

PART – II

Recommendations/Observations

The Banks and other Financial Services accept deposits and channels those deposits into lending activities, either directly or through capital markets and connect customers with capital deficits to customers with capital surpluses by acting as Financial Intermediary. The Service Tax on the Banking and other Financial Services (BFN) was levied with effect from 1 July, 2001 and it is a major contributor to Service Tax revenue. Its contribution during the years 2007-08 and 2008-09 was 7.09 per cent (` 3634.94 crore out of ` 51,301.79 crore) and 6.15 per cent (` 3747.65 crore out of ` 60,940 crore) respectively. Audit conducted a comprehensive review of the performance of this sector with a view to (i) seek assurance that the mechanism to identify and bring in potential assesseees to tax net is effective enough; (ii) examine the rules, regulations and procedures to identify ambiguities and lacunae therein, and (iii) to identify instances of non-compliance with rules leading to loss of revenue. The Committee's examination of Service Tax on Banking and other Financial Services revealed several procedural deficiencies in registration of assesseees, receipt of returns and scrutiny of returns. Further, instances of non-compliance with rules and provisions on incorrect valuation, incorrect/excess availment and utilization of cenvat credit, non-remittance of Service Tax, etc. had resulted in revenue leakages. Furthermore, Service Tax of ` 1.41 crore was collected but not remitted to the Government. These issues alongwith the related issues have been examined in detail by the Committee and commented upon suitably in the succeeding paragraphs.

2. While the law clearly envisages that every person liable to pay Service Tax has to apply for registration within a period of 30 days from the date of commencement of businesses, the Committee note that, in 26 out of 60 Commissionerates, there were 1142 service providers, who, though liable to pay Service Tax , were not available on the departmental registration lists. Out of

these 1142 assesseees, 65 potential assesseees had not paid Service Tax to the extent of ` 92.12 crore with additional penalty upto ` 92.12 crore and further interest liability of ` 21.35 crore. The Committee were apprised that out of 65,17 cases involving Service Tax of ` 46.12 crore have not been accepted by the Government. In respect of 19 Audit objections involving Service Tax of ` 36.47 crore, necessary remedial measures have been taken to recover Government revenue. 17 cases involving Service Tax of ` 5.34 crore were pending investigation. While deploring the belated remedial measures being taken by the Department, the Committee should like to be apprised of the latest status of cases that are pending investigation within 03 months of the presentation of this Report and also the detail of the 17 cases not accepted by the Government and the reasons therefor.

3. The Committee are concerned to note that out of 1074 cases of non-registration pointed out in Audit, only 370 cases had been verified by the Ministry, 21 cases were under investigation and in case of 188 service providers verification report was yet to be received as on 31.07.2012. In case of Bangalore Service Tax Commissionerate, out of 725 cases only 208 service providers had been verified and the verification of remaining 517 cases was underway but obviously hamstrung due to paucity of staff. Furthermore, while admitting the problem of non-registration of Service Tax assesseees, the Secretary, Department of Revenue testified before the Committee that till 2010, they had no means to find out as to which of the assesseees were effectively into the system and underlined the need for building up a good electronic system and engagement of additional manpower to deal with the problem. The Committee are concerned to note that though Service Tax was levied with effect from 1 July, 2001, no whole-hearted and sustained efforts have been made by the Ministry either to build up a good electronic system for this purpose and engage the additional manpower. Apparently, the Service Tax was levied without working out the methodology for its effective implementation even after having realized the immense revenue potential of Service Tax and its rampant evasion. The Committee would like to be apprised about the efforts made by the

Department during the last 11 years to ensure that the work of collection of Service Tax from Banking and other Financial Services does not suffer for want of manpower and introduction of good electronic system. The Committee further recommend that the verification of 517 cases be expedited and they be apprised of the same.

