Report of the Comptroller and Auditor General of India

for the year ended March 2005

Union Government

Indirect Taxes (Customs, Central Excise and Service Tax)

No.7 of 2006

Laid on the Table of the Lok Sabha and Rajya Sabha on ....

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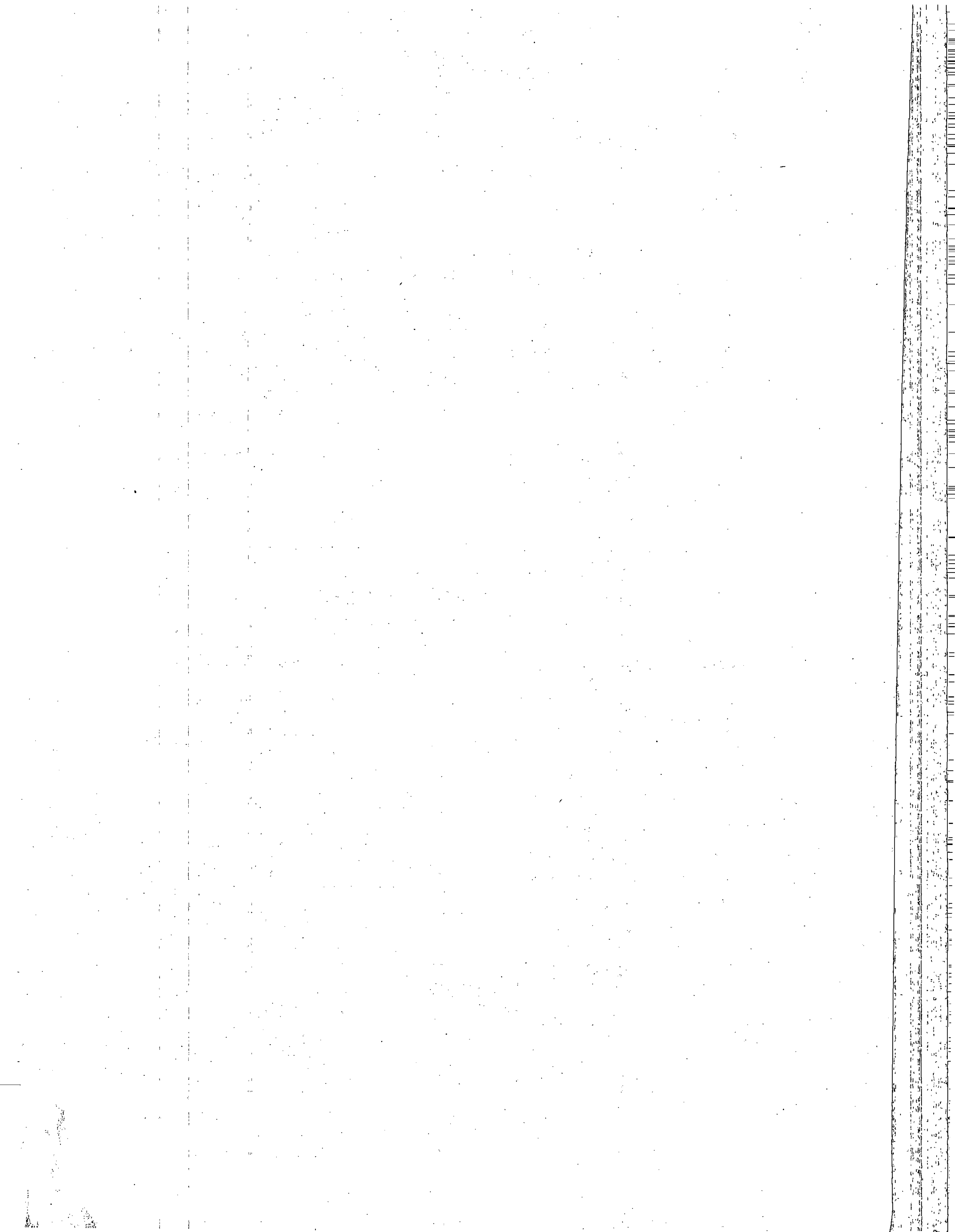
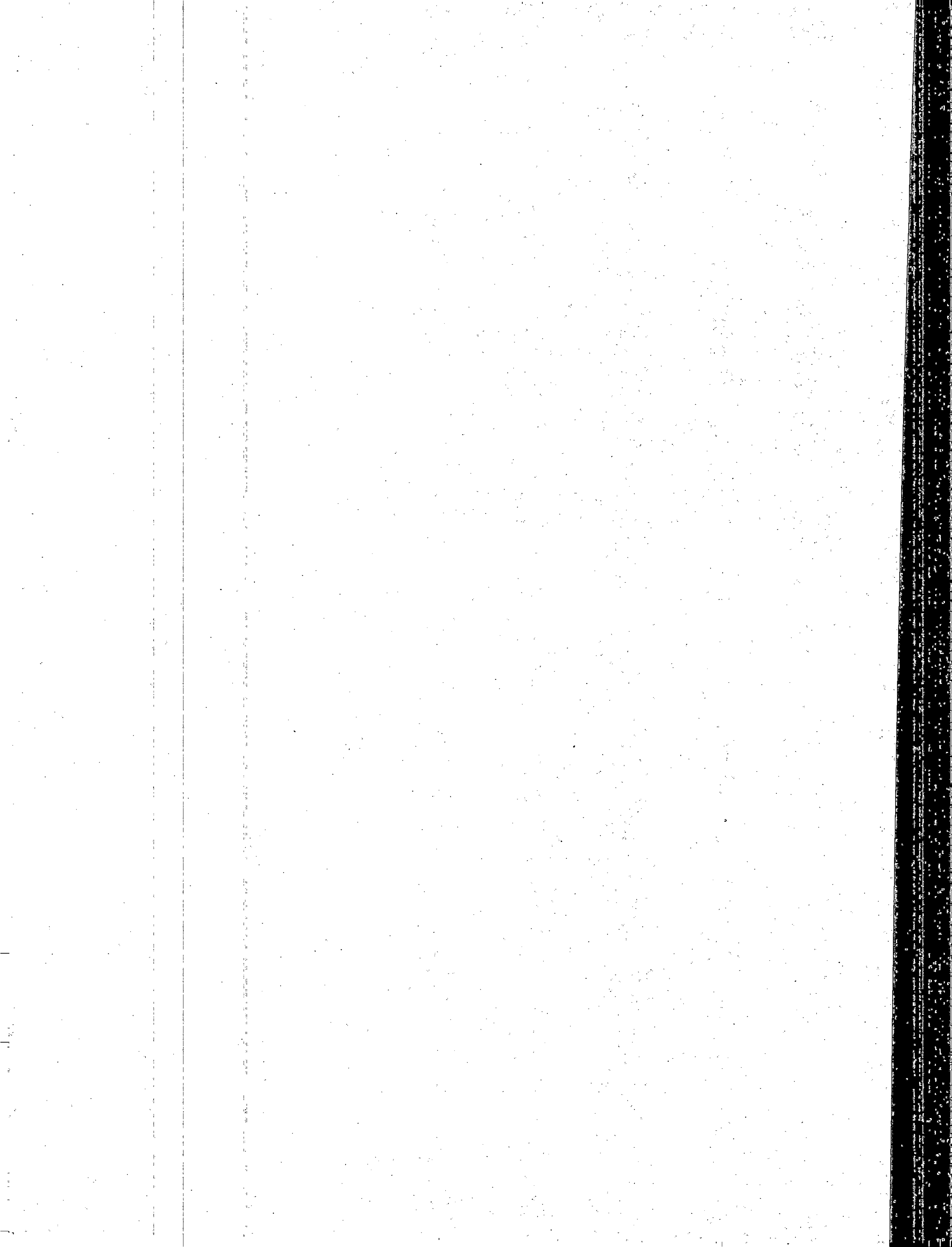


PREFACE

This Report for the year ended 31 March 2005 has been prepared for submission to the President under Article 151 of the Constitution based on the test audit of Indirect Taxes (Customs, Central Excise and Service Tax Receipts) of the Union of India in terms of Section 16 of the Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971.

Section 1 of the Report covers matters relating to 'Customs', section 2 covers 'Central Excise' and section 3 covers 'Service Tax'.

The cases mentioned in the Report are among those which came to notice in the course of audit during 2004-2005 and early part of the year 2005-2006, as well as those which came to notice in earlier years but were not reported.



OVERVIEW

This report is presented in three sections:

Section 1	**Chapters I to VII**	**Customs**
Section 2	**Chapters VIII to XVIII**	**Central Excise**
Section 3	**Chapters XIX and XX**	**Service Tax**

Some of significant findings are highlighted below:

SECTION 1 - CUSTOMS

This section contains 256 paragraphs featured individually or grouped together and miscellaneous cases with audit impact of Rs.112.41 crore attributable to non compliance of Rules/Regulations. Financial implication of Rs.243.38 crore relating to lacunae/ shortcomings in notification/Act/Regulations have also been brought out in this section. Some of the important findings included in the section are highlighted below:

I. General

- Budget estimate 2004-05 was pitched at Rs.54,250 crore and revised estimate at Rs.56,250 crore. Actual collections however were more than both, mainly due to increase in collection of import duty on petroleum products, non-ferrous metals, chemicals and iron and steel.

{Paragraph 1.1}

- The amount of duty foregone under the various export promotion schemes during the year was Rs.41,033 crore which was 71per cent of the total customs receipts.

{Paragraph 1.4.1}

II. Irregularities in assessments

- Dutiable imported goods were incorrectly classified and assessed to duty at lesser rates leading to short levy of Rs.50.65 lakh in seven cases.

{Paragraphs 2.1 to 2.3}

- Extending the benefit of exemption notifications to dutiable goods not covered by them resulted in short collection of duty of Rs.6.21 crore in 23 cases.

{Paragraphs 3.1 to 3.3}

- Short levy on account of undervaluation of assessable goods in six cases amounted to Rs.1.07 crore due to non compliance of Rules/Regulations and in two cases loss of revenue amounting to Rs.1.25 crore.

{Paragraphs 4.1 to 4.3}

- Additional duty leviable under section 3 of the Tariff Act amounting to Rs.36.04 lakh was not levied/short levied in eight cases.

{Paragraphs 5.1 & 5.2}

III. Recoveries from defaulting export houses

- Non levy/loss of customs revenue of Rs.61.15 crore due to failure to recover benefits of export incentives under schemes like DEPB, EPCG and EOU from defaulting exporters and financial implication of Rs.199.23 crore relating to lacunae/ shortcomings in Notification/Act/Regulations.

{Paragraphs 6.1 to 6.6}

IV. Other irregularities

- Non levy of penalty/special additional duty, excess payment of drawback and non levy of anti dumping duty etc. amounting to Rs.42.84 crore in 102 cases and issue of delayed notification resulted in loss of revenue of Rs.42.89 crore.

{Paragraphs 7.1 to 7.9}

SECTION 2 - CENTRAL EXCISE

This section contains 183 paragraphs involving monetary impact of Rs.911.60 crore directly attributable to audit pointing out non compliance to rules/regulations and 43 paragraphs involving Rs.6781.53 crore arising out of lacunae in law/procedure or control weakness. Audit has also in one paragraph pointed out notional interest amounting to Rs.3.80 crore. Some of the significant findings included in this section are indicated below :-

I. General

- The actual collections fell short of the budget estimates as well as the revised estimates year after year. Despite this, Government continued to make optimistic projections during presentation of the annual budget. The budget estimate 2004-05 was pitched at Rs.1,08,500 crore, an increase of 12.56 per cent over budget estimates, 18.13 per cent over revised estimate and 19.53 per cent over actuals of 2003-04. The collections fell short of the budget estimates by Rs.9375 crore or 8.64 per cent and short of revised estimates by Rs.875 crore or 0.88 per cent in 2004-05.

{Paragraph 8.1}

- A total of 45,804 cases involving duty of Rs.28,691.02 crore were pending finalisation as on 31 March 2005 with different authorities.

{Paragraph 8.5}

II. Non-levy/short levy of duty

- Incorrect payment of duty at concessional rate on finished goods by 76 manufacturers of processed fabrics led to short realisation of duty of Rs.266.24 crore.

{Paragraph 9.2}

- Incorrect availment of Modvat/Cenvat credit amounted to Rs.359.32 crore.

{Paragraph 10}

- Instances of undervaluation due to non-inclusion of additional consideration in assessable value, adoption of lower mutually agreed price, incorrect adoption of transaction value, incorrect adoption of assessable value of goods manufactured by job work or incorrect adoption/non-adoption of assessable value on the basis of MRP etc. were noticed. Duty levied short amounted to Rs.316.15 crore.

{Paragraph 11}

- Duty amounting to Rs.177.17 crore was short levied because of incorrect grant of exemption to units manufacturing tobacco products situated in North-Eastern States or to goods manufactured for captive consumption or exemption granted without notification under Central Excise Act etc.

{Paragraph 12}

- Incorrect classification of sulphur, pre-fabricated structural insulated panel etc. resulted in short realisation of duty of Rs.5.76 crore.

{Paragraph 13}

- Duty or additional duty not paid by due dates, not levied on goods lost in transit, goods found short or sold through vendors amounted to Rs.13.73 crore.

{Paragraph 14}

- Interest not levied or realized, or penalty not imposed in cases of delayed payment of duty amounted to Rs.8.24 crore.

{Paragraph 15}

- Demands for duty not raised or confirmed demands not realised resulted in blockage of revenue of Rs.6.10 crore.

{Paragraph 16}

- Cess amounting to Rs.3.54 crore was not realised from producers of processed textile fabrics and cement.

{Paragraph 17}

SECTION 3 - SERVICE TAX

This section contains 48 paragraphs with revenue implication of Rs.86.57 crore directly attributable to audit pointing out non-compliance to rules/regulations. Significant findings of audit included in this section are mentioned below :-

I. General

- Except in 2000-01 and 2004-05, actual collections had been lower than the budget estimates all through the five year period. Shortfall ranged from Rs.110 crore to Rs.1904 crore or 1.38 to 31.60 per cent over budget estimates during these years. In one of the five years i.e. 2002-03 receipt did not match even scaled down revised estimates and in 2003-04 did not reach increased budget estimate.

{Paragraph 19.2}

- A total of 36,367 cases involving tax of Rs.2535.02 crore were pending as on 31 March 2005 with different authorities, of which 70 per cent in terms of number were with adjudicating officers of the department. Pendency of demands for coercive recovery measures with departmental officers had increased from 5,460 in 2003-04 to 9,722 cases in 2004-05 i.e an increase of about 78 per cent.

{Paragraph 19.3}

II. Non-levy/short levy of service tax

- Service tax of Rs.54.74 crore was not paid on services provided by Prasar Bharti, storage or warehouse keepers, management consultants, clearing and forwarding agents etc.

{Paragraph 20.1}

- Non-collection of service tax on services rendered by foreign consultants providing engineering and management consultancy in India amounted to Rs.23.90 crore.

{Paragraph 20.2}

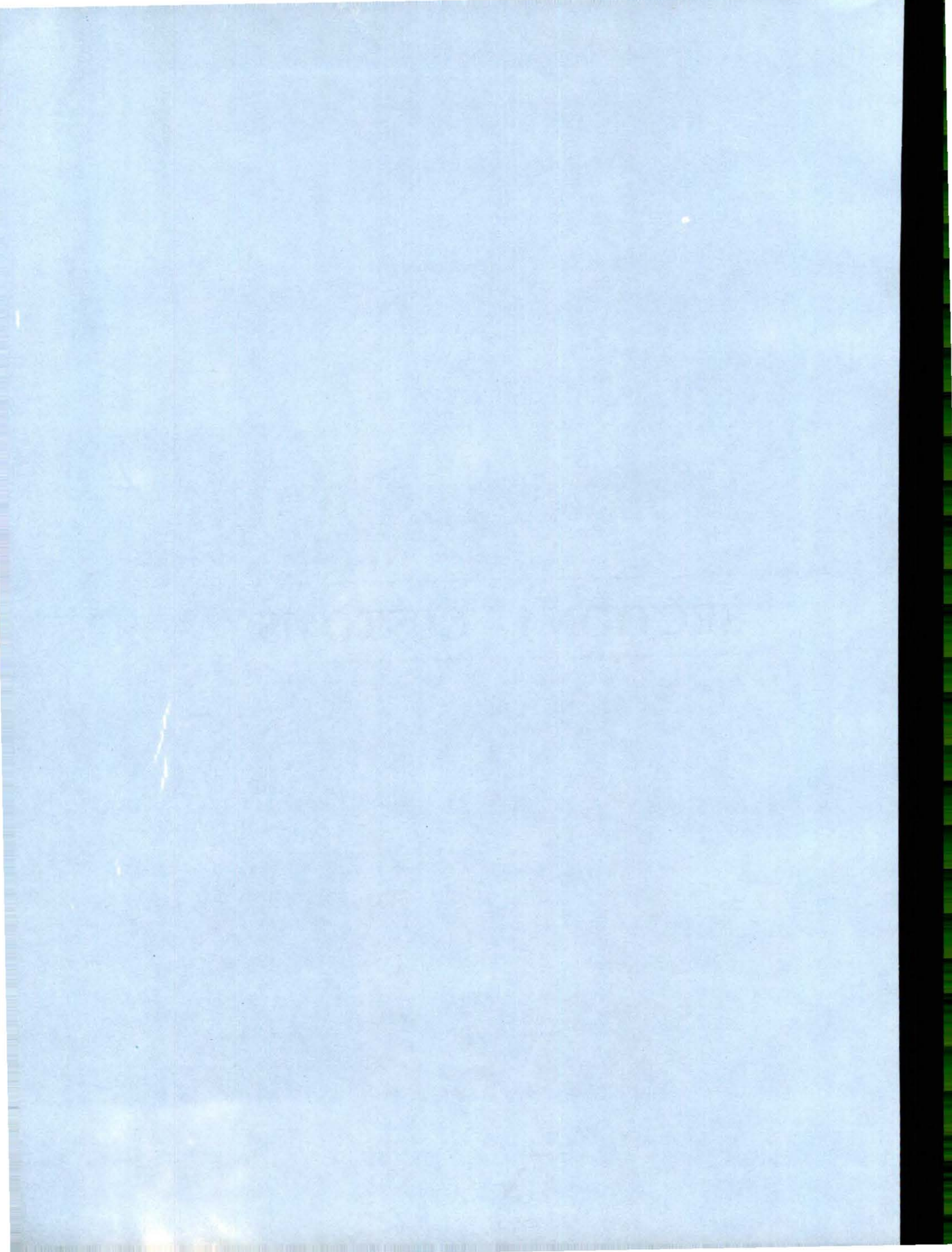
- Service tax amounting to Rs.5.04 crore was short paid on services of consulting engineers or on goods transport operators.

{Paragraph 20.3}

- Non-recovery of service tax on services of goods transport operators amounted to Rs.1.48 crore.

{Paragraph 20.4}

SECTION 1 – CUSTOMS



CHAPTER I: ANALYSIS OF RECEIPTS

1.1 Budget estimates, revised budget estimates and actual receipts

The budget estimates, revised budget estimates and actual receipts of customs duties during the years 2000-01 to 2004-05 are exhibited in the table below:-

(Amount in crore of rupees)

Year	Budget estimates	Revised budget estimates	*Actual receipts	Difference between actual receipts and budget estimates
2000-01	53576	49781	47542	(-)6034
2001-02	54822	43170	40268	(-)14554
2002-03	45193	45500	44851	(-) 342
2003-04	49350	49350	48629	(-)721
2004-05	54250	56250	**57610	(+)3360

* Figures as per finance Accounts.

** Figure is provisional.

Actual collection was more than both budget and revised estimate in 2004-05, mainly due to increase in collection of import duty on petroleum products, non-ferrous metals, chemicals and iron and steel.

1.2 Trend of receipts

A comparison of total year-wise imports with corresponding net customs duties collected during 2000-01 to 2004-05 has been shown in the table below :

VALUE OF IMPORTS AND IMPORT DUTY COLLECTED 2000-01 to 2004-05 (YEAR-WISE)

(Amount in crore of rupees)

Year	Value of Imports	Import duties	Import duty as percentage of value of imports
2000-01	228307	46569	20.40
2001-02	243645	39406	16.17
2002-03	296597	44137	14.88
2003-04	353976	48002	13.56
2004-05	490532	55807	11.38

1.3 Commodity wise details of customs receipts

Major commodity wise value of imports and exports and the gross duty realised therefrom during the financial year 2004-05 and the previous year 2003-04 are given overleaf:

1.3.1 Imports

(Amount in crore of rupees)

Sl. No.	Commodities	Value of imports*		Import duties**		Percentage share in total import duties collection	
		2003-04	2004-05	2003-04	2004-05	2003-04	2004-05
1.	Food and live animals chiefly for food	16902.93	17564.08	3285	3880	6.84	6.95
2.	Mineral, fuels and related materials	13235.64	24718.88	3974	4796	8.28	8.59
3.	Petroleum, crude and products	94520.00	134094.00	7491	9761	15.61	17.49
4.	Chemicals and related products	21381.64	44688.23	4185	5385	8.72	9.65
5.	Manufactured goods	38188.16	119662.81	4614	5057	9.61	9.06
6.	Machinery and transport equipment	29531.39	51819.41	13441	14817	28.00	26.55
7.	Professional instruments etc.	5635.56	6688.19	3319	3788	6.91	6.79
8.	Others	134580.29	91296.07	7693	8323	16.03	14.92
	Total	**353975.61**	**490531.67**	**48002**	**55807**		

1.3.2 Exports

(Amount in crore of rupees)

Sl. No.	Commodities	Value of exports*		Export duty and cess**	
		2003-04	2004-05	2003-04	2004-05
1.	Food items	24636.61	28492.77	10	08
2.	Beverages and tobacco	1562.05	1376.23	08	07
3.	Petroleum, crude and products (including mica)	105.66	30847.50	02	02
4.	Others	267062.43	301162.66	143	172
	Total of exports and re-exports	**293366.75**	**361879.16**	**163**	**189**

Source - *Ministry of Finance, New Delhi.
**Directorate General of Export Promotion, New Delhi.

1.4 Duty foregone

1.4.1 Under export promotion schemes

The break-up of duty foregone for export promotion schemes viz., advance licence, duty exemption pass book (DEPB), export promotion capital goods (EPCG), export promotion zone (EPZ), export oriented units (EOUs) and refund of duty under the drawback and other schemes for the period from 2001-02 to 2004-05 is shown in the table overleaf:

CUSTOMS DUTY FOREGONE UNDER EXPORT PROMOTION SCHEMES AND DUTY DRAWBACK SCHEME

(Amount in crore of rupees)

Year	Advance licence & others	DEPB	EPCG	EPZ/ SEZ	EOU	Duty drawback	Total
2001-02	7890	5661	2008	2064	4219	2957	24799
2002-03	7462	6831	3026	1106	4820	4520	27765
2003-04	10812	11692	3399	1320	9422	3059	39704
2004-05	11741	10076	4681	3457*	8266	2812	41033

* includes DFRC/DFCEC schemes also

The total duty foregone under various export promotion schemes for the period 2001-02 to 2004-05 as a percentage of customs receipts is shown in the table below:

(Amount in crore of rupees)

Year	Customs duty collected	Total duty foregone under export promotion schemes	Duty foregone as a percentage of customs receipts
2001-02	40268	24799	62
2002-03	44851	27765	62
2003-04	48629	39704	82
2004-05	57610	41033	71

Duty foregone under export promotion schemes has gone up from 62 per cent of customs duty receipts in 2001-02 to 71 per cent of customs receipts in 2004-05.

1.4.2 Other duty foregone

Duty foregone under section 25 (1) and (2) of Customs Act, 1962 (other than for export promotion schemes vide para 1.4.1) during 2001-02 to 2004-05 is shown in the table below:

(Amount in crore of rupees)

Year	No. of notifications issued under 25(1)	No. of total notifications issued under 25(2)	Total No. of notifications issued	Duty foregone under 25(1)	Duty foregone under 25(2)	Total duty foregone
2001-02	39	NA	NA	2477	NA	NA
2002-03	54	50	104	3512	34	3546
2003-04	57	63	120	4267	258	4525
2004-05	32	10	42	2496	09	2509

Section 25(1) General exemption & section 25(2) adhoc exemption

1.5 Cost of collection of customs receipts

The expenditure incurred on collection of customs duty during the year 2004-05 alongwith the figures for the previous year are given below:

(Amount in crore of rupees)

Cost of collection	*2003-04	**2004-05
Revenue cum import export and trade control functions	155.56	145.42
Preventive and other functions	514.58	573.10
Total	670.14	718.52
Cost of collection as percentage of customs receipts	1.38	1.25

* Figures as per finance Accounts.

** Figure is provisional.

1.6 Searches and seizures

The details of searches conducted and seizures effected by the customs officers as given by the Ministry of Finance (Ministry) are indicated below:

SEARCHES AND SEIZURES

Sl. No.	Description	2003-04	2004-05
1.	Number of searches	3780	3331
2.	Value of goods seized (Rupees in crore)	454.16	642.73
3.	Number of seizure cases adjudicated	10165	6781

Figures relate to 80 custom houses/commissionerates

1.7 Arrears of customs duty for recovery

The amount of customs duty assessed upto 31 March 2005 which was still to be realised as on 30 June 2005 was Rs.1805.92 crore in 106 custom houses and commissionerates.

1.8 Demands of duty barred by limitation

Demands raised by the department upto 31 March 2005 which were pending realisation as on 30 June 2005 and where recovery was barred by limitation amounted to Rs.41.93 crore in 106 custom houses and commissionerates.

1.9 Duty written off

Customs duties written off, penalties waived and exgratia payments made during the year 2004-05 and the preceding two years are given below:

(Amount in lakh of rupees)

Year	Amount
2004-05	*2.46
2003-04	57.13
2002-03	36.08

* Figure relates to 118 custom houses/commissionerates

1.10 Number of pending audit objections

The number of audit objections raised upto 31 March 2005 and pending settlement as on 30 September 2005 in the various custom houses and combined commissionerates of central excise and customs are given below:

OUTSTANDING OBJECTIONS AND AMOUNT INVOLVED

(Amount in crore of rupees)

Sl. No.	Commissionerate	Number	Amount
1.	Ahmedabad	40	70.06
2.	Ahmedabad (Prev.)	51	22.05
3.	Bangalore/Mangalore	469	68.61
4.	Bhubaneshwar	43	191.12
5.	Chennai (Sea)	1535	264.94
6.	Cochin	109	53.07
7.	Delhi	1419	143.42
8.	Jamnagar (Prev.)	30	114.08
9.	Kolkata	1708	2438.42
10.	Mumbai (Air)	537	11.35
11.	Mumbai (Sea)	887	332.57
12.	Hyderabad	536	757.83
13.	Others	3519	5923.55
	Total	**10883**	**10391.07**

1.11 Categories of outstanding audit objections

(Amount in crore of rupees)

Sl. No.	Categories of objections	No. of objections	Amount
1.	Short levy due to misclassification	1595	85.33
2.	Short levy due to incorrect grant of exemption	922	140.25
3.	Non levy of import duties	870	120.23
4.	Short levy due to undervaluation	540	57.37
5.	Irregularities in grant of drawback	933	17.97
6.	Irregularities in grant of refunds	92	21.67
7.	Irregularities in levy and collection of export duty	21	0.59
8.	Other irregularities	5910	9947.66
	Total	**10883**	**10391.07**

1.12 Contents of the section

This section contains 256 paragraphs (including 45 cases of total under assessment), featured individually or grouped together, arising from test check in audit. Two hundred forty four paragraphs contain audit impact of Rs.112.41 crore attributable to non compliance of Rules/Regulations. In 12 paragraphs audit has pointed out lacunae/shortcomings in notifications/Act/Regulations with financial implication of Rs.243.38 crore. Ministry did not respond to 40 paragraphs issued to them. Out of which in 22 cases, replies from even department were not provided (January 2006). The department/Ministry had (till January 2006) accepted audit objection in 178 paragraphs involving Rs.45.41 crore and recovered Rs.4.13 crore.

CHAPTER II: SHORT LEVY DUE TO INCORRECT CLASSIFICATION

Some illustrative cases of short levy of customs duty arising from incorrect classification of goods are briefly narrated below:

2.1 Automatic data processing machines/electronic equipment

The Tribunal in the case of commissioner of customs, Inland Container Depot (ICD), New Delhi vs Keihin Penalfa Ltd., {2003 (154) ELT 680 (Tribunal-Delhi)} held that 'electronic automatic regulators' are classifiable under sub-heading No.8543.89 of the Customs Tariff.

M/s. Ford India Ltd., Chengalpattu, imported (May and June 2000) two consignments of 'processor assembly' (also known as electronic automatic regulators) through custom house Chennai (sea). The department classified and cleared the goods under sub-heading 9032.89 as 'automatic regulating or controlling instruments and apparatus'. Incorrect classification resulted in short levy of duty of Rs.19.52 lakh and interest thereon.

On this being pointed out (October & November 2000), the Ministry reported (November 2005) recovery of Rs.21.77 lakh including interest.

2.2. Chemical products/tin plates

Preparations based on carbon in the form of pastes, blocks and plates and other semi manufactures are classifiable under heading No.38.01 of Customs Tariff.

M/s. Steel Authority of India Ltd., Bokaro Steel Plant imported a consignment of carbon blocks, mass and paste through Kolkata sea customs in February 2003 and the department classified them under CTH 6902.90 treating them as refractory product. This misclassification resulted in short levy of duty of Rs.11.90 lakh.

On this being pointed out (July 2003), the department reported (May 2005) recovery of Rs.10.55 lakh. Recovery particulars of the balance were awaited (January 2006).

2.3 Other cases

Five other cases of incorrect classification of goods imported by five importers involving short levy of duty of Rs.16.98 lakh were reported to the Ministry. The department/Ministry admitted the objection in two cases involving Rs.4.31 lakh as per details overleaf:

(Amount in lakh of rupees)

Sl. No.	Details of product	Name of the importers M/s.	Heading where classifiable	Heading where classified	Amount short levied	Amount admitted	Amount recovered
1	Tools	Bilakhia Holding (P) Ltd.	9031.00	8803.30	7.74	Not admitted	--
2	Colour television	Bigesto Foods (P) Ltd.	8528.00	8532.29	3.15	Not admitted	--
3	Sugar spheres	Cipla Ltd.	1701.99	3824.90	3.04	3.04	3.04
4.	Modular router	Network Solutions (P) Ltd.	8517.50	8473.30	1.78	Not admitted	--
5.	Process mills and accessories	Process mills & accessories	8479.00	8437.80	1.27	1.27	--
	Total				**16.98**	**4.31**	**3.04**

CHAPTER III: SHORT LEVY DUE TO INCORRECT GRANT OF EXEMPTION

Short levy of duties aggregating Rs.6.21 crore in 23 cases on account of incorrect grant of exemptions were pointed out to the Ministry. Some illustrative cases are narrated below:

3.1 Condition of notification not fulfilled

3.1.1 Crude palm oil and its fraction of edible grade falling under CTH 15.11 having acid value of two or more and beta carotene in the range of 500-2500 mg/kg in loose or bulk form are eligible for concessional rate of duty in terms of notification No.21/2002-cus (serial No.34) dated 1 March 2002.

Thirty two consignments of palm oil imported by M/s. Liberty Oil Mills Ltd. and others through Jawahar Lal Nehru custom house (JNCH), Mumbai between August and November 2004 were provisionally assessed at concessional rate of duty under the notification ibid in the absence of test reports establishing their eligibility for this benefit. The exemption benefit was Rs.3.70 crore.

On this being pointed out (August 2005), the Ministry stated (October 2005) that these imports were provisionally assessed under customs notification dated 1 March 2002 ibid at lower rate of duty on the basis of import and other documents submitted by the importer. There was no stipulation in the notification to test these imports for establishing these goods as crude only. They further stated that in all cases, goods were sent for chemical test and these provisional assessments are being finalised. Based on test reports, demand notices would be issued wherever required.

The reply of the Ministry is not tenable as concessional rate of duty was leviable only on crude palm oil of 'edible grade' for which chemical test was required, the fact substantiated by their own action while invariably sending all imports for testing. However, the fact remains that the imports made in 2004 were not yet finally assessed even after a lapse of two years despite six month's time limit having been prescribed.

Further scrutiny by audit revealed that test report received on 25 August 2004 in respect of another consignment imported in May 2004, established that beta carotene level was only 398.3 mg/kg rendering it ineligible for exemption benefit of Rs.11.16 lakh. Department failed to finalise assessment till date thereby giving unintended financial benefit of Rs.11.16 lakh plus interest to importer. Ministry while accepting the fact reported (October 2005) that a less charge demand for Rs.11.16 lakh has been issued.

Further progress was awaited (January 2006).

3.1.2 As per condition 35 of notification No.21/2002-cus dated 1 March 2002, crude sunflower oil upto an aggregate of one lakh and fifty thousand metric tonne of total imports of such goods in a financial year is eligible for concessional rate of duty.

Four consignments of 'crude sunflower oil' imported by M/s. Godrej Industries Ltd. in August 2004 were assessed (October 2004) provisionally at concessional rate of duty under

notification ibid. Audit scrutiny revealed that neither were test reports available determining classification of the goods as 'crude' nor was any record of aggregate import of such goods by the importer in the financial year maintained to monitor quantity restrictions. Since both conditions stipulated in the notification were unfulfilled, benefit of exemption granted was irregular. This resulted in short levy of duty of Rs.42.11 lakh.

Delay in finalisation of the above mentioned cases was also violative of provisional assessment rules, which provided for finalisation within six months.

On this being pointed out (August 2005), the Ministry reported (October 2005) that the cases are being finalised on the basis of test reports received.

The fact remains that even after a lapse of more than two years the provisional assessments were pending. Further progress was awaited (January 2006).

3.1.3 As per customs notification No.16/2000 dated 1 March 2000 (serial No.204), as amended, import of goods required for setting up of crude petroleum refinery are leviable to concessional rate of basic customs.

Two consignments of goods imported during April and May 2000 by M/s. Hindustan Petroleum Corporation Ltd., an existing refinery through air customs, Chennai were cleared at concessional rate of duty under notification ibid. Incorrect grant of exemption resulted in short levy of duty of Rs.7.05 lakh and interest thereon.

On this being pointed out (October and November 2000), the Ministry reported (November 2005) recovery of the duty of Rs.12.54 lakh including interest.

3.1.4 In terms of customs notification No.236/1989 (serial No.11) dated 1 September 1989, appendix-I thereto, phosphoric acid classifiable under CTH 2809.20 imported from countries specified in appendix ibid, other than South Africa was leviable to concessional rate of customs duty.

M/s. Indian Farmers Fertilisers Co-operative Ltd., New Delhi, imported from South Africa two consignments of phosphoric acid through customs house, Kandla and cleared them in January 2004. Goods were allowed exemption vide notification ibid, even though country of import i.e South Africa is not specified in the appendix ibid. Incorrect grant of exemption resulted in short levy of duty of Rs.8.36 lakh and interest of Rs.0.51 lakh.

On this being pointed out (June 2004), the Ministry reported (November 2005) recovery of the amount.

3.2 Incorrect application of exemption notification

Notification No.21/2002-cus and 06/2002-CE dated 1 March 2002 (serial No.156 and 87A) provides for import of 'light weight coated (LWC) paper' weighing up to 70 GSM by actual users for printing of magazines at concessional rate.

Thirty three consignments of 'LWC paper' import by M/s. Delhi Press Patra Prakashan Pvt. Ltd., and 25 others were imported between December 2004 and January 2005 through Delhi commissionerate. Department classified the goods under CTH 48102200 and assessed them by extending benefit of notifications ibid.

Audit scrutiny revealed that importers were eligible to import standard/glazed newsprints only, for printing of magazines classifiable under CTH 4801 as per registration certificates issued by the office of registrar of newspapers for India (RNI). Thus, incorrect grant of notification benefit to importers resulted in short levy of duty of Rs.1.35 crore. Besides this, in cases of three importers, registration certificate was also not found on record.

On this being pointed out (March/April 2005), the department stated (May 2005) that there was no condition of taking any type of undertaking or bond, surety etc for allowing notification benefit and that magazine publishers were registered with RNI. As general practice, the department has been obtaining copy of registration certificate issued by RNI to determine whether the importers were actual users or not and whether they were engaged in the publishing of magazines. The department further stated that the magazine editions/inserts of several newspapers were printed on LWC. The department's reply is not tenable as the RNI had specifically declared eligibility of type of paper to be imported as standard/glazed newsprint. Besides, the registration certificates supplied by the department with their reply ibid, confirms eligibility to import standard/glazed newsprint only.

Further progress was awaited (January 2006).

