Chapter 2. Systemic issues

Rough diamond, precious coloured gemstones and gold are not produced in India. These are imported from major source countries or trading hubs. These are essential inputs for the Gems and Jewellery (G&J) sector. G&J sector in India has a unique availability of traditional skills, a huge socio-economic importance and a large domestic market for different kinds of plain and studded jewellery. This sector also generates a fair amount of economic activity and contributes to the GDP of the country if value is added to the final product. Currency and asset demand of gold in India is one of the highest in the world vis-a-vis other currencies and investment asset categories. Given global demand for Indian design and workmanship, Cut and Polished Diamond (CPD) and jewellery has been one of the top exporting products for decades. Conversion of rough diamonds to CPD and gold to plain/studded jewellery creates substantial value integration with ramifications on all the economic factors.

G&J sector, in India, contributed substantially (15 per cent) to the export basket and merchandize exports growth, with commensurate revenue contribution. Reasons for growth in gems and jewellery exports were considered by DoC to be dynamic entrepreneurship, favourable Foreign Trade Policy (FTP) provisions, and market size[1]. The problems identified were that the industry was import sensitive with 90 percent of the raw material imported from overseas; the raw material was not available from direct sources adding to its cost; increasing requirement of skilled human resources; improvised training and facility centres; high trade related transaction cost and availability of competitive finances, interest rates with a favourable tax regime. Being a leading foreign exchange earner and a labour intensive sector which employed around 34 lakh workers (2008[2]) it was estimated that for an annual average growth of 25 percent[3] of the sector, 66 lakh workers would be required by 2018.

Schemes for exporters of G&J are in Chapter 4 of the FTP of the DoC. The trading transaction is captured by the Customs department, DoR, under Chapter 71 of the Customs Tariff Heading (CTH). The process of importation and exportation is monitored through valuation, tariff, certification (source and authenticity) and facilities instituted by Customs. The trade related payments and remittances in foreign exchange are regulated under the

[1] Report of the Working Group on 'Boosting India's manufacturing Exports' (2012-17), DoC; September 2011.
[2] Impact of the Global crisis on the diamond cutting and polishing Industry in India, UNDP, Indira Hirway.
[3] Strategic Plan DoC; Strategy for Doubling Exports in Three Years (2011-12 to 2013-14), DoC.

relevant regulations/schemes of the RBI. The financial flow based on imports and exports of G&J products, irrespective of the end use, is substantial.

This chapter analyses the trend and composition of the customs trading data, product category wise, both in value and quantities. The impact of the schemes under the FTP, FTAs and the prevalent tariff was analysed, country wise, year wise and major product category wise. The direction of trade is analysed with respect to significant trading partners. Quality of the database for valuation and efficiency of the Electronic Data Interchange (EDI) system maintained has been commented at systemic levels.

Performance of the 20:80 scheme has been audited to evaluate its efficacy while the indicators like Net Foreign Exchange Earnings (NFEE), Export Obligation (EO), Tariff etc have been analysed from the perspective of the trade and transaction. Observations have been made on SEZ/EoU, trade facilitation procedures and institutions as instruments of export growth with respect to the extant provisions of law.

2.1 Trend and composition of Imports/Export under Chapter 71 goods

Import and export performance of goods under Chapter 71 of CTH during 2010-11 to 2014-15 is tabulated in Appendix 1 to 1C. There were about 84 different items imported under this chapter and 89 items were exported. Share of value of import of rough diamond, gold, jewellery, polished diamonds and other items to that of total imports under Chapter 71 revealed that gold and rough diamond formed 75-80 per cent of the imports whereas exports comprised around 85 per cent of CPD and jewellery. There was a general increase in the share of rough diamond. Therefore the significant four category of goods viz. non currency gold, rough diamond, cut and polished diamond (CPD) and gold jewellery of the Chapter 71 trade have been analysed.

The import of gold, jewellery etc. increased from ₹ 3,50,396 crore in 2010-11 to ₹ 3,81,515 crore (9 per cent) in 2014-15. Export of similar goods also increased to ₹ 2,53,940 crore (28 per cent) in 2014-15 from ₹ 1,98,886 crore in 2010-11. In 2014-15 the share of imports of Chapter 71 goods to all imports was 13.93 percent whereas the share of its exports was 13.39 percent. While imports grew by 10.57 percent, the exports grew only by 0.7 percent over the last year. The value and quantity of goods imported and exported under the four categories revealed a generally increasing trend of export of rough diamond, gold and an increasing trend of imports of jewellery over its exports.

In the last five years, similar to the total Chapter 71 imports, the rate of growth of the value of gold imports as well as value of gold, jewellery and

CPD exports was irregular, whereas, rate of growth of both imports and exports of rough diamonds declined.

Trade deficit has decreased from 43 per cent (FY 11) to 34 per cent (FY 15) but the duties foregone have increased from 14 per cent (FY 11) to 20 per cent (FY 15) of the value of imports.

During this period, value of the US Dollar increased by 34 percent making the imports proportionately expensive and exports cheaper. The entire five year period saw, imports of gold as a major component of the imports under the chapter 71 but it suffered a negative NFEE vis a vis corresponding exports of jewellery. International gold prices reached its peak in 2012 and steadily declined by 2015. Evidently, in 2013-14 rough diamonds formed the dominant category of the Chapter 71 imports and CPD formed the majority of the exports with a positive NFEE between these two categories. The value addition in this category of goods was however, far better during the previous period 2010-2013. Import, re-import and export of CPD through PCCCC, Mumbai alone had increased manifolds. Re-import of CPD to total import grew from 27 to 79 per cent and re-import of CPD to exports increased from 10 to 29 per cent in the last five years.

India barely produced diamond or gold. It was the highest average importer of gold in the last five years. There was a sharp increase in the share of import of gold after 2007-08 because of its rise in its asset demand[4]. Interestingly, in 2013-14 the export of rough diamond and non monetary form of gold was also at maximum levels of 10.10 and 11.04 percentages, respectively. Correspondingly, seizures of like items increased from Rs 22.11 crore in 2010-11 (0.006 per cent of value of imports) to Rs 1,419.22 in 2014-15 (0.37% of value of imports). There was a quantum jump in the value of seized Chapter 71 goods from Rs 156.61 crore in 2012-13 to Rs 950.16 crore in 2013-14. The duty evasion cases detected by DRI under different schemes also increased between 2010-11 to 2014-15.

The export growth (0.7 per cent in 2014-15) was much below the rate envisaged in the DoC strategy affecting employment generation and other economic indicators. Mid-Term review of DoC's strategy indicated downward revision of the export targets almost by 30 percent (2013-14) owing to both global and domestic conditions. FTP 2015-20 acknowledged the suboptimal performance of the sector and highlighted[5] better use of information technology infrastructure in trade transactions; input based

[4] RBI (2013): 'Report of the Working group to study the Issues Related to Gold Imports and Gold Loans by NBFCs' Reserve Bank of India New Delhi.
[5] FTP 2015-20 highlights.

indirect tax remission for export price competitiveness and augmenting production and labour efficiency.

Direction of Trade

The major sources for rough diamonds were Russia, Canada, Botswana, Angola, Namibia, South Africa, Australia DRC and Zimbabwe. Coloured gemstone was available from Tanzania, Myanmar, Thailand, Srilanka, Namibia, Columbia and Brazil. The major existing market hubs were Hongkong, UAE and Singapore.

Export-import data of DoC in respect of import of gold jewellery from Singapore, Malaysia, Indonesia, Hongkong, Thailand and UAE during 2010-11 to 2014-15 as mentioned in Appendix 2A revealed that there was a surge in import of gold jewellery from Asian Countries during the year 2013-14 and 2014-15 when 20:80 scheme was in operation, since import of gold bar was restricted for normal importers during the above period (Appendix 4 and 6). UAE's diamond trade slumped after 2011, post imposition of the 2 per cent customs duty (January 2012) when gold and gold jewellery received a boost[6].

Top seven source countries and destination countries of goods of Chapter 71 during 2010-11 to 2014-15 have been included in Appendix 2B and 2C respectively.

It has been observed that on an average 64 per cent of imported gold jewellery were from Switzerland, UAE and Hong Kong out of the 120 odd source countries. However, the importing countries were not being exported to, except in case of UAE and Hong Kong. Similarly, 63 per cent exports of jewellery were to UAE and Hong Kong. Analyse of the trade of four main goods category of Chapter 71 with UAE in 2014-15 reveals that 15 percent (of the total like goods imported) were imported from UAE and 29 percent of the total like goods were exported to UAE. The country trade analysis further indicates repeated transactions between each of the four categories of products under Chapter 71; cases of related party transactions, inverted duty structure and re-export which have been mentioned in the following paragraphs. Evidently, trade with UAE involving re-export did not create major economic activity while inflating the total value of the trade. It necessitated a detailed examination to distinguish imports and exports tied to the real economy through value addition and creation of economic growth, rather than from the re-exports simply passing through the trade accounting and bank financing channels.

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[6] idexonline.com, International Diamond Exchange; Thomson Reuter (2013) Gold Survey 2013 Update.

No analysis of the incremental changes in the transaction cost associated with the sector was measured by DoC. The change in gold price, import regulation, export promotion schemes did not have a material impact on the gold trade. In FTP 2015-20, DoC did not make any defining provision for the G&J sector different from the earlier FTPs despite its climb down in the mid-term review of the departmental strategy and withdrawal of 20:80 scheme. The G&J trade related financial outflow continued unabated.

CBEC in their reply (December 2015) stated that in the 2003 circular, there is no ban on import of jewellery and no country restriction. Jewellery is covered under the FTA.

Department's reply is not satisfactory since it had not analysed the potential impact of the 20:80 scheme before implementing it nor its outcome after withdrawing it in a year's time, in terms of imports, exports, revenue or CAD, especially with respect to specific source and destination countries. The lessons learnt from this scheme could have been useful for development of similar promotional schemes in future.

Recommendation No. 1*: Department of Commerce should undertake an outcome analysis of the important schemes implemented to boost the gems and jewellery sector from an economic, trading and revenue perspective. All inverted duty structures, transaction costs, related party transactions, re-export transactions, facilitation measures need to be carefully reviewed before designing an effective promotional scheme.*

2.2 Analysis of Database of imported and exported goods

The DGoV, Mumbai was established in the year 1997 to assist the Board in policy matters concerning valuation. To carry out this task, the DGoV had to develop a comprehensive real time electronic database of imported and exported goods.

The Expert Committee on Gems and Jewellery had expressed concern over the absence of reliable turnover statistics in this sector and had opined that the domestic trade was grossly under-estimated to avoid both sales tax and income tax and had recommended sharing of the trading data with other tax authorities to detect instances of tax evasion. Given the multiple uses of the database, completeness of data was a prerequisite for doing any reliable analysis.