4. Notably, the Government have largely relied on “Voluntary Compliance” for registration of eligible service providers. The Committee have been informed that to make the service providers aware of the registration, the Department has been running a media campaign by issuing a number of advertisements in the print/electronic media, displaying outdoor hoardings, etc. Further, help desks have been set up in the Commissionerates for answering the tax payers queries and the problems faced by them. Seminars have been organized in Mumbai, Chennai, Kolkata, Delhi, Ahmedabad, Hyderabad, Jaipur, Chandigarh and Bangalore. While Voluntary tax compliance is a laudable objective, the considered view of the Committee is that the results have been far from encouraging. The Committee feel that with proper focus on non-intrusive but penetrating methods of collecting data through the instruments like returns and surveys, the Government would be able to widen the tax base and ensure better tax compliance. The Committee urge the Ministry to make all out efforts to ensure that while the Government remain assessee-friendly, tax evaders are dealt with stringently and that non-compliance becomes a costly proposition. The Committee are also of the opinion that if need be, measures taken in respect of Central Excise and Customs assessees also be taken with regard to Service Tax assessees i.e. for registration of eligible BFNs.

5. As per the action plan issued in May 2003 by the Director General of Service Tax, Mumbai, field surveys had been identified as one of the important mechanisms to identify and broaden the tax base. The Committee are disappointed that none of the 60 Commissionerates test checked in Audit had fixed any targets for surveys during 2007-08 to 2008-09 and no surveys were conducted in 27 out of 60 Commissionerates. Out of 32 Commissionerates,

where surveys were conducted, in 9 Commissionerates 154 new service providers of BFNs were registered. However, no new service provider could be registered through surveys for this service in remaining 23 Commissionerates. In 32 Commissionerates where surveys had taken place, the outcome was not monitored as prescribed in the DGST circular. Moreover, during the years 2009-10 and 2010-11 although the number of surveys conducted was 113 and 87 respectively, no assesseees were registered thereafter. Again, during the year 2011-12, out of 1003 surveys conducted only 90 assesseees were registered realizing ` 0.44 crore only as a Service Tax . The Committee deplore that field surveys, construed as an important mechanism for widening the tax net have not been carried out with right earnestness by the Commissionerates. The Committee are dismayed that the Department was devoid of any mechanism to assess, monitor and enhance the efficiency of survey operations. Though instructions have been issued to filed formations on 23-11-2011 to create special cell in each Commissionerates mandated with the task of identifying potential assesseees, the Committee find the reply of the Ministry silent regarding the status of creation of these cells in all the Commissionerates, the number of cells created so far and the number of service providers that were brought to the tax net as a result thereof. The Committee believes that these survey operations, if conducted methodically and efficiently, would discover new assesseees and bring additional tax revenue to the Government. The Committee would like to be apprised of the present position of creating these cells Commissionerate-wise and the outcome thereof.

6. The Committee find that a large number of returns for Service Tax by BFNs were either not received or received late by the Department. During the period September 2004 to March 2009, about six per cent of the returns were received late and 14 per cent of the returns were not received at all. Surprisingly, the Commissionerates had not followed any monitoring mechanism to ascertain the reasons for non-submission of returns. The Committee note that amongst the returns not received, 301 service providers, whose annual receipts had exceeded ` four lakh during the year 2005-06 had not submitted the returns for

the year 2006-07. Further, 440 service providers whose annual receipts had exceeded ` eight lakh during the year 2006-07 had not submitted the annual returns for the year 2007-08. Similarly, 513 service providers whose annual receipts had exceeded ` ten lakh during the year 2007-08 had not submitted the returns for the year 2008-09. The Committee are deeply concerned to note that the Department had not initiated any action to ascertain the reasons for not filing annual returns. The Committee further find that the Department had not levied penalty on defaulting assesseees which constituted about 97 percent of the total amount leviable (` 4.50 crore). Apparently, the defaulting assesseees are either allowed to go scot-free or let off with lighter punishment. The Committee, therefore, recommend that the Ministry devise a foolproof system so as to ensure that all the BFN assesseees, taxable under Service Tax Rules file their returns regularly. The Committee should be informed within 3 months about the system so desired. Further, defaulting assesseees be suitably penalized to act as a deterrent.

