

Chapter 3

Results of Test Check Based on Sampling in View of Manual Processing

An essential pre-requisite of trade facilitation via automated tools would be a system with inbuilt checks and balances duly mapping the key rules, procedures and conditions of the Scheme. Audit observed certain gaps in integrating the policy and procedures of the scheme with the automated module as detailed in Chapter 2. Many of the intermediate procedures were still being handled manually. This necessitated test check in selected units to examine the manual checks exercised by RAs and DC offices. The 32 units selected for test check (25 RAs and 7 DC offices) represented 93.12 per cent of MEIS / SEIS scrips covering a money value of 95.19 per cent of the scrips. A sample of 6205 scrips (5747 MEIS Scrips and 458 SEIS Scrips) was selected in these 32 units on the basis of random sampling. **As the audit findings are based on test check, there is every likelihood that such errors of omission and commission might exist in many more cases. Department may therefore, check all the remaining transactions also on the lines of audit findings reported in this Chapter and take appropriate corrective action.**

The audit findings emanating from the test check so carried out have been summarised hereunder:

- Findings relating to MEIS:
 - Delay in issue of MEIS scrips due to incomplete system driven checks necessitating manual checks and
 - Deficiencies indicating insufficient linkage of rules of the scheme to MEIS module
- Findings relating to SEIS:
 - SEIS incentives to ineligible services due to misclassification;
 - Incorrect grant of SEIS scrips to Mode-3 and Mode-4 manner of services;
 - Errors in SEIS claims due to incorrect self-declarations and Chartered Accountant (CA) certificate;
 - Excess issue of SEIS rewards due to incomplete checks by RAs;
 - Condition of effecting exports through specified ports in Customs Notification (16 of 2015 dated 1 April 2015) for allowing exemption of import duties for goods imported against SEIS scrips is not consistent with SEIS provisions;
 - Declaration of same services differently to DGFT and to the Reserve Bank of India (RBI);
 - Absence of uniform procedure in processing SEIS claims

- Findings relating to Monitoring and Evaluation:
 - Audit could not find evidence of systematic monitoring on the performance of the RAs by the DGFT;
 - Mid-term review of FTP made by the Department of commerce was silent on effect of SEIS on service sector exports. Performance of the schemes in terms of achievement of goals was not assessed by DGFT and
 - Nothing was found on record to establish that grievance redressal system existed in the online module of MEIS/SEIS and that any pendency analysis of MEIS/SEIS grievances had been done so far by DGFT.

Detailed audit findings are given below:

Findings relating to MEIS

3.1 Analysis of delay in issuance of MEIS scrips

Analysis of Pan-India MEIS data for the period of April 2015 to October 2018 revealed significant delay in issuance of MEIS licences, as detailed in Para 2.1.1 of Chapter 2. To analyse the reasons for delay, 926 MEIS files were test checked from the selected units, and the findings had been summarized below:

- More than 10 days were taken in issuing scrips in 380 (88 per cent) files out of 433 files where no deficiency letters were issued by the RAs while the scrips were supposed to be issued within 3 days.
- In 493 files, where deficiency letters were issued, the time taken to issue deficiency letters exceeded the prescribed period of 3 days in 337 files (68 per cent).
- Further in 378 out of the above 493 files (77 per cent), more than three days' time was taken to issue the scrips even after receipt of full compliance from the exporters (**Statement 13**).

Audit ascertained from DGFT whether any physical records were required at RA level for processing of claims under MEIS. DGFT informed that no documents were required to be submitted in physical form, if the exports were through EDI ports. Further, as per guidelines issued on 11 September 2018, RAs were to process MEIS applications based on a system driven approval mechanism.

However, audit noticed that RAs were verifying divergent issues like

- Availability of documents such as RCMC and landing certificate,
- Correctness of "Late Cut" and classification with item description etc.

Above checks like classification of exported goods, availability of landing certificate etc., were essential for issuing scrips correctly. These checks were not system driven, leading to physical interference and delay in issuance of scrips.

DGFT, while accepting a few instances of delay, stated (September 2018) that about 85 per cent applications were being processed automatically and attributed the delays to shortage of man power. They held that though the system was automated, RAs might be asking physical files and assuming a larger role than required. It was further stated that though faster issue of license was a priority, more important was to ensure that entitlements were correct and there was no revenue loss. Hence, some checks by RAs were warranted which might have resulted in delay.

Audit appreciates DGFT's view that prevention of revenue loss is important. However, ***manual verification of arithmetical accuracy calculated by IT system was necessitated as the system was not properly programmed as detailed in chapter 2.*** In view of such a deficient electronic system, it is not difficult to understand why RAs have been carrying out checks which were supposed to be system-driven. ***Besides leading to wastage of manpower, the deficiencies in automated system have also resulted in delaying the whole process and avoidable physical interface and discretion in the hands of authorised officials regarding checks to be exercised, thereby defeating the scheme objectives.***

3.2 Deficiencies indicating insufficient linkage of rules of the scheme to MEIS module:

During test check of selected scrips, the instances of excess grant of scrips noticed indicated that the rules of the scheme have not been sufficiently linked to MEIS module as detailed below:

3.2.1 Declaration of Intent on shipping bills for claiming rewards under MEIS

To be eligible for claiming rewards under MEIS, declaration of intent to that effect on the Shipping Bills was mandatory with effect from 1 June 2015. Also in EDI generated shipping bills, exporters are required to mark 'Y' or 'N' in the reward box, in case they intend or do not intend to claim benefits under MEIS. Further, in terms of DGFT PN No. 40 dated 9 October 2015 and PN No. 47 dated 8 December 2015 for exports made before 30 September 2015 through EDI shipping bills, if the exporters have inadvertently marked 'N' in the reward box item but declared his intention in the affirmative in the SB, the same are allowed for transmission to DGFT; the exporters are to submit the physical

export promotion (EP) copy of such SBs to RA, for verification of declaration in the SBs.

(a) Audit noticed that 9 units (RA Delhi, Jaipur, Kanpur, Kolkata, Ludhiana, Panipat, Mumbai, SEZ-Visakhapatnam and SEZ-Falta) had granted rewards of ₹2.73 crore in 441 SBs though the prescribed declaration of intention to claim rewards under the MEIS was not available on the SBs (**Statement 14**). RA, Jaipur reported (December 2018) recovery of ₹3.88 lakh including interest.

