

Bangalore Chamber of Industry and Commerce

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1. Preamble

It is now almost six years since value added tax regime has been implemented and it is now time for introspection and ringing in changes to the law and procedures. We have in the past raised several issues, which affect the industry at large through various memorandums. Some of the issues that concern the trade and industry that require amendments to law / clarification / issue of notifications etc., are detailed below:

2. Uniformity in law across States

Presently, there is no uniformity in respect of VAT laws across States. Each State has its own definitions / notifications / schedules / rates of tax / list of goods, etc., resulting in chaos leading to innumerable litigations. Although, the States had experimented to bring in uniformity only with respect of rates of taxes (floor rates), this was an absolute failure with each State issuing notifications reducing / exempting taxes in respect of certain commodities. This has resulted in tax / trade wars amongst States causing a lot of heartburn to developing States. It is of utmost importance to ensure that such aberrations do not continue since the VAT law is in place and more so since Goods and Services Tax is on the anvil. However, this issue presently seems to have taken a back seat. This fact becomes clear when one goes through the VAT law of different States including our own States. This issue, if adequately addressed, would put to rest the issues that are hitherto litigated under the sales tax laws.

3. Uniform classification of goods across States

While it is desirable to have a uniform classification of goods across States, it has not been the practice under the existing sales tax laws. There was an attempt made by the States to usher in uniformity in rates of tax during the year 2000. Most States for reasons best known to them have not adhered to this. In order to usher in the VAT law, which is expected to be simple, transparent, easy to understand and consequently generate buoyant revenues, it is desirable to:

- Classify goods on HSN basis. This would ensure uniformity in classification across States.
- The ideal way of classification of goods would be to follow the HSN system since it will bring in uniformity in classification in respect of all indirect tax levies in the Country.
- The same VAT rates should be applied across States in respect of similar goods.
- The set off provisions should be uniform across States in respect of similar commodities / trade.
- There should be no disparity in respect of branded / unbranded, man-made / machine made, packed / unpacked, etc., under the harmonized system of classification of goods.
- Exemptions / reduction in tax rates should be uniform across the States.
- Similar provisions must exist across States in respect of computation of taxable turnovers.

4. HSN Classification

There are a number of commodities, which have been either classified as inputs or capital goods that are clearly not in consonance with the HSN classification adopted under the central Excise laws. It is also brought to your notice that the classification is not uniform across States that have adopted VAT. **In case there is an amendment to the Central Excise Tariff Act, there is no provision under the VAT law to suitably take care of such amendments.**

Recommendation

We request you to kindly re-look into the said anomaly and make suitable amendments to create a level playing field.

5. Capital Goods

a. Parts and accessories of capital goods

The present definition of capital goods is silent as to whether parts and accessories of capital goods will be treated as capital goods or as inputs.

Recommendation

It is suggested that necessary clarificatory amendment be made to include parts in the definition of capital goods.

b. Installation, erection, testing & commissioning

Trade and industry invest substantial amounts in respect of buildings / factories where production / offices / warehousing facilities are located. The present VAT laws / rules does not provide for tax paid on inputs used for construction although such buildings are in the nature of capital assets. It is our request that input taxes paid on inputs used in such construction must be permitted set-off by bringing in buildings / factories within the scope and definition of the term capital goods.

Recommendation

It should also be clarified that the input tax paid on capital goods would include input tax paid on incidental expenses like erection, modification and improvements to bring the capital goods to its present location and condition.

The credit should be made fully VATable if the capital goods are used in relation to taxable goods. In other words, the capital goods should not be subject to partial rebating if it is used in relation to both taxable and exempt goods akin to Central Excise Rules. As a natural consequence, section 19(2) of the KVAT Act should be suitably amended. Instead it should be provided that if the use of capital goods is changed, to be exclusively used in relation to non-taxable transactions like Stock

transfer outside the State or exempt goods, the credit should be reversed after providing for reasonable depreciation for use. If the capital goods are sold on payment of output tax or CST, no reversal should be insisted as the State has realised the tax due to it. Suitable amendments should be made in Section 19. Where capital goods are procured on lease basis, in the hands of the lessee, the tax reimbursed to the lessor should be treated as input tax and not as tax paid on capital goods. Otherwise, the taking of credit on equated installments would be cumbersome.

Section 2(19) defines input. It refers to various activities undertaken while carrying on a business as well as "for any other use in business". It is suggested that section 2(19) should be amended to say that input means any goods including capital goods purchased by the dealer in the course of his business. There is no need to refer to activities like manufacturing/resale.

The reference to prevailing market price is likely to create more confusion. There are many goods for which wholesale price in the market cannot be ascertained. Hence it may be deleted. Consequential amendments should be made to various sections.

6. Time of sale of goods – Section 7

Section 7 dealing with time of sale of goods creates unintended hardship to the dealers. For instance, if tax invoice is not raised within 14 days of incorporation of goods in execution of any works contract, the date on which the incorporation takes place is deemed to be the time of sale. It is practically impossible to determine the value of such goods and pay output tax. In the case of lease, it raises questions as to when the tax is to be paid; whether on delivery of goods on the whole amount of lease rent payable under the contract or on monthly lease rentals as is being charged now.

