

Judiciary Appointed, Government Disappointed "CA/CMA"

Bounce Back Move by government w.r.t Service Tax Audit

- CA Swapnil Munot

Controversial and debated issue of whether board (CBEC) has power to conduct service tax audit of assessee has gone into various folds recently, but now it has got finality. Department has initiated and conducted Service Tax Audit of many assessees. However there was no explicit powers given under Finance Act 1994 to conduct the service tax audit by department officials, unlike in case of Central Excise Audit as per Section 37(2)(x) of the Central Excise Act, 1944 to be conducted by Excise Department or Special Audit of Service Tax as per Section 72A of Finance Act 1994 to be conducted by CA/CMA . Hence this issue has put before judiciary to decide the impugned power of department to initiate and conduct the Service Tax Audit. High court wherein said that the issue was under consideration, has stated that department does not have authority to initiate and conduct Service Tax Audit and same is to be carried out as per Section 72A by CA/CMA.

Section 94 of Finance Act 1994 has given power to Central Government to make Rules. Said section was not empowering government to frame the rule to authorize department to conduct service tax audit by departmental officer till 6th August 2014. However Rule 5A of Service Tax Rules 1994 has vested the power to the Commissioner to appoint audit party consisting of departmental officer to conduct verification/scrutiny of records of assesses. Hence judiciary in below mentioned case, decided that Rule 5A of Service Tax Rules 1994 is *ultra vires* to the provisions of Finance Act 1994 and same is to be quashed away.

TRAVELITE (INDIA) VS. UOI & ORS.

[W.P. (C) 3774/2013, C.M. No. 7065/2013]

Pronounced on 4th Aug 2014

The Hon'ble High Court of Delhi in the case of Travelite (India) Vs. UOI & ORS. [W.P. (C) 3774/2013, C.M. No. 7065/2013] held that "Rule 5A(2) of the Service Tax Rules, 1994 is ultra vires to the provisions of the Finance Act, 1994. No Service Tax Audit can be conducted by the Department and only Special Audit within the Statute as mentioned under Section 72A of the Finance Act 1994 can be done either by a Chartered Accountant or Cost Accountant only in specified certain circumstances mentioned in said Section 72A. Service Tax Audit as envisaged in Rule 5A(2) of the Service Tax Rules does not have appropriate statutory backing"

ACL Education Centre Pvt. Ltd. & ORS. Vs. UOI

[2014-TIOL-120-HC-ALL-ST]

Pronounced on 19th Dec 2013

Hon'ble Allahabad High Court in the case of ACL Education Centre Pvt. Ltd. & ORS. Vs. UOI [2014-TIOL-120-HC-ALL-ST] has held that the Audit under Service tax is to be conducted by Chartered Accountants/ Cost Accountants only.

All this back to back judgments has made professional fraternity of CA/CMA happy but this dish of audit was taken away partly by government through statutory amendments. Through Finance Act 2014, government has amended Section 94 of Finance Act 1994 and vested power to Central Government form the rules for conducting audit of Service Tax by departmental official, which is quoted as under:

Section 94(2)(k) of Finance Act 1994

Substituted with effect from 6th Aug 2014:

Section 94(2)(k) - Central government has power to make rules to provide for:

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

With this amendment, government has made Rule 5A of Service Tax Rules 1994 alive and given appropriate statutory backing to it. It has also nullified the effect of above mentioned judgments of high courts. Government has also amended Rule 5A(2) of Service Tax Rules 1994 vide Notification No 23-2014 ST dated 5th Dec 2014, in order to make it in line with amendments in Section 94(2)(k) as mentioned above. Rule 5A is quoted below:

Rule 5A of STR 1994 as amended by

Notification No 23-2014 ST dated 5th Dec 2014

“Rule 5A (1) An officer authorised by the Principal Commissioner or Commissioner as the case may be, in this behalf shall have access to any premises registered under these rules for the purpose of carrying out any scrutiny, verification and checks as may be necessary to safeguard the interest of revenue

(2) Every assessee, shall, on demand make available to the officer empowered under sub-rule (1) or the audit party deputed by the Commissioner or the Comptroller and Auditor General of India, or a cost accountant or chartered accountant nominated under section 72A of the Finance Act, 1994,-

(i) the records maintained or prepared by him in terms of sub-rule (2) of rule 5;

(ii) the cost audit reports, if any, under section 148 of the Companies Act, 2013; and

(iii) the income-tax audit report, if any, under section 44AB of the Income-tax Act, 1961,

for the scrutiny of the officer or the audit party, or the cost accountant or chartered accountant, within the time limit specified by the said officer or the audit party or the cost accountant or chartered accountant, as the case may be.”

To clarify the intent of above amendments, board has issued circular No 181/7/2014 dated 10th Dec 2014:

Circular No 181/7/2014

Dated 10th Dec 2014

Board Clarified that:

- 1) In exercise of the rule making powers under Section 94(2)(k) of the Finance Act, 1994, the Central Government has inserted a new rule 5(A)(2) in the Service Tax Rules, 1994 vide notification no. 23/2014-Service Tax dated 5th December, 2014. This rule, interalia, provides for scrutiny of records by the audit party deputed by the Commissioner. Such

scrutiny essentially constitutes audit by the audit party consisting of departmental officers.

- 2) Verification of records mandated by the statute is necessary to check the correctness of assessment and payment of tax by the assessee in the present era of self-assessment. It may be noted that the expression “verified” used in section 94(2)(k) of the said Act is of wide import and would include within its scope, audit by the departmental officers, as the procedure prescribed for audit is essentially a procedure for verification mandated in the statute.
- 3) It may also be noted that the Hon’ble High Court of Delhi in the judgment dated 04.08.2014 in the case of M/s Travelite (India) [2014-TIOL-1304-HC-DEL-ST] had quashed rule 5A(2) of the Service Tax Rules, 1994 on the ground that the powers to conduct audit envisaged in the rule did not have appropriate statutory backing. This judgment can now be distinguished as a clear statutory backing for the rule now exists in section 94(2)(k) of the said Act.
- 4) Departmental officers are directed to audit the Service Tax assessee as provided in the departmental instructions in this regard.

❖ **Conclusion:** So now law as on date is –

- 1) Commissioner has power to direct for Service Tax Audit of assessee by audit team consisting of Departmental officer.
- 2) Special Audit under special circumstances as mentioned u/s 72 of Finance Act 1994 may be directed by Principal Commissioner/ Commissioner to be conducted by Chartered Accountant/ Cost Accountant

❖ **Arising Issues:**

Whether Service Tax Audit initiated and conducted by departmental officer before amendment to Section 94(2)(k) that is before 6th Aug 2014 are void, in terms of various judgments of high court ? It is well settled law that unless stated expressly, any amendment to law will be prospective and will not have retrospective impact.

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(The views in this Article are that of the author and are not intended as a substitute for a legal advice)