

CHAPTER II: ADVANCE LICENSING SCHEME/DUTY EXEMPTION ENTITLEMENT CERTIFICATE (DEEC)

2.1 Highlights

- Data furnished by 18 regional licensing authority (RLAs) revealed that free on board (FOB) value of exports actually realised was only 27 percent of that prescribed for 90,807 licences. It did not tally with that furnished by director general of foreign trade (DGFT).

(Paragraphs 2.4.1 and 2.4.2)

- In 146 advance licences issued by 16 RLAs duty of Rs.67.85 crore and interest of Rs.26.10 crore was recoverable. Of this 57 percent was recoverable from 13 licences alone.

(Paragraph 2.5.1)

- In 76 cases of RLA Chennai and Kolkata, customs failed to initiate action against defaulter importers to recover customs duty of Rs.7.99 crore, interest of Rs.6.30 crore on duty free imports of goods worth Rs.21.34 crore.

(Paragraph 2.5.2)

- Non monitoring of 185 cases of non submission of documents evidencing fulfilment of EO on expiry of EO period by RLAs/customs resulted in duty foregone amounting to Rs.187.82 crore besides interest of Rs.56.02 crore.

(Paragraph 2.6)

- Import of material in excess of adhoc norms/standard input output norms (SION) fixed by special advance licensing committee (SALC) in 33 cases and imports made despite rejected applications in seven cases entailed recovery of duty amounting to Rs.3.52 crore besides interest of Rs.1.67 crore.

(Paragraphs 2.7.1 and 2.7.2)

- Extension of EO period by seven RLAs in 18 cases without imposition of composition fee and non recovery of duty and interest in cases of extension beyond validity period entailed recovery of Rs.4.21 crore.

(Paragraphs 2.8.1 and 2.8.2)

- Non monitoring of 1739 bonds for Rs.2,537.50 crore and non renewal of bank guarantee (BGs) in 566 cases for Rs.33.52 crore executed in nine custom houses and one RLA led to non discharge/enforcement of bonds/BGs on expiry of their EO/validity period.

(Paragraphs 2.9.1 and 2.9.3)

- Non realisation of foreign exchange of Rs.19.43 crore in 12 cases entailed recovery of customs duty amounting to Rs.7.68 crore besides interest of Rs.1.94 crore on unutilised inputs of Rs.13.74 crore.

(Paragraph 2.10)

- **Other irregularities like incorrect fulfilment of EO, availment of double benefit, imports of inputs beyond validity period of licence as well as before issue licence, incorrect clubbing of licences and excess imports due to non observance of licence conditions involved incorrect grant of exemption of duty amounting to Rs.15.08 crore besides interest of Rs.6.93 crore.**

(Paragraph 2.14)

- **Lack of coordination between customs and RLA non monitoring/submission of documents in RLAs was in evidence in 194 cases of import/export involving customs duty of Rs.122.42 crore along with interest of Rs.49.11 crore besides penalty of Rs.50.59 crore.**

(Paragraphs 2.15 and 2.15.2)

2.2 Introduction

The objective of advance licensing scheme (DEEC) introduced in 1976 is to provide registered exporters with basic inputs at international prices without payment of customs duty in India. Customs notifications No.30/97, 31/97, 36/97, 48/99, 50/2000 and 51/2000 envisage duty free imports of raw materials, intermediates, components, consumables, parts, computer software, accessories, mandatory spares (not exceeding five/ten percent with effect from 25 May 1998 of cost insurance freight (CIF) value of duty free licence). Advance licences are issued on basis of inputs and export items given under SION and also on basis of adhoc norms or self declared norms subject to approval of advance licensing committee (ALC) constituted by DGFT which also has representatives of department of revenue. Scheme is administered by Ministry of Commerce/DGFT while exemption from levy of customs duty on imported inputs is allowed by Ministry of Finance/department of customs. Advance licences are granted under relevant Exim Policy.

2.3 Objectives of audit

Review on advance licensing scheme was featured in Audit Report No.4 of 1996. PAC in their 24th report (11th Lok Sabha) had adversely commented on major deficiencies in monitoring of EO and lack of internal check. In the light of shortcomings and misuse observed, Ministry of Commerce made major changes in new Exim Policy 1997-2002 to plug loopholes.

Audit evaluated working of advance licence scheme within the framework of law and Exim Policy 1997-02, covered by customs notifications issued during 1 April 1997 to 31 March 2002 (as amended). Test check of 10,008 licences involving CIF value of Rs.24,915 crore out of 90,807 licences issued for CIF value of Rs.84,701.51 crore was undertaken in 18 offices of JDGFT and concerned custom houses with a view to seek assurance that:-

- (i) main objectives of the scheme viz. fulfilment of EO, timely realisation of foreign exchange was achieved,
- (ii) bonds/bank guarantee (BG)/legal undertaking (LUT) were obtained and wherever required enforced by licensing/customs authorities,
- (iii) pre/post importation conditions laid down in customs notifications were duly fulfilled and

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- (iv) proper internal controls like periodical monitoring and coordination between licensing and customs authorities were in place.

2.4.1 Macro data furnished by 18 RLAs located in eight States.

(Amount in crore of rupees)

Year	No of DEEC licences issued	CIF value of licences prescribed	CIF value of actual imports	Amount of duty foregone on imports	FOB value of exports prescribed	FOB value of exports actually realised
1997-1998	16247	6593.44	4918.02	1802.70	13322.40	6267.24
1998-1999	16983	10895.45	5424.76	1856.68	19014.19	7042.11
1999-2000	18534	13497.20	4366.79	1549.47	20649.82	8776.08
2000-2001	19082	20596.19	4605.43	1875.49	55384.55	8385.32
2001-2002	19961	35634.72	4751.56	1922.24	58079.48	15221.67
Total	90807	87217.00	24066.56	9006.58	166450.44	45692.42

Details of CIF value of actual imports, duty foregone on imports has not been furnished by JDGFT Chennai, Pondicherry, Kolkata, Bangalore, Ahmedabad, Vadodara, Surat, Rajkot, Hyderabad and Visakhapatnam. and FOB value actually realised by Pondicherry, Kolkata, Mumbai, and Pune not available.

