

## Chapter 5

### *Import and installation of capital goods and progress report on export obligation fulfilment*

After issue of EPCG authorisation, the licensee is required to submit the authorisation to the Customs authority at the designated port, where the capital goods are scheduled to be imported, along with request for registration. After execution of bond and Bank Guarantee with the Customs department, the licence gets registered. We scrutinised 588 licences, which were registered in the ports situated at the same station as that of issuing RLAs, out of our sample of 1814 licences test checked and found that there were no delays in the process of registration.

After registration, the licensee can import and install the capital goods and use them for generating exports which would be counted towards his EO. The RLAs/ Customs authorities are required to monitor the imports and installation.

#### 5.1 Monitoring of imports by RLAs

As per Paragraph 2.12 of HBP, the import of capital goods should be completed within three years from the date of issue of EPCG licence, failing which the licence becomes invalid.

We found that the RLAs did not have any system to monitor whether the imports were being completed within the prescribed three years, in respect of all licences. There were 572 licences in our sample of 1814 licences that had been issued between April 2007 and March 2008. The imports should have been completed in these cases as more than three years had passed (upto March 2011). We found that the details of import of capital goods against 301 licences (53 per cent) were not available in the licence files as tabulated below. The RLAs had not initiated action on these cases to verify the completion of import.

Table 5 - Monitoring of imports by RLAs			
RLAs	Period	No. of licences issued during 2007-08	Details of import of Capital Goods not available in file
Kolkata	2007-9/2011	27	17
Ludhiana	Do	39	31
Hyderabad	Do	41	40
Ernakulum	Do	7	2
Coimbatore	Do	70	13
Chennai	Do	55	3
Bengaluru	Do	49	0

RLAs	Period	No. of licences issued during 2007-08	Details of import of Capital Goods not available in file
Ahmedabad	Do	11	1
Delhi	Do	72	72
Madurai	Do	20	11
Mumbai & Pune	Do	181	111
<b>Total</b>		<b>572</b>	<b>301</b>

The high level of exception showed that this is an area of concern and is required to be monitored closely. Reply was received from RLA, Hyderabad who stated that as on date there is no online system or otherwise for confirmation regarding the date of completion of import of capital goods by the EPCG licensee and this information is also not communicated by the Customs Department. This aspect hinders monitoring which is therefore done manually. The reply highlighted an instance of lack of coordination with Customs department. Since all import details are on the Customs EDI system, a data interface would ensure that RLAs get the requisite import data against the licences issued.

## 5.2 Monitoring of submission of Installation Certificates by RLAs

Paragraph 5.3.1, of the HBP provides that the authorisation holder shall produce to RLA a certificate of installation of capital goods from concerned Jurisdictional Central Excise Authority/independent Chartered Engineer. The certificate has to be furnished within six months from the date of completion of import.

Submission of the Installation Certificate (IC) is a control mechanism in the scheme to ensure that Capital goods imported under the scheme are used for the intended purpose by the intended beneficiary. The Department of Revenue had stated in 2008 that Certificate from Central Excise authorities is an inbuilt safeguard mechanism in the EPCG Scheme.

We found that the RLAs had not instituted any system to monitor the receipt of ICs. Out of 1814 cases checked, in 1542 (85 per cent) cases involving CIF value of ₹ 5,99,861.21 crore, we found that the ICs were not available in the licence files. In another 25 cases where ICs were submitted, we found that the certificates were deficient as the most crucial detail i.e., the date of installation of the imported machinery was not mentioned. The details are tabulated overleaf:

Table 6 - Monitoring of submission of Installation Certificates by RLAs					
RLAs	Period	Total no. of licences audited	No. of cases in which installation certificate was not submitted	CIF value (₹ in crore)	No. of ICs not mentioning date of installation
Kolkata	2007-Sept 2011	108	91	2376.94	7
Ludhiana	do	136	117	1006.28	13
Hyderabad	do	147	146	565.74	Nil
Ernakulum	do	23	8	168.07	Nil
Coimbatore	do	193	190	2135.63	Nil
Chennai	do	135	78	1012.43	Nil
Bengaluru	do	134	50	119.14	Nil
Ahmedabad	do	56	34	577.60	4
Delhi	do	267	267	588990.12	Nil
Madurai	do	55	52	407.86	1
Mumbai and Pune	do	560	509	2501.40	Nil
<b>Total</b>		<b>1814</b>	<b>1542</b>	<b>599861.21</b>	<b>25</b>

The RLAs had not initiated action in any of these cases. RLA, Pune agreed that the ICs were not available in the licence files and stated that remedial action would be taken to safeguard revenue. RLA, Delhi stated that the licencees were submitting ICs but they were not placed in the licence file due to heavy workload. The RLAs of Coimbatore, Ludhiana and Hyderabad stated in reply that licencees submit the installation certificate at the time of redemption. The replies indicated that the monitoring of installation within six months had been virtually dispensed with and a key control had been totally diluted. The RLAs, Madurai and Mumbai stated that ICs have been called for and submitted by authorisation holders. RLA, Bengaluru accepted the audit observation and assured necessary corrective action. RLA, Ernakulum informed that in seven cases, the IC has been called for and in another case the licencee surrendered the unutilised authorisation, which has been cancelled. RLA, Rajkot accepted the audit observation.

### 5.3 Random Verification of addresses by Customs

The CBEC issued Circular No. 5/2010 in March 2010, directing the jurisdictional Commissioner of Customs to randomly verify for some of the authorisations issued under EPCG Scheme registered at their port to check the correctness of the addresses shown in the authorisation. It specified that this was important as the scheme required the installation of the capital goods.

We found that the Customs Department had not initiated any address verifications at any location, except at Hyderabad, even after one year from the date of circular i.e. till March 2011.

In Hyderabad, in 20 cases out of 218 cases registered between April 2010 and January 2011 with jurisdictional ports, the Customs Commissionerates had sent letters addressed to Central Excise Commissionerate for verification of addresses. Only in respect of two cases the addresses mentioned by the licensee had been confirmed. The verification reports had not been received by the Customs Commissionerate for the other 18 cases.

While responses of the Commissionerates were awaited at most places, the Assistant Commissioner, ICD Sabarmati stated that verification of the licences would be done during the validity period. The Commissioner of Customs (EP), New Customs House, Mumbai replied (June 2011) that the verification of addresses has now been started and the Commissionerate at Nhava-Sheva informed opening of register for recording of verification of addresses from March 2011.

Our findings showed that the address verification of licensees is yet to be initiated and needs to be taken up on priority.

**Recommendation 5:** *As authentication of the licensee premises is an important check which makes it possible to verify at any time that the imported capital goods are installed and operated at the declared location, Board may examine alternate methods similar to the ones followed by Credit Card Companies/Banks etc. which periodically call for copies of utility bills containing the address.*

The DGFT in their reply stated (August 2011) that excise authorities check the premises of the authorisation holder, therefore alternate method viz. calling of utility bills will add to the transaction cost of the exporter and is, therefore, not required.

The reply of the DGFT is not acceptable as authentication of licensee premises is an important check and calling for utility bill periodically from the exporters as an alternate inexpensive method may be appropriate. Reply of the MOF is awaited.

## 5.4 Physical Verification of Installation

Since we found a high degree of non compliance by the authorisation holders in submitting ICs, we undertook physical verification of installation of a small sample of 234 licences. This was done with the assistance of Central Excise commissionerates. Out of the 234 installations verified by us at ten RLAs<sup>6</sup>, we found that the machines had not been installed in seven cases and the machines had been installed in premises other than that mentioned in the licences in another seven cases as tabulated overleaf:

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<sup>6</sup> RLAs at Ahmedabad, Bengaluru, Chennai, Coimbatore, Delhi, Ernakulum, Hyderabad, Kolkata, Mumbai, and Ludhiana