7. The Committee further observe that 7 assesseees in Nagpur Commissionerate had not filed their Service Tax returns but they had continued to provide services which were subjectable to tax during the period of non-filing. This resulted in non-payment of Service Tax of ` 20.33 lakh and interest of ` 4.97 lakh. It was submitted before the Committee that protective Show Cause Notices have been issued on 13.10.2011 in respect of all the said 7 cases and that instructions have been issued to field formations on 14th and 27th July, 2011 to create special cell in each Commissionerate mandated with the task of identifying potential assesseees and stop filers. The Committee, therefore, recommend that field Commissionerates should periodically monitor the cases where assesseees have stopped filing returns and the Committee be apprised by the Ministry about the latest position with regard to Show Cause Notices issued, within 03 months of the presentation of this Report.

8. Every individual liable to pay Service Tax has to assess and voluntarily pay the tax. Further, half-yearly returns are to be furnished to the Department. An assessee failing to furnish timely returns is liable to pay a penalty subject to a maximum of ` 1000. The information furnished by the Ministry relating to BFN for the period September 2004 to March 2009, reveals that out of 2,37,593 returns due during the said period as many as 18,684 were not received. The Committee further note that out of ` 60.32 lakh of penalties levied, penalties of ` 25.22 lakh has not been recovered. While emphasizing the need for effective monitoring of Service Tax returns and timely recovery of penalties imposed, the Committee would like to be informed about the current position with regard to recovery of outstanding penalties of ` 25.22 lakh, and the efforts made by the Ministry to ensure timely recovery of outstanding dues within 03 months of the presentation of this Report. The Committee also strongly express the need for taking stringent action against the defaulters and also have a re-look at the penalty provisions as the present penalty is insufficient to act as a deterrent with regard to non-submission of returns.

9. The Committee are shocked to learn that the vital database of the actual number of BFNs filing returns and those who have failed to do so, is not available with the Department. The Committee was informed that such data base is not being developed by the Directorate General of Service Tax. Further, the registered assesseees who were not filing Service Tax returns are issued Show Cause Notices. Obviously, the Department cannot function effectively and monitor their collection of Service Tax from BFNs in the absence of vital database. The Committee would, therefore, urge the Department of Revenue to put in place an effective mechanism to facilitate monitoring of the progress of revenue receipts and processing of returns on a periodical basis.

10. Audit scrutiny of returns revealed that during 2008-09 (i) in 67 Commissionerates 12.38 per cent returns received were pending preliminary verification/scrutiny; (ii) in 22 Commissionerates, there were 99 cases in which

Department failed to detect irregularities like payment of Service Tax at lower rate, non-levy of interest and penalty, short payment of interest, etc. leading to short levy of Service Tax totalling ` 7.02 crore and interest of ` 1.56 crore; (iii) there was no system in place to co-relate the taxable income as shown in the Income Tax return with the ST-3 return; and (iv) 116 assesseees had shown lower figures in ST returns which had Service Tax implication of ` 21.91 crore and interest of ` 2.94 crore during the period from September 2004 to March 2009. Accepting the Audit observation, the Department issued Show Cause Notices for ` 9.43 crore in July 2010. On the issue of 12.38% of returns that were received and were pending preliminary verification/scrutiny, the Committee have been apprised that norms for scrutiny of returns have since been fixed and Service Tax Return Scrutiny Manual has been prepared, guidelines have been issued for checking/verifying the ST-3 returns. Further, electronic filing of Service Tax returns made mandatory w.e.f. 01.10.2011, the system of Automation in Central Excise and Service Tax (ACES) has been introduced throughout the country and instructions have also been issued by CBEC on 21.02.2012 that the function of detailed scrutiny be implemented in all the Ranges. The Department, however, could not furnish reasons for their failure to have timely verification/scrutiny of returns. The Committee would like to be apprised of the revenue due and realized as a result of the various corrective measures initiated by the Ministry and recommend a comprehensive review for identification of bottlenecks, if any, in the present system of scrutiny of returns, and overcome the same through appropriate policy intervention.