Above figures, reveal that FOB value of exports actually realised was only about 27 percent of that prescribed.

2.4.2 Macro data furnished by DGFT office

(Amount in crore of rupees)

Year	No of DEEC licences issued	CIF value of licences prescribed	CIF value of actual imports	*Amount of duty foregone on imports	FOB value of exports prescribed	FOB value of exports actually realised
1997-1998	19330	9712.30		3878.00	20071.58	
1998-1999	16682	9272.11		4135.09	16408.48	
1999-2000	17593	12002.30		4429.45	19992.01	
2000-2001	17026	23462.98		5611.88	39274.61	
2001-2002	19921	33009.46		7890.25	45353.04	
Total	90552	87459.15		25944.67	141099.72	

*Duty foregone furnished by Ministry of Finance, drawback directorate without commissionerate wise details as such it does not pertain to 18 RLAs covered in table.

Information in table (para 2.4.1) has been furnished by RLAs whereas information in table (para 2.4.2) has been furnished by DGFT and Ministry of Finance. Comparison revealed that:

- the information does not tally. Licences issued as per RLAs were 90807 whereas according to DGFT, number of licences issued during five years period were 90552. Similarly CIF value and FOB prescribed there against do not tally. CIF value as furnished by RLAs is less by Rs.242.15 crore while FOB value prescribed was more by Rs.25350.72 crore.

- Para 7.25 of HBP Vol.I (as on 31 March 2001) provides for submission of bank certificate of exports and realisation by licence holder in appendix 25 or 14-B as the case may be while para 7.26 *ibid* provides for submission of DEEC both for imports and exports for redemption of licences. After redemption of licences, discharge certificate is to be sent to customs authorities. Yet, DGFT has expressed their inability to provide data of actual realisation of FOB value and imports made against the licences issued during the five years period not only for all licences issued but even for those licences which were redeemed.

Audit findings are contained in the succeeding paragraphs.

2.5 Non/shortfall in fulfilment of EO

According to para 7.14 of Exim Policy 1997-02, period of fulfilment of EO under duty free licence commences from date of issue of licence. EO shall be fulfilled within a period of 18 months except in case of supplies under special imprest licence/advance licence to project/turnkey projects. In case of bona fide default in fulfilment of EO according to para 7.28 of HBP Vol I, licence holder is required to pay to:-

(i)(a) customs authority, customs duty on unutilised value of imported material along with interest at 15 per cent per annum;

(b) licensing authority, an amount equivalent to three per cent of CIF value of unutilised imported material as per public notice dated 17 September 2001. However, these provisions shall not apply if unutilised imported material was freely importable.

(ii) if EO is fulfilled, in terms of quantity, but not value, no penalty shall be imposed provided licence holder has achieved minimum prescribed value addition/positive value addition. However, if value addition falls below prescribed/positive level, licence holder is required to deposit equivalent amount so that 100 times the deposited amount and FOB value realised in Indian rupees together account for positive value addition over CIF value.

(iii) if EO is not fulfilled both in terms of quantity and value, licence holder shall for regularisation pay according to (i) and (ii) above

2.5.1 Non fulfilment of EO

Test check revealed that 146 advance licences were issued by 16 RLAs with EO of Rs.309.77 crore. Though licencees imported raw materials for CIF value of Rs.134.19 crore, no exports were made (May 2005) and entire imported material remained unutilised. Hence the licencees were liable to pay customs duty amounting to Rs.67.85 crore along with interest of Rs.26.10 crore to customs authorities. They were also liable to surrender special import licence (SIL) equivalent to five times CIF value of imported goods for licences issued upto 16 September 2001 and thereafter three per cent CIF value of unutilised raw materials as per public notice 37 of 17 September 2001 to licensing authority which worked out to Rs.291.43 crore apart from penalty of Rs.1.35 crore on shortfall in fulfilment of EO. In reply, RLA Ahmedabad, Mumbai and Kolkata accepted (September/October 2005) objections in 12 cases and initiated action for recovery of Rs.10.57 crore.

Audit noticed that just 13 licencees (in six RLAs) comprised 57 percent of total recoverable amount on account of duty and interest payable to customs department and penalty to DGFT as given in the following table: -

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(Amount in lakh of rupees)

Sr. No.	Licencees	Licence No.	Date	Duty	Interest	Penalty
1.	Modipon Fibres Co.	510039962	13.7.01	144.96	64.47	3.13
2.	Gujarat Guardian Ltd	500692	26.2.98	171.49	137.19	4.89
3.	-do-	501226	27.8.98	174.82	113.63	2.89
4.	-do-	510056227	28.03.02	138.98	31.27	3.05
5.	-do-	510050401	8.01.02	136.84	39.34	3.01
6.	-do-	510032197	15.02.01	192.25	72.09	3.17
7.	Ranbaxy Labs Ltd.	501316	22.9.98	173.33	160.33	3.13
8.	-do-	501394	15.10.98	148.20	109.30	2.74
9.	-do-	501855	19.2.99	170.05	136.04	2.25
10.	Satnam Overseas Ltd.	510049227	19.12.01	110.31	30.34	21.84
11.	-do-	510053521	19.2.02	115.97	22.76	11.48
12.	Dishman Pharmaceutical	810013577	8.10.01	154.27	-	2.45
13.	BPL Ltd.	710008405	14.5.01	132.00	70.95	2.81
14.	Nobel Merchandise (I) Ltd.	310002643	29.7.99	165.12	134.16	2.21
15.	Alam Tannery	210026490	13.9.01	156.72	55.35	2.47
16.	Jord Engg. (I) Ltd.	137947	21.12.99	496.12	-	11.67
17.	Bharat Electronic Ltd.	710000317	6.8.99	104.38	-	-
18.	Indian Designs	710008341	9.5.01	178.79	-	-
19.	VWF Industries Ltd.	710009028	26.6.01	180.00	-	-
20.	NSP Electronics	710009005	22.6.01	950.00	-	-
	Total			4194.60	1177.22	83.19

In 25 cases of RLA Bangalore, CIF value of actual imports and other details were not available.