3.3 Other cases

In 19 other cases, objections were issued to the Ministry on incorrect grant of exemption involving short levy of Rs.41.54 lakh. The department admitted the objection in six cases involving Rs.16.74 lakh and reported recovery of Rs.16 lakh as per table below:

(Amount in lakh of rupees)

Sl. No.	Product on which exemption granted	Name of the importers M/s.	Amount short levied	Amount admitted	Amount recovered
1.	Integrated processing module	Grasim Industries Ltd.	4.66	4.66	4.66
2.	X-ray tubes	Steel Authority of India Ltd.	3.77	3.77	3.77
3.	Switches	Bharti Teletech Ltd. & two others	3.54	Not admited	--
4.	Stainless steel bars	Steellite Metal & Tubes & another	3.37	3.37	2.63
5.	Density meter	Alstom Projects (I) Ltd.	3.27	Not admited	--
6.	Computer software	Cyber Multimedia (I) Ltd.	2.61	Not admitted	--
7.	Test kits	Spectral Diagnostic (P) Ltd.	2.37	Not admitted	--
8.	Spare parts for gas chromatograph	Indian Acrylics Ltd. & another	2.25	Not admitted	--
9.	Motion picture raw film	Patel India Distributions (P) Ltd.	2.11	2.19	2.19

10.	LWC paper	Chhaya Deep News	1.87	Not admitted	--
11.	Galvanized steel sheets	L.G. Electronics (I) Pvt. Ltd.	1.77	Not admitted	--
12.	Stainless steel scrap	Lohia Metal	1.42	Not admitted	--
13.	Nickel & article of nickel	Surya Kiran Udyog (P) Ltd.	1.39	1.39	1.39
14.	Pokemon lenticular cards (toys)	Frito –Lay India	1.36	1.36	1.36
15.	Flint button refractive index	Pratiti Industries	1.31	Not admitted	--
16.	Scanners	Delhi University, North Campus & AIIMS	1.27	Not admitted	--
17.	Nickel alloy wire	Punjab Lighting Aids (P) Ltd.	1.14	Not admitted	--
18.	Strip cronifer II extra B, cold rolled	Daulat Ram Inernational	1.05	Not admitted	--
19.	Tools	Jindal Iron & Steel Co. Ltd.	1.01	Not admitted	--
	Total		**41.54**	**16.74**	**16.00**

CHAPTER IV: SHORT LEVY OF DUTY DUE TO UNDERVALUATION

4.1 Tariff values inconsistent with Board's own decision

Sub-section 2 of section 14 of Customs Act, 1962 stipulates that if the Central Government is satisfied that it is necessary or expedient so to do, it may, by notification in official gazette, fix the tariff value of any class of import or export goods having regard to the trend of value of such or like goods. Accordingly tariff values of brass scrap, palm oil and soyabean oil (all grades) were fixed by the Government from time to time.

In an earlier response, Ministry stated (December 2004) that tariff values were to be revised when computed value based on average international prices went beyond ten per cent of the tariff values (less or higher) in respect of palm oil/soyabean and five per cent in respect of brass scrap.

Audit scrutiny of 98 consignments of brass scrap/palm oil imported through JNCH, Mumbai and custom house, Kandla during August 2003 to January 2005 revealed that variation between invoice values and tariff values on which the goods were assessed ranged from six to thirty per cent resulting in under valuation of the consignments and consequent loss of revenue to the extent of Rs.1.25 crore.

On this being pointed out during April 2004 to June 2005, the Ministry stated (September 2005) that the goods were assessed with reference to tariff value fixed by the Government irrespective of invoice value.

The reply was not tenable being at variance with the Board's decision for revision of tariff values. Audit is of the view that pace of revisions needs to be commensurate with market trends.

4.2 Incorrect reckoning of foreign exchange rate

Section 14 of Customs Act, 1962 read with "explanation" appended to customs notification No.36/2001 (NT) dated 3 August 2001 as amended stipulates that the relevant date for determination of rate of exchange for the conversion of tariff value shall be the date of presentation of bill of entry under section 46 of Customs Act. Date of presentation of bill of entry for warehoused goods under section 46 of Customs Act is the date of filing the into-bond bill of entry.

One hundred and seventy five consignments of palmolein and palm oil imported through custom house, Chennai (sea) by M/s. Maharaja Industries and 26 others were warehoused and cleared during the period from December 2003 to June 2004. While converting tariff value in US dollar applicable for the goods, exchange rate on the date of filing the ex-bond bill of entry was reckoned instead of the exchange rate that prevailed on the date of filing the into-bond bill of entry. This resulted in incorrect computation of assessable value and consequential short collection of duty to the tune of Rs.98.83 lakh.

On this being pointed out (August to October 2004), the department/Ministry reported (November 2005) recovery of Rs.13.16 lakh in respect of 26 cases. Further 40 cases were under appeals with CESTAT/Commissioner (Appeals) and 79 time barred cases are under persuasive action. Further progress was awaited (January 2006).

4.3 Other cases

In four other cases, objections were issued to the Ministry on undervaluation involving short levy of Rs.8.59 lakh. The department admitted the objection in one case involving Rs.1.48 lakh as per table below:

(Amount in lakh of rupees)

Sl. No.	Name of product	Name of the importers M/s.	Amount short levied	Amount admitted	Amount recovered
1.	Caller ID phones	Bharti Systel	3.41	Not admitted	--
2.	Desktop computers	Apple Computers International (P) Ltd.	1.98	Not admitted	--
3.	Components for DVD player	BPL Sanyo (P) Ltd.	1.72	Not admitted	--
4.	Polished marble slabs	MTAR Technology (P) Ltd. & another	1.48	1.48	0.34
	Total		**8.59**	**1.48**	**0.34**

CHAPTER V: NON LEVY/SHORT LEVY OF ADDITIONAL DUTY

According to section 3 of CTA, 1975, any article which is imported into India shall also be liable to additional duty equal to the central excise (CE) duty for the time being leviable on a like article produced in India.

Short levy of additional duties amounting to Rs.36.04 lakh were reported to the Ministry in eight cases, as narrated below:

5.1 Non levy of additional duty due to incorrect grant of exemption

Notification No. 76/2004-cus dated 26 July 2004 provides that central processing unit with monitor, mouse and key board imported as a set are chargeable to additional duty under Computers (Additional Duty) Rules, 2004.

5.1.1 Four consignments of 'various computer parts' imported by M/s. Hewlett Packard India Ltd. and three others through Mumbai commissionerate in July/August 2004 were classified under CTH 8471 and assessed to concessional duty of CVD under the notification ibid. This resulted in non levy of additional duty of Rs.23.21 lakh.

On this being pointed out (August 2004), the Ministry admitted the objection and reported (October-December 2005) recovery of Rs.19.93 lakh in three cases. Reply in the remaining case was awaited (January 2006).

5.1.2 In terms of notification No.94/96-cus dated 16 December 1996, re-importation of goods exported under duty exemption entitlement certificate (DEEC) attracts additional duty of customs equivalent to CE duty leviable at the time and place of importation of goods and SAD. However, in case of manufacturer-exporter, payment of CE duty may be deferred on execution of transit bond with customs authority specifying that CE duty payable at the time of importation shall be paid as and when the said goods are removed for home consumption, besides de-logging of the shipping bill from DEEC.

M/s. Tega Industries Ltd., Kolkata had initially exported a consignment of 'rubber plate and rubber conveyor belt including elastocer' under DEEC scheme in January 2002 and subsequently re-imported the same in December 2003 through custom house, Kolkata (port). On the basis of transit bond executed by the importer, department allowed clearance of the goods without levying any duty. The importer did not submit the re-warehousing certificate from the central excise authority within the stipulated period of six months from the date of importation. As such the unit was liable to pay additional duty of customs of Rs.3.89 lakh and SAD of Rs.1.13 lakh.

On this being pointed out (June 2004), the Ministry reported (January 2006) that a show cause notice has been issued demanding CVD and SAD. Further progress was awaited (January 2006).

5.2. Other cases

In three other cases, incorrect application of rate, incorrect classification, incorrect computation resulted in short levy of additional duty of Rs.7.81 lakh of which two cases involving Rs.6.80 lakh were admitted and recovery of Rs.5.18 lakh in one case was reported by the department, as per details below:

(Amount in lakh of rupees)

Sl. No.	Details of product	Irregularity	Amount short levied	Amount admitted	Amount recovered
1.	Dry wipe marker ink	Non levy of CVD	5.18	5.18	5.18
2.	Video games	Incorrect grant of exemption	1.62	1.62	--
3	Laboratory equipments	Misclassification	1.01	Not admitted	--
	Total		**7.81**	**6.80**	**5.18**

CHAPTER VI: DUTY EXEMPTION SCHEME

6.1 Duty Entitlement Passbook (DEPB) Scheme

DEPB Scheme was introduced with effect from 1 April 1997 in Exim Policy 1997-2002 with objective to neutralise the incidence of customs duty on the import content of export product which was provided by way of grant of duty credit. Exporter could apply for credit, at specified percentage of free on board (FOB) value of exports, made in freely convertible currency against such export products and at such rates as may be specified by DGFT by way of public notice issued in this behalf, for import of raw materials, intermediates, components, parts, packaging material etc. Holder of DEPB has the option to pay additional customs duty, if any, in cash.

Test check of records of 19 out of 23 regional licensing authorities (RLA) covering 11 States for the years 2002-2005 revealed the following:-

6.1.1 Duty credit not related to actual incidence of duty

DEPB credit is allowed on basis of standard input output norms (SION) regardless of whether that particular industry imported any goods at all to manufacture the export product.

Test check revealed that in 1237 licences of exports items namely fish products, zinc ingots, zinc concentrate etc; issued by RLA Hyderabad, Visakhapatnam, Jaipur, Ludhiana, Amritsar, Mumbai and Ahmedabad, exporters needed little or no imported material but were granted credits of Rs.48.82 crore based on DEPB rates which were not related to actual incidence of duty.

On this being pointed out (June 2005), RLA, Hyderabad, Jaipur and Visakhapatnam stated that it being policy matter would be taken up with DGFT, New Delhi. Replies from remaining RLAs were awaited (January 2006).

6.1.2 Unintended benefit of DEPB credit

In terms of para 4.31 of Exim Policy (2002-2007) read with para 4.3.7 of handbook of procedures (HBP) Vol-I (2002-2007), duty credit under the scheme shall be calculated by taking into account deemed import content of the said export product as per SION and BCD payable on such deemed imports. Value addition (VA) achieved by export of such product shall also be taken into account while determining rate of duty credit. In the case of marine product (66/2), leather (64/4, 64/7) and textiles (89/16) scrutiny showed that DEPB credit rate was not revised according to the change in the rate of BCD. This resulted in unintended benefit to 3140 licencees amounting to Rs.20.48 crore.

6.1.3 Non/short realisation of export proceeds

As per para 7.38 of HBP-Vol-I (1997-2002) read with para 4.45 of HBP-Vol-I (2002-2007), if export proceeds are not realised within six months from date of export or such extended period as may be allowed by the reserve bank of India (RBI), DEPB credit allowed shall be recovered from exporter in cash with interest. In case of proportionate realisation, proportionate credit attributable to non realised export proceeds shall be recovered in cash.

In 221 licences issued by RLAs, Hyderabad, Jaipur, Ludhiana, Mumbai and Ahmedabad export proceeds of Rs.177.32 crore were not realised within the prescribed period. As such DEPB credit of Rs.21.78 crore and interest was recoverable from the licencees.

On this being pointed out (June 2005), RLA, Hyderabad while accepting the observation advanced shortage of staff as reasons for inability to monitor cases every month and said that complete information was being collected. RLA Ludhiana accepted the observation and stated that further reply would follow.

However, Minstry in their response (September 2005/January 2006) to seven cases of Mumbai reported recovery of Rs.1.81 lakh in two cases, surrender of unutilised DEPB by one licencee and submission of foreign exchange by another licencee and remaining three cases have been referred to Revenue authority. RLA Jaipur reported recovery of Rs.0.32 lakh in seven cases. Further progress was awaited (January 2006).

6.1.4 Excess grant of DEPB credit due to incorrect fixation/incorrect application of credit rate

Audit scrutiny revealed that in 4835 licences issued by RLA, Ahmedabad, Bangalore, Ludhiana, Kochi and Thiruvananthapuram, incorrect computation of FOB value/incorrect fixation/ incorrect application of credit rates resulted in grant of excess DEPB credit amounting to Rs.126.59 crore.

On this being pointed out (June 2005), RLA, Ludhiana while accepting the fact stated that detailed reply would be furnished.

RLA Ahmedabad stated (September 2005) that the licencees had been correctly allowed DEPB credit. The reply is not tenable as the licencee were granted excess DEPB credit by applying higher rate for the export product out of two different credit rates prevalent at that time. Reply from RLA, Bangalore, Kochi and Thiruvananthapuram were awaited (January 2006).

6.1.5 Grant of credit to items not specified in DEPB rate list

DEPB credit of Rs.41.47 lakh in seven licences was granted by RLA, Bangalore and Ahmedabad for exports products namely 'internal combustion engine parts (serial No.61/455)', 'polyester cotton blended grey fabrics with polyester content more than 50 percent by weight (serial No.89/53 (a)' not covered under DEPB rate list.

This was pointed out in June 2005, the department's reply was awaited (January 2006).

6.1.6 Irregular grant of exemption of education cess on DEPB clearance

In terms of section 91, 92 and 94 of Finance (No.2) Act, 2004 (23 of 2004), 'education cess' is leviable as duty of customs on all imported goods with effect from 9 July 2004 at the rate of two per cent of the aggregate of duties of customs and any sum chargeable on such goods under any other law for the time being in force. Further, in terms of notification Nos.104/95-cus dated 30 May 1995, 45/2002-cus dated 22 April 2002 and 69/2004-cus dated 9 July 2004 import made under DEPB Scheme may be exempted from BCD, additional duty and SAD by making corresponding debit from DEPB. However, the said notification does not provide for debit of education cess from DEPB and so the same has to be collected in cash or cheque.

On imports of 310 consignments of 'crude palm oil, carbon, graphite bricks, coating material etc.' under DEPB by M/s. Jhunjhunwala Vanaspati Ltd., Varanasi and other importers

through custom houses at Kolkata (sea), Tuticorin, Chennai (sea) and Mumbai (sea) between August 2004 and February 2005, department debited both BCD and education cess from DEPB under notifications ibid. Since there was no provision for setting off education cess from DEPB such debit was irregular to the extent of grant of exemption of education cess of Rs.2.40 crore.

On this being pointed out between October 2004 to May 2005, the Ministry in respect of 262 consignments stated (September 2005 to December 2005) that education cess was debited from DEPB as per customs circular No.5/2005 dated 31 January 2005. Reply of the Ministry is not tenable because customs duty can be exempted only through notification and not through a circular.

Meanwhile, in respect of 30 consignments wherein education cess was neither debited from DEPB nor paid in cash, the Ministry reported recovery of Rs.14.37 lakh and issue of demand notices in remaining ten cases.

6.1.7 Grant of excess DEPB credits

As per para 4.38 read with appendix 10A of HBP 2002-2007 Vol-I while fixing DEPB rates BCD and SAD paid on imported inputs for manufacture of export goods are considered. Vide notification No.6/2004-cus dated 18 January 2004, levy and collection of SAD was withdrawn from all imported goods with effect from 9 January 2004. DEPB rates were, however, revised with effect from 9 February 2004 vide public notice No.47 (RE-2003)/2002-2007.

Audit scrutiny of records of regional Jt. DGFT (licensing authority) Ludhiana and Amritsar revealed that in 69 cases (47 Ludhiana and 22 Amritsar) of licences issued after 9 February 2004, DEPB credit at old rates to the extent of Rs.3.35 crore was allowed which included Rs.1.15 crore on account of exempted SAD.

On this being pointed out (September/December 2004), the licensing authority Ludhiana (November 2004) stated that DEPBs were issued applying rates applicable on the date of let export order, while licensing authority at Amritsar (December 2004) stated that DEPB certificates had been correctly issued as per notification. Reply of the department was not tenable as let export date in these cases was after 9 February 2004. It was therefore incorrect to include element of SAD in DEPB.

In another case, M/s. Steel Authority of India Ltd., imported six consignments of various goods namely 'sea water magnesia, top bottom pinion, taper roller bearing, mechanical spares made of iron and steel and roasted molybdenum ore and concentrates' through Kolkata (sea) customs between August 2004 and February 2005 under the notification ibid. Although credits available in these were not sufficient to cover duties leviable, department allowed partial debit to DEPBs and balance payment of duties through cheque or by debiting personal ledger accounts, in contravention of the provision of the notification ibid. This resulted in irregular grant of exemption to the tune of Rs.29.55 lakh.

On this being pointed out (May 2005), the department stated (June 2005) that importer had option either to pay full duty through DEPB debit or to pay partly by cash under DEPB scheme. Reply of the department is not tenable because proviso to condition (3) (iii) of the notification requires that benefit of exemption from duty shall not be admissible if there is insufficient credit in the DEPB for debiting duty leviable on the goods but for this exemption.

In these cases credit available in DEPBs was insufficient for effecting debit. Hence notification leaves no scope for partial debit from the DEPB in the absence of sufficient credit therein and partial payment by cash.

6.1.8 Incorrect grant of credit under DEPB scheme

According to Board circular No.26/2002 dated 16 May 2002, exporter who availed benefit of customs notification No.32/1997 dated 1 April 1997 which provided for exemption to goods imported for execution of export order for jobbing, was not entitled to credit under DEPB Scheme.

Thirty four consignments of 'printing machinery parts' exported during March 2001 to January 2003 by M/s. Craftsman Automation Pvt Ltd., were allowed credit under DEPB even though benefit in terms of notification ibid was availed by the exporter. This had resulted in incorrect grant of DEPB credit of Rs.93.41 lakh which was recoverable.

On this being pointed out (March 2003), the licensing authority stated (March 2004) that declaration in terms of notification No.32/1997 was obtained from the firm by the customs authority and the matter pertained to them. Reply was not acceptable since DEPB credit was allowed by the licensing authority and appropriate safeguards should have been in place. Moreover, Ministry of Finance vide their circular dated 27 August 2002 had reiterated that due care needed to be taken to ensure that such unintended/double benefit in the form of duty free imports and DEPB benefit at the time of export were not availed of by unscrupulous exporters. Further progress was awaited (January 2006).

Further, as per para 4.42 of HBP of Exim Policy 2002-2007, credit under DEPB may be utilised for payment of customs duty on any item, which is freely importable except capital goods. Para 9.10 of the HBP ibid defines capital goods as any plant, machinery, equipment or accessories required for manufacture or production, either directly or indirectly, of goods or for rendering services, including those required for replacement, modernisation, technological upgradation or expansion.

M/s. Steel Authority of India Ltd, Rourkela imported three consignments of 'secondary reformer burner assembly, welding transformer and control unit etc' under DEPB in September and November 2002 through custom house, Kolkata (sea). However, imported goods being capital goods in terms of para 9.10 of the HBP were not eligible for the exemption. This resulted in incorrect grant of exemption under DEPB amounting to Rs.25.86 lakh.

On this being pointed out (June and July 2003), the department issued demand notice for Rs.23.86 lakh in respect of one consignment in August 2004). Reply in remaining was awaited (January 2006).

6.1.9 Non-imposition of restriction on DEPB clearance

As per para 4.46 of HBP of 2002-2007 effective from 1 April 2002, the CIF value of imports effected under DEPB shall not exceed FOB value against which DEPB certificate has been issued. Further, in terms of clarification of Ministry of Commerce under policy circular dated 9 August 1999, in cases where clearance is sought after clubbing different DEPBs, FOB value taken for restriction should be proportionate to credit availed against such DEPBs by the importer. Thus, in case of clubbing of two or more DEPBs in respect of clearance of

single consignment, proportionate FOB value of each certificate is to be calculated separately and sum total of FOB value so calculated should not exceed the CIF value of import of the said consignment for allowing benefit of debiting duty from DEPB credit,

Audit scrutiny revealed that ten consignments of coking coal imported by M/s. Tata Iron and Steel Industries Ltd., Mumbai clubbing 31 different DEPBs between December 2002 and May 2003 through commissionerate of central excise and customs, Bhubaneswar-I were allowed DEPB benefit without applying restriction on CIF value of import against FOB value of the DEPB certificate either in single use or in case of clubbing of different DEPB certificates in single consignment as per circular ibid. Non-imposition of restriction on such DEPB clearance resulted in undue financial benefit of Rs.2.08 crore.

On this being pointed out (October 2004), the department stated (December 2004) that the DEPB scrips had been debited from FOB value of exports till the balance of DEPB credit or FOB value got exhausted. The department's reply is not tenable being contrary to the policy circular ibid.

Further progress was awaited (January 2006).

6.1.10 Other cases

Thirteen other cases of excess DEPB credit of Rs.57.65 lakh were pointed out, of which department accepted eight cases as per table below:

(Amount in lakh of rupees)

Sl. No.	Irregularity	Licensing authority	Amount objected	Whether accepted
1.	Non application of DEPB rates on date of let export order	Hyderabad Ludhiana, Jaipur	16.72	Yes
2.	Excess grant of DEPB due to misclassification	Pune	10.63	No
3.	Excess grant of DEPB due to misclassification	Coimbatore	6.36	Yes
4.	Exemption from anti dumping duty under DEPB scheme	Kolkata	7.08	Yes
5.	Credit allowed on inappropriate documents	Ahmedabad	1.15	--
6.	Grant of DEPB after expiry of prescribed period	Visakhapatnam Ahmedabad	4.39	No
7.	Non application of late cut	Ahmedebad Jaipur	2.48	Yes
8.	Incorrect utilisation of DEPB scrip	Chennai	2.17	Yes
9.	Excess grant of DEPB credit	Mumbai	1.84	Yes
10.	Non application of late cut	Mumbai	1.69	No
11.	Foreign exchange less realized	Jaipur	1.31	--
12.	Excess grant of DEPB credit due to non application of value cap	New Delhi	1.23	Yes
13.	Excess DEPB credit due to excess agency commission	Hyderabad	0.60	Yes
	Total		**57.65**	

6.2 Export Promotion Capital Goods (EPCG) scheme

Non fulfilment of EO

According to para 6.2 of Exim Policy 1997-2002, capital goods may be imported at concessional rate of customs duty subject to fulfilment of specified EO. Further as per 6.19 of the policy ibid, in the event of failure to fulfil EO, the licencee was liable to pay customs duty plus interest thereon.

6.2.1 M/s. Suvarna Apparels and Fashion Exports Ltd., Hyderabad, a 100 per cent EOU under Visakhapatnam export processing zone (VEPZ) was allowed to debond during May 1998 by concerned development commissioner with permission to switch over to EPCG scheme. Jt.DGFT, Hyderabad, accordingly, issued EPCG licence (May 1998) at zero rate of duty for CIF value of Rs.8.61 crore representing depreciated value of capital goods imported under EOU scheme against export of goods valued at Rs.52.93 crore. Duty saved on depreciated value of capital goods transferred was Rs.2.76 crore.

As licencee failed to produce any documentary evidence towards fulfilment of EO during obligation period, he was liable to pay customs duty of Rs.2.76 crore and interest of Rs.2.86 crore upto March 2005.

On this being pointed out (April 2004), Jt.DGFT, Hyderabad while accepting the fact stated (May 2005) that licencee had since been declared defaulter. Further progress was awaited (January 2006).

6.2.2 M/s. Suditi Industries was issued zero per cent EPCG licence in June 1998 to import capital goods worth Rs.3.41 crore (US$ 16,27,894) and EO was fixed at US $ 51,19,615 with average export to be maintained at US $ 73,61,251.

Audit scrutiny revealed that though licencee had fulfilled EO they had failed to maintain average export level during the licence period. Thus, customs duty saved on imported goods amounting to Rs.1.25 crore was recoverable in terms of provisions ibid.

On this being pointed out (August 2004), the DGFT issued show cause notice (SCN) to the licence holder (September 2004) and adjudicated the case in October 2004 by levy of fiscal penalty of Rs.3.69 crore under section 13 of FT (DR) Act, 1992. The department further stated (March 2005) that case had been referred to district collector for recovery of dues. Details of recovery of duty were awaited from the customs department (January 2006).

6.2.3 An EPCG licence was issued (November 1998) to M/s. Phil Corpn. Ltd., Mumbai to import capital goods worth Rs.99.45 lakh with EO of Rs.59.67 crore. The licencee utilised licence in full, but failed to produce any evidence either for fulfilment of EO or for extension for any particular block years. As such they were liable to pay customs duty exempted amounting to Rs.47.44 lakh plus interest of Rs.46.25 lakh.

On this being pointed out (March 2004), department intimated that (August 2004) case had been referred to district collector for recovery of fiscal penalty amounting to Rs.1.34 crore.

Further progress was awaited (January 2006).

6.2.4 M/s. Sai Agri International (P) Ltd., Kakinada was issued EPCG licence to import capital goods under zero duty EPCG scheme valuing Rs.1 crore (February 1999) with EO of Rs.5 crore to be discharged within eight years in four blocks from the date of issue of licence. Audit scrutiny revealed that licencee failed to make any exports during the first two blocks ending February 2003 and consequently became liable to pay proportionate duty on imports made alongwith interest.

On this being pointed out (May 2003), RLA, Visakhapatnam admitted the objection and stated (March/May 2005) that the licencee actually imported goods valued Rs.67.06 lakh involving customs duty of Rs.29.86 lakh between February and August 1999 but failed to make any exports. The licensing authority further stated that customs authorities, Chennai, had enforced bank guarantee and realised (April 2005) entire customs duty of Rs.29.86 lakh and also stated that further progress on recovery of interest would be intimated. Report on recovery of interest of Rs.27.48 lakh was awaited (January 2006).

6.2.5 M/s. Mitsu Industries was issued licence under ten per cent EPCG Scheme in March 1999 to import capital goods for CIF value of Rs.1.26 crore (US$ 2,95,596) with EO of US$ 11,82,384 (i.e. 4 times CIF value). Annual average export of US$ 2.07 crore was required to be maintained.

Audit scrutiny revealed that licencee fulfilled EO during the period March 1999 to November 2000. Hence, licencee was required to maintain average exports also for 1998-99 and 1999-2000 (till November 2000). Adopting average export performance (AEP) of US$ 2.07 crore per annum, target was US$ 3.46 crore for the period from 1998-1999 till November 2000. Licencee however, achieved AEP of US$ 1.22 crore. Jt.DGFT had redeemed the licence. Entire duty saved amounting to Rs.40.65 lakh was required to be recovered from the licencee alongwith interest of Rs.39.13 lakh.

On this being pointed out (January 2005), Jt.DGFT stated (February 2005) that demand cum SCN was issued on 3 February 2005. Customs department also intimated (April 2005) that SCN demanding duty amounting to Rs.40.65 lakh and interest thereon was issued in April 2005.

Further progress was awaited (January 2006).

6.2.6 M/s. Schefields Ltd., Kolkata was issued EPCG licence in February 1999 by Zonal Jt.DGFT, Kolkata for import of 'ball pen manufacturing machine' at concessional rate of duty against EO of US$3.22 lakh to be achieved in five years. This obligation was over and above maintaining annual average of past exports of US$87362 per year. Against import of capital goods valuing Rs.34.33 lakh in April 1999, the licencee exported goods worth US$3.79 lakh during February 2000 to February 2001. However, AEP during February 1999 to January 2000 and February 2000 to January 2001 was US$33244 and US$49761 respectively, which was less than the AEP prescribed. Licencee was liable to pay duty foregone amounting to Rs.16.31 lakh alongwith interest of Rs.14.67 lakh thereon on failure to maintain average EO.

On this being pointed out (January 2003), zonal Jt. DGFT stated (August 2004) that EO had been fulfilled as per the statement of the firm. Reply was not tenable since verification of record furnished by the firm revealed that three export consignments amounting to US$78453 and two amounting to US$52282 shown towards fulfilment of average EO during the periods February 1999 to January 2000 and February 2000 to January 2001 respectively had already

been utilised towards fulfilment of two other EPCG licences. Reutilisation of the same exports towards fulfilment of different EOs as well as average export performance was not in order.

Further progress was awaited (January 2006)

6.2.7 A ten per cent EPCG licence was issued to M/s. KFA Corporation to import capital goods of CIF value Rs.17.43 lakh (US$ 2,75,000) and EO was fixed at rate of US$ 11,00,000. The capital goods were imported in January 1999.

Audit scrutiny revealed they were installed on 20 November 1999. As such exports made prior to date of installation would not qualify for counting towards fulfilment of EO. However, Jt.DGFT did not exclude exports made by licencee for the period prior to installation of capital goods before allowing redemption. Grant of redemption of licence was therefore not in order and duty saved amounting to Rs.30.83 lakh was required to be recovered alongwith interest thereon.

On this being pointed out (November 2004), Jt.DGFT intimated (April 2005) that demand notice was issued in January 2005. Customs department also accepted the stand taken by audit (September 2005).

6.2.8 M/s. Jaymex was issued licence under ten per cent EPCG Scheme in November 1999 to import capital goods for CIF value of Rs.51.61 lakh (US$ 120029) with EO US$ 4,80,116 and annual AEP to be maintained at US$ 8,02,297.

Audit scrutiny revealed that against prescribed AEP of US$ 16,04,594 the licencee could maintain AEP of US$ 9,14,536 only during the period 1999-2000 and 2000-01 resulting in shortfall of US$ 6,90,058. Thus he was liable to pay duty saved of Rs39.34 lakh including interest. However, it was observed that Jt.DGFT redeemed the licence without recovering amount due from the licencee.

On this being pointed out (March 2005), the department stated that action was being initiated. Further progress was awaited (January 2006).

Failure to monitor EO

In terms of para 6.11 (a) of HBP, Vol-I, 1997-2002, the licence holder under EPCG Scheme shall fulfil year wise EO within a period of five years from the date of issue of licence. In the event of failure to to do so for three consecutive years, he is liable to pay customs duty on the entire amount along with interest.

6.2.9 M/s. Suryavarada Spinning Mills Ltd., Dharapuram, was issued (June 1997) a licence for CIF value of Rs.1.93 crore under ten per cent EPCG scheme with an obligation to export cotton yarn of 41 counts and above, and earn foreign exchange of US dollar 21,49,648 within five years from date of issue of licence. They imported (December 1997) second hand machinery for value of Rs.1.99 crore but failed to manufacture and export yarn during EO period. No action was initiated by the department to demand duty liability with interest immediately after expiry of third year (June 2000) of EO. After delay of about three years, SCN was issued (April 2003) by licensing authority and no further follow up action was initiated to recover the dues. This resulted in locking up of revenue to the tune of Rs.1.01 crore including interest.

On this being pointed out (February 2004), the licensing authority stated (December 2004) that the firm was placed under denied entity list and that the customs department was informed by Jt.DGFT, Coimbatore to collect customs duty with interest and also to forfeit the bank guarantee executed by the firm. Consequently, the bank guarantee was forfeited by the customs department and Rs.40 lakh was realised in December 2004. However, the recovery particulars for the balance amount of Rs.60.60 lakh were awaited (January 2006).

6.2.10 M/s. Bipin Exports, Tiruppur was issued (April and July 1997) two licences under ten per cent EPCG Scheme for CIF value of Rs.21.01 lakh and Rs.22.37 lakh with an obligation to export embroidered cotton hosiery garments and earn foreign exchange to the extent of US dollar 2,34,068 and US dollar 2,48,644 respectively within a period of five years. The licencee imported (April 1997 and January 1998) embroidery machine valued at Rs.21.68 lakh and Rs.21.73 lakh against the licences. EO period expired on 30 April 2002 and 1 July 2002 respectively. Licence holder, however, failed to discharge minimum of 25 per cent of EO as required under the licence for three consecutive year period ended on 30 April 2000 and 1 July 2000 respectively. Therefore action to recover whole of the duty of customs alongwith interest should have been taken forthwith. Licensing authority, however, issued (March, April 2003) SCN to the licence holder for non fulfilment of EO after a delay of over three years. No further follow up was taken to recover duties alongwith interest, which led to blocking up of revenue to the tune of Rs.23.36 lakh including interest.

On this being pointed out (March 2004), the licensing authority placed (December 2004) the firm under denied entity list and requested commissioner of customs, Chennai (sea) to collect customs duty with interest thereon and also to forfeit the bank guarantee executed by the firm. However, customs department is yet to recover the amount (January 2006).

6.2.11 Non fulfilment of EO due to incorrect reckoning of exports

In terms of para 6.5 (i) of Exim Policy 1997-2002, as amended, the EO under EPCG scheme shall be fulfilled by export of goods manufactured or produced by using the capital goods imported under the scheme. Para 6.19 of HBP, Vol-I of Exim Policy provides that the licence holder shall pay the duties of customs with interest in the event of failure to fulfil EO.

M/s. Saran Garments, Tiruppur was issued (May 1998) licence under EPCG scheme for CIF value of Rs.1.36 crore for import of circular knitting machine with an obligation to export knitted garments for a total value of US$ 25,64,947. The machinery was imported in June 1998. Though licencee exported goods for a total value of US$ 25,69,142 (February 2001) exports of the value of US$ 2,53,164.22 were made prior to the date of import of machinery. Thus there was shortfall in EO to the extent of US$ 2,47,966.52 and the licencee was liable to pay the duties of customs of Rs.1.07 crore including interest.

On this being pointed out (December 2004), the department stated (December 2004) that as per para 6.5.1 of Exim Policy, EO could be fulfilled by goods manufactured in different manufacturing units of the licence holder which implied that the export goods need not be produced out of the imported machinery. Reply of the department was not tenable because para 6.3 (a) of the Exim Policy 1992-1997 provides that capital goods imported by the licence holder shall be installed at the factory of the licence holder or his supporting manufacture(s)/ vendor(s). In the instant case, the capital goods were imported during June 1998. Exports prior to that would not count for fulfilment of EO since they were neither produced by use of imported machinery by licence holder nor by his supporting manufacture(s)/vendor(s).

6.2.12 Irregular grant of exemption under EPCG scheme

Para 5.1 of Exim Policy 2002-2007 read with customs notification No.55/2003 dated 1 April 2003 as amended stipulates that import of capital goods under EPCG scheme for pre-production, production and post production (including CKD/SKD thereof as well as computer software systems) at concessional rate of duty is permissible subject to fulfilment of prescribed EO within stipulated period of eight years reckoned from date of issue of licence. Para 4 of customs notification ibid however provided that capital goods imported or assembled are to be installed in importer's factory or premises and certificate to this effect should be produced from the jurisdictional deputy/assistant commissioner of central excise, within six months from the date of completion of imports or within such extended period as the said deputy/assistant commissioner of central excise may allow.

M/s. Hy-Grade Pellets Ltd., Visakhapatnam was issued EPCG licence in January 2004 by Jt.DGFT, Visakhapatnam to import 'electric resistance welded (ERW) pipes' with an EO to export 'iron ore pellets' equivalent to eight times of duty saved on goods imported. Licence holder imported ERW pipes in two consignments and cleared the same in February 2004 and April 2004 through Customs House, Visakhapatnam. Customs duty to the extent of Rs.13.85 crore was saved. Pipes imported were installed between their beneficiation plant (mine site) at Kirundal in Bailadila (Chattisgarh) and pelletisation plant (manufacturing unit) at Visakhapatnam (A.P.) for transportation of iron ore fines in the form of slurry for manufacture of export product ie, iron ore pellets.

Licence to import was issued in January 2004 on basis of the declaration of factory premises as Visakhapatnam. However, based on his request licence was amended in April 2004 by changing place of installation of imported goods as 'Bailadila (beneficiation plant) to Visakhapatnam (pelletisation plant).' This was after goods had been cleared. Thus, it was evident that imported goods were allowed to be installed outside the importer's factory or premises in violation of the condition of notification.

Commissioner of Customs, Visakhapatnam had made a reference to Board for clarification on the issue of installation of 'capital goods', in response to which it clarified in October 2004 that so long as the imported ERW pipes had been installed for the purpose for which they had been imported and installation certificate was produced by the licence holder, the technical aspect of capital goods not having been installed within specified licensing premises could be overlooked. Consequently, commissioner of customs, Visakhapatnam also opined that this case should not be taken as a precedent for future imports. Import of this item was clearly against provisions of Exim Policy and conditions of the notification. Irregular extension of benefit in this case thus resulted in loss of duty amounting to Rs.13.85 crore besides interest.

On this being pointed out (February 2005), the department contended that (i) benefit under the notification was granted based on the licence issued by the Jt.DGFT, Visakhapatnam (ii) installation of ERW pipes in the factory premises was as per notification and was in order (iii) the Board clarified (October 2004) that since ERW pipes are required for transportation of iron ore fines in the form of slurry from the mine site at Bailadila to the factory at Visakhapatnam, which is a pre-production operation for manufacture of iron ore pellets, it qualified as capital goods.

Reply of the department was not tenable as (i) the notification ibid specifically provides that capital goods imported should be installed in the importer's factory or premises whereas

pipes were laid outside 'factory premises' connecting beneficiation plant at Bailadila (mines site) and pelletisation plant at Visakhapatnam (factory site) covering enroute distance of 267 kms in four States viz, Chattisgarh, Madhya Pradesh, Orissa and Andhra Pradesh which cannot be construed as 'part of the factory' or 'premises' of the importer. In this context, reference is made to judgement of Supreme Court in the case of C.C.E, Jaipur vs. J.K. Udaipur Udyog Ltd., reported in 2004 (171) ELT 289 (SC) wherein Apex Court referring to definition of 'factory' as per section 2 (e) of Central Excise Act, 1944, has clearly held that mine connected to factory by ropeway for carrying excavated raw materials could not be considered as part of factory since no manufacturing activity was undertaken therein. The ropeway is merely a device or mechanism for transporting limestone. On the same analogy pipes were mechanism for transportation, not installed in the assessee's premises.

Further progress was awaited (January 2006).

