

CHAPTER II

DUTY EXEMPTION/REMISSION SCHEMES

2.1 The Government may exempt wholly or part of customs duties for import of inputs and capital goods under an export promotion scheme through a notification. Importers of such exempted goods undertake to fulfill certain export obligations (EO) as well as comply with specified conditions, failing which the full rate of duty becomes leviable. During test check (July 2010 to February 2012) of records pertaining to the period July 2007 to November 2011, a few illustrative cases noticed where duty exemptions were availed of without fulfilling EOs/conditions are discussed in the following paragraphs. The total revenue implication in these cases is ₹ 20.48 crore.

Advance licensing Scheme

Regional Licensing Authority (RLA), Bangalore issued license for non-Standard Input Output norm (SION) item which benefitted the licensee to the tune of ₹ 6.40 crore.

2.2 Paragraph 4.1.3 of the Foreign Trade Policy (FTP) 2004-09, while permitting the issue of advance license based on Standard input and output (SION) norms for free import of inputs which are physically incorporated in the export product also empowers the Director General of Foreign Trade (DGFT) to exclude any product (s) from the purview of Advance Authorization by means of Public Notice. DGFT's Public notice no. 31 dated 14 December 2004 deleted SION norm appearing at serial number E90 in the Product Group-Food Products. The DGFT by the same Public notice also amended paragraph 4.7 of the Handbook of Procedures (HBP), Vol-1. 2004-09 to the effect that advance license (based on self-declaration) for the import of pepper should not be issued under paragraph 4.7 of HBP either. Thus, both the possible options for issue of Advance Authorization for import of pepper were excluded. The Joint Director General of Foreign Trade reiterated deletion of Serial number E90 of SION norms vide Policy circular no.03/2005-09 dated 21 April 2005.

2.3 The Regional Licensing Authority (RLA), Bangalore issued (March 2007) an Advance authorization (AA) to M/s S.A. Rawther Spices Pvt Ltd., Bangalore authorizing import of black pepper against the export of processed pepper. The licensee imported (March and July 2007) 23 consignments of unprocessed black pepper falling under CTH 09041140 valued at ₹ 80.99 crore through Custom House, Kochi and availed exemption of customs duties of ₹ 6.40 crore. The issue of licence by the RLA and subsequent import of black pepper was irregular as ban on import of pepper using 'AA' was in force at the time of issue of license and also on the date of import. Accordingly, duty of ₹ 6.40 crore alongwith interest was recoverable from the importer.

2.4 The Assistant Commissioner of Customs, Kochi stated (May 2011) that the import had been permitted as per the condition sheet attached to the advance license issued by the RLA, Bangalore.

2.5 The RLA , Bangalore, stated (February 2012) that the licence was issued as per paragraph 4.7 of HBP, 2009-14 read with public notice no.63 dated 28 March 2005, wherein it was prescribed that issue of licences against export of spices under paragraph 4.7 of HBP 2009-14, should have not been allowed only if there are no norms available. But in the instant case, there are norms available vide SION E-90 for import of Black Pepper against export of processed one and therefore, the above authorization was issued.

2.6 The reply of the RLA, Bangalore is to be viewed in the context of the fact that the SION norm E90 had already been deleted vide DGFT public notice no.31 dated 14 December 2004i.e before issue of licence in March 2007 and actual imports made in 2007, as well. Further, the department reply is also contrary to what was envisaged in the public notice no.63 dated 28 March 2005, wherein it was categorically stated that no license should be issued for import of spices classified under chapter 9 & 12 of ITC (HS) having a duty of more than 30 percent and the imported item 'Black Pepper' falls in such banned category.

2.7 *Ministry of Finance, Drawback Division authorities stated (December 2012) that Commissioner of Customs, Cochin has permitted imports as per license issued by JDGFT, Bangalore. The DEEC Bond under which clearances were made had not been closed in view of the audit objection and matter was referred to JDGFT, Bangalore.*

2.8 *DGFT, Delhi stated (December 2012) that policy relaxation committee in its meeting held in June 2012 (NOC/13 dated 12 June 2012) had regularized the case as the firm had undertaken exports in accordance with authorisation issued by the RA, Bangalore. The committee noted that at the time of issue of licence RA overlooked the fact that norms were already been deleted/suspended.*

2.9 *The DGFT, Delhi reply has to be viewed in the context of the fact that action of the RA in overlooking the norms which were in existence at the time of issue of licence resulted in unintended benefit to the licensee. The responsibility for this lapse needs to be fixed.*

Regional Licensing Authority (RLA), Chennai irregularly clubbed advance authorizations which caused duty benefit of ₹ 43.72 lakh to the licensee.