Apart from these, some others are narrated below:-

M/s. Tamilnadu Steel Tubes Ltd. Chennai, was issued advance licence (November 1999) by JDGFT Chennai and allowed to import raw material for CIF value of Rs.2.15 crore with EO of Rs.3.48 crore for export of steel tubes. Licence holder imported raw material worth Rs.1.38 crore but did not export end products till February 2005. Hence, duty and interest amounting to Rs.91.87 lakh and Rs.79.24 lakh respectively were recoverable for non-fulfilment of EO. Besides, penalty of Rs.1.38 lakh was also recoverable.

M/s. Epicenzyms Pharmaceutical and Industries Chemicals Ltd. (Mumbai) was issued advance licence for duty free import of various goods with CIF value of Rs.1.42 crore, with EO of Rs.2.30 crore. Though, licensee imported goods worth Rs.77.38 lakh, no exports were made. Hence they were liable to pay customs duty of Rs.47.14 lakh along with interest of Rs.27.11 lakh apart from penalty of Rs.0.77 lakh on unutilised imported material.

M/s. Mahendra Petrochemicals Pvt. Ltd., Ahmedabad was issued advance licence (October 2000) for duty free import of goods valued at Rs.84.83 lakh with EO of Rs.1.13 crore. Though licensee imported raw material of CIF value of Rs.60.63 lakh in February/March 2000 and used the same in manufacturing activities, finished goods were not exported and were sold in local market. For selling finished goods in local market, licensee had not sought permission as required under para 4.14 of Exim Policy. Hence unutilised imported material was liable to duty amounting to Rs.29.45 lakh along with interest of Rs.22.09 lakh apart from penalty of Rs.0.61 lakh. On this being pointed out (May 2005), RLA Ahmedabad accepted (September 2005) the objection.

2.5.2 Non recovery of customs duty and interest in cases adjudicated by JDGFT for non submission of documents

Review of cases adjudicated by two RLAs Chennai and Kolkata revealed that in 76 licences issued (April 1997 to February 2002) with Chennai and Kolkata as port of registration, licence holders failed to fulfil EO after importing raw materials for CIF value of Rs.21.34 crore. Consequently, RLAs adjudicated the cases and levied penalty for failure to do so. Customs duty of Rs.7.99 crore and interest Rs.6.30 crore involved in these cases has not so far been recovered (November 2005) by the respective custom houses. Although RLA Kolkata communicated to customs the fact of issue of defaulter order and orders in adjudication, customs did not initiate action against defaulter importers to produce evidence in discharge of EO as per condition (vi) of notification No.30/97-Cus. In Chennai, action taken by customs was still awaited (November 2005).

2.5.3 Shortfall in fulfilment of EO

Audit scrutiny revealed that 152 licences were issued by 16 RLAs with prescribed EO of Rs.537.25 crore. Though licencees imported inputs worth Rs.268.86 crore and fulfilled EO to the extent of Rs.399.12 crore, EO fulfilled was short either quantitatively or proportionate value wise by Rs.155.57 crore. Of these, in 52 cases, value addition achieved was negative ranging from 0.35 percent to 91.32 percent, while in other cases quantitative shortfall was noticed. This resulted in non utilisation of duty free imported goods worth Rs.72.06 crore and licencees were liable to duty amounting to Rs.27.09 crore along with interest of Rs.16.72 crore apart from penalty of Rs.22.40 lakh on unutilised goods. On this being pointed out (September 2003 to April 2004) RLA Mumbai and Kolkata adjudicated 14 cases raising demand of Rs.4.50 crore, of these a sum of Rs.43.97 lakh has since been recovered in six cases. RLA Hyderabad reported recovery of Rs.16.84 lakh in one case. Reply in remaining cases was awaited (November 2005).

A few cases are narrated below:-

M/s. S.P. Garments (Chennai) was issued advance licence (March 2000) and allowed to import raw materials worth Rs.1.01 crore with EO of Rs.1.22 crore. Though licencee imported raw materials for Rs.67.96 lakh, EO achieved was only partial leading to shortfall of Rs.48.03 lakh. Therefore, licence holder was liable to pay customs duty of Rs.36.10 lakh and interest of Rs.25.33 lakh on excess imported quantity worth Rs.38.37 lakh, which had not been recovered even after lapse of 27 months from date of expiry of EO period (September 2002).

M/s. Hussnain International (Delhi) was issued advance licence (February 2000) with EO of Rs.1.41 crore. Though licencee made actual imports of input worth Rs.1.17 crore, export of finished product of Rs.78.18 lakh resulted in negative value addition of 33 percent with shortfall in EO to the extent of Rs.62.32 lakh. Hence they were liable to pay duty amounting to Rs.68.06 lakh along with interest of Rs.39.13 lakh apart from penalty of Rs.0.39 lakh on unutilised imported goods of Rs.1.07 crore.

M/s. Zenith Ltd. was issued advance licence (May 2001) by JDGFT Mumbai for duty free import of raw material worth Rs.4.56 crore with EO of Rs.4.96 crore. Licencee had imported goods valued at Rs.4.13 crore and made exports worth Rs.75.44 lakh resulting in shortfall in achievement of EO to the extent of Rs.4.20 crore (negative value addition of 81.74 percent). As such they were liable to pay customs duty of Rs.1.91 crore along with interest of

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Rs.69.31 lakh apart from penalty of Rs.3.38 lakh on unutilised value of imported goods of Rs.3.67 crore.

M/s. Sterlite Industries India Ltd. was issued advance licence (August 2000) by JDGFT Mumbai for duty free imports of various goods worth Rs.47.54 crore against export of 'single mode optical fibre' (300000 kms) for Rs.56.59 crore. Audit scrutiny revealed that licensee had imported 2191.70 kg of silica substrate tubes, 16086.72 kg of silica sleeving tubes, and 1164 kg silica inlet tubes to export 107100.70 km of single mode optical fibre. According to SION norms, for above exports licensee was entitled to import 1249.87 kg of silica substrate tube, 10100.67 kg of silica sleeving tubes and 415.51 kg of silica inlet tubes. There was shortfall in achievement in terms of quantity as per SION. Excess imports of above items entailed recovery of Rs.1.81 crore as duty and Rs.1.04 crore as interest on unutilised value of Rs.6.63 crore.