6.3 Export oriented units (EOU) scheme/export processing zones (EPZ) scheme

6.3.1 Non utilisation of imported goods in export

Notification No.53/97-cus (now 52/03 dated 31 March 2003) as amended from time to time, exempts specified goods that are imported into India from whole of duty of customs and additional duty, if any, leviable thereon, provided they are used for purposes of manufacture of articles for export or for being used in connection with production or packaging or job work for export of goods or services by EOUs.

M/s. Sandoz Pvt. Ltd., an export oriented unit was issued letter of permission (LOP) in January 2000 under 100 per cent EOU scheme for manufacture of celphalosporins, their intermediates and bulk drugs.

Audit scrutiny revealed that it received insurance amount of Rs.1.97 crore for loss of goods in fire in the unit on 17 October 2002. Cost of raw material destroyed in fire was declared at Rs.1.87 crore. Since raw material imported was not used in the final product, duty of Rs.1.06 crore needed to be recovered from the importer.

On this being pointed out (August 2004), the department issued demand notice to the unit (September 2004). Further progress was awaited (January 2006).

6.3.2 Excess grant of central sales tax (CST)

In terms of para 9.14 of Exim Policy read with para 9.29 and appendix 43 of HBP 1997-2002, EOUs are entitled to full reimbursement of central sales tax (CST) paid by them on purchases made from domestic tariff area (DTA) for production of goods meant for export subject to following conditions:

i) supplies from DTA to EOU must be utilised by them for production of goods meant for export and may include raw materials, components, consumables, packing materials, capital goods, spares, material handling equipment etc. on which CST has been actually paid by EOUs.

ii) while dealing with application for reimbursement of CST, development commissioner shall see inter-alia that purchases are essential for production of goods meant for export and/or to be utilised for export production by the units.

Further, para 9.9. of Exim Policy 1997-2002 provides that entire production of EOU unit is to be exported subject to the relaxation that 50 per cent of the FOB value of exports may be sold in DTA on payment of applicable duties and on fulfilment of minimum net foreign exchange earning as percentage of exports (NFEP) by the unit.

During audit of development commissioner, Visakhapatnam special economic zone (VSEZ), it was observed that two 100 per cent EOU units viz, (i) M/s. Tata Coffee Ltd., and (ii) M/s. Sanghi Spinners India Ltd., were sanctioned and reimbursed CST amounting to Rs.4.34 crore on raw materials/consumables procured/utilised by them in entire production during January 2001 to September 2003. These two units were permitted to sell 50 per cent of the FOB value of exports in DTA. Grant of CST on entire production of goods instead of restricting it to export production resulted in excess grant to the extent of Rs.1.45 crore.

On this being pointed out (May 2004), the development commissioner, VSEZ stated (June 2005) that as per CST guidelines, there is no such restriction for reimbursement of CST in proportion to value of inputs used in export production. Hence CST is reimbursed wherever it is paid on the inputs used in the production by the EOUs and DTA sale is allowed subject to payment of applicable duties which is generally on high side when compared to the duties payable on the goods produced by DTA unit.

Reply of department is not tenable as reimbursement of CST is admissible only in respect of goods meant for actual export and not so in respect of goods produced/meant for domestic sale. Further, effective rates of duties levied on DTA sales made by 100 per cent EOUs under section 3 of Central Excise Act are far less than the duties chargeable on direct imports. Duty structure of domestically produced goods is not comparable with the duties chargeable on DTA sales as goods produced and cleared from 100 per cent EOUs stand on par with imported goods.

6.3.3 Non achievement of NFEP

Hundred per cent EOU is required to manufacture and export entire manufactured product and fulfil the EO annually as well as cumulatively and execute legal undertaking to the effect that in event of failure to fulfil the EO within stipulated time, it shall be liable to pay customs duty on imported duty free capital goods, raw materials, consumables, and components etc. alongwith interest at the rate of 24 per cent per annum from the date of import to the date of payment of duty, besides penalty imposable under FTDR Act, 1992. Further, in terms of para 9.5 and para 9.2.9 of Exim Policy 1997-2002, it is required to achieve NFEP which is calculated annually and cumulatively for the entire period of five years from commencement of commercial production.

Scrutiny of export performance of M/s. R.G.B. Garments Pvt. Ltd., Kolkata, a 100 per cent EOU under the Falta special economic zone (FSEZ) revealed that LOP was issued to it in September 1997 to manufacture 60 lakh pieces of garments made from viscous fibre and other material with EO of US$ 3,540,000 to be achieved in five years. The unit failed to do so and its NFEP performance stood at negative 399.27 per cent during the five year period. It was liable to pay duty foregone of Rs.10.54 lakh on imports of Rs.88.32 lakh {Rs.63.69 lakh (capital goods) + Rs.24.63 lakh (raw material)} and interest of Rs.14.28 lakh (from the date of import upto 31 March 2004).

On this being pointed out (April 2002), development commissioner, FSEZ stated (March 2004) that penalty of Rs.10000 was imposed on the basis of exim performance of the unit during and upto 2000-01 and the unit had deposited the amount in February 2002. The unit was further imposed penalty of Rs.1 lakh for non-achievement of NFEP during 2002-03. Reply regarding recovery of custom duty of Rs.10.54 lakh and interest of Rs.14.28 lakh was awaited (January 2006).

6.3.4 Non maintenance of separate records for indigenous and imported raw materials

Notification No.8/1997-CE dated 1 March 1997 exempts finished products, rejects and waste produced or manufactured in scrap or FTZ wholly from raw materials produced or manufactured in India, and allowed to be sold in India from so much of the duty of excise leviable thereon under section 3 of the Central Excise Act, 1944, on like goods, produced or manufactured in India other than in 100 per cent EOU or a FTZ, if sold in India. Further, Board clarified vide CBEC circular No.442/8/99-CX dated 4 March 1999 that benefit of the above mentioned notification may be allowed to units importing as well as indigenously procuring raw materials provided unit is able to satisfy jurisdictional central excise authorities beyond doubt that inputs used, in manufacture of goods to be sold in DTA are manufactured out of indigenous raw materials only, by way of maintenance of records, physical scrutiny/verification and the manufacturing process etc. In case of common inputs or final products, adequate precautions should be taken and unless it is conclusively proved that goods for sale in DTA are manufactured wholly out of indigenous raw materials, benefit of notification should not be allowed.

Scrutiny of records revealed that M/s. Antarctica Ltd., unit under FSEZ, was permitted in March 1993 'to manufacture and export printed cardboard cartons' and it started commercial production in May 1995. With use of imported raw materials 'low density polyethylene' and indigenous raw materials 'M.G. poster paper' the unit manufactured finished products 'Linear teenpati tea cartons' through job work and sold the same to some units in Nepal against rupee payment and in DTA, UNICEF organisation in India etc. It availed benefit of exemption notification dated 1 March 1997 and paid only applicable excise duty on such sale. Audit scrutiny revealed that the goods were manufactured from both indigenous as well as imported raw materials and the unit did not maintain separate records for indigenous or imported raw material as prescribed under circular dated 4 March 1999. As such exemption allowed was irregular and short levy of Rs.41.98 lakh, recoverable from the unit.

On this being pointed out (March 2004), the department accepted the objection in principle and stated (December 2004) that protective demand was raised. Further progress was awaited (January 2006).

6.4 DTA sale

Irregular DTA sale

In terms of para 9.9 (b) of the Exim Policy 1997-2002, DTA sale up to 50 per cent of the FOB value of exports is admissible to a 100 per cent EOU subject to payment of applicable duties and fulfilment of minimum NFEP prescribed in appendix-1 of the policy. Further, in terms of para I (f) and (g) of Appendix-42 of the HBP Vol-I (1997-2002), advance DTA sale

is admissible to a 100 per cent EOU in respect of trial productions and in cases of capacity expansion/product diversification which shall not exceed entitlement accruable on the exports envisaged in the first year.

6.4.1 M/s. Tauras Esdan Hydraulics Ltd., an existing DTA unit under FSEZ, Kolkata on conversion into a 100 per cent EOU (October 1999) was permitted (May 2000) advance DTA sale of nylon tubing valued at Rs.2 crore. Against this, the unit cleared goods valued at Rs.3.16 crore during 2000 to 2003. Audit scrutiny revealed that it did not undertake any capacity expansion/product diversification. Also, NFEP achieved during the years 2001-02 and 2002-03 was negative 1.44 per cent and 6.86 per cent respectively, below the prescribed limit of ten per cent. Thus, not only was the grant of permission for advance DTA sale not in conformity with the provisions of Exim Policy, there was also DTA sale of Rs.2.91 crore more than entitlement. The unit was, therefore, liable to pay differential duty of Rs.91.78 lakh.

On this being pointed out (March 2004), FSEZ authorities while admitting the fact stated that the unit sought regularization of advance DTA sale made by them, which was turned down by Ministry of Commerce. It was stated (January 2005) that commissioner of central excise and customs, Jamshedpur had been requested to finalise the demand. Further progress was awaited (January 2006).

6.4.2 M/s. India Poly Films Ltd., Silvassa a 100 per cent EOU in Vapi commissionerate was engaged in manufacture of biaxially oriented polythelene terphthalate (BOPT) films. During 1995-96 and 1996-97 it achieved VA of negative 130.96 per cent against 29 per cent prescribed. It had effected DTA sales for a value of Rs.1.70 crore on payment at concessional rate of customs duty of Rs.61.26 lakh between September 1996 and February 1997.

Failure to achieve prescribed VA, made DTA sales irregular. Therefore, the unit was liable to pay differential customs duty of Rs.70.17 lakh.

On this being pointed out (October 1999), the assistant development commissioner, SEEPZ, SEZ, Mumbai stated (July 2004) that excise authorities had been asked to recover differential duty of Rs.91.44 lakh. Department reported (February 2005) that SCN was issued in August 2004.

6.4.3 M/s. Sarita Software and Industries Ltd., a 100 per cent EOU under VSEZ cleared 17,52,583 meters of cotton grey fabric and 6,33,145 meters of polyester grey fabric in DTA during 1998-1999 to 2000-01 availing benefit under notification ibid as amended. Audit scrutiny revealed that the said EOU manufactured its final products from raw material procured from other 100 per cent EOUs. There was no evidence on record to establish that the raw materials procured from other EOUs were manufactured by such EOUs wholly from indigenous materials. This was in violation of notification dated 18 July 1998 ibid, and resulted in short levy to the tune of Rs.51.90 lakh.

On this being pointed out (May 2001), the department confirmed (April 2004) demand of Rs.38.74 lakh and Rs.13.16 lakh and also imposed penalty each of equal amounts in respect of cotton grey and polyester grey fabrics respectively. The importer filed an appeal in customs, excise and service tax appellate tribunal (CESTAT) and obtained stay against the recovery. Further progress was awaited (January 2006).

6.5 Duty free service entitlement credit certificate (DFSECC) scheme

In terms of notification No.54/2003-cus dated 1 April 2003, spares, office equipments and furniture, professional equipments and consumables are exempted from whole of the duty of customs, additional duty of customs, on their import into India against a DFSECC issued under para 3.8 of Exim Policy 2002-07 subject to various conditions. One of the conditions requires that these DFSECC and goods imported against it shall not be transferred or sold.

Six importers i.e. M/s. Taj Bengal Hotel and five others imported 254 consignments of whisky, beer and liquor free of duty under DFSECC through custom house, Kolkata (port). Department cleared (between March 2004 and February 2005) these consignments and exempted customs duties in terms of notification ibid after debiting the DFSECC for duties leviable but for this exemption. Declarations from importers to the effect that items imported against DFSECC would be used/utilised by their guests only and the same would not be traded outside the hotel were also obtained. Since whisky, beer and liquor do not fall under any of the ibid category of spares, office equipments, furniture and consumables etc. and the hotels importing whisky, beer and liquor under DFSECC being trading concerns would not supply them free of cost, such use or utilisation tantamounted to sale. Thus, extension of the benefit of duty free clearance of the said goods was irregular to the extent of Rs.1.25 crore.

On this being pointed out between January and May 2005, the department stated (May 2005) that Ministry of Commerce, categorised the items as 'consumables' for hotel industry and held that the sale of liquor to the guests within the hotel premises was in order. The department further stated that there was anomaly in the wording of the Finance Ministry's notification.

Reply of the Ministry of Finance was awaited (January 2006).

6.6 Other cases

In 18 other cases of non fulfilment of EO, irregular DTA sales etc., short levy of Rs.1.35 crore alongwith interest of Rs.33.81 lakh were pointed out as per table below. Department/Ministry admitted objections in 13 cases.

(Amount in lakh of rupees)

Sl. No.	Irregularity	Name of the importers/ exporters (M/s.)	Commi-ssionerate	Amount objected	Interest	Whether accepted
1.	Non levy of duty on DTA sales	Toonz Animation	Thiruvanant-hapuram	21.04	--	Yes
2.	Short levy of duty on DTA sales	Modern Denim Ltd.	Ahmedabad	19.63	--	Yes
3.	Incorrect exemptions under EPCG scheme	Essar Oil Ltd.	Jamnagar	8.33	8.76	Yes
4.	Failure to monitor EO	Sikora India	Coimbatore	11.64	--	Yes
5.	Excess DTA sales	Sindhu Apparels (P) Ltd.	Surat-I	11.41	--	Yes
6.	Non-imposition of late cut on DFRC scheme	Arihant Arts & four others	Jaipur	9.56	--	Yes
7.	Non fulfilment of EO	RD Curer (P) Ltd.	Bangalore	7.19	--	Yes
8.	Non fulfilment of EO	Ganesh Anhydride Ltd.	Mumbai	7.43	--	Yes

9.	Incorrect exemptions under EPCG scheme	ITC Hotels Ltd.	Bangalore	6.57	--	No
10.	Non fulfilment of EO	Mitsu Industries Ltd.	Mumbai	6.88	6.54	Yes
11.	Non fulfilment of EO	Ponnappa Coffee Curing Works	Bangalore	4.05	4.70	Yes
12.	Non fulfilment of EO	Indus Insul (P) Ltd.	Hyderabad	4.64	4.99	No
13.	Non fulfilment of EO	CM Textiles (P) Ltd.	Mumbai	4.05	--	Yes
14.	Non fulfilment of EO	Indiana Conveyers (P) Ltd.	Mumbai	3.99	5.92	Yes
15.	Non fulfilment of EO	Durga Hotels & two others	Mumbai	3.62	2.90	Yes
16.	Non levy of education cess	--	JNCH, Mumbai	2.08	--	No reply
17.	Short levy of duty on DTA sales	JJ Spectrum Silk Ltd.	Kolkata	1.30	--	Interim reply
18.	Non levy of education cess	AMC cookware (I) Pvt. Ltd. & two others	Bangalore	1.09	--	No
	Total			**134.50**	**33.81**	

CHAPTER VII: OTHER TOPICS OF INTEREST

7.1 Non disposal/delay in disposal of warehoused goods

Section 72 (2) of Customs Act, 1962 provides that where goods have not been removed from a warehouse, after expiration of the prescribed period under section 61, the proper officer may detain and sell such goods and realise full duty, penalties, rent, interest and other charges payable in respect of such goods.

7.1.1 Ten consignments of machinery imported by M/s. JVC Nova Magnetics and seven others through custom house, Chennai (sea) and warehoused between January 1987 and May 2000 in central warehousing corporation (CWC) were kept uncleared for periods ranging from three to seventeen years after expiry of permitted warehousing period. No action was initiated by department to dispose off the goods and realise the duty involved, resulting in locking up of revenue of Rs.22.01 crore including interest.

This was pointed out to the department in February 2005, their reply was awaited (January 2006).

7.1.2 Audit scrutiny revealed that 82 cases of imported goods warehoused between March 2002 and June 2004 under Kandla commissionerate, remained uncleared after expiry of the warehousing period. Duty and interest recoverable in these cases amounted to Rs.6.97 crore and Rs.1.82 crore (upto March 2005) respectively.

On this being pointed out (December 2003), the department issued (March 2004) SCN in respect of two cases involving duty of Rs.4.38 lakh and interest of Rs.2.11 lakh. Further progress was awaited (January 2006).

7.1.3 Scrutiny of records of CWC, Pratapnagar, Udaipur revealed that M/s. J.K. Cement Works, Chittorgarh, imported machinery during August/September 1996 involving duty of Rs.1.06 crore which was allowed to be warehoused upto 31 December 1998 (extended period). However, the goods were not removed from the warehouse after the expiry of the extended period and no action was initiated by the department to recover duty, penalty, interest etc., from the importer. This resulted in blockage of revenue of Rs.1.06 crore and interest of Rs.1.56 crore upto March 2005.

On this being pointed out (December 2001), the department stated (June 2005) that demand notice was issued in March 2003 but recovery could not be enforced as the unit was under BIFR. Meanwhile importer's request to relinquish the title on goods had been turned down (June 2005) by the department since demand notice under section 72 has already been issued prior to exercising the relinquishment action. Matter was under stay by High Court of Rajasthan against recovery of dues. The department further stated that as goods had already been attached recovery would be made on vacation of stay. Further progress was awaited (January 2006).

7.1.4 Ten consignments of goods with assessable value of Rs.94.05 lakh involving duty of Rs.46.33 lakh imported through custom house, Chennai (sea) customs and warehoused between August 2002 and December 2003 in public bonded warehouse were kept uncleared after the expiry of the warehousing period of one year permitted under section 61. No action

had been initiated ibid to dispose off the goods and realise duty, resulting in blocking of revenue to the tune of Rs.50.10 lakh including interest for periods from six to twenty one months.

This was pointed out to the department in January 2005, their reply was awaited (January 2006).

7.1.5 Supreme Court in the case of M/s Kesoram Rayon vs. collector of customs, Kolkata {1996 (86) ELT 464 (SC)} ruled that "where the goods have been allowed to be cleared after expiry of the warehoused period, removal of such goods should be treated as 'improper removal' and rate of customs duty payable should be at the rate applicable on the date on which the permitted warehoused period came to an end". Further, as per CEGAT's decision in the case of M/s KLJ Plastics Ltd. vs. commissioner of customs, Chennai {2000 (117) ELT 108 (Tribunal)}, benefit of concessional rate of duty is not admissible in respect of improperly removed goods at a later date under the DEEC Scheme.

M/s. TIL Ltd., Kolkata warehoused various parts and accessories of crane on 28 October 2002. Though warehousing period expired on 27 October 2003 they did not clear goods within validity period of one year i.e. 27 October 2003, nor did they apply for extension of warehousing period. The department allowed clearance of the goods on 4 August 2004 under DEEC licence dated 8 July 2004 without levying any duty. Action of the department was irregular in terms of both judicial pronouncements and section 72 of Customs Act, 1962. Improper removal of the goods as well as incorrect facility of DEEC benefit resulted in loss of customs duty of Rs.29.95 lakh and interest of Rs.7.13 lakh.

On this being pointed out (January 2005), the department stated (June 2005) that demand-cum SCN was issued to the importer. Further progress was awaited (January 2006).

7.1.6 Board's circular dated 7 September 1961 stipulates that 'reserve price' should be the absolute minimum below which the consignment should not be sold.

M/s. Ranit Pharma Ltd., Hyderabad imported 1500 kgs. of 'quinaldic acid' in December 2000 involving duty of Rs.26.78 lakh and warehoused it in public bonded warehouse (ICBC) at tollgate, Chennai. Warehousing period expired in December 2001 and no extension thereof was obtained by the importer. The department after delay of 28 months from expiry of the warehousing period initiated action in April 2004 to auction goods by fixing reserve price of Rs.50 lakh based on chemical test report establishing purity of goods at 99.5 per cent. Despite recommendations by assistant commissioner/deputy commissioner/joint commissioner for rejecting the highest bid, the goods were auctioned in June 2004 to the highest bidder at a price of Rs.1.71 lakh being much lower than the reserve price fixed. This resulted in loss of revenue of Rs.25.07 lakh.

On this being pointed out (December2004 and January 2005), the department stated (February 2005) that the bid was accepted by the commissioner on the plea that chemical value would not increase. Reply was not tenable because within a month of fixing reserve price there seemed to be no possibility of deterioration in quality of the chemical when reserve price was fixed on 20 May 2004. Further, recommendations made by AC/DC/JC for rejecting the bid were overlooked for no apparently justified reasons. Auction of goods below the reserve price was also in contravention of Board's circular of 7 September ibid.

7.2 Non levy of SAD

7.2.1 Serial No.56 of customs notification No.23/2002 dated 1 March 2002 exempts goods imported into India from levy of SAD provided imported goods are exempted from levy of both BCD and additional duty of customs.

Floating crane imported (January 2003) by Chennai Port Trust through custom house, Chennai (sea) was assessed to BCD. The SAD leviable, however, was incorrectly exempted in terms of provisions cited, which resulted in short collection of duty of Rs.1.07 crore.

On this being pointed out (June 2003), the Ministry stated (October 2005) that demand notice for Rs.1.07 crore was issued and confirmed (May 2004). Appeal filed by the importer was dismissed (September 2004) by the Commissioner (Appeals). The importer filed further appeal before CESTAT which was dismissed in February 2005. The importer has filed writ petition in the High Court against the order of the tribunal which is pending.

7.2.2 As per notification No.29/2003-cus (serial No.62) dated 1 March 2003 SAD on import of nylon fabric (un-dipped) was leviable.

Five consignments of 'nylon fabric (un-dipped)' imported by M/s. J&K Industries Ltd., Kankroli under Jaipur-II, commissionerate were cleared from customs bonded warehouses during March/April, 2003 without levy of SAD. This resulted in non levy of SAD amounting to Rs.11 lakh and interest thereon.

On this being pointed out (March/April 2004), the department reported (June 2004) recovery of Rs.11 lakh. Recovery of interest was awaited (January 2006).

7.3 Short levy of duty from sale proceeds of uncleared goods

Section 48 of Customs Act, 1962 deals with disposal of goods not cleared by importers through person having custody thereof. Section 150 deals with the apportionment of sale proceeds of such goods. Balance amount, if any, after adjusting all expenses, dues of the Government etc is payable to importer. As per ratio laid down in the case of M/s. Instamedic International vs. collector of customs, New Delhi (tribunal) reported in 1999 (111) ELT 833 it was held that "once the assessment of duty is complete, the fact that the goods were not physically removed by the importer and that it had to be sold subsequently in auction cannot by itself become a ground for reassessing the goods for demanding duty thereon". This implies that duty is recoverable based on assessment done at the time of assessment of bill of entry filed by the importer.

Various goods imported by M/s. Gujarat Sico Textiles and 12 others with duty liability of Rs.1.38 crore as per original bills of entry filed by importers between June 1995 to October 2001 through Mumbai (sea) commissionerate were put to auction by the department/custodian between 1998-99 and 2001-02 and Rs.83.94 lakh was realised as duty. Rs.1.09 crore was refunded to the importers in terms of section 150 of CTA.

Audit scrutiny revealed that at the time of auction, department re-assessed the goods by adopting value and rate of duty different to the original bills of entry. Non-application of rate of duty prevalent on the date of import had resulted in incorrect quantification of surplus and consequently refund and short levy of duty of Rs.54.72 lakh.

This was pointed out to the department in June 2005, their reply was awaited (January 2006).

7.4 Short collection of cost recovery charges

Customs officers are posted in custom bonded warehouses for supervising the manufacturing operations on cost recovery basis. According to Ministry of Finance letter dated 1 April 1991, cost of officers posted as such is fixed at 1.85 times monthly average cost of the post plus dearness allowance (DA), house rent allowance (HRA), city compensatory allowance (CCA), adhoc bonus etc.

Audit scrutiny of files relating to the 'cost recovery charges' at Cochin Shipyard Ltd. for the period from October 1999 to September 2003 revealed that DA and bonus sanctioned from time to time to officers were not taken into account while calculating cost recovery charges.

On this being pointed out (December 2003), the department stated (April 2005) that out of short collection of cost recovery charges of Rs.21.16 lakh in eight cases, Rs.14.30 lakh was recovered in seven cases and recovery in the remaining case was under progress.

7.5 Non levy of additional duty of excise (ADE)

Notification Nos.30/97-cus dated 1 April 1997 and 51/2000-cus dated 27 April 2000, exempt raw materials from levy of customs and additional duty under section 3 of CTA, 1975 under actual user DEEC scheme. However, ADE leviable under the Additional Duties of Excise (Goods of Special Importance) Act, 1957, is not covered under these notifications.

Further, it has been judicially held in the case of Gokak Mills vs commissioner of central excise {2001 (129) 523 (T) Bangalore} that where a notification granting exemption was issued under a particular rule without reference to any other statute making provisions of levy and collection of special, auxiliary or any other kind of excise duty levied under such statute, the exemption must be construed as limited to the duty of excise payable under the Central Excise and Salt Act, 1944 and cannot cover such special, auxiliary or other kind of duty of excise.

Audit scrutiny of records of assistant commissioner, CFS (OWPL), Ludhiana revealed that eleven consignments of nylon tyre cord dipped fabrics falling under CTH 5902.10 imported by M/s. Govind Rubber Ltd., Ludhiana and five others between June and August 2001 under DEEC Scheme were cleared without levy of additional excise duty leviable under ADE (GSI) Act, 1957 amounting to Rs.13.11 lakh.

On this being pointed out (November 2003), department stated (October 2004 and January 2005) that additional duty equal to central excise duty leviable on like goods manufactured in India was leviable under section 3 of CTA. ADE (GSI) was levied under central excise law on those goods which were chargeable to duty of excise under section 3 of central excise Act, 1944 and section 2 of the CET Act 1985. In case it was accepted that ADE (GSI) was not duty of excise charged under above section it would not be chargeable under section 3 of Customs Act. Reply of the department was not tenable because ADE (GSI) is a duty of excise but it is leviable under the ADE (GSI) Act 1957. Section 3 A (5) of CTA ibid provides that nothing contained in that section, shall apply to any article which is chargeable to additional duties levied under sub section (1) of section 3 of ADE (GSI) Act 1957. The exemption notifications issued under sub section (1) of section 25 of the Customs Act would not automatically exempt the levy of ADE leviable under ADE (GSI) in view of the judicial pronouncement ibid.

7.6 Non levy of interest

In accordance with section 61 (2) (ii) of Customs Act 1962, goods remaining in a warehouse beyond a period of 30 days attract interest at the specified rates.

M/s. Plastolene Polymers Pvt. Ltd., and three other units under the FSEZ warehoused 19 consignments of different goods between February 2002 and March 2003 and the department allowed clearance of such goods after the warehousing period of 30 days without levying any interest for the belated period. This resulted in loss of revenue of Rs.11.45 lakh.

On this being pointed out (March 2004), the department admitted (December 2004) the irregularity. Recovery particulars were awaited (January 2006).

7.7 Non levy of anti-dumping duty

As per section 9A of the CTA, 1975, where any article is exported from any country or territory to India at less than its normal value, then upon the importation of such article into India, the Central Government may, by notification, impose an anti dumping duty. Accordingly, anti dumping duty was imposed on 'nylon fabric, vitrified and porcelain tiles, acrylonitrile butadiene rubber, graphite electrode' etc. from time to time.

Audit scrutiny revealed that 26 consignments of above articles imported by 17 importers were cleared without levying/short levying anti dumping duty. This resulted in short levy of anti dumping duty of Rs.1.83 crore.

On this being pointed out (September 2001 to June 2005), the department/Ministry admitted short levy of Rs.1.52 crore in 11 consignments and reported recovery of Rs.37.99 lakh in eight cases.

7.8 Excess payment of drawback

7.8.1 All Industry Rates of duty drawback are reviewed by the drawback directorate annually as per post budgetary exercise to provide input stage duty neutralisation of customs and central excise duties suffered on inputs and packing materials used for manufacture of export product. Consequent on presentation of Union Budget for the year 2004-05 on 8 July 2004 there was reduction in the rates of customs duties ranging from 25 to 75 percent for some items like metals, minerals, refractories, zinc speller dross, copper mill scale, all primary, semi finished and finished form of iron and steel etc and platinum with effect from 9 July 2004. Accordingly, All Industry Rates of drawback for 2004-05 should have been announced by Ministry soon thereafter or within 90 days as was the convention prior to 2003-04. During 2003-04 they had in fact been notified in a month's time. However, they were notified vide notification No.8/2005-Customs (NT) only on 18 January 2005 effective from 19 January 2005 i.e. after more than five months.

Test check of 22022 shipping bills of drawback in nine commissionerates at Chennai, Delhi, Mumbai, Jaipur and Cochin revealed excess payment of drawback amounting to Rs.42.89 crore to exporters during the period 9 August 2004 to 18 January 2005 when reimbursement of customs duties in excess of duty incidence suffered on inputs used in export products was allowed.

Since rates of drawback have all India applicability financial implications of the delay would be much larger.

This was pointed out to the Ministry in January 2006; their reply was awaited.

7.8.2 On export of goods, refund of excise and customs duties paid on components and raw material could be claimed as drawback as per provisions in the relevant Acts and rules thereunder. Of 63 cases, where excess payment of drawback amounting to Rs.3.22 crore had been pointed out, the department admitted the facts in 47 and reported recovery of Rs.63.84 lakh in 36 cases.

7.9 Other cases

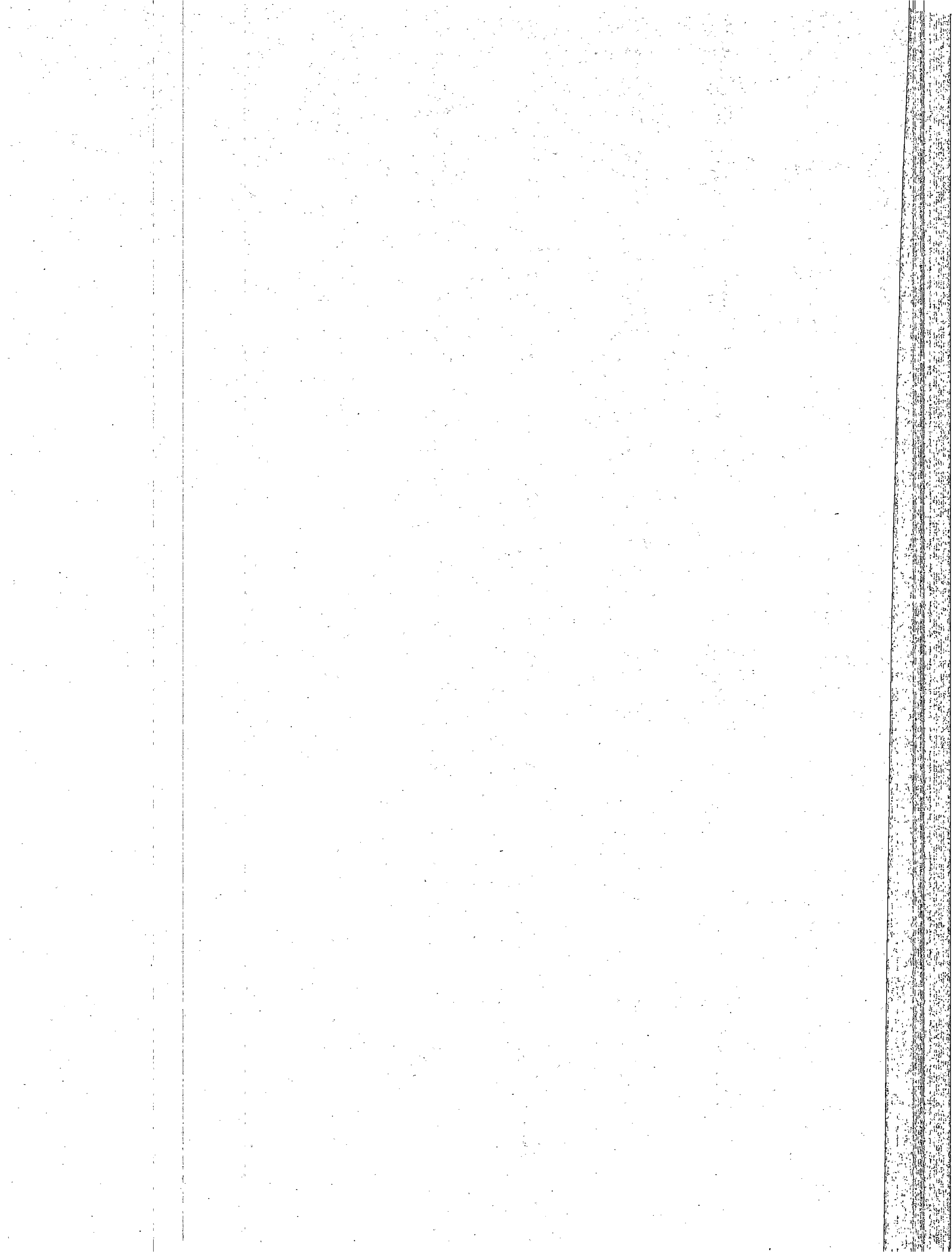
Of 14 cases, which audit pointed out involving Rs.56.61 lakh as detailed below, the department accepted objections in nine involving duty effect of Rs.36.95 lakh and reported recovery of Rs.10.72 lakh in three cases.

(Amount in lakh of rupees)

Sl. No.	Subject	Importer/exporter M/s.	Amount objected	Amount admitted	Amount recovered
1.	Incorrect grant of refund	Rao Insulating Co. Ltd. & another	10.09	Not admitted	--
2.	Non levy of SAD	Birla Tyres & nine others	7.39	7.39	3.02
3.	Non levy of NCCD	J.M. Textiles & 53 others	6.74	6.74	6.74
4.	Delay in disposal of confiscated vehicle	Ahmedabad (Preventive)	6.55	6.55	0.96
5.	Project import	The Indure Ltd.	4.73	4.73	--
6.	Non levy of SAD	Indian Rayon & Industries Ltd.	3.85	Not admitted	--
7.	Delay in implementation of CEGAT order	Tata Infotech Ltd.	3.16	No reply	--
8	Non disposal of seized goods	Kolkata (Air) commissionerate	2.85	2.85	--
9.	Non disposal of uncleared goods	Magnum Overseas	2.78	2.78	--
10.	Non disposal of seized goods	Shillong (Preventive)	2.23	2.23	--
11.	Non realisation of revenue on pilfered goods	Entrack International Trading (P) Ltd.	2.13	2.13	--
12.	Non realisation of duty on excess baggage	ITDC, Kolkata	1.55	1.55	--
13.	Delay in adjudication of demand	Kelvin Infotech (P) Ltd.	1.33	Interim reply	--
14.	Non levy of special excise duty	Triumph Properties Ltd. & another	1.23	Not admitted	--
	Total		**56.61**	**36.95**	**10.72**

7.10 Miscellaneous

Three hundred and forty other cases involving duty of Rs.51.35 lakh were also pointed out. The department has accepted all the objections and reported recovery of Rs.48.43 lakh in 299 cases.



SECTION 2 - CENTRAL EXCISE

CHAPTER VIII : CENTRAL EXCISE RECEIPTS

8.1 Budget estimates, revised budget estimates and actual receipts

The budget estimates, revised budget estimates and actual receipts of central excise duties during the years 2000-01 to 2004-05 are exhibited in the table below: -

(Amount in crore of rupees)

Year	Budget estimates	Revised budget estimates	Actual receipts*	Difference between actual receipts and budget estimates	Percentage variation
2000-01	70967	70399	68526	(-) 2441	(-) 3.44
2001-02	81720	74520	72555	(-) 9165	(-) 11.22
2002-03	91141	86993	82310	(-) 8831	(-) 9.69
2003-04	96396	91850	90774	(-) 5622	(-) 5.83
2004-05	108500	100000	99125**	(-) 9375	(-) 8.64

* Figure as per Finance Accounts.

** Figure is provisional.

The actual collections fell short of the budget estimates as well as the revised estimates year after year. Despite this, Government continued to make optimistic projections during presentation of the annual budget. The budget estimate 2004-05 was pitched at Rs.1,08,500 crore, an increase of 12.56 per cent over budget estimates, 18.13 per cent over revised estimate and 19.53 per cent over actuals of 2003-04. The collections fell short of the budget estimates by Rs.9375 crore or 8.64 per cent and short of revised estimates by Rs.875 crore or 0.88 per cent in 2004-05.

8.2 Value of output** *vis-à-vis* central excise receipts

The value of output from the manufacturing sector vis-a-vis receipt of central excise duties through personal ledger account (cash collection) during the years 2000-01 to 2004-05 are as follows: -

(Amount in crore of rupees)

Year	Value of output	Central excise	Percentage of central excise receipts to value of production
2000-01	991564	68526	6.91
2001-02	1050239	72555	6.91
2002-03	1158294	82310	7.11
2003-04*	1242849	90774	7.30
2004-05*	1357191	99125	7.30

* Estimated figure - as actual figure is under preparation in Ministry of Statistics and Programme Implementation.

** Includes value of all goods produced during the given period including net increase in work-in-progress and products for use on own account. Valuation is, at producers values, that is the market price at the establishment of the producers. As separate figures of value of production by small scale industry units and for export production were not available, these have not been excluded from the value of output indicated. Value of output for the year 2004-05 is based on estimates. Source : Central Statistical Organisation (Government of India).

The foregoing table reveals that value of output had increased by a factor of 1.37 during the years 2000-01 to 2004-05 and the corresponding increase in the central excise receipts was by a factor of 1.45.