Audit observed that the import/export data was incomplete and could not be used as the base data for any realistic analysis. Undervaluation and overvaluation of imports and exports of high unit value products are also liable to be used for financial outflows from the country due to trade mis-invoicing. The DGoV database management system was not fully functional

(C&AG's Report No. 8 of 2015) and it was not integrated with the EDI system of Customs department or DGFT. The value of imports and exports for the total transactions captured in the DGoV database for Chapter 71 did not match with the trade figures reported by Commissionerate of Customs in Mumbai (Appendix 3). DGoV had noticed some transactions of undervaluation and overvaluation, however 'no valuation Alert/Guidelines was issued.

Data of the DGoV and the respective Commissionerates revealed that the data captured by National Import Database (NIDB)/Export Commodity Database (ECDB) was not complete. The variation in the export data ranged from 1.33 to 81 times the actual data provided by different Commissionerates for the period 2010-11 to 2013-14, similar variation was also observed on the import side. However, the import and export data pertaining to the PCCCC was not being captured in the database of DGoV, and import data of Gold Dore Bars are manually processed in PCCCC.

The difference between the transaction wise valuation of trade between India and its exporting/importing partners, indicated[7] that India ranks 4th in volume of illicit financial outflows in the world. This was almost $83 billion USD in 2013 and growing akin to the last ten years trend. It is around 4.5 per cent of India's GDP (against global average of 4 per cent) and totally comprises of outflows due to trade mis-invoicing.

CBEC in their reply (December 2015) stated that DGoV data is regularly updated and CBEC is willing to share the DGoV data on request basis.

Reply of CBEC is not acceptable because during the audit it was observed that DGoV data was neither fully functional nor regularly updated. There is no existing mechanism/protocol of sharing of the data with other Government agencies.

Recommendation No. 2*: CBEC should maintain a robust and updated valuation data for all the tariff lines so that these could be utilised and shared with other concerned departments.*

2.3 20:80 Scheme

To control the deteriorating Current Account Deficit (CAD) during 2012-13 gold import was identified by DGFT, DoC as an important constituent. RBI in consultation with Government of India introduced 20:80 scheme. Vide the circular dated 22 July 2013 RBI imposed certain restrictions on import of gold and gold dore bar in to the country with a view to decrease the import of

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[7] Global illicit Financial Flows Report: 2015; Global Financial Integrity; www.gfintegrity.org

gold and consequential outflow of foreign exchange and prescribed certain conditions to be followed by the authorized importers.

DGFT considered gems and jewellery sector as one of the largest exporting sector in India and to promote export of gold and jewellery and earn foreign exchange RBI vide circular dated 14 August 2013 prescribed revised guidelines for import of gold. It required all the nominated banks/agencies to ensure Export Obligation of 20 per cent of every lot of gold imported and the balance 80 per cent was to be used for domestic purpose. They were permitted to import 1st consignment of gold on the basis of their past imports. After exporting 20 per cent of imported quantity they again became eligible to import the 2nd lot of gold by submitting proof of exports, and so on.

For border control measures, CBEC vide circular dated 4 September 2013, notified guidelines to be followed by the Customs Department and importers of gold.

Vide circular dated 14 February 2014 RBI restricted the import of gold after the 2nd lot to be limited to lesser of the two quantities of, five times of export for which proof had been submitted, OR quantity of Gold permitted to a Nominated Agency in the first or second lot.

The Star Trading Houses/Premier Trading Houses (STH/PTH) were allowed to import gold for export purpose only and were kept outside the purview of the scheme. However, based on a modification proposed by Department of Economic Affairs (DEA), RBI vide circular dated 21 May 2014 allowed STH/PTH to import gold under the scheme. They were to be registered as nominated agencies by the Director General of Foreign Trade (DGFT)

The scheme was withdrawn by RBI vide circular dated 28 November 2014.

(A) Import of gold jewellery under 20:80 Scheme

In terms of RBI's circular dated 14 August 2013, Gold in any form/purity including Gold Dore was allowed to be imported under 20:80 scheme. However, RBI vide circular dated 1 July 2014 disallowed import of gold in the form of jewellery/Mountings, etc. from the purview of 20:80 scheme.

An analysis of all India data on Gold Jewellery import received from DG (System), revealed that the import of gold jewellery surged substantially during the period of 20:80 scheme. The average monthly jewellery import during the period of 20:80 scheme (i.e. 14 August 2013 to 27 November 2014) had risen to ₹ 425.05 crore from the average monthly jewellery import of ₹ 25.48 crore when 20:80 scheme was not operational as shown in

Appendix 4. Again average import of gold jewellery had significantly come down after withdrawal of the 20:80 scheme.

In our opinion allowing import of Gold jewellery without any limit during the 20:80 scheme period affected the domestic Gold jewellery industry which employed a large number of workers.

CBEC in their reply (December 2015) stated that, Customs did not allow the import of jewellery after the issuance of the RBI Circular dated 1 July 2014.

Department's reply is not acceptable as allowing import of gold jewellery without any limit during the 20:80 scheme period and RBI's clarification dated 01 July 2014 thereafter defeated the objective of minimizing CAD intended in 20:80 scheme as a result of the sudden surge in import of gold jewellery during the currency of the 20:80 scheme. Further this was also against the interest of domestic jewellery industry which employed millions of artisans.

(B) Irregular permission to import gold under 20:80 scheme

In terms of RBI circular dated 14 August 2013, the nominated banks/agencies/refineries and other entities not having a previous record of having supplied gold to the exporters needed to seek prior approval from RBI before placing orders for import of gold for the first lot under the 20:80 scheme.

Audit scrutiny revealed that M/s Diamond India Ltd (DIL) had not supplied any gold to exporters in the financial year 2010-11 to 2012-13 thus it was not entitled to import gold under 20:80 scheme. However, DGFT, New Delhi granted permission to DIL to import 100 kg gold bars, each at Mumbai, Ahmedabad, Chennai, Hyderabad, Delhi, Kolkata, Bangalore and Kochi locations for first two lots, under the 20:80 scheme in contravention of the RBI circular dated 14 August 2013.

DIL had imported 700 kg of gold bars (Assessable value ₹ 178.82 crore) in Mumbai. The details of quantity of gold actually imported at Ahmedabad, Chennai, Hyderabad, Delhi, Kolkata, Bangalore and Kochi locations during the 20:80 period (14.08.2013 to 27.11.2014) by DIL have not been furnished by the department.

In our opinion, allowing DIL to import gold bars under 20:80 scheme by DGFT was irregular. Imports, exports and DTA sale of the imported gold may be investigated and remedial action under FTDR Act may be taken under intimation to audit.

DGFT in their reply (December 2015) stated that the permission to DIL for import of only 600 Kgs was given with approval of the competent authority

on the basis of their entitlement as per RBI circular dated 14 August 2013 and as per criteria laid down in the circular. Further, the permission was not utilised by M/s DIL as Govt had withdrawn all restrictions on import of gold vide RBI Circular dated 28 November 2014.

Documentary evidence may be produced to audit for verification.

(C) Anomaly in different sets of guidelines issued by RBI under 20:80 scheme

RBI's circular dated 22 July 2013 imposed certain restrictions on import of gold and gold Dore bar into the country with a view to control CAD by decreasing the import of gold and consequential outflow of foreign currency and prescribed certain conditions to be followed by the authorized importers. RBI's circular dated 14 August 2013 revised the guidelines for import of gold. In this circular STPs/PTHs were kept outside the purview of 20:80 scheme and were allowed to import gold for export purpose only. Later on RBI in consultation with Govt. of India allowed STHs/PTHs to import gold under 20:80 scheme in 21 May 2014 after taking into account views of DGFT, RBI, DRI and PTHs/STHs. However, concurrence of DoR/CBEC was not sought though DoR had strong reservations on allowing STHs/PTHs to import gold at the time of earlier RBI circular issued on 14 August 2013. Audit is of the opinion that the views of DoR were important as the gold policy affected the tax administration of the Government. GJEPC, one of the Apex body for promotion of gems and jewellery exports was also opposed to the idea of allowing STHs/PTHs to import and sell gold in domestic area.

It can be seen that while the import entitlement of PTHs/STHs were based on highest quantity imported by them in last 24 months prior to introduction of 20:80 scheme whereas, the import entitlements of banks/nominated agencies were determined by exports during previous years. Analysis of the scheme revealed that there was built in discrimination in the scheme in favour of STH/PTHs.

Audit observed that extending the 20:80 scheme to PTH/STH had resulted in spurt in import of gold during June 2014 to November 2014 which negated the objective of 20:80 scheme to reduce the CAD. Average monthly gold import increased by 2.74 times. Further analysis of imports by trading houses revealed that the major trading houses took advantage of the notification and imported in huge quantities after the relaxation was brought in by RBI (Appendix 5).

It can be observed that imports of PTHs/STHs shot up by more than three times during the comparable period. Total gold imports during June 2014 to November 2014 was 533 MTS, out of that 282.77 MTS i.e. approximately 53

percent of total gold imports were by 13 trading houses. Further, top seven trading houses accounted for approximately 50 percent of total gold imported during 20:80 period. Thus, allowing PTH/STH to import gold under the scheme allowed benefits to be cornered by a few business houses.

Audit scrutiny of the records of selected PTHs/STHs showed that PTHs/STHs mostly exported plain gold jewellery, bangles or medallions with negligible or no value addition. Even cases of export of 24 carats gold jewellery were noticed. In many cases plain jewellery were exported within same day or within 1 to 3 days of receipt of gold. Exports were also made to related parties. Some of the remittances were being received the very next day. Possibility of exporting products without even nominal value addition as plain jewellery by these agencies could not be ruled out. These importers were importing high quantities of gold by repeated exports at very short intervals, so as to maximise their domestic sale entitlement against 80 percent component of 20:80 scheme. DRI had also observed that the export obligation was mostly met by exporting machine made plain jewellery viz. bangles and chains which are re-melted abroad and cast into primary bars for the purpose of re-import.

Analysis of export data furnished by DG (Systems), New Delhi (Appendix 6) revealed that average monthly export of plain gold jewellery increased 3.5 times after relaxation was brought under the 20:80 scheme. However, internal analysis by the Department showed that the export of plain gold jewellery had actually surged by more than 10 times after the relaxation.

Further, STHs/PTHs with the status of exporters imported huge quantity of gold without any cap and supplied it in the domestic market contributing to the anomalous situation.

Reply of the department is awaited (January 2016).

(D) Inclusion of new refiners under 20:80 scheme without notification

RBI circular dated 14 February 2014 stipulated that DGFT through a notification, could include new refiners, and fix licence quantity for them.

Audit scrutiny of the records of at DGFT, New Delhi, revealed that seven[8] refiners had applied for Import Authorisations to import gold dore bars for the first time. On file approval for Import Authorisations for total quantity of 13.8 MT to these seven refiners were accorded by DGFT on 07.03.2014. These new refiners were issued Import Authorisations and brought under

[8] M/s Bhandari Gold and Jewellers Pvt. Ltd., Shree Surya Refinery, Uttarakhand, Multivision, Mumbai, Parekh Industries Ltd., Mumbai, Rajesh Exports Ltd., Bangalore, Diamond Forever International, Mumbai and Chemmanur Gold Refinery Ltd., Cochin.