(b) In RAs Cuttack, Delhi, Ludhiana and Panipat rewards amounting to ₹5.28 crore were granted involving 167 SBs with intent marked 'N' without physical verification of SBs (**Statement 15**).

RA Delhi admitted (January 2019) that SBs were submitted with intent marked 'N' and other RAs intimated that matter would be examined and recovery made.

(c) Audit noticed in RA, Delhi that in one application involving one SB, the column on declaration of intent was not available in office note and MEIS reward amounting to ₹46.94 lakh (**Statement 16**) was granted without due verification. RA Delhi intimated (January 2019) that they called for intent declaration from the firm. Final outcome is awaited (March 2020).

3.2.2 Incorrect grant of higher MEIS benefits to non-handicraft items

Handicraft exports were incentivized with higher rates for specified countries in group A, B & C vide DGFT Public Notice No. 27/2015-20 dated 14 July 2015.

RA, Mumbai had granted rewards to an exporter for exports of Dress materials of manmade fabrics to Group B and C countries during the period from October 2015 to April 2016, at the rate of 2 or 3 per cent, amounting to ₹9.05 lakh. However, exports to B & C group countries were not eligible during that period unless they are handicraft goods. Since the exporter ticked the goods as handicrafts, system allowed the higher rates.

Audit scrutiny revealed that the exporter unit was not a member of Export Promotion Council for Handicrafts (EPCH), and had furnished RCMC from Synthetic & Rayon Textiles EPC. Para 2.94 of the HBP prescribed that an exporter has to declare his main line of business in the application to get RCMC from the notified EPCs and obtain RCMC from the Council which was concerned with the product of his main line of business. Hence, neither the rates as applicable to handicrafts should have been allowed to the exporter, nor was the unit eligible under other than handicrafts because goods were exported to

Group B and C countries. Thus, the benefit granted was irregular and required to be recovered.

Similarly, RA Kanpur had granted rewards of ₹0.47 lakh for ineligible exports of Steel kitchen utensils to the Group C countries. **(Statement 17)**.

DGFT stated (February 2020) that on wrongful disbursement of benefits under MEIS/SEIS, the Directorate had already initiated action for recovery for certain matters and for remaining matters, recovery action would be initiated as per rules, RA wise.

3.2.3 Issue of MEIS scrips to ineligible categories

As per para 3.06 of Foreign Trade Policy 2015-20, supplies made from Domestic Tariff Area (DTA) units to SEZ units are not eligible for MEIS claims.

During test check, Audit noticed that MEIS scrips of ₹8.29 lakh were granted by RA, Kolkata on supplies to SEZ by DTA unit **(Statement 18)**. Thus, neither the system prevented issue of MEIS scrips in respect of these supplies by DTA to SEZ units, nor there were checks prescribed to ensure that scrips are not issued to ineligible categories.

DGFT stated (February 2020) that on wrongful disbursement of benefits under MEIS/SEIS, the Directorate had already initiated action for recovery for certain matters and for remaining matters, recovery action would be initiated as per rules, RA wise.

3.2.4 Incorrect utilization of MEIS scrips

In terms of para 3.02(i) of FTP 2015-20, duty credit scrips issued under MEIS and SEIS can be used for payment of Customs duty for import of inputs of goods, including capital goods except items listed in Appendix 3A of the HBP. As per Sl. No. 2, 3 and 4 of Appendix 3A, coconut, arecanut, oranges, lemon, fresh grapes, apple and pears and all other fruits and all spices with a Duty of more than 30 per cent falling under Chapter 8 and 9 respectively of ITC (HS) Classification are not eligible items for import by utilising MEIS duty credit scrips. Sales to DTA units from SEZ unit are not imports and therefore applicable customs duties on DTA sales cannot be set off against MEIS scrips.

Audit observed 323 instances of incorrect utilisation of MEIS scrips amounting to ₹6.47 crore, in contravention of provisions quoted *ibid*, as detailed below:

- i) Audit observed from verification of utilisation of MEIS scrips that the import items with Tariff rate of duty of more than 30 per cent were imported through Chennai and Tuticorin Sea Customs by utilising MEIS

licences for customs duty amounting to ₹27.70 lakh in seven instances, in contravention to the provisions *ibid*.

In 11 instances, items like spices, oil seeds, peas harvester machines, and stationery diesel engines specified in Appendix 3A were imported by utilizing MEIS licenses through Nhava Sheva Customs port, which was in contravention to the provision cited above. The utilization of duty credit amounting to ₹33.95 lakh was not in order **(Statement 19)**.

DoR replied (March 2020) that recovery of ₹20.20 lakh along with interest was made in 5 cases and corrective action was initiated in the remaining 13 cases commented in audit. The reply was however silent about absence of validation in the system to prevent such incorrect utilisation of MEIS scrips.

- ii) In SEZ-Indore, it was noticed that MEIS scrips were used in 305 instances for payment of customs duties amounting to ₹5.85 crore **(Statement 20)** at the time of clearance/sale to DTA units from SEZ units.

DGFT stated (September 2019) that the matter was being examined in consultation with SEZ Division in the Department, since the interpretation of the SEZ rules was involved and different SEZs gave different interpretation of the eligibility of MEIS scrips for DTA Sale.

Findings relating to SEIS:

3.3 SEIS incentives to ineligible services on account of misclassification

3.3.1 Information Technology/ Information Technology Enabled Services (IT/ITES)

More than 40 percent of India's services exports are in the IT/ITES sector. DGFT has clarified¹⁴ (April 2018) that Appendix 3D does not mention any services as IT/ITES Service. Majority of the services delivered through IT/ITES platform viz., computer related-hardware, software and other database services falls under CPC (Central Product Classification of United Nations Statistics Division) provisional codes 841 to 849. However, such codes are not specified in Appendix 3D.

Audit noticed that 5 units (RA Goa, Mumbai, Pune, SEZ-Kochi and SEEPZ-Mumbai) had incorrectly granted incentives in 28 claims aggregating to ₹130.83 crore to services for which CPC codes were not specified in Appendix 3D **(Statement 21)**.