8.3 Central excise receipts vis-a-vis Modvat/Cenvat availed*

A comparative statement showing the details of central excise duty paid through personal ledger account (PLA) and the amount of Modvat/Cenvat availed during the years 2000-01 to 2004-05 is given in the following table: -

(Amount in crore of rupees)

Year	Central excise duty paid through PLA		Modvat/Cenvat availed		Percentage of Modvat/Cenvat to duty paid through PLA
	Amount	Percentage increase	Amount	Percentage increase	
2000-01	68526	11.11	44986	9.11	65.65
2001-02	72555	5.88	47509	5.61	65.48
2002-03	82310	13.44	53039	11.64	64.44
2003-04	90774	10.28	66576	25.52	73.34
2004-05	99125	9.20	76665	15.15	77.34

* Figures furnished by the Ministry of Finance (the Ministry).

The above table shows that while central excise receipts had grown only by 45 per cent during the years 2000-01 to 2004-05, growth in Modvat/Cenvat availed during the relevant period was much more at 70 per cent. Percentage of Modvat/Cenvat availed to duty paid by cash which decreased consistently from 65.65 to 64.44 till 2002-03, increased sharply to 73.34 in 2003-04 and 77.34 in 2004-05. This was also reflected in the steep rise in Modvat/Cenvat credit availed during 2002-03 and 2003-04.

8.4 Cost of collection

The expenditure incurred during the year 2003-04 in collecting central excise duty alongwith the corresponding figures for the preceding four years is given below: -

(Amount in crore of rupees)

Year	Receipts from excise duty		Expenditure on collection		Cost of collection as percentage of receipts
	Amount	Percentage increase over previous year	Amount*	Percentage increase over previous year	
2000-01	68526	11.11	615.84	5.30	0.90
2001-02	72555	5.88	635.78	3.24	0.88
2002-03	82310	13.44	702.80	10.54	0.85
2003-04	90774	10.28	750.58	6.80	0.83
2004-05	99125*	9.20	825.90**	10.03	0.83

* Figure as per Finance Accounts.

** Figure is provisional.

8.5 Outstanding demands *

The number of cases and amount involved in demands for excise duty outstanding for adjudication/recovery as on 31 March 2004 and 31 March 2005 are as follows: -

(Amount in crore of rupees)

		As on 31 March 2004				As on 31 March 2005			
		Number of cases		Amount		Number of cases		Amount	
		More than five years	Less than five years	More than five years	Less than five years	More than five years	Less than five years	More than five years	Less than five years
(a)	Pending with Adjudicating officers	860	19988	566.64	10963.23	963	19452	985.56	11061.77
(b)	Pending before								
(i)	Appellate Commissioners	826	9724	273.59	1640.77	498	4954	53.54	1445.64
(ii)	Board	4	1	0.01	0.39	4	5	0.01	0.03
(iii)	Government	181	48	6.13	5.27	13	129	0.13	64.23
(iv)	Tribunals	1989	7879	755.95	6300.17	1789	7969	921.23	6944.79
(v)	High Courts	514	1382	224.61	722.55	551	1082	377.29	1886.59
(vi)	Supreme Court	121	346	142.64	676.01	92	282	87.44	2144.44
(c)	Pending for coercive recovery measures	3884	6243	317.27	1115.85	2514	5507	632.38	2085.95
	Total	**8379**	**45611**	**2286.83**	**21424.24**	**6424**	**39380**	**3057.58**	**25633.44**

* Figure furnished by the Ministry and relates to 93 commissionerates of central excise.

A total of 45,804 cases involving duty of Rs.28,691.02 crore were pending finalisation as on 31 March 2005 with different authorities.

8.6 Fraud/presumptive fraud cases **

The position of fraud/presumptive fraud cases alongwith the action taken by the department against the defaulting assessees during the period 2002-03 and 2004-05 is depicted in the following table :

(Amount in crore of rupees)

Year	Cases detected		Demand of duty raised	Penalty imposed		Duty collected	Penalty collected	
	Number	Amount	Amount	Number	Amount	Amount	Number	Amount
2002-03	1757	1692.06	593.12	284	589.74	51.80	97	0.33
2003-04	2274	1832.18	1103.70	596	188.20	56.81	62	0.16
2004-05	1368	1373.90	891.09	189	88.04	96.22	29	0.09
Total	**5399**	**4898.14**	**2587.91**	**1069**	**865.98**	**204.83**	**188**	**0.58**

** Figure furnished by the Ministry and relates to 93 commissionerates.

The above data reveals that while a total of 5,399 cases of fraud/presumptive fraud were detected during the years 2002-05 by the department, involving duty of Rs.4,898.14 crore, it raised a demand of Rs.2,587.91 crore only and recovered Rs.204.83 crore (7.91 per cent) out

of it. Similarly, out of penalty of Rs.865.98 crore imposed, the department recovered only Rs.0.58 crore (0.07 per cent).

8.7 Commodities contributing major revenue *

Commodities which yielded revenue of more than Rs.1,000 crore during 2004-05 alongwith corresponding figures for 2003-04 are as follows :

(Amount in crore of rupees)

Sl. No.	Commodity	2003-04 (Actual)	2004-05 (Actual)	Percentage variation of actual over previous year	Percentage share in total collection
1.	Refined diesel oil	13469.72	14454.83	7.31	13.83
2.	Motor spirit	12574.96	13791.95	9.68	13.19
3.	Iron & steel	7330.33	7662.86	4.54	7.33
4.	Cigarettes and cigarillos of tobacco or tobacco substitutes	5495.34	5994.85	9.09	5.73
5.	Cement, clinkers, cement all sorts	4219.93	4522.65	7.17	4.33
6.	All other machinery articles and tools falling under chapter 84	2321.21	2851.04	22.83	2.73
7.	Motor cars and other motor vehicles for transport of persons	2141.10	2739.22	27.94	2.62
8.	All other motor vehicles falling under chapter 87	2061.52	2730.61	32.46	2.61
9.	Plastics and article thereof	2151.83	2531.12	17.63	2.42
10.	Petroleum gases and other gaseous hydrocarbons	2552.10	2424.36	(-) 5.01	2.32
11.	Organic chemicals	1722.34	2170.66	26.03	2.08
12.	Articles of iron and steel	1137.39	2106.57	85.21	2.01
13.	Sugar	1779.38	1766.76	(-) 0.71	1.69
14.	Pharmaceutical products	1434.45	1616.40	12.68	1.55
15.	All other electronic and electrical goods falling under chapter 85	1104.41	1316.88	19.24	1.26
16.	Paper and paper board, articles of paper pulp or paper or paper board	1350.40	1300.43	(-) 3.70	1.24
17.	Public transport type passenger motor vehicles and motor vehicles for the transport of goods	1239.41	1278.03	3.12	1.22
18.	Kerosene	1700.08	1273.26	(-) 25.11	1.22
19.	Diesel oil, N.E.S.	991.58	1246.16	25.67	1.19
20.	Tyre, tubes and flaps	808.79	1095.38	35.43	1.05
21.	Miscellaneous chemical products	942.82	1088.00	15.40	1.04
22.	Aluminium and articles thereof	745.56	1035.31	38.86	0.99

* Figure furnished by the Ministry.

The above table reveals that there was lower collection of revenue during 2004-05 in kerosene, petroleum gases and other gaseous hydrocarbons, paper and paper board, articles of paper pulp or paper or paper board and sugar to the extent of (-) 25.11, (-) 5.01, (-) 3.70 and (-) 0.71 per cent respectively over previous year.

8.8 Provisional assessments*

The number of cases of provisional assessments and amount involved therein as on 31 March 2004 and 31 March 2005 is exhibited in following table.

(Amount in crore of rupees)

		As on 31 March 2004		As on 31 March 2005	
		Number of cases	Duty involved	Number of cases	Duty involved
(a)	Pending decision by court of law	47	119.62	26	21.05
(b)	Pending decision by Ministry or Board	6	30.43	25	71.58
(c)	Pending adjudication with the Commissioner	179	180.88	97	17.08
	Total	**232**	**330.93**	**166**	**109.71**

* Figure furnished by the Ministry and relates to 93 commissionerates.

8.9 Revenue remitted or abandoned**

Amount of central excise duty remitted/abandoned or written off due to various reasons for the years 2003-04 and 2004-05 are shown below:

(Amount in crore of rupees)

		2003-04		2004-05	
		Number of cases	Amount	Number of cases	Amount
	Remitted due to :				
(a)	Fire	8	1.18	17	2.44
(b)	Flood	4	0.15	5	0.62
(c)	Theft	1	0.01	0	0.00
(d)	Other reasons	438	2.45	545	2.04
	Total	**451**	**3.79**	**567**	**5.10**
	Abandoned or written off due to :				
(a)	Assessees having died leaving behind no assets	10	0.14	109	0.13
(b)	Assessees untraceable	64	15.61	49	13.31
(c)	Assessees left India	0	0.00	4	0.03
(d)	Assessees incapable of payment of duty	19	12.46	8	0.06
(e)	Other reasons	16	0.20	432	2.42
	Total	**109**	**28.41**	**602**	**15.95**

** Figure furnished by the Ministry and relates to 93 commissionerates.

8.10 Refunds*

The amount of duty refunded by the department during 2002-05 because of excess collection is given below:

(Amount in crore of rupees)

		2002-03	2003-04	2004-05
(i)	No. of cases	31574	33965	16541
(ii)	Amount of refunds (other than rebate)	999.77	965.75	1128.83
(iii)	Interest on refunds			
	(a) No. of cases	16	44	35
	(b) Amount paid	1.22	25.11	61.02

* Figure furnished by the Ministry and relates to 93 commissionerates.

Interest is payable under section 11BB of Central Excise Act, 1944 if amount is not refunded within three months from the date of receipt of application. However table shows consistent increase in amount of interest refunded indicating delayed disposal of cases.

8.11 Contents

This section contains 227 paragraphs (including cases of total under assessment), featured individually or grouped together, arising from test check of records maintained in departmental offices and premises of the manufacturers. Of these, 183 paragraphs contain monetary impact of Rs.911.60 crore directly attributable to audit pointing out non-compliance to rules/regulations and 43 paragraphs involving Rs.6781.54 crore dealing with lacunae in law or procedure or control weakness. Audit has in one paragraph pointed out notional interest amounting to Rs.3.80 crore. In 16 cases replies from Ministries were awaited (January 2006). The concerned Ministries/departments had accepted (January 2006) audit observations in 122 paragraphs involving Rs.200.40 crore and recovered Rs.20.02 crore. Statutory audit has detected objections in 111 cases where internal audit had already been conducted by the department but it had not detected the irregularity.

CHAPTER IX : TOPICS OF SPECIAL IMPORTANCE

9.1 Export of goods allowed free of additional duties without notification

Additional duty of excise (AED) at the rate of one rupee per litre was imposed on motor spirit (MS) with effect from 2 June 1998 by Finance Act, 1998 and on high speed diesel (HSD) oil with effect from 1 March 1999 by Finance Act, 1999. This rate was increased to one rupee fifty paise per litre on both products from 1 March 2003 by Finance Act, 2003. Besides, special additional excise duty (SAED) is leviable on MS at the rate of six rupees per litre from 1 March 2002 by Finance Act, 2002.

Under rule 13 of Central Excise Rules, 1944 (now rule 19 of Central Excise Rules, 2002), read with notification dated 22 September 1994, as amended and superceded on 26 June 2001, excisable goods meant for export outside India may be cleared from factory of the manufacturer or warehouse without payment of duty under bond. Rule 2(7) of the said rules read with rule 2(e) of Central Excise Rules, 2002 defines the term 'duty' to mean duty payable under section 3 of Central Excise Act. Additional duty/SAED leviable under the Finance Act is not covered under notification ibid, since this duty is distinct and different from that leviable under section 3 of the Act ibid.

Supreme Court in the case of M/s. Modi Rubber Ltd. {1986 (25) ELT 849 SC} held that where notification was issued under rule 8(1) of Central Excise Rules, simpliciter without reference to any other statute, exemption granted under it must be construed as limited only to duty of excise payable under Central Excise Act and not to special, auxiliary or other kind of duty leviable under Finance Act.

9.1.1 Six assessees in Haldia, Lucknow, Rajkot, Siliguri and Visakhapatnam I commissionerates, engaged in manufacture/marketing of petroleum products cleared MS and HSD oil for export under bond during the period from April 2001 to August 2004. The clearance was without payment of additional duty and special additional duty leviable under the Finance Acts ibid. Since additional excise duty and SAED leviable was not covered under rebate/exemption, clearance of HSD oil and MS without payment thereof resulted in non-levy of duty of Rs.6118.07 crore.

On this being pointed out (between June 2003 and June 2005), the Ministry stated (January 2006) that for levy and collection of AED, SAED, NCCD and education cess, provisions of Central Excise Act and Rules were extended by respective Finance Acts and hence the provisions of rebate of central excise duty would be applicable to such duties as well. The Board, however issued section 37B order on 13 January 2006 requiring department not to recover said duties payable on export of goods under bond.

Reply is not tenable in view of Supreme Court decision in the case of Modi Rubber Limited upholding that exemption from duty of excise did not mean exemption from special excise duty or additional duty of excise. Further notification dated 26 June 2001 had been amended on 24 March 2003 to cover AED leviable on tea and tea waste under Finance Act 2003 and on 10 August 2004 to cover NCCD and education cess leviable under respective Finance Acts but no such amendment had been made for AED and SAED leviable on MS and HSD.

9.1.2 Seven manufacturers, in four commissionerates, engaged in manufacture of tobacco products/yarn/textile products falling under chapters 24, 52, 54 and 55 of Central Excise Tariff exported their products under bond/letter of undertaking during 1997-98 to

2004-05 without payment of duties under provisions of notifications issued under rule 13 of Central Excise Rules, 1944/rule 19 of new Central Excise Rules, 2001/2002. Since the goods attracted levy of additional duties under Goods of Special Importance Act, 1957/Textiles and Textile Articles Act, 1978 (T&TA), assessees were liable to pay additional duties amounting to Rs.62.10 crore on these exports in the absence of specific exemption in the relevant notifications.

Non-levy of additional duty in four cases was pointed out between May 2000 and February 2001. The Ministry stated (May 2003) that (i) intention of both rules 12 and 13 was to make duty incidence 'nil' in the case of all exports (ii) when exports were made under claim for rebate in terms of erstwhile rule 12, additional duty of excise (T&TA) was also abatable along with duty of excise paid under Central Excise Act and (iii) on harmonious construction of these two rules, it was to be construed that the facility stands extended to additional duties of excise both for purpose of export under claim for rebate as well as export under bond.

Contentions of Ministry are not tenable since notification issued under rule 13 of erstwhile Central Excise Rules, 1944 or rule 19 of Central Excise Rules, 2001/2002, unlike the notifications issued under rule 12/rule 18 ibid, did not cover additional duties leviable under Goods of Special Importance Act, 1957 or T&TA upto 9 August 2004. Further, the term 'duty' as defined under rule 2(7) of Central Excise Rules, 1944/rule 2(e) of Central Excise Rules, 2001/2002 means only the duty payable under section 3 of Central Excise Act, 1944. Therefore, the provisions of any notification issued under the rules framed under Central Excise Act shall normally have application only to the duties leviable under the said Act unless the notification itself makes a specific mention about duties of excise payable under other Acts. Since benefit of rebate of additional duties was specifically extended to exports made under rule 12/rule 18 only, the same cannot be interpreted as having been extended as well to exports made under bond. If this was so, there was no necessity of issuing amending notification dated 10 August 2004. Further, the said amendment shall take effect only from the date of issue in terms of provisions of section 38A of Central Excise Act, 1944.

9.2 Short realisation of revenue due to incorrect adoption of rate of duty

In terms of notification dated 1 March 2002 concessional/effective rate of basic and additional duty of excise on processed textile fabrics was prescribed at 12 per cent (BED 8 per cent and AED 4 per cent) subject to the condition that they were manufactured from textile fabrics on which appropriate duty of excise and duty as specified in Additional Duties of Excise (Goods of Special Importance) Act, 1957 had been paid. The interpretation of the expression "appropriate duty of excise has been paid" was considered by Supreme Court in the case of M/s. Dhiren Chemical Industries {2002 (139) ELT 3 (SC)} and followed by the Board while issuing circular dated 26 September 2002, wherein it was held that the word "appropriate" in the context of such exemption notification means the correct or specified rate of duty and that where an exemption was subject to the condition that "appropriate duty of excise had been paid" on the inputs, the exemption would not be available if the inputs were exempted from excise duty or were subject to nil rate of excise duty.

Seventy six assessees in Ahmedabad I, Delhi IV, Hyderabad II, III, IV, Jaipur II, Surat I and II commissionerates, engaged in manufacture of processed fabrics from duty free grey fabrics, cleared finished goods on payment of concessional rate of 12 per cent availing exemption under notification dated 1 March 2002 ibid. Since grey fabrics were exempted from duty, concessional rate of duty on finished goods was not admissible in terms of

Supreme Court decision ibid. Duty was required to be paid at the rate of 24 per cent (BED 16 per cent and AED 8 per cent). This resulted in short realisation of duty of Rs.266.24 crore between March 2002 and February 2003.

On this being pointed out (between May 2004 and August 2005), the Ministry stated (December 2005) that the condition of payment of appropriate duty was satisfied by virtue of explanation II of the notification dated 1 March 2002 and clarification of the Board dated 10 December 2002.

Reply is not tenable as explanation II to the notification allows exemption from production of documents only. Deeming provisions cannot be made applicable to those fabrics which are exempt from duty. While interpreting a similar provision, the tribunal in case of M/s. Machine Builders vs. collector of central excise {1996 (83) ELT 576} ruled that the intention was not to deem that the inputs which actually did not suffer duty can be treated as duty paid inputs. The purpose was to ensure benefit to those who use duty paid inputs but where it may not be possible for them to produce duty paying documents. Further the clarification dated 10 December 2002 is not relevant to independent processors who procure unprocessed fabrics at nil rate of duty and use in the manufacture of processed fabric.

9.3 Non-levy of national calamity contingent duty (NCCD) on exports made under bond

Section 136 of Finance Act, 2001, imposed surcharge by way of duty of excise called NCCD with effect from 1 March 2001 on cigarettes, chewing tobacco, pan masala etc. falling under chapter 24 of Central Excise Tariff Act, 1985. Similarly by section 169 of Finance Act, 2003, NCCD has been imposed on manufacture of motor vehicle and motor cycles with effect from 1 March 2003.

Rule 13 of Central Excise Rules, 1944/now rule 19 of Central Excise Rules, 2001/2002, and notifications issued thereunder from time to time allows clearance of goods from factory of manufacturer for export outside India without payment of duty under bond. On imposition of NCCD, consequential amendments were not introduced simultaneously in relevant notifications extending benefit of exemption to NCCD also when goods are exported under bond. This particular duty was notified by Government as duty eligible for exemption only on 10 August 2004 by amending the relevant notification issued under rule 19 ibid.

Test check of records of six assessees in six commissionerates, engaged in manufacture of cigarettes, chewing tobacco etc. showed that they exported different brands of cigarettes and chewing tobacco under bond without payment of central excise duties as well as NCCD during the period from April 2001 and 9 August 2004. Similarly six assessees in five commissionerates engaged in manufacture of motor vehicles, motor cycles etc. falling under chapter 87 exported motor vehicles and motor cycles under bond without payment of central excise duties as well as NCCD. Exemption from payment of NCCD was not available in respect of goods exported under bond upto 9 August 2004 as the term 'duty' mentioned in the pre-amended notification meant only duty payable under Central Excise Act whereas NCCD is levied under Finance Act which was not covered by the notification till the date of amendment. Amendment in the relevant notification was only prospective in application. Therefore clearance of goods for export without payment of NCCD was incorrect. This resulted in non-payment of NCCD of Rs. 208.85 crore on chewing tobacco exported between April 2001 and 9 August 2004. and Rs.25.69 crore on motor vehicles and motor cycles

exported between March 2003 and 9 August 2004. Aggregate duty not paid on products ibid worked out to Rs.234.54 crore.

On this being pointed out (between January 2004 and May 2005), the Ministry stated (August and September 2005) that Board had clarified on 26 June 2002 that no NCCD was leviable on goods exported under bond since it was the policy of the Government to grant relief from element of domestic taxes on goods exported. It further stated (January 2006) that for levy and collection of AED, SAED, NCCD and education cess, provisions of Central Excise Act and Rules were extended by respective Finance Acts and hence the provisions of rebate of central excise duty would be applicable to such duties as well. The Board, however issued section 37B order on 13 January 2006 requiring department not to recover said duties payable on export of goods under bond.

Reply of the Ministry is not tenable as exemption from duty on export goods should have been extended only through amendment to the relevant notification and not by clarification. Such benefit was extended by the Government by issue of notification dated 10 August 2004 hence was not applicable prior to that date.

9.4 Shortcomings in exemption on goods manufactured in notified areas of Himachal Pradesh (H.P) and Uttaranchal

Government of India introduced concessions for the States of Uttaranchal and H.P. in January 2003 with a view to develop industries and generate employment in the two States. Accordingly, notifications 49/2003-CE and 50/2003-CE both dated 10 June 2003 were issued exempting specified goods (other than certain restricted items) cleared from industrial units located in the specified areas from excise duty for a period of ten years from date of their publication or from the date of commencement of commercial production, whichever was later. Exemption under these notifications was available to (i) new industrial units which had commenced commercial production on or after 7 January 2003; and (ii) industrial units existing before 7 January 2003 but which had undertaken substantial expansion by way of increase in installed capacity by not less than 25 per cent on or after 7 January 2003 but not later than 31 March 2007.

Audit scrutiny of 38 units (30 in H.P. and 8 units in Uttaranchal) revealed several major shortcomings in the manner in which notifications were being resorted to. Given that Government foregoes huge revenue, unintended or skewed benefits warrant deep scrutiny of the scheme. Major audit findings are given below: -

9.4.1 Definition of 'new unit'

An assessee, filed declaration claiming to be 'new industrial unit' in H.P. Audit scrutiny, however, revealed that unit was already functioning in the same name and style at Noida and had shifted to H.P. where a unit owned by managing director of the company was already engaged in manufacture. The proprietary unit was declared closed and taken on lease where the assessee, claiming to be a 'new industrial unit' started manufacturing goods of same product line.

Government was, thus, deprived of revenue amounting to Rs.3.99 crore which the erstwhile unit had paid during 2003-04 before opting for the exemption.

9.4.2 Shifting of units to exempted areas as 'new units'

An assessee established a unit at Parwanoo H.P. and filed declaration as 'new unit' for the manufacture of wrist watches (heading 91.02). The manufacturer already had a unit in the same name at Noida where 93,862 watches per month (average) were manufactured during the year 2003-04. Production at Noida unit came down to 57,848 watches per month (average) during 2004-05 and to 14,120 (average) during April and May 2005. Production at Parwanoo unit during 2005-06 was 57,395 watches per month (average). Duty forgone at Parwanoo unit amounted to Rs.8.57 crore (Rs.6.87 crore during 2004-05 and Rs.1.70 crore during 2005-06 upto June 2005).

Another assessee in Baddi Tehsil Nalagarh, District Solan H.P. established as a 'new unit' for manufacture of medicaments (sub-heading 3003.10), had another manufacturing unit at Ahmedabad from where product line was shifted and established in exempted area in H.P. Duty forgone by the Government amounted to Rs.18.38 crore (Rs.8.36 crore during 2004-05 and Rs.10.02 crore during 2005-06).

Similarly another assessee in Nahan H.P. established as a 'new unit' engaged in manufacture of aluminium cans (sub-heading 7612.91) had a manufacturing unit of the same type at Jagadhari (Haryana) which was closed and activities shifted to the exempted area in H.P. Manufacturer had cleared goods valuing Rs.5.25 crore during 2004-05 on which duty forgone by Government amounted to Rs.83.98 lakh.

Audit noticed that exemptions were afforded under Income Tax Act, 1961, in fact, after section 80-1(C)(4) clearly spelt out the following conditions for new units: -

(i) it is not formed by splitting up or the re-construction of the business already in existence; and

(ii) it is not formed by the transfer to a new business of machinery or plant previously used for any purpose.

No such clarity existed under central excise notifications due to which several units as described above could avail exemption as new units after shifting.

9.4.3 Definition of substantial expansion

An existing unit could avail exemption if substantial expansion by way of increase in installed capacity by not less than 25 per cent had been undertaken on or after 7 January 2003. In the subsequent clarification issued by the Government vide circular dated 21 January 2004, it was clarified that the only criterion to be satisfied was increase in the installed capacity by at least 25 per cent with additional plant and machinery irrespective of the quantum of increase in the value of investment in plant and machinery. Some lacunae came to notice: -

No addition in plant and machinery

An assessee in Meerut I commissionerate, an existing unit engaged in manufacture of mild steel ingot falling under sub-heading 7206.90, had declared substantial expansion by way of increase in installed capacity and availed exemption on clearance of 26828.645 tonne during the period 3 August 2003 to 31 March 2005 without payment of duty of Rs.5.08 crore calculated at the rate of 16 per cent on assessable value of Rs.31.77 crore whereas as per balance sheet for the year 2002-03 and 2003-04 no addition in plant and machinery had been

made by the assessee unit. As such, the unit had irregularly availed exemption amounting to Rs.5.08 crore on the clearance of M.S. ingot.

Increase in installed capacity not linked with increase in investment

Records of an assessee in Meerut I commissionerate, revealed that assessee started availing exemption by substantially increasing installed capacity from 20 lakh watches to 30 lakh watches per annum (50 per cent increase) from 15 October 2003. In support of their claim, they furnished a certificate from chartered engineer which had not linked increase in installed capacity with increase in value of plant and machinery. Unit's records disclosed that during 2002-03, the assessee had produced 18,58,572 watches against capacity of 20 lakh watches (thus there was an idle capacity of seven per cent), whereas production during the period 2004-05 (under exemption) jumped to 31,76,995 watches against the new installed capacity of 30 lakh per annum (there was excess production over capacity by 1,76,995 watches) which was about six per cent even after off setting shortfall of 1,41,428 watches during 2002-03.

Annual report of the assessee showed that the main manufacturing plant was located at Hosur in Chennai. Main components were manufactured there and 'stock transferred' to Dehradun unit for assembly, after which same were sent to clearing and forwarding agents as per their headquarters specific instructions. Thus, neither was there complete manufacturing nor any genuine sale being made from the factory gate.

Moot question of whether benefit envisaged for manufacturer should be given to assessee who was essentially engaged as a job worker/assembler was not addressed in the scheme.

Unutilised capacity

An existing duty paying unit opted for exemption from April 2004 as it claimed to have undertaken substantial expansion (30 per cent) of installed capacity. Scrutiny, however, revealed that existing installed capacity had remained unutilised by almost 22, 23 and 19 per cent during 2001-02 to 2003-04 respectively.

Since there was no provision to link installed capacity, with actual production, this resulted in creation of 'idle assets'. The assessee had paid revenue of Rs.2.81 crore per annum before opting for exemption which would be the net annual loss to Government exchequer from April 2004 onwards.

Basis of calculation of 'expansion in installed capacity' not spelt out in notification

An assessee engaged in manufacture of kraft paper (sub-heading 4804.90), filed declaration as an existing unit opting for exemption on basis of substantial increase in installed capacity.

The unit started availing exemption with effect from 22 October 2003 on the basis of chartered engineer's certificate of increased capacity given to State industries department. However, jurisdictional central excise department later detected that the unit already had existing capacity of 30,000 tonne per annum instead of 26,400 tonne as claimed by the unit and consequently issued show cause notice (SCN) (June 2005) demanding duty of Rs.3.53 crore. The fact remained that the exemption notification was silent about (i) the authority empowered to certify installed capacity; and (ii) clear definition of the term 'existing capacity'. In the instant case unit did not exceed 93 per cent of its capacity utilization and by enhancing installed capacity by about 25 per cent it would still remain short by seven percent of the requirement of 25 per cent of expansion (as contemplated in the notification) if installed capacity was co-related with actual production.

9.4.4 Utilisation of resources from outside the State

Audit scrutiny revealed instances of large manufacturers/brand name owners transferring dutiable manufactured goods from outside the state only for processes of packing/repacking through job workers in H.P./Uttaranchal. In four cases noticed by audit, products such as razors, cells, toiletries, razor blades, shoes, perfumed hair oil, cosmetics etc., were sent by large manufacturers/brand name owners for packing/repacking. The duty forgone by revenue in case of these four units amounted to Rs.27.45 crore.

Since no manufacturing was involved in the processes carried out by job worker, there was no evidence of utilisation of resources from within the State.

9.4.5 Flight of capital by relocation of units

Notifications lack provision to prevent misuse of the exemption as a result of which established brand name owners were found to have shifted from duty paying areas to exempted areas in H.P./Uttaranchal. Some instances noticed in audit are as under: -

An assessee established as a 'new unit' are manufacturing branded air conditioners (heading 84.15). Their entire production was supplied to two brand name owners were earlier supplied to brand name owners from their other unit situated at Punjab which was duty paying area. Manufacturing activities were shifted to exempted areas in H.P. The sale pattern remained the same. Goods valued at Rs.9.70 crore were supplied in the month of March 2005 upon which duty forgone amounted to Rs.1.55 crore.

An assessee established as new unit were engaged in manufacture of food preparation of flour/edible preparations with brand name 'Spert' (heading 1901.19/2108.99) which was a popular brand name in the market even before its production started in H.P. Brand name owner apparently searched for vendors in exempted area. During 2004-05, manufactured goods valued at Rs.2.50 crore were supplied by the assessee to the brand name owner on which duty forgone amounted to Rs.39.98 lakh.

Six assessees of home appliances like electric iron, mixer and grinders, electric fans and water heaters had since established their 'new units' in the notified area at Kala Amb H.P. in Chandigarh commissionerate. Goods were being manufactured with the brand name 'Bajaj'/'Hotline' and were solely supplied to the depots of brand name owners. Cross check of records revealed that vendors had earlier supplied branded goods from their own or sister units at Delhi or Noida (Uttar Pradesh). Introduction of grant of exemption in H.P. encouraged 'brand name owners' to shift vendors and procure supplies of the manufactured goods from exempted areas.

Shifting of supply line from Delhi/Noida to notified areas of H.P. led to duty to the extent of Rs.13.63 crore being foregone by Government with corresponding gain to large manufacturers during the period between 2003-04 and 2005-06 (upto June 2005) from these five vendor units alone.

9.4.6 No provision for recovery of Cenvat credit on inputs/capital goods diverted for use in production of final goods under exemption notification

According to sub-rule (4) of Rule 6 of Cenvat Credit Rules, 2002, no Cenvat credit shall be allowed on capital goods which are used exclusively in manufacture of exempted goods.

There is no provision in notification dated 10 June 2003 for recovery of Cenvat credit already taken, before opting for exemption, on inputs/capital goods. Cases of irregular utilization of Cenvat credit are given below: -

Two existing manufacturers availed total exemption from central excise duty after undertaking substantial expansion in plant and machinery as per provisions of notification dated 10 June 2003. They had also availed and utilised Cenvat credit involved on plant and machinery installed during expansion of the project. Availment of credit was not in order because expansion was undertaken with clear understanding that such capital goods would be utilised in manufacture of goods which would be cleared without payment of duty.

Credit amounting to Rs.45.54 lakh had been availed and utilised by manufacturers during the period when expansion was going on. Omission to make provision in this regard in the notifications resulted in incorrect availment of credit of Rs.45.54 lakh by them.

9.4.7 Non-recovery of duty on finished dutiable goods lying in stock on the date of opting exemption

An assessee in Meerut II commissionerate, an 'existing unit' engaged in production of sugar and molasses (headings 17.01 and 17.03) had dutiable goods (sugar and molasses) lying in stock as on date of opting for exemption (i.e 8 November 2004) under notification dated 10 June 2003. Such goods were also cleared from the mill without payment of duty on the plea that there was no specific provision in the said notifications to charge duty on such goods lying in stock and subsequently cleared under the said notification. Audit scrutiny revealed that the sugar mill had on date of declaration, an unsold stock of sugar (3,95,895 quintal) and molasses (14,47,715 quintal) on which duty at normal rate was payable by the sugar mill. However, instead of paying duty on entire stock, the sugar mill cleared 3,24,162 quintal of sugar worth Rs.50.79 crore without payment of duty of Rs.9.57 crore. Department neither proceeded for recovery of duty nor initiated any penal proceedings.

On balance quantity of sugar and molasses central excise duty at the rate of 16 per cent on sugar and Rs.750 per tonne on molasses was also recoverable.

9.4.8 Shifting of duty paying units out of State

Though, promulgation of the scheme of duty exemption under notifications 49/2003-CE and 50/2003-CE attracted new units in H.P. at the same time it also resulted in shifting of existing duty paying units to other areas where similar exemption was available, thereby negating the desired objective of development of the State.

A renowned group of companies had number of duty paying units functioning in H.P. before grant of exemption. After promulgation of the exemption scheme the company shifted duty paying units viz. amla extract unit, hair oil unit from H.P. to areas in Uttaranchal where similar exemption was available and in turn shifted duty paying units such as glucose unit, shampoo unit and toothpaste unit from other areas to exempted areas in H.P.

Duty forgone on goods manufactured in H.P. after availing exemption amounted to Rs.12.72 crore on account of goods cleared during 2004-05 and duty loss due to shifting of unit out of H.P. amounted to Rs.7.28 crore (duty which the unit had paid). There was, therefore, no check on migration of units from one area to the other.

Audit, therefore, recommends that lacunae in the notifications be taken care of by clearly defining the conditions and a review of the benefits in terms of value additions and large scale employment generation be undertaken.

Reply of the Ministry to the above observations had not been received (January 2006).

9.5 Non-payment of education cess on goods exported under bond

Section 91 read with section 93 of Finance Act, 2004, provide for levy of education cess at the rate of two per cent on all goods cleared on or after 9 July 2004. Notification dated 26 June 2001 issued under rule 19 of Central Excise Rules allows clearance of goods for export without payment of duty under bond/letter of undertaking. For purpose of this notification, duty means duty as defined in Central Excise Act, 1944 and also additional duty levied under section 157 of Finance Act, 2003. Definition of duty under the said notification was expanded vide notification dated 10 August 2004 to include education cess leviable under Finance Act, 2004. Hence for the intervening period i.e. during 9 July 2004 to 9 August 2004, goods exported under above said notification were not exempted from levy of education cess.

Twenty nine assessees in eighteen commissionerates, exported various excisable goods during the period from 9 July 2004 to 9 August 2004 without payment of education cess, which was not correct. Non-levy of education cess amounted to Rs1.93 crore.

On this being pointed out (between October 2004 and May 2005), the Ministry stated (January 2006) that for levy and collection of AED, SAED, NCCD and education cess, provisions of Central Excise Act and Rules were extended by respective Finance Acts and hence the provisions of rebate of central excise duty would be applicable to such duties as well. The Board, however issued section 37B order on 13 January 2006 requiring department not to recover said duties payable on export of goods under bond.

The Ministry's reply is not tenable in view of Supreme Court decision in the case of Modi Rubber Limited upholding that exemption from duty of excise did not mean exemption from special excise duty or additional duty of excise. If benefit of rebate of education cess was extendable to exports made under rule 12/rule 18 then there was no necessity of issuing amending notification dated 10 August 2004. Moreover, the said amendment shall take effect only from the date of issue in terms of provisions of section 38A of Central Excise Act, 1944.

CHAPTER X : GRANT OF MODVAT/CENVAT CREDIT

Under Modvat/Cenvat scheme, credit is allowed for duty paid on 'specified inputs' and 'specified capital goods' used in manufacture of finished goods. Credit can be utilised towards payment of duty on finished goods subject to fulfilment of certain conditions. Some cases of incorrect availment of Modvat/Cenvat credit noticed in test audit are elucidated in the following paragraphs :-

10.1 Incorrect availment of credit on inputs not involving purchase and sale

Rule 57AE(3) of Central Excise Rules, 1944, prescribes maintenance of proper records for receipt, disposal, consumption and inventory of inputs and capital goods by manufacturers. Relevant information regarding value, duty paid, person from whom inputs or capital goods have been purchased were to be recorded. Burden of proof regarding admissibility of Cenvat credit shall be upon the manufacturer taking such credit. Similar provision has also been made in rule 7(4) of Cenvat Credit Rules, 2001 effective from 1 July 2001. The Ministry clarified on 3 April 2000 that the basic responsibility to prove that inputs or capital goods were purchased and used by him for intended purpose lay upon the manufacturer.

Test check of records of seventeen assessees in Ahmedabad II, Belapur, Bhopal, Mumbai II, IV, V, Pune III, Surat I, Thane I, II and Vapi commissionerates, manufacturing excisable goods, revealed that they received inputs from sister units on stock transfer basis. Invoices indicated that goods sent were not sale and valuation of such inputs by the sender unit was made under rule 8 of Valuation Rules, 2000. Sales tax was not paid on such goods as the transaction was not a sale. Since assessees did not purchase the inputs, availment of Cenvat credit of Rs.144.19 crore between April 2000 and February 2003 was not correct.

On this being pointed out (between December 2002 and June 2005), the Ministry stated (November 2005) that rule 4 of Cenvat Credit Rules, 2000 allows Cenvat credit on inputs received in the factory of manufacturer irrespective of whether goods in question were purchased or procured. It further stated that rule 57AE (3) stipulated maintenance of relevant information and did not impose condition regarding admissibility of credit on purchase of inputs. It further stated that the word 'purchased' had been replaced by 'procured' to alter the nature of information to be maintained.

