

CHAPTER-II GST, TAXES/VAT ON SALES, TRADE ETC.

2.1 Tax administration

Kerala General Sales Tax (KGST)/Kerala Value Added Tax (KVAT)/Goods and Services Tax (GST) laws and rules made thereunder are administered at the Government level by the Secretary, Taxes. The Commissioner, State Goods and Services Tax (SGST) Department is the head of the State Goods and Services Tax Department (SGSTD) who is assisted by Additional Commissioner, Joint Commissioners (JCs), Deputy Commissioners (DCs), Assistant Commissioners (ACs) and State Tax Officers. The assessment, levy and collection of tax are done by ACs and State Tax Officers.

KGST is leviable on sale of Ganja, opium, foreign liquor and certain petroleum products. KVAT was leviable on the intra-state sale of remaining commodities and Central Sales Tax (CST) on inter-State sales. GST came into effect from 01 July 2017 subsuming VAT, CST etc.

2.2 Internal audit

The Internal Audit Wing (IAW) of the SGSTD is monitored by the Commissioner. The effective functional unit of IAW for the year 2018-19 was one JC assisted by five DCs and nine State Tax Officers. No specific training has been imparted to the officers of the IAW. During 2018-19, the wing planned audit of 181 units but could audit only 32 units. Out of an overall outstanding of 15,665 paras only 3,134 paras (20 *per cent*) were cleared. The reason for low clearance of observations made by IAW, though called for (July 2019) was not furnished (December 2020).

2.3 Results of audit

There are 185 auditable units in the SGST Department. Out of these, audit selected 101 units for test check during the year 2018-19. Test check of the records relating to KVAT/KGST and CST assessments and connected documents during 2018-19 showed under-assessment of tax and other irregularities in 556 cases relating to non/short levy of tax/interest, irregular allowance of Input tax credit, escape of turnover from assessment, irregular exemptions and other lapses amounting to ₹ 198.07 crore. These cases are illustrative only as these are based on the test check of records. As this was test audit in the test checked cases and the audit observation is of a nature that may reflect in other cases not covered in test audit, the Department may therefore, like to internally examine the position in rest of the units with a view to ensure that the instances of noncompliance are taken care of by taking remedial measures, and may also fix responsibility for the lapses in all such cases. Audit pointed out some of the similar omissions in the earlier years also. Not only do these irregularities persist, but they also remain undetected till the next audit is conducted. Underassessment of tax and other

irregularities involving ₹ 266.23 crore in 557 cases which fall under the following categories are given in **Table - 2.1**.

Table - 2.1

(₹ in crore)

Sl. No.	Categories	Number of cases	Amount
1	Compliance Audit on Transition from KVAT to GST	1	68.16
2	Short payment of tax due to escape of turnover from assessment	138	48.69
3	Grant of irregular exemption	67	33.06
4	Short payment of tax due to excess availing of input tax credit	80	81.93
5	Short payment of tax due to misclassification/incorrect rate of tax	78	15.19
6	Others	193	19.20
Total		557	266.23

During the course of the year, the Department accepted under-assessment and other deficiencies amounting to ₹ 145.56 crore in 974 cases, which were pointed out by Audit. An amount of ₹ 12.23 crore pointed out in 535 cases was realised during the year.

The Department recovered the entire amount of ₹ 0.04 crore in a case pointed out by Audit during 2018-19. A few Audit observations involving ₹ 76.52 crore are given in the succeeding paragraphs.

2.4 Compliance Audit on Transition from Kerala Value Added Tax to Goods and Services Tax

2.4.1. Introduction

The Goods and Services Tax (GST) is a tax on supply of goods or services or both and a single tax on entire value chain of supply, right from the manufacturer to the consumer. GST was rolled out from 01 July 2017. Tax administration in GST regime is a technology driven one and the Government of India has constituted a Private Ltd. company named Goods and Services Tax Network (GSTN) to provide IT infrastructure and services to the Central and State governments, taxpayers and other stakeholders. GSTN is responsible for building the GST common portal for providing three core services viz. registration, return filing and e-payment. The common portal of GST is to be integrated with the State systems. Some States opted to develop their own backend application for performance of statutory functions such as assessment, refund, enforcement etc. These States are termed as Model 1 States. Some States use the common back end application developed by GSTN. These States are termed as Model 2 States. Kerala opted for Model 1 wherein the State will setup the data center and develop backend modules.

2.4.2 Audit Objectives

The Compliance Audit was conducted to examine whether:

- the Rules, Notifications, Circulars and Orders issued under GST were adequate to strengthen tax net;
- the transitional input tax credit availed and refund of unutilised credit issued during transition were in compliance with the extant provisions.

2.4.3 Scope and methodology of audit

The period of coverage of audit is from 2017-18 to 2018-19 and audit was conducted from July 2019 to February 2020. Thiruvananthapuram tax district was selected as Government/Department headquarters is located here and Ernakulam tax district was selected because of its high tax effect. The remaining six⁹ out of balance 13 tax districts¹⁰ were selected as sample districts using random sampling method for ensuring high reliability and coverage. The criteria for selection of transitional claims for scrutiny is shown in **Table –2.2**

⁹ Kollam, Pathanamthitta, Mattancherry, Thrissur, Malappuram and Palakkad.

¹⁰ Kollam, Pathanamthitta, Alapuzha, Kottayam, Idukki, Mattancherry, Thrissur, Palakkad, Malappuram, Kozhikode, Wayanad, Kannur and Kasaragod.

Table –2.2
Criteria for selection of transitional claims for audit

Claims of Transitional Credit by dealers	Total number of transitional claims	Number of transitional claims test checked by audit	Percentage of selection
Above ₹ 10 lakh	699	491	70
Between ₹ one lakh and ₹ 10 lakh	1,846	464	25
Between ₹ one and ₹ one lakh	4,621	232	5
Zero claim	950	197	21
Total	8,116	1,384	17

An Entry Conference was held with the Additional Secretary, Taxes Department on 05 July 2019, wherein the objective, scope and methodology of audit were discussed.

