007-08. The subcontractor did not charge any service tax from the assessee. It is evident that the subcontractor has not paid the service tax of ₹ 94.56 lakh. Interest of ₹ 12.29 lakh and penalty upto ₹ 94.56 lakh was also leviable.

10.1.3 M/s Jain Infra Projects Ltd., in Division-III of Kolkata ST commissionerate, engaged in providing CCS as a 'sub-contractor', received payment of ₹ 5.09 crore for services provided but did not pay service tax of ₹ 62.66 lakh during the period April 2006 to March 2008. Interest of ₹ 12.20 lakh and penalty was also leviable.

10.2 Non payment of Service Tax by contractor

10.2.1 The Air Force allotted the work of construction of dwelling units and external services for officers and airmen at Chandigarh to M/s Megh Raj Bansal, Manimajra, in Chandigarh commissionerate, in June 2006. We found that the contractor received a sum of ₹ 21.72 crore from Indian Air Force upto June 2008 on which service tax of ₹ 2.68 crore was neither charged by the contractor nor paid by the recipient of services.

On being pointed out by us (December 2008), the department intimated (April 2009) that a SCN for ₹ 2.68 crore (without allowing abatement) had been issued (April 2009). Further progress was awaited (December 2010).

10.2.2 M/s. Maytas Infra Ltd., in Hyderabad II commissionerate, received ₹ 92.28 crore during January 2006 to March 2008 for construction of staff quarters for IIT, Chennai and armed forces but did not discharge the service tax liability of ₹ 3.61 crore. The assessee was also liable to pay interest of ₹ 46.93 lakh and penalty upto ₹ 3.61 crore.

10.3 Import of service

Section 66A of Finance Act, 1994, stipulates that in respect of taxable service provided by a person, who is a non-resident or is from outside India and does not have an office in India, the person receiving the taxable service in India is liable to pay service tax.

10.3.1 M/s. Nagarjuna Constructions Company Limited, in Hyderabad II commissionerate, engaged the services of persons from outside India and not having office in India, as lead managers and paid an amount of ₹ 12.99 crore as commission. Although service tax of ₹ 1.32 crore was payable, the assessee paid an amount of ₹ 25 lakh only in November 2007 leaving a balance of ₹ 1.07 crore. The assessee was also liable to pay interest of ₹ 13.76 lakh and penalty upto ₹ 1.07 crore.

10.3.2 In another case, M/s Aliens Developers (P) Ltd. in Hyderabad IV commissionerate, received architectural services from four foreign companies who were not having offices in India during the year 2006-07 and 2007-08 and paid ₹ 4.58 crore as service charges but did not discharge service tax liability of ₹ 56.13 lakh. The assessee was also liable to pay interest of ₹ 7.30 lakh and penalty upto ₹ 56.13 lakh.

10.4 Issue of incorrect SCN

M/s Bharucha & Motiwala Poona Pvt Ltd., in Pune III commissionerate, engaged in providing CCS, paid service tax on abated value of service provided during the period March 2006 to June 2006 but also availed cenvat credit on input services. The Department noticed the irregularity and directed the assessee to pay the differential amount of service tax on the basis of gross value instead of paying differential service tax, the assessee paid the amount of cenvat credit availed during March 2006. The Department issued a Show Cause Notice demanding the differential service tax for the month of March 2006 only. The SCN should have covered the period from April 2006 to June 2006 also as the assessee had continued to avail and utilise the cenvat credit on input services during the period.

Due to this non-inclusion, the demand of ₹ 39.63 lakh including interest had not been raised.

10.5 Non-filing of return electronically

According to Notification No. 27/2006-ST dated 21 September 2006, an assessee, who has paid service tax of rupees fifty lakh or above in the preceding financial year or has already paid service tax of rupees fifty lakh in the current financial year, shall deposit the service tax to be paid by him electronically, through internet banking with effect from 1 October 2006.

M/s National Building Construction Company Ltd., in Raipur commissionerate, paid service tax of ₹ 55.40 lakh during 2007-08 through GAR-7 challan and not electronically, which was in contravention to the notification.

Similarly M/s Tirath Ram Ahuja Private Ltd., in Delhi ST commissionerate, also had not used the e-payment option from October 2006 onwards though the assessee had made service tax payment of more than ₹ 50 lakh during the year 2005-06.

10.6 Difference in figure as shown in ST-3 returns with TR-6 challans

10.6.1 We compared the returns and the challans submitted by M/s. Ahluwalia Contracts (India) Ltd., in Division-II of Kolkata ST commissionerate and found that a return filed in March 2006 showed that service tax and education cess of ₹ 43.53 lakh and ₹ 0.87 lakh respectively were paid through challan no. 044/01/1036/06-07. However, the challan showed that service tax and education cess amounting to ₹ 21.05 lakh and ₹ 0.42 lakh were actually deposited. This had resulted in short payment of service tax including education cess of ₹ 22.93 lakh. The assessee was also liable to pay interest of ₹ 5.97 lakh and penalty upto ₹ 22.93 lakh.

Reply of the department was awaited (December 2010).

10.6.2 M/s Gannon Dunkerley Company Limited, in Delhi commissionerate, had enclose challans that were less than the amount shown

in the returns during the financial year 2006-07 by an amount of ₹ 158.24 lakh.

On this being pointed out by us (February 2008), the department intimated (April 2010) that the assessee had furnished copies of challans for ₹ 149.35 lakh but had not given any reply for the remaining amount of ₹ 8.89 lakh. Thus, the short payment of ₹ 8.89 lakh was recoverable with applicable interest and penalty.

New Delhi **(SUBIR MALLICK)**
Dated : **Principal Director (Indirect Taxes)**

Countersigned

New Delhi **(VINOD RAI)**
Dated : **Comptroller and Auditor General of India**

Glossary of terms and abbreviations

Abbreviated form	Expanded form
ACES	Automation of Central Excise and Service Tax
BHEL	Bharat Heavy Electrical Limited
CBEC	Central Board of Excise and Customs
CCS	Commercial or industrial construction services
Cenvat	Central value added tax
CON	Construction of complex (residential) services
CPWD	Central Public Works Department
DGST	Director General Service Tax
GDP	Gross domestic product
IPO	Initial public offering
Ltd.	Limited
NTPC	National Thermal Power Corporation
PSU	Public Sector Undertaking
Pvt.	Private
SCN	Show cause-cum-demand notice/show cause notice
SRA	Slum rehabilitation authority
TDR	Transfer development right
VAT	Value added tax
WCS	Works contract services