

## Service tax audits - Are not valid?

- CA Mahadev.R

Validity of service tax audit by the department has been questioned regularly in recent times by various high courts. Central government also took few initiatives to amend the provisions to overcome the effect of these judgments and legalise it. Recently the New Delhi high court has once again held that service tax audit is invalid in case of *Mega Cabs Private Ltd Vs. UOI* [2016-TIOL-1061-HC-Del]. In this article, we have analysed the impact of earlier decisions, changes made by government and the impact of the latest decision of high court on service tax audits.

The self assessment scheme is in place for more than a decade now where the interaction of revenue with the tax payer is supposed to be only in exception. Section 72A of Finance Act 1994 provides for special audit by chartered accountant or cost accountant but does not provide for general audit by department. Such special audit can be conducted only in following circumstances:

- a) When there is a failure to declare or compute value of taxable service correctly
- b) When the Cenvat credit utilized in excess of limit permissible or by fraud etc.
- c) When the business operations of the assessee are spread across multiple locations and it is not possible to get true and complete.

Even under Section 94 of Finance Act 1994 (which empowers government for framing rules) there was no provision for general audit by the department.

For the purpose of carrying out service tax audit by tax department, Rule 5A (2) was introduced in 2007 in Service tax Rules 1994. According to Rule 5A(2), records are to be made available to audit party deputed by Commissioner or the CAG.

In case of *ACL Education Centre (P) Ltd Vs. UOI* (2014-TIOL-120-HC-ALL-ST), Allahabad High Court held that Rule 5A(2) only empowers the officers duly authorized by the Commissioner to ask for and collect records from the assessee. The audit can be undertaken only by an authorized Chartered Accountant or Cost Accountant, as provided in Section 72A.

The Calcutta High Court in *SKP Securities Limited Vs. Deputy Director* (2013-TIOL-38-HC-KOL-ST) held that Finance Act 1994 or the CAG Act 1971 does not empower the CAG to undertake audit of accounts of a non-governmental assessee as these

assessee are not in receipt of any aid or grant from the government. According to this decision, CAG cannot undertake audit of private companies.

In case of *Travelite (India) Vs. UOI & Ors (2014-TIOL-1304-HC-DEL-ST)*, the High Court held that Rule 5A(2) of the Service tax Rules 1994 is ultra vires the provisions of Finance Act 1994. The central government was successful in obtaining stay order for the decision.

### ***After effects of High Court decisions***

After the decisions of high courts, Central Government found resistance to conduct audits as assessee started opposing. To overcome the problem, in Section 94 (2) of Finance Act 1994, clause (k) was introduced from 6<sup>th</sup> August 2014 as under:

*“Imposition, on persons liable to pay service tax, for the proper levy and collection of the tax, of duty of furnishing information, keeping records and the manner in which such records shall be verified”*

Based on this provision, Rule 5A(2) was amended with effect from 5<sup>th</sup> December 2014 providing that every assessee should provide all necessary details to audit party deputed by the Commissioner or CAG or a cost / chartered accountant nominated under Section 72A of Finance Act 1994 for the scrutiny. Simultaneously, circular 181/7/2014-ST dated 10<sup>th</sup> December 2014 was issued by the CBEC clarifying necessary changes have been made in Section 94 and Rule 5A(2) providing for audit by departmental officers.

In spite of all these changes, the general audit by revenue was still being questioned due to the concept of self assessment and lack of legal strength.

### ***Latest decision of High Court after changes in provisions***

Recently, the New Delhi high court in case of *Mega Cabs Private Ltd* has struck down the amended Rule 5A(2) of the Service Tax Rules 1994 on the basis that Section 94(2)(k) does not authorize audit by Service Tax Department or the CAG. The high court differentiated the words ‘verify’ and ‘audit’ by holding that audit is a special function which has to be carried out by duly qualified persons like a Cost Accountant or a CA. Circular No. 181/7/2014-ST was also held to be ultra vires. Now again the government would approach the Supreme Court for remedy. Till such time, the service tax assessee at least in that jurisdiction can certainly find

shelter under the judgment of high court. Similar questions are likely to be raised in other jurisdictions.

### ***Remedy in GST regime for Government***

In the recent model GST law released by the government, it appears that adequate measures have been taken to overcome the problems being faced by the department with regard to audit of records of assessee. Section 49 of model GST gives adequate powers for department to take up audit at prescribed frequency. Instead of using word such as 'verify', the word 'audit' has been used in Section 49 with definition for the word 'audit' as well in Section 2 (14). For the purpose, audit includes detailed examination of records, returns and other documents maintained or furnished by taxable person.

The audit by professionals beyond a certain limit has also been built in the model law in section 42(4) similar to Tax Audit under Income tax and VAT 240 audit. It is expected that intrusive verification audits by revenue would reduce significantly other than in cases enumerated under Section 72A discussed earlier in this article.

### ***Conclusion***

The assessee who get intimation for audits could question the validity once again based on the latest decision of Mega Cabs. However, as a law abiding assessee he can cooperate with department if audit is insisted. Compliant assessee could advantage from audits by department as they would be safeguarded from law of limitation.

Please mail feedback / suggestions on [mahadev@hiregange.com](mailto:mahadev@hiregange.com).

-This article has been uploaded in KSCAA  
journal in the month of July 2016.