Recommendation

It is submitted that during the last 48 years of implementation of KST Act, no serious legal or practical difficulties were encountered in the absence of the definition of time of sale. **Hence section 7 may be deleted.**

7. Tax Deducted at Source – Section 9-A

Section 9-A should be amended to clarify that the tax required to be deducted should be with reference to net tax payable. There are practical problems in implementation of section 9-A. The contractor is liable to pay tax in the next month whereas the credit is given only when the contractee remits the taxes deducted. The wordings in section 9A(7) imply that the deduction from output tax payable would be given only if the output tax on a particular contract for which tax has been deducted at source is included in the relevant monthly returns. This is not practical. In many cases, the contract would have been executed and in the month of deduction of tax, no output tax is payable in respect of such contract.

It is also possible that the contractor engages the services of a sub-contractor on a back to back basis. In those cases, the taxes deducted by the awarder on the principal contractor. The principal contractor is entitled to deduction on sub-contract payments while computing the taxable turnover resulting in refund of taxes deducted by the awarder.

Recommendation

Therefore, it is suggested that the credit should be given without linking it to output tax on a particular contract. It should be simply stated that deduction is allowed from the output tax payable for the month or quarter in which the certificate of deduction is received.

In cases where, back to back contracts are entered into by the principal contractor, the law must be suitably amended to either transfer the credits or for non-deduction of tax by the awarder on the principal contractor.

8. Issues relating to input tax set-off

Purchases from URD

The input tax paid on purchases from unregistered dealers is given a deduction only when the output tax is payable on sale of goods in which such goods are put to use. One-to-one correlation is insisted on purchases from unregistered dealers unlike purchases from registered dealers. There is no logic in treating the purchases from unregistered dealers and registered dealers differently. Tax is also paid on purchases from unregistered dealers.

Recommendation

Therefore, the purchases from unregistered dealers should be treated on par with purchases from registered dealers and instant deduction should be permitted. Section 11(a)(8) may kindly be deleted. References to section 3(2) in Section 10(4) should be deleted.

9. Input tax set-off on free samples and warranty replacements

Issue

Input tax credit would be denied on goods issued as free samples or as warranty replacements.

Recommendation

It is recommended that input tax set-off should not be denied in respect of goods supplied as free samples or as warranty replacements that are dispatched within or outside the State of Karnataka. Alternatively, it is suggested that such supplies should be zero rated by suitably amending section 20 of the KVAT Act.

10. Discounts

With effect from 01.04.2006 the Government of Karnataka introduced the Karnataka Value Added Tax (Second Amendment) Rules, 2006 vide notification FD 124 CSL 2006 dated 27.05.2006. In terms of the said rules the proviso to rule 3(2)(c) was amended. The relevant rule prior to and after amendment is as follows:

Prior to amendment & up to 31.03.2006 the law stood as follows:

All amounts allowed as discount:

Provided that such discount is allowed in accordance with the regular practice of the dealer or is in accordance with the terms of any contract or agreement entered into in a particular case; and

Provided further that the accounts show that the purchaser has paid only the sum originally charged less discount.

After amendment and from 01.04.2006

All amounts allowed as discount:

Provided that such discount is allowed in accordance with the regular practice of the dealer or is in accordance with the terms of any contract or agreement entered into in a particular case ***and the tax invoice or bill of sale issued in respect of the sales relating to such discount shows the amount allowed as discount;*** [words in italics have been inserted with effect from 01.04.2006] and

Provided further that the accounts show that the purchaser has paid only the sum originally charged less discount.

Facts & issues

Generally discounts arise or are allowed by the selling dealer under the following circumstances among others:

1. Discounts allowed in the invoice – either quantity or value;
2. Volume discounts allowed in the invoice – once the buying dealer purchases a particular quantity;
3. Off-take discounts – or target discounts - it may be value or quantity – generally such discounts are known (after the tax invoice is issued) when a particular milestone is achieved – say if one ton is purchased in a year or period etc.,

4. Seasonal discounts – selling dealer allows such discounts during say a festival season or during a period when the sales are low;
5. Any other parameters agreed between the buyer and seller.

Except in cases 1 & 2 above, normally the discount rates / amounts / percentages are known only on occurrence of a particular event or on achieving a particular target or milestone. Thus, such discounts cannot be shown / allowed on the face of the invoice. However, the selling dealer issues a credit note for such discounts at a later point in time.

In each of the above situation there was no liability to tax under law till 31.03.2006. However, with effect from 01.04.2006 the discounts stated in 3, 4 & 5 above would not be allowed as deduction while computing the taxable turnover of the selling dealer on account of the amended rule which inter-alia provides that *“and the tax invoice or bill of sale issued in respect of the sales relating to such discount shows the amount allowed as discount”*.

The nature of discounts stated in 3, 4 & 5 above cannot be reflected in the invoice or bill of sale since the very nature of discount itself is on the occurring of a particular target / milestone. Thus, the above amendment is not in accordance with law and ought to be omitted / deleted and the original position of law restored. It will not be out of place to mention that the amended rule [***and the tax invoice or bill of sale issued in respect of the sales relating to such discount shows the amount allowed as discount***] is against the principles of law laid down in the case of **Motor Industries Co. Ltd., Advani Oerlikon Ltd., Belgaum Structurals case etc.**

The levy of tax under the scheme of the Act is as ad-valorem. Therefore, the levy of tax is attracted on the sum of money received or receivable as consideration for sale of goods, which is mutually agreed upon by the seller and the buyer. Where, subsequent to issue of a tax invoice / bill of sale, the sales consideration gets reduced on account of allowance of trade discount, it is such reduced sum which constitutes the sale consideration which alone is receivable or received and can be subjected to tax under the Act. {Sec 2(29)}