An Exit Conference was held on 09 September 2020 with the Additional Secretary, Taxes and Commissioner, SGSTD. The SGSTD assured that all cases would be verified and reply would be furnished. Audit acknowledges the co-operation rendered by the SGSTD in providing records and other facilities.

2.4.4 Trend of Revenue

GST was implemented from July 2017 and total receipts under GST from July 2017 to March 2019 is ₹ 52,672.72 crore. Receipts under pre-GST including non-subsumed taxes¹¹ during 2017-19 is ₹ 43,803.57 crore as indicated in **Table –2.3**.

Table –2.3
Trend of Revenue for the period 2014-15 to 2018-19

Year	Budget Estimate	Receipts under pre-GST taxes	Receipts under GST			Total receipts under pre-GST and GST	Percentage of increase	Compensation received	Protected revenue ¹²
			SGST	IGST Apportionment	Adhoc Settlement ¹³				
2014-15	31,913.47	27,908.33	--	--	--	27,908.33	--	--	--
2015-16	34,712.28	30,736.78	--	--	--	30,736.78	10.13	--	--
2016-17	36,952.98	33,453.49	--	--	--	33,453.49	8.84	--	--

¹¹ Central/State Excise duty and VAT on five Petroleum products, Tobacco products, Alcoholic liquor for human consumption.

¹² Part settlement of integrated tax.

¹³ The States should be compensated for any shortfall in getting a revenue of 14 per cent over the base year (2015-16) revenue relating to taxes/duties subsumed into GST.

Year	Budget Estimate	Receipts under pre-GST taxes	Receipts under GST			Total receipts under pre-GST and GST	Percentage of increase	Compensation received	Protected revenue ¹²
			SGST	IGST Apportionment	Adhoc Settlement ¹³				
2017-18	42,187.57	24,577.82	12,007.69	6,065.00	736.00	43,386.51	29.69	2,102.00	16,398.00
2018-19	46,791.10	19,225.75	21,014.71	10,114.95	2,734.37	53,089.78	22.36	3,532.00	24,924.00

Source: Finance and Appropriation Accounts and Departmental figures

2.4.5 Preparedness to implement GST

2.4.5.1 Legal provisions

For effecting GST in the State from 01 July 2017, the Government of Kerala had promulgated the Kerala Goods and Services Tax Ordinance, on 22 June 2017. The Legislative assembly of Kerala, on 17 August 2017, passed the Kerala Goods and Services Tax Bill, 2017. The SGSTD had issued 190 notifications and 31 clarifications as on 31 March 2019 for the smooth implementation of GST.

2.4.5.2 Administrative structure

In Kerala, GST is administered by the SGSTD. At the Government level, SGSTD is under the administrative control of the Secretary to Government, Taxes Department. The Commissioner of State Taxes is the Head of the Department, who is assisted by Special Commissioner, Additional Commissioners, JCs, DCs, Inspecting Assistant Commissioners and by ACs and State Tax Officers at the assessment circles. The State is divided into 15 tax districts, each headed by a DC and each tax district is divided into several circles, which are the smallest administrative units in the Department.

2.4.5.3 GST Training

Knowledge sharing on GST and GSTN was provided to different stakeholders by conducting extensive trainings by the State department. The details of GST training imparted to the department staff including line department staff, dealers and various stakeholders across the State is given below in **Table – 2.4**.

Table – 2.4
Details of GST trainings

Imparted to	No. of trainings planned	No. of trainings conducted	Percentage
Department Officials including field officials	564	564	100
Dealers and Stake holders	524	524	100
Line departments	314	311	99.04

Source: Departmental figures

Trainings were given to the SGSTD officials/line departments/ taxpayers in a phased manner (mainly in Three phases). Source trainers were identified at the national level who trained the master trainers of the State. These master trainers trained the staff, dealers etc. Further, GST helpdesks were established in all the 15 district headquarters offices to facilitate the taxpayers to address GST related issues.

2.4.6 Registration and migration of taxpayers

Section 139 of Kerala State Goods and Services Tax Act (KSGST Act), provides that on and from the appointed date¹⁴, every person registered under any of the existing laws and having a valid Permanent Account Number shall be issued a certificate of registration on provisional basis, subject to such conditions as may be prescribed, which unless replaced by a final certificate of registration, shall be liable to be cancelled, if the conditions so prescribed were not complied with. As per Section 22 of KSGST Act, every supplier making a taxable supply of goods or services or both in the State shall be liable to be registered under this Act, if his aggregate turnover in a financial year exceeded ₹ 20 lakh¹⁵.

As per the quarterly report (September 2018) of SGSTD, 98.86 *per cent* taxpayers were migrated. Total number of registered dealers in the erstwhile KVAT regime was 2,65,128 and total number of dealers whose sales turnover of ₹ 20 lakh and above was 2,25,813. Total number of dealers not required to take registration was 39,315. Total number of taxpayers under GST was 3,21,448 out of which 2,34,291 was migrated taxpayers and 87,157 was new taxpayers. Total migrated taxpayers of 2,34,291 includes cancelled taxpayers of 8,478. Mapping of dealers with the assessing authorities was done based on the pin code of the taxpayer.

2.4.7 Division of tax payers

The introduction of GST in the state was followed up with migration of existing tax payers to the GST regime and registration of new ones. These tax payers were divided between the Central and State on the basis of turnover. As per the guidelines¹⁶ issued by the GST Council, with respect to the division of taxpayer base between the Central Government and State Governments, the taxpayers registered in the State of Kerala have been allocated under two categories. Taxpayers whose turnover is ₹ 1.5 crore and above are allocated as 50 *per cent* to the Centre and 50 *per cent* to the State and those taxpayers whose turnover is less than ₹ 1.5 crore are allocated as 10 *per cent* to the Centre and 90 *per cent* to the State.

¹⁴ The date on which the provisions of this Act shall come into force. Section 139 came into force with effect from 22 June 2017.

¹⁵ Notification No.10/2019 – Central tax dated 07 March 2019 enhanced the threshold limit to ₹ 40 lakh from 01 April 2019 onwards.