¹⁴vide Trade Notice No.04/2018 dated 25 April 2018

Three illustrations are given below:

- i) DC, SEEPZ, Mumbai granted duty credit scrip of ₹41.17 crore to **M/s. A Ltd.**, for Technical testing & Analysis services not included in Appendix 3D.
- ii) DC, Kochi SEZ had granted duty credit scrips to five units of **M/s. B Ltd.**, amounting to ₹14.12 crore for the year 2015-16 for engineering services, technical testing and analysis and management consultancy services not included in Appendix 3D. The SOFTEX filed before Specified Officer in SEZ also declared type of service under RBI distinct code, 907 representing software development, falling under CPC 842 not specified in Appendix 3D.
- iii) **M/s. C Ltd.**, provided various testing services as part of the software delivery in an IT enabled platform, which fall under Provisional CPC code 842 which was not included in Appendix 3D and therefore not eligible for SEIS. However, the exporter misclassified the services under CPC Code 8676 – ‘Technical Testing and analysis services’ and got the SEIS reward of ₹6.21 crore and ₹4.77 crore claimed from O/o DC, CSEZ, Kochi for the years 2015-16 and 2016-17 respectively. The grant of the rewards was irregular.

3.3.2 Other Services

Audit noticed that exporters in 4 units (RA Bengaluru, Kochi SEZ, Mumbai, and Pune) in nine applications, got excess rewards amounting to ₹41.89 crore (**Statement 22**) by misclassifying the services, though actual services rendered were not specified in Appendix 3D. RAs placed reliance on CA certificates. Misinterpretation of description of services and overlapping of services among different codes also led to unintentional benefit to exporters as detailed hereunder:

i) Patent and Copy right distribution rights

Royalties for right to use Patents, copyrighted materials fall under CPC 8921 and 8923 respectively, which were not specified in Appendix 3D and hence not eligible to incentives. But RA Mumbai and DC, SEZ-Kochi granted scrips amounting to ₹17.33 crore to three exporters on earnings of royalties on patent and copyrighted materials.

ii) Medical transcription services

M/s. D Ltd., providing Medical transcription services coming under CPC 8432 (not included in Appendix 3D), claimed SEIS for the year FY 16 by misclassifying these services under 8675 "related scientific technical services". DC, SEZ-Kochi had incorrectly granted reward of ₹ 19.56 lakh as claimed by the exporter.

iii) Services auxiliary to financial intermediation & banking

M/s. E Ltd., claimed incentive under Management Consultancy services (CPC 865) and Accounting, auditing and book keeping service (CPC 862).

DC, SEZ-Kochi granted scrip of ₹16.95 crore to the exporter in 22 split SEIS scrip. Audit scrutiny revealed that services claimed under CPC 865 and 862 were in fact related to banking and financial services falling under CPCs¹⁵ which were not specified in Appendix 3D. Hence grant of scrips to ineligible services was irregular.

iv) Testing and analysis services of beauty care products

RA, Mumbai granted duty credit scrips to **M/s. F Ltd.** against NFE earned during the years FY 16 and FY 17 classifying the services under marketing and related services (CPC 865), and technical testing and evaluation services related to beauty products under related scientific and technical consulting services (CPC 8675).

Audit observed that the classification “Related scientific and technical consulting services” codified with CPC 8675 was about engineering related scientific and technical consulting services. The services of the exporter were related to technical testing and evaluation of beauty products, and hence not classifiable under CPC 8675. This resulted in incorrect grant of scrip to the extent of ₹7.06 crore for two years.

v) Services not related to Air Transport services

RA, Bengaluru issued two SEIS scrips for ₹ 35.24 lakh to **M/s. G Ltd.**, for rendering Technical, Installation and Support Services related to Unmanned Aerial Vehicle (UAV) or Drone which were not covered under Appendix 3D and hence not eligible.

DGFT replied (September 2019) that the policy did not mandate all invoices/ service agreement to mention Provisional CPC Code. They held that the Provisional CPC with the service categories were notified to describe the nature of services under the incentivized category. They further stated that there were some service categories in the Appendix 3D, such as Sound

¹⁵CPC 81-Financial Intermediation services and auxiliary services therefore; 8111- Service of monetary intermediaries, 8132- services relating to securities market, 8133- Other services auxiliary to financial intermediation and 8425- system maintenance services and 8439- other data processing services

recording and Ground Handling in which the matching Provisional CPC code was not notified.

The reply of DGFT was not tenable as incorrect grant of SEIS pointed out in audit was the result of misclassification of services, while the actual services rendered were not notified in Appendix 3D.

3.4 Incorrect grant of SEIS scrips to ineligible (Mode-3 and Mode-4) services

SEIS scrips shall be granted¹⁶ to an exporter of notified services, who rendered specified services and earned net foreign exchange from the export of services under Mode 1 (Supply of service from India to any other country) and Mode 2 services (Supply of service from India to service consumers of any other country in India).

The Scheme does not provide rewards to service providers who provide service through commercial presence in any other country (Commercial Presence-Mode 3) or supply of a service from India through the presence of natural persons in any other country (Presence of natural persons-Mode4).

The self-declarations and CA certificates were insufficient to provide assurance about eligibility of services for grant of rewards under SEIS. But department relied heavily on these self-declarations and CA certificates for granting rewards. RAs failed to distinguish between eligible (Mode 1 & 2) and ineligible (Mode 3 & 4) services and to segregate and deny rewards to ineligible services.

Test check of Contractual agreements, work orders or description of invoices of 13 exporters revealed supply of materials, inspection, transport, fabrication, installation and supervision of projects being done at onsite. This was also corroborated by exporters' personnel frequent foreign visits; recovery of their foreign travel, stay expenses, which pointed out that the manner of supply of service to some extent would fall under Mode-4 manner of supply, viz. through natural persons in any other country.

Audit also observed that six exporters provided services to their clients through their group/related companies. All invoices were raised to such companies located abroad and foreign exchange received from such group companies (Mode-3 manner of services)

¹⁶In terms of paragraphs 3.08 to 3.12 of FTP, 2015-20

Though RAs had such information, they did not record the manner of services rendered in any of the files. The CA certificates based on which claim would be determined did not throw light on involvement of Mode-3 and Mode-4 manner of services. All foreign exchange receipts were declared having received through Mode-1 and extended the SEIS benefits.