20:80 scheme by virtue of the approval of DGFT. However, no notification was issued by the Government to include these refineries under 20:80 scheme. This contravened the procedure prescribed by RBI in its circular dated 14 February 2014.

DGFT in their reply (December 2015) admitted that in there is no procedure/practice in DGFT for notifying list of refineries as every time a new refinery applies for licence/authorisation the quantity to be allowed from time to time would vary which cannot be pre-determined. Further, they stated that refineries are different from Nominated Agencies as refiner has to fulfil the condition of actual user and therefore furnish the details of utilization of gold dore to excise authorities and customs authorities about the quantity of gold extracted. Hence it was felt appropriate that licence/authorisation for import of gold dore was granted case to case as per the refining capacity instead of issuing notification and adding names of the refineries to the list subsequently.

Reply of DGFT is not acceptable because by not notifying the refineries in advance, other agencies like CBEC, GJEPC, RBI etc were kept out of the loop.

(E) Irregular exports fulfilling under 20:80 scheme

As per Board's circular dated 4 September 2013 read with RBI's circular dated 14 August 2013 for every consignment of gold imported, at least 20 percent quantity was to be supplied to the exporters only.

Further HBP stipulated that the exporters had to furnish export promotion (EP) copy of the SB along with other documents in support of proof of export of gold jewellery and such exporters were required to export the jewellery made there from within 90 days.

(i) In Air Cargo Complex, Mumbai, M/s Diamond India Ltd, Mumbai imported 100 kg of gold in 7th lot (October 2014) under 20:80 scheme. Out of 30 kg of gold supplied to exporters, export fulfilment against 18 kg of gold was shown prior to issue of gold.

Similar observation was also noticed in the case of The Bank of Nova Scotia, Mumbai, where it imported 3000 kg of gold (August 2014) under 20:80 scheme. Out of this, 10 kg of gold was issued to exporter in September 2014. The export fulfillment against this gold was shown prior to issue of gold.

Above export fulfilling prior to receipt of gold was not in order and thus the importer was liable to pay duty of ₹ 72.87 lakh in both the cases.

CBEC in their reply (December 2015) stated that (i) in case of DIL, delivery of gold was made to M/s Bhindi Manufacturers on 17 October 2014 and not on 20 October 2014 as pointed by Audit and the same was reflected in SB dated

17 October 2014. Thus the export has not taken place prior to receipt of gold. (ii) in the case of M/s Nova Scotia Bank, appropriate reply will be sent on the basis of verification and action taken.

CBEC's reply regarding date of supply to M/s Bhindi Manufacturers on 17 October 2014 is not acceptable, as evident from the register maintained in Bond section at ACC, Mumbai, indicated that gold was supplied on 20 October 2014. Even if it is assumed that the gold was supplied on 17 October 2014, the export on the same date is doubtful as manufacturing of gold jewellery involves a number of processes. This needs detailed examination. Detailed reply in respect of M/s Nova Scotia Bank may also be furnished.

(ii) Similar observation was noticed in the case of M/s. MMTC Limited under Cochin Air Customs Commissionerate with a duty impact of Rs 18.46 lakh along with interest.

CBEC in their reply (December 2015) stated that M/s. MMTC Limited had been granted extension by proper officer in terms of notification dated 08 May 2000 and the goods had been re-exported and no duty liability was involved on the goods in terms of the notification.

Reply is not acceptable as according to HBP no extension for fulfilment of export obligation was to be allowed.

(iii) Scrutiny of records of two Nominated Agencies (NA) IndusInd Bank and Axis Bank in Kolkata revealed that EP copies of SBs of exports (IndusInd Bank - 16 SBs and Axis Bank -15 SBs) were not available with them. In absence of these EP copies of SBs as proof of exports, proportionate import duty amounting to ₹ 9.40 crore stood recoverable from the NAs concerned.

Subsequently, Axis Bank Ltd. vide their reply (17.08.2015) submitted only 03 nos. of EP copy of SBs and expressed their inability to submit the remaining EP copy of SBs.

Final outcome may be intimated to audit.

(iv) Board circular dated 4 September 2013 stipulated that import of gold Dore Bars from the third consignment onwards was to be allowed only up to 5 times of the quantity for which the proof of export had been submitted by importer and this was to be on accrual basis.

M/s Kundan Care Products Ltd had made first export of 26 Kg of Plain gold jewellery on 28 November 2013 against the import of 210.70 kg Gold Dore Bars on 12 November 2013. Further, the unit imported of 26.87 Kg and 76.80 Kg gold Dore Bars on 20 January 2014 and 21 January 2014 respectively without fulfilling the export obligation against earlier imports.

Thus, permission to the unit for imports for the consignment of 103.67 Kg without fulfilling the export obligations was irregular and the unit was liable to penalty under Foreign Exchange Management Act, 1999 (FEMA).

CBEC in their reply (December 2015) stated that it appeared that M/s Kundan Care Products Ltd., Haridwar has imported the consignment of 103.667 Kg of Gold Dore Bar after fulfilment of the export obligation of earlier imports.

The reply is not relevant because audit raised the observation regarding allowing the importer to import third consignment without furnishing the export proof for earlier imports. Ministry may provide a specific reply.

(v) Assistant Commissioner Customs & Central Excise Division, Rampur issued the permission in October 2013 to M/s Sri Sai Vishwas Polymers for import of Gold Dore Bars and manufacturing of gold/silver bars and coins.

Audit observed that the unit imported 29.12 kg gold Dore bars having assessable value of Rs7.08 crore during the period June 2014 to August 2014 and exported 7.51 Kg plain gold jewellery having assessable value of ₹ 1.77 crore, for which the permission for manufacturing of gold jewellery was not obtained from the Customs & Central Excise Department. Accordingly, the unit was liable for penalty under FTDR Act and FEMA.

Reply of the department is awaited (January 2016).

(F) Inconsistency in circulars issued by RBI, SEZ and DGFT for granting status Certificate and Nominated Agency Certificate to STH and PTHs

Merchant as well as Manufacturer Exporters, service providers, units located in EoUs, SEZs, EHTPs, STPs, BTPs and Agri-Export Zones were to be eligible for status of STH/PTH. Further, as per FTP (2009-14) Status recognition depended upon EP. Minimum prescribed EP for a status of STH and for PTH House was ₹ 2,500 crore and ₹ 7,500 crore respectively. The export performance was to be counted on the basis of FOB value of export proceeds realized during current plus previous three years (taken together).

RBI circular dated 14 February 2014 excluded any import under Advance Authorisation (AA)/Duty Free Import Authorisation (DFIA) from the purview of 20:80 scheme. However, RBI on 21 May 2014 allowed STH/PTH to import gold under 20:80 scheme. Further, in order to streamline regulatory mechanism for the SEZ units dealing in gold/gold medallions DoC decided (dated 25 April 2013) that no DTA transactions was to be permitted for SEZ units transacting in gold. The SEZ units were not permitted to trade in gold even for export activity.

Audit observed that three trading houses discussed below had achieved the required minimum turnover for getting star/premier trading house certificate

either through exports from SEZ units or against the exports under DFIA licence. Since SEZ units are not permitted to import gold for trading in DTA in terms of DoC's decision dated 25 April 2013, the PTH/STHs status earned through exports from SEZ should not have been allowed to import gold for supplying to DTA and their imports should have been restricted for use within SEZ.

However, neither RBI circular dated 21 May 2014 nor DoC had brought any amendments to SEZ/EoU rules/provisions to this effect. Further as per RBI clarification dated 14 February 2014 exports under DFIA was not entitled for determining eligibility to further import under 20:80 scheme. However, past exports made under DFIA were not excluded for granting status and nominated agency certificate.

Audit observed that trading houses had taken advantage of the inconsistency in circulars issued by different departments and got their status either by clubbing exports from SEZs or by exports under DFIA. As a result they became eligible for import of gold under 20:80 scheme and sold substantial quantity in domestic area. Few illustrative cases are narrated below:

Documentary evidence may be produced to audit for verification.

(i) M/s Edelweiss Commodities Services Ltd (formally M/s Edelweiss Trading & holdings limited) while applying for STH declared their export turnover of ₹ 2,537.17 crore. Audit scrutiny revealed that export worth ₹ 2,479.75 crore was through Manikanchan SEZ, Kolkata and only ₹ 57.42 crore was through units other than SEZ. Therefore, the status allotted as a Star Trading House and as a nominated agency to the exporter was not in order. This resulted in import of gold bars to the tune of 19,000 kg (₹ 4,699 crore) during 20:80 scheme out of which 15200 kgs of gold bar was consumed for domestic use.

Further, it was also observed that erstwhile company M/s Edelweiss Trading & holdings limited (IEC No. 0909004790) had applied for status certificate and status certificate were issued on 06 September 2011 and certificate was subsequently amended in favour of M/s Edelweiss Commodities Services Ltd (IEC No. 0307050521). It is pertinent to mention that FTP 2009-14 does not allow the transfer of status certificate to another entity holding a different IEC as the Star Trading Certificate was issued to the exporters for his own export performance.

Further, it was noticed by audit that the same export turnover of the year 2010-11 (₹ 406.41 crore) and 2011-12 (₹ 2,130.76 crore) had been claimed by both the companies i.e. M/s Edelweiss Trading & holdings limited and M/s Edelweiss Commodities Services Ltd and both of which were certified by the

same Chartered Accountant. In any circumstances, one export performance could not be claimed by two companies accordingly, the certificate of the Chartered Accountant was not in order. A mechanism to verify the details certified by the exporter as well as the CA was not available with DGFT.

DGFT in their reply (December 2015) stated that In this regard, it is stated that the name of the new entity was endorsed on the status certificate in pursuance of the order of the Hon'ble High Court of Andhra Pradesh on account of transfer of assets/liability by virtue of amalgamation/merger.

Reply of DGFT was not addressing the issue of not having a mechanism to verify the details certified by the exporter as well as the CA.

(ii) M/s Shree Ganesh Jewellery House(I) Ltd, applied for PTH on 26 May, 2014 on the basis of declared export turnover of ₹ 19,754.74 crore during April 2011 upto April 2014. The Status was granted by Additional, DGFT, Kolkata on 6 June, 2014. Audit scrutiny revealed that out of total export turnover of Rs 19,754.74 crore shown, Rs 17981.23 crore was through its SEZ units. Thus the status holder certificate granted in contravention of DoC's decision dated 25 April 2013 was not in order, this resulted in unintended benefit to the exporter and consequent import of gold bars of 400 kgs (₹ 98.75 crore) by them under 20:80 scheme out of which 320 kgs were supplied in domestic area.

In terms of the FTDR Act, 1992, the above units were liable for penalty. Penalty was also leviable under Section 112 of Customs Act, 1962.