2.10 Paragraph 4.20.3 of Handbook of Procedures (HBP) Vol-I, (2009-14) envisage that the AA holder has the facility of clubbing of the authorizations for redemption/regularization without further utilization for import or export. This facility is available only for AA(s), where there is shortfall in export obligation and which is sought to be clubbed with an AA (s) which is valid for import.

2.11 The Zonal Joint Director General of Foreign Trade (RLA), Chennai issued (September 2006) an advance authorization to M/s Virgo Polymer (India) Ltd., for duty free import of 2,65,785 Kg of 'Polypropylene (PP) Granules' for export of Flexible Intermediate Bulk Containers. The authorization holder for regularization of shortfall in export obligation against the license issued

(September 2006) applied for (April 2009) clubbing of this authorization with three other AAs issued in July and October 2006 in which both imports and matching or excess exports were made. The RLA correctly rejected the application stating that the three authorizations sought to be clubbed with the authorization issued in September 2006 with EO shortfall, were expired and not valid for import on the date of application. The RLA also rejected (August 2010) subsequent request (July 2010) of the authorization holder for clubbing for the same reasons. The authorization holder once again applied (November 2010) for clubbing of aforesaid four AAs (issued in July/September/October 2006) with one AA issued in April 2010 which was valid for import. On this occasion, the RLA first rejected (November 2010) the clubbing on the similar earlier grounds but subsequently on representation from the licensee incorrectly clubbed all the five authorizations and redeemed (January 2011) them instead of restricting the clubbing of AA issued in September 2006 with that issued in April 2010 as there was no shortfall in other three authorizations issued in July and October 2006.

2.12 The action of the RLA in clubbing all the 5 AAs including the 3 AAs issued in July / October 2006, with no shortfall in export obligation and rightly rejected at the first instance, resulted in non-payment of duty of ₹ 43.72 lakh on the excess import of 2,43,265 Kgs.

2.13 *DGFT, Delhi stated (December 2012) that the four authorizations were clubbed with the authorisation issued in April 2010 which was valid for import under paragraph 4.20.3 of HBP.*

The reply of DGFT, Delhi has to be viewed in the context of the fact that clubbing for Advance Authorisation (s) is available where there was shortfall in fulfillment of export obligation. But in the instant case, the three out of four Advance Authorisation (s) clubbed have no shortfall in fulfillment of export obligation. Accordingly, these three licences were not eligible for clubbing.

Regional licensing authority (RLA), Bangalore counted exports made after expiry of obligation period for fulfillment of export obligation.

2.14 According to paragraph 4.1.3 of Foreign Trade Policy (FTP) 2004-09, Advance licenses are issued to allow duty free import of inputs, which are physically incorporated in the export product' subject to fulfillment of specified export obligation (EO). Further, as per paragraph 4.28 of the Handbook of Procedure (HBP), Vol-I, in the event of failure to fulfill EO, the licensee was liable to pay customs duty plus interest and penalty on unutilized imported raw materials.

2.15 The Regional licensing authority (RLA), Bangalore issued (December 2007) two advance licenses to M/s Khoday Silk Twisting Factory, Bangalore for duty free import of 21600 kgs of 'Mulberry Raw silk (MRS) of any grade (other than Dupion yarn) and 7500 kgs of 'Dupion Silk Yarn' worth ₹ 3.16crore with a stipulation to export 8093.25 kgs of 100 percent 'Natural silk fabrics/Mulberry

raw silk yarn' worth ₹ 1.59 crore and 13165 kgs of 100 percent 'Natural silk fabrics' worth ₹ 1.95 crore within 36 months from the date of issue of license (i.e. upto December 2010).