Reply of the Ministry is not tenable as rule 57AE(3) stipulates condition of purchase and to have proof in this regard for admissibility of Cenvat credit. Supreme Court in case of A.N. Sehgal vs. Raje Ram Sheoram (AIR 1991 SC 1406} held that effect should be given to both provisions of an enactment which cannot be reconciled with each other. Ministry remained silent on its own circular dated 3 April 2000 where it was clarified that basic responsibility was upon the manufacturer to prove that inputs or capital goods were purchased and used for the intended purpose. Moreover, rule 57AE(3) has been amended by a notification dated 1 March 2003 in which the word 'purchased' in rule 7 (4) (identical to rule 57AE (3)) of Cenvat Credit Rules, 2001 has been substituted by the word 'procured' prospectively. This lends credence to the stand taken by Audit. Hence, credit availed was recoverable for the period before 1 March 2003.

10.2 Removal of inputs without payment of duty

10.2.1 Rule 3(4) of Cenvat Credit Rules, 2002, stipulates that when inputs or capital goods on which Cenvat credit has been taken are removed as such from the factory, manufacturer of the final products shall pay an amount equal to duty of excise leviable on the date of removal of inputs/capital goods and such removal shall be made under the cover of invoice referred to in rule 7. From 1 March 2003, this rule has been amended requiring payment of duty equal to credit availed in respect of such inputs or capital goods. However, requirement of removal under cover of an invoice remained unchanged thereby implying that each removal of inputs/capital goods should be made on payment of duty.

Further, rules 12 and 13 of the said rules, provide that where Cenvat credit has been taken or utilized wrongly, the same along with interest shall be recovered from the manufacturer and provisions of sections 11A and 11AB of Central Excise Act, 1944, shall apply mutatis mutandis for effecting such recoveries. On contravention of any of the provisions in respect of any inputs or capital goods, such person shall also be liable to penalty not exceeding the amount of duty or ten thousand rupees whichever is greater.

As stipulated in rule 4 of Central Excise Rules, 2002, excisable goods produced or manufactured in a factory shall be cleared on payment of duty leviable on such goods in the manner provided in rule 8 of Central Excise Rules, ibid. It, therefore follows that facility to make payment of duty on monthly basis (by fifth of the following month) shall not be applicable to goods not manufactured in the factory but removed as such in terms of rule 3(4) of Cenvat Credit Rules.

During test check of records of twenty one assessees in twelve commissionerates, it was noticed that they had removed input and capital goods as such during April 2002 to November 2004. Duty amounting to Rs.71.54 crore was not paid on the date of removal of inputs but on 15th day or the last day of the month or 20th and fifth of the next month availing facility of fortnightly/monthly payment under rule 8 of Central Excise Rules, 2002 (erstwhile rule 173 G of Central Excise Rules, 1944). This was in contravention of rule 3(4) ibid since inputs were not manufactured by the assessees and tantamounted to removal of inputs/capital goods without payment of duty. The assessees were, therefore, liable to pay interest of Rs.45.63 lakh and penalty of Rs.71.54 crore under rules 12 and 13 of rules ibid.

On this being pointed out (between October 2004 and May 2005), the Ministry stated (between September and December 2005) that subsequent reversal under rule 3(4) of credit taken was payment of duty which was correct under rule 8 of Central Excise Rules, 2002.

Reply of the Ministry is not tenable as rule 8 of Central Excise Rules refers to time and manner of payment of duty of manufactured goods. Rule 3(4) of Cenvat Credit Rules 2002 stipulates that an amount equal to credit availed shall be paid when goods (inputs/capital goods) are removed as such. Since such goods were not manufactured in the factory from where they were removed, provisions of rule 8 (read with rule 4) of Central Excise Rules were not applicable.

10.2.2 In terms of provisions of rule 57AB(1)(c) of Central Excise Rules, 1944, and rule 3(4) of Cenvat Credit Rules, 2001, for all inputs on which credits have been taken, and removed as such from the factory, manufacturer of final product shall pay an amount equal to credits availed/duty of excise which is leviable on such goods on the date of such removal and on the value determined for such goods under section 4 of Central Excise Act. Such removal shall be made under cover of an invoice referred to in rule 52A.

M/s. Kandhari Beverages Ltd., Baddi and M/s. Pepsico India holdings Pvt. Ltd., in Chandigarh and Raigad commissionerates, engaged in manufacture of aerated water (heading 2202.20) and availing Cenvat credit on inputs viz., glass bottles and plastic crates etc., cleared/transferred such inputs to other units without issuing invoice and without payment of duty or reversing credit which was not correct. This resulted in non-recovery of Rs.71.04 lakh between the period from April 2000 and July 2004.

On this being pointed out (July 2002 and December 2002), the Ministry stated (October and November 2005) that the bottles and crates returned from distributors being durable and returnable containers, no credit was taken on them. Therefore no duty was payable on subsequent removal of such goods.

Reply of the Ministry is not tenable as credit was taken on crates and bottles on purchase thereof and these remain the property of the assessee even on receipt from distributors. Further, the practice of distribution of finished goods and collection of empties is such that Modvatable and non-Modvatable bottles cannot be distinguished, as there is no mark on bottles as such, therefore duty was required to be paid on clearance to other units.

10.3 Loss of revenue due to absence of appropriate provisions in Modvat/Cenvat credit rules

Under erstwhile rule 57CC/rule 57AD of Central Excise Rules, 1944 and present rule 6 of Cenvat Credit Rules, 2002, where a manufacturer is engaged in manufacture of any final product which is chargeable to duty as well as any other final product which is exempt or is chargeable to 'nil' rate of duty and the manufacturer takes credit of specified duty paid on any inputs for manufacture of both categories of final products without maintaining separate accounts, he shall pay an amount equal to eight per cent of the price of second category of final product (viz. exempted one) as charged by the manufacturer at the time of clearance from the factory.

Bangalore I commissionerate, issued periodical SCNs to M/s. Rail Wheel Factory, Bangalore demanding differential duty of Rs.62.96 crore for the period between September 1996 and March 2001 for clearance of goods without raising invoices, non-reversal of an amount equal to eight per cent of the price charged in terms of erstwhile rule 57CC/rule 57AD/present rule 6 and incorrect valuation etc. Demands were confirmed in April 2002 and 28 January 2003. CESTAT in August 2003 and August 2004 set them aside on appeal by assessee relying upon their earlier decision in the case of Gas Authority of India Ltd. {2001 (135) ELT 795} upholding that recoveries under rule 57CC were not in the nature of duty and, therefore, rule 57(I) could not be invoked for recovery. Department had lost an appeal in similar case against the tribunal's order in M/s. Pushpaaman Forgings case {2002 (149) ELT 490 (T)} in Apex Court on the grounds that there were no machinery/provisions for recovery of eight per cent amount under erstwhile rule 57CC of Central Excise Rules or new rule 6 of Cenvat Credit Rules, 2002. Hence, lack of suitable provisions in the said rules resulted in total loss of revenue of Rs.62.96 crore to the Government.

On this being pointed out (November 2004), the Ministry admitted the objection and stated (December 2005) that recovery mechanism had been introduced by Finance Act 2005.

10.4 Incorrect availment of Cenvat credit on capital goods before use

Rule 57AC of Central Excise Rules, 2001, as amended and superceded by rule 4 of Cenvat Credit Rules 2002, provides that Cenvat credit in respect of capital goods received in factory in a financial year shall be taken only for an amount not exceeding 50 per cent of duty paid on such capital goods in the same financial year. Balance 50 per cent can be availed in any subsequent year provided that capital goods are still in possession and use of the manufacturer of the final product in such subsequent years. The Ministry clarified on 5 May 2000 that balance credit may be taken in subsequent financial year subject to the capital goods still being in use and in possession of the assessee.

10.4.1 M/s. National Aluminium Company Ltd., Angul in Bhubaneswar I commissionerate, availed of balance 50 per cent Cenvat credit of Rs.6.02 crore in April 2002, of Rs.6.10 crore in April 2003, of Rs.11.95 crore in April 2004 on capital goods received during 2001-02, 2002-03 and 2003-04, respectively before installation and actual use of the said goods which were either lying with co-ordinator of the expansion programme of the captive power plants or partly issued to construction site after availment of credit. Expansion programme of power plants of both units was under progress and production had not commenced by the time the assessee availed of the balance 50 per cent credit. Therefore, availing of the balance credit of Rs.24.07 crore was incorrect.

On this being pointed out (February 2004), Ministry stated (August 2005) that so long as capital goods were in possession of the manufacturer it could not be said that the manufacturer was not using capital goods in his factory of manufacture.

Reply of the Ministry is not borne from the provisions of rule 57AC (2)(b) ibid. Further deletion of word 'use' from rule 4(2)(b) of Cenvat Credit Rules with effect from 10 September 2004 corroborates audit views. In a similar case Ministry had admitted the objection in December 2003.

10.4.2 Similarly, M/s. Jayaswals NECO Ltd., M/s. Raipur Alloys and Steel Ltd. and M/s. Ambuja Cement Eastern Ltd. in Raipur commissionerate, M/s. IOCL Vadodara in Vadodara I commissionerate and M/s. Maruti Udyog Ltd. in Gurgaon commissionerate availed balance fifty per cent Cenvat credit of Rs.3.31 crore in April 2004 on capital goods received during 2003-04. Assessees availed/utilised the credit before installation and actual use of the capital goods which was incorrect.

On this being pointed out (between July 2004 and January 2005), the department stated (March and April 2005) that Cenvat Credit Rules did not provide for installation of capital goods as pre-requisite for taking Cenvat credit and keeping of capital goods itself would imply their possession and use. In one case it also stated that though installation work was completed on 13 August 2004 right to avail Cenvat credit stood unaffected.

Reply of the department was not tenable as rule 4(2)(b) clearly prescribed that possession and use of capital goods for availing Cenvat credit were pre-conditions. Further deletion of word "use" from rule 4(2)(b) with effect from 10 September 2004 also supported audit stand.

Reply of the Ministry had not been received (January 2006).

10.4.3 Three other assessees in Mumbai III, Pune I and Thane II commissionerates, availed initial 50 per cent of Cenvat credit on capital goods during 2000-01, 2001-02 and 2003-04. Balance 50 per cent of Cenvat credit amounting to Rs.55.96 lakh was incorrectly availed in subsequent years even though the said capital goods were not put to use.

On this being pointed out (February 2004, January 2002 and September 2004), department in one case intimated (September 2004) recovery of Cenvat credit of Rs.4.90 lakh. In remaining two cases, it stated (May 2004 and January 2005) that there was no legal requirement of installation/use of capital goods for availing of balance 50 per cent of credit and quoted decision of tribunal in case of M/s. Ballarpur Industries Ltd. {2003 (156) ELT 423 (Tri-Mumbai)} in favour of their argument.

Department's reply is not tenable in view of tribunal's subsequent judgment in the case of M/s. Parasrampuria Synthetics {2004 (170) ELT 327 (Tri-Del)} wherein it was held that balance 50 per cent credit could not be allowed without installation and use of goods in financial year during which it was claimed. Further, decision in the case of M/s. Ballarpur Industries Ltd. was also reckoned with in case of M/s. Parasrampuria Synthetics.

Reply of the Ministry had not been received (January 2006).

10.5 Cenvat credit availed but amount not paid on final goods

Rule 57CC of Central Excise Rules, 1944 and rule 6(3)(b) of Cenvat Credit Rules 2001/2002, stipulate that where manufacturer is engaged in manufacture of any final product which is chargeable to duty as well as any other final product which is exempt or chargeable to nil rate of duty and he takes credit of specified duty on any input which is used in relation to manufacture of both categories of final products, whether contained in the said final product or not, and opts not to maintain separate accounts of common inputs, he shall pay an amount equal to eight per cent of price of second category of final product charged for sale of such goods, at the time of clearance from the factory.

Above position was further clarified by the Board on 19 August 2002 wherein manufacturer had no option but to reverse eight per cent of price of the exempted goods if he had taken credit on common inputs used in both dutiable and non-dutiable products.

10.5.1 Six assessees in Bhopal, Kolkata III, IV, VII, Pune I and Raigad commissionerates, availed Cenvat credit on inputs and used them in dutiable as well as exempted finished goods. No separate inventory was kept in respect of exempted category of goods. Assessees were therefore liable to pay sum of Rs.10.94 crore representing eight per cent of value of exempted goods cleared between April 2000 and June 2005. Three assessees had, however paid a sum of Rs.42 lakh, Rs.3 lakh and Rs.10 lakh representing reversal of actual credit availed on such inputs. This did not absolve assessee from responsibility of making payment of duty of Rs.10.94 crore. Differential amount of Rs.10.39 crore was required to be recovered.

On this being pointed out (between October 2003 and June 2005), the Ministry admitted objection in five cases and reported (between September and November 2005) issue of SCNs for Rs.3.27 crore out of which Rs.1.40 lakh stands recovered. In sixth case it stated (August 2005) that assessee was maintaining two separate stores for keeping raw material required for dutiable and exempted category of boilers and only on limited occasions did it transfer inputs from dutiable stores to exempted stores with reversal of appropriate credit. Ministry further stated that assessee was not required to pay eight per cent of price of the final product in view of maintenance of separate records.

Reply of the Ministry was not tenable as no separate account for items used in manufacture of exempted goods were maintained. Further, credit would not have been ab-initio available on all such inputs which were subsequently transferred for use in exempted final products. Pro

rata reversal of credit was not supported by any legal provisions. Recovery of eight per cent of price of exempted product is also required to be made in terms of Board's clarification of 19 August 2002 on which Ministry's reply is silent.

10.5.2 M/s. Orient Paper Mills, Amlai and M/s. Ispat Godawari Ltd., in Bhopal and Raipur commissionerates, engaged in manufacture of paper and paper board, sponge iron, steel ingots and billets, also produced electricity which was partly used in production of final products and partly sold outside the factory to residential colony of the staff, government offices, autonomous bodies, shopkeepers, industrial units, Chhattisgarh State Electricity Board (CGSEB), and two other manufacturers through its transmission grid. Assessees had availed credit on inputs such as furnace oil, caustic soda, hydrochloric acid, clean flo and other chemicals for generation of electricity (non-excisable). Cenvat credit so availed was utilised for payment of duty on final products. Since no separate accounts of inputs intended to be used in the generation of electricity cleared for sale were maintained and electricity valuing Rs.5.55 crore between April 2001 and October 2004 was sold, amount of Rs.44.41 lakh, being eight per cent of the price of electricity, was recoverable.

On this being pointed out (August 2004 and January 2005), the Ministry admitted the objection in principle and stated (December 2005 and January 2006) that electricity being non-excisable product, credit of duty paid on inputs used for generation of electricity sold outside factory should be recovered proportionately.

Reply of the Ministry is not tenable as Cenvat Credit Rules do not provide proportionate reversal of credit after opting of the facility of non-maintenance of separate inventory of common inputs to be used in both dutiable and non-dutiable output goods.

10.6 Incorrect availment of Cenvat credit on inputs cleared to job workers

Rule 4(5)(a) of Cenvat Credit Rules, 2002, stipulates that Cenvat credit shall be allowed even if inputs as such or after being partially processed are sent to job workers for further processing, testing, repair, re-conditioning or any other purpose, and it is established from records, challans, memos or any other document produced by assessee that goods are received back in the factory within one hundred and eighty days of their despatch to job workers. If such inputs are not received back within the stipulated period, the assessee shall pay an amount equivalent to Cenvat credit availed on such inputs or capital goods by debiting Cenvat account or otherwise.

Benefit of job work in respect of clearance of petroleum oils for generation of electricity outside the factory of production and getting back electricity is neither available under notification dated 25 March 1986 nor under rule 4 of Cenvat Credit Rules, 2001, since electricity has not been specified in Central Excise Tariff Act, 1985.

10.6.1 M/s. Gujarat Alkalis and Chemicals Ltd., Vadodara, in Vadodara commissionerate, availed Cenvat credit on naphtha and supplied naphtha to their other unit at Dahej to generate electricity on job work basis. Electricity so generated by consignee was transmitted to consignor through Gujarat Electricity Board. Since electricity has not been specified in the first schedule of Central Excise Tariff Act, 1985 and provisions of Cenvat Credit Rules also do not permit availment of Cenvat credit on fuel used outside the factory, availment of Cenvat credit of Rs.5.88 crore during the period from January to October 2001 was incorrect.

On this being pointed out (November 2001), the Ministry stated (December 2005) that the Cenvat credit scheme was basically to avoid cascading effect of taxes and it would be unfair to deny credit on technicalities.

The Ministry's contention is untenable since application of sub rule (5)(a) of rule 4 of the Cenvat Credit Rules, 2002, was restricted to cases where the goods returned from the job worker were covered under the schedule to the Central Excise Tariff Act, 1985 which was not the case here. Further, intermediate goods sent to the job worker for generation of electricity outside the factory of production did not satisfy the definition of inputs as per rule 2.

10.6.2 Fifteen assessees in eight commissionerates, engaged in manufacture of various excisable goods removed certain inputs on which Cenvat credit was availed between the years 2002-03 and 2004-05 to job workers for undertaking certain processes. Input materials sent to job workers were not received back in assessee's factory after processing even after expiry of permissible limit of 180 days. Cenvat credit amounting to Rs.1.54 crore attributable to such inputs was neither paid back nor demanded by the department.

On this being pointed out (between September 2003 and April 2005), the Ministry admitted the objection and intimated (between August and October 2005) recovery of Rs.1.20 crore in twelve cases. In one case it stated that the assesses had received back all the inputs/semi finished goods from job worker, therefore, reversal of credit was not required. Recovery of duty in two cases was awaited.

10.7 Incorrect availment of Cenvat credit of additional duties of excise

Prior to 1 March 2003, utilisation of Cenvat credit on Additional Duties of Excise (Goods of Special Importance) Act, 1957 {AED (GSI)}was restricted to payment of AED (GSI) only. Rule 3(6)(b) of Cenvat Credit Rules, 2002, was amended with effect from 1 March 2003 to allow credit of AED (GSI) for payment of duty of excise leviable under the first or the second schedule of Central Excise Tariff Act, 1985.

M/s. J.K. Industries, Banmore, in Indore commissionerate, engaged in manufacture of tyres and tubes availed Cenvat credit of Rs.5.52 crore on 16 March 2004 which related to duty paid under Additional Excise Duties (Goods of Special Importance) Act, 1957, on inputs purchased between July 1995 to July 1998. Credit so availed was utilized on 30 April 2004 for payment of basic excise duty/special excise duty on finished goods. Amendment allowing utilisation of AED (GSI) for payment of duty other than AED (GSI) was effective from 1 March 2003 with no retrospective effect, as such availment and utilization of credit for the period July 1995 to June 1998 was not admissible on 16 March 2004. Duty of Rs.5.52 crore was recoverable with interest, and penalty of Rs.5.52 crore under rules 12 and 13 of Cenvat Credit Rules, 2002.

On this being pointed out (January 2005), the department stated (January 2005) that draft SCN was under process. Subsequent verification revealed that it was issued on 22 February 2005.

The Ministry admitted the objection in principle (December 2005).

10.8 Non-recovery of Cenvat credit on inputs written off/destroyed

Board clarified vide circular dated 22 February 1995 that where Modvat credit is availed on inputs, but later on they are not used in manufacture and their value written off from stock

accounts for any reason, it should be reversed. It further clarified on 16 July 2002 that Modvat/Cenvat credit of duty availed on inputs/capital goods which are subsequently written off being obsolete or unfit for use is to be reversed.

Tribunal in the case of M/s. Mafatlal Industries vs. commissioner, Ahmedabad {2003 (154) ELT 543 (Tri-Mumbai)} held in March 2003 that when duty on finished goods burnt/destroyed in fire, etc was remitted and the manufacturer received compensation from insurance companies in respect of destroyed goods, credit of duty taken on inputs used in finished goods burnt/destroyed is recoverable from the manufacturer.

10.8.1 M/s. Telco, Jamshedpur and M/s. Indian Petrochemical Corporation Ltd. (IPCL), in Jamshedpur and Raigad commissionerates, engaged in the manufacture of motor vehicles and parts thereof, and plastic articles respectively availed Modvat/Cenvat credit on inputs received. Verification of their records revealed that they had written off materials and spares/components valuing Rs.42.38 crore in their accounts between April 2000 and March 2003. Corresponding credit of duty of Rs.4.39 crore on such inputs/components was, however, not reversed/paid back.

On this being pointed out (March 2003 and February 2004), the Ministry admitted (September 2005) the objection and stated that two SCNs for Rs.4.39 crore were issued out of which one pertaining to M/s. IPCL (for Rs.2.14 crore) had been confirmed besides imposition of penalty of Rs.2.64 crore against which assessee had gone in appeal.

10.8.2 M/s. Vinoram Ltd. and M/s. Bharat Fritz Wrener Pvt. Ltd. in Bangalore I and III commissionerates, engaged in manufacture of lathes, bearing and mills machines, industrial perfumes and flavours etc., availed Cenvat credit of duty paid on inputs received in their factory from time to time. During 1999-2000 and 2003-04, the assessees had written off raw materials valued at Rs.9.53 crore in their annual accounts declaring them as obsolete or as surplus/redundant due to non-movement of such inventories. Corresponding credit of duty of Rs.1.52 crore on such inputs was, however, not reversed from their Cenvat accounts notwithstanding the fact that the items became unfit for use for the specified purposes and thus ceased to be inputs.

On this being pointed out (November 2003 and August 2004), the Ministry stated (August 2005) that assessees had made provision for slow moving stocks in accordance with the generally accepted accounting principles and that inputs were available in the stores ledger for future utilization in production.

Reply is not tenable as Ministry did not have proof of full value of inputs not written off, hence credit was to be paid back irrespective of whether or not such inputs were capable of being used in terms of Board's clarification dated 16 July 2002.

10.8.3 M/s. Dharampal Satyapal Ltd., Barotiwala in Chandigarh commissionerate, engaged in manufacture of tobacco products viz. 'tulsi mawa mix' (heading 2404.49) destroyed some consignments of defective finished goods and raw material (inputs). However, corresponding credit of Rs.27.77 lakh availed on the inputs during April 2000 to January 2001 was not reversed.

On this being pointed out (January 2002), the Ministry stated (August 2005) that permission of destruction of goods in question and remission of duty thereon was granted on 4 January 2002 subject to reversal of Cenvat credit availed. Therefore appropriate amount of Cenvat credit would be got reversed as and when the party undertook destruction of goods.

Reply of the Ministry is not tenable as credit should have been recovered immediately on granting of permission on 4 January 2002. Since duty involved has been remitted and the assessee has already used the credit of defective unusable material leaving no proportionate credit balance in Cenvat credit account, as such there was also financial accommodation in the shape of interest of Rs.10.32 lakh for the period from February 2002 to August 2005.

10.8.4 M/s. Kalyani Sharp India Ltd. and M/s. Expogel (I) Ltd., in Pune III commissionerate, were granted remission of duty amounting to Rs.91.73 lakh in the month of July 2003 in respect of finished goods/semi finished goods, valued at Rs.5.73 crore, destroyed in fire during April 1999 and May 2001. Assessees had received compensation from insurance companies in respect of the value of goods destroyed in fire. Department did not take action to recover Cenvat credit taken on inputs used in the manufacture of goods destroyed in fire. In the absence of exact details of credit taken on inputs, the amount required to be reversed worked out to Rs.45.86 lakh at the rate of eight per cent of the value of goods destroyed and for which remission of duty was granted.

On this being pointed (April 2004), the department stated (June 2004) that as per Board's circular dated 7 August 2002, no recovery of such credit was to be made. The Ministry stated (December 2005) that delay in withdrawal of Board's circular was on account of factors like deliberation of the issue within the Board, soliciting views of the trade interests etc.

The fact remains that the tribunal decided the matter in favour of revenue in March 2003 and the Board withdrew its circular dated 7 August 2002 only on 1 October 2004. Delay in withdrawal of circular by the Board resulted in loss of revenue.

10.9 Incorrect utilisation of Cenvat credit of NCCD

Notification dated 17 May 2003 grants exemption to goods falling under heading 54.02, from whole of NCCD leviable thereon if they are manufactured from goods falling under the same heading. Further, as per explanation under rule 3 (6)(b) of Cenvat Credit Rules 2002, where the provisions of any other rule or notification provide for grant of partial or full exemption on condition of non-availability of credit of duty paid on any input, provisions of such other rule or notification shall prevail over the provision of the rules.

M/s. Central India Polyester Ltd. and M/s. Indorama Synthetics Ltd., in Nagpur commissionerate, manufactured partially oriented polyester yarn (POY) under sub-heading 5402.42 and cleared it for captive consumption by making payment of NCCD at the rate of 1 per cent ad valorem for manufacture of polyester filament yarn (drawn) falling under sub-heading 5402.43 and texturised yarn of polyester (drawn) under sub-heading 5402.32 respectively. They availed credit of NCCD of Rs.3.49 crore between June 2003 and September 2004 and utilised it for making payment of NCCD on domestic clearances of POY. Subsequently both claimed exemption from payment of NCCD on POY (drawn) on the plea that the goods were manufactured from NCCD paid POY, though on these goods NCCD stood exempted since 17 May 2003. Thus, they irregularly availed credit of NCCD of Rs.3.49 crore, and claimed exemption from payment of NCCD on POY (drawn). The assessees thus by taking credit of NCCD at captive stage cleared POY drawn without payment of NCCD.

On this being pointed out (March 2004 and January 2005), the Ministry admitted the objection and intimated (November 2005) issue of SCNs for Rs.3.30 crore. Further developments in the case had not been intimated.

10.10 Inputs credits availed for manufacture of exempted goods

As per rule 57C of Central Excise Rules, 1944, Modvat credit on inputs was not admissible if it was used in the manufacture of fully exempted final products or if the final product was chargeable to nil rate of duty.

Board in consultation with Ministry of Law, clarified on 4 January 1991 that if a manufacturer availed of Modvat credit and paid duty on exempted products on his own volition, such payments were not in the nature of duty and were to be treated as deposits, hence, credits of duty paid on inputs would not be admissible.

10.10.1 M/s. Rungta Irrigation Ltd., in Chandigarh commissionerate, engaged in manufacture of 'sprinkler irrigation system' (sub-heading 8424.10) manufactured high density polyethylene (HDPE) pipes which were cleared on payment of duty after availing of Modvat credit of duty paid on inputs which were finally used in manufacture of 'sprinkler irrigation system (final product) although final goods and parts (HDPE pipes)both attracted nil tariff rate of duty. This resulted in irregular availment of credits amounting to R.1.79 crore during October 1994 to January 1999.

On this being pointed out (between April 1997 and April 1999), the Ministry admitted the objection in principle (December 2005).

10.10.2 In case of M/s. Sidwal Refrigeration Industries Pvt. Ltd., and M/s. Intec Industries, in Chandigarh commissionerate, engaged in manufacture of roof mounted package air conditioners and their parts for railway coaches (heading 84.15) and control panels (heading 85.37), the assessee availed credits of BED and SED paid on main chassis cabinets and control panels received as parts of the air-conditioning machines from their sister unit. As parts of air conditioners attracted nil rate of SED, credit of Rs.1.77 crore availed during the period from April 2001 to October 2002 was not correct.

On this being pointed out (March 2004), the Ministry stated (August 2005) that suppliers of inputs had paid duty at instance of department and on vacation of demand, they had not claimed any refund. As such payment of SED should not be treated as duty deposit with Government. It was further stated that there was no ground for the department to deny Modvat credit to the purchaser of inputs since goods with duty paid documents were received by them.

Since SED on parts of air conditioners was unconditionally exempt under notification dated 1 March 2002, payment of duty enabled the assessees to pass on duty paid on inputs which could not be recovered.

10.11 Simultaneous availing of Cenvat credit on capital goods and depreciation under Income Tax Act.

Rule 4(4) of Cenvat Credit Rules, 2002, stipulates that Cenvat credit in respect of goods shall not be allowed in respect of that part of value of capital goods which represents amount of duty on such capital goods, which the manufacturer claims as depreciation under section 32 of Income Tax Act, 1961.

10.11.1 M/s. Mahanagar Gas Ltd., in Mumbai II commissionerate, engaged in manufacture and supply of compressed natural gas received capital goods during the years 2001-02 and 2002-03 and availed 100 per cent of Cenvat credit of Rs.4.79 lakh and Rs.134.16 lakh in

March 2004. Scrutiny of financial accounts of assessee for 2001-02 and 2002-03 revealed that they had claimed depreciation under Income Tax Act, 1961 on entire value of capital goods upto 2002-03. Availment of Cenvat credit of Rs.1.39 crore was, therefore, not correct.

On this being pointed out (July 2004), the Ministry stated (November 2005) that assessee had not availed credit in 2001-02 and 2002-03 and for regulating credit availed during March 2004, the assessee had filed revised return on 31 August 2004 to the income tax authorities excluding the duty amount.

Ministry's reply is not tenable as rules specifically restrict availment of credit of duty where depreciation was claimed under section 32 of Income Tax Act, 1961.

10.11.2 M/s. Bajaj Auto Ltd., in Pune I commissionerate, engaged in manufacture of motor vehicles, claimed Cenvat credit on dies and moulds. Dies were cleared to vendors/job workers on payment of duty. The assessee then capitalized excise duty in books of account in respect of such dies on which excise duty was paid while clearing them to vendors/job workers. They also claimed depreciation on value including excise duty element under section 32 of Income Tax Act till the dies were received back from vendors. Again, the assessee availed Cenvat credit on receipt of these dies from vendors. This resulted in incorrect availment of Cenvat credit to the extent of Rs.69.21 lakh.

On this being pointed out (September 2003), the Ministry admitted the objection (September 2005).

10.12 Loss of revenue due to allowance of deemed credit in respect of unprocessed fabrics in stock

10.12.1 Rule 9A of Cenvat Credit Rules, 2002 (inserted on 25 March 2003) envisages that manufacturers of processed fabrics were allowed credit of duty paid on inputs of processed fabrics lying in stock or in process or contained in finished products lying in stock as on 31 March 2003 subject to availability of the documents evidencing actual payment of duty thereon. In case where manufacturer was unable to produce documents evidencing actual payment of duty he was allowed to take such credit on deemed basis {as per provisions contained in sub rule (2) and (3) of rule 9A} at rates as were notified by Central government.

While interpreting rule 57G(2), tribunal in case of M/s. Machine builders {1996 (83) ELT 576} held that intention was not to deem that inputs which actually did not suffer duty were inputs which suffered duty, the purpose was to ensure benefit to those who used inputs in manufacture of which, duty had actually been paid, but it might not have been possible to produce duty paying documents.

Nine assessees, in Jaipur II and Surat I commissionerates, engaged in manufacture of processed fabrics from duty free unprocessed fabrics availed deemed credit of Rs.1.26 crore on inputs (unprocessed fabrics) lying in stock or in process or contained in finished goods as on 31 March 2003. Since duty was not leviable on unprocessed fabrics lying in stock or in process or contained in finished goods, grant of deemed credit was incorrect which resulted in loss of revenue of Rs.1.26 crore.

On this being pointed out (July 2004), the Ministry confirmed the facts (August 2005) in two cases. In remaining seven cases, it stated (December 2005) that credit was taken as per rule 9A as the grey fabrics were manufactured out of duty paid yarn/fibre. It further stated that

though the yarn/fibre was not directly used by the independent processors, grey fabrics used contained duty paid yarn/fibre.

Reply of Ministry is not tenable as the assessees procured grey fabrics which did not suffer duty. Further grey fabrics was not specified input for availing deemed credit under notifications which was in force till 31 March 2003 and hence grant of deemed credit on stock of grey fabrics lying in stock as on 31 March 2003 was incorrect.

10.12.2 As per notification dated 1 March 2001 (as amended on 29 June 2001) and 1 March 2002, government allowed deemed credit ranging from 20 per cent to 66.66 per cent of aggregate of duty of excise leviable under Central Excise Act, 1944, and Additional Duty of Excise (Goods of Special Importance) Act, 1957 on the final product declared therein. Grey fabrics had not been declared as inputs.

M/s. Saroj Textiles, in Kanpur commissionerate, engaged in manufacture of processed fabrics out of grey fabrics, received on job work basis from outside availed and utilized deemed credit of Rs.98.30 lakh during the period from March 2001 to March 2003, even though grey fabrics were not leviable to basic duty and additional duty {under Additional Duty of Excise (Goods of Special Importance) Act, 1957} and were not declared as an eligible input. Allowance of deemed credit was not correct.

On this being pointed out (June 2004), the Ministry stated (December 2005) that deemed credit scheme was introduced to complete the Modvat chain and in no way provided credit where no duty incidence had been suffered on the inputs. It was further stated that this issue had recently been taken up in litigation and the CEGAT, New Delhi had held (November 2002) that the assessee was entitled to deemed credit.

Reply of the Ministry does not address the issues raised in audit.

10.13 Excess availment of Cenvat credit on grinding media

Rule 4 of Cenvat Credit Rules stipulates that Cenvat credit in respect of capital goods including their components, spares and accessories, shall be taken only for an amount not exceeding 50 per cent of duty paid on such capital goods in the same financial year and balance of Cenvat credit may be taken in subsequent financial year.

Tribunal in the case of collector, Mumbai vs. New Heaven Engineering Co. Pvt. Ltd. {1994 (72) ELT 307) decided that grinding steel balls (rough shaped) are used solely and principally with the particular kind of machine and hence are required to be classified alongwith machines under heading 84.74

M/s. Hindustan Zinc Ltd., Rampura and three others in Jaipur II commissionerates, engaged in manufacture of zinc concentrate/lead concentrate and cement allowed Cenvat credit on grinding media balls treating them as inputs for manufacture of cement. Grinding balls were an integral part of grinding mill/ball mill {1998 (99) ELT 278} and were capital goods. So credit thereon was admissible to extent of 50 per cent (instead of 100 per cent) in the same financial year. Omission resulted in excess allowance of credit amounting to Rs.72.53 lakh.

On this being pointed out (between August 2004 and January 2005), the Ministry stated (December 2005) that Tribunal in its various decisions had held grinding media as inputs.

Reply of the Ministry is not tenable as the decision of tribunal relied upon by the Ministry were given under the Modvat rules which were no more in existence. Even under Modvat

rules, decision of CEGAT, treating grinding media as input, given in case of M/s. Indian Rayon & Industries was appealed against in Rajasthan High Court (OTR/04/2002-40 I). Hence there were differing decision of tribunals and the matter remained unresolved.

10.14 Availment of Cenvat credit on the basis of invalid documents

Rule 57AE of Central Excise Rules, 1944, specifies the documents on basis of which Cenvat credit may be taken. Supplementary invoice was eligible for grant of credit except where additional duty became recoverable from manufacturer of inputs or capital goods on account of any non-levy or short levy of duty by reason of fraud, collusion or any willful mis-statement or suppression of facts in contravention of any provisions of the Act or rules made thereunder with intent to evade payment of duty.

10.14.1 M/s. Ispat Industries Ltd., in Mumbai VII (now Raigad) commissionerate, availed Cenvat credit of Rs.68.89 lakh on basis of supplementary invoice issued by M/s. Ispat Metallics India Ltd. (manufacturer-supplier) in respect of oxygen supplied to the assessee during the period from 1 October 2000 to 15 March2001. Test check of records of manufacturer revealed that they had neither maintained production records shown in the monthly return nor issued any excise invoice for clearance of oxygen during the period from 1 October 2000 to 15 March 2001. Manufacturer had filed declaration under rule 173B only on 28 February 2001. Hence for the period from 10 October 2000 to 28 February 2001 the fact of manufacture and supply of oxygen to the assessee was suppressed from department by supplier.

On this being pointed out (November 2002), the Ministry admitted the objection and intimated (August 2005) that amount had been recovered but SCN had been issued (September 2004) for appropriation of duty already recovered, imposition of penalty and recovery of interest.

10.14.2 M/s. Aditya Cement, in Jaipur II commissionerate, took Cenvat credit amounting to Rs.35.99 lakh for which no valid document was available with them. In fact, assessee had taken credit on these goods earlier (March and June 1994), which was disallowed. Matter was pending in appeal before commissioner (appeals) till date. Taking of suo-motu credit on such goods, which were subject matter of appeal was not correct.

On this being pointed out (July 2004), the Ministry admitted the objection in principle (December 2005).

10.15 Excess availment of Cenvat credit

Rule 8 of Central Excise (Valuation) Rules, 2000, envisages that where excisable goods are not sold by the assessee but are used for consumption by him or on his behalf, in production or manufacture of other articles, the value shall be 115 per cent of the cost of production or manufacture of such goods.

M/s. Ranbaxy Laboratories Ltd., in Chandigarh commissionerate, engaged in manufacture of bulk drugs (heading 29.42) and medicinal formulations (heading 30.03), besides exporting 'bulk drugs' under rebate of duty, also transferred provastatin sodium (bulk drug) on payment of duty to their formulation unit located within the same premises, at value which was nearly thrice higher than cost of production. For duty paid in bulk drug unit, they availed credits in formulation unit. Modus operandi for overvaluation was to artificially inflate price of bulk

drug so that surplus credits, mainly on account of export under rebate of duty, could be transferred and utilised in the formulation unit. This resulted in excess transfer/availment of credit amounting to Rs.38.09 lakh during the year 2001-02.