M/s. Usha Beltron Pvt. Ltd. was issued advance licence (December 1999) by JDGFT Kolkata for CIF value of Rs.17.22 crore against EO of Rs.25.87 crore. Licence fulfilled 92.45 percent of EO during validity of the licence. ZJDGFT, Kolkata discharged the licensee from EO after recovery of duty of Rs.22.90 lakh including interest of Rs.8.84 lakh for excess import of two items (waste scrap and LAM coke). Scrutiny of documents, however, revealed that there were excess imports in respect of the remaining nine other items also. Short recovery of duty and interest on such excess import worked out to Rs.20.34 lakh. On this being pointed out, JDGFT, Kolkata reported (September 2005) recovery of the full amount.

M/s. GKW Ltd. Kolkata was issued advance licence (September 1998) for duty free import of goods valued at Rs.1.07 crore against EO of Rs.1.50 crore. Licensee imported goods worth Rs.78.88 lakh against which export was only Rs.97.99 lakh resulting in quantity wise shortfall in fulfilment of EO. As such the licensee was liable to pay customs duty of Rs.14.79 lakh along with interest of Rs.12.02 lakh.

M/s. Aurobindo Pharma, Hyderabad was issued advance licence (March 2002) for CIF value of Rs.40.16 crore with EO of Rs.48.50 crore. Even after expiry of two extensions, licensee could export 20824.60Kg. of indinavir sulphate against EO of 25000 Kg. Total unutilised value of raw materials imported was Rs.1.94 crore for which liability of customs duty was Rs.1.01 crore and interest Rs.9.03 lakh.

2.5.4 Non- fulfillment of EO due to short shipment

M/s. Uttam Steel Ltd. (RLA Mumbai) was issued advance licence (May 1999) for export of 200 MT C.R. galvanised sheets for FOB value of Rs.43.56 lakh against CIF value of Rs.32.26 lakh. It was noticed that against total shipment of 100 bundles involving two MT each (200 MT), 30 bundles were short shipped. Adoption of total export quantity as 199 MT was not in order as product bundles exported were of the same size as specified in purchase order. Taking into account average weight of two MT of each bundle, quantity short shipped worked out to 60 MT. Due to short shipment there was shortfall in fulfilment of EO, therefore, licensee was liable to pay customs duty of Rs.7.78 lakh and interest of Rs.6.22 lakh as well as penalty of Rs.0.26 lakh as three percent of unutilised CIF value in terms of para 7.28 of HBP Vol.I. Reply on this being pointed out in December 2004 was awaited (November 2005).

2.5.5 Shortfall in EO due to de logging

M/s. Zuari Industries Ltd., Chennai was issued advance licence (RLA Chennai) in July 2000 for import of “components of furniture” for CIF value of Rs.19.81 lakh with EO of 89.100 cubic meter of furniture for FOB value of Rs.31.70 lakh. Licencee exported entire quantity. However, 72.01 cubic meter was rejected and returned to licence holder. The re-import was de-logged from the advance licence. Excess import arising as result of de-logging of the licence remained to be regularised by payment of duty of Rs.7.58 lakh and interest of Rs.4.83 lakh.

2.6 Delay in monitoring cases of non-submission of documents by concerned RLA/Customs

According to para 7.24 of HPB Vol.I. (1997-2002) licensing authority shall maintain proper records for monitoring achievements of EO and other particulars within specific period for completion of EO. Every licencee has to submit requisite evidence in discharge of EO within a period of two months. In case of failure to complete EO or failure to submit information regarding export, licensing authority should initiate action. However, in respect of shipments where 180 days period for realisation of foreign exchange has not become due, licensing authority shall not initiate action for non submission of bank certificate of exports and realisation, provided, other documents substantiating fulfilment of EO have been furnished. In such cases, licensing authority should take action such as, refuse further licences, enforce conditions of the licence and undertaking and also initiate action as per law.

During review of 185 licences, it was noticed that though EO period had expired, licencees did not submit evidence for fulfilment of EO. On the other hand, RLAs too failed to initiate action against licence holders to call for details of import and export for adjudication. CIF value of import and FOB value of export prescribed in the licences were Rs.339.92 crore and Rs.491.54 crore respectively, on which duty foregone amounted to Rs.187.82 crore besides interest of Rs.56.02 crore on CIF value of prescribed/actual imports. RLA Hyderabad reported (October 2005) recovery of Rs.18.27 lakh in one case.

2.7 Excess imports due to violation of standard input output norms (SION)

According to para 7.8 of HBP Vol.I. (1997-2002), licensing authority issues advance licences with actual user condition to manufacturer exporter or merchant exporter where the SION are not fixed, based on self declaration and undertaking by the applicant for final adjustment as per adhoc norm/SION fixed by the SALC. Applicant gives undertaking that he shall abide by the norms fixed by SALC and accordingly pay duty together with interest on unutilised inputs. In such cases, where the norms are not finalised by ALC within six months, norms as applied for shall be treated as final. If application for fixation of norms is rejected on account of non-furnishing of required documents/information, the licence holder shall be liable to pay duty, interest and penalty.

2.7.1 Import of material in excess of adhoc norms

Audit observed that in 33 applications for fixation of adhoc norms, though SALC had admitted applications, it reduced the norms declared by licencees. They had imported entire quantity as per the self declared norms. Since SALC had reduced the quantity, they had to

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pay customs duty amounting to Rs.2.87 crore along with interest of Rs.1.37 crore on excess imported raw material worth Rs.4.22 crore as per undertaking furnished by them. However, the licencees had not paid duty and RLAs had not adjudicated the cases and informed the customs authorities to recover duty on such excess imports. In reply, RLA Mumbai reported (September 2005) recovery of Rs.5.38 lakh including interest in one case.