Table 7 - Physical verification of installation				
RLAs	No. of installation verified	No. of correct installation	No. of installation in other premises	No. of installation not found in the premises
Chennai	45	40	5	Nil
Kolkata	12	9	1	2
Ludhiana	33	30	0	3
Delhi	2	2	0	0
Ernakulum	6	4	0	2
Hyderabad	21	20	1	Nil

The exceptions pertained to five RLAs. All installations were found to be correct at the other five RLAs. Two illustrations of wrong installation/non installation are given below:

(i) M/s Apollo Ziper India Ltd. imported capital goods worth ₹ 62.78 lakh on 4 December 2008 through Kolkata (Sea) port under EPCG authorisation for which duty amounting to ₹ 18.14 lakh was foregone. We conducted physical verification on 5 April 2011 of installation at the licensee's declared premises and found that the machinery was lying in stock and not installed even after lapse of 28 months from the date of import.

(ii) M/s JMC Garments Ltd was issued an EPCG authorisation from RLA, Kolkata for import of capital goods. Capital goods valuing ₹ 88.77 lakh were imported by February 2010 and duty foregone was ₹ 14.11 lakh. During physical verification of installation of capital goods imported under EPCG authorisation conducted on 7 April 2011 under EPCG authorisation, we found that the capital goods were installed at another factory of the authorisation holder at Baruipur, West Bengal instead of the factory at APC Roy Road, Kolkata. Installation certificate had not been submitted.

Our findings indicated that there was a risk of non-installation/wrong installation of the capital goods imported under EPCG but both the Customs Department and the RLAs were oblivious to this risk and had virtually non-operationalised the prescribed control system.

## 5.5 Registration of imported vehicles

The scheme provides for import of vehicles by the hospitality industry. The imports are required to be registered as tourist vehicles. In these cases, the registration was similar to the installation of capital goods.

In 2008, the Department of Revenue, Ministry of Finance had brought to the notice of the Commerce Ministry several irregularities noticed in case of import of vehicles under the EPCG Scheme. The DGFT subsequently issued a circular in May 2008 by which the Customs authorities were required to endorse the Bills of entry while clearing vehicles imported under the scheme so that they had to be registered as 'tourist vehicles'.

The circular further directed that in all past cases where redemption was due till 30 June 2008, such EPCG licencees would have to get the vehicles registered as tourist vehicle by 31 August 2008. RLAs were directed to monitor and ensure compliance. The directions under the circular were also incorporated in the FTP 2009-14 in paragraph 5.2.

We found that the RLAs did not have any mechanism to monitor the receipt of the registration certificates. Of 101 cases scrutinised by us in RLA, Pune, Mumbai, Hyderabad, Chennai, Delhi and Coimbatore, where EPCG authorisations had been issued for import of motor vehicles, we found that mandatory registration certificates were not submitted in 83 cases as tabulated in Table below.

Table 8 – Registration of imported vehicles				
RLA	Year in which licences issued	Number of Licences audited	No. of Registration certificate submitted	No. of Registration where certificate not submitted
New Delhi	2007-08	38	2	36
	2008-09			
	2009-10			
Mumbai	2007-08	41	11	30
	2008-09			
	2009-10			
	2010-11			
Pune	2007-08	10	2	8
	2008-09			
	2009-10			
	2010-11			
Hyderabad	2008, 2009	2	0	2
Chennai	2007-08	9	2	7
	2008-09			
	2009-10			
Coimbatore	2008-09	1	1	0
<b>Total</b>		101	18	83

No action was, however, initiated by the RLAs concerned. Except in 11 cases in Mumbai and two cases in Pune, the Customs department also did not endorse the Bill of Entry as mandated. Therefore, the control introduced to track intended use of concessional duty imports of motor vehicles was not being exercised and we were unable to gather assurance on the end use of the imported vehicles for the intended purpose.