The law relating to discounts that existed prior to its amendment (stated above) was a settled position of position of law. The said rule existed even under the KST Act, 1957. There was no litigation in respect of discounts. The purpose of the said amendment is not known although there could have been some unscrupulous dealers who may have taken advantage of the old provisions by not accounting properly. It may not be right on the part of the Government while impliedly trying to plug possible revenue leakage, to cause undue hardship to a large number of bonafide dealers by amending the relevant provisions relating to discounts. However, on its amendment from 01.04.2006 it appears that:

- Litigation is likely to abound;
- Bonafide dealers are put to undue hardship;
- A well-settled position of law is being tinkered with for no authentic reasons;
- Similar provisions do not exist in any sales tax / VAT laws in the country;

- Judgements of various Courts have not been followed and are given the go-by.

We are unable to understand the rationale as to why the time-tested procedure / provision relating to discounts have been done away with and yet another new proviso has been introduced. It will be extremely difficult for both the selling and buying dealers.

Suggestion

It is suggested that the time-tested procedure / provision relating to discounts be re-introduced as it is simple and easy to administer both from the point of view of the dealer and the department. We hope this request of ours will be considered favourably.

11. Purchases from unregistered dealer - Total turnover for composition scheme

Issue

The total turnover for the purpose of composition scheme, as defined in the Act, includes purchases from unregistered dealer. A retrospective amendment was introduced wef 01.04.2006 in terms of which a works contractor was required to pay tax on purchases effected from unregistered dealers.

Recommendation

It is submitted that the value of such purchases should be excluded while determining the total turnover for the purpose of composition. This is on account of the fact that purchase tax would have already been paid by the dealer. The benefit of such deduction, as extended to other composition dealers, must also be extended to the works contractor who opted to pay tax under composition dealers.

Insertion of a proviso requiring a dealer to pay tax with retrospective effect is unconstitutional and requires an amendment deleting such proviso.

12. Developers & Contractors carrying on works contracts

The present Rules 136 to 147 dealing with composition are too complicated. In a few cases like denying the benefit of opting for composition if the dealer holds stock, which has been acquired from, outside the State would in fact prevent dealers from exercising option at any time. It is suggested that composition Rules should be made simple. The composition scheme under VAT regime should be broadly in line with the present scheme under the KST Act.

Rules 3(2)(l) of the Rules permits a deduction of labour charges for erection, installation, fixing, fitting out or commissioning. This rule applies where the amount is ascertainable from the books of accounts of the dealer. Rule 3(2)(m) permits a deduction of a fixed percentage on the contract value in case labour charges are not ascertainable from books of accounts. In both the cases, the

Rule refers to only a few of the activities that may fall under works contract like erection, installation etc. The other works contract activities, like manufacture, processing, fabrication, repair, construction are not mentioned. The rule may be amended to say that labour and like charges incurred for execution of works contract would be deductible.

13. Labour and other like charges - substitution of Explanation I

The Government has substituted the existing Explanation – I to rule 3 (2)(l) & 3(2)(m) of the KVAT Rules, 2005. On a reading of the proposed substitution of Explanation I to rule 3 of the KVAT rules the following facts emerge:

- It appears that the amendment restricts the amount of “labour and other like charges” actually expended on a proportionate basis to the value of goods used in the execution of works contract.
- The balances of unutilized deductions will be permitted to be carried forward.

What is not clear in the rule is:

Quote

“.....and if the total turnover is not sufficient to cover apart from other deductions, such taxable turnover and such deduction, they shall be determined and allowed proportionately to the extent of the turnover of the dealer in that period, and the balance shall be carried forward to the following tax period or any subsequent tax period to be determined and allowed in the same manner.”

Unquote

It appears that the explanation introduced by way of single sentence is more complicated than the relevant rule itself. Is it possible for an explanation to be introduced which control the operative part of the rule – it is common understanding that the rule 3 of the KVAT Rules, 2005 provides for determination of total turnover and taxable turnover. Apart from this difficulty there is no clarity emerging in the explanation and the purpose for which the relevant explanation was introduced. Such a complex explanation cannot be comprehended / understood by a normal dealer.

Let us try and make an effort to understand the proposed explanation through two simple examples:

Example 1

Let us assume the following facts - A dealer X receives a sum of Rs. 1,00,000/- from a customer. The dealer X effects payments to registered sub-contractors at Rs. 60,000/-. Labour and other like charges actually expended is at Rs. 20,000/-. In the same example if the dealer X effects URD purchases of sand / jelly then how does one go about answering the above questions.

Example 2

Let us assume the following facts - A dealer X receives an advance of Rs. 1,00,000/-. Assume that the excavation works has commenced and the dealer X effects payments to registered sub-contractors at Rs. 2,00,000/- towards mobilization advance. Labour and other like charges actually expended towards earth-work is at Rs. 20,000/-. In the same example if the dealer X effects URD purchases of sand / jelly then how does one go about answering the above questions.