2.7.2 Non recovery of duty on rejected applications for fixation of norms

In respect of seven licences issued by two RLAs, adhoc norms submitted by licencees were rejected by SALC for want of information and existence of nexus between imported and export goods. Duty and interest recoverable on actual imported inputs worked out to Rs.65.04 lakh and Rs.29.86 lakh respectively.

Though SALC had initiated action on applications for fixation of adhoc norms within the prescribed period, licencees imported raw materials in full and did not come forward to pay duty and interest on imports made against licences, which had been rejected by SALC. Imports were made without norms approved by SALC and RLAs failed to adjudicate the cases according to provisions and declarations obtained from the licencees for final adjustment of actual imports as per approved norms.

2.8 Non realisation of penalty for non fulfilment of EO

According to para 7.28 (ii) of HBP Vol.I, if EO is fulfilled in terms of quantity, but there is shortfall in terms of value, no penalty shall be imposed if there is positive value addition. If value addition falls below positive level, licence holder is required to deposit an equivalent amount so that 100 times deposited amount and FOB value realised in Indian rupee together account for positive value addition over CIF value.

In respect of 10 licences issued by JDGFT Coimbatore, the licencees had not made any export after import of raw material for permitted CIF value of Rs.25.18 crore. For non-fulfilment of EO, the licencee had paid the customs duty with interest to the customs authorities; however, the penalty amount of Rs.29.97 lakh demanded by the licensing authority was awaiting recovery for two to five years from the expiry of EO period

In respect of 11 licences issued by JDGFT Hyderabad, Mumbai and Ernakulam, EO had been partly fulfilled and licencees paid duty and interest on unutilised raw materials worth Rs.169.83 crore to customs authorities but penalty amount of Rs.20.76 lakh payable to RLAs for shortfall in fulfilment of EO was not paid.

Total penalty unrealised by RLAs amounted to Rs.50.73 lakh in aforesaid 21 cases, while in reply, NCH Mumbai stated that a SCN for recovery of duty and interest of Rs.72.77 lakh has been issued in May 2005 in one case.

2.8.1 Non realisation of composition fee

According to para 7.22 of HBP Vol.I (1997-2002), RLAs shall grant extension of EO period for six months from date of expiry of licence on receipt of composition fee of one percent on unfulfilled FOB value of EO corresponding to CIF value of imports made, and further extension of six months shall be granted on receipt of composition fee of five percent.

Audit scrutiny revealed that in 18 licences issued by seven RLAs, licencees had not paid composition fee in full. Extension of EO period allowed by licensing authorities without

collecting composition fee was not in order and led to non recovery of fee amounting to Rs.1.39 crore in these cases.

Of these 18 licencees, five were liable to pay Rs.1.09 crore representing around 78 percent of total recoverable amount.

2.8.2 Exports made beyond valid EO period

M/s. Tractor and Farm Equipment and two others were issued five advance licences by RLA Chennai (May 1997 to March 2001). As exports in these cases were made beyond valid EO period, they were not eligible for consideration against EO as no composition fee was paid and no extension was allowed. Thus, for excess imports made consequent to shortfall in fulfilment of EO, payment of duty and interest was necessary. Customs duty and interest to be recovered in above five cases worked out to Rs.1.70 crore and Rs.1.12 crore respectively.

2.9 Non-enforcement of bonds/BG

According to customs notifications issued from time to time, the importer at the time of clearance of imported material is required to execute a bond/BG with customs department to pay on demand an amount equal to duty leviable but for exemption, on imported material in respect of which conditions specified therein have not been complied with. One of the conditions for grant of exemption is that the licence holder should submit export obligation discharge certificate (EODC) issued by RLAs to customs department within 30 days of expiry period allowed for fulfilment of EO or within the extended period granted.

2.9.1 Non discharge/enforcement of bond by customs

Audit scrutiny revealed that in 1739 cases of imports made through eight customs commissionerates, on advance licences issued by six RLAs, bond for value equivalent to duty foregone amounting to Rs.2537.50 crore were executed with customs authorities. In all these cases EO period expired; however, in cases where EO had not been fulfilled, enforcement of bonds was to be initiated to recover duties from defaulting licencees. The cases have been kept alive for want of EODC from licensing authorities. As huge amount of Government revenue is involved, custom houses should have reviewed the cases expeditiously in order to enforce bonds in cases of default to recover the duty.

Board's circular No.24/96-Cus. dated 19 April 1996 provided that monitoring of EO remain the primary responsibility of licensing authority (DGFT) and in addition to submission of DEEC book by licence holders to customs, EODC from licensing authority be insisted upon for discharge of bonds. Thus both departments failed to adequately discharge their control functions. In reply, customs department (ACC Mumbai) intimated (August 2005) that in seven cases bonds were cancelled while in 54 cases SCNs were issued to the parties.

2.9.2 Execution of insufficient bond

It was observed that in 22 cases of imports made through Delhi and ICD Bangalore commissionerate insufficient bonds were accepted by customs authorities to the tune of Rs.125.56 crore. In case of necessity, government revenue to that extent would not be legally enforceable and would remain unprotected.

2.9.3 Non renewal of BG executed with customs/JDGFT

In 552 cases BGs executed with seven customs houses were not renewed after validity period, though licencees had not fulfilled EO and EODC had not been issued by RLAs. It

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was the duty of customs houses to enforce BGs before their maturity period wherever licencees had not come forward to renew them. In these cases government revenue equivalent to duty of Rs.33.37 crore had not been safeguarded.

Apart from this 14 BGs executed with JDGFT, Chennai for Rs.15 lakh towards excise duty foregone for obtaining advance release order were also not renewed. Total BGs not renewed thus, worked out to Rs.33.52 crore. In reply, NCH Mumbai intimated (July 2005) that in three cases BGs for Rs.12.31 lakh were encashed while in four cases licences were redeemed on fulfilment of EO.