2.16 The licensee had imported raw materials valued at ₹ 3.62 crore between October 2008 to May 2010 through Chennai Custom House and duty of ₹ 1.05 crore was foregone. We found that out of total export of 20474.09kgs of fabrics/yarn, the licensee had exported only 9628.52kgs of fabrics during obligation period i.e. upto December 2010 and the remaining 10845.57kgs of fabrics/yarn was exported on 29 June / 7 July 2011 i.e. after expiry of the export obligation period (December 2010).

2.17 As the licensee failed to fulfill the prescribed EO, he was liable to pay proportionate customs duty of ₹ 55.97 lakh alongwith interest.

2.18 *DGFT, Delhi accepted that the firm had achieved partial exports and been directed to regularize the case.*

Served From India Scheme (SFIS)

RLA, Chennai considered earnings from ineligible services for grant of duty credit.

2.19 The Supreme Court, in the case of Tata Consultancy Services Vs the State of Andhra Pradesh (STC Vol.137 of 2004) and in the case of BSNL Vs the Union of India and others (STC Vol. 145 of 2006) judicially held that Copyright or right to use the title are termed as 'goods' under the Sale of Goods Act. Accordingly, remittance from Copyright or right to use the title is not to be considered for duty credit under SFIS.

2.20 Regional licensing authority (RLA), Chennai granted (May 2010) duty credit of ₹4.70 crore and ₹ 0.35 crore to M/s Sun TV Network Ltd., and M/s Kalaingar TV Pvt. Ltd., respectively under SFIS at 10 percent of the free foreign exchange of ₹ 46.98 crore and ₹ 3.55 crore earned by them during the year 2009-10. The duty credit was granted for the license fee earned by them from various television channels abroad. The earnings could not be reckoned for duty credit under SFIS because they were on account of transfer of right to use the title or copy right and not on account of rendering of any service. This had resulted in irregular grant of duty credit of ₹5.05 crore which was recoverable with interest. Ministry response had not been received (March 2013).

2.21 *DGFT, Delhi stated (December 2012) that there is no stipulation in the FTP/HBP that while calculating the SFIS entitlement, the copy right component is to be equated as 'goods' and excluded. DGFT, Delhi further added that that parties concerned being TV channels claimed SFIS for the services originated from India.*

2.22 *The reply may be viewed in the context of the fact that exports of 'goods' shall not be considered for calculation of SFIS entitlement. While, copy right has*

been termed as 'goods' by the Apex court. Further, Foreign Inward Remittance Certificates (FIRCs) issued by the bank indicated realization of FE on account of licensing fee for supply of video programmes in the form of media and not through direct transmission of programmes.

JDGFT, Chennai did not review sanctioned telecom sector SFIS cases despite directions from DGFT, New Delhi.

2.23 Director General of Foreign Trade, Department of Commerce, New Delhi vide their policy circular no.38/2009-10 dated 15 July 2010 directed all the Regional Licensing Authorities (RLA) to review all previously sanctioned telecom sector SFIS cases within six months for re-computing their entitlements in terms of the decision of Policy interpretation committee (PIC) meeting of July 2010 by calling for the desired information from the licensee and to recover the excess grant if any. This review exercise was to be completed within six months from the date of policy circular issued in July 2010. The progress of review exercise for each telecom sector applicant was required to be reported on a monthly basis to the DGFT Headquarters.

2.24 The Joint Director General of Foreign Trade, Chennai granted (June 2010) duty credit of ₹ 2.14 crore to M/s Dishnet Wireless Ltd., a Telecom service provider under SFIS at 10 percent of the foreign exchange earned during April to August 2009. We found that although the duty scrip was issued prior to aforesaid policy circular and required to be reviewed by the RLA, Chennai upto January 2011, but no action had been taken till May 2011. Thus, inaction by the RLA resulted in deferment of revenue payment, if any, in case excess grant of SFIS credit was established.

2.25 DGFT, Delhi stated (February 2013) that M/s Dishnet Wireless Ltd., in their response had cited High Court, Bangalore judgment (Writ Petition No.2357 of 2010) filed by M/s Vodafone Essar Ltd., striking down the DGFT policy circular dated 15 July 2010 as 'ultra-vires' to the FTP 2004-09. The firm had also stated that an appeal filed by the Government in Supreme Court (civil appeal No.10117 of 2011) against the High Court judgment to grant interim relief was not entertained. Further progress is awaited (March 2013).