Audit observed that 4 units (RA Kolkata, Mumbai, Pune and SEEPZ-Mumbai) had granted rewards of ₹57.52 crore to 13 service providers which included Mode-3 and Mode-4 manner of services (**Statement 23**) in contravention to extant provisions.

DGFT stated (February 2020) that on wrongful disbursement of benefits under MEIS/SEIS, the Directorate had already initiated action for recovery for certain matters and for remaining matters, recovery action would be initiated as per rules, RA wise.

3.5 Errors in SEIS claims due to incorrect self-declarations and CA certificate

In terms of para 3.04(b) of HBPv1, an application for grant of duty credit scrip for eligible service rendered shall be filed online on annual basis under digital signatures. Further, in terms of para 3.10 ibid, RAs shall process the application after due scrutiny of the application as well as information in annexure being signed by the Chartered Accountants.

Thus RAs have to grant scrips based on scrutiny of application and its annexure, duly signed by the Chartered Accountant. In absence of any further instructions on scrutiny of extra documents, reliance is placed on self-declaration of applicant and chartered accountant certificates for grant of scrips.

Audit observed irregular grant of rewards on services in 62 applications involving incorrect issue of scrips amounting to ₹40.74 crore (**Statement 24**) due to following lacunae:

3.5.1 Incorrect grant of scrips for services rendered prior to the start of the Scheme

In terms of para 3.12 of the FTP, the rewards under SEIS shall be admissible for exports made/services rendered on or after the date of notification of the Policy.

Audit noticed irregular grant of rewards of ₹26.02 crore to services rendered prior to April 2015 by 8 units (RA Ahmedabad, Chennai, Coimbatore, Mumbai, Pune, SEZ-Kandla, SEEPZ-Mumbai and SEZ-Kochi) in 24 applications. CA certificates had failed to flag this discrepancy, based on which scrips were allowed.

DC, KASEZ and RA Chennai reported recovery of ₹81.36 lakh along with the interest.

3.5.2 Excess grant of scrip due to incorrect Net Foreign Exchange (NFE) values

Five RAs (Ahmedabad, Chennai, Kochi, Kolkata and Jaipur) in 15 applications, had issued excess rewards of ₹4.31 crore on account of

- errors in computation of NFE by including expenses in foreign exchange,
- not adopting the lower value between the invoice value or actual receipts,
- improper Foreign Inward Remittance Certificate (FIRCs) and
- incorrect consideration of services.

RA Kochi reported recovery of ₹8.31 lakh including interest in one case.

3.5.3 Incorrect grant of scrip on NFE including sums collected towards Government taxes

DGFT has clarified¹⁷ that Central/State Government taxes collected by the service provider from the Customers on behalf of the Governments concerned, are not earnings of the service provider and thus not eligible to export incentives on such taxes.

RAs, Jaipur, Kochi and Mumbai had incorrectly granted rewards on taxes amounting to ₹2.35 crore in eight applications.

RA Kochi reported (September 2018) recovery of ₹9.90 lakh along with interest in four cases.

¹⁷ Vide Trade notice No.11/2015-20 dated 21 July 2016

3.5.4 Incorrect grant of scrip due to non-exclusion of expenses of withholding taxes

In terms of para 3.08(d) of the FTP, incentive is granted at a notified rate on net foreign exchange earned, which is arrived at by deducting total expenses/payments/remittances in foreign exchange from the gross earnings of foreign exchange. Receipts in foreign exchange are evidenced from FIRC's issued by the Banks for grant of benefit. When such amounts are received after deduction of withholding tax payable to foreign country, net amount shown in FIRC's shall be considered for grant of rewards.

RAs, Mumbai and SEEPZ-Mumbai had issued scrips on NFE which included amounts paid towards withholding taxes to foreign countries, resulting in grant of excess reward of ₹3.21 crore.

RA SEEPZ Mumbai reported (May 2019) recovery of ₹ 0.68 lakh.

3.5.5 Excess grant of scrip due to adoption of incorrect exchange rates

Annexure A of application captures details of transaction, date wise foreign exchange earnings in USD, and in case of proceeds received in other than USD, their equivalent USD on the date of transaction, by applying exchange rate as per customs notification on the date of transaction.

Scrutiny of the Annexure A filed by **M/s. H Ltd** in SEZ Kandla revealed that the exporters had not adopted the custom notified exchange rates applicable as on date of transaction (invoice date), resulting in incorrect declaration of NFE and consequent excess grant of reward by ₹2.53 crore. SEZ Kandla reported (May 2019) recovery by way of cancelling unutilized licence of ₹2.5 crore and cash payment of remaining amount of ₹2.13 lakh.

Similarly, **M/s. I Ltd.**, incorrectly adopted the exchange rates prevailing at the time of realization of foreign currency instead of rates prevailing on the transaction date, resulting in excess issue of rewards by RA, SEEPZ-Mumbai amounting to ₹1.39 lakh.

3.5.6 Incorrect grant of incentives to ineligible remittances

Audit observed that in eleven applications in 4 RAs (Bengaluru, Goa, Jaipur and Kochi) reward of ₹2.32 crore was granted on ineligible remittances viz., earnings from un-notified services and cases where the nature of service for such currency earnings was not known. In one case, CA had not certified the

correlation of bills/invoices with forex receipts which was essential to establish eligibility of the remittances for SEIS rewards.

The above observations were brought to the notice of the DGFT (September 2019) and DGFT replied that (February 2020) on wrongful disbursement of benefits under MEIS/SEIS, the Directorate had already initiated action for recovery for certain matters and for remaining matters, recovery action would be initiated as per rules, RA wise.

3.6 Excess issue of SEIS rewards due to incomplete checks by RAs and system

The process of scrip issue is semi-automatic involving both system and manual interventions. The extent of checks that are required to be exercised by RA before issue of scrips under SEIS are not clearly spelt out.

In 34 applications, audit noticed incorrect grant of scrips on account of non-deduction of "Late Cut", scrips issued without RCMC/IEC, Services rendered to Indian companies, incorrect adoption of NFE amounting to ₹13.02 crore **(Statement 25)**.