2.9.4 Non/insufficient execution of BGs with customs

According to Board's circular No.45/96-Cus. dated 28 August 1996, importers of different categories were required to execute BGs as prescribed for them.

- | | | | |
|-----|---|---|-------------------|
| (a) | Super star/star trading houses/export houses/PSUs | - | Nil |
| (b) | Manufacturers/exporters other than at (a) above | - | 25 percent |
| (c) | Others | - | 100 of duty saved |

Audit scrutiny revealed that 12 cases in four custom houses wherein BGs executed were Rs.2.69 crore against requisite amount of Rs.6.16 crore, involved shortfall in amount of BGs to the extent of Rs.3.47 crore.

Of these in Cochin custom house, BG of M/s. Zam Zam Exports Trissur, of Rs.0.80 lakh expired on 11 April 2001. In another case of M/s. General Spices Trissur, BG was for 25 percent against requirement of 100 percent. All the so called exporters were represented by one and the same person who was absconding, as such BGs were deficient to the extent of Rs.1.13 crore resulting in loss of interest of Rs.61.69 lakh.

2.9.5 Furnishing of fake BG

M/s. Kozy Silk Ltd. (Bangalore) executed BG with customs department for Rs.7.31 lakh valid upto 25 February 1999 as security for duty forgone in respect of imports made under licence issued in August 1995. While seeking extension (January 2002) of BG for non fulfilment of EO, it was found to be fake. No penal action except to address letters to licencee in January 2002/2003 and March 2004 (which were returned undelivered) for payment of duty of Rs.7.31 lakh was taken by department.

2.10 Non realisation of foreign exchange

According to para 7.25 of HBP Vol. I read with para 11.3 of Policy, licence holder is required to submit bank realisation certificate within six months of shipment showing receipt of foreign exchange from concerned bank as evidence in fulfilment of EO.

Audit scrutiny revealed that against 12 licences issued by four RLAs, foreign exchange had not been realised in full. RLAs had also not adjudicated the cases to obtain requisite documents in support of having fulfilled EO and evidence for realisation of foreign exchange. Total CIF value of inputs made in proportion to unrealised foreign exchange worked out Rs.13.74 crore on which the duty recoverable was Rs.7.68 crore with interest of Rs.1.94 crore.

2.11 Non recovery of penalty

According to para 4.20 of Exim Policy read with section 11(2) of Foreign Trade (Development and Regulation) Act, 1992, penalty is leviable for violation of any of the conditions of licence or failure to fulfil EO. Where any person makes or abets or attempts to make any export or import in contravention of any provision of this Act or any rules or orders made thereunder or export and import policy, he shall be liable to penalty not exceeding one thousand rupees or five times value of goods in respect of which any contravention is made or attempted to be made, whichever is more.

A penalty imposed under this Act, may, if it is not paid, be recovered as an arrear of land revenue and importer-exporter code number of the person concerned, may on failure to pay the penalty by him, be suspended by the adjudicating authority till the penalty is paid.

Audit scrutiny revealed that ten RLAs had imposed penalty in 573 cases for a total amount of Rs.478.52 crore. However, recovery was meagre in 33 cases for only Rs.15.54 lakh, which represented even less than one percent. Balance amount of Rs.478.37 crore was pending for recovery for period ranging from six months to 19 years in 543 cases.

Of these, penalty of Rs.409 crore (i.e. 85 percent) was recoverable in 286 cases by three RLAs i.e. Delhi, Mumbai and Ahmedabad alone for non-fulfilment of EO.

2.12 Incorrect reckoning of EO by including exports made prior to date of application for advance licence.

According to para 7.18 of Exim Policy 1997-2002, exports/supplies made from date of receipt of an application for duty free licence alone could be counted towards discharge of EO. In case of application for advance intermediate licence, only such supplies shall be covered towards discharge of EO, which are made after the issuance of the invalidation letter to ultimate exporter.

In 22 advance licences issued by RLA Coimbatore and three licences issued by RLA Chennai under deemed export category, licencees had supplied/exported their products before date of submission of application to obtain the advance licence. Supplies made prior to the date of application had been reckoned for fulfilment of EO, which was contrary to the provisions of Exim Policy. Total CIF value of raw materials used in the export/supplies made prior to the date of application was Rs.16.49 crore and duty recoverable thereon was Rs.9.06 crore beside interest of Rs.5.61 crore.

2.13 Non realisation of duty and interest in cases adjudicated by custom houses

According to para 7.2 and 7.4 of Exim Policy 1997-2002, DEEC licences are issued with actual user condition. Customs notifications Nos.30/97 and 51/2000 issued under the aforesaid policy provisions imposed a condition viz. exempted materials were not to be disposed of or utilised in any manner except for utilisation in discharge of EO. Section 28 AA of Customs Act, provides time limit of three months for payment of demand of duty determined under section 28 (2) from date of determination failing which importer is liable to pay duty along with interest.

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Review of confirmed demands pending realisation in respect of DEEC scheme at Chennai, Bangalore and Delhi custom houses revealed that 102 advance licences were issued for import of raw materials under aforesaid notifications with actual user condition, but material was diverted to local market in violation of conditions of notifications. Customs house/directorate of revenue intelligence took action on misuse of licence, by licence holders and confirmed demand (between December 1997 to January 2005) of duty of Rs.113.17 crore, fine and penalty of Rs.29.56 crore and Rs.90.88 crore respectively. Licence holders paid a sum of Rs.16.58 crore by cash/enforcement of BGs but balance of Rs.217.02 crore was pending realisation against these licences.

Of these, demand in five cases ranged for more than Rs.5 crore to Rs.27 crore.

A case is illustrated below.

M/s. Manba Enterprises, a partnership firm, was issued seven advance licences by RLA, Pondicherry and 11 advance licences by RLA, Chennai. Licence holder registered them with Chennai (sea) custom house and imported "non magnetic SS sheet/coil of AISI 304 grade" for total value of Rs.23.09 crore under above notification. They had stated in licence applications that place of manufacture was located in three different places at Kumbakonam, Chennai and New Delhi. Investigation made by DRI subsequently proved that declaration was incorrect and no manufacturing unit existed in those places. Consequent on non fulfilment of EO and violation of conditions of notification, demand for customs duty of Rs.15.42 crore was confirmed by customs department (February/March 2004) along with fine of Rs.6 crore and penalty of Rs.15.42 crore.