¹⁶ Circular No.01/2017, issued vide F.No.166/Cross Empowerment/GSTC/2017 dated 20 September 2017.

According to the criteria mentioned above, dealers in the State have been divided among the Centre and State as mentioned in **Table - 2.5**.

Table – 2.5
Allotment of taxpayers

Annual Turnover of dealers	Total No. of dealers	Division of dealers	
		State	Centre
₹ 1.5 crore and above	36,110	18,055	18,055
Less than ₹ 1.5 crore	1,86,667	1,68,000	18,667
Total	2,22,777	1,86,055	36,722

Source: Departmental figures

Audit Findings

Excess/Irregular carry forward of transitional credit in 234 out of 1,384 cases test checked, excess sanctioning of refund in 80 out of 1,073 cases test checked and irregular option of composition scheme were observed in audit. Audit was limited to the above extent due to lack of access to GSTN data. The details of the above irregularities are shown in the succeeding paragraphs.

2.4.8 Lack of access to GSTN data

Audit was not given access to GSTN data dump and even after much pursuance, the Commissioner of State Taxes could share only the excel sheet data relating to GST migration, FORM GST TRAN-1¹⁷, FORM GST TRAN-2¹⁸, refunds and division of taxpayers alone as on 30 April 2019. In respect of carry forward of the CGST transitional credit attributable to Central Excise and Service tax, Audit could not verify the credit as the records relating to the central taxes were not made available. In the absence of access to data, Audit carried out a limited audit of transitional credit claims and refunds in the selected tax districts.

2.4.9 Irregular option of composition scheme

As per Section 10 of the KSGST Act 2017, a registered person other than supplier of services, whose aggregate turnover in the preceding financial year did not exceed one crore rupees (threshold limit was revised to ₹ 1.5 crore with effect from 01 April 2019) may opt for composition scheme subject to some conditions prescribed. Registered persons who opted for this scheme

¹⁷ Form of declaration by the dealers for claim of transitional credit. Every registered person entitled to take credit of input tax as transitional credit shall submit a declaration electronically in FORM GST TRAN-1 on the common portal within 180 days from the appointed day.

¹⁸ Declaration of dealer regarding the details of stock held by the dealer as on 30 June 2017. The registered person availing of the transitional credit of stock of goods have suffered tax and he is not in possession of any document evidencing payment of tax shall submit a statement in FORM GST TRAN-2 at the end of each of the six tax periods.

have to pay tax at a fixed rate (Manufacturer-0.5 per cent¹⁹, Restaurant-2.5 per cent and Others-0.5 per cent) on the aggregate turnover without collecting tax from the recipients and is not entitled to input tax credit. As per paragraph 6 (a) of Schedule II of the KSGST Act, 2017, works contract shall be treated as supply of services and the persons supplying works contract service cannot opt for composition scheme. As per Section 10(5) of the KSGST Act, if the proper officer has reasons to believe that a taxable person has paid tax under composition scheme despite not being eligible, such person shall, in addition to any tax that may be payable by him under any other provisions of this Act, be liable to a penalty and the provisions of Section 73 or Section 74 shall apply for determination of tax and penalty.

Scrutiny of records relating to 4,000 out of 19,776 registered persons who had opted for composition scheme during the period 2017-18 revealed that 24 of them had aggregate turnover above ₹ one crore in the preceding financial year, and for the period 2017-18 & 2018-19, 15 were works contractors as detailed in **Appendix - IV and V** respectively. Hence, these taxable persons are not eligible to opt for composition scheme and liable to pay tax with penalty under Section 73 or 74 of KSGST Act. The department failed to verify the aggregate turnover in the preceding financial year and the nature of business of the taxpayer in KVATIS before sanctioning the registration.

The Government stated (November 2020) that out of the 39 cases pointed out all the cases were verified. Notices were issued in 16 cases and the remaining cases are under processing.

Recommendation: The department may verify the aggregate turnover in the preceding financial year and the nature of business of the taxpayer before the sanctioning of composition scheme.

2.4.10 Transitional credit

With the implementation of GST, the taxable persons can carry forward the taxes they had already paid on inputs or input services in the pre-GST regime. Section 140 to 142 of the KSGST and CGST Acts enumerate the necessary provisions governing the claim of transitional credits²⁰. Every registered person under existing law, who were paying tax at the regular rate, may claim transitional credit and carry forward the balance input tax credit (ITC) available under Central Excise, Service Tax, State VAT and unavailed portion of ITC in respect of capital goods. For this, the registered person has to submit a declaration electronically in FORM GST TRAN-1 on the GST portal and has to furnish all the returns required under the existing law for the period of last six months as on 01 July 2017

¹⁹ Notification No.1/2018 – Central tax dated 01 January 2018 revised the rate from one per cent to 0.50 per cent.

²⁰ A registered person can carry forward the closing balance of input tax credit under Central Excise and Service Tax Act as CGST and input tax credit under State VAT Act as SGST, subject to specified conditions.

(Monthly Returns from January 2017 to June 2017). Moreover, some specified category of dealers/goods are also entitled to the claim of transitional credit on stock held on 30 June 2017, subject to some conditions and limitations²¹.

These specified category dealers are those who were not liable to be registered under the existing law, who were paying tax at compounded rate, those who were having goods in transit on the appointed day etc.

The due date for filing or revising FORM GST TRAN-1, originally fixed as 28 September 2017 was extended to 27 December 2017 and in certain cases owing to technical difficulties in GST portal extended up to 31 March 2019.

The circular²² issued (June 2017) by the Commissioner, Commercial Taxes Department indicated that State Tax Officers would verify transitional credit claims as and when the dealers filed FORM GST TRAN-1.

Out of 11,581 tax payers under the jurisdiction of SGSTD of Kerala who had filed TRAN-1 returns, 801 dealers had filed TRAN-2 returns as on 31 March 2019. In eight tax districts selected for audit, 8,116 taxpayers filed TRAN 1 returns and out of them 621 taxpayers filed TRAN-2 returns.