Vishesh Krishi and Gram Udyog Yojana (VKGUY)

Regional Licensing Authority (RLA), Chennai allowed credit under VKGUY without verifying status of the Exporter.

2.26 As per paragraph 3.8.2 of the FTP 2004-09, exporters of notified products are entitled for Duty Credit scrip equivalent to 5 percent of FOB value of exports under Vishesh Krishi and Gram Udyog Yojana (VKGUY). Further, for exports of flowers, fruits and vegetables made w.e.f. 1 April 2008, additional duty credit scrip for 2.5 percent of FOB value of exports; over and above the 5 percent was allowed. Export oriented units (EOU) which do not avail Direct tax benefits/exemption are also eligible for VKGUY duty credit in terms of paragraph 3.8.2.1 of the FTP, provided they produce necessary evidence of change of

exemption status from the jurisdictional Income Tax authorities to the effect that they would not be claiming direct tax exemption henceforth (DGFT circular No 56(RE-2008)/2004-09 dated 21 January 2009).

2.27 The Regional Licensing Authority (RLA), Chennai issued (May 2009) two VKGUY scrips to M/s Sudershan Overseas Ltd., a 100 percent EOU at the rate of 7.5 percent of FOB value for export of 51 consignments (June 2008 to March 2009) of 'Dates, Figs, Pineapples, Mangoes & Mangoes teens Fresh or dried' (Sl. No.13.10, Table 13 of Appendix 37 A). The total duty credit of ₹ 92.66 lakh was allowed in these two scrips. The shipping bills filed by the exporter were under EOU status as evident from the export scheme code '21' indicated therein, but the unit failed to furnish prescribed Direct tax evidence regarding change of exemption status from the jurisdictional Income Tax authorities. The RLA, Chennai also failed to ascertain the status of the exporter by calling for such evidence which is a pre-requisite for claiming the duty under VKGUY scheme by EOUs. The lapse has resulted in irregular grant of duty credit of ₹ 92.66 lakh, which is recoverable from the unit.

2.28 When we pointed this out (May/June 2011/March 2012), there was no response from the department. However, on subsequent audit verification it was noticed that several letters issued by the RLA, Chennai to the unit for depositing the requisite Direct tax exemption certificate were returned undelivered. The department consequently, suspended (September 2011) the Importer Exporter Code (IEC) of the exporter.

2.29 The Assistant Director General of Foreign Trade, Chennai meanwhile, in October 2011, found that the erstwhile company had formed a new company under the name of M/s Rayalseema Commodities Ltd, Chennai and requested for changing their postal address. Accordingly, the licensing authority called for the direct tax exemption certificate from the new company in respect of already issued two VKGUY scrips. The Assistant Director General of Foreign Trade, Chennai directed (January 2012) the unit to refund the duty credit of ₹ 92.66 lakh because it failed to produce the requisite certificate. There has been no response from the unit (December 2012).

2.30 The fact remains that because of the delay in taking timely action by the department, either for recovery of irregularly granted duty credit of ₹ 92.66 lakh or for cancellation of the VKGUY scrips issued, there is every likelihood of loss to the Government.

2.31 *DGFT, Delhi stated (February 2013) that recovery action was initiated.*

Export Promotion Capital Goods (EPCG) Scheme

Regional Licensing Authority (RLA), Ahmedabad counted ineligible exports for export obligation fulfillment.

2.32 As per paragraph 5.5(iv) of the FTP, 2009-14, exports under EPCG scheme shall be physical exports. However, deemed exports as specified in paragraphs

8.2 (a), (b), (d), (f), (g) & (j) shall be counted towards fulfillment of export obligation. This implies that 'supply of capital goods to EPCG authorization holders' as provided under paragraph 8.2 (c) viz supply of capital goods to EPCG authorization holders, could not be considered towards fulfillment of export obligation.