RLA, Hyderabad informed that registration certificates have been obtained from the firms. RLA, Pune has called for the registration certificates from the authorisation holders and RLA, Mumbai stated that registration certificates would be insisted at the time of redemption.

## 5.6 Progress reports for fulfilment of export obligation

Paragraph 5.9 of the HBP prescribes that the licensee shall submit to the RLA concerned, by 30th April every year, a progress report on fulfillment of export obligation. RLA may issue partial EO fulfillment certificate, subject to proportionate fulfillment of EO.

The provision enables the RLAs to monitor the fulfillment of export obligation on a regular basis through the progress reports. We found that the RLAs had not instituted any system to monitor the receipt of progress reports. We scrutinised 743 licences issued prior to April 2004 at 12 RLAs<sup>7</sup>. In 543 out of 743 checked, i.e. in 73 per cent cases involving CIF value of ₹ 3,085.69 crore, we found that the progress reports were not available in the licence files and in another 87 cases progress reports were submitted belatedly i.e. after 30<sup>th</sup> April. Our findings showed that the RLAs were not monitoring the progress of EO fulfillment.

The RLA, Mumbai replied (May 2011) that at the time of applying for fresh licence the applicant gave details of EPCG authorisations held and the percentage of fulfillment of EO. Further, if any violations were noticed the authorisation holders were directed to pay the customs duty along with interest and in the event of failure thereof, cases were taken up for adjudication.

The RLA, Hyderabad stated (March, 2011) that it was not feasible to know the due date of submission of progress reports in the absence of provision in the system. The Ernakulum RLA, office replied that the Master Register tracked the receipt of progress reports of EPCG licences. We observed that while the Register was being maintained, it was not being used to carry out such monitoring. The replies indicated that the RLAs were aware of shortcomings in the monitoring mechanism but initiative had not been taken to address the problem. There is a clear need to develop a monitoring system and given the huge number of licences, it has to be an automated solution.

The RLA, Ludhiana stated that although there is provision for submission of progress reports, there is no provision in the Policy/Procedures for taking penal action against the exporters for not complying with this requirement and the licensees submit the complete details at the time of redemption. RLA, Delhi gave a similar reply and further stated that block-wise EO is checked at the time of redemption. The replies indicated that the RLAs were agreeable to not doing any monitoring during the eight year obligation period and postpone all their responsibilities to the redemption stage. Moreover, the reply regarding provisions was not correct as paragraph 5.17 of the HBP (2009-14) provides for penal action in case of failure to fulfil any condition of authorisation.

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<sup>7</sup> RLAs at Ahmedabad, Bengaluru, Chennai, Coimbatore, Delhi, Ernakulum, Hyderabad, Kolkata, Ludhiana, Madurai, Pune and Mumbai.

In our opinion, the issue of non submission of progress reports and installation certificates is far more significant than mere non compliance to instructions by licencees. The findings indicate complete dilution of monitoring of licencees after issue of licences till redemption. Both the RLAs and Customs authorities have virtually abrogated their responsibility for any monitoring of licences after they are issued. They have not initiated any measures, although the monitoring can largely be achieved through automation and linkage of RLA data to the EDI data of Customs.

**Recommendation 6:** *DGFT and CBEC should co-ordinate their effort to monitor installation of capital goods and progress reports. This would include identifying automated solutions and using the EDI data of Customs. Penal provision should also be introduced for non-compliance.*

The DGFT in its reply stated (August 2011) that installation of capital goods is monitored by excise authorities and fulfilment of EO is done by DGFT which has a monitoring mechanism laid down in paragraph 5.9 of the FTP. It was also stated that EDI in DGFT is actively engaged in automation. Reply of the MOF is awaited.

The DGFT being the issuing authority for EPCG licences, cannot transfer the entire responsibility of monitoring of installation to excise authorities. The excise authorities verify the installations but the DGFT is required to track and obtain the verification reports.

The reply did not indicate whether an interface was being built up with the customs EDI system. It also did not comment on our recommendation for introducing penal provisions in cases of non-compliance.