In both the above scenarios:

1. How does one compute the taxable turnover?
2. How does one compute the gross profit on labour and other like charges?
3. How does one determine the value of goods, the property in which has been transferred in the execution of works contract relating to sub-contract payments?
4. How does one issue a tax invoice in the amended scenario?
5. How does one go about implementing this explanation if one assumes that 10 flats out of a total of 50 flats remain unsold?
6. How does one pay tax without raising a **tax invoice assuming that the proposed explanation I is pressed into operation?**
7. How does one maintain books and records?
8. How does one shift from regular scheme to composition scheme (or vice versa) assuming that there is a carry forward scenario?
9. How practical will it be to implement the operation of the explanation?
10. Is it easy to understand, transparent and simple?

The above issues raised are simple issues in the case of a works contractor. There are much more complex issues in a real time business scenario.

Suggestion

In the background of the above facts it is suggested that the existing explanation 1 be retained.

14. Works Contract - Issue of Tax Invoice

A dealer who is involved in the execution of works contract more specifically a builder or a developer finds it very difficult to raise a Tax Invoice as required under the KVAT Act, 2003 when he receives advances or executes the work etc. The difficulty in raising the Tax Invoices is compounded when he has to comply with rule 3 of the KVAT Rules, 2005. We have been repeatedly insisting that a proper procedure be laid down in the rules to maintain uniformity in collection / assessment / recoveries of tax.

The amendment to rule 27(2)(b) provides that a dealer has to issue a **tax invoice** even under the circumstances, where the dealer has not received the money either as consideration or as advance towards execution of works contract. In this scenario:

1. How does one compute the taxable turnover based on the proposed substitution of explanation I to rule 3(2) of the KVAT Rules, 2005?
2. How does one maintain accounts, books and records as normally works contractors maintain a cash system of accounting?
3. Is the Government proposing a hybrid system of accounting for tax purposes?
4. Does the rule 27 override rule 3 of the KVAT Rules, 2005 and section 7 of the KVAT Act, 2003?
5. Is it possible to imply that the rule 27 of the KVAT Rules, 2005 control the determination of gross turnovers? If yes – then why should rule 3(1)(c) of the KVAT rules exist in the statute book? The explanation I can be converted into a charging provision, which determines the gross turnovers? This may imply that by applying rule 27, the explanation I will become redundant.

Suggestion

The amendment has inherent deficiencies and as such there is no requirement for any amendment since the existing rules serve the purpose.

15. Amendment to rule 29 / 30 - Issue of Tax Invoice

Some of the issues among others that need to be considered are as follows:

1. For a Civil Works Contractor to issue a **tax invoice** is practically not possible based on our objections to the proposed amendments to rule 3 and rule 27;
2. In a majority of the cases relating to purchases of immovable property by the customer, the customer's are not registered dealers and assuming that such buyers are registered dealers the input tax set-off is not permissible in the hands of such buyers. As such the issue relating to furnishing of **tax invoice** being made mandatory is merely of academic interest causing undue hardship to the dealers.
3. All the developers issue receipts to the customers in respect of each payment received which in itself is sufficient proof that such amounts are duly accounted. As such, prescribing a rule, mandating issue of **tax invoice** is nothing but additional paper work.
4. A developer develops many projects / properties across the State at different locations. If the proposed rule mandates issue of tax invoices with consecutive serial numbers at entity level it would be highly impractical.

Suggestion

Considering all the above practical difficulties, it is hereby requested that the Government exempt the civil works contractors from the purview of issuing tax invoices as proposed in the draft rules.

16. Submission of copies of Agreements to the Departments:

Generally developers / works contractors enter into agreements with a large number of customers on a daily basis. Such agreements are generally identical / standard in nature for a particular project and hence it is suggested that one copy of the draft agreement of the particular project be submitted to the department instead of submitting agreements entered into with all the customers, which would be no relevance to the department. The submission of copies of agreements entered into with all the customers to the department, will only increase the paper work / administration work of dealers and the department. Normally copies of the agreements are sought for by the department at the time of assessment / audit / inspection. Filing of one copy with the LVO will be add-ons. If the department still insists that a copy be filed, then no further copies must be insisted at the time of inspection / assessment / audit etc.

Suggestion

Considering the practical difficulties it is suggested that the new provision be deleted.

17. Partial rebating

The formula prescribed under Rule 131 of the KVAT Rules, 2005 is not very clear. If a dealer who is involved in sale of taxable goods, stock transfers etc., then he is required to apply Rule 131. In terms of Section 11(a)(5) read with section 14 of the KVAT Act, 2003 a dealer who effects stock transfer outside the State, is eligible to avail the input tax credit to the extent of 10.5% and the balance is of input tax restricted. If one applies Rule 131, he will be denied the benefit of section 11(a)(5) read with section 14 of the KVAT Act, 2003. A dealer who applies Rule 131 is required to submit a return every six month by re-computing the tax liability as specified in Rule 132.

Recommendation

The formula as specified in Rule 131 must be suitably amended by giving effect to section 11 read with section 14 of the KVAT Act, 2003.