2.33 Regional Licensing Authority (RLA), Ahmadabad issued (March to June 2006) three EPCG authorization to M/s Alpha Nippon Innovative Ltd., Authorization holder applied (August 2009) for clubbing of these three EPCG authorization¹⁰ for redemption and accordingly the RLA allowed (August 2009) the clubbing and fixed new specific export obligation of ₹ 9.64 crore and Average export performance (AEP) of ₹ 50.77 lakh for clubbed EPCG authorization. On submission of export documents by the authorization holder, Export obligation discharge certificate (EODC) was issued by RLA in May 2010. We found from scrutiny of the CA certificate attached to the application for redemption that authorization holder had effected deemed exports of ₹ 6.59 crore in 2006-07 by supplying goods to other EPCG authorization holders¹¹. However, an amount of ₹ 3.75 crore out of the value of goods (₹ 6.59 crore) supplied to other EPCG authorization holders was claimed towards fulfillment of specific export obligation against authorization of March 2006 by authorization holder. This resulted in short fulfillment of export obligation of ₹ 3.75 crore and proportionate customs duty was required to be recovered.

2.34 *DGFT, Delhi stated (December 2012) that EODC granted was cancelled. However, the licensee could fulfill export obligation upto March-June 2014 ie the validity period of three licences. The fact remains that EODC was cancelled only after audit intervention.*

Special Economic Zones (SEZ)/Export Oriented Units (EOUs)

Deputy Commissioner of Customs, Falta SEZ allowed duty exemption against expired DFIA license.

2.35 As per Section 30 of SEZ Act, 2005, read with Rule 47 (1) of SEZ Rules, 2006, any goods removed from an SEZ to the DTA are chargeable to duties of customs as leviable on such goods when imported subject to submission of import license, under the provisions of the Foreign Trade Policy (FTP). Further, for a Duty Free Import Authorization (DFIA), the validity period for imports is 24 months (paragraph 2.12 (i) of Handbook of Procedure (HPB) Vol-I) and the export obligation period (EOP), which was 24 months earlier, is now 36 months from the date of issue {(Paragraph 4.22 of HPB Vol-I, read with Public Notice (PN) 151 dated 26 February 2009 and Policy circular Nos. 80 and 86 (RE-2008)/2004-2009)}. The licensing authority (RA) may grant one revalidation for imports for 6

¹⁰Authorisation Nos.0830001219 dated 7.3.2006, 0830001273 dated 17.4.2006 and 0830001353 dated 13.6.2006

¹¹ M/s Electrotherm (India) Ltd. 7 others

months from expiry date, on the request of the original authorization holder (paragraphs 4.23 and 4.65 of HBP).

2.36 M/s Exotica International, Kolkata, a DTA unit, cleared (between August 2010 and March 2011) 10 consignments of 'Silk fabrics' valuing ₹ 3.17 crore, from two Falta SEZ units, namely, M/s Roto India and M/s S.R. Enterprises. The Deputy Commissioner of Customs, Falta SEZ allowed full duty exemption amounting to ₹ 72.70 lakh against a DFIA license issued in March 2008 by the Joint Director General of Foreign Trade, Kolkata (RLA). However, validity of the DFIA license for imports being 24 months from the date of issue had expired in March 2010 before clearances made in August 2010/March 2011 and its validity was not extended. The license was amended (July 2010) by RLA only for extending the EO period from 24 to 36 months, in pursuance of the aforementioned policy circulars. But the customs authority apparently mistook the extension of EO period of 36 months as extension of validity for imports which remained at 24 months (i.e. upto March 2010) only.

2.37 Thus duty exemption availed against the expired DFIA license amounting to ₹ 72.70 lakh was irregular and recoverable from the DTA unit along with interest.

2.38 The Superintendent of Customs, Falta SEZ intimated (June 2012) that they had written to the firm asking why the duty forgone amount should not be recovered from them, as they had not submitted export obligation discharge certificate (EODC) from the RLA as proof of validity of the said license.

2.39 The Falta SEZ authorities action in response to the audit observation has to be viewed in the context of the fact that submission of EODC from the RLA is of no consequence in the instant case, as submission thereof will not absolve the firm from its liability of paying duty and interest on imports against the expired license. Therefore, the department should immediately initiate recovery measures instead of waiting for the EODC from the RLA, as its submission will not render the exemption valid. Audit response was conveyed to the department in August 2012, their response had not been received (March 2013).

Central Excise, Pune III Commissionerate allowed excess DTA clearances of the export product.