Some issues are detailed below:

3.6.1 Non deduction of "Late Cut" in SEIS applications received beyond due dates

Audit observed non-imposition of "Late Cut" in 24 SEIS applications filed before 6 units (RA Ahmedabad, Chennai, Delhi, Mumbai, SEZ-Kochi and SEEPZ-Mumbai), though they were received after due dates. The "late cut" recoverable was ₹5.49 crore.

DGFT stated (February 2020) that on wrongful disbursement of benefits under MEIS/SEIS, the Directorate had already initiated action for recovery for certain matters and for remaining matters, recovery action would be initiated as per rules, RA wise.

3.6.2. Irregular issue of SEIS scrips without RCMC/IEC

Para 3.08 (f) of FTP prescribes that service provider shall have an active IEC at the time of rendering services for which rewards are claimed. Further Para 2.56 prescribes requirement of a valid RCMC from relevant export councils,

(i) Audit noticed that RA, Delhi had irregularly issued scrips of ₹4.07 crore in two applications without valid RCMC.

(ii) In three applications, RAs Kochi and Chennai had irregularly issued scrips amounting to ₹85.33 lakh to service providers without an IEC at the time of rendering services.

RAs, Delhi and Kochi intimated issue of notices and surrender of scrips and also recovery of ₹43.63 lakh by RA Kochi.

3.6.3. Incorrect grant of SEIS benefits when services rendered to Indian companies

In case of maritime transport services specified in Appendix 3E, services rendered in Customs notified Areas to a foreign liner (or procured by a foreign entity in case of services included in rental of vessels with crew) would be considered as deemed to be received in foreign exchange and deemed to be earned in foreign exchange and shall be eligible for issuing rewards under the Services Exports from India Scheme. Accordingly, a unit providing port terminal services to foreign shipping liners is eligible to rewards.

Audit observed in RA Mumbai that an applicant, **M/s. J Ltd.**, had rendered such services partially to four Indian companies/shipping lines. As the service consumers are Indians, no benefits shall be allowed on amounts received from Indian consumers as per para 9.5(i) of the policy. Accordingly, scrips issued to the tune of ₹175.58 lakh (5 per cent of ₹35.12 crore) were irregular, which were to be recovered from the service provider.

DGFT stated (February 2020) that on wrongful disbursement of benefits under MEIS/SEIS, the Directorate had already initiated action for recovery for certain matters and for remaining matters, recovery action would be initiated as per rules, RA wise.

3.6.4 Grant of SEIS rewards on incorrect adoption of NFE

In two applications, RA, SEEPZ-Mumbai, and Indore granted excess rewards of ₹7.96 lakh without verifying the variations in NFE declarations in 'online application' and CA certificates.

DGFT stated (February 2020) that on wrongful disbursement of benefits under MEIS/SEIS, the Directorate had already initiated action for recovery for certain matters and for remaining matters, recovery action would be initiated as per rules, RA wise.

3.6.5 Non maintenance of jurisdiction discipline

Under Para 3.06 of HBP read with DGFT PN 30/2015-20 dated 26th August 2015 and 58/2015-20 dated 10th February 2017 IEC holders having units in SEZs /EOUs shall apply to the concerned DCs of SEZs given in appendix 1A.

RA, Mumbai had granted SEIS scrip of ₹76.52 lakh to **M/s. K Ltd.**, a Free Trade and Warehousing Zones (FTWZ) unit operating under the provisions of SEZ Act, 2005. As the unit falls under the jurisdiction of DC, SEEPZ, Mumbai, the grant of reward on forex earnings made during the FY 2015-16 was irregular.

DGFT stated (February 2020) that on wrongful disbursement of benefits under MEIS/SEIS, the Directorate had already initiated action for recovery for certain matters and for remaining matters, recovery action would be initiated as per rules, RA wise.

3.6.6 Excess payment of SEIS under Port Services

DGFT has clarified¹⁸ that SEIS benefits in case of Port services shall be given to the actual service providers and not to the aggregator of services who simply routed the earnings through them, for making payments to actual service providers. The aggregator of services (Ports) shall be entitled for benefits under SFIS/SEIS for services exclusively rendered by them and for which the foreign exchange earnings (or INR payments as allowed under the scheme) are received and retained by them on this account.

RA, Mumbai, in the case of **M/s. L Ltd**, which was engaged in international maritime transport, granted rewards for foreign exchange earnings on freight and demurrage charges received from international charterers. However, the maritime transport freight amount also includes the Terminal handling charges (THC) of loading, unloading at ports and storage charges. Hence, part of the freight actually goes to the actual service providers in INRs who provide Terminal handling services viz. Ports, loading and unloading agencies.

Thus, the shipping liners as in this case are not eligible to claim benefit on freight portion which represents THC and storage charges paid to actual service providers. These payments were not excluded from shipping liner claim as there was no mechanism to make an applicant to deduct expenses incurred in INR.

¹⁸vide Policy Circular Nos.06 dated 22 May 2018 and 08 dated 21 June 2018

Similarly, **M/s. M Ltd** had supplied repair and maintenance services to foreign aircrafts in Indian airports during FY 16 and 17. The concerned service invoices depicted levy and collection of charges in the range of 13 to 32.50 per cent which was retained by the aggregator. Since these levies ultimately belong to the aggregator, the proportionate benefit on account of such levies was not to be granted to M/s. M Ltd.

DGFT informed (March 2020) that Mumbai RA has been asked to examine and scrutinize the applications based on certain DRI references received in the HQs.