18. Procedural issues – Assessments, Penalties & Appeals

- a. Section 38 does not specifically provide for issue of pre – assessment notice. Section 38 should be amended to provide for a pre – assessment notice. The dealer should be given a time of 30 days from the date of receipt of demand notice to pay the tax.
- b. Sections 72(3), 76, 77 do not specifically provide for affording an opportunity of hearing to the dealer for levy of penalty. Suitable amendments may be made.
- c. The KVAT Act prescribes various penalties for various offences even where there is no malafide intention or suppression. Further, the penalty amounts are typically equal to the tax amount resulting in high demands of penalty even for minor procedural infractions. It is requested that a graded system of penalty be introduced with a nominal penalty being imposed

- for procedural violations and a higher penalty (equal to the tax amount) being imposed only where fraudulent suppression/ evasion of tax is established.
- d. The requirement of pre – deposit of 50% of the tax including disputed tax including interest and penalty as a pre – condition for admitting an appeal should be dispensed with. Otherwise, the Tribunal / appellate authority should be empowered to waive the pre – deposit as is done in the case of Central Excise. The appellate authorities should be given full discretion in the matter of stay. These powers should not be restricted to granting of stay upto 50% of the demand. Alternatively, the pre-deposit amount can be revised to 25% of the disputed tax.
 - e. Section 40(1)(b) of VAT law makes all assessments open-ended. An Assessing Officer can always justify the reassessment on the ground that the evidence of fact justifying reassessment came to his knowledge within the period of limitation. It is an accepted legal position that the finality of assessment is as important as correctness of assessment. Section 40(1)(b) would cause harassment to honest dealers. It is submitted that Section 40(1)(b) should be deleted. Similarly, section 40(2), which provides for limitation of 10 years, should also be deleted. In the present scenario of shrinking office places, it would be impossible for a dealer to retain books of account for 10 years.
 - f. Section 41 of the VAT law as it stands today, permits a rectification within a period of 5 years from the date of judgment in the case of any dealer anywhere in India. This would cause unbearable hardship as the past assessment for any number of years can be rectified. There will be no finality for an assessment. Section 41(1) should be deleted.

19. Inspections / Audits / Assessments / Re-assessments

After introduction of VAT, most of the dealers are subject to repeated inspections / audits / assessments / re-assessments etc by Officers of audit wing, inspection wing, assessing authority, intelligence wing etc. In most of the cases the same issues are looked into and many of the departmental authorities commence inspection, not knowing that the unit / dealer have been already inspected and also re-assessment notices are issued based on the intelligence report. It is nothing but duplication of work putting the dealers to a lot of hardship.

Recommendation

A dealer should be subject to audit once in a year and not by all the authorities. The VAT law should clearly empower any one authority who can visit the premises of the dealer to conduct an audit. Duplication must be avoid except in circumstances where the department deems fit.

20. Condonation

You will appreciate the fact that we are moved into a VAT regime with absolutely very little time to understand the pros and cons of the laws or rules and the procedural issues that may arise as a consequence. In this scenario, it has been extremely difficult for dealers to move into this historic regime given the time frame. It is the earnest request of the trade and industry that any lapse which may arise for bonafide reasons or on account of procedural requirement must be fully condoned for

the year 2005-06, 2006-07 and 2007-08 without any interest / penalty. In this situation it is also requested that input tax credit if any must not be denied on flimsy reasoning.

21. Administrative issues

There are number of administrative issues which need to be streamlined. The following among others are some areas that need immediate attention:

- Repeated visits by the intelligence / cross verification / inspection / audit / assessment wings must be avoided to avoid undue hardship to the dealers. Suitable guidelines to be framed and data made available departmentally to all Officers so that duplication of visits are avoided.
- An audit checklist to be evolved and made available to the dealers, which will enable the dealers to keep the data ready during the visit of the departmental authorities.
- In many instances penal provisions are invoked as a matter of routine. Under the KVAT Act, 2003 the penalties are harsh and as such, these provisions need a thorough re-look / revamp / reframing.
- A separate memorandum is being filed in respect of hardship faced by trade and industry on implementation of e-SUGAM for movement of goods.

Notifications, amendments to law etc., must be carried out on specific dates say end of every month or quarter. If this routine is followed it becomes easier for the dealers to keep a tab of the changes / consequential amendments etc. Presently, the notifications / amendments to law etc., are carried out as and when the department chooses carry out such changes.

22. Substitution of sub-rule 3 of Rule 33 - provisos to Rule 127 & 128

The amendment envisages entry of data in the department's website relating to sales effected to registered dealers and purchases effected from registered dealers in the individual accounts. The following issues among others need to be addressed:

1. If one were to enter such data in the web site notified by the Commissioner what guarantee can the government provide that such data will not be tampered with;
2. What is confidentiality of such data that the government possess online;
3. What comfort level does a dealer get that such data will not be made available to competitors;
4. What accountability does the Government assume that sale / purchase prices will not be shared / made available to any other person;

5. If such data is to be used by the department for comparison of sales / stock of one entity with reference to the purchase / stock of the other entity, how does one ensure the accuracy of the data fed into the system by the seller or the buyer;
6. Assuming that the data is entered into the website then why should the department insist on furnishing the very same data along with the returns.

23. Issues faced by software service providers

Software service providers are being slapped with huge tax demands on their entire service revenue on grounds that the same pertains to sale of software liable to VAT.

While there is a circular issued by the Commissioner of Commercial Taxes, Karnataka on July 24, 2006, the same is not being followed in its true spirit. Any transaction connected with software is being treated as sale of "goods", eg, implementation services, manpower supply services (ie, of software engineers), etc. These transactions would have suffered service tax.

Suggestion

A specific instruction be issued to the field officers to follow the circular above in its right spirit and no tax be sought to be levied on these service transactions.

24. Levy of VAT on all India services revenue

VAT demands are being raised on the all India services revenue by levying tax on the gross revenue disclosed in the financial statement of the Company without taking cognizance of the fact that the said revenue pertains to multiple Indian States.