2.40 Paragraph 6.8 (a) of Foreign Trade Policy (FTP), 2008-09, as amended, stipulates that an EOU may sell goods in the Domestic Tariff Area (DTA), upto 50 percent of the value of its exports at concessional rate of duties subject to fulfillment of positive Net foreign exchange (NFE). It further stipulates that units which are manufacturing and exporting more than one product can sell any of these products into DTA, upto 75 percent (90 percent from 2009-10) of FOB value of export of the specific products, subject to the condition that total DTA sale does not exceed the overall entitlement of 50 percent of FOB value of exports.

2.41 The Development Commissioner, SEEPZ, SEZ issued letter of permission (LOP) in February 2004 (as amended) to M/s Cipla Ltd., (Unit-I), in Pune III Commissionerate, for manufacture and export of 'Bulk drugs'. Unit had cleared two bulk drugs namely, 'Fluconazole' worth ₹ 3.34 crore and 'Glatiramer Acetate' valued at ₹ 6.76 lakh during the year 2009-10 in DTA at concessional rate of duty under notification no.23/2003-CE dated 31 March 2003. Audit found that FOB value of Fluconazole and Glatiramer exported in the year 2009-10 was ₹ 93.55 lakh and ₹ 6.75 lakh respectively. As per aforesaid provisions, DTA clearance of said products should be restricted to 90 percent of FOB value of export of these items. Since the unit had cleared more than 90 percent of FOB value of these goods in DTA, clearance at concessional rate of duty was irregular. This had resulted in short levy of duty of ₹ 10.20 lakh.

2.42 The Central Excise, Pune III Commissionerate authorities contested the observation and stated (March 2012) that these bulk drugs were manufactured as per the LOP issued and assessee is a status holder and had intimated the Development Commissioner (DC) for clearances of DTA sales at concessional rate of duty. The excise authorities further stated that the total value of DTA sales of these specific products during 2009-10 and 2010-11 was within the stipulated limit of 50 percent of FOB value of bulk drugs. However, the department added that differential duty to be recovered, for the period 2009-10 to 2011-12 was ₹ 42.90 lakh and a protective demand notice is under process for issue.

2.43 The department reply is to be viewed in the context of the fact that audit is not objecting to the clearances of these drugs in DTA within 50 percent of their FOB value but to clearances of specific drugs in excess of prescribed limit of 90 percent of FOB value of export of specific products.

2.44 The matter was reported (October 2012) to Ministry; their response had not been received (March 2013).

2.45 The Development Commissioner, SEEPZ, Mumbai granted (November 2006) a letter of permission (LOP) to M/s Privi Organic Ltd. for manufacture and export of Chemicals namely 'Alpha/Beta ionone, Citranellol, Citronellal etc'. The unit made DTA sales of items Citranellol and citronellal worth ₹ 5.74 crore (2008-09) and ₹ 6.62 crore (2009-10) at concessional rate of duty. Audit found that FOB value of exports of these items during the year 2008-09 and 2009-10 was ₹ 2.23 crore and ₹ 2.60 crore respectively. Accordingly, the unit was entitled to DTA sales upto 75 percent and 90 percent of FOB value of export of these items in respective years but they exported upto 257 to 255 percent. Non restriction of DTA sales resulted in short levy of duty of ₹ 35.89 lakh.

2.46 The Central Excise Authorities, Mahad Division stated (August 2011) that citronellol belongs to the group of alcohols while citronellal belongs to the group of aldehydes and since the unit was manufacturing alcohols and aldehydes of similar nature, the eligibility for DTA clearances is required to be taken under the

one group. The Central Excise Authorities also stated that the product like citronellol is one of the several alcohols manufactured by them which is similar in characteristics and use and should therefore be grouped together and to be considered as similar goods. The department further added that under alcohols, DTA sale percentage was 49.66 percent and under aldehydes, the DTA sale percentage was 88.20 percent during 2007-08 to 2009-10 and the same was within the prescribed norms.

2.47 The department reply has to be viewed in the context of the fact that the LOP specified the products to be manufactured and exported, wherein 'Citronellol and Citronella' were specified as separate products. Audit is not objecting to the clearances of these similar chemicals in DTA within 50 percent of FOB value but to clearance of specific chemicals in excess of prescribed limit of 75/90 percent of FOB value of export of these specific products. Ministry response had not been received (March 2013).