11. The Committee are distressed to note that no system exists in the Department to co-relate the taxable income as shown in the Income Tax Return with the ST-3 returns to identify cases for further scrutiny. Cross verification of a few ST returns with Income-tax returns had revealed Service Tax implication of ` 21.91 crore and interest of ` 2.94 crore during the period September 2004 to March 2009. Consequently, the Department issued SCNs for ` 9.43 crore in July 2011. Taking note that the Ministry had initiated steps to safeguard the revenue interest, the Committee recommend a suitable but effective system be devised

for correlating the data of various Departments and ensuring that the revenue due to the Government is collected without remiss.

12. As per Rule 5(2) of Service Tax Rules, 1994, 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. Despite clear statutory provision, the Committee note that 26 per cent of service providers had not given the list of books of accounts maintained by them. During the period from April 2007 to March 2009, in 10 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 BFN. The Committee are surprised that the Commissionerates did not pursue these cases to ascertain the reasons for non-submission of these details. The Ministry attributed staff crunch and lack of proper training to the available staff of Service Tax Department as the main hurdles in the implementation of the Service Tax Rules. Since effective scrutiny of relevant books of accounts is imperative for ensuring proper assessment of Service Tax, the Committee urge the Ministry to take urgent measures to augment the staff strength and also to train the Service Tax staff for developing a better understanding of the various books of accounts maintained by BFN assesseees. The Committee should like to be apprised of the necessary follow-up action taken in this direction and the outcome thereof. Further, as regards the strategy formulated to obtain list of books of accounts alongwith the returns from defaulters, the Department reported that non-compliance with the Rule 5(2) of the Service Tax Rules 1994 invites penal action and a letter has been issued to field formations to ensure compliance to the said Rule. The Committee would like to be apprised about the number of defaulters prosecuted so far as a result thereof.

13. The Committee further find that there were 110 cases of wrong availment of exemption or abatement during 2009-10 and 91 cases during 2010-11. The amount of Service Tax involved therein is ` 339.47 crore and ` 250.07 crore

respectively. The Committee are concerned to note that only ` 10.53 crore and ` 20.23 crore respectively have been recovered by the Department. Further, zone-wise details as received from the Ministry indicates that maximum number of wrong availment of cases have been noticed in the Kolkata zone. While 27 cases during 2009-10 and 16 cases during 2010-11 involving Service Tax of ` 157.64 crore and ` 204.85 crore respectively were noticed in Delhi zone, out of which only ` 0.0019 crore has been recovered during the year 2009-10. Similarly, 64 instances of undervaluation with short payment of Service Tax of ` 53.80 crore was detected in the Audit. The Committee are concerned to note that the entire process involved has resulted in locking up of substantial revenue for the years 2009-10 and 2010-11. The Committee, therefore, urge the Government to revisit the extant provisions of Service Tax law and the rules framed thereunder so as to ensure that the Service Tax dues are collected effectively and within the given time frame.

14. In terms of Rule 4 of the Cenvat Credit Rules, 2004 credit of Service Tax paid on any input service is allowed to a provider of taxable service. The Committee notice incorrect availment and utilization of cenvat credit totaling ` 105.30 crore by providers of banking and financial services in 75 cases including interest of ` 6.26 crore. The Committee have been apprised that in 46 cases involving ` 52.59 crore, proceedings have been initiated by issuing Show Cause Notices to the defaulting service providers and 8 cases involving ` 5.47 crore are pending investigation. The Ministry has not submitted the reasons for allowing Cenvat Credit incorrectly. Furthermore, in cases where the Ministry has differed from Audit, no justification has been adduced before the Committee. Merely issuing Show Cause Notices cannot be construed as action taken by the Ministry. The Ministry needs to explain to the satisfaction of the Committee the reasons for the same and also the initiatives taken to ensure that all such leakages are plugged and that there are no such recurrences.