Further, the VAT authorities usually insist on production of VAT returns/ assessment orders from other States evidencing inclusion of these revenues in the respective State VAT returns/ assessment orders in order to grant exemption under the KVAT law, failing to appreciate the fact that, being services revenue the software company would not have disclosed the same in the VAT return.

Further, most of the companies file their service tax returns on a centralized basis, and hence, state-wise bifurcation of the service revenue would not be typically reported in any statutory return.

Suggestion

Therefore, such documentary evidence, being impossible to produce, ought not to be insisted upon by the VAT authorities as a condition precedent for non levy of KVAT and the authorities should confine their inquiry to the Karnataka turnover of the taxpayer as reflected in books of accounts.

25. Levy of VAT on export of services revenue

VAT demands are also being raised on the export revenue failing to consider the fact that, export, irrespective of whether the same pertain to goods or services is not liable to tax.

Specifically, the department insists on production of documents such as “bill of lading” / “airway bill” for software service exports failing to appreciate that, unlike goods which are tangible, software services supplied electronically will not be exported under the cover of a “bill of lading” / “airway bill”.

Suggestion

Therefore, such documentary evidence, being impossible to produce, ought not to be insisted upon by the VAT authorities as proof of export and a condition precedent for grant of exemption.

Further, to contest such exorbitant tax demands as above, the tax payer is forced to pay 50 percent of the disputed taxes as a pre condition of having their appeal heard.

It is our humble submission that the entire approach of the VAT department in targeting software service providers as above is causing enormous hardship to the IT/ software services industry and further tarnishing the image of the State of Karnataka as a preferred destination for the IT Industry.

26. Time frame for processing of VAT refunds and fresh issues being brought up

a. Time frame

Delays are being faced by exporters (especially SEZ units) in obtaining refund of input VAT relatable to exports, and the time frame for processing refund application/ passing refund orders varies depending upon the jurisdiction/ authority.

b. Refund on certain products being sought to be denied

Refund is being sought to be denied on schedule V goods like furniture, air conditioners, telephones, etc. The VAT authorities are contending that as input credit on these goods is restricted in the normal course of business, refund cannot be claimed by SEZ developers as well.

Rule 130A of the KVAT Rules clearly provides that a registered dealer being a developer of an SEZ shall be eligible for refund of tax paid on any inputs purchased by him despite fulfilling the following conditions –

- Such inputs are purchased for the purpose of development and maintenance of the processing area of the SEZ; and

- Such inputs are purchased for the purpose of setting up, operation or maintenance of an unit in the processing area of the SEZ;

This Rule is not being followed.

c. Refund being sought to be denied where credit claimed later than the purchase

SEZ developers and units account for purchases post acceptance of purchases (including post inspection of purchases). Hence, on a practical basis, there may be a difference in the date of actual purchase and date of availment of Input VAT credit. In all such cases, the credit is only claimed later.

Some authorities are seeking to deny credit/ refund, if credit is claimed in a month other than month of actual purchase. This is against the design of the KVAT law and in any case the dealer does not benefit on his own by claiming credit late.

Suggestion

- a. With a view to streamline and infuse an element of certainty in the refund adjudication process, it is requested that a specific time frame be laid down as a part of the refund process, mandating adjudication of refund claims and issuance of refund orders within such time frame.

It is our specific recommendation that a time period of 30 days be prescribed as being the time frame within which refund applications are to be processed and refund orders issued.

- b. A circular be issued that:

- The interpretation that restrictions of credit in Schedule V do not apply to SEZ developers/ units claiming refund.
- Credit/ refund of VAT can be availed in any month post the month of purchase.

27. Acceptance of Revised Monthly Returns

Under Section 35 (4) of the KVAT Act 2003, revised monthly returns for the period up to 6 months from the end of the month to which the tax relates is accepted. But, the Commissioner of Commercial Taxes in Circular No.5-08-09, dated 7-7-2008 under point 2 (iii) has clarified that the VAT officer can accept revised return for the period beyond 6 months only if there is additional tax liability. Further, the Hon'ble Karnataka High Court in the case of M/s: Federal Mogul Goetze (I) V/s The A.C.CT & Ors, has opined that the limitation of 6 months has only discretionary value and not mandatory.

In light of the above clarification, it is suggested that the registered dealer may be permitted to file the revised monthly return for a period beyond six months, even if there is no additional tax liability.

28. Filing of Annual Return

The filing of Annual Return in VAT Form 115 was omitted w.e.f. 1-8-2008. But, this is causing practical difficulties to the trading and business community.

Therefore, it is suggested that the filing of Annual Return in Form VAT 115, be reintroduced. Further, the annual return should be treated as the base for assessment proceedings. Since, books of accounts are closed only at the end of the year and the assessment under Income Tax Act and in earlier Karnataka Sales Tax Act was only on the basis of Annual Return.

29. Continuation of exemption on Food Grains, Pulses & Wheat Products

The Govt. of Karnataka vide notification No.FD 82 CSL, 10 dated.31-3-2010, had exempted the following commodities from VAT Tax, for a period of one year ending 31st March 2011.

1. Paddy & Rice
2. Wheat
3. Pulses
4. Flour and soji of rice and wheat
5. Maida of wheat.

The Hyderabad Karnataka region is considered as the feeding bowl of pulses for the entire South India. The pulses processing industry is major industry in this area as the production of pulses is abundant in this region.