Reply of the department is awaited (January 2016).

(G) No norms for fulfilling Export obligation without any value addition in terms of purity

Under the 20:80 scheme, M/s. Rajesh Exports Pvt. Ltd, imported 68,500 Kgs of gold from Switzerland and United Arab Emirates and exported 13,700 Kgs of medallions and bangles to United Arab Emirates fulfilling the 20 percent export criteria.

Audit observed that the export obligation was made by exporting medallions and bangles of 24 carat purity. This indicates that the imported gold (24 carat purity) was exported in 24 carat purity medallions and bangles without substantial value addition to the exported products. The Goods imported in bars were merely converted to medallions or other articles of gold of same purity (24 carat) and exported so as to meet export obligation. The risk of round tripping of imports/exports of gold bars in absence of a value addition provision could not be ruled out.

In our opinion, to achieve desired results of export promotion schemes, the scheme should have included specific minimum value addition criteria instead of regular value addition prescribed in FTP to mitigate the risk of round tripping.

(H) Irregular allowance of exemption

20:80 scheme was withdrawn from 28 November 2014.

Scrutiny of records of M/s. Rajesh Exports revealed that the unit imported 500 Kgs of gold having assessable value of ₹ 121.44 crore vide BE dated 28 November 2014 and warehoused. The unit filed two ex-bond bill of entry on 2 December 2014 for home consumption for 100 KGs and 400 KGs of Gold respectively under 20:80 scheme. The unit paid duty of ₹ 10 crore on 400 kgs gold and availed exemption of ₹ 2.50 crore for 100 kgs of gold under the scheme, which is irregular since, the 20:80 scheme was withdrawn with immediate effect from 28 November 2014.

Similar irregularity was also noticed in the case of M/s. Reliance Industries Ltd who cleared 10 Kgs of warehoused gold having assessable value of ₹ 2.49 crore vide Ex-BE dated 22 January 2015 and claimed duty exemption of ₹ 73 lakh.

The exempted duty of ₹ 3.23 crore along with interest of ₹ 27 lakh stands recoverable from the importers.

Reply of the department is awaited (January 2016).

(I) Cancellation of bonds without obtaining bank realisation certificates (BRCs)

According to Board circular dated 4 September 2013, proof of export was to be furnished by the exporter for having exported the jewellery made from the duty free gold released to them within the period prescribed in the FTP. The instructions contained that the realisation of payments related to those exports should be submitted to the Customs officer.

According to HBP Vol, export against supply by Nominated Agencies was to be effected within a maximum period of 90 days from the date of outright purchase/release of gold on loan basis of precious metal.

Similarly, in terms of notification dated 8 May.2000, as amended, Gold falling under CTH 7106 was exempted from whole of customs duty under the scheme of 'Export Against Supply by Nominated Agencies' subject to certain condition.

Seven nominated Agencies imported 54 consignments of Gold bars (995 purity) through Chennai Air and Coimbatore Air Customs, during the period the 20:80 Scheme was in operation and supplied 20 percent or more of the

quantity to exporters involved in manufacture and export of Gold Jewellery. The nominated agencies submitted only the copy of the shipping bills as proof of exports for shipments made. However the Bank certificates of realization was not insisted upon by the authorities.

Similarly, M/s Bank of Nova Scotia imported 40 consignments of Gold bars (995 purity) during the period 2010-11 to 2012-13 (till August 2013) through Coimbatore Air Customs and supplied it to exporters of Gold Jewellery. However BRC was not submitted by the exporters.

Department's action in considering the export obligation as fulfilled and cancelling the Bonds without insisting on the BRC from the concerned exporters was not in order as one of the important purposes of exemption was to realize foreign exchange to meet the balance of payments position.

CBEC in their reply (December 2015) stated that importing banks have been asked to furnish BRCs for the SBs furnished as 'proof of exports' by them and the same is being monitored.

Final outcome may be intimated to audit.

2.4 Net Foreign Exchange Earnings (NFEE)

(A) Non Inclusion of the value of procurement made from DTA on payment of foreign exchange in calculation of NFE

As per SEZ Rule, 2006, supply of goods to DTA by SEZ units made against payment in foreign currency has been considered as export for SEZ for NFE calculation. However, no provision exists in SEZ rules to treat procurements made by SEZ from DTA on payment in foreign currency as import for purpose of NFE calculation.

Audit observed that four units under DC, SurSEZ, Surat, procured goods worth ₹ 2,292.03 crore from DTA against payment made in foreign exchange. In absence of the provision for inclusion of the same outflow of FE, the NFE arrived at for these units, in our opinion does not give the correct picture of transactions made in foreign currency.

Reply of the department is awaited (January 2016).

(B) High cost of earning foreign exchange under Advance Authorization Scheme

Scrutiny of records of Advance authorization/DFIA licenses issued to three importers under CLA, Delhi, for import of gold bar of purity 99.5 percent and silver bar of fineness 0.999 issued during 2010-11 to 2014-15 revealed that in five cases, on comparison of duty foregone on import of gold bar/silver bar with respect to Net Foreign Exchange (NFE) earned by the exporter, it was observed that to support earning of 1US$ by the exporter, government had

borne expenditure in the form of duty foregone in the range of ₹ 56.67 to ₹ 221.75 (Appendix 7) which was higher than the exchange rate of US$ in the open market during the period. The primary reason for the difference between earning of Net Foreign Exchange and duty foregone by the Government was the fact that minimum value addition required to be done by the jewellery exporter according to HBP ranged between 1.5 to 5 percent whereas the duty foregone/exempted when the gold bar was imported was 10 per cent. As such, the Department was foregoing more revenue amount than what was being earned through foreign exchange earnings.

DGFT in their reply (December 2015) stated that the primary objective for allowing Advance Authorisations against the export of a product was to allow duty free import of inputs (after allowing wastage admissible for the inputs) so that these inputs are used by the exporter and the export product is exported within a specified time after using the inputs. In case the exporter fails to export full quantity, he becomes liable to pay customs duty and interest on the inputs remaining with him. Further, the wastage which were allowed in 2009-14 FTP have been reduced in the new FTP and minimum VA have been increased for some of the export products. However while deciding on the Value addition; one of the points which emerged was that if very high value addition norms are prescribed then exports from India will be adversely impacted as the exporters from India have to compete with exporters from other countries. Hence, Value additions were decided keeping this aspect in view.

Reply of the department is not acceptable since duty foregone on import under advance authorisation or in any export incentive schemes is allowed to boost the export of the country and realising sufficient FE for the country. When NFE realised is less than the duty forgone, it has a direct impact on the fiscal management. Very low value addition did not help in generating economic activity in the sector and induced inflated trade data, opening up the window for round tripping.

Recommendation No. 3: *CBEC may consider rationalising the duty structure so that Foreign Exchange Earning could at least be at par with duty foregone under the FTP.*

2.5 Customs EDI System

(A) Non-Implementation of ICES 1.5

(i) Indian Customs Electronic Data Interchange System (ICES) captures details of imports and exports in all Commissisonerates. It was introduced to speed up assessments, improve transparency and to act as a repository of data.

Audit observed that although the Precious Cargo Customs Clearance Centre (PCCCC) had a dedicated server, the entire data relating to customs clearance for exports is still kept manually. Transactions relating to imports were integrated with EDI (ICES 1.5) on 28 November 2013.

Since bulk of the imports and exports transaction of the country is handled by the PCCCC, therefore and not capturing the data in EDI system resulted in escaping the scrutiny of the Risk Management System (RMS) and Post Compliance Audit (PCA) introduced by the department for examination of the high risk cargo. In our opinion, the delay in integrating export transactions with EDI has increased the risk of tax evasion and undervaluation/overvaluation which were sought to be reduced by the introduction of ICES 1.5.

Further, imports made with corresponding export obligations under various export incentive schemes of government remain largely unmonitored as the export data are not captured by the system.

Audit also observed that all the transaction relating to import of Gold Dore Bars are done manually since there is no facility to generate Bills of Entry and debit respective licenses in the EDI system therefore the control mechanism envisaged through RMS, PCA, Special Valuation Branch (SVB), DRI and other authorities are not being exercised. DGFT was also not able to track the imports against various export promotion schemes licenses through their system since DGFT EDI system is not connected with the customs system.

Similarly, EDI facility at Surat Hira Bourse is yet to be enabled by the Customs Authority. Further, audit observed that in absence of the EDI facility, the register is the sole record for maintaining the details of imports/ exports based on which various internal reports are prepared were not being authenticated by any Customs authority providing hardly any assurance on the report returns prepared.

In Air Cargo Complex, Indore, even after installation of EDI system, ICES 1.5 system was not operational.

CBEC in their reply (December 2015) stated that ICES 1.5 has already been implemented since November 2013 in import and since 2015 in exports with facility to process Precious cargo including Gold Dore Bars and several sites are using the Systems.

Department's reply is not tenable since ICES 1.5 for export at PCCCC is still under implementation as EP copy is not generated through the system which has been accepted by the DG System. Regarding 100 per cent examination of import and export at PCCCC, department has not issued any circular to that

effect neither any instruction through system is given for compulsory examination. In PCCCC, gold dore bar is still processed manually.

(ii) In terms of HBP, during export of plain/studded jewellery, SBs and invoice presented to customs authorities were to contain description of item, its purity, weight of gold/silver/platinum content, wastage claimed thereon, total weight of gold/silver/platinum content plus wastage claimed and its equivalent quantity in terms of 0.995/0.999 fineness for gold/silver and in terms of 0.9999 fineness for platinum and its value, value of precious/ semi-precious stones/diamonds/pearls used in manufacture and weight /value of any other precious metal used for alloying gold/silver, FOB value of exports and value addition achieved.

Audit observed that all SBs in respect of export of plain/studded jewellery are filed manually in Chennai and Coimbatore Air Commissionerate. Moreover, SBs for gold Jewellery exported by hand carriage in substantial numbers are also filed manually.

Being a high value item, department may initiate necessary steps to extend ICES 1.5 system to accommodate the SBs for export of Gold Jewellery through hand carriage so that manual filing of shipping bills are avoided to control the risks associated with such transactions.

CBEC in their reply (December 2015) stated that ICES development is being done by taking into account common requirement of all field formations. Accordingly, BEs and SBs etc. are standardised to avoid needless entry of data. Incorporation of Additional data in standardised formats needs careful considerations and development of additional modules to link such data to processing of documents. Further, many EDI sites including ACC Delhi is processing such export on ICES. CBEC also stated that Board may consider defining an alternate proof of export (which is conducive to automation) for such consignments.

Final outcome may be intimated to audit.

(B) Delay in revision of rates in ICES 1.5 systems

The Board from time to time notifies the change in Tariff value, duty rates and currency exchange rate to be adopted by the assessing officer while assessing the import and exports made to the country or from the country.