Out of 8,116 TRAN 1 returns filed in the selected tax districts as on 31 March 2019 the assessing authorities verified only 3,717 returns as on 30 November 2019. Audit test checked 1,384 (17.05 *per cent*) out of 8,116 transitional claims received in the selected eight out of 15 tax districts.

The observations noticed with respect to transitional credit are detailed below:

2.4.10.1 Carry forward of ITC not reflected in the last return under KVAT

Section 140(1) of KSGST Act stipulates that a registered person can carry forward the credit of Value Added Tax and Entry Tax, if any, as given in the last return filed under KVAT i.e. for the month of June 2017, in his electronic credit ledger²³ (ECL).

Audit noticed that 20 out of 1,384 test checked registered persons carried forward higher transitional credits in the ECL than the amount declared in their last return under KVAT. The irregular availing of transitional credit without adhering to the provision as above involves a revenue of ₹ 2.33 crore as detailed in **Appendix – VI**.

²¹ The conditions are: (a) Taxes paid on stock for which input tax credit was not already taken under the erstwhile laws; (b) Taxes on exempted goods or services under the erstwhile Acts but taxable under the GST regime; (c) Taxes paid under the erstwhile Acts on goods received after 01 July 2017.

²² Circular No.GSTC 24614/16/CT E office 11137/17 dated 22 June 2017.

²³ The electronic credit ledger shall be maintained for each person eligible for input tax credit and every claim of input tax credit under the Act shall be credited to the said ledger.

The Government stated (November 2020) that out of the 20 cases pointed out all the cases were verified. Assessment was completed in one case, notices were issued in seven cases, recovery was effected in two cases and the remaining cases are under processing.

2.4.10.2. Carry forward of credit in ledger higher than that in TRAN-1 return

Rule 117 (1) of KSGST Rule, 2017, provides that every registered person entitled to transitional credit, has to submit a declaration electronically in FORM GST TRAN-1 on the common portal. As per Rule 117(3), the amount of credit specified in the application in FORM GST TRAN-1 shall be credited to the ECL of the applicant maintained in FORM GST PMT-2 on the common portal.

Audit noticed that 61 out of 1,384 registered persons in the eight selected tax districts availed excess transitional credit amounting to ₹ 46.41 crore over and above the Input Tax Credit as disclosed through FORM GST TRAN-1 by crediting a higher amount in the ECL. Even in 40 cases where TRAN-1 return showed 'Nil' credit, the respective registered persons carried forward excess credit amounting to ₹ 3.69 crore in the ECL. This resulted in irregular carry forward of transitional credit amounting to ₹ 46.41 crore as detailed in **Appendix - VII and VIII.**

The Government stated (November 2020) that out of the 61 cases pointed out all the cases were verified. Notices were issued in 21 cases, recovery was effected in one case and the remaining cases are under processing.

2.4.10.3 Claim of Transitional Credit on Stock having no document evidencing payment of duty

As per proviso to Section 140(3) of CGST Act, a registered person other than 'manufacturer or service provider' may claim transitional credit on stock having no supporting invoice subject to conditions in Rule 117(4) of CGST Rules.

A verification of the TRAN 1 and TRAN 2 returns of registered persons, who had availed transitional credits under this scheme, revealed the following:

(a) **As per Rule 117(4)(a)(i) of CGST Rules 2017, a registered person who was not registered under the existing law shall be allowed to avail of input tax credit on goods held in stock on the appointed day in respect of which he is not in possession of any document evidencing payment of central excise duty.** Hence the registered persons availing ITC under this scheme on goods held in stock on the appointed day should not have been registered under the existing law (Central Excise and Service Tax).

Audit noticed in the six selected tax districts that 46 out of 1,384 test checked persons were not having any supporting invoices on goods held in stock on the appointed day but registered under the existing law as manufacturer/service provider. However, these persons claimed transitional credit in respect of stock held on the appointed day which resulted in irregular claim of CGST credit amounting to ₹ 13.08 crore as detailed in **Appendix - IX**.

The Government stated (November 2020) that out of the 46 cases pointed out all the cases were verified. Notices were issued in 21 cases and the remaining cases are under processing.

(b) Rule 117(4)(b)(iii) of KSGST/CGST Rules 2017 prescribes that the registered persons who are not in possession of an invoice or any other documents evidencing payment of tax/duty in respect of inputs have to initially submit details of such stock in FORM GST TRAN 1 and thereafter on effecting supply of these goods by six tax periods²⁴, have to file a return in FORM GST TRAN 2 showing the details of goods supplied in each tax period.

Scrutiny of TRAN 1 and TRAN 2 returns of tax payers who availed ITC under this scheme in the four selected tax districts revealed that, in respect of six out of 1,384 cases test checked, credits were availed on submitting return in FORM GST TRAN 1 alone; without filing a return in FORM GST TRAN 2 for each tax period after effecting supply of these goods. This resulted in irregular claim of transitional credit amounting to ₹ 0.18 crore as detailed in **Appendix – X**.

The Government stated (November 2020) that out of the six cases pointed out all the cases were verified. Notices were issued in three cases and the remaining cases are under processing.

2.4.10.4 Irregular carry forward of Transitional credit without adhering to the conditions stipulated in provisions

As per Sections 140(3), 140(4)(b) and 140(6) of the KSGST Act, 2017 and Rule 117(4)(a)(i) of Kerala GST Rules 2017, the amount of VAT and Entry Tax paid on inputs held in stock and inputs contained in semi-finished or finished goods held in stock on the appointed day supported by invoices/documents evidencing payment of tax can be carried forward to ECL as credit by the GST registered person in the following circumstances:

1. The person was not liable to be registered under KVAT Act.
2. The person was engaged in sale of exempted goods.
3. Goods suffered tax at first point of sale and subsequent sale were not subjected to tax.

²⁴ July 2017 to December 2017.

4. The person was entitled to take ITC at the time of sale of goods.
5. The person was paying tax at fixed rate under KVAT Act.

Audit noticed in the seven selected tax districts that in 77 out of 1,384 cases test checked, credits were carried forward even though these taxpayers do not fulfil any of the above-mentioned criteria. Non-adherence of the above provisions resulted in the availing of irregular SGST transitional credit to the tune of ₹ 3.99 crore as detailed in **Appendix – XI**.