On this being pointed out (March 2003), the Ministry admitted the objection in principle (December 2005).

10.16 Incorrect passing on Cenvat credit to buyers of exempted goods

Erstwhile rule 57CC of Central Excise Rules, 1944 and now rule 6 of Cenvat Credit Rules, 2001/2002, envisages that where an assessee manufactures final products which are chargeable to duty as well as exempted goods but avails credit of duty on inputs meant for use in both categories of final products, and does not maintain separate accounts, he shall pay an amount equivalent to eight per cent of the total price of the exempted goods. The amount so payable is in lieu of Cenvat credit availed on inputs used in exempted goods and hence liability is to be borne by the manufacturer himself.

In case of M/s. Vimal Moulders (India) Ltd., CESTAT held that amount of eight per cent paid by manufacturer but collected from customer was to be deposited with Central government as excess collection of duty as per provisions of section 11D of Central Excise Act, 1944 {2004 (164) ELT 302}.

M/s. Electronic Corporation of India Ltd., M/s. Kesoram Spun Pipe and Foundry and M/s. Larsen and Toubro Ltd., in Hyderabad III, Kolkata IV and Pondicherry commissionerates, manufacturing both dutiable and exempted goods availed Cenvat credit on common inputs but did not maintain separate account. While clearing exempted goods or goods chargeable to nil rate of duty assessees paid Rs.52.92 lakh (i.e. Rs.13.35 lakh + Rs.28.02 lakh + Rs.11.55 lakh respectively) which was equal to eight per cent of the exempted goods from Cenvat account. Assessees at the same time collected such amount in the name of excise duty from customers between April 1999 and August 2004. Since there was no provision to collect such amount from customer, such collection ought to have been paid to the Government as per section 11D of the Act.

On this being pointed out (between July 2000 and October 2004), Ministry admitted (August 2005) the objection in two cases (viz M/s. Electronic Corporation India and M/s. Kesoram Spun Pipe and Foundry) and stated in the case of M/s. Larsen and Toubro Ltd. that excise duty had neither been charged to the buyer nor received.

The reply of the Ministry is not borne out by invoices issued in this case, which indicate value of goods, BED and central sales tax charged separately. Since eight per cent had been charged as BED on them, amount was recoverable under section 11D of Central Excise Act, 1944 in terms of Board's circular dated 12 November 2001.

10.17 Availment of inadmissible Modvat credit

As per erstwhile rule 57 G of Central Excise Rules, 1944 and Board's circular dated 26 November 1996, a manufacturer could take credit of duty paid on inputs within six months from the date of payment of countervailing duty on the basis of triplicate copy of relevant bill of entry.

Test check (January 1998) of central excise records of M/s. Dujodwala Resins and Tarpens Ltd. in Jammu division revealed that assessee had availed (January to September 1997) Modvat credit of Rs.54.24 lakh on inputs after six months from the dates of issue of 18 bills of entry between May 1996 and March 1997 which included inadmissible Modvat credit of Rs.40.08 lakh availed (March to July 1997) after six months from the dates of payment of CVD (September 1996 to January 1997) as recorded on nine bills of entry.

On this being pointed out (January and August 1998), the department stated (May 1998, September 1999 and March 2001) that credit had been correctly availed by the assessee within six months from dates of payment of CVD. Audit scrutiny of the attested photocopies of the relevant bills of entry furnished (March 2001) by the department in support of their reply revealed that payment dates on photocopies of nine bills of entry were not in conformity with those recorded on the original triplicate copies of the relevant bills of entry and in seven bills of entry duty payment dates were not in conformity with the Mumbai customs house record. The remaining two bills of entry could not be confirmed due to illegible name of the concerned customs house recorded on the photocopies. On this again being pointed out (November 2003), the department persistently maintained that the fact of tampering/alteration of duty payment dates by the assessee could not be established in absence of original triplicate copies of the bills of entry which had reportedly been destroyed

Audit rebuttal to department's reply was issued in December 2004 whereupon it admitted (April 2005) that dates verified by audit were in conformity with the duty payment dates in the custom house and that disciplinary action was being initiated against the officer concerned for not issuing a protective demand to the assessee when audit objection was received (August 1998). It was further stated that the assessee had paid (February and March 2005) Rs.12.26 lakh besides promising to pay the balance and that department was contemplating initiation of prosecution proceedings against him after examining the documents, but alleged that demand could not be raised due to the receipt of audit objection after six months from the relevant date prescribed for raising demand under the Act/Rules.

Contention of the department was not tenable as demand could have been raised within five years from the relevant date as per proviso to section 11A of the Act and rule 57I. Failure of the department in not taking immediate action resulted in demand becoming time barred.

The Ministry admitted the objection in principle (November 2005).

10.18 Other cases

In 393 other cases of grant of Modvat/Cenvat credit, the Ministry/department had accepted objections involving duty of Rs.7.13 crore and reported recovery of Rs.4.70 crore in 379 cases till January 2006.

CHAPTER XI : VALUATION OF EXCISABLE GOODS

Ad valorem rates of duty are charged on a wide range of excisable commodities. Valuation of such goods is governed by section 4 of Central Excise Act, 1944, read with Central Excise (Valuation) Rules, 1975 and Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000. Valuation of excisable goods introduced with effect from 14 May 1997 with reference to retail sale price is governed by section 4A. Some illustrative cases of short levy due to incorrect valuation are narrated in the following paragraphs :

11.1 Revenue foregone due to non-valuation of branded goods on MRP basis

Section 4A of Central Excise Act, 1944, empowers Central government to charge duties of excise on specified goods with reference to maximum of retail sale price (MRP). In response to Audit Report 1996-97, the Ministry stated that the primary objective for introduction of MRP was to check undervaluation to safeguard Government revenue. It was also stated that the scheme was meant to prevent revenue loss due to adoption of lower assessable value by job workers in respect of goods manufactured and cleared by brand owners. Having been vested with requisite powers by Parliament, it was imperative that Government plug revenue leakage expeditiously.

11.1.1 Test check revealed that 17 assessees, in 13 commissionerates, manufacturing motor vehicles, two and three wheelers, IC engines etc. got automobile parts manufactured by vendors at contract price (procurement price). Vendors paid duty on this contract price. When goods were sold in the market as spare parts, the assessees used brand name with MRP rate on the packages. Sales were made through dealers adopting only net dealer price. Test check of procurement prices and net dealer prices of various spare parts, procured from vendors revealed that net dealer prices were higher than the procurement prices. This difference between procurement price and dealer price was due to adoption of lower assessable value at job workers end and very high MRP at the time of clearance under brand name of the owner. MRP is fixed taking into account, the value of advertising/selling expenses and brand value. Non-inclusion of branded automobile spare parts within the ambit of section 4A, resulted in revenue of Rs.178.16 crore being foregone during 2001-02 and 2004-05.

11.1.2 M/s. Menon Pistons Ltd. and M/s. Menon Piston Rings Pvt. Ltd. in Pune II commissionerate and M/s. NRB Bearing Ltd. in Aurangabad commissionerate were engaged in manufacture and clearance of automobile spare parts to original equipments (OE) manufacturers as well as to the replacement market i.e, dealers and distributors. Clearance to OE manufacturers was as per purchase orders. However, in case of clearances to the replacement market, the goods were packed, affixed with brand name and MRP labels and sold on payment of duty at transaction value. It was noticed that value under section 4A after abatement of 40 per cent from MRP would be ten to 20 per cent higher than transaction value. Had the goods being cleared under MRP tag been brought under ambit of section 4A, assessee would have paid higher excise duty. Non-inclusion of branded automobile spare parts within the ambit of section 4A, resulted in escapement of duty of Rs.1.12 crore on goods cleared between April 2003 and January 2005.

11.1.3 M/s. Diparneena Investments Pvt. Ltd., in Nasik Commissionerate, engaged in manufacture of electric distribution board cleared them after affixing MRP on each packet. Goods not being covered under section 4A, duty was discharged on the value at which such

goods were cleared to the marketing company who finally sold them based on printed MRP. After allowing abatement at 40 per cent from MRP, assessable value would be thrice higher than value at which duty was being paid. Had the goods being cleared under MRP been brought under the ambit of section 4A, the assessee would have paid higher excise duty. Non-inclusion thereof resulted in short collection of duty amounting to Rs.3.50 crore between April 2003 and December 2004.

11.1.4 M/s. Rishivally Bio Tech Pvt. Ltd., in Thiruvananthapuram commissionerate, manufactured and cleared medicated plaster (sub-heading 3004.90) under brand name 'plastaid' for M/s. Hindustan Latex Ltd., and paid duty on value based on contract price, whereas the products were sold in the market with MRP affixed on them. Non-inclusion of medicated plaster under MRP based assessment, resulted in revenue of Rs.11.79 lakh being foregone for the period April 2002 to October 2004.

On the above being pointed out (between August 2003 and May 2005), the Ministry stated (October/November 2005) that assessees were not manufacturer and were not liable to pay duty with reference to section 4A. Government had not yet issued notification covering the products under MRP.

The fact remains that, had the Government covered automobile parts under section 4A, interest of revenue could have been protected.

11.2 Undervaluation due to non-inclusion of additional considerations

11.2.1 Notification dated 13 May 2002 as amended on 21 June 2002, provides that all petroleum products cleared from specified refinery would be exempted from so much of the amount of excise duties as is in excess of the amount collected at the rate of 50 per cent of each of the duties.

As per provisions of section 4(1)(a) of Central Excise Act, 1944 read with rule 6 of Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, where excisable goods are sold in the circumstances specified in clause (a) of sub-section (1) of section 4 of the Act except the circumstances where price is not the sole consideration for sale, the value of such goods shall be deemed to be the aggregate of such transaction value and the amount of money value of any additional consideration flowing directly or indirectly from the buyer to the assessee.

M/s. Bongaigaon Refinery and Petrochemicals Ltd. and M/s. IOCL both situated in Shillong commissionerate, cleared petroleum products against payment of duty at eight per cent of BED availing exemption under notification dated 13 May 2002 for onward sale through their marketing terminals/marketing agents on uniform cum-duty price. Records of the assessees revealed that the difference of excise duty allowed through exemption notifications mentioned above (16 per cent realized from the customers minus eight per cent paid to Government) amounted to Rs.747.90 crore for the years 2002-03 and 2003-04 which was received back from the marketing terminals/marketing agents and credited to the company's profit and loss account as "north east refinery benefits". Since this amount was received by the assessees as an additional consideration in relation to the sale of goods, it was required to be added to the assessable value of the goods cleared from the refineries and entailed differential duty of Rs.59.83 crore.

On this being pointed out (August 2005), the Ministry stated (January 2006) that the amounts transferred by marketing companies to the refineries were their internal fund flows which could not be treated as additional consideration.

Reply of the Ministry is not tenable as the exempted amount of duty was recovered from the customers through marketing companies and passed back to the assessees and hence it was additional consideration flowing indirectly to the assessees.

11.2.2 Board's circular dated 1 July 2002 read with circular dated 12 December 2002 clarifies that pre-delivery inspection (PDI) charges and cost of after sales service (free service charges) provided by dealer of vehicle during warranty period are includible in transaction value with effect from 1 July 2000.

M/s. Fiat India Pvt. Ltd. and M/s. Tata Motors Ltd., in Mumbai II and Pune I commissionerates, cleared motor vehicles to various dealers appointed by them. Agreement entered with dealers revealed that they were required to carry out pre delivery inspection of the vehicles, free after sales services and incur expenses on advertisement. Cost of these services was incurred by dealers out of dealer's margin/discount passed on by the assessee. As per provisions cited above, cost of the services was includible in assessable value. Non-inclusion thereof resulted in short levy of duty of Rs.15.84 crore for the period from 1 July 2000 to 30 September 2003.

On this being pointed out (June 2003 and January 2004), the Ministry admitted the objection and stated (October/November 2005) that demand of duty of Rs.3.02 crore with penalty of Rs.3.02 crore had been confirmed in February 2005 on account of PDI and after sale service charges but M/s. Fiat India Pvt. Ltd. had preferred appeal with CESTAT. Another SCN for Rs.3.90 crore on account of advertisement charges to M/s. Fiat India Pvt. Ltd. and two SCNs for Rs.14.13 crore to M/s. Tata Motors Ltd. had also been issued which were pending adjudication.

11.2.3 Government of Maharashtra introduced package incentive scheme for deferred payment of sales tax whereby assessee was allowed to collect sales tax from the buyer, retain it and repay it after prescribed period. Government thereupon amended provisions of Sales Tax Act and issued a notification in November 2002 providing further incentive for premature repayment of sales tax liability.

Five assessees in Pune I, III, Nagpur and Nasik commissionerates, engaged in manufacture of excisable goods had opted for premature repayment of sales tax deferred liability under the scheme. Scrutiny of their financial records revealed that they had received abatement of Rs.24.84 crore due to premature repayment of sales tax liability accrued upto March 2002 and March 2004 at net present value (NPV). Difference between actual sales tax collected from customers and payment made at NPV was retained by them as income in the respective annual accounts. Non-inclusion of sales tax amount collected but not paid or payable to the Government in the assessable value resulted in undervaluation of goods with consequential short levy of Rs.3.53 crore.

On this being pointed out (January and March 2005), the Ministry admitted the objection in principle (November 2005).

11.2.4 M/s. Diamond Beverages Pvt. Ltd., in Kolkata IV commissionerate, manufacturing aerated water (heading 22.02) and syrup (sub-heading 2108.10), sold syrups in canisters of 18 litre capacity to different dealers having dispensing machines supplied by M/s. Taratala Soft

Drinks Pvt. Ltd. who was a related person of the assessee (as confirmed by the assessee on 16 June 2003). The canisters were fitted to dispensing machines which had an inbuilt system to mix syrup, water and carbon-di-oxide gas to produce aerated water. Dealers then sold such aerated water in cups to ultimate customers. The assessee while clearing syrup to the dealers also supplied appropriate number of cups and gases (in cylinder) along with such syrup from the factory paying duty only on value of syrup. Audit noticed from the agreement with dealers and the related person of the assessee that (i) the dealer would get dispensing machine free of cost, (ii) would have to purchase appropriate number of cups alongwith carbon-di-oxide gas, and (iii) would have to pay annual maintenance charges for such machines. The assessee recovered all such charges from the dealers through his related person but did not include them in the assessable value of syrup. This resulted in short levy of duty of Rs.83.10 lakh during the period from April 2001 to February 2003.

On this being pointed out (July 2003), the Ministry admitted the objection and intimated (August 2005) issue of SCN for Rs.2.47 crore for the period from April 1999 to December 2004.

11.2.5 M/s. Vesuvius India Ltd., in Kolkata V commissionerate, manufacturing refractory products which included mono block stopper, ingate sleeve and other ceramic parts of the plant and also powder –mix coating material of blast furnace cleared such capital goods to iron and steel industry. In connection with the sale of such goods, the assessee also charged customers for providing technology services like tube changer device and robotic gunning of blast furnace stack through machines and personnel provided by them. Scrutiny revealed that the goods were high technology replacement parts and/or application materials and could be consumed within the plant only with the help of such advanced technology services provided by the assessee which therefore formed an integral part of the sale. The assessee collected 'service charge' and 'machine hire charge' over and above the assessable value but did not include the same in the value. Non-inclusion of this charge resulted in short levy of duty of Rs.80.08 lakh during the period between April 1999 and December 2000.

On this being pointed out (July 2003), the Ministry admitted the objection (December 2005).

11.2.6 M/s. HPCL (Suryapet), M/s. IOCL (Siliguri) and M/s. BPCL (terminal) Kharirohar and Siliguri, in Hyderabad III, Rajkot and Siliguri commissionerates, engaged in manufacture and sale of petroleum products cleared MS and HSD oil through dealers and also through their own outlet viz., company owned and company operated (COCO) outlets in different zones. Assessable value of the products cleared through dealers and COCO outlets remained the same. But in cases of goods cleared to COCO outlets, dealers' margins in the name of COCO charges and delivery charges was retained by assessees who owned such outlets. Such dealers' margins should therefore have formed part of assessable value as per rule 9 of the rules, ibid. Non-inclusion of dealers' margins resulted in short payment of duty of Rs.64.18 lakh between July 2000 and April 2004.

On this being pointed out (between September 2003 and June 2004), the Ministry admitted the objection and intimated (December 2005) recovery of Rs.12.26 lakh.

11.2.7 M/s. Oil and Natural Gas Commission (ONGC), Hazira in Surat I commissionerate, supplied superior Kerosene oil (SKO) to M/s. IOCL, charging higher rate than the price fixed under administered price mechanism. Duty was paid on the administered price. Records revealed that an amount of Rs.1.79 crore was recovered as additional

consideration during November and December 2000 on which no differential duty was paid. This resulted in short levy of duty to the extent of Rs.14.31 lakh.

On this being pointed out (June 2001), the department stated (September 2001) that except for above two months ONGC had paid duty at higher value though they got lower value for their products. Department, however, issued protective demand to the assessee in October 2001 which was pending adjudication.

The reply of the department is not tenable in view of the fact that additional consideration had been retained by the assessee.

Reply of the Ministry had not been received (January 2006).

11.3 Undervaluation due to adoption of lower mutually agreed price

Section 4 as effective from 1 July 2000 brought the concept of transaction value. The Ministry in circular dated 30 June 2000 clarified that but for the normal value being replaced by transaction value, there was no difference in the scheme of valuation of petroleum products under the old section 4 and new section 4 and that the provisions of new section 4 when applied to the administered price of petroleum products should not make any material difference in assessable value.

Five terminals of M/s. IOCL at Bhatinda, Jalandhar, Jaipur, Jodhpur and Sangrur in Jaipur I, II, Ludhiana and Jalandhar commissionerates were engaged in storage and marketing of various petroleum products received in their bonded warehouse, stock of MS, HSD and SKO etc. from their refineries. The IOCL terminals apart from clearing the products to their own distribution outlets also cleared MS, HSD and SKO etc. to terminals/depots belonging to other oil companies like M/s. BPCL and M/s. HPCL on payment of duty on assessable value which was much less than that charged from their own outlets/terminals.

It was observed that though the administered price mechanism was dismantled from April 2002, prices of petroleum products continued to be monitored and regulated by Oil Co-ordination Committee (OCC). Basic price structure of the products which formed the basis for determination of retail outlet prices charged from the ultimate consumer remained uniform for all the oil companies. As such adoption of lower assessable value at the stage of clearance of the products by IOCL installations to other oil companies resulted in lower duty realisation. Clearance of products at lower (agreed) rates resulted in inflow of extra consideration to the other oil companies from ultimate consumers because the benefit of lower excise duty was not passed on to the ultimate consumer retail sale price having remained same. Accordingly, the price charged did not remain the sole consideration for sale and, hence, could not be considered as 'transaction value' for the purpose of levy of duty. The differential duty lost on the clearances of MS and HSD made to M/s. BPCL and M/s. HPCL terminals and their depots during April 2003 to September 2004 amounted to Rs.27.76 crore.

On this being pointed out (between July 2003 and August 2004), the department in respect of two terminals (Bhatinda and Sangrur) intimated (May 2005) that SCNs for Rs.5.90 crore covering clearance upto 31 March 2004 had been issued and in respect of Jalandhar and Jodhpur that SCNs were being issued. Reply in respect of Jaipur had not been received.

The Ministry stated (November 2005) that the transactions had taken place in accordance with an agreement entered into between IOCL and other oil marketing companies and the

price charged was the sole consideration for sale. It further stated that the transactions satisfied the conditions laid down in section 4 leaving no ground for invoking the provisions of Valuation Rules.

Reply of the Ministry is not tenable as the price mutually agreed upon by the oil companies cannot be considered as transaction value in terms of section 4(i)(a) as products so cleared were actually sold by other petroleum companies at the same price at which their own products were sold. The clearance by IOCL to other oil companies at lower assessable value was thus not based upon purely commercial considerations and the assessable value was to be determined in terms of rule 11 read with rule 7 of the Valuation Rules.

11.4 Undervaluation of goods cleared for job work or sold through job worker

11.4.1 Section 4 of Central Excise Act, 1944, as amended with effect from 1 July 2000, read with rule 8 of Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, provides that where excisable goods are not sold by the assessee but are used for captive consumption by him or on his behalf in the production or manufacture of other articles, the value shall be 115 per cent of the cost of production or manufacture of such goods.

M/s. Alloy Steel Plant (a unit of SAIL), Durgapur, in Bolpur commissionerate, engaged in manufacture of articles of iron and steel stock transferred some excisable products like billets, rounds and high tensile bars on payment of duty for conversion job. As this transaction was not a sale, the assessee was required to determine the value of the product on cost basis. However, the assessee undervalued the products arbitrarily and treated such value as the assessable value. Incorrect determination of price thus led to undervaluation as well as short levy of duty of Rs.2.97 crore on clearances during the year 2002-03.

On this being pointed out (March 2004); the Ministry admitted the objection and intimated (September 2005) issue of demand for Rs.15.65 crore in August 2005.

11.4.2 Notification dated 25 March 2003 prescribed that merchant manufacturer manufacturing goods under chapters 61 and 62 on his account, could authorise job worker to pay duty leviable on goods on his behalf on clearance of the same from job worker's end and the job worker so authorized undertook to discharge all liabilities and comply with the provisions of these rules.

M/s. Indian Rayon and Industries Ltd., Bangalore in Bangalore I commissionerate, engaged in manufacture of ready made garments supplied raw material to job worker free of cost. The job worker after carrying out processing, returned the ready made garments to assessee on payment of duty on the assessable value determined at mutually agreed value. The assessee after carrying out processes like packing, affixing brand names etc cleared the goods without payment of duty. Audit noticed that the value adopted for payment of duty by job worker was much lower than 60 per cent of retail sale price declared by the assessee and resulted in short levy of duty of Rs.4.62 crore from January 2004 to April 2004.

On this being pointed out (June 2004), the Ministry admitted the objection (November 2005).

11.4.3 M/s. Saralee Household and Body Care India Pvt. Ltd. (unit I), in Chennai III commissionerate, manufactured shoe polish (sub-heading 3405.10) and cleared them to Saralee godown on payment of duty on MRP basis (goods were notified under section 4A). Assessee also cleared shoe polish in bulk to job worker for repacking into smaller containers,

adopting value determined on cost basis under section 4. Such clearance in bulk was not on sale and the job worker did not take credit of the duty paid by the assessee. The job worker transferred the repacked goods to Saralee godown without payment of duty availing SSI exemption for unit located in a rural area. Sale of repacked goods took place only from Saralee godown to stockist/dealer/customer. By getting the goods repacked through job worker and eventually selling branded goods, the brand name owner avoided payment of duty of Rs.90.75 lakh during the period from April 2003 to March 2004.

On this being pointed out (November 2004 and February 2005), the Ministry stated (December 2005) that the goods cleared in bulk was not a packaged commodity at the time of removal to the job workers place in rural area and therefore, there was no requirement to adopt MRP.

Reply is not tenable as section 4A was introduced to check undervaluation of goods. By getting the goods repacked through job worker and eventually selling branded goods, the assessee avoided payment of duty under section 4A and paid duty under section 4. Necessary provisions in Central Excise Act are needed to check avoidance of payment of duty under section 4A in such cases.

11.5 Incorrect adoption of transaction value

Section 4(3)(d) of Central Excise Act, 1944, defines 'transaction value' as the price actually paid or payable for the goods, when sold, and includes in addition to the amount charged as price, any amount the buyer is liable to pay to or on behalf of the assessee, by reason of, or in connection with the sale payable at the time of sale or any other time.

The Board, clarified on 30 June 2000 that cash discount or prompt payment discount would not form part of the transaction value unless such discount had actually been passed on to the buyer of the goods.

11.5.1 Twelve assessees, in five commissionerates, engaged in manufacture of motor vehicle parts and accessories (heading 87.08) and fasteners (sub-heading 7318.10) cleared the subject goods to M/s. TELCO on purchase order basis after abating 1.9 per cent towards bill discounting charges from the contract price. The bill discounting charges were payable by the buyer to M/s. HDFC Bank Ltd. on the basis of agreement between them. Since deduction made from contract price was paid by the buyer to the banker as bank charges, on behalf of the assessee, it was inadmissible because it was not in the nature of trade discount/cash discount/prompt payment discount and was not passed on to the customer. This resulted in short levy of duty of Rs.1.87 crore during the period from April 2000 to May 2004.

On this being pointed out (between May 2002 and October 2004), the department stated (between July 2002 and March 2005) that it was in the nature of cash discount/prompt payment discount and quoted CESTAT decision, in the case of M/s. PACE Marketing Specialities Ltd. vs. commissionerate of central excise {2004 (167) ELT 401(T)}, wherein discounts availed by the seller from the bank for immediate payment were allowed to be excluded from the value. Price discount was exhibited in invoice and the amount payable as per invoice was transaction value of which there was no flow back to assessee.

Reply of the department is not acceptable since the abatement had not been passed on to the customer; discount of 1.9 per cent was also in the nature of bill discounting charges and was not a consideration for the sale of goods. Case law is not relevant as arrangement was

between seller and bank whereas this case dealt with customer and bank. However, department had issued SCNs for Rs.52.66 lakh in respect of three assessees.

Reply of the Ministry had not been received (January 2006).

11.5.2 The Board clarified on 30 June 2000 that exclusion of cost of transportation is allowed only if assessee has shown them separately in the invoice for such excisable goods and the exclusion was permissible only for the actual cost so charged from buyers.

M/s. Thermax Ltd. and M/s. Thermax B&W Ltd., in Pune I commissionerate, engaged in the manufacture of boilers had not shown cost of transportation in invoices. Those charges were separately recovered by the assessee. Transportation charges so recovered from the buyers after the sale of excisable goods were includible in the assessable value. Non-inclusion thereof resulted in short levy of Rs.1.59 crore during the period between July 2000 and February 2003.

On this being pointed out (December 2003), the Ministry admitted the objection and intimated (November 2005) issue of SCNs for Rs.2.43 crore

11.5.3 The Board clarified on 1 July 2002 that where an assessee recovered an amount from the buyer towards cost of return fare in addition to the outward freight from the place of delivery, the amount so charged towards return freight was not available as deduction.

M/s. BPCL and M/s. IOCL, in Visakhapatnam I and Kolkata II commissionerates, cleared petroleum products to various distribution outlets located at different places on payment of duty on ex-terminal prices. Companies had been delivering goods at distribution points in hired tankers for which they collected delivery charges in the name of round trip kilo meter (RTKM) charges from dealers. The entire amount so collected on account of transportation both ways was claimed as deduction by them whereas deduction or exclusion from assessable value was permissible only for onward freight. Incorrect deduction resulted in short levy of duty of Rs.1.79 crore for the period from July 2000 to September 2004.

On this being pointed out (June and August 2003), the Ministry admitted (October 2005) the objection in one case. However in the second case it stated (December 2005) that the Tribunal had held that the transportation charges incurred for return journey of specialized vehicles were permissible for deduction {2004 (61) RLT 480 (CESTAT)}. Though the Ministry had accepted the Tribunal's decision, the Board has not withdrawn circular of July 2002, ibid.

11.5.4 Section 4A(1) of Central Excise Act, 1944, envisages that excisable goods covered under the provisions of the Standards of Weights and Measures Act, 1976 or the rules made thereunder may be notified by the Central government under sub-section (2) ibid for the purpose of levy of duty with reference to MRP (R.S.P. from 14 May 2005) after allowing permissible abatement. Accordingly toilet soaps (sub-heading 3401.19) have been notified under section 4A for MRP basis assessment.

M/s. V.V.F. Ltd., in Daman commissionerate, manufactured and cleared toilet soap (weighing 75/50 grams) valued Rs.65.93 lakh during the period from September to December 2001 to M/s. Dabur India Ltd. for free supply alongwith 'dabur lal tel'. The goods were incorrectly assessed to duty under section 4 though similar products were also cleared for sale and duty was paid on assessable value under section 4A.

On this being pointed out (February 2002), the department admitted the objection (September 2003) and stated that demands for Rs.1.17 crore for the period from February 2001 to August

2002 were issued out of which demand of Rs.0.51 crore with penalty of equal amount had been confirmed in July 2002.

The Ministry admitted the objection in principle (November 2005).

11.5.5 M/s. IOCL, in Siliguri commissionerate, engaged in warehousing and clearing of petroleum products received goods from north-east refineries under the cover of AR-3A and/or joint certificate (for pipeline products only) and subsequently cleared such goods on payment of duty. The assessee while clearing the goods of north-east origin availed of duty concession under notification dated 13 May 2002 meant for north east refineries and paid such duty on assessable value lower than that meant for products of north-east origin. The undervaluation, thus, resulted in short levy of duty of Rs.46.05 lakh between April 2003 and March 2004.

On this being pointed out (September 2004), the Ministry stated (November 2005) that they followed the principle of parity of cum-duty values irrespective of origin of the product. The fact, however, remained that even after adoption of the parity principle the transaction price differed and products of north-east origin were transacted at a lower value.

11.5.6 M/s. Bharath Aluminium Company Ltd., Korba placed an order on 30 October 2002 with M/s. Bharat Heavy Electricals Ltd. (BHEL), New Delhi for supply, erection and commissioning of pulverised fuel fired steam generator and auxiliaries at a total cost of Rs.44.40 crore. Work of design, manufacture and supply of steam generator and auxiliaries was allocated to M/s. BHEL (High Pressure Boiler Plant), Trichy at a cost of Rs.25.72 crore. The assessee was also entrusted work of system engineering, design and detailed engineering including supply of 93 drawings at a cost of Rs.3.50 crore over and above the contract price of Rs.25.72 crore. The assessee had supplied 63 drawings and collected Rs.2.37 crore till March 2003. Value of the drawings was, however, not included in the transaction value of the goods resulting in short levy of duty of Rs.41.61 lakh.

On this being pointed out (between November 2003 and March 2005), the Ministry stated (November 2005) that manufacturer did consultancy work like feasibility study/preparation of project report, erection and commissioning of boiler system etc. which were not subjected to excise duty. System engineering drawings were predominantly relatable to laying down broad parameters for each component, procurement of bought out items, erection and commissioning. The charges for erection and commissioning had been kept outside the value of manufactured item and service tax at appropriate rate was paid.

Reply of the Ministry is not tenable since system engineering comprised activities related to design and detailed engineering for the creation of product. The value of system engineering was therefore includible in the value of manufactured items. Further, since the customer had entered into separate erection and commissioning contract at cost of Rs.4.30 crore, system engineering would not cover post manufacturing activities to a large extent.

Department, however, reported issue of SCN demanding differential duty of Rs.41.16 lakh in March 2004. Further developments were awaited.

11.6 Undervaluation of goods sold through depots/stockyards

The Board clarified vide 3rd March 2003 order that where excisable goods removed from factory were sold at depot or consignment agent's premises or at any other place, assessable value of such goods would be determined with reference to the point of sale. Resultantly,

factory gate price ceased to be the basis for discharging duty liability and closing stocks lying uncleared with depots/stockyards/consignment agents but sold on or after 1 March 2003 attracted levy of duty based on actual sale price.

M/s. Rashtriya Ispat Nigam Ltd., an integrated steel plant in Vizag I commissionerate, cleared huge quantities of stocks of iron and steel products on which exemption was availed of under notification dated 1 March 2000 (remained effective upto 28 February 2003) at the time of their clearance from factory, which were lying as closing stock at depots/stockyards/consignment agents as on 28 February 2003. These stocks were actually sold from such depots/stockyards, etc. at much higher prices on or after 1 March 2003. The assessee did not, however, discharge differential duty liability on those higher prices charged from customers as per Board's clarification dated 3 March 2003 ibid. Department was asked to take necessary action towards recovery of differential duty.

On this being pointed out (September 2003), department reported (February 2005) issue of SCN for Rs.1.43 crore. Ministry stated (November 2005) that the goods were assessed at the time of removal from the factory without reference to the value at the depot and re-assessment was not consequent on withdrawal of the notification of 1 March 2000.

Ministry's reply is silent on action taken to realise the differential duty.

11.7 Incorrect valuation of inputs/capital goods cleared as such

Rule 57AB(I)(b) of Central Excise Rules and explanation thereunder provides that when the inputs or capital goods are removed from the factory, the manufacturer of the final product shall pay the appropriate duty of excise leviable thereon as if such inputs or capital goods have been manufactured in the said factory. Further, according to rule 3(4) of Cenvat Credit Rules, 2002, as applicable upto 28 February 2003 when inputs or capital goods, on which Cenvat credit has been taken, are removed as such from the factory, the manufacturer of the final products shall pay an amount equal to the duty of excise which is leviable on such goods at the rate applicable to such goods on the date of such removal and on the value determined for such goods under sub-section (2) of section 3 or section 4 or section 4A of the Act, as the case may be.

Further, rule 8 of Central Excise (Valuation) Rules, 2000, provides that where excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in the production or manufacture of other articles, the value shall be 115 per cent of the cost of production or manufacture of such goods.

11.7.1 Five assessees one each in Belapur, Delhi II, Gulbarga, Mumbai III and Nasik commissionerates, procured inputs/capital goods and availed Modvat/Cenvat credit, thereafter cleared them as such to their other units for further use in manufacture of excisable goods. Assessees discharged duty liability equivalent to credit taken which was not correct as the goods were not sold. Various expenses like freight, octroi etc. incurred for procurement of inputs/capital goods and 15 per cent were to be added to the landed cost of inputs/capital goods cleared as such for purpose of determining value for payment of duty. Non-determination of correct value resulted in short levy of duty of Rs.66.22 lakh during the period between July 2000 and February 2003.

On this being pointed out (March 2004), Ministry stated (August 2005) in one case that rule 8 of Valuation Rules was not applicable as the inputs/capital goods were not manufactured by

the assessees in their factory. In three cases it stated (October and November 2005) that objection would be revenue neutral. In one case it stated (November 2005) that the clearance made and duty paid was very much in conformity with rule 3(4) of Cenvat Credit Rules and Boards letter dated 1 July 2002.

Reply of the Ministry is not tenable in view of clear provisions of rule 57AB of Central Excise Rules, 1944/rule 3(4) of Cenvat Credit Rules 2002. Reply relating to neutrality of revenue is not relevant as assessment is to be done correctly irrespective of whether credit would be available to sister units for utilisation. Further, Boards clarification of July 2002 was not in conformity with rule 8 of Valuation Rules.

11.7.2 Tribunal in the case of M/s. Bharat Berg Ltd. vs. Collector {1995 (80) ELT 312 CEGAT} held that defective portion of C.R. coils were liable to pay duty as C.R. coils itself and not as waste and scrap.

M/s. Him Ispat Ltd., in Chandigarh commissionerate, engaged in manufacture of C.R. strips/C.R. sheets (heading 72.09/72.11) cleared 2827.810 tonne of defective H.R. Coils/H.R. narrow slit on payment of duty as waste and scrap to their own depot at value much lower than the value of 'inputs' upon which credits were taken. This resulted in short levy of duty amounting to Rs.26.77 lakh during the period 1998-99.

On this being pointed out (April 2000), the Ministry stated (November 2005) that the case of M/s. Bharat Berg Ltd. was distinct as in that case HR coils were cleared which were found unfit for galvanization.

Reply of the Ministry is not acceptable because case cited was specific to the issue reported by Audit as CEGAT had determined line of action for treatment of defective H.R. coils/H.R. narrow slit as such and not as waste and scrap for purposes of valuation and subsequent recovery of excise duty.

11.8 Undervaluation of goods cleared to related person

Where excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in any other factory of the same manufacturer, in the production or manufacture of other articles, assessable value is to be determined under section 4(1)(b) of Central Excise Act read with rule 8 of Central Excise (Valuation) Rules, 2000 on the basis of 115 per cent (110 per cent from 5 August 2003) of the cost of production or manufacture of such goods.

Section 4(3)(b) stipulates that persons shall be deemed to be related if (i) they are inter-connected undertakings; (ii) they are relatives; (iii) amongst them the buyer is a relative and distributor of the assessee or a sub-distributor of such distributor; or (iv) they are so associated that they have interest directly or indirectly in the business of each other. This section also stipulates that 'inter-connected undertakings' shall have the meaning assigned to them in clause (g) of section 2 of Monopolies and Restrictive Trade Practices Act, 1969 (MRTP Act). Section 2(g) of MRTP Act provides that two bodies corporate shall be deemed to be under the same management if managing director or manager of one such body corporate is the managing director or manager of the other.

11.8.1 M/s. Escorts Piston Ltd., formerly known as M/s. Escorts Mahale Ltd. {up to 1 November 2002 merged with M/s. Goetze (India) Ltd.} in Bangalore II commissionerate, transferred nickel iron waste and scrap (heading 72.14) to their amalgamated unit M/s. Goetze (India) Ltd. on payment of duty on the assessable value arrived at on cost basis. While

arriving at assessable value, profit margin at 15 per cent was not included and increase in cost of basic raw material not taken into account. This resulted in undervaluation of goods by Rs.2.13 crore with consequential short levy of duty of Rs.34.11 lakh during the period July 2000 and May 2003.

On this being pointed out (November 2000), the Ministry stated (November 2004 and September 2005) that though the two units had the same managing director and would merit being called as inter-connected undertaking as per MRTP Act, it would not be sufficient to bring them under rule 9 of Central Excise (Valuation) Rules, 2000 unless it was established that relationship was in terms of sub-clause (ii), (iii) or (iv) of section 4(3)(b) of Central Excise Act.