Most of the assessment, after introduction of the EDI system in Customs is done through the system with minimum human interference. Thus, it is not only important but also necessary to effect those changes in tariff value, duty rates and exchange value rates in the system without any delay by the system manager to mitigate the risk of under/over assessment.

(i) On analysis of import data of Air Cargo Complex, Mumbai, ACC, Bangalore, Chennai Air Customs and Delhi Airport revealed that the tariff value or exchange rate or both as notified by the Board has not been updated in the ICES 1.5 system resulting in non- adoption of correct tariff value involving short levy of duty and interest of ₹ 16.82 crore for the period 2012-13 to 2014-15 on gold bars imported.

CBEC in their reply (December 2015) stated that in case of ACC, Bangalore, out of duty of ₹ 3.87 crore short paid by 17 importers, ₹ 25 lakh has been recovered from four importers (Axis Bank, MMTC, Rajesh Exports Limited and Titan Industries Limited) along with interest of ₹ 9 lakh from 3 importers. M/s Rajesh Exports Limited has been instructed to pay interest of ₹ 29,573. SCN has been issued to M/s IndusInd Bank Limited, for recovery of ₹ 0.32 crore along with interest. SCNs are in the process of being issued to the remaining 12 importers for recovery of ₹ 3.30 crore along with interest.

(ii) Through notification dated 21 January, 2013, the Board revised BCD rate on import of gold bar from 4 percent to 6 percent with effect from 21 January 2013.

Analysis of import data audit of Bangalore Air Port, Delhi Air Port and Ahmedabad Air Port revealed that nine importers cleared 1528.25 Kg of gold bars through 12 BEs (16 items) of assessable value of ₹ 457.64 crore on 21 January 2013. However, due to non updation notification directory in the ICES 1.5 system, these BEs were assessed at lower rate of duty of 4 percent instead of 6 percent resulting in short levy of duty of ₹ 9.43 crore.

CBEC in their reply (December 2015) stated that the issue of notification dated 21 January 2013 was communicated at 9.25 PM and updated on 9.45 PM on the same day. Since it was in ICES 1.0, it came into effect on 22.01.2013 at 00:00 hours. In case of ACC, Bangalore, SCN is in the process of being issued to M/s IndusInd Bank Limited for recovery of ₹ 1.23 crores short paid by them.

CBEC further, stated that Standard Operating Procedure (SOP) had been issued on 11 June 2015 for timely updation of Notification Directories. Further, to strengthen the mechanism even more, the Board has approved a new mechanism of Peer Audit.

Department's reply is not acceptable as notification the came into existence on 21 January 2013 and it should have been simultaneously updated on ICES system so that it can be implemented by field formations. Time lag between issue of notification and its updation on system may lead to revenue loss to exchequer.

(C) Computerized system for assessment of duty on commodity brought by passenger

Audit observed that duty of customs for the baggage brought in by passengers is assessed manually at SVP International Airport, Ahmedabad. Details of passengers' viz., name, duration of stay abroad, description and value of commodity, duty levied on commodity etc., are filled up manually in the Duty Debit Register (DDR) voucher after which duty assessed on the voucher is deposited in the bank and goods are handed over to passenger. No computerized system exists for assessment of duty on commodity brought by passenger.

In order to have a greater transparency, department may evolve a system wherein mentioning of certain information like value of free allowance availed and date of last departure may be made mandatory before making assessment of duty. This can be achieved if the system of assessment is computerized wherein such information may be made compulsory before assessment is processed.

Similarly, Sanganer Airport, Jaipur, also does not have any computerized system for assessment of duty on commodity brought by passenger.

CBEC in their reply (December 2015) while admitting that the computerization process at passenger terminal has not been undertaken stated that computerization of assessment procedure, the aspects has been looked into and feasibility study is being undertaken, the necessary steps would be taken on top-priority.

Final outcome of the feasibility study being taken may be intimated to audit.

Recommendation No. 4: *CBEC may expedite implementation of ICES 1.5 to all the high valued and sensitive commodities. The EDI system may be extended to import/export of gold dore bars, export of gold jewellery, hand baggage and disposals. Effective mechanism may be adopted to ensure the updating of tariff value, exchange rate and duty rate in the EDI system in a timely manner.*

2.6 Inadequate trade facilitation

(a) The regulations of Courier Imports and Exports (Clearance) Regulations, 1998, was not to apply to the imported (i) animals and parts thereof, plants and parts thereof; (ii) perishables; (iii) publications containing maps depicting incorrect boundaries of India; and (iv) precious and semi-precious stones, gold or silver in any form; requiring testing of samples thereof or reference to the relevant statutory authorities or expert before their clearance.

Audit scrutiny of the records of Foreign Post Office, Jaipur, revealed that precious and semi-precious stones, gold jewellery and silver jewellery value of ₹ 43.90 crore imported through 3970 parcels during 2010-11 to 2014-15 by units were cleared by applying regulations of Courier Imports and Exports (Clearance) Regulations, 1998 in contravention of the provisions of regulations.

CBEC in their reply (December 2015) stated that goods imported or exported by post are governed by Sections 82, 83, and 84 of the Customs Act, 1962. The procedure for clearance of goods through post is prescribed in Rules regarding Postal Parcels and letter packets from Foreign Ports In/Out of India of 1953. The Import through Foreign Post office is not covered by Courier Imports and Exports (Clearance) Regulations, 1998.

Reply is not tenable because as per regulation 2(1) of Courier Imports and Exports (Clearance) Regulations, 1998, these Regulations shall apply for assessment and clearance of goods carried by the 'Authorised Couriers' on incoming or outgoing flights or by any other mode of transport on behalf of a consignee or consignor for a commercial consideration.

(b) The Task Force Committee constituted by MoC to reduce transaction cost in their Report (January 2011) suggested various measures to reduce transactions cost and time impacting the country's Foreign Trade Transactions. Customs Circular dated 16 March 2010 mandates detailed verification of export obligation fulfilment. Further Customs Instruction dated 18 January 2011 mentioned that in cases where RLA has endorsed on the Export Obligation Discharge Certificates (EODC), customs should verify the SBs and other documents.

In Mumbai, RLA Mumbai was issuing EODC in respect of EPCG licences after verification of all the required documents and copy of the same is also forwarded directly to the Custom EPCG Cell and concerned Port of Registration for cancellation of Bond. However, the licensee have to attach all these documents again along with the original and attested copy of the EODC letter to the custom at the time of filling Bond Cancellation Application. Therefore the current process is not aligned with the suggestions of above Task Force as the recommendations of reducing the cost and time impact on foreign trades is not yet implemented.

DFGT in their reply (December 2015) stated that they are in agreement with the audit observations that EODC, once issued by RA, should be honoured by Customs without insisting on any further documentation unless there is a compelling reason to do so.

Reply of CBEC is awaited (January 2016).

(c) As per CBEC Circular dated 25th August 2006, 100 percent screening of import/export consignments (documents and all type of cargo) was required to be done through X-ray or other non-Intrusive Inspection (NII) technology. However, no such facility, either X-ray or NII techniques as available in Office of the Dy. Commissioner (Customs), FPO, Jaipur. Apart from this computerisation was also not done in respect of import through courier in this office.

CBEC in their reply (December 2015) stated that Presently 11 X Ray Baggage Inspection System (XBIS) systems are installed at 7 FPOs/PADs at different locations and in addition 5 more machines are proposed to be installed.

CBEC may intimate the location where these machines were installed and or proposed to be installed.

(d) As per sub-regulation 2(b) of regulation 2 of Courier Imports and Exports (Clearance) Regulations, 1998, these regulations shall not apply to the goods where the weight of the individual package exceeds 70 kilograms.

Further, these regulations shall apply to export of cut and polished diamond, gems and jewellery under any scheme of export and import policy published by the government of India under Ministry of Commerce as amended from time to time from Export Oriented Units, units in Export Processing Zones or units in the Domestic Tariff Area if the value of each export consignment under such export does not exceed rupees twenty lakh.

Audit observed that export consignment of goods of chapter 71 having value more than ₹ 20 lakh and also import consignment of rough semi-precious stones under chapter heading 71031029 and having weight more than 70 Kilograms were allowed to clear from FPO office, Jaipur.

CBEC in their reply (December 2015) stated that goods imported or exported by post are governed by Sections 82, 83, and 84 of the Customs Act, 1962. The procedure for clearance of goods through post is prescribed in Rules regarding Postal Parcels and letter packets from Foreign Ports In/Out of India of 1953. The Export through Foreign Post office are not covered by Courier Imports and Exports (Clearance) Regulations, 1998. As Import and Exports through postal is one of the oldest practices. There is no such financial limit in Section 82, 83 and section 84 of The Customs Act, 1962.

Reply is not tenable, as per regulation 2(1) of Courier Imports and Exports (Clearance) Regulations, 1998, these Regulations shall apply for assessment and clearance of goods carried by the 'Authorised Couriers' on incoming or outgoing flights or by any other mode of transport on behalf of a consignee or consignor for a commercial consideration. Foreign Post Office is covered

under the definition of 'Authorised Courier' according to sub-regulation 3(a) of Regulation ibid. Thus export through Foreign Post office is covered by the Courier Imports and Exports (Clearance) Regulations, 1998.

(e) As per the Customs Act 1962, proper officer has power to search any suspected person who has landed from or is about to board or is on board any vessel within the Indian Customs waters, screen or X-ray bodies of suspected persons for detecting secreted goods. Further, as per the Customs Act, 1962, all imported goods unloaded in a customs area shall remain in the custody of authorized person and it can be allowed to be cleared only with the written permission of authorized person.

Audit scrutiny of the procedure followed and systems in place at Mumbai Port Trust under the preventive wing of Commissioner of Customs-General, Zone-I, Mumbai, revealed that no screening machine was installed at 'A' division passenger terminal and that the officers were provided with only hand held metal detectors. Further, Central Industrial Security Force (CISF) officers employed at Exit/Entry gates were screening the baggage of passengers as well as crew members only with respect to security angle.

It was further observed that passengers alighting from foreign vessels were allowed to exit with temporary pass to enter the city and return. Crew members were allowed to sign off from Mumbai if their duty period is over. In the absence of screening machines installed at the passenger terminal, Customs Officers may not be in a position to detect whether passengers allowed to exit on temporary pass and crew members signing off after duty hours carry any dutiable or prohibited goods with them.

Allowing passengers/crew members passage without any screening of their baggage/person is fraught with the risk of dutiable goods/prohibited goods being cleared without payment of applicable duty.

CBEC in their reply (December 2015) stated that there was no baggage scanner for passengers and crew members disembarking from ships/vessels is provided and to install Scanning Machine at MBPT, Mumbai.

Final outcome may be intimated to audit.

(f) As per Customs Manual 2014 no passenger can leave a Custom Station without thoroughly checking of Baggage and other items imported by him on each existing Airport, International Railway Station or Air/Rail Cargo unless permitted by Customs Officer after clearance of all the formalities like payment of duties.