The Government stated (November 2020) that out of the 77 cases pointed out all the cases were verified. Assessment was completed in one case, notices were issued in 36 cases, recovery was effected in one case and the remaining cases are under processing.

2.4.10.5 Irregular carry forward of transitional credit on capital goods

As per Section 140(2) of KSGST Act, 2017, a registered person, other than composition taxpayer, shall be entitled to take, in his ECL, unavailed portion of input tax credit on capital goods, not carried forward in a return, furnished under the existing law by him, for the period ending with the day immediately preceding the appointed day in such manner as may be prescribed.

Audit noticed that, in the eight selected tax districts, as per the KVAT monthly return (Form 10) for June 2017, 24 out of 1,384 test checked registered persons, the unavailed portion of credit on capital goods was 'Nil' in 18 cases, or less than the credit claimed in FORM GST TRAN 1 in six cases. Thus, the transitional credit on capital goods to the tune of ₹ 0.65 crore was inadmissible as detailed in **Appendix - XII**. The reason for the excess credit in the ECL higher than the KVAT monthly return was called for. But the reply has not been received.

The Government stated (November 2020) that out of the 24 cases pointed out all the cases were verified. Notices were issued in eight cases, recovery was effected in one case and the remaining cases are under processing.

Recommendation: The Department may re-examine all the transitional credit cases and take appropriate action to recover the revenue while making final assessment of the dealers.

2.4.11 Refunds

Sections 54 to 58 of CGST/KSGST Act 2017 and Sections 15 and 16 of IGST Act 2017 provide for refund under GST. Refund can be claimed mainly under the following circumstances:

- Unutilised ITC due to zero rated supply²⁵ of goods or services or both.
- Unutilised ITC at the end of any tax period where the credit has accumulated on account of rate of tax on inputs being higher than the rate of tax on output supplies (i.e. Inverted Duty Structure).
- Balance cash in ECL.
- Refund of IGST paid on export supply.
- Any tax paid by UN²⁶ entities for inward supplies.

Any person claiming refund of any duty and interest, may make an application for refund to the department before the expiry of two years from the relevant date²⁷ in the prescribed form.

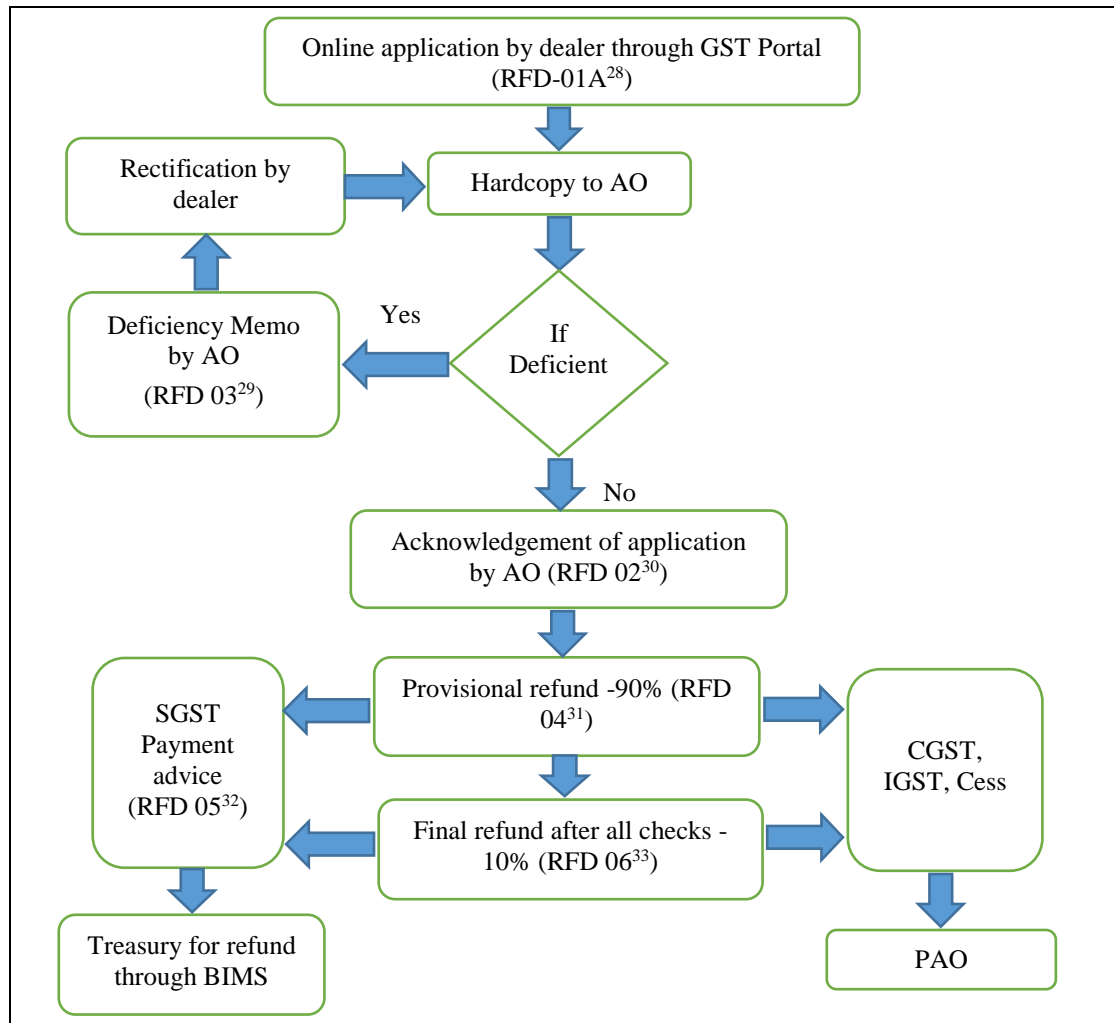
The refund application should be accompanied by such documentary or other evidence as the applicant may furnish to establish that the amount in relation to which the refund is claimed was collected from him or paid by him and the incidence of such duty/interest had not been passed on by him to any other person.