The following are the statistical details of Gulbarga APMC Market Cess collection in the recent years.

(Rs. In Lakhs)

Sl.No.	Financial Year	APMC Cess Collection (Rs.)	Remarks
1	2004-05	190.52	Sales Tax 1%
2	2005-06	375.93	VAT Tax Nil
3	2006-07	690.89	VAT Tax Nil
4	2007-08	722.00	VAT Tax Nil
5	2008-09	816.00	VAT Tax Nil
6	2009-10	850.00	VAT Tax Nil
7	2010-11	900.00 (Expected)	VAT Tax Nil

From the above statistical details, it clearly indicates that, even after exempting Food Grains and Pulses from VAT Tax, there is fivefold increase in the APMC Cess collection during year, when compared with Sales Tax of 1% on pulses was in vogue during 2004-05. This increase is mainly

due to huge arrivals of pulses in the local market, which was earlier being diverted to neighboring districts of Maharashtra State. Further, the agriculturalists are getting remunerative prices in the local market.

Despite, the VAT Tax exemption on Food Grains, Pulses and allied goods, there is almost 20% increase in the Commercial Tax revenue of Gulbarga Division, which indicates that this exemption has facilitated in the overall development of Trade, Commerce and Industry in this area

The above mentioned Notification to be continued for one more year up to 31-3-2012.

30. Uniform taxation of foods and food preparations supplied by Hotels and Bar & Restaurants.

The foods and food preparations supplied by Hotels are taxed at 5%, where as if the same is supplied to Bar & Restaurants it is taxed at 13.5%. Hence, it is requested that the uniform rate of 5% be levied on food and food preparations irrespective of place of consumption.

31. Introduction of jurisdictional and pecuniary limits for Audit Officers

Under the present law there are no jurisdictional and pecuniary limits for Audit Officer. This is causing inconvenience to the trading and business community. Therefore, it is suggested that precise pecuniary and jurisdictional limits may be prescribed for Audit Officers for effective implementation of the Act. This system was erstwhile in Karnataka Sales Tax Act.

32. Fill-up vacancies in the Department:

It is brought to your notice that several important post in the Commercial Taxes Dept. are vacant in our region, this is causing undue hardship to the members of trade and industry, so it is requested to fill the vacancies at the earliest.

33. Constitution of District Level consultative Committee:

The District Level Consultative Committee has not been constituted for a long period of time. Therefore there is no platform to urge the genuine problems of trade and industries so following suggestions are made.

- To constitute Dist Level Consultative Committee consisting of representatives from the Chamber and other Dist. level trade & industry associations.
- To hold regular meetings of the Dist. level committee, at least once in a quarter of the year.
- To intimate action taken report on the proceedings of the Dist. level Consultative Committee to the Chamber and other Associations.

34. Check Posts:

The following grievances against inspecting authorities are brought to our notice:

- The Check Post authorities are not following correct procedure during verification of documents at check posts.
- Introduce manual of procedure for Check Post authorities for verification of documents and smooth movement of goods.

35. Unregistered dealer

There are many unregistered dealers who are causing unhealthy competition in the market. Therefore, its extensive, proper & systematic survey is conducted by the department to rope in potential unregistered dealers and widen the tax base. Further, VAT awareness programme is essential to lure such dealers for voluntary registration and also such dealers should not be heavily penalized if they approach the department voluntarily.

Further, the check posts should be modernized and the documents collected at the Check posts should be cross-checked regularly in order to prevent revenue loss to the Govt.

These measures will enable the Govt. to increase the revenue to the Govt. and also promote healthy trade practices in the trade and industry.

36. Printing Industry

In the industry relating to the Printing, this year the printers in the State of Karnataka lost in the Government tendering process to the tenderers from the neighboring states. This is due to the fact that the stand taken by the department regarding printing of School text books falls under the category of Works Contract. As the department is aware that, even 5% makes a huge difference in the tendering process. It is learnt that in the other States such activity of printing text books is exempt. Due to this the tenderers from Karnataka are not able to compete with the tenderers from the neighboring States. When the country is moving towards the concept of GST having uniformity in tax structure throughout the country, here there is a disparity in the States, in which Karnataka is taxing whereas there is an exemptions given in other States. The purpose of levying uniformity of taxes would be defeated. During this year, approximately more than 100 crores of the work has moved from the State of Karnataka to other States. Due to this a number of printers are losing the business opportunity.

A number of firms have not been successful in the bidding process in Karnataka and if this continues then it may result in closure of such printing units.

Other point of consideration is that the Sale of text books is exempt under the First Schedule to the Karnataka Value Added Tax law. But if the same is taxed through the mechanism of works contract then the intention of the legislation would be defeated. Hence, it is a request from the industry to safeguard the printers in Karnataka by exempting such printing activity.

Moreover, these books are for educating the student fraternity. This being a social cause and these books are issued free of cost to the students in the Government Schools all over the State of Karnataka. If the activity is exempt then the pricing of books could be lowered and in turn benefit the Government and its schemes at educating the masses. This would benefit for Government, students and even this would help in safeguarding the Small scale Industries/ancillary units in the field of printing.