3.7 Inconsistency between policy and notification

CBIC issued Notification No.25/2015-cus dated 8 April 2015 providing exemption from Import duties if goods are imported against SEIS scrip issued by the RAs under paragraph 3.10 read with paragraph 3.08 of the FTP subject to the conditions mentioned therein. Two such conditions are:

(1) the duty credit scrip is issued to a service provider located in India against export of notified services listed in Appendix 3D of Appendices and Aayat Niryaat Forms (ANF) of Foreign Trade Policy 2015-2020;

(2) that the imports and exports are undertaken through the seaports, airports or through the inland container depots or through the land customs stations as mentioned in the Table 2 annexed to the Notification No. 16/2015- Customs dated 01 April 2015 or a Special Economic Zone notified under section 4 of the Special Economic Zones Act, 2005 (28 of 2005):

Provided that the Commissioner of Customs may within the jurisdiction, by special order, or by a Public Notice, and subject to such conditions as may be specified by him, permit import and export through any other sea-port, airport, inland container depot or through any land customs station;

i) RAs, Mumbai and Pune issued SEIS duty credit scrips to 16 service suppliers who had exported services like engineering design services, legal and attorney services, management consultancy, book keeping, accounting and auditing services, construction related services; or supplied services to foreign consumers in India in Hotel and Hospital industries. These service exports were not undertaken through any of the ports specified under Sl.No.2 of the Customs Notification, but exported directly from exporters' offices either through data links or consumption in Hotel and Hospital premises. There was no proof in RAs office that services were exported through any of the specified ports.

ii) RA, Mumbai had also issued scrips to two suppliers of deemed export services notified in Appendix 3E vide public notice No.7/2015-20 dated 4 May 2016 of the DGFT. These services were mostly related to Maritime Transport and support services in port areas, where no actual export of services would take place. Services rendered to foreign liners within port areas did not satisfy the conditions of customs notification, which allowed services enlisted in Appendix 3D to be eligible for exemption when exports were undertaken through specified ports.

Thus conditions of notification dated 8 April 2015 are not consistent with SEIS provisions. However, 33 scrips related to such services have been registered in Jawaharlal Nehru Customs House (JNCH), Mumbai and used for payment of import duties (**Statement 26**).

DoR replied (October 2019) that Custom's Notification no.25/2015 dated 8 April 2015 was not consistent with SEIS provisions and that they were in the process of removing the inconsistency.

3.8 Declaration of same services differently to DGFT and to the RBI

Audit observed in three applications filed in DC, CSEZ-Kochi, SEEPZ- Mumbai and SEZ-Kandla that the exporters had declared their services as Engineering services (CPC code 8672) as per Appendix 3D. In the declaration of foreign exchange earnings filed to the RBI through SOFTEX returns,¹⁹ the same services were declared as software development and other software falling under distinct codes 907 and 908 respectively. Thus, to one authority (DGFT) the services were classified as Technical Testing and analysis services/Engineering services and to another (RBI) the services were declared as software development.

DCs, being the administrators of SEZ units, are authorised to issue Letter of Approvals for specified authorized operations. These operations are normally declared on the SOFTEX returns. DCs are also authorities to grant rewards for their export performance under SEIS. The different declarations of nature of services from the same exporter for the same export could have been checked by the DC offices before issue of scrips.

Besides, different classification codes exist for the same service and vendors are reporting different codes to different authorities for the same service.

¹⁹As per regulations 3 and 6 of Foreign Exchange Management (Export of Goods & Services) Regulations, 2000

DGFT replied (February 2020) that the Directorate would notify the codes in line with the GST Service Accounting Codes (SAC), so that there would be an inbuilt check while reporting service categories to different authorities at the firm level from the year 2020-21 and suitable measures would be accordingly incorporated in the procedures and policy paragraphs.

3.9 Absence of uniform procedure in processing SEIS claims

As per Note 3.04 (c) of HBP, “RA shall process the application received online after due scrutiny”. However, it was observed that no guidelines were issued by DGFT to RAs regarding checks to be exercised as part of due scrutiny before sanctioning SEIS.

Audit observed that there was no uniformity in procedure being followed for processing SEIS claims across RAs or DC offices. For instance, in 5 RAs (Mumbai, Kolkata, Pune, Ahmedabad, Kochi), applications were processed based on verification of sample invoices, FIRCs, CA certificates, etc. In 2 DC offices (CSEZ-Kochi and SEEPZ-Mumbai), SEIS claims were being sanctioned relying only on the certificates of CA regarding correctness and admissibility of the SEIS claim without any cross-verification.

DGFT stated (March 2020) that CA certificate was the document based on which the claims were currently being processed and additional documents were being sought by RAs based on typical scenarios of any specific case, wherein service classification was not correct. It was stated that this was being done to prevent a claim being granted on misclassification or for an ineligible category.

In absence of specific directions, divergent practices were being followed by the RAs regarding scrutiny required to be undertaken before issue of scrips.

Monitoring and Evaluation:

3.10 Monitoring mechanism of the scheme

It is imperative that for major scheme like MEIS/SEIS, performance of the RAs be periodically monitored on identified performance criteria to ensure that scheme is being implemented as per design. The details of oversight/monitoring mechanism and related files called for by audit (January 2019) were not furnished by DGFT. Audit could not find evidence of systematic monitoring on the performance of the RAs by the DGFT.

DGFT informed (March 2020) that since January 2017, monitoring of delays in processing of MEIS / SEIS applications was being done through JASPER

reporting module and RMS also was fully functional and that RAs had been asked to clear the pendency.

The reply of DGFT dealt only on monitoring the pendency of claims since 2017 and was silent on monitoring of scheme implementation and overall performance of RAs.

3.11 Evaluation of the schemes

MEIS/SEIS are the major trade facilitation schemes under FTP 2015-20 with significant revenue foregone implications to the government. Periodic evaluation of the scheme would have helped in ensuring that scheme objectives are being met and also for mid-course correction in case of any deficiencies.

It was observed that performance of the schemes in terms of achievement of goals was not assessed by DGFT (February 2019).

Audit enquired (January 2019) whether any specific targets/goals were fixed for MEIS and SEIS schemes and if fixed, whether they were evaluated. DGFT stated (March 2019) that the same was not possible because they provided incentives based on exports already happened and they could not set a target to achieve the exports. Moreover, export growth was a multi-factorial issue and not dependent on MEIS alone. DGFT stated that exports depended on a variety of international factors, such as global demand, currency fluctuations, seasonality of exports and as such, no cause effect analysis was done. The products once included for MEIS benefit stayed for a certain period to have a stable regime. DGFT further stated that a study on the schemes by Niti Ayog was in progress and no other studies were conducted.