The process of refund is depicted below:

²⁵ Export of goods or services or both, supply of goods or services or both to a Special Economic Zone developer or a Special Economic Zone unit.

²⁶ UN entities are provided with Unique Identification Number (UIN). UIN is a special class of GST registration for foreign diplomatic missions and embassies which are not liable to taxes in the Indian territory.

²⁷ The date on which the return relating to export of goods/services or deemed exports is furnished.



On receipt of the above application the proper officer should issue an acknowledgement/deficiency memo based on the completeness of the application within 15 days. After scrutiny of the claim and on being *prima facie* satisfied that the amount claimed as refund is correct, the proper officer should sanction ninety *per cent* of the total amount as refund on a provisional basis, within a period not exceeding seven days from the date of the acknowledgement. Further, the proper officer has to issue the order sanctioning the final refund after due verification and examination of claim within 60 days from the date of receipt of application. Refund processing is done by the concerned jurisdictional authority. The CGST and IGST components are disbursed by the CGST department and the SGST component is disbursed by the SGST department.

²⁸ Application for refund filed electronically by the applicant. Even though online submission of refund application started from 1 July 2017, it became completely automated from 26 September 2019 onwards only.

²⁹ Form in which the proper officer communicates the deficiencies to the applicant.

³⁰ Acknowledgement of the application made available to the applicant.

³¹ Order sanctioning the amount of refund on a provisional basis.

³² Payment advice of the amount sanctioned.

³³ Form for sanctioning the amount of refund to which the applicant is entitled.

Audit examined the records relating to refunds of 1,073 out of 1,532 sanctioned refund claims in the 75 offices of selected eight tax districts. Audit noticed that delay had occurred in various stages of sanctioning refund as detailed in the **Table 2.6**.

Table – 2.6
Delay in various stages of sanctioning refund

	Number of offices	Number of cases
Delay in acknowledgement	33	167
Delay in issuing deficiency memo	11	26
Delay in provisional refund	29	295
Delay in final refund	64	574

2.4.11.1 Ineligible refund in respect of zero rated supply of goods or services or both without payment of tax

As per proviso to Section 54(3) of CGST Act, no refund of input tax credit shall be allowed, if the supplier of goods or services or both avails of drawback in respect of central tax paid or claims refund of the integrated tax paid on such supplies.

Scrutiny of records relating to 1,073 refund claims revealed that in 41 cases in the five selected tax districts the unutilised input tax credit on account of zero rated supply of goods without payment of tax were sanctioned to the taxpayers who had availed drawback of central taxes. The ineligible refund on zero rated supply of goods or services or both without payment of IGST and availing drawback of central taxes amounted to ₹ 0.76 crore as detailed in **Appendix - XIII**.

The Government stated (November 2020) that out of the 41 cases pointed out all the cases were verified. Notices were issued in 16 cases, recovery was effected in one case and the remaining cases are under processing.

Recommendation: The Assessing Authorities while verifying the refund claims shall ascertain whether the assessee had availed drawback of central taxes.

2.4.11.2 Excess refund due to erroneous application of formula

Rule 89(4) and 89(5) of the KSGST/CGST Rules 2017, prescribes the formula³⁴ for refund of input tax credit in the case of zero-rated supply of goods or services or both done without payment of tax and inverted duty structure. As per the rule *ibid*, ‘Adjusted Total Turnover’ means the turnover in a State or a Union Territory, as defined under sub-section (112)

³⁴ Refund in respect of export of goods or services = (Turnover of zero-rated supply of goods + Turnover of zero-rated supply of services) x Net ITC ÷ Adjusted Total Turnover.
Refund in respect of Inverted duty structure = {(Turnover of inverted rated supply of goods and services) x Net ITC ÷ Adjusted Total Turnover} - tax payable on such inverted rated supply of goods and services.

of section 2, excluding the value of exempted supplies other than zero-rated supplies, during the relevant period.

Scrutiny of refund documents/ records and monthly returns for the relevant period³⁵ in FORM GSTR-3B in the six selected tax districts revealed that in 22 out of 1,073 claims test checked, 'Adjusted total turnover' was erroneously taken as the turnover of zero-rated supply alone. This resulted in excess allowance of refund to the tune of ₹ 0.57 crore as detailed in **Appendix – XIV**.

The Government stated (November 2020) that out of the 22 cases pointed out all the cases were verified. Assessment was completed in two cases, notices were issued in three cases, recovery was effected in two cases and the remaining cases are under processing.

Recommendation: The Assessing Authorities may observe utmost caution in order to avoid calculation mistakes while processing refunds.

2.4.11.3 Excess allowance of refund due to erroneous inclusion of credit on 'Capital goods' in net ITC

Rule 89(4) and 89(5) of the KSGST Rules, 2017, prescribes the formula for refund of unutilised ITC. As per the rule *ibid*, net ITC means the ITC availed only on inputs during the relevant period. The definition of 'input' as per Section 2 (59) of CGST Act 2017, means any goods other than capital goods used or intended to be used by a supplier in the course or furtherance of business.

During the test check of 1,073 refund claims, Audit observed that, in respect of nine claims in the two selected tax districts, the refund of input tax credit on capital goods were included in net ITC, which resulted in excess allowance of refund amounting to ₹ 0.13 crore as detailed in **Appendix – XV**.

Replies have not been received from the Government. Reply is awaited.

Recommendation: While processing the refund claim the credit on capital goods shall not be included as part of Net ITC.

2.4.11.4 Sanction of refund by ineligible jurisdictional authority

Rule 96(3) of KSGST Rules stipulates that 'Upon the receipt of the information regarding the furnishing of a valid return in FORM GSTR-3 or FORM GSTR-3B, as the case may be from the common portal, the system designated by the Customs or the proper officer of Customs, as the case may be, shall process the claim of refund in respect of export of goods and an amount equal to the integrated tax paid in respect of each shipping bill or bill of export shall be electronically credited to the bank account of the applicant

³⁵ The period for which the claim has been filed.

mentioned in his registration particulars and as intimated to the Customs authorities’. As mentioned in the rule, the taxable person is to claim the Integrated Goods and Service tax (IGST) portion of export of goods from the Customs authorities.