37. Abolition of CST

We assert that continuance of CST and VAT cannot go hand-in-hand and CST has to therefore be abolished. Some of the reasons in favour of the abolition of CST are as follows:

- VAT envisages tax on value addition by a mechanism of set-off, whereas continuance of CST will only ensure that the cost of inputs increase since set-off of CST paid on purchase is not envisaged.
- VAT is a destination based levy, whereas CST is an origin based levy. It is the experience of most countries across the globe that an origin-based taxation is not progressive and does not generate buoyant revenues.
- Historically, it is evident that the very CST was introduced only to protect dealers against multiple taxation on same transactions by different States, whereas, at present, the CST law has become a means to generate additional revenues to the Centre.
- It has been proved time and again that CST law abets cross-border evasion. While evasion cannot be controlled through complex laws, it is felt that proper administration through 'Zero' rating of CST or set-off provisions of CST will check evasion, which can be coupled with stringent punishment if such frauds are detected. At the same time, there must be speedy redressal of grievances.

Among others, the following are certain advantages that will accrue on abolition of CST under the VAT regime:

- Free movement of goods in the course of inter-State trade or commerce;
- Cascading effect of taxes will be curtailed;
- Will reduce tax induced distortion on account of vertical / horizontal integration;
- Will give way to introduction of VAT in its pure form;
- Transparency in tax structure in the cost of goods;
- Decreases incentive for evasion of taxes due to its self-policing nature;
- Generates large and buoyant revenues due to levy of tax on value addition at each stage;
- Will reduce a lot of paper work like issue / receipt of forms, etc. The invoice itself can act as a document for claiming rebate / proof of inter-State purchase, etc., ensuring smooth and speedy administration.

We understand that as an alternative to abolition of CST, the Central Government is considering the option of abolishing CST over a period of 4 years. To achieve this goal, the CST must be abolished in this year. The advantages of this scenario are as under:

- Higher compliance as trade and industry will not look at tax planning avenues such as branch/ stock transfers and consignment sales. This will ensure buoyancy in revenue.
- The loss of revenue to the exchequer on account of reduction in rate of tax from 2% will be offset by higher compliance and reduction in branch/ stock transfer and consignment sales.
- Improve the confidence of taxpayers towards the proposed reforms and abolition of CST in subsequent years.

38. Receipt of Form C

The introduction of Notification GSR 588(E) dated 16.09.2005 in respect of collection of statutory forms [C,H, I, EI & EII] on quarterly basis has created a lot of difficulties in the trade & industry in recent times. Obtaining the statutory forms from Eastern and Western region is very difficult and the same is delayed.

Non-submission of statutory within the stipulated time with the Commercial Tax Department leads to re-assessment proceedings wherein the dealer / assessee is required to remit the differential taxes along with penalty and interest.

Suggestion

It is suggested that in case of non-submission of statutory forms, the assessee must be permitted to go for an appeal without depositing 50% of the taxes along penalty and interest due. Alternatively, in respect of eastern and western region, the dealer must be permitted to submit the statutory form within one year instead of on a quarterly basis.

39. Entry Tax

- a. **Oil & Lubricants:** - Oil & Lubricants are subjected to Entry Tax of 5%. These commodities are not subjected to Entry Tax in neighbouring states of Maharashtra and Andhra Pradesh, resulting in disparity in the rates of taxes, which in turn causes diversion of trade.

Therefore, it is requested that, Entry Tax on these commodities be removed.

- b. This Act has been the most litigated Act time and again, in Court's. Trade and industry has been crying for abolition of this Act, which is complicated, confusing and highly litigated. The cost of administering this Act, the revenue generation, practical problems etc., has time and again come up for discussion. The end result for all these problems will be its abolition.

This Act was introduced with a view to augment revenues to local bodies. Today, it appears that the complete collections are yet to be transferred to such local bodies. In order to overcome this problem, it is easier to make budgetary allocations to local bodies. This will not

result in any loss of revenues to the Government and even if there is a minor loss of revenue, it can be compensated by better enforcement of the KVAT Laws.

40. Karnataka Sales Tax

Sales Tax on Petrol and Diesel - The rate of tax on Petrol and Diesel is high when compared to Maharashtra and Andhra Pradesh States.

This disparity in rates of taxes has resulted in diversion of trade to neighboring states. Therefore the rate of taxes should be at par with neighboring states. This will result in additional revenue to the Government.

41. Power to write-off old and irrecoverable arrears under KST and allied Acts

Under the present Act, very meager limits are provided to assessing officer for writing off the old and irrecoverable arrears under KST and allied acts. Since, KST and other allied Acts are in the process of elimination, the limit for writing off such arrears may be enhanced, which will result in effective utilization of existing department personnel.

42. Conclusion

Suitable amendments / issue of clarifications as suggested above, alone will usher in a strong and vibrant industrial atmosphere. In the result, if this is not done one can only visualize industrial chaos. The tax regime should be transparent, simple and broad based resulting in better tax adherence and compliance.

The most important factor that can play a role in generating buoyancy in revenue to the State is a positive attitude in making the dealer tax compliant. The Government needs to appreciate the fact that the dealers are honest and intend to discharge their tax obligations diligently. The department is unable to detect large-scale evasion that is being resorted to by the dealers. If this fact is to be accepted, one has reason to believe that a very large percentage of generation of the revenue is on account of dealers' voluntary compliance. Thus, a system should be created wherein a dealer is accepted at face value to meet his tax obligations and the procedures should be simple and hassle free. This will encourage higher compliance and encourage the dealer to have a positive attitude to discharge his tax obligations. If these objectives are met, it will be a win-win situation for both the Government and the dealer.

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