During test check of records of Customs stations i,e SGRDJI Airport, ICP Attari Road, LCS Attari Rail under the Custom (Preventive) Commissionerate,

Amritsar, it was noticed that at all the stations only x- rays, metal detectors were installed but there was no mechanism or any other equipment available to detect the Precious Stones like Diamond, Gems & others. Thus the department had inadequate equipment to detect smuggling of precious stones items like Diamond, gems etc, except gold and gold articles.

CBEC in their reply (December 2015) stated that as regards availability of mechanism for detection of precious stones like diamonds, gems or others, after clearance of the passenger by the immigration, customs officers X-ray all luggage items carried by the passenger and the passenger himself is made to pass through the door frame metal detector. It is pertinent to mention that precious metals and stones have identifiable signatures in X-rays. If a doubt arises during the X-ray, the baggage of the passenger is marked and sends for thorough examination. Customs also deploys sniffer dogs at the stations for this purpose. In addition to the above mentioned measures, the profiling of the passengers is also done and close liaison is maintained with the various intelligence agencies and if suspicious movement of a passenger is noticed, he is subjected to rigorous checking.

(g) An Indian passenger who has been residing abroad for over 1 year is allowed to bring jewellery, free of duty, in bonafide baggage up to an aggregate value of ₹ 50,000 in the case of a male passenger or ₹ 1 lakh in the case of a lady passenger.

Any passenger of Indian origin (even foreign national) or a passenger holding a valid passport issued under the Passport Act, 1967 if coming to India after a period of not less than 6 months of stay abroad is allowed to import specified quantities of gold and silver as baggage on payment of duty, which has to be paid in foreign currency.

Audit scrutiny of the baggage receipts for the years 2010-11 to 2014-15 at Devanahalli Airport revealed that in number of cases period of stay abroad was not recorded. Further, no column has been provided in baggage receipt for recording the same.

Since quantity permitted to be brought to India depends on period of stay abroad, column for Period of Stay abroad ought to have been provided in baggage receipt book to minimise the misuse of the provisions.

CBEC in their reply (December 2015) stated that instructions have been issued to all officers preparing such baggage receipts to ensure that all details including the stay in abroad are invariably mentioned in the baggage receipt prepared by them.

However, copy of the instruction issued was not produced to audit.

2.7 Activities in SEZs

(A) Exports of Plain gold jewellery from SEZ

In two cases, audit observed that the process of importing gold bars, transporting them to the manufacturing units and exporting them to the buyers were completed within very short time leaving a space to doubt the entire process of import to declared export by the units.

DC, NOIDA, issued (July 2010) an LOA in favour of M/s SRS Ltd for manufacturing of gold jewellery. The unit exported 923.60 kgs of pure gold jewellery manufactured from gold bars during November 2013 to March 2015. Audit observed that the unit imported the gold bars just one or two days before the date of exports. The manufacturing of gold jewellery from imported gold bars and export thereof entails a elaborate process such as completing import formalities at Indira Gandhi International Airport (IGI), New Delhi and NSEZ, transportation from the port of import to the unit, manufacturing of gold jewellery from gold bars, completion of export formalities at NSEZ and then export from the port of shipment, IGI in this case. The entire process described above has been completed within a day or two.

Manufacturing of gold jewellery by the unit beyond its installed capacity and within a short span of a day or two prima facie, needs to be investigated.

Further, though the unit had declared production capacity of manufacturing plain gold jewellery of 25 Kg per day and exported gold jewellery having value more than 25 kg per day against 18 SBs which indicates that the unit might have exported gold jewellery obtaining the same from DTA.

In another case, M/s Kundan Care Products Ltd, Haridwar transferred 1815 Kg gold Bars to its sister unit at Gurgaon and exported gold jewellery after manufacturing at Gurgaon during the period November 2013 to November 2014. Audit scrutiny revealed that the unit exported 879 kg of pure gold jewellery, which had been received from Haridwar just one day before the date of export through 103 invoices.

The series of activities from transportation from Haridwar to Gurgaon, completing all manufacturing process at Gurgaon unit and fulfilling the export formalities does not seem possible in a single day. Hence, the export of gold jewellery made by the unit needs to be investigated.

Department may revisit the provisions of the export incentive schemes under FTP and introduce proper checks and balances to avoid doubtful import and export under the schemes.

CBEC, in respect of M/s Kundan Care Products Ltd, Haridwar, in their reply stated that (December 2015) the issue requires an in depth coordinated investigation. However, investigation is being initiated in this regard and outcome of the investigation will be intimated on conclusion of the investigation.

Final outcome may be intimated to audit.

(B) Absence of provision for Value Addition and non-existence of mechanism for ensuring the actual wastage in the SEZ Rules

HBP prescribed the value addition EoUs in Gem and Jewellery Sector. However, no such provision exists in the SEZ Rules, 2006 and therefore Gems and Jewellery Units in SEZ are placed in an advantageous position as compared to other exporters/EoUs. Further, In case of failure to achieve the prescribed value addition, the EoUs were liable to pay duty forgone amount in proportion to non-achievement of VA, whereas, units in SEZs are only are required to achieve a positive value addition. In paragraph 2.4 (B) of this report audit opined that when NFE realised is less than the duty forgone under Advance Authorization Scheme, it has a direct impact on the fiscal management. The situation may also prevail for SEZ units.

Audit analysed the import/export data pertaining to Cochin SEZ and found that M/s Rajesh Exports Ltd has contributed 86.18 percen*t* of import of gold and 83.84 percent of exports from Cochin Special Economic Zone**.** Analysis of the data for the period 2007-08 to 2013-14 revealed that out of total 1108 export consignments, the unit achieved 1.5 percent value addition in 112 consignments as prescribed in the HBP. Out of remaining 996 cases, in 554 cases the value addition achieved was less than 1.5 percent and in 412 consignments there was negative value addition of US$ 200,775,820. Moreover, actual purity of exported goods could not be ascertained as there was no mechanism in place at that time to check the purity of the exported goods in CSEZ. Since M/s Rajesh Exports Ltd was the major importer/exporter of Gold in CSEZ, absence of provision in the SEZ Rules to prescribe the minimum value addition in the Gem and Jewellery Sector defeated the intended objective of foreign exchange earnings.

Similarly, seven SEZ units (4 in NOIDA SEZ and 3 in Manikanchan SEZ), could not achieve the VA prescribed for EoUs though they have achieved the NFE.

DGFT in reply to recommendation stated (December 2015) that the action to be taken by DoC as it requires changes in SEZ Act/ Rules.

Final outcome may be intimated to audit.

(C) Insufficient SEZ rules to curb smuggling activities

Customs Act, 1962, empowers the department to confiscate goods on account of improper importation, mis-declaration etc., and to initiate action to adjudicate the cases after issuing show cause notice. The Directorate of Revenue Intelligence (DRI) is functioning to prevent smuggling activities of prohibited goods and goods prone to evasion of customs duty which includes Gold, Silver, Diamond and other precious and semi-precious metals/stones.

During the period 2010-11 to 2014-15, there was increasing trend in the seizures affected by DRI, Chennai as detailed in Appendix 8.

In Cochin SEZ, two instances of unauthorised removal of gold were reported which involved non-accountal of 10.5 Kg Gold by M/s Ashwin Gold Pvt. Limited noticed by the Preventive Wing and 900 gm of Gold seized from an employee of M/s. Rajesh Exports Ltd by the Directorate of Revenue Intelligence which was taken out of SEZ premises without authorisation

The mechanism prevailing in SEZ to curb unauthorised movement of goods through SEZ gate was sought and it was informed that security personnel were deployed at the SEZ gate to prevent unauthorised movement of goods. The reply is not tenable as the security personnel are not authorised to carry out any customs preventive functions, nor is the gate-pass data linked to SEZ online data for any control check.

SEZ Rules provides freedom to SEZ units by way of self-declaration and no routine examination of these goods, prescribed thereby restricting Customs officials from exercising their normal functions. Taking into consideration, the inherent risks associated with revenue aspect in respect of Gem and Jewellery sector, audit is of the opinion that MOCI may introduce a mechanism to prevent clandestine removal/smuggling of Gold/Diamonds as in the case of any other schemes where duty exemption is extended under strict customs supervision/scrutiny by virtue of various notifications and orders issued by Ministry of Finance.

CBEC in their reply (December 2015), while admitting the audit observation stated that after cadre restructuring, sanctioned strength has been increased in various grades. Further working strength has also been improved.

The issue is about the existing vacancy of officials posted in preventive work and the reply is silent regarding the filling up of those vacancies.

(D) Non-accounting of imported Gold/Silver by SEZ units

Every SEZ Unit shall maintain proper accounts, financial year-wise and such accounts should clearly indicate the value of goods imported, consumed and

utilised goods produced, disposed by way of exports and the balance in stock in accordance with the provisions of SEZ Rules, 2006.

(i) Jewels Magnum (SEZ Unit) under MEPZ, imported goods worth ₹ 1,405.47 crore during the period 2009-10 to 2011-12 and the consumption of Gold was stated as ₹ 1,397.50 crore leaving a stock of ₹ 7.97 crore as on 31 March 2012 whereas the closing stock of value of goods has been stated as ₹ 2.87 lakh in the APR for the year 2011-12. Since there are no imports and exports during the years 2013-14 and 2014-15, the actual stock of material and its value needs to be examined by the Specified Officer of Customs in view of the above discrepancy as the duty at 10.3 percent on the closing stock value of gold short accounted works out to ₹ 82.11 lakh.

(ii) M/s Forever Precious Jewellery & Diamonds Ltd , a CSEZ unit, requested for permission to exit from SEZ scheme in 2013 and intimated (March 2014) that they had stock of 1.304 Kgs of Gold and 54.730 Kgs of Silver with them. On request of the unit, the department permitted (May 2014) to transfer the same to any other unit in CSEZ.

The import-Export data revealed that the unit had imported (March 2011 to March 2013), 8985 Kgs of Gold and exported 8909.697 Kgs leaving a balance of 75.303 Kgs whereas the actual stated stock of Gold was 1.304 Kgs. The data also showed that the unit had not exported 90 Kg of Silver granules imported by them during the same period whereas the actual stock was 54.730 Kgs of Silver. Hence, the unit has unaccounted quantity of 73.999 Kgs of Gold and 35.270 Kgs of Silver granules on which they are liable to pay duty of ₹ 1.89 crore and ₹ 1.22 lakh respectively.

Audit observed that Exit permission has not been issued to the unit yet which led to blockage of revenue of ₹ 1.90 crore towards duty of unaccounted Gold and Silver.

Reply of the department in the above cases is awaited (January 2016).

(E) Physical examination of consignments in SEZs

Under SEZ Rules, the assessment of imports and domestic procurement by a Developer or a Unit, shall be on the basis of self-declaration and shall not be subjected to routine examination except in case of procurement from the Domestic Tariff Area under the claim of export entitlements provided that where based on a prior intelligence the examination becomes necessary the same shall be carried out by the Authorised Officer(s) after obtaining written permission from the DC or the Specified Officer.