15. The Committee further find that as per the provisions, the assessee was liable to restrict the utilization of cenvat credit to 20 percent of the Service Tax payable during the period 2006-07 and 2007-08. Out of the 24 months in 2006-07 and 2007-08, the assessee paid Service Tax of ` 1198.04 lakh in 12 months. While the utilization of cenvat credit to make these payments should have been restricted to ` 239.61 lakh (20 percent) the actual utilization was ` 626.65 lakh. This led to excess utilization of credit of ` 387.04 lakh which was recoverable with interest of ` 95.84 lakh. The assessee also did not maintain separate accounts for receipt, consumption and inventory of input services used for taxable and exempted services. The Committee have been informed that the field formations at the time of scrutiny of returns and while auditing the records of the party take necessary measures to stop revenue leakages on this count. The Committee seek explanation as to how the mechanism failed in these cases which resulted in a considerable loss of revenue to the Government. The Department has reported that SCN of ` 5.52 crore (period 2005-06 to September 2009) including ` 387.04 lakh had been issued in March, 2010, which is pending adjudication. The Committee would like to be apprised about the latest position in this regard.

16. Further, failure to consider the interest on cash credit and overdraft facility which were exempted from Service Tax had resulted in short-payment of ` 515.56 lakh for the period from April 2008 to March 2009 which was recoverable with interest of ` 47.69 lakh. The SCN dated 09.02.2010 issued for the period 2008-09 is pending adjudication. Again, incorrect reflection of cenvat credit in ST-3 returns of M/s Citi Finance Consumer Finance India Limited in Delhi ST Commissionerate for the period April 2006 to September 2006 resulted in excess availment of Cenvat credit to the extent of ` two crore. Show Cause Notice dated 20.10.11 for a demand of ` 199.99 lakh has been issued to the assessee. Having observed that in a large number of cases the basic prerequisite i.e. proper maintenance of records is wanting, the Committee would

like the Ministry to enumerate the concrete measures taken by them to ensure compliance with the instructions regarding maintenance of records.

17. Section 73A of the Finance Act, 1994 (as amended w.e.f 18th 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 should without fail, pay the amount so collected to the credit of the Government. The Committee find that during the years 2007-08 to 2010-11, there have been 2111 cases in which service providers have collected the Service Tax to the tune of ` 1134.82 crore but had not deposited the same in the Exchequer. During the same period, recovery of ` 560.07 crore involving 1343 cases has been effected. Further, out of the 2111 cases, 1065 cases pending realization are under litigation and the revenue involved is to the extent of ` 1043.20 crore. The Committee are perturbed to note that the amount involved in the SCNs issued constitute nearly 90% of the total amount that was collected by the service providers from the consumers but not deposited with exchequer. The Committee desire that the adjudication process be expedited and recoveries be made at the earliest.

18. The Committee note that there is a lack of perspective planning in the matter of deployment of staff on such a vital source of revenue collection viz., Service Tax. Taking into consideration the amount of revenue collected from Service Tax and Central Excise during the year 2011-12, the Committee are surprised to find that in contrast to the deployment of nearly 40000 officers for excise, only 4000 to 5000 officers have been deployed for Service Tax stream and that too after withdrawing from the Central Excise stream. Apparently, Service Tax wing has been working for more than 15 years, with no staff of its own. The Committee are dismayed to note the helplessness expressed both by the Finance Secretary and Chairman, Central Board of Excise & Customs in this regard especially when, Ministry of Finance is itself one of the nodal authorities for examining and sanctioning requisite staff to Ministries. The Committee feel that the staff requirement be examined on priority basis by the concerned

authorities in order to ensure that the Service Tax Collections, which have increased phenomenally from ` 407 crore in 1994-95 to ` 97,389 crore in 2011-12 does not suffer for want of human resource.