Scrutiny of 1,073 refund claims revealed that six persons in the three selected tax districts were sanctioned refund of IGST paid for the export of goods. The registered persons submitted the refund application and claimed the refund of IGST as Export of Services with payment of tax instead of export of goods with payment of tax. Here, the taxpayers used the wrong term ‘export of services’ instead of ‘export of goods’ in the refund application and the SGSTD sanctioned refund without detailed verification. This had resulted in ineligible payment of IGST, CGST and SGST amounting to ₹ 0.06 crore as detailed in **Appendix – XVI**.

The Government stated (November 2020) that out of the eight cases pointed out all the cases were verified. Recovery was effected in one case and the remaining cases are under processing.

Recommendation: The Assessing Authorities may thoroughly scrutinise the details furnished by the assessee in order to avoid mistakes in the sanctioning of refund claims.

2.4.12 Conclusion

In the absence of access to GST data, the conclusions of this audit are based on limited checks carried out in the field. The department had taken adequate steps for GST implementation by imparting training to officials, issuing instructions to field offices for the verification of transitional credits/refunds, providing GST help desks in all district headquarter offices etc. Eligibility of taxpayers opting for the composition scheme, verification of transitional credits arising from VAT returns, complying with the provision of Acts and Rules for sanctioning refunds, computation of refund amount and eligibility of jurisdictional authority for sanctioning refunds are areas which require necessary remedial action from the department as discussed in the Audit paras. Our observations were for the selected samples and hence the department may examine similar issues outside the sample as well to control the potential revenue loss.

2.5 Short levy of tax

During the year 2018-19, out of 185 offices under the SGSTD, 101 offices were audited including 82 State tax offices/Assessment circles. Some illustrative cases on incorrect assessment, excess availing of input tax credit and excess refund are detailed below :

2.5.1 Short levy of tax due to incorrect assessment

As per Rule 38 of the KVAT Rules, 2005, where an assessing authority resorting to best judgment assessment under Section 22 or Section 23 or Section 24 deems it necessary to verify the books of accounts of the assessee, such authority may serve on the dealer a notice in Form No. 17 calling upon him to produce the books of accounts or other records or evidences, if any, to prove his turnover and tax liability, and also the correctness of the stock statement, goods or the turnover reported or the input tax credit or the refund claimed, at a time and place to be specified in the notice and shall scrutinise them, if produced, as specified in the notice.

Where the dealer fails to prove the correctness of the turnover, stock etc as above, the assessing authority shall proceed to make the best judgment assessment. The dealer shall be given a reasonable opportunity of being heard before completing the best judgment assessment.

Out of total number of 7,790 assessment completed files 1,640 files were audited. Scrutiny of assessment records relating to seven assessees in seven assessment circles for the periods 2017-18 and 2018-19 revealed irregular assessments by the assessing authorities due to turnover escaping assessment, application of incorrect rate of tax, irregular exemption, irregular allowance of input tax and irregular assessment of CST. The above discrepancies in assessment resulted in short levy of tax and interest amounting to ₹ 6.33 crore as detailed in the **Appendix – XVII**.

Recommendation: It is recommended that the department may ensure proper scrutiny of records by the assessing authorities while finalising the assessments in order to avoid irregular assessments.

2.5.2 Short levy of tax due to excess availing of input tax credit

As per Section 6(7) of KVAT Act, sale of any building materials, industrial inputs, plant and machinery including components, spares, tools and consumables in relation thereto to any developer or industrial unit or establishments situated in any Special Economic Zone in the State for setting up the unit or use in the manufacture of other goods shall, subject to such conditions or restrictions, as may be prescribed, be exempted from tax. As envisaged in Rule 12A of KVAT Rules, where taxable goods are used during a return period partly in relation to taxable transaction and partly in relation to exempted or non-taxable transaction, the IPT paid or special rebate to

which the dealer has become entitled to during such period shall be apportioned between the taxable and exempted/non-taxable transaction on the basis of the ratio of taxable and exempted turnover during the period in which the input tax credit or special rebate or refund is claimed. The portion of the input tax credit or special rebate allocable to such exempted sale or transaction shall be disallowed.

Out of total number of 28,700 self-assessed files, 8,200 cases were audited. Scrutiny of assessment records of M/s Prism Cement Ltd, registered in the rolls of the State Tax Office (STO), Special Circle I, Ernakulam for the periods 2014-15, 2015-16 and 2016-17 and M/s Neptune Readymix Concrete(P) Ltd registered in the rolls of the STO, Special Circle III, Ernakulam for the periods 2015-16 and 2016-17 revealed that the assessees purchased goods in the State which are used for manufacture of ready mix concrete and sold to SEZ as exempted sale. The dealers were not eligible for ITC for the portion of goods used for exempted sale. Total short levy of tax and interest due to excess availing of ITC works out to ₹ 1.43 crore as detailed in the **Table 2.7** below.

Table – 2.7
Assessee wise details of short levy

(₹ in crore)

Name of assessee	Period	Total turnover	Exempted Turnover	IPT allowed	Ineligible IPT	Interest	Total
M/s Prism Cement Ltd	2014-15	72.88	11.32	2.07	0.32	0.15	0.47
	2015-16	77.84	8.85	2.83	0.32	0.11	0.43
	2016-17	68.31	7.05	2.49	0.26	0.05	0.31
M/s Neptune Readymix Concrete (P) Ltd	2015-16	49.57	4.22	1.22	0.10	0.03	0.13
	2016-17	65.91	3.32	1.60	0.08	0.01	0.09
Total					1.08	0.35	1.43

On this being pointed out, the Government stated that in the case of M/s Prism Cement Ltd, notice under section 25(1) was issued for the year 2014-15 and assessment for the year 2015-16 and 2016-17 were completed creating demands of ₹ 58.41 lakh and ₹ 75.32 lakh respectively. In the case of M/s Neptune Readymix Concrete(P) Ltd, the assessments for the years 2015-16 and 2016-17 were completed creating an additional demands of ₹ 14.18 lakh and ₹ 9.94 lakh respectively and advised for revenue recovery.