Whereas, as per RBI circular dated 1 July 2006, customs authorities are required to examine and certify the value of the goods exported in the

guaranteed remittance (GR) form to be submitted by the exporters to their respective banks.

Audit observed from information furnished by DC, (SEEPZ, Mumbai that during 2010-11 to 2013-14 SEZ units had made imports of ₹ 14,738.35 crore and export of ₹ 41,494.21 crore. All these imports and exports consignments by SEZ units were allowed without any physical examination except cases of re-imports to verify the genuineness of consignment. However, same analogy was not adopted to examine the case of imports of cut and polished diamonds on loan basis and exports thereof to verify whether the diamonds used in studding are the same or not.

Enabling provision of physical examination in the SEZ Rules is of utmost significance in view of cases of fraud/duty evasion detected by DRI and Customs Authorities at various SEZs. DRI has detected 29 cases of duty evasion in EoU/EPZ/SEZ during FY 2010 to FY 2014.

Further audit noticed that DC, Surat SEZ on 22 November 2013/1 December 2013 issued directions for random sample checking of import/export consignments of gold, gold jewellery and other jewellery to the extent of minimum of 10 percent of total consignment in case of import/export from/to gulf countries and Hong Kong was and for other countries, examination and purity checking was to be carried out on random basis. In our opinion such instruction has no real impact as the same is not backed by amendment in SEZ rule 2006.

In the absence of an enabling provision in the SEZ Rules, the department is not in a position to check the adequacy of assessments done by the units and the revenue consequently realized. Therefore there is a need for a convergence between the SEZ rules with RBI instructions. Thus, in the absence of any rule or instructions from the Board to physically examine the goods imported/exported by a SEZ unit, undervaluation/overvaluation of goods in import/exports cannot be ruled out and accordingly, the value addition/net foreign exchange (NFE) achieved by the SEZ units cannot be relied upon.

Reply of the department is awaited (January 2016).

(F) No provision to check the purity of gold medallions and coins

In MEPZ-SEZ, Chennai, M/s Surana Corporation Limited, was issued (May 2008) LoA for manufacture and trading activity of Jewellery articles, medallions and bars of any precious metals. The unit manufactured and exported Gold Medallions/coins and stopped manufacturing and trading activity during 2013-14.

As per APR, during 2009-10 to 2013-14, the unit achieved NFEE of ₹ 161.25 crore. However, as per Bank realisation details an amount of ₹ 298.97 crore were outstanding for a period of more than two years. This resulted in achieving negative NFE to the tune of ₹ 137.72 crore due to non-realisation of export proceeds. Consequently, the duty forgone of ₹ 15.63 crore extended on import of Gold bars proportionate to the unrealized FOB value of exports may be recovered along with applicable interest.

Moreover, the Directorate of Revenue Intelligence, Chennai seized 5.242 Kg of smuggled gold valued at ₹ 1.40 crore from M/s Surana Corporation Limited from its showroom premises at NSC Bose Road, Chennai and also found that 408.739 kg of gold covering jewellery (jewellery made of copper coated with golden colour) were tagged with markings as 22 carat gold jewellery.

There is currently no provision to check the purity of gold medallions and coins (mentioned to be of purity 995 fineness in SBs) exported to various countries from SEZs by Customs authorities.

Reply of the department is awaited (January 2016).

Recommendation No. 5*: Department of Commerce may consider introducing suitable provisions in the SEZ rules, to prescribe a minimum value addition by the SEZ units; to provide certain minimum percentage of examination of goods to check the purity of Gold jewellery, caratage of Diamonds and for regular stock verification to check diversion into DTA. The provisions should include value of procurements made by SEZ from DTA (on payment in foreign currency) for the purpose of calculation of NFEE.*

2.8 Absence of norms and enabling conditions

(A) Non-existence of uniform procedure for re-import of 'cut and polished diamonds' (CPD)

As per of the Customs Act, 1962, if the goods are imported into India after exportation, such goods shall be liable to duty and subject to all the conditions and restrictions, if any, to which goods of like kind and value are liable or subject on the importation there of.

Similarly, FTP 2009-14 stipulates that Gems and Jewellery exporter are allowed to export diamonds, gem stones and jewellery on consignment basis as per procedure prescribed under Handbook of Procedure (HBP) Vol-I and Customs Rules and Regulations. Further, HBP laid down that re-import of these items (either in complete or partial lot) exported on consignment basis shall be subject to condition that the exporter follows prescribed provisions of relevant Custom notification to establish that goods are the same which

are exported. Some of the important exemption notifications governing the re-import of CPD are listed in Appendix 9.

Audit observed that in the case of re imports against export on consignment basis, there is no procedure prescribed under FTP or in Customs notifications for maintenance of any control register or reporting system for monitoring re-import of CPD. There is also no system in place to ensure that the CPD re-imported are same which were exported and the importer has not claimed any export incentives on such export. The value of re-import of CPD done at PCCCC, Mumbai during the period from 2010-11 to 2014-15 was ₹ 1,17,698.14 crore (Appendix 10). In PCCCC, Mumbai imports through EDI were implemented from January 2014 and exports are not yet integrated with EDI.

Analysis of import and re-import of CPD through PCCCC during 2010-11 to 2014-15 revealed that the percentage of total re-import cases against the total imports of CPD was only 27 percent in 2010-11 and 30 percent in 2011-12 when there was no duty on CPD. However re-import cases increased significantly in the subsequent years when duty of 2 percent was introduced on CPD and amounted to 73 percent, 66 percent and 79 percent of total imports in the year 2012-13, 2013-14 and 2014-15 respectively. It is also significant to note that the re-import of CPD in the year 2014-15 amounted to ₹ 40,440 crore which is 29 percent of the total export of CPD from PCCCC, Mumbai.

CBEC in their reply (December 2015) stated that proper mechanism for establishing the identity of re-imported goods is already in place. The parameters like size, colour, cartage, clarity certification no. etc. made by the exporter at the time of export are endorsed on the export documents and these parameters are tallied with the re-imported goods.

Regarding the audit observations on the re-import of CPD in the year 2014-15 records at PCCCC, Mumbai is being verified. A detailed reply in this regard will be submitted shortly.

Reply of the department is not tenable as there is no procedure or conditions prescribed under FTP or in any Custom notifications for maintenance of any control register or reporting system for monitoring re-import of CPD. In the absence of any record of re-imports being maintained there is no audit trail to ensure that the department has followed due procedure at the time of allowing re-import. Detailed reply in respect of re-import of CPD in 2014-15 at PCCCC is awaited.

***Recommendation No. 6**: Department of Commerce may review the export incentives allowed on G&J exports, product category and country wise,*

considering the volume and value of re-imports involved, to safeguard the interest of revenue and to prevent round tripping.

(B) Delay in increasing import duty on Gold jewellery

The Board notified (17 March 2012) the rates of duty on gold jewellery and gold bars at 10 per cent and four percent respectively. The rate of duty on gold bars was further increased to six per cent w.e.f. 21 January 2013, to eight per cent w.e.f. 5 June 2013 and to ten per cent w.e.f. 13 August 2013.

In order to avoid an inverted duty structure and protect domestic gold jewellery manufacturing industry sufficient gap between customs duty rates of gold and gold jewellery was maintained. It was observed that rate of duty on gold jewellery was not simultaneously increased from the existing ten per cent while rate of duty on gold bars was increased to ten per cent w.e.f. 13 August 2013. The rate of duty on gold jewellery was increased to 15 percent w.e.f.17 September 2013. It was observed that gold jewellery valued at ₹ 13.79 crore was imported at PCCCC during the period from 13 August 2013 to 16 September 2013 by paying custom duty at the rate of ten per cent. Had the duty rate on gold jewellery been increased to 15 percent w.e.f 13 August 2013, the govt could have earned ₹ 68.96 lakh extra from the import of gold jewellery made through PCCC, Mumbai alone during the period. All India data of the imports made during 2013-14 was called from DG (System), New Delhi, which has not been furnished to audit for detailed examination.

CBEC in their reply (December 2015) stated that subsequent to increase in import duty on gold, DRI had suggested that a duty differential of at least 5 per cent over the primary rate should be provided to protect this labour intensive sector from cheap imports. Similarly, Committee of Privileges, Lok Sabha had also suggested that a gap of at least 10 per cent should be maintained between bullion (gold and silver) and jewellery thereof, to protect the interests of artisans dependent on this sector for their livelihood. Accordingly, the matter was examined and notification dated 17 September 2013 was issued to increase tariff rate of duty on gold jewellery. The above process took time of about one month and the duty rates on gold are increased using emergency powers. The time lapse of 1 month is not too much to destabilize the Indian jewellery units.

Department's reply is not satisfactory as duty rate was increased to 15 per cent only after recommendation of DRI and Committee of Privileges, Lok Sabha instead of a considered change to protect the employment and domestic value addition chain.

(C) Incomplete authorisation of Ports for import licences

As per HBP, every licensee has to fill an application in original to concerned RLA in form ANF 2B for issuance of import license by the DGFT in case of restricted items. Also import authorizations for a restricted item, shall be issued for import through one of the sea ports or air ports or ICDs or CFS, as per the declaration by the applicant.

RLA Mumbai and JDGFT, Dehradun issued authorised 26 and 2 licenses respectively for import of Gold Dore Bars during 2010-11 to 2014-15. Audit observed from the licenses that port of registration was mentioned as "O" which indicates any Port in India against the Port of registration instead of specific port mentioned by the licensee in their application. Due to the imports not routed through EDI, DGFT was not in a position to monitor the imports of gold Dore Bars and also to capture the specific port of registration in the licenses.

Department while accepting the audit observation stated that they have requested to NIC/Computer cell to make necessary modification in the exiting software system meant for issuance and printing of relevant authorization.

DGFT in their reply (December 2015) stated that the NIC in DGFT is being requested to make adequate provisions in Software so that Port of Registration automatically comes in the licence to be issued.

Final outcome may be intimated to audit.

(D) Inconsistencies/ambiguities in notifications and provisions

(i) CBEC notified the tariff value on Gold and Silver effective from 17 January 2012 for imports through baggage, post and courier for assessment and collection of revenue. However, the tariff value for regular imports of Gold and Silver i.e. other than import through post, courier and baggage was introduced on 30 March 2012 by the Board. The difference of tariff value for gold and silver for two different sets of import procedure i.e. import through post, courier and baggage and other than import through post, courier and baggage resulted in short collection of revenue to the tune of ₹ 1.55 crore on import of 50 items imported through 32 BEs during 17 January 2012 to 30 March 2012 in ACC, Mumbai, Chennai, Coimbatore, Nedumbassery and Cochin Air Commissionerate

Similarly, excess duty to the tune of ₹ 1.45 crore was collected on import of 46 items through 22 BEs in in Chennai, Coimbatore, Cochin and Air Commissionerate.