The amount was still pending realisation (May 2005). Reason for non realisation were not on record.

2.14 Other irregularities

Irregularities like incorrect fulfilment of EO, availment of double benefit, imports of inputs beyond validity period of licence as well as before issue of licence, incorrect clubbing of licences and excess imports due to non observance of licence conditions etc. involved incorrect grant of exemption of duty amounting to Rs.15.08 crore besides interest of Rs.6.93 crore as given below:

(Amount in lakh of rupees)

Sr. No.	Irregularity	Number of importers/ licences involved	RLA	Duty recoverable	Interest recoverable	Whether accepted
1.	Incorrect fulfillment of EO	1/3	Chennai	30.78	12.91	No reply
2.	Availment of double benefit	7/10	Coimbatore and Chennai	95.91	61.96	-do-
3.	Import of inputs beyond the validity of licences	13/17	New Delhi and Mumbai	952.00	385.00	SCN was issued in one case for Rs.21.59 lakh.
4.	Incorrect allowance of imports before issue of licence	7/7	New Delhi	126.09	61.84	No reply

5.	Excess imports than licence	1/1	New Delhi	210.00	126.00	No reply
6.	Incorrect reckoning of exports made by third party	1/2	Coimbatore	11.25	6.38	-do-
7.	Incorrect clubbing of licences	2/7	Madurai and Coimbatore	14.27	6.59	-do-
8.	Irregular grant of advance licences	1/2	Mumbai	42.39	18.02	-do-
9.	Lack of follow up action	1/5	Bangalore	2.80	-	No reply (SIL Rs.48.19 lakh)
		13/38	Ahmedabad & Vadodara	-	-	CIF value of Rs.58.44 crore. RLA Ahmedabad accepted objection in 11 cases.
10.	Issue of advance licence on misdeclaration	1/1	Bangalore	-	-	Non utilisation of imported inputs worth Rs.1.87 crore in export product.
11.	Non utilisation of raw material in export product	1/1	Kolkata	12.24	8.01	Rs.0.88 lakh payable to RLA.
12.	Issue of fresh licences where EO was not met for previous licences	1/11	Bangalore	-	-	No reply
13.	Avoidance of payment of duty	1/1	Bangalore	-	-	No reply
14.	Excess import due to non observance of licence conditions	1/2	Madurai	10.04	6.32	-do-
	Total	39/108		1507.77	693.03	21.59

In reply, NCH Mumbai stated that a SCN has been issued (May 2005) demanding duty and interest of Rs.21.59 lakh in one case.

2.15 Non Monitoring of EO

Para 7.24 of HBP Vol.I (1997-2002) provides that licensing authority shall maintain proper records to monitor achievement of EO and other particulars within specific period. Licence holder is required to submit requisite evidence in discharge of EO within two months from expiry of period prescribed to meet EO. In case of failure to complete EO or to submit relevant information/records, licensing authority should take action such as refusing further licence, enforce conditions of licence and initiate penal action with recovery of duty/interest.

It was observed in audit that in RLA Chennai, no import/export documents were furnished by the licence holders in 54 cases in which EO period expired between September 2000 and September 2003. In 14 licences issued by RLA Pondicherry, the importer did not furnish the

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import/export details. In respect of 12 licences issued by RLA Ahmedabad, documents were not produced by licencees towards fulfilment of EO even after 12 to 17 months after EO period. In absence of any import/export details having been furnished by the licencees in 80 cases, customs duty of Rs.36.78 crore and interest of Rs.6.14 crore remained un-recovered besides penalty of Rs.49.17 crore in 12 cases. In reply RLA Pondichery reported recovery of Rs.9.28 lakh in two cases.

2.15.1 Non issuance of refusal order/initiation of penal action

According to para 7.24 and 7.25 of HBP Vol. I, licensing authority with whom the advance licence holder executes legal undertaking (LUT) shall maintain proper record in master registers. Licence holder is required to submit requisite evidence in discharge of EO within two months from date of expiry of period of obligation. In case, licence holder fails to complete EO or fails to submit the relevant information/documents, licensing authority shall refuse issuance of further licences, enforce conditions of licences and LUT and shall take penal action.

Scrutiny of records (JDGFT Mumbai) revealed that in respect of 39 licences pertaining to 1999-2000 and 2001-2002, involving FOB value of Rs.49.16 crore, licence holder failed to submit any information/details, and licensing authority had not taken any action, such as issue of refusal order, forfeiture order and initiation of penal action etc. as prescribed above.

It was also noticed that in 17 cases involving FOB value of Rs.40.19 lakh, licensing authority had only refused the issuance of further licence. Further action such as enforcement of condition of licence and initiation of penal action was pending.

2.15.2 Lack of co-ordination between licensing and customs authority

As per para 7.24 read with para 7.28 of HBP Vol.I 1997-02 where licence holder fails to complete EO or fails to submit relevant information/documents, licensing authority shall take action by refusing further licences, enforcing the conditions of the licence and LUT and shall also initiate penal action as per law. In case of default in fulfilment of EO, licences shall be regularised in the manner stated in para 7.28 of HBP Vol.I. Customs department was responsible for keeping on record, LUT, bond and bank guarantee and raising of demand in cases where imported goods were not utilised for intended purpose.

Implementation of the scheme required co-ordinated functioning of the two authorities i.e. DGFT and Customs. However, licensing authorities responsible for monitoring EO did not have any mechanism to know import/export details till documents were submitted by users of the scheme. Licensing authority did not call for information relating to imports/exports from customs department. Since fulfilment of EO is directly linked to imports made, it was necessary for licensing authority to have such details on record. Customs authorities, on the other hand, cleared goods imported/exported but did not devise any system to ascertain actual fulfilment of EO although non fulfilment of EO renders importer liable for payment of duties as per customs notifications. Customs department does not ascertain details of EO from licensing authority, in order to ensure that BGs are revalidated and demands for unutilised imports are raised. There was also no formalised system of exchange of information regarding defaulting exporter between the two authorities.