The Ministry's reply is not tenable as companies in 'related party disclosure' which is exhibited in balance sheet as per Companies Act, 1956, were shown as related. Further, the fact that the managing director was common, showed that conditions (i) and (iv) of section 4(3)(b) ibid were satisfied.

11.8.2 M/s. Gujarat Narmada Valley Fertilizers Company Ltd., in Vadodara II commissionerate, engaged in manufacture of fertilizers cleared 12490.825 tonne of concentrate nitric acid between December 2003 and March 2004 to its subsidiary company M/s. Narmada Chematur Petrochemicals Ltd. for further use in production of goods. The assessee paid duty at the rate of Rs.8600 per tonne instead of at 110 per cent of cost of production which ranged between Rs.8836 and Rs.11,858 per tonne from December 2003 to March 2004. Payment of duty on lower assessable value resulted in short levy of duty of Rs.34.31 lakh.

On this being pointed out (January 2005), the Ministry admitted the objection and intimated (September 2005) recovery of Rs.72.43 lakh in February 2005.

11.8.3 M/s. Jamipol Ltd., in Jamshedpur commissionerate, engaged in manufacture of desulphonising compound (heading 38.24) cleared products (Mag 97 and Mag 87) to M/s. TISCO Ltd., Jamshedpur, a sister concern of the assessee at a price which was lower than its cost of production during the year 2003-04. As the clearances were made by the assessee to a related person for consumption in the manufacture of final products its valuation was to be done at the rate of 115 per cent (110 per cent from 5 August 2003) of the cost of production. Incorrect valuation of products resulted in short levy of duty of Rs.13.33 lakh during the period April 2003 and March 2004.

On this being pointed out (September 2004), the Ministry stated (September 2005) that the assessee was not related and that their transaction with M/s. TISCO was purely on commercial consideration.

Reply of the Ministry is not tenable as duty had been paid (i) at a price which was less than cost of production of the products and (ii) note 16 to the schedule 15 on balance sheet and profit and loss account for the year 2003-04 of the assessee indicated that M/s. TISCO was related party of the assessee well covered in the definition of the term 'related' under section 4(3)(b)(iv) of Central Excise Act, 1944.

11.9 Other cases

In 71 other cases of grant of valuation of excisable goods, the Ministry/department had accepted objections involving duty of Rs.4.91 crore and reported recovery of Rs.2.73 crore in 58 cases till January 2006.

CHAPTER XII : EXEMPTIONS

Under section 5A(1) of Central Excise Act, 1944, Government is empowered to exempt excisable goods from the whole or any part of the duty leviable thereon either absolutely or subject to such conditions as may be specified in the notification granting the exemption. Some of the major cases of incorrect allowance of exemption noticed in audit are detailed in the following paragraphs:

12.1 Exemption for units manufacturing tobacco products situated in North Eastern States

12.1.1 Non recovery of revenue on withdrawal of exemption

Government vide notification dated 8 July 1999 allowed exemption by way of refund of duty paid on specified goods through PLA by certain manufacturers of North Eastern States. Exemption for manufacturers of tobacco products was withdrawn on 1 March 2001. By section 154 of Finance Act, 2003 (enacted on 14 May 2003) the benefit of refund of duty paid on cigarettes (chapter 24) and pan masala containing tobacco (heading 21.06 or sub-heading 2404.49) were withdrawn retrospectively from 8 July 1999. Recoveries of exemption already availed were to be made within 30 days from 14 May 2003.

Scrutiny of records of five manufacturing units engaged in manufacture of tobacco products (pan masala and gutkha), one under Dibrugarh commissionerate and four under Shillong commissionerate, enjoying benefit under the notification ibid revealed that assessees aggrieved on withdrawal of exemption filed writ petition before Guwahati High Court. They continued claiming exemption through refund. Court allowed (December 2002) them to make adjustment from their refund claims. Accordingly, four assessees, in Shillong commissionerate, adjusted Rs.46.52 crore, being their duty liabilities from November 2002 to May 2003, from their refund claims.

With withdrawal of exemption with effect from 8 July 1999, sum of Rs.101.02 crore for the period upto February 2001 had become recoverable by 13 June 2003. Assessees, however, challenged the constitutional validity of section 154 before Guwahati High Court, which stayed the recovery by their interim order dated 27 June 2003.

Section 154 of Finance Act, 2003 (already enacted on 14 May 2003) stipulated that no enforcement be made by any court, tribunal or other authority of any decree or order relating to such action taken or omitted to be taken as if the amendments made by sub-section (1) had been in force at all material times. Despite this, there was no evidence to show that department had made any attempts to pursue vacation of stay. Resultantly recovery of Government revenue to the tune of Rs.101.02 crore alongwith interest remained blocked.

12.1.2 Non recovery of duty on rejection of investment claim

Exemption was re-introduced vide notification dated 25 August 2003 with new terms and conditions for those manufacturers of tobacco products who had availed exemption benefit under notification dated 8 July 1999. Notification of 25 August 2003 as superseded and amended upto 9 July 2004 stipulated that if the manufacturer failed to make the deposit or did not invest the amount within the stipulated period, duty equivalent to the amount not so deposited or invested would be recoverable from him along with interest thereon at the rate specified under section 11AB of Central Excise Act, 1944.

Test check of records of four assessees in Shillong commissionerate, revealed that Investment Appraisal Committee had rejected investment claims amounting to Rs.22.78 crore in August 2004. The amount was, therefore, recoverable with interest. No action, however, was taken by the department for its recovery.

12.1.3 Exempted duty collected but not paid to Government

M/s. Kothari Product Ltd. Jorhat, in Dibrugarh commissionerate, charged all duties of excise in their invoices. The amount so charged amounted to Rs.7.06 crore during the period from April 2004 to December 2004 against which only Rs.0.99 crore was paid by way of debit from their Cenvat credit account. Remaining Rs.6.07 crore was not paid into Government account. Since duty had been collected from customers, benefit of the exemption notification was not available and the amount alongwith interest as stipulated under rule 8 of Central Excise Rules, 2002 was recoverable.

Reply of the Ministry on above audit observations was awaited (January 2006).

12.2 Incorrect grant of exemption on goods captively consumed

12.2.1 Rubberised tyres cord fabrics

Tyre cord fabrics (TCF) classifiable under heading 59.02 is liable to AED under Additional Duties of Excise (Goods of Special Importance Act, 1957). Notification dated 2 June 1998 granted exemption from AED to processed tyre cord fabrics falling under heading 59.02 manufactured from unprocessed TCF on which AED had been paid.

M/s. J.K. Industries, Banmore, in Indore commissionerate, manufactured dipped tyre cord fabrics and rubberized tyre cord fabrics of high tenacity yarn of nylon from purchased nylon tyre cord fabrics. TCF was dipped in chemical to produce dipped tyre cord fabrics. This dipped TCF was consumed captively for rubberisation without payment of duty. It was thereafter coated with rubber on calendering machine to produce rubberized tyre cord fabrics, which were again cleared for manufacture of tyres without payment of either excise duty or AED. Since rubberized tyre cord fabrics manufactured from processed tyre cord fabrics (i.e. dipped tyre cord fabrics) were not exempt under notification dated 2 June 1998, AED was leviable. This resulted in non-levy of duty of Rs.17.39 crore during the period 2 June 1998 to 31 March 2003 which was recoverable with penalty of equal amount under Rule 25 of Central Excise Rules, 2001 (erstwhile Rule 173Q of Central Excise Rules, 1944).

On this being pointed out (February 2005), the Ministry stated (December 2005) that rubberized tyre cord fabrics was classifiable under heading 59.06 as per Supreme Court decision in MRF case and hence it did not attract AED.

Reply of the Ministry is not tenable and is contradictory to it's own actions, as after considering Supreme Court decision in MRF case, the Commissioner Central Excise Indore in its order in original dated 4 March 2005 for assessee had decided classification of dipped rubberized fabrics under heading 59.02 due to non-predominance of rubber content in the product.

12.2.2 Bunkers, saw beams etc.

By notification dated 16 March 1995, capital goods manufactured in a factory and used within it are exempt from whole of duty of excise leviable thereon provided they conform to the definition of capital goods as specified in rule 57Q of Central Excise Rules, 1944/Rule

2(b) of Cenvat Credit Rules, 2001/2002. Tribunals while interpreting scope of the above exemption notification, in a number of cases held that benefit of exemption was not available to structural and other fabricated items of iron and steel if assessee failed to establish that such items manufactured in factory were used as components of capital goods specified in Rule 57Q of erstwhile Central Excise Rules, 1944 {2000 (121) ELT 114/ 2003 (160) ELT 440}.

M/s. Rashtriya Ispat Nigam Ltd. Visakhapatnam, in Visakhapatnam I commissionerate, engaged in manufacture of iron and steel products had several auxiliary shops within their factory which manufactured different structural items and other articles of iron and steel and claimed exemption during the years 1999-2000 to 2002-2003 on a variety of products like bunkers, saw beams, etc. on the ground that the said goods were being used internally as parts of capital goods. Scrutiny revealed that none of the items were identifiable as parts or components of any individual machines installed in their factory. They also did not fall under the description of capital goods or parts as provided under rule 57Q/rule 2(b) ibid. They were cleared for captive consumption and assessable to duty as iron and steel products falling under chapter 72 of Central Excise Tariff Act. Duty of Rs.1.18 crore was not levied on such goods manufactured and cleared from auxiliary shops during the period from July 1999 to June 2002. Duty was arrived at on the basis of cost of raw materials used in the said products.

On this being pointed out (September 2002), department issued (July 2004) SCN demanding duty of Rs.2.97 crore in respect of clearances during June 1999 to March 2000. The Ministry stated (November 2005) that the goods manufactured in auxiliary shops were internal parts of the machinery which in turn was used in manufacture of final products and hence eligible for credit. It also stated that the goods are eligible for exemption under notification dated 16 March 1995.

Contention of Ministry is not tenable as none of the goods manufactured by the assessee in its auxiliary shops were identifiable as parts or components of any individual machinery installed in the factory and hence they did not, prima facie, satisfy the definition of capital goods. Further the notification specifically mentions that goods manufactured for use within the factory should be capital goods as defined in rule 57Q/rule 2(b) ibid. In case of M/s. Nava Bharati Ferro Alloys Ltd. {2004 (174) ELT 375} CESTAT held that coal bunkers, chequered plates, hard plates etc. were not capital goods and that columns of heavy fabricated structures and bracing used as supporting columns were in the nature of construction material and therefore, were not to be regarded as capital goods under rule 57Q.

12.2.3 Parts of footwear

By notification dated 23 July 1996, goods produced and consumed within the factory of production in manufacture of footwear of retail sale price not exceeding Rs.125 are fully exempt from payment of duty. Notification dated 1 March 2002 fully exempts footwear of retail sale price not exceeding Rs.125 from payment of duty. This has been amended on 9 July 2004 to provide exemption to footwear of retail sale price not exceeding Rs.250. However, the other notification dated 23 July 1996 has been amended on 9 August 2004 to provide exemption to intermediate products (parts or components) consumed in manufacture of footwear of retail sale price not exceeding Rs.250. Thus captive consumption of intermediate products used in the manufacture of footwear of retail price exceeding Rs.125 but not exceeding Rs.250 were not covered under exemption till 8 August 2004.

M/s. Elastrex Polymers (P) Ltd., M/s. Bata India Ltd. and M/s. Condor Footwear (I) Ltd. in Bangalore II, Kolkata V and Surat I commissionerates, engaged in manufacture of footwear and parts thereof cleared some models of footwear of retail price exceeding Rs.125 but not exceeding Rs.250. Scrutiny revealed that the assessee captively consumed different intermediate products in manufacture of such footwear between 9 July 2004 and 8 August 2004. Neither did assessees pay any duty on such captive consumption nor did the department demand it. This resulted in non-levy of duty of Rs.29.27 lakh which was recoverable with interest of Rs.2.37 lakh.

On this being pointed out (December 2004), the Ministry admitted the objection and intimated (November and December 2005) issue of three SCNs for Rs.29.79 lakh.

12.3 Exemption availed without exemption notification

By three different notifications dated 1 March 2003, Government exempted 'five per cent ethanol blended petrol' (sub-heading 2710.19 consisting by volume 95 per cent MS and five per cent ethanol and conforming to Indian Standard Specification 2796) from levy of BED, SED, AED leviable under section 111 of Finance Act, 1998 and also SAED leviable under Finance Act 2002 subject to the condition that such ethanol blended petrol was manufactured out of MS and ethanol on which appropriate duties of excise had already been paid. These notifications were initially given validity upto 29 February 2004 which was further extended upto 30 June 2004 by subsequent notification dated 4 February 2004. No further extension was, however, granted beyond the said date. Through three other notifications issued on 4 August 2004, exemption from levy of all the above mentioned duties had once again been given subject to fulfilment of the same conditions stipulated in earlier notifications. These fresh notifications restoring the exemption took effect only from the date of issue, and hence ethanol blended petrol cleared during the intervening period from 1 July 2004 to 3 August 2004 attracted levy of the said duties.

Two bulk terminals of M/s. BPCL and M/s. IOCL in Hyderabad III and IV commissionerates, engaged in marketing of various petroleum product, undertook the process of blending ethanol with petrol in their warehousing stations and cleared the resultant product 'five per cent ethanol blended petrol' without payment of duties availing exemption under the aforementioned notifications. Availment of exemption on 2730 kilo litre of ethanol blended petrol cleared during the period from 1 July 2004 to 3 August 2004 was not correct and resulted in non-payment of excise duties aggregating to Rs.3.07 crore.

On this being pointed out (January/February 2005), the department stated (April 2005) that the issue was already under investigation by director general of central excise intelligence and issue of notification under section 11C of Central Excise Act, 1944 was under consideration.

The fact however, remained that neither SCN demanding duty nor notification under 11C waiving such duty had been issued (May 2005).

Reply of the Ministry had not been received (January 2006).

12.4 Incorrect availment of exemption on goods cleared

12.4.1 Cement

By notifications dated 1 March 2002 and 1 March 2003, manufacturers of cement were allowed to clear cement at concessional rate of duty viz. Rs.200 per tonne (in place of tariff rate Rs.350 per tonne) and Rs.250 per tonne (in place of Rs.400 per tonne) respectively upto maximum quantity of 99000 tonne in a financial year subject to conditions that (i) it was manufactured in factory with installed capacity not exceeding 900 tonne per day or 2,97,000 tonne per annum; and (ii) the total clearances of cement produced by the factory, in the financial year did not exceed 3,00,000 tonne.

M/s. DCM Shriram Consolidated Ltd., in Jaipur I commissionerate, produced 294317 tonne cement during 2002-03 and 295101 tonne in 2003-04. They cleared 1,98,000 tonne, during April 2002 to March 2004 at concessional rate of duty whereas installed capacity of the plant worked out to 327018 tonne per annum. Availment of exemption was incorrect and resulted in short payment of duty amounting to Rs.2.97 crore during the said period.

On this being pointed out (November 2003/March 2004), the Ministry stated (December 2005) that the assessee had fulfilled the conditions of the notification as the notification speaks about installed capacity of the klin and not about the capacity of cement plant.

Reply of the Ministry is not tenable as assessee had manufactured 1100 tonne of cement per day against declared capacity of 900 tonne per day during some of the days of the year indicating an increased production capacity. Reply of the Ministry that the said notification speaks about installed capacity of klin is also not tenable as it speaks about the installed capacity of the plant/factory as a whole and not only klin capacity as plant can not have two capacities. The assessee had, since, stopped availing exemption with effect from 24 May 2004.

12.4.2 Electronic relays

Notifications dated 4 January 1995 and 31 March 2003 specify that goods cleared to an electronic hardware technology park (EHTP) unit in connection with manufacture or development of electronic hardware or software for export would be exempt from the whole of duty of excise including additional duty of excise leviable under the Additional Duty of Excise (Goods of Special Importance) Act, 1957 subject to conditions stipulated in the notifications. Conditions, inter alia, included that (i) manufacturer of the said goods follow the procedure contained in rule 156A and rule 156B of Central Excise Rules, 1944/rule 11 and 20 of Central Excise Rules 2002, (ii) user industry follow the procedure contained in chapter X of Central Excise Rules 1944/Central Excise (Removal of Goods at Concessional Rate of Duty for manufacture of Excisable Goods) Rules, 2001. Notifications stipulated issuance of certificate in form CT 3 in place of usual CT 2 certificate by central excise officer in charge of the user industry.

M/s. American Power Conversion (India) Ltd., EHTP unit based at Bangalore obtained permission to remove 9,78,000 electronic relays and parts thereof from OEN India Ltd. in Cochin commissionerate vide two CT 3 certificates without payment of duty in terms of the notifications mentioned above. However, OEN India Ltd. cleared excess quantity of 14,76,745 relays valued at Rs.5.05 crore without production of valid CT 3 certificates. Such clearance without payment of duty of Rs.80.83 lakh in the absence of a valid CT3 certificate was not in order.

On this being pointed out (July 2003), the Ministry admitted the objection (September 2005).

12.4.3 Sewing thread

Under note 3 to section XI of schedule to Central Excise Tariff Act, 1985, 'sewing thread' means multiple (folded) or cabled yarn (a) put up on supports (e.g reels and tubes etc.) of a weight (including supports) not exceeding 1000 gram, (b) dressed for use as sewing thread; and (c) with a final 'z' twist.

In terms of notification dated 7 May 1997 and 2 June 1998, sewing thread was chargeable to concessional rate of duty at 15 per cent ad valorem.

M/s. Pasupati Weaving & Spinning Mills Ltd., in Chandigarh commissionerate, engaged in manufacture of sewing thread of polyester (heading 55.08) besides clearing it on reels, also cleared thread in hanks form each weighing 250 gram by paying duty at concessional rate of 15 per cent ad valorem. The good cleared in hanks form, and not on supports, was thus thread/yarn and could not be termed as 'sewing thread'. As such concessional rate of duty was not admissible. This resulted in short levy of duty of Rs.52.56 lakh during the period from May 1997 to March 1999.

On this being pointed out (March 1999 and March 2000), the Ministry admitted the objection in principle (August 2005).

12.4.4 Writing or printing paper

Sub-heading note 1 to sub-heading 4802.10 of chapter 48 of first schedule to Central Excise Tariff Act, 1985, prescribes nil rate of duty only to "writing or printing papers" when supplied directly from the factory of its manufacture against a purchase order (a) placed upon the manufacturer by a State text book publication corporation or Board, or in case of State which do not have such corporation or Board, by an officer not below the rank of deputy secretary in the State, and (b) in which the said Corporation or Board or the said officer of the State Government declares that the said paper shall be used for the printing of educational text books.

M/s. Hindustan Paper Corporation Ltd., in Shillong commissionerate, cleared 1002.07 tonne printing paper valuing Rs.2.53 crore during 23 May 2004 to 30 June 2004. Goods were cleared at nil rate of duty. Clearance was made on the basis of an order placed by the State project director, Sarva Shiksha Abhiyan Authority (SSAA), Punjab according to which supply and billing of paper was to be made to M/s. Capital Business System of Delhi and end use certificate was to be issued by that unit. Clearance of goods at nil rate of duty was not correct as SSAA was not specified in tariff note ibid and benefit was passed on to party other than government agency. This resulted in non-levy of duty of Rs.40.45 lakh.

On this being pointed out (August 2004), the Ministry admitted the objection (November 2005) and reported issue of SCN.

12.5 Incorrect grant of exemption of NCCD on goods captively consumed

Section 136 of Finance Act, 2001 as amended by Finance Act, 2003, imposed NCCD at the rate of one per cent ad valorem on dumper chassis fitted with engines (sub-heading 8706.49) for motor vehicles of sub-heading 8704.30 (dumpers) with effect from 1 March 2003. Notification dated 16 March 1995, as amended exempts duty of excise leviable under Central

Excise Tariff Act, 1985 for goods captively consumed within the factory. Levy of NCCD is not exempt under this notification.

M/s. Tatra Udyog Ltd. Hosur and M/s.Caterpillar (I) Ltd. Tiruvallur in Chennai II and III commissionerates, manufactured dumper chassis falling under sub-heading 8706.49 and captively used them in manufacture of dumpers (sub-heading 8704.30) without payment of NCCD, availing exemption under notification dated 16 March 1995. Availment of exemption of NCCD of Rs.1.39 crore for the period from March 2003 to August 2004 was incorrect.

On this being pointed out (between April 2003 and October 2004), the Ministry accepted (December 2005) the objection in case of M/s. Tatra Udyog Ltd. and issued SCN for Rs.16.10 lakh. In case of M/s. Caterpillar (I) Ltd., it stated that no chassis with engines emerged independently as dumper was manufactured in the assembly line in a continuous process. The assessee manufactured only two chassis on specific request of customer which cannot be taken as criteria for holding that chassis arose in the course of manufacture.

Reply of the Ministry is not tenable as department in its letter dated 14 July 2003 has intimated that the manufacturing process involved, manufacture of chassis, mounting/fabrication of engines, hydraulic system, fabrication of drivers cab, fitting of tyres etc. upto the manufacture of dumpers. Clearance of two chassis alone outside the factory does not disprove the manufacture and captive consumption of chassis within the factory.

12.6 Exemption meant for small scale industries availed of by large scale manufacturers

Notifications dated 1 March 2000/2001/2002, interalia, stipulated that manufacturers whose aggregate value of clearances for home consumption in the preceding financial year did not exceed Rs.3 crore were eligible for concessional rate of duty/full exemption from duty. Value of clearances relating to (i) branded goods manufactured and cleared on behalf of another person on payment of normal rate of duty, (ii) excisable goods which were either exempt or chargeable to nil rate of duty and (iii) excisable goods exported to countries except Nepal and Bhutan, were to be excluded for reckoning the eligibility limit of Rs.3 crore.

Union Budget 2003-04, had recognized that while small scale exemption scheme aimed at providing a distinctive advantage to labour – intensive units, there was possibility of misuse of this facility in certain sectors. Consequently the eligibility limit of Rs.3 crore under general small scale industries scheme was rationalised and the clause relating to exclusion of exempted goods for purpose of computation of total clearances was deleted. Value of clearances pertaining to exempted goods or goods cleared with nil rate of duty was therefore includible for purpose of determining eligibility criterion of Rs.3 crore with effect from 1 April 2003. However, the relevant clauses which provided for exclusion of clearances pertaining to branded and export goods were not deleted and consequently value of those clearances continued to be excluded for purpose of reckoning the eligibility limit of Rs.3 crore even after 1 April 2003.

In case of M/s. Food Specialities Ltd. vs. Government of India, Supreme Court had ruled that where goods are produced with customer's brand name under his quality control, it does not mean that the customer is the manufacturer {1985 (22) ELT 324}. Despite judicial pronouncement providing enough justification and ground for inclusion of value of clearance pertaining to branded goods under the over all ceiling of Rs.3 crore, Government has not so far made suitable amendment in SSI notifications.

Seven assessees in Jalandhar, Ludhiana and Panchkula commissionerates, availed benefits of notification ibid and cleared goods during preceding financial years of value between Rs.3.5 crore and Rs.9.7 crore. The continued retention of exclusion clause relating to branded and export goods thus enabled these large manufacturers to derive benefit of duty exemption which amounted to Rs.62.89 lakh during the years 2003-04 and 2004-05.

On this being pointed out (January 2005), the Ministry stated (November 2005) that the exclusion of export and branded goods from the purview of aggregate clearances of Rs.3 crore was a deliberate policy decision of the government.

The fact remains that this ran contrary to the declared intentions of the Government through budget, which enabled large scale manufacturers to derive such benefit of duty concession.

12.7 Other cases

In 16 other cases of exemptions, the Ministry/department had accepted objections involving duty of Rs.1.98 crore and reported recovery of Rs.0.91 crore in three cases till January 2006.

CHAPTER XIII : CLASSIFICATION OF EXCISABLE GOODS

The rates of duty leviable on excisable goods are prescribed under various headings in Central Excise Tariff. Some illustrative cases of incorrect classification of goods resulting in non/short levy of duty are given in the following paragraphs:

13.1 Sulphur

Heading 28.02 of first schedule to Central Excise Tariff covers sulphur, sulphur sublimed or precipitated and colloidal sulphur. Note 2 to chapter 25 ibid specifies that heading 25.05 covers products which have been washed of impurities without changing structure, ground, powdered etc., by flotation or magnetic separation (except crystallisation) but not those that had been roasted, calcined or subject to process beyond those mentioned in the headings. Further, as per note 1 to chapter 25, sublimed sulphur was not covered by that chapter.

M/s. Chennai Petroleum Corporation Ltd. (CPCL), in Manali I commissionerate, engaged in manufacture of various petroleum products (chapter 27), initially removed hydrogen sulphide in the de-sulphurisation plant. It was then burnt with oxygen in its sulphur recovery unit and sulphur was liberated in vapour form which was condensed and drained into a pit to obtain solid granules of high purity called 'sublimed sulphur'. The sulphur so manufactured by assessee merited classification under heading 28.02 attracting duty at 16 per cent ad valorem. Instead it was classified under heading 25.05 and cleared at nil rate of duty. Non-levy of duty due to misclassification worked out to Rs.52.28 lakh from April 1996 to February 2001.

On this being pointed out (March and May 2001), the department issued SCN (April 2001) for Rs.22.83 lakh from March 2000 to February 2001 but adjudicating authority decided the case in favour of assessee (December 2001). Commissioner of central excise, Chennai I on review of the order-in-original observed that 'sulphur' produced by assessee was classifiable under heading 28.02 and directed (October 2002) the department to file an appeal. As of January 2005, the case was pending in CESTAT. The department had also issued four more SCNs (August 2002, January and November 2003 and September 2004) for duty aggregating Rs.68.64 lakh for the period from July 2001 to July 2004 which was pending adjudication (December 2004). Total non-levy of duty on sulphur for the period from April 1996 to July 2004 amounted to Rs.2.32 crore. Ministry stated (October 2005) that the excise tariff had been amended so as to classify sulphur recovered as by-product in refining crude oil under heading 250300.10 w.e.f 28 February 2005.

Ministry's reply is silent on recovery of duty for the period prior to 28 February 2005.

13.2 Pre fabricated structural insulated panel

Note 11(b) of chapter 39 of Central Excise Tariff, states that heading 39.25 inter alia covers structural elements used in floors, partitions, ceilings or roofs. Further as per note 4 of chapter 94 "pre-fabricated buildings" as expressed under heading 94.06 means buildings which are finished in the factory or put up as elements, cleared together, to be assembled on site, such as housing or work site accommodation, offices, schools, shops, sheds, garages or similar buildings.

M/s. Beardsell Ltd. in Belapur commissionerate, manufactured 'iso wall pre-fabricated structural insulated panels' and classified them under heading 94.06 as pre-fabricated

buildings. The panels so manufactured consisted of thermal insulation made of 'expanded polystyrene' (commonly known as thermacole) bonded between two metal sheets. Since expanded polystyrene gave essential character to the structural insulated panel, the goods were aptly classifiable under heading 39.25. Incorrect classification resulted in short levy of duty of Rs.15.34 lakh in 1997-98.

On this being pointed out (February 1999), the Ministry admitted the objection (August 2005) and intimated confirmation of demand of duty for Rs.2.92 crore for the period from November 1996 to October 2003. Demand of Rs.31.56 lakh for December 2003 to July 2004 was reportedly pending adjudication.

13.3 Other cases

In four other cases of incorrect classification, the Ministry/department had accepted objections involving duty of Rs.0.20 crore and reported recovery of Rs.0.10crore in 4 cases till January 2006.

CHAPTER XIV : NON-LEVY OF DUTY

Rules 9 and 49 read with rule 173G of Central Excise Rules, 1944, prescribe that excisable goods shall not be removed from the place of manufacture or storage unless excise duty leviable thereon has been paid. If a manufacturer, producer or licencee of a warehouse, violates these rules or does not account for the goods then besides such goods becoming liable for confiscation, penalty not exceeding duty on such excisable goods or ten thousand rupees, whichever is greater, is also leviable under rule 173Q. Similar provisions exist in rules 4 and 25 of Central Excise Rules, 2002 which came into force from 1 March 2002. Some illustrative cases of non-levy of duty noticed in test check are given in the following paragraphs :

14.1 Duty not paid by due dates

14.1.1 Sub-rule (1) of rule 8 of Central Excise Rules, 2002, stipulates that duty on goods removed from the factory or warehouse during a month shall be paid on fifth of the following month. Further sub-rule (3) envisages that if the assessee fails to do so, he shall be liable to pay the outstanding amount along with interest at the rate of two per cent per month or rupees one thousand per day whichever is higher for the period starting with first day after due date till the date of actual payment of outstanding amount.

M/s. Shree Synthetics Ltd., Ujjain, in Indore commissionerate, manufactured nylon/polyester filament yarn falling under heading 54.02 and removed finished goods from the factory between July 2003 and November 2003, without payment of duty amounting to Rs.3.47 crore by due dates. Duty was recoverable on which interest at the rate of two per cent per month was also leviable. On this being pointed out (July 2004 and February 2005), the Ministry admitted the objection and reported recovery (September 2005) of Rs.65.13 lakh. Report on recovery of remaining amount was awaited.

M/s. Indo Ashahi Glass, Ramgarh, in Ranchi commissionerate, cleared products of glass involving central excise duty of Rs.1.50 crore during the months of September 2003, October 2003 and November 2003 without payment of duty by due dates. This resulted in non-levy of duty of Rs.1.50 crore besides interest of Rs.2.59 lakh leviable under rule 8(3) ibid. On this being pointed out (December 2003); the Ministry admitted the objection and intimated (September 2005) that Rs.1.50 crore besides interest of Rs.9.50 lakh had since been paid by assessee.

M/s. Hotline CPT Ltd., in Indore commissionerate, a manufacturer of cathode ray television colour picture tube (sub-heading 8540.11) did not pay duty of Rs.90.91 lakh for the month of November 2004 by due date and was liable to pay outstanding amount alongwith interest of Rs.1.35 lakh (upto 28 December 2004). On this being pointed out (December 2004), the Ministry admitted the objection and intimated (December 2005) recovery of duty of Rs.90.91 lakh and interest of Rs.2.35 lakh in January 2005.

14.1.2 Rule 173G of Central Excise Rules, 1944, prescribes that duty on goods removed from a factory or warehouse during the first fortnight of the month shall be paid by the 20th of that month and that on goods removed during the second fortnight be paid by the fifth of the following month. If assessee fails to pay any one instalment beyond period of 30 days from

due date or the due date on which full payment of instalments are to be made is violated for the third time in the financial year, whether in succession or otherwise, then manufacturer shall forfeit facility to pay dues in intalments for a period of two months, starting from the date of communication of an order passed by the proper officer in this regard or till such date on which all dues are paid which ever is later and during this period, the manufacturer shall be required to pay excise duty for each consignment by debit account current. Any failure would deem goods to have been cleared without payment of duty and consequences and penalties as provided in central excise rules shall follow.

M/s. Betul Tyre and Tubes Industries Ltd. and M/s. Wear Well Tyre and Tube Industries Pvt. Ltd., Betul, in Bhopal commissionerate, engaged in manufacture of tyre and tubes had not paid full duty on due dates. M/s. Betul Tyre and Tubes Industries Ltd. defaulted in full payment of instalments of duty six times in financial year 2000-01 and eight times in financial year 2001-02. Similarly M/s. Wear Well Tyre and Tube Industries Pvt. Ltd. defaulted five times in financial year 2001-02. The proper officer had not initiated any action to forfeit the facility to pay dues in instalments.

On this being pointed out (August 2001), the department admitted the objection and intimated (February 2004) that facility to pay duty on fortnightly basis had since been withdrawn. Besides, an amount of Rs.87.94 lakh had been recovered from PLA during the months of September 2001 to November 2001.

The Ministry admitted the objection (November 2005).

14.2 Duty not levied on goods lost in transit

The Board in circular dated 23 September 2002 prescribed procedure of accountal of petroleum products movement through pipeline without payment of duty. Accordingly, assessees are required to submit quarterly statements of loss/gain for bonded movement of petroleum products and also, annual statements duly certified by chartered accountant within 60 days from the end of financial year. The department would assess such clearances, product-wise and destination-wise, after condoning prescribed limit of 0.25 per cent of such loss. On shortages in excess of 0.25 per cent, assessment may ordinarily be carried out on highest value and highest rate of duty applicable for the particular product during the period.

M/s. IOCL Haldia, in Haldia commissionerate, transferred petroleum products (chapter 27) under bond without payment of duty through pipeline and prepared periodical reconciliation statements of loss/gain. Scrutiny of such statements with reference to the products despatched through pipelines revealed loss in excess of 0.25 per cent in the case of aviation turbine fuel (ATF) and motor turpentine oil (MTO) during the year 2002-03. Duty was required to be demanded on the quantity lost beyond the condonable limit. But neither did the assessee pay such duty nor did the department demand it. This resulted in non-levy of duty of Rs.1.46 crore during the period April 2002 to March 2003.

On this being pointed out (June 2004), the Ministry stated (December 2005) that transit loss had not been exceeded for all products taken together.

Reply of the Ministry is not tenable since this was in violation of Board's circular dated 23 September 2002. As a result loss of one product was set off against another product which was not in order.

14.3 Duty not levied on excisable goods found short

Rule 10 of Central Excise Rules, 2002, provides that every assessee shall maintain proper records on daily basis, of goods produced or manufactured, quantity removed, assessable value and the amount of duty actually paid. In terms of rule 4, no excisable goods on which duty is payable shall be removed from a factory or warehouse without payment of requisite duties. However, rule 21 ibid provides for remission of duty in cases where it is shown to the satisfaction of commissioner that goods have been lost or destroyed by natural causes or by unavoidable accident or become unfit for consumption/marketing before their removal.

14.3.1 M/s. Alloy Steel Plants, Durgapur, in Bolpur commissionerate, manufacturing iron and steel products maintained their production records on estimated basis and at the end of year carried out physical verification. Scrutiny of annual stock verification report vis-à-vis annual account for the year 2001-02 disclosed that shortages in quantity of different products, viz., ingot, slab, bloom, round, bar, channel, forging and plates located during physical verification had been recorded but the assessee adjusted such shortages in the books of account by reducing closing balances of products without assigning any reason. The assessee did not pay any duty on shortages. Such type of adjustment was not permissible under the rules. The department also did not demand any duty. Failure to do so thus resulted in non-levy of duty of Rs.78.48 lakh during the period from April 2000 to March 2002.

On this being pointed out (March 2003), the department admitted the objection and stated (March 2005) that SCN was under issue.

The Ministry stated (September 2005) that shortages were to be dealt with in accordance with Board's instructions of 26 October 1979.

Further development in the case had not been received (January 2006).

14.3.2 Scrutiny of internal physical stock verification reports of M/s. Rashtriya Ispat Nigam Ltd., in Visakhapatnam I commissionerate, revealed (September 2004) that there was shortage of stock of pig iron to the extent of 2669 tonne at the end of March 2004. There was no evidence on record to show that goods were lost or destroyed by natural causes, etc. or became unfit for consumption/marketing warranting remission of duty under rule 21 of Central Excise Rules, 2002. Neither had the assessee paid nor had department demanded duty of Rs.30.60 lakh payable on the said goods. Shortages to this extent were to be regarded as clearances without payment of duty.

On this being pointed out (February 2005), the Ministry admitted the objection and intimated (November 2005) issue of show cause notice for Rs.76.22 lakh in October 2005.

14.4 Non-levy of additional duty

Section 3 of Additional Duties of Excise (Textiles and Textiles Articles) Act, 1978 (AED Act, 1978), levies additional excise duty at the rate of 15 per cent of BED chargeable which is to be calculated after excluding any exemption for giving credit or for reduction of duty already paid on raw material used in the production or manufacture of such goods.

14.4.1 M/s. Suryalaxmi Cotton Mills Ltd., Nagardhan, in Nagpur commissionerate, manufactured cotton yarn and used it captively in manufacture of denim fabrics falling under sub-heading 5207.10 without payment of BED and also without levy of AED under Additional Duties of Excise (Goods of Special Importance) Act, 1957 availing exemption

under notification dated 16 March 1995. The assessee did not pay AED leviable under Additional Duties of Excise (Textile and Textile Articles) Act, 1978 on 7490616.16 kilogram of cotton yarn valuing Rs.52.43 crore captively consumed in manufacture of cotton fabric. This resulted in non-levy of AED amounting to Rs.62.92 lakh at the rate of 15 per cent of notional BED of Rs.4.19 crore during April 2003 and March 2004.

14.4.2 M/s. Sanghi Polyesters Ltd. and M/s. Reliance Industries Ltd., in Hyderabad III and Raigad commissionerates, manufactured partially oriented yarn (POY sub-heading 5402.42) and polyester tow and utilized it captively in manufacture of polyester textured yarn (sub-heading 5402.32) and goods falling under chapter 54 or 55 (respectively) without payment of BED by availing exemption under notification dated 16 March 1995, as amended. Assessees did not pay AED which was leviable by working out quantum of BED on POY and polyester tow chargeable but for exemption benefit availed through the above notification. This resulted in non-levy of AED of Rs.32.05 lakh for the period October 1996 to July 2004.