There was inconsistency in the stand taken by the Board adopting two different valuations on import of Gold/Silver bars through Baggage/Courier and regular imports during the relevant period.

CBEC in their reply (December 2015) stated that after the change from specific duty rates to an ad-valorem duty rate, to facilitate speedy clearance of passengers at the airports, tariff values were fixed for import of gold and silver by passengers and later on based on a number of representations, it was extended to import of gold and silver through cargo also. However, fixation of tariff value is not revenue raising measure but a measure to ensure certainty and uniformity in assessment. Further department stated that accepting the recommendation to adopt tariff value or transaction value whichever is higher for charging duty will be a violation of WTO agreement on valuation to which India is a signatory.

Further, CBEC reported that in case of Coimbatore ACC, all the six BEs (filed by five importers) pertain to the years 2012 and 2013 are time barred, however, the importers were asked to pay the short levied duty with interest. Out of the five, importers, two importers viz. M/s The Handloom & Handicrafts Exports Corporation of India and M/s Riddhi Siddhi Bullions Ltd. have paid the short levied duty and interest, amounting to ₹ 4.21 lakh. Regarding excess collection of duty, due to non-adoption of tariff value and incorrect application of tariff value, for which no action is pending, as no importer had filed any refund claim for the excess paid duty.

Department's reply is not acceptable as fixation of tariff value was done to prevent undervaluation as seen from various minutes of meeting of Chief Commissoners of Customs. In fact, due to inconsistency in the stand taken by the Board by adopting two different valuations on import of Gold/Silver bars through Baggage/Courier and regular imports during the relevant period created anomaly. Therefore there is no question of an audit recommendation to adopt tariff value or transaction value whichever is higher for charging duty rather CBEC has been asked to remove the anomalous situation. However, outcome in the remaining cases may be intimated. The excess amount collected by the Government from the importer should have been deposited to the National Consumer Fund as stipulated in Section 27 of Customs Act, 1962.

(ii) Articles of Jewellery falling under heading 7113 are leviable to CVD at 6 percent in terms of notification dated 01 March 2011. Audit observed that the rate of CVD for Articles of jewellery falling under heading 7113 which was 1 per cent effective from 17 March 2012 was amended to 'Nil' rate of duty vide the Finance Act 2012 (23 of 2012) dated May 2012 with retrospective effect from 17 March 2012.

As both the aforesaid notifications are in force, there is ambiguity with regard to the levy of CVD on import of Articles of Jewellery. The Board may review these notifications and rationalise the duty rate to remove the ambiguity.

CBEC in their reply (December 2015) stated that it is settled legal position that when two notifications are available to the assessees, he may make use of the notification beneficial to him.

CBEC's may review their reply in the context of the fact that the Board does not benefit reacting to the situation rather than proactively rectifying the ambiguity in the notifications highlighted by audit.

(iii) According to HBP, 'export against supply by foreign buyer' and 'export against supply by nominated agencies' respectively, the exports shall be completed within 90 days and no extension for fulfilment of EO shall be allowed

However, the Customs Notifications 5 May 2000 and 8 May 2000 under which the Scheme of 'Export against Supply by Foreign buyer' and Export Against Supply by Nominated Agencies' are implemented by the Customs department for monitoring the Scheme provides that the importer exports gold/silver/platinum jewellery or articles within 120 days from the date of import. Thus, there exists an inconsistency in the provisions of the HBP and the Customs Notification regarding the period of fulfilment of EO.

M/s. Malabar Gold Ornaments Makers Pvt. Ltd imported (December 2014) 25 Kgs of 995 purity gold from M/s. Trendy Jewellery LIC, UAE under the scheme 'Export Against Supply by Foreign buyer' through ACC Nedumbasserry (Kochi). The export of Jewellery of 22CT were fulfilled (April 2015) by M/s. Malabar Gold Private Limited (name changed after amalgamation) after a period of 112 days from the date of import.

Inconsistency in the provisions between the Customs Notification and the HBP resulted in undue advantage by way of extension of Export obligation period by 22days and hence the duty foregone of ₹ 65.11 lakh could not be realised from the importer.

CBEC in their reply (December 2015) stated that they would rectify the ambiguity in consultation with DoC. Whereas, DGFT replied (December 2015) that for consistency between Customs and DGFT provisions, Customs were required to follow the HBP.

Final outcome may be intimated to audit.

(E) Tariff value fixed by the Board does not relate to the transaction value

The Customs Act also provides that if the Board is satisfied that it is necessary or expedient to do so the Board by notification in the Official Gazette, fix

tariff values for any class of imported goods or export goods, having regard to the trend of value of such or like goods, and where any such tariff values are fixed, the duty shall be chargeable with reference to such tariff value. The World Gold Council (WGC) notifies daily international rate of gold in their website www.gold.org.

The Board notified the tariff value of Gold and Silver effective from 17 January 2012. Thereafter, based on the market fluctuations, the Board periodically revised the tariff value on import of gold.

On analysis of data for import of gold bars imported through ACC, Mumbai, ACC, Bangalore, Chennai Air, Coimbatore Air Customs, Kolkata Airport and Cochin Customs Commissionerate revealed that the tariff value fixed by the Board was lower than the invoice price (CIF value) in 646 consignments imported during the period 2012-13 to 2014-15 which resulted in short levy of duty of ₹ 46.55 crore.

The intention of fixing the tariff value by the Board was to prevent undervaluation of goods. However, the tariff value fixed by the Board on weekly or fortnightly basis was not commensurate with the prevalent international price of the Gold/Silver as the rates changes frequently in a day. To stop the under/over valuation of Gold and Silver, Audit is of the opinion that in order to augment the revenue, the Board may consider reviewing the existing mechanism for fixing tariff value so that there is no revenue loss.

CBEC in their reply (December 2015) stated that India's Customs valuation law flows from the WTO Agreement on Customs Valuation (ACV) which is a binding agreement. The Tariff Values are calculated on the basis of prevailing international prices of gold and silver. The tariff values are accepted as the assessable values for these commodities, irrespective of whether the declared values for these commodities are higher or lower than these tariff values. These tariff values are not fixed but are floating values and are reviewed and revised every fortnight based on international prices so as to keep them close to the transaction values.

Focus of Audit comment is to strengthen the process of fixation of tariff and is not against the WTO principle. Department's view on fixing tariff value in such a way so that there would not be a revenue loss is not acceptable as the Valuation Directorate developed the following criteria to select commodities for recommending tariff values: (i) large volume of imports and significant revenue contribution, (ii) high rates of duties and sensitivity of under-valuation, (iii) wide fluctuation in assessed values at different Customs stations (iv) reliable information concerning international price is available (daily rates notified by WGC), (v) adequate information and data are available for periodic review of the tariff value so as to keep it as close to international

prices. From above it is clear that data on transaction value received from different customs stations in an online environment was not considered for review of the tariff value. Unreal value of Tariff results in both over assessment and under assessment, causing loss of importer confidence and/or revenue loss of Government. Audit maintains the view that tariff value should be fixed in such a way to prevent undervaluation.

Recommendation No. 7*: Existing mechanism for fixing tariff value may be reviewed by CBEC so as to facilitate a balance between the revenue management and valuation concerns.*

(F) Absence of mechanism to correlate the Annual Export Turnover declared in Aayaat Niryaat Form

As per HBP, application for Replenishment (REP) Authorisation may be made to RA concerned. Licensees are liable for penal action for any inaccurate details in their application.

RLA Mumbai authorized 19 and 36 REP authorisation to M/s Vishrut Gems and M/s Dipak Dipchand Taswala respectively during 2010-11 to 2014-15. Audit observed that the disclosed export of the last three year in Aayaat Niryaat form did not tally with the export declared in the Profit and loss accounts. This indicates that the department had no mechanism to check correctness of declaration made by the licensee in their application and thereby no action had been initiated by the department against the licensees.

The complete reliance of the department on the declaration furnished by the Licensee for grant of duty credit certificates and non-correlation of the declaration with other statutory documents like audited annual accounts was a risk area which was left open by the department for misuse of the schemes.

DGFT in their reply (December 2015) stated that in keeping with the spirit of trade facilitation, every effort is made by DGFT and the DoC to reduce the transaction cost by avoiding insistence on additional documents. In any case, if any mis-declaration comes to the notice even subsequently, the authorisation holder can be proceeded against under Rule 10 of the Foreign Trade (Regulation) Rules, 1993.

(G) Separate International Tariff Classification (Harmonized System) code for Manmade Diamonds and Natural Diamonds

(i) Lab grown/synthetic/manmade diamonds and natural diamonds were classified under same ITCHS code from 16 January 2012, prior to that they were classified under different headings.

The rationale for classifying both Lab grown/synthetic/manmade diamonds and natural diamonds under one heading was not made available to audit.

Audit observed that Natural diamonds takes long time to form in comparison to lab grown diamonds. Good quality synthetic diamonds can only be distinguished in the laboratory with the use of specialized instruments. The prices of manmade diamonds are cheaper than natural diamonds to the extent of 30-60 percent. As per report of Diamond Intelligence Briefs the clubbing under the same ITC HS Code has led to illicit and undisclosed mixing of manmade diamonds with natural diamonds. This also leaves scope for duping consumers and possible money laundering. Further, this threatens the consumer and trade confidence in Indian diamond industry. Hence a clear categorization specific to man-made diamonds is needed to enable specific tracking of synthetic diamonds. Similar proposals were made by DoC in their budget proposal for the year 2014-15.

CBEC in their reply (December 2015) stated that the issue is being examined. There is no revenue angle. The decision may be taken as soon as possible.

Final outcome may be intimated to audit.

(ii) GJEPC on 25 October 2013, apprehended before CBEC regarding possible fraud being committed by way of passing off lab grown diamond as natural diamond by unscrupulous parties in order to make quick profit. GJEPC also raised concern that such activity may contaminate the entire natural diamond industries in India, thus negatively effecting the credibility of India in international market and made recommendation (November 2013) to the Chief Commissioner of Customs, Gujarat zone for testing the consignment imported/exported under CTH 7104.2000 and 7104.9000 (i.e., synthetic or reconstructed precious or semi-precious stones) to check such activity.

Audit observed that the department, based on the above recommendation, started the practice of sending every consignment, declared as commodity classifiable under CTH 7104.2000 and 7104.9000, for testing to Indian Diamond Institute, Surat.

The process of testing the goods which has already been declared as synthetic diamonds defeated the purpose for which GJEPC made the request for testing of the consignments. It would be more appropriate to test the goods declared as natural diamond to ensure that it does not contain synthetic diamond. However, audit did not find any instance where consignment declared as 'natural diamond' was sent for testing. Hence, the present system being followed may be re-looked.

Reply of the department is awaited (January 2016).

Recommendation No. 8*: To maintain the consumer and trade confidence in Indian diamond industry, CBEC may consider a clear categorization for manmade diamonds to differentiate from natural diamonds.*