Audit understands that export growth is a multi-factorial issue and not dependent on trade facilitation schemes alone. At the same time, it is an area of concern that such major schemes (with annual revenue foregone figure more than ₹25,000 crore) are being implemented without having any performance matrix.

Mid-term review of FTP made by the Department of commerce was silent on effect of SEIS on service sector exports. The impact of new features introduced in SEIS viz. extension of incentives to all 'service providers located in India' as against 'Indian service exporters'; restriction of rewards to Mode-1 and Mode-2 manner of services were not evaluated and commented upon. There was no periodic review of duty foregone, sector-wise services, and its impact on

sectoral growth in service exports. Mid-term review was also silent on rewards gained by the Foreign Service providers located in India and rewards gained by the Indian service exporters to estimate the impact of deviation of SEIS from its earlier version, SFIS.

DGFT stated (March 2020) that NITI Aayog Committee reviewed the MEIS Scheme and for SEIS, the revenue foregone was being monitored regularly in the Monitoring Committee meetings.

The reply was silent about non-evaluation of effect of SEIS on service sector exports and impact of amended provisions brought in SEIS as compared with its earlier version SFIS in the Mid-term review of Schemes by DGFT.

3.12 Grievance redressal system

The provisions/modes available for redressal of grievances of applicants for MEIS and SEIS were examined in audit. It was noticed that there are no specific grievance redressal system for MEIS/SEIS in the online module. On audit enquiry, DGFT informed that applicants seeking redressal of grievances can address through (i) e-mail, (ii) Centralised Public Grievance Redress and Monitoring System (CPGRAMS) portal and (iii) Contact@DGFT. While the first two were general grievance redressal mechanisms in government, Contact@DGFT service was implemented on 6 September 2017 as single point contact for all foreign trade related issues. Importers/exporters could use this through email specified or toll-free number for resolution of foreign trade related issues either directly through DGFT (Headquarters or regional offices) or through other agencies of the Central or State Governments.

It was seen that the details regarding total number of cases of grievances and total cases resolved for the period FY 16 to FY 18 in respect of MEIS and SEIS were not maintained in DGFT. The details only in respect of Contact@DGFT for FY 18 were made available to audit, as given below:

Table 5 : Grievance redressal

| Description | Total no. of cases of grievances received | Cases resolved within 5 days | Total no. of cases pending as on March 2018 |
|----------------------|---|------------------------------|---|
| MEIS/SEIS-Ch.3 | 868 | 815 | 53 |
| MEIS application-EDI | 3189 | 3023 | 166 |
| SEIS application-EDI | 182 | 133 | 49 |

The reasons for pendency of cases under Contact@DGFT, sought (January 2019) by audit were not furnished till date. The details of grievances through channels other than Contact@DGFT and their status of redressal were not furnished to audit.

In the absence of all the relevant records/data, audit was not in a position to assure whether grievances of the exporters were adequately addressed in a timely manner.

Conclusion

The substantial delays in issue of MEIS scrips were due to incomplete system driven checks necessitating manual intervention. No clear instructions were issued to field level RAs about the extent of checks required for issuance of MEIS scrips. RAs ended up checking divergent issues. Despite having a system driven approval mechanism, RAs were checking issues like correctness of "Late Cut". Manual verification of arithmetical accuracy calculated by IT system was necessitated as the system was not properly programmed as detailed in chapter 2. In view of such a deficient electronic system, it is not difficult to understand why RAs have been carrying out checks which were supposed to be system-driven.

Test check also revealed failure of systemic controls in MEIS leading to incorrect grant of reward even though declaration of intent to claim reward was not given/unavailable in SBs, grant of higher rates applicable to handloom products and incorrect utilization of scrips.

SEIS suffered from semi-automation and lack of uniformity in processing of claims by various RAs. The exporters got rewards in cases where the services were misclassified though actual services rendered were not specified in Appendix 3D and benefits amounting to ₹172.72 crore in respect of these services were granted by 7 RAs in 37 cases, by placing reliance on CA certificates. The self-declarations and CA certificates were insufficient to provide assurance about eligibility of services and remittances for grant of rewards under SEIS. However, department relied heavily on these self-declarations and CA certificates for granting rewards. RAs failed to distinguish between eligible (Mode 1 & 2) and ineligible (Mode 3 & 4) services and to segregate and deny rewards to ineligible services resulting in excess rewards of ₹57.52 crore to 13 service providers in contravention to extant provisions. Errors in claims amounting to ₹40.47 crores were noticed in 62 cases due to incorrect self-declarations and CA certificates. Excess issue of rewards amounting to ₹13.02 crores was noticed in 34 cases due to incomplete checks by RAs and system.

There was lack of clarity in SEIS provisions for port services as to how the actual service providers would get the benefit when they were not directly providing service to foreign consumers.

Condition of effecting exports through specified ports in Customs Notification (16 of 2015 dated 1 April 2015) for allowing exemption of import duties for goods imported against SEIS scrips is not consistent with SEIS provisions.

Exporters declared different nature of services in SOFTEX returns and SEIS claims for the same export. These could have been checked by the DC offices before issue of scrips, which was not done.

No guidelines were issued by DGFT to RAs regarding checks to be exercised as part of due scrutiny before sanctioning SEIS and there was no uniformity in procedure being followed for processing SEIS claims across RAs or DC offices.

There were significant discrepancies in respect of SEZ units, which were brought under the export incentive schemes for the first time and the scrips were processed without proper scrutiny.

Audit could not find evidence of systematic monitoring on the performance of the RAs by the DGFT. DGFT stated that delays in processing of MEIS / SEIS applications were monitored through JASPER reporting module. However, there was no monitoring of scheme implementation and overall performance of RAs. Periodic evaluation of the scheme would have helped in ensuring that scheme objectives were being met and also for mid-course correction in case of any deficiencies. Mid-term review of FTP made by the Department of commerce was silent on effect of SEIS on service sector exports. Performance of the schemes in terms of achievement of goals was not assessed by DGFT.

Nothing was found on record to establish that grievance redressal system existed in the online module of MEIS/SEIS and that any pendency analysis of MEIS/SEIS grievances had been done so far by DGFT.