On above cases being pointed (between June 2000 and May 2005), the Ministry stated (November 2005) that notifications dated 16 March 2005 and 23 July 1996 exempted excise duty which were equally applicable on additional duty by virtue of section 3(3) of AED Act, 1978 and tribunal's decision in case of M/s. Nahar Spinning Mills Ltd. {91 – ELT 103}.

Reply of the Ministry is not tenable since these notifications were not relevant for determining additional duty in terms of section 3 of the Act 1978 ibid. Tribunals decision too did not relate to exclusion clause of section 3 of AED Act, 1978, which specifically excludes exemption of central excise while working out AED.

14.5 Non-levy of duty on treated water cleared under brand name

Note 2 to chapter 22, stipulates that in relation to waters including natural and artificial mineral waters of chapter heading 22.01 of Central Excise Tariff Act, 1985, processes such as filtration, purification or any other process or any one or more of these processes to render the product marketable, shall amount to manufacture. Waters, including natural or artificial mineral waters bearing brand name are classifiable under sub-heading 2201.19 and attracted levy of duty at 18 per cent ad valorem upto 28 February 1999 and 16 per cent thereafter. Under chapter note 3 ibid, 'brand name' means a name or mark such as symbol, monogram, signature or invented words or any writing which is a word in relation to product for the purpose of indicating connection in the course of trade between the product and some person using such name or mark with or without any indication of the identity of that person.

M/s. Hindustan Coca Cola Beverages Ltd., in Hyderabad III commissionerate, engaged in manufacture of aerated waters, produced treated water by subjecting ordinary water to various processes such as bleaching, filtration and treatment with activated carbon in order to remove impurities and micro organisms and to make it fit for use as an input in aerated waters. While bulk of the purified water so produced was consumed within the factory, some was cleared to vending machine outlets in canisters embossed with the brand name 'Coca cola' alongwith beverage base for manufacture of soft drinks at vending machine outlets. No duty was paid on branded goods under sub-heading 2201.19 from December 1997 onwards. Department also did not demand duty.

On this being pointed out (November 1998), the Ministry admitted the objection and intimated (December 2005) issue of SCN for Rs.40.64 lakh.

14.6 Other cases

In 168 other cases of non-levy of duty, the Ministry/department had accepted objections involving duty of Rs.2.95 crore and reported recovery of Rs.2.15 crore in 164 cases till January 2006.

CHAPTER XV: NON-LEVY OF INTEREST AND PENALTY

Where any duty of excise has not been levied or paid or has been short levied or short paid or erroneously refunded, the person liable to pay duty as determined under section 11A, shall, in addition to the duty, be liable to pay interest at the rate of 20 per cent per annum till 11 May 2000, 24 per cent with effect from 12 May 2000, 15 per cent with effect from 13 May 2002 and 13 per cent from 12 September 2003 under relevant sections of Central Excise Act, 1944. Some illustrative cases of interest and penalty not levied or realised are mentioned below:

15.1 Absence of provision for timely recovery of interest on delayed payment

Sections 11AA and 11AB of Central Excise Act, 1944, prescribe payment of interest on delayed payment of duty at the specified rate. Time limit within which the assessee is required to pay interest due, has however not been prescribed.

Commissioner of central excise, Mumbai II in case of M/s. IOCL Trombay installation, had confirmed demand of Rs.24.91 crore vide order in original dated 3 August 1995. Assessee paid the demand in two instalments of Rs.14.94 crore in September 1996 and balance Rs.9.95 crore in October 1996 with Rs.2 lakh being adjusted against refund. Interest leviable on delayed payment of duty worked out to Rs.4.39 crore. Ministry reported (March 2005) that interest of Rs.2.81 crore was recovered in November 1997 and Rs.1.58 crore in March 2001. Thus, recovery of entire interest took more than five years from the date of passing of the order in original.

Demands raised for payment of interest under section 234A, 234B, 234C or any other levy of penalty or fine or any other sum payable under provisions of Income Tax Act, 1961 fall within the ambit of notice of demand under section 156 and non payment or delay or default in payment thereof calls for levy of interest under section 220(2) of the Act ibid. This provision takes care of levy of interest on delayed payment of interest or penalty etc. recoverable from the assessee. There is no such provision in Central Excise Act/Rules.

Absence of provisions thereunder or non provision of mandatory penalty for delayed payment of interest leads to unintended financial accommodation to the assessee which in the instant case was to the extent of Rs.3.80 crore.

The Ministry stated (December 2005) that there is no provision to collect interest on delayed payment of interest and audit's observations have been taken note of.

15.2 Non-levy of interest

15.2.1 As per sub-rule 3 of rule 8 of Central Excise Rules, 2002, effective from 1 April 2003, if any assessee failed to pay amount of duty by due date, he would be liable to pay the outstanding amount along with interest at the rate of two per cent per month or rupees one thousand per day, whichever was higher, for the period starting with the first day after the due date till the date of actual payment of the outstanding amount. However, such interest payable would not exceed the amount of duty that had not been paid within the due date.

M/s. Alloy Steel Plant, Durgapur, in Bolpur commissionerate, manufacturing iron and steel products removed different excisable goods between July 2000 and October 2003 to their sister unit on payment of duty on value worked out at 100 per cent of cost of production whereas such value ought to have been arrived at on 115 per cent upto 4 August 2003 and

110 per cent thereafter under rule 8 of Valuation Rules, 2000. Though assessee paid differential duty payable on such account between 5 November 2003 and 31 March 2004, interest for such delayed payment to the tune of Rs.1.73 crore as per rule ibid was not paid.

On this being pointed out (March 2004), the Ministry admitted the objection in principle (September 2005).

15.2.2 Notification dated 26 June 2001 as amended issued under rule 19 of Central Excise Rules, 2001, stipulates that if excisable goods cleared for export from the factory of production or warehouse under bond without payment of duty are not exported, the exporter shall pay the duty along with interest from the date of removal for export from factory or warehouse till the payment of duty.

M/s. Birla Tyres, Balasore, manufacturer of tyre, tube and flaps in Bhubaneswar I commissionerate, diverted goods meant for export to home consumption during November 1998 to July 1999. The assessee paid duty only after confirmation of demand by adjudicating authority, but interest of Rs.44.44 lakh for the period from 24 December 1998 to 31 December 2003 accrued due to belated payment of duty was neither demanded by the department nor paid by assessee.

On this being pointed out (April 2004), the Ministry admitted the objection (December 2005).

15.3 Non-recovery of interest

15.3.1 Section 112 of Finance Act, 2000 which received assent of President of India on 12 May 2000 stipulates that no credit of duty on HSD shall be deemed to be admissible at any time during the period commencing on and from 16 March 1995 to 12 May 2000 notwithstanding any thing contained in any rule under Central Excise Rules, 1944. It further provides that (i) no suit or other proceedings shall be maintained or continued in any court, tribunal or other authority for allowing such credit of duty and (ii) no enforcement shall be made by any court, tribunal or other authority of any decree or order allowing such credit. It also provides that recovery shall be made of all the credit of duty availed or utilised within a period of thirty days from 12 May 2000 failing which, in addition to the amount of credit recoverable, interest at the rate of 24 per cent per annum shall be payable till the date of payment.

M/s. India Cement Ltd. and M/s. Suvarna Cements Ltd., in Tirupathi and Hyderabad III commissionerates, availed Modvat credit of Rs.1.90 crore on HSD oil between March 1997 and April 1999 and utilised the amount towards payment of duty on their final product. With passing of retrospective amendment Act validating denial of Modvat credit on HSD oil, the assessees were required to reverse or pay the entire credit by 10 June 2000. It was, however, noticed (November 2000/Janauary 2001) that the assessees did not do so and therefore became liable to pay interest of Rs.35.75 lakh to the end of March 2001 on the credits not so reversed or paid. On further reference (May 2001), the department in the case of first assessee stated (July 2002/April 2004) that though the assessee reversed credit of Rs.1.49 crore in December 2001, interest of Rs.55.79 lakh payable thereon could not be recovered on the interim orders of High Court, Chennai on writ petition filed by assessee. Department reported (December 2004/January 2005) that credit of Rs.40.60 lakh was remitted by second assessee by December 2001 in six instalments and the assessee had so far paid (November/December 2004) an amount of Rs.4 lakh out of Rs.13.12 lakh payable as interest upto end December 2001.

Hence, ineffective action on the part of department in getting the interim Court directions vacated or getting interest amount deposited even after five years led to non-realisation of Rs.55.79 lakh interest in the first case, Rs.9.12 lakh in the second. This also resulted in financial accommodation/blockage of revenue to that extent.

The Ministry stated (December 2005) that in the first case the recovery could not be effected as the matter was pending in the Court. In the second case, the Ministry intimated recovery of interest of Rs.13.12 lakh between January and December 2005.

15.3.2 M/s. Kwality Ice Cream, in Delhi I commissionerate, engaged in manufacture of ice cream/kulfi etc., was issued nine SCNs between August 1995 and December 1998 demanding duty on wholesale prices charged by M/s. Brook Bond Lipton (India) Ltd. for the period from January 1995 to November 1998. Seven SCNs issued upto December 1997 were adjudicated in December 1998 but two for the period December 1997 to November 1998 involving duty of Rs.113.70 lakh were not adjudicated till February 2000. Audit pointed out (March 2000) delay in adjudication of demand and resultant financial accomodation to the assessee.

Department stated (September 2004) that the demand was confirmed in April 2000 for Rs.123 lakh (including Rs.9.30 lakh demanded through SCN issued in April 1999). This was reduced to Rs.75.17 lakh by appellate authority in September 2001 and reduced duty was paid by assessee in October 2001. However, interest of Rs.24.05 lakh payable on account of delay in payment of duty during the period from July 2000 to October 2001 still remained unrealised.

The Ministry admitted the objection (July 2005).

15.3.3 During test check of records of M/s. Siddhartha Tubes Ltd., in Indore commissionerate, it was noticed that two demands for Rs.17.54 lakh on account of disallowing of Modvat credit were confirmed alongwith penalty of Rs.1.75 lakh vide order in original dated 30 July 1998. In compliance thereof, assessee paid the entire amount in June/May 2002. Interest amounting to Rs.19.63 lakh due on belated payment beyond three months was, however, not paid.

On this being pointed out (March 2003 and November 2004), the Ministry while admitting objection stated (August 2005) that Rs.10.20 lakh had been recovered and recovery proceedings for remaining amount were in progress.

15.4 Short payment of interest

M/s. Kothari Products Ltd. in Dibrugarh commissionerate, manufacturing 'pan masala' and 'gutka' paid Rs.94.22 lakh between December 2002 and April 2003 being differential duty from March 2001 to June 2001 arising out of disputed assessable value as confirmed by the tribunal on 12 March 2003. On an appeal preferred by the department, tribunal decided (11 November 2003) that assessee was liable to pay interest from 11 May 2001 on short paid duty at that time till full duty payment was made. Audit scrutiny revealed that assessee paid interest of Rs.9.79 lakh on 16 January 2004 on amount of duty which was short paid after 11 May 2001 but not on the amount which was short paid prior to 11 May 2001. This resulted in short payment of interest of Rs.25.36 lakh for the period from 11 May 2001 to 17 April 2003.

On this being pointed out (December 2004), the Ministry admitted the objection and intimated (November 2005) recovery of Rs.25.36 lakh.

15.5 Non-levy of penalty

Rule 8 of Central Excise/Rules, 2002, prescribes that duty on goods removed from a factory or a warehouse during the first fortnight of the month shall be paid by 20th of that month and that on goods removed from factory or warehouse during the second fortnight of the month be paid by the fifth of the following month. If assessee fails to pay any one instalment within 30 days from due date or instalment by due dates for the third time in a financial year, he shall forfeit facility for a period of two months from the date of communication of orders or till such date on which all dues are paid, whichever is later. During this period assessee is required to pay duty for each clearance through PLA. Failure to do so would attract liability to penalty not exceeding amount of duty leviable or ten thousand rupees, whichever was greater.

M/s. Kailash Auto Builders Ltd., in Bhopal commissionerate, engaged in manufacture of motor vehicle and parts, defaulted in payment of duty on due dates, on twelve occasions in succession between April 2002 and January 2003, delay ranging from three to 111 days. Therefore, facility of fortnightly payment ought to have been forfeited and assessee should have paid duty in cash on consignment basis. Department did not initiate action. Assessee continued to pay duty from Cenvat account and utilised Cenvat credit of Rs.13.60 lakh between June 2002 and January 2003 in contravention of rules. This tantamounted to clearance of goods without payment of duty. Therefore penalty of Rs.13.60 lakh was also leviable.

On this being pointed out (February 2003), the Ministry stated (November 2005) that the adjudicating authority had imposed a penalty of Rs.13.82 lakh but the Appellate Commissioner had set aside the orders in July 2004 as the failure of appellant was found unintentional and committed for the first time.

15.6 Other cases

In 65 other cases of non-levy of interest and penalty, the Ministry/the department had accepted objections involving duty of Rs.1.07 crore and reported recovery of Rs.0.70 crore in 64 cases till January 2006.

CHAPTER XVI: DEMANDS NOT RAISED OR REALISED

Short payment or non-payment of duty on excisable goods is to be recovered by issuing SCN under section 11A to be followed up with its adjudication and recovery proceedings. Period of limitation for issue of SCN is one year (six months upto 11 May 2000) in normal cases of non-levy/short levy of duty. In case of short levy/non-levy due to fraud, collusion etc., limitation period stands extended to five years. Some illustrative cases of demands not raised or realised are given in the following paragraphs: -

16.1 Demands not raised

Section 11A(1) of Central Excise Act, 1944, provides that where any duty of excise has not been levied or paid or has been short levied or short paid or erroneously refunded by reasons of fraud, collusion or any wilful mis-statement or suppression of facts, or in contravention of provisions of Central Excise Act or Central Excise Rules with intent to evade payment of duty, by such person or agent, demand can be raised within five years.

16.1.1 M/s. Maratha Cement Works, in Nagpur commissionerate, engaged in manufacture of cement availed irregular Cenvat credit of Rs.8.22 crore on capital goods utilised for construction, erection and commissioning of captive thermal power plant during October 2000 and January 2003. Since the power plant was used exclusively in generation of non excisable goods i.e. electricity, Cenvat credit was not admissible. Department issued four SCNs amounting to Rs.2.86 crore between September 2002 and February 2003 covering the period August 2001 to January 2003 for recovery of irregular availment of credit. No action to recover credit of Rs.5.36 crore availed during the period October 2000 to July 2001 was, however, taken by it.

On this being pointed out (November 2003), the Ministry admitted the objection in principle (September 2005).

16.1.2 Section 11D of Central Excise Act, 1944 stipulates that every person liable to pay duty under this Act and who had collected any amount on excisable goods from buyer of the goods representing duty of excise, shall forthwith pay the amount so collected to credit of Central government.

M/s. IOCL Hisar, in Rohtak commissionerate, received furnace oil and light diesel oil on payment of duty at appropriate rate prevalent at the relevant point of time. Material was stored in separate duty paid tanks from where the same was sold and central excise duty collected at higher rate applicable at the time of sale. Extra duty of Rs.18.33 lakh so collected between April 2002 and October 2002 was not remitted to government. Department did not take any action to realise the amount due. On this being pointed out (September 2003), the Ministry admitted the objection and intimated (November 2005) that assessee had deposited the amount.

16.2 Non-realisation of confirmed demand

Section 11 of the Central Excise Act stipulates that the officer empowered by the Board may recover duty and any other sums of any kind payable to the central government under Central Excise Act or Rules by deducting the amount payable to assessee by government or by attachment and sale of excisable goods belonging to person from whom sums are

recoverable. In case amount payable is not so recovered, certificate action may be taken through collector of the district for recovery as arrears of land revenue.

Scrutiny of records of Coochbihar division and Birpara range revealed that demands involving revenue of Rs.36.20 lakh in respect of nine tea estates (three in Coochbihar and six in Birpara) had been confirmed between August 2003 and March 2004 with penalty of Rs.2.84 lakh on non payment of duty on 'tea' packed in container exceeding 20 kilogram and bearing brand name cleared between 2 June 1998 and 23 June 1998. Assessees neither paid the amount nor did department initiate any action to recover the amount as provided in the Act ibid. This resulted in blockage of government revenue of Rs.39.04 lakh as well as interest at applicable rate.

The Ministry stated (December 2005) that the Appellate Commissioner had set aside the orders confirming demand. The Ministry has not intimated about acceptance of the orders of Appellate Commissioner as the duty for the period from 2 June 1998 to 23 June 1998 was not exempted by issue of any statutory notification.

16.3 Other cases

In two other cases of demands, the Ministry/department had accepted objections involving duty of Rs.16.08 lakh till January 2006.

CHAPTER XVII : CESS NOT LEVIED OR DEMANDED

Cess is levied and collected in the same manner as excise duty under provisions of various Acts of Parliament.

Some of the cases in which cess was not levied or demanded are mentioned below:

17.1 Non-levy of cess on textiles

Cess at 0.05 per cent ad valorem is leviable on textiles manufactured in India under section 5A(1) of Textile Committee Act, 1963, and notification issued by the Ministry of Commerce on 1 June 1977. For this purpose, textiles interalia include fabrics made wholly or partly of cotton, wool, silk, artificial silk or other fabric. Authority to collect such cess is vested in 'textile committee' constituted under sub-section (3) of Act, ibid.

17.1.1 Audit revealed that in textile processing units in Ahmedabad I, Daman, Surat I, Vadodara II and Vapi commissionerates, between December 2003 and October 2004, eighteen assessees engaged in manufacture of processed textile fabrics did not pay textile cess amounting to Rs.2.12 crore between 1996-97 and 2003-04.

On this being pointed out (between February 2002 and October 2004), the Ministry of Textiles stated (June 2005) that the committee was closely pursuing the matter to recover the cess on priority.

17.1.2 Fifty three assessees, in Thane I and II commissionerates, engaged in manufacture of textile materials/articles falling under chapters 52,54,55,58 and 60 did not pay cess of Rs.91.13 lakh on products cleared during the years 2002-03 and 2003-04. No action was taken by textile committee for collection of cess from the assessees in accordance with the rules, ibid.

On this being pointed out (December 2004), the Ministry of Textiles stated (September 2005) that the committee was pursuing recovery of cess on priority.

17.2 Non-payment of cess on cement

According to provisions of section 9(1) of Industries (Development and Regulation) Act, 1951 and Cement Cess Rules, 1993 made thereunder, cess at the rate of Rs.0.75 per tonne is leviable on cement manufactured and removed. The authority to collect such cess is vested with the development commissioner of cement industry, Ministry of Industry.

M/s. Shree Digvijay Cement Company Ltd., in Rajkot commissionerate, manufactured and removed 64,59,934 tonne of cement between 1996-97 and 2003-04 but did not pay cess amounting to Rs.48.45 lakh.

On this being pointed out (February 2005), the Ministry of Commerce and Industry stated (June 2005) that the assessee was being pursued for recovery from January 2001.

17.3 Other cases

In one other case of cess, department had accepted the objection involving cess of Rs.2.46 lakh and reported (January 2006) its recovery.

CHAPTER XVIII : MISCELLANEOUS TOPICS OF INTEREST

18.1 Loss of revenue due to inconsistency between Act and notification

Government through Finance Act, 2000 amended section 3(1) of Central Excise Act so as to levy BED as well as "additional custom duty" (CVD) under Customs Tariff Act on goods manufactured by 100 per cent EOU and brought to any other place in India. This amendment was given retrospective effect from 11 May 1982.

Under notification dated 4 January 1995 all excisable goods produced or manufactured by 100 per cent EOU and cleared in DTA were exempt from so much of duty of excise leviable thereon under section 3 of Central Excise Act which was in excess of the amount calculated at the rate of 50 per cent of each of duties of customs which would be leviable under section 12 of Customs Act, 1962. The notification was amended on 16 September 1999 to substitute references to "the duties of customs leviable under section 12 of the Customs Act, 1962" with "the duties of customs leviable under the Customs Act, 1962 or under any other law for the time being in force". This amending notification was effective prospectively. However, section 3(1) of Central Excise Act levied, retrospectively from 11 May 1982 'basic custom duty' as well as 'additional customs duty' on goods manufactured by 100 per cent EOU and brought to any other place in India. Thus, there was an anomaly between the Act and the notification during the period between 11 May 1982 and 15 September 1999.

M/s. Century Denim and M/s. Maral Overseas Ltd. Khargone, both 100 per cent EOUs in Indore commissionerate, engaged in manufacture of cotton yarn, cotton fabric denim, knitted cotton fabrics and garments, cleared their products under DTA on payment of central excise duty in terms of exemption notification. Department demanded CVD and special duty of Rs.1.97 crore for April 1997 to January 1998 from the first assessee and Rs.0.17 crore for March 1997 to August 1999 from the second but the demands were struck down by CEGAT in April 2003 in the first case and by Commissioner Indore on June 2004 in the second as the amended notification was applicable only from 16 September 1999. Had the amendment in notification of 4 January 1995 also been made concurrent with amended section 3(1) of the Act, revenue of Rs.2.14 crore could have been recovered.

On this being pointed out (August 2004), the department stated (September 2004) that it was a policy matter of the Government.

The fact remains that non-amendment of notification retrospectively in line with section 3(1) of Central Excise Act created inconsistency between Act and notification which resulted in revenue becoming irrecoverable.

Reply of the Ministry had not been received (January 2006).

18.2 Non-filing of appeal led to financial accommodation to the assessee

Rule 8 of Central Excise Rules, 2002, prescribes that duty on goods removed from a factory or a warehouse during the first fortnight of the month shall be paid by 20th of that month and that on goods removed from the factory or the warehouse during the second fortnight of the month shall be paid by fifth of the following month. If assessee fails to pay any one instalment within 30 days from the due date or defaults in payment of instalment by the due dates for the third time in a financial year, he shall forfeit the facility for period of two months starting from date of communication of order or till such date on which all dues are

paid, whichever is later. Assessee is required to pay excise duty for such clearance through PLA. In the event of any failure, it shall be deemed that such goods have been cleared without payment of duty and he shall be liable to penalty not exceeding duty leviable or ten thousand rupees whichever is greater.

M/s. ISI Bars Ltd. in Raigad commissionerate, defaulted in payment of instalment for more than 30 days and jurisdictional deputy commissioner passed forfeiture order dated 30 April 2002 forfeiting facility of fortnightly payment of duty directing assessee to remove goods on payment of duty consignment-wise by debiting through account current (PLA) for a period of two months or till such date till all dues were paid. The assessee went in appeal against the said forfeiture order and commissioner (appeals) vide his order in appeal dated 13 May 2002 lifted the embargo and allowed assessee to utilise Cenvat credit account, after ten days of receipt of forfeiture order. As a result the assessee utilised credit of Rs.1.90 crore for payment of duty on fortnightly basis during May 2002 and June 2002. In a similar case of M/s. G.K.W. Ltd. department had appealed to tribunal and won the case. No appeal, however, was filed against the order of commissioner (appeals) in this case.

On this being pointed out (June 2004), the Ministry stated (August 2005) that the order in appeal was accepted by the commissioner in June 2002 and therefore it had attained finality in terms of legal provisions.

Reply is not tenable as provisions of rule 8 were mandatory in nature and therefore the case was fit for appeal. Failure of department in not doing so resulted in financial accommodation to the assessee to the tune of Rs.1.90 crore.

18.3 Unintended availment of benefit

Explanation III given under rule 5 of Hot Air Stenter Independent Textile Processor Annual Capacity Determination Rules, 1998 as amended, stipulates that if processor of specified fabrics has proprietary interest in any other factory primarily and substantially engaged in the spinning of yarn or weaving of fabric, he cannot be treated as an independent processor for the purpose of levy of duty under section 3A of Central Excise Act. Since the term 'proprietary interest' has not been defined in the Act, related provisions in Companies Act, 1956 (section 370 sub section 1B) and in Monopolies and Restrictive Trade Practice Act, 1969 {section 2(g) and explanation thereto} have to be applied for interpretation of this term. As per explanatory note to section 2(g) of MRTP Act, two undertakings shall be deemed to be inter-connected if one owns, manages and controls the other. Ministry of Law clarified on 28 June 2001 that the term 'proprietary interest' means any right, title etc. one has by virtue of being holder of any account of property or establishment. Where proprietary interest in spinning unit or weaving of fabric was proved, such independent processors would discharge duty liability on processed fabrics at ad valorem rate.

M/s. SSM Processing Mills Ltd. Komarapalayam manufacturing processed textile fabrics in Coimbatore commissionerate, paid duty on their products under section 3A i.e. based on capacity of production. Directors of assessee company were also majority directors of another company viz., M/s. TAN India Ltd. a manufacturer of yarn. In terms of provisions cited in para 1 supra, the assessee and other company (manufacturer of yarn) were under the same management and the assessee company had proprietary interest in the other. Therefore, payment of duty on production capacity basis was not correct and resulted in short payment of duty of Rs.1.44 crore during the period from 16 December 1998 to May 2000.

On this being pointed out (July 2000), the Ministry stated (December 2005) that two companies were separate legal entities and there was no flow back of funds or sharing of profits and hence they did not have any proprietary interest and that the provisions of the Companies Act, and the MRTP Act, could not be applied to section 3A.

The reply is not relevant since the question involved in this case is of "proprietary interest" which has not been defined in the relevant rules. Both companies had four common directors having majority of voting rights. As such, by virtue of legal opinion ibid the assessee did have "proprietary interest" in the other company and were not eligible for availment of facility for payment of duty on basis of capacity of production.

18.4 Escapement of duty by short accountal of production

Rule 53 of Central Excise Rules, 1944 (now rule 10 of Central Excise Rules 2001/2002), envisages that every manufacturer shall maintain proper records, on daily basis, indicating the particulars regarding description of the goods produced or manufactured, opening balance, quantity produced or manufactured, inventory of goods, quantity removed, assessable value, the amount of duty payable and particulars regarding amount of duty actually paid.

Test check of records of M/s. Martin and Harris Laboratories Ltd. Gurgaon, in Delhi III commissionerate, for the period from 1998-99 to 2001-02 revealed that production of medicines viz tablets, capsules and liquids/syrup as shown in excisable records (R.T.12/E.R.1) was less than that as shown in balance sheets for the years ended March 1999 and March 2002. Thus short accountal of production of medicines resulted in escapement of duty of Rs.58.77 lakh.

On this being pointed out (March 2003), the Ministry admitted the objection (September 2005).

18.5 Irregular refund taken as credit in PLA

Section 11B of Central Excise Act, 1944, provides that any person claiming refund of any duty of excise may make an application for refund of such duty to assistant commissioner/deputy commissioner of central excise before expiry of one year from the relevant date in such form and manner as may be prescribed. It further provides that application shall be accompanied by such documentary or other evidence as the applicant may furnish to establish that amount of duty of excise in relation to which such refund is claimed was collected from, or paid by, him and the incidence of such duty had not been passed on by him to any other person.

Further, there is no provisions in Central Excise Law to take *suo motu* credit of central excise duty paid/debited by the assessee due to wrong calculations of duty, on invoices issued for clearances during preceding months in PLA/Modvat credit account in the succeeding months.

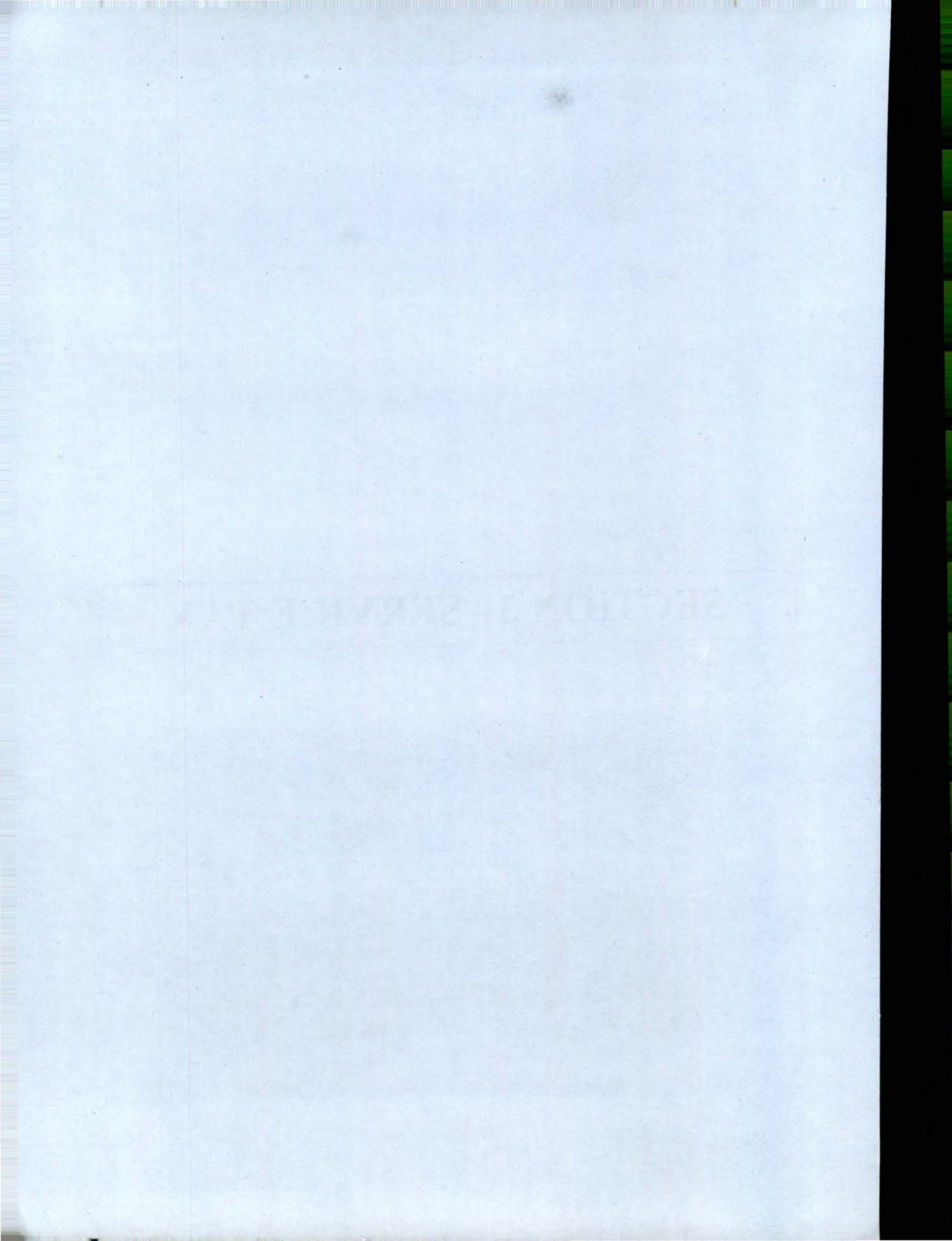
M/s. Bharat Heavy Electricals Ltd. in Kanpur commissionerate, took *suo motu* credit of Rs.37.22 lakh of their own accord in PLA (April 2000) on ground that excess duty was paid due to oversight and wrong calculation in respect of clearance made through 17 invoices. This was in contravention of section 11B of the Act and violation of procedures of refund of duty as per rules ibid, which was recoverable alongwith penalty and interest.

On this being pointed out (between December 2000 and September 2004), the Ministry admitted the objection and intimated (November 2005) that demand of Rs.37.63 lakh had been confirmed.

18.6 Other cases

In 353 other cases of miscellaneous topics of interest the Ministry/department had accepted objections involving duty of Rs.4.13 crore and reported recovery of Rs.3.41 crore in 349 cases till January 2006.

SECTION 3 - SERVICE TAX



CHAPTER XIX : SERVICE TAX RECEIPTS

19.1 Tax administration

Service tax was introduced from 1 July 1994 through Finance Act, 1994. Administration of service tax has been vested with the central excise department under the Ministry of Finance (the Ministry). Central Board of Excise and Customs (the Board) has set up a separate apex authority headed by Director General Service Tax (DGST) at Mumbai for its administration. Commissioners of central excise have been authorised to collect service tax within their jurisdiction. The number of services under the net has increased from 26 in 1999-2000 to 71 in 2004-05.

19.2 Trend of receipts

Revenue projected through annual budget and actual receipts from service tax during the years 2000-01 to 2004-05 is exhibited in the table below:-

(Amount in crore of rupees)

Year	No. of services covered by tax	Budget estimates	Revised budget estimates	Actual receipts*	Difference between actual receipts and budget estimates	Percentage variation
2000-01	26	2200	2200	2612	412	18.73
2001-02	41	3600	3600	3302	(-) 298	(-) 8.28
2002-03	51	6026	5000	4122	(-) 1904	(-) 31.60
2003-04	58	8000	8300	7890	(-) 110	(-) 1.38
2004-05	71	14150	14150	14196**	46	0.33

* Figure as per Finance Accounts

** Figure is provisional

It can be seen that except in 2000-01 and 2004-05, actual collections had been lower than the budget estimates all through the five year period. Shortfall ranged from Rs.110 crore to Rs.1904 crore or 1.38 to 31.60 per cent over budget estimates during these years. In one of the five years i.e. 2002-03 receipt did not match even scaled down revised estimates and in 2003-04 did not reach increased budget estimate.

19.3 Outstanding demands *

The number of cases and amount involved in demands for service tax outstanding for adjudication/recovery as on 31 March 2005 are given below:

(Amount in crore of rupees)

		As on 31 March 2004				As on 31 March 2005			
		Number of cases		Amount		Number of cases		Amount	
		More than five years	Less than five years	More than five years	Less than five years	More than five years	Less than five years	More than five years	Less than five years
(a)	Pending with Adjudicating officers	41	29374	2.02	700.54	153	25466	2.67	1256.29

(b)	**Pending before**								
(i)	Appellate Commissioners	0	823	0.00	85.48	0	589	0.00	764.77
(ii)	Board	0	14	0.00	0.12	0	7	0.00	2.11
(iii)	Government	0	0	0.00	0.00	0	2	0.00	0.08
(iv)	Tribunals	0	283	0.00	81.16	8	291	0.03	407.07
(v)	High Courts**	8	149	0.00	27.12	9	105	0.05	35.47
(vi)	Supreme Court	0	10	0.00	4.20	0	11	0.00	0.57
(c)	**Pending for coercive recovery measures**	16	5444	0.00	38.55	474	9248	0.23	65.67
	Total	**65**	**36097**	**2.02**	**937.17**	**648**	**35719**	**2.97**	**2532.05**

* Figure furnished by the Ministry and relates to 93 commissionerates of central excise (commissionerates).

** The Ministry intimated that the amount when rounded off amounts to zero

A total of 36,367 cases involving tax of Rs.2535.02 crore were pending as on 31 March 2005 with different authorities, of which 70 per cent in terms of number were with the adjudicating officers of the department. Pendency of demands for coercive recovery measures with the departmental officers has increased from 5,460 in 2003-04 to 9,722 cases in 2004-05 i.e an increase of about 78 per cent.

19.4 Fraud/presumptive fraud cases *

The position of fraud/presumptive fraud cases alongwith the action taken by the department against defaulting assessees during the period 2002-03 to 2004-05 is depicted in the following table :

(Amount in crore of rupees)

Year	Cases detected		Demand of duty raised	Penalty imposed		Duty collected	Penalty collected	
	Number	Amount	Amount	Number	Amount	Amount	Number	Amount
2002-03	195	40.26	14.46	22	3.08	1.56	6	0.01
2003-04	995	172.75	130.85	240	30.38	14.94	115	0.09
2004-05	1415	296.54	181.23	323	22.32	19.74	159	0.23
Total	**2605**	**509.55**	**326.54**	**585**	**55.78**	**36.24**	**280**	**0.33**

* Figure furnished by the Ministry and relates to 93 commissionerates

The above data reveals that while a total of 2,605 cases of fraud/presumptive fraud were detected during the years 2002-05 by the department, involving tax of Rs.509.55 crore, it raised demand of Rs.326.54 crore only and recovered Rs.36.24 crore (11.10 per cent). Similarly, out of penalty of Rs.55.78 crore imposed, the department recovered only Rs.0.33 crore (0.59 per cent).

19.5 Provisional assessments*

The number of cases of provisional assessments and amount involved therein as on 31 March 2004 and 31 March 2005 is exhibited in table as follows :-

(Amount in crore of rupees)

		As on 31 March 2004		As on 31 March 2005	
		Number of cases	Duty involved	Number of cases	Duty involved
(a)	Pending decision by Court of law	7	0.01	7	0.03
(b)	Pending decision by Government of India or Board	0	0.00	0	0.00
(c)	Pending adjudication with the Commissioners	3	0.09	8	16.65
	Total	**10**	**0.10**	**15**	**16.68**

* Figure furnished by the Ministry and relates to 93 commissionerates

19.6 Contents

This section contains 48 paragraphs (including cases of total under assessment) featured individually or grouped together with revenue implication of Rs.86.57 crore directly attributable to audit pointing out non-compliance to rules/regulations. The Ministry/department had accepted audit observations in 42 paragraphs involving Rs.35.59 crore and recovered Rs.5.41 crore till January 2006.

CHAPTER XX : NON/SHORT LEVY OF SERVICE TAX

Test check of records relating to service tax assessments revealed cases of non-payment, non-levy, short levy or non-recovery, some of which are given below :

20.1 Non-payment of service tax

20.1.1 Broadcasting services

Broadcasting services have been brought under service tax net with effect from 16 July 2001.

Test check of records of service tax division-X, in Delhi I commissionerate of service tax, revealed that Prasar