Recommendation: *The Department may try to find out similar cases of tax evasion and take steps for reversal of IPT in such cases.*

2.5.3 Short levy of tax due to excess refund

- As per Section 6(7) of KVAT Act 2003, sale of any building materials, industrial inputs, plant and machinery including components, spares, tools and consumables in relation thereto to any developer or industrial unit or establishments situated in any Special Economic Zone in the State for setting up the unit or use in the manufacture of other goods shall, subject to such conditions or restrictions, as may be prescribed, be exempted from tax.
- As per proviso below Section 11(3) of KVAT Act 2003, where sale in the course of interstate sale is exempted from tax, input tax credit shall be limited to the amount of IPT paid in excess of five *per cent* of the purchase turnover of such goods sent outside the state.
- As per Rule 12A of KVAT Rules, where taxable goods are used during a return period partly in relation to taxable transaction and partly in relation to exempted or non-taxable transaction, the input tax paid or special rebate to which the dealer has become entitled to during such period shall be apportioned between the taxable and exempted or non-taxable transaction on the basis of the ratio of taxable and exempted turnover during the period in which the input tax credit or special rebate or refund is claimed. The portion of the input tax credit or special rebate allocable to exempted sale or transaction shall be disallowed.
- As amended by Kerala Finance Act 2017, Section 6 of KVAT Act provides that the sale of packing materials by a registered dealer to an exporter for the purpose of use in the packing of exported goods shall be exempted from the tax for the period up to 31 March 2016.
- Interstate sales turnover of rubber sheet supported with C Form is exempted from tax vide G.O(P) No.181/2011/TD dated 30 November 2011.

Out of total number of 1,230 refund files, 902 files were audited and scrutiny of records in two offices revealed excess refund amounting to ₹ 0.60 crore in respect of three assesseees as detailed in the **Table 2.8** below:

Table – 2.8
Assessee wise details of excess refund availed

Sl No	Office	Name of assessee	Section under KVAT/CST/ KGST Act	Gist of objection
1	STO, I Circle Kalamassery	M/s Leetha Pack Pvt Ltd	Section 6 of KVAT Act as modified by Kerala Finance Act 2017, Rule 12A of KVAT	Audit observed that in 2014-15 and 2015-16, 56.45 <i>per cent</i> and 66.86 <i>per cent</i> out of ITC availed by the assessee related to sales of packing materials to an exporter which should have been disallowed in conformity with the provision of Act/Rules. The net tax

Sl No	Office	Name of assessee	Section under KVAT/CST/ KGST Act	Gist of objection
			Rules	due including interest payable by the assessee after disallowing IPT proportionate to exempted sale for the years 2014-15 and 2015-16 works out to ₹ 11.50 lakh. While the assessee was liable to pay the output tax of ₹ 11.50 lakh, refund of ₹ 3.24 lakh was ordered by the State Tax Officer, resulting in short levy of tax and interest of ₹ 14.74 lakh.
2	STO, I Circle Kalamassery	M/s Amy Jewellery Designers	Rule 12 A of KVAT Rules	M/s Amy Jewellery Designers was allowed a refund of ₹ 3.94 lakh in October 2018 for the year 2016-17. Scrutiny of the refund file revealed that the portion of input tax credit and special rebate of ₹ 6.87 lakh allocable to interstate stock transfer out which was to be disallowed was not done, resulting in short levy amounting to ₹ 3.55 lakh. Against the tax liability of ₹ 3.55 lakh the assessee was given an irregular order for refund of ₹ 3.94 lakh, resulting in short levy of tax and interest of ₹ 7.49 lakh.
3	STO, Special Circle (Produce), Mattancherry	M/s Njavallil Latex Pvt Ltd	Section 6(7), Proviso below Section 11(3) of KVAT Act, Rule 12 A of KVAT Rules	<p>Scrutiny of the assessment records of M/s. Njavallil Latex Pvt Ltd, for the period 2015-16 revealed that interstate sale of rubber sheet worth ₹ 6.25 crore is supported with C form. The input tax relating to the purchase turnover of exempted goods was not eligible for credit. However, the assessee availed credit for purchase related to exempted turnover resulting in excess credit of ₹ 27.70 lakh.</p> <p>Moreover, the assessee sold rubber latex to SEZ for ₹ 1.20 crore and ₹ 1.09 crore during 2015-16 and 2016-17 respectively and claimed IPT on account of this exempted turnover. This resulted in excess credit of ₹ 5.59 lakh and ₹ 4.80 lakh.</p> <p>The ineligible IPT for the portion of goods thus used for exempted sale worked out to ₹ 33.29 lakh and ₹ 4.80 lakh for 2015-16 and 2016-17 respectively. Without disallowing the ineligible IPT, refund of ₹ 1.25 crore and ₹ 1.63 crore for 2015-16 and 2016-17 respectively was made to the assessee which resulted in excess refund of ₹ 38.09 lakh.</p>

On this being pointed out, the Government stated (May 2020) that in the case of M/s Leetha Pack Pvt Ltd, an additional demand of ₹ 14.33 lakh was created and the assessee remitted ₹ one lakh under Amnesty scheme. The reply is not

acceptable as the tax element alone worked out to ₹ 9.95 lakh whereas the recovery is limited to ₹ one lakh. Clarification has been sought from the Government about the remittance of ₹ one lakh under amnesty scheme. Further reply is awaited. In the case of M/s Njavallil Latex Pvt Ltd., the Government stated (February 2020) that the assessing authority completed the assessment creating an additional demand of ₹ 36.28 lakh for the years 2015-16 and 2016-17. In the case of M/s Amy Jewellery Designers the Government stated (March 2020) that an additional demand of ₹ 8.04 lakh was created.

Recommendation: It is recommended that the department may ensure that sanction of refunds by the assessing authority which involve large amounts are being scrutinised by a higher authority.