Recommendations

We recommended that

4. The audit findings on excess grant of incentives reported in chapter 3 were based on test check done on sampled cases using random sampling, in view of the prevalent manual verification. There is every likelihood that such errors of omission and commission might exist in many more cases. Department may check all the remaining transactions also on the lines of audit findings reported in Chapter 3.

5. To prevent scope of misclassification of power loom products under Handloom category, the distinction between power loom and handloom process may be clearly specified.

DGFT stated (March 2020) that classification of goods was required to be checked at the Customs Ports. The online system can identify only the HS Codes and cannot read the item description for interpreting the misclassification of an item. The RAs would be informed to initiate recovery action, wherever due.

6. To avoid ambiguity and to bring in more clarity on eligible services, DGFT may consider insisting for CA certificate on exact classification of service with Central Product Classification (CPC) code and the Mode under which it falls, rather than simply stating the serial number of the list of eligible service. Suitable clarity regarding the codes and the modes available for scheme benefits and penal provisions on the shortcomings found in applicant's declarations and CA certificates may be brought in the system. Responsibility of CAs must also be clearly defined and failure on their part be reported to appropriate authority.

DGFT, while accepting the recommendation, stated (March 2020) that it would be implemented in the next FTP, if the SEIS is continued. In the instances, where CAs have been found to mis-declare/ certify a claim based on misclassification the Regional Authorities have been asked to take necessary action under Foreign Trade (Development and Regulation) Act, 1992.

This recommendation may be considered for any such scheme where reliance is placed on CA certificates.

7. DGFT may issue clear instructions to RAs about basic checks required before issuing SEIS scrip. Invoking penal provisions may be made mandatory on shortcomings found in applicant's declarations and CA certificates.

DGFT stated (March 2020) that this recommendation will be examined for implementation in the next FTP, if the SEIS is continued.

This recommendation may be considered for any such scheme where reliance is placed on CA certificates.

8. DGFT should provide clarity in the policy and procedures on segregation of four types of services. Applicants' declarations and CA certificates on classification of services should be reviewed to address the distinction of services.

DGFT, while accepting the recommendation, stated (March 2020) that ANF 3B, would be modified to add an entry wherein the CA would be able to certify that the services claimed under SEIS would fall under Mode 1 and Mode 2 specifically for each category of service claimed.

9. DGFT may devise mechanism in respect of port services so that the intention of granting rewards to actual service providers are protected against claims of aggregator of services and the conditions of exemption in Customs Notification may be drawn in sync with the provisions of the SEIS scheme.

DGFT stated (March 2020) that the service was rendered at the port but since it was made to a foreign liner, it would fall into the category Mode 2 and Rupee payment for such services were eligible for rewards.

The reply did not address issue raised by audit in the recommendation, which was about mechanism to have a distinction between rewards due to service providers and aggregators.

10. The classification of services by various agencies (DGFT, RBI, Customs etc.) needs to be aligned to the Central Product Classification (CPC) code of UNSD to avoid any misuse of incentives which is based on CPC codes.

DGFT, while accepting the recommendation, stated (March 2020) that it would be implemented in the next FTP by aligning with the GST SAC codes, if the SEIS is continued.

11. A mechanism must be put in place to ensure that Jurisdictional Development Commissioners verify the validity of classification of service being reported by the service providers to different authorities (DGFT, RBI, Customs etc.) for the same exports.

DGFT stated (March 2020) that verification of reporting of services from multiple organizations, which follow different reporting formats for the same kind of services would make the Scheme non-implementable. Audit's recommendation was not with reference to reporting format but with a mechanism to ensure uniformity in classification reported to various agencies. Department should consider devising a feasible mechanism to ensure uniformity in classification used for reporting of same services to different agencies.

Besides, the cases pointed in audit pertained to SEZs wherein jurisdictional DCs were the authorities for granting SEIS and also had the administrative control of SEZs. Thus, reporting of divergent classification for same services could be checked at least on a test check basis.

12. RAs should insist for SOFTEX forms, which was a mandatory declaration under Foreign Exchange Management (Export of Goods and Services) Regulations 2000 for supply of services through data links, in cases where the services were classified/declared under Mode-1 category.

DGFT stated (March 2020) that the suggestion on the requirement of SOFTEX forms would be examined, however, this would add to the documentary requirements for the scheme and would be an intrusive measure, as there may be a scope of having this SOFTEX also confirmed from RBI.

SOFTEX is already a mandatory requirement under Foreign Exchange Management Act (FEMA) for Mode 1 type of services rendered through data link. This recommendation of RAs being given access to these forms, will provide an additional confirmation for Mode-1 services in software and related

services and is already being followed by SEZs and Software Technology Park of India (STPI) units.

13. For ease of doing business, we recommend that the DGFT may consider an inbuilt system for grievance redressal. The analysis of the same can be used as feedback mechanism for improving the scheme. Monitoring of the schemes on such parameters viz. time taken to process claims, RMS scrutiny etc. could be done to assess the performance of RAs in implementing the scheme.

DGFT stated (March 2020) that the revamp of Information Technology backbone for the MEIS/SEIS scheme was underway and a monitoring dashboard was being built to address issues such as time taken to process claims, RMS etc. They informed that the JASPER system at the DGFT headquarters had been currently monitoring the pendency of MEIS and SEIS claims.

Audit appreciates DGFT's endeavour of bringing such reengineered software platform, however, such software with built-in quantifiable performance metrics, dashboard, etc. should be developed with generic features so as to be useful for all the existing and new schemes envisaged by DGFT. Such solution would not only be cost effective but also would provide pedestal for evaluating/comparing all the related schemes against common benchmarks.

14. We recommend that DGFT may consider commissioning a mid-term evaluation study of the achievements of any such schemes introduced vis-à-vis the main objectives of the scheme.

DGFT stated (March 2020) that since the FTP 2015-20 was expected to sunset from 31 March 2020, a mid-term evaluation might not be feasible.

Audit recommendation was generic as periodic evaluation of schemes would ensure that its intended objectives were being met besides providing for mid-course corrections in case of any deficiencies.

New Delhi
Dated: 13 July 2020


(Sandeep Lall)
Director General (Customs)

Countersigned

New Delhi
Dated: 15 July 2020


(RAJIV MEHRISHI)
Comptroller and Auditor General of India