In 90 licences issued by JDGFT Mumbai (1998-2002), licence holders had not furnished documents/information towards discharge of EO, even after validity period of licences.

However, no action was initiated, as per above cited provisions, by licensing authority for issuance of refusal order etc.

Data collected by audit from Customs/EDI department, revealed that though the licencees had imported goods worth Rs.128.21 crore, export details were not available. Therefore customs duty of Rs.76.79 crore along with interest of Rs.36.75 crore (upto December 2004), plus Rs.1.28 crore as an amount equivalent to one percent of the CIF value of unutilised import material was recoverable. Files made available by licensing authority did not contain any details about import made though in these cases imports in fact were made as seen from database of Customs department. Neither Customs department nor the licensing authority had taken any action to demand and recover these dues. (November 2005.)

In other 24 cases of JDGFT Mumbai, though imports were made for CIF value of Rs.14.02 crore, no export details were available on record and no action was taken to recover duty of Rs.8.85 crore and interest of Rs.6.22 crore.

Non-existence of proper mechanism for co-ordination between DGFT and customs authorities in case of default, resulted in government revenue to the extent of Rs.130.03 crore remaining not demanded and collected from licence holders. In reply, NCH Mumbai reported (July 2005) recovery of Rs.21.82 lakh in two cases.

2.15.3 Computerisation/EDI system

Non-availability of licence wise details of import/export

Indian Customs EDI System (ICES) envisages acceptance of customs documents and exchange of information electronically in centralised/structured formats, integrating customs with other agencies such as Reserve Bank of India, DGFT, custodian of imports and exports goods and regulatory agencies involved in international trade. Within the customs house, documents would move from desk of customs officer to another in electronic form.

Main objective of ICES was to respond more quickly to the needs of trade and to provide quick and correct information on imports/exports statistics to director general of commercial intelligence and statistics.

Information with regard to imports and exports made against advance licences were called for from RLA, Mumbai, who could not furnish them. No reports were stated to have been generated to indicate (i) number of licences where imports were made with corresponding fulfilment of EO (ii) whether BGs were valid in respect of cases where EO was not fulfilled (iii) number of cases where BGs were enforced (iv) cases where EODC were received from the JDGFT, Mumbai (v) the cases where licensing authority had imposed fiscal penalty for non/short fulfilment of EO (vi) the details of unutilised imported material.

Similarly, the JDGFT had also designed/developed module for issue of licences. However, no details of exports were available in database. Although licensing authority was responsible for monitoring exports, relevant database did not have vital details of exports in respect of each licence. The system was not integrated with customs. There was no mechanism for exchange of information for monitoring conditions of licence.

Despite module/application software having been developed by both departments, there was dependence upon manual check/verification for monitoring EO and recovery of duty on unutilised imports.

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Maintenance of records by licensing authority

Licensing authority with whom LUT is executed by advance licence holder under para 7.15 of HBP Vol.I, 1997-2002, is to maintain proper record in master register, containing information about licence holder viz licence number, date of receipt of application, CIF and FOB value prescribed (in rupees and US\$), date of expiry of licence, revalidation etc.

Scrutiny of records of JDGFT, Vadodara revealed that columns of master register were not filled in and register not updated, entries in columns were either not made or partially made, reference to enforcement cum adjudication (ECA) files were also not recorded. Follow up action taken was not mentioned in master register. As a result, timely action against defaulting licence holder could not be initiated. In RLA Delhi and Kolkata too essential information such as actual imports/exports, submission/non submission of documents extension/revalidation granted, amendment in CIF/FOB value, initiation of penal action were not found recorded in master registers. ECA section of RLA Kolkata did not maintain separate register showing date wise receipt of files for enforcement/adjudication against defaulter exporters. Category of licence, CIF value and subsequent follow up action were also not recorded.

RLA Vadodara replied that master register would be updated and intimated.

2.16 Audit impact

Review contains audit comments involving financial implication of Rs.1,371.46 crore arising from non compliance of provisions of Exim Policy, notifications, act, rules and instructions etc. apart from audit observations in discharge of bonds/BGs and other procedural irregularities. At audit's behest, demand of Rs.17.27 crore was confirmed in 40 cases, of which Rs.1.16 crore was recovered.

2.17 Conclusion

Review has revealed lack of well-coordinated and concerted action by RLAs and customs authorities providing opportunity to defaulting importers to misuse provisions of Exim Policy and customs notifications. There was evidence of non/short fulfilment of EO, insufficient coverage of BG and violations of pre/post importation conditions. Shortcomings in monitoring and follow up led to continued weaknesses and lacunae in implementing advance licensing scheme as pointed out in earlier Audit Report relating to Exim Policy 1992-97, which continued unabated in the next five years of Exim Policy period.

2.18 Recommendations

Since introduction of DEEC in 1976, PAC in their 230th Report (Seventh Lok Sabha), 65th Report (Eighth Lok Sabha) and 24th Report (11th Lok Sabha) had repeatedly emphasised the need to plug various loopholes and deficiencies in its working to ensure that the scheme fully served its purpose. To this end audit recommends that:-

- monitoring of EO be done as prescribed in exim policy and customs notifications through proper internal control mechanism and enforcement of bonds/BGs on expiry of EO period without delay.

- **Ministry adequately address disparities between SION norms and export product to prevent possibility of substitution of imported material and its diversion in domestic market.**
- **maintenance of registers and updation of complete and self-contained information with reference to licences issued, imports/exports made, execution of bonds/BGs and redemption thereof etc be made incumbent upon designated authorities.**
- **the two ministries concerned set up proper coordination mechanism to allow exchange of information and proper follow up of penal action prescribed for them.**

The review was issued to the Ministry of Finance and Ministry of Commerce in October 2005. At exit conference (November 2005) Board stated that reply would follow after detailed examination of issues involved by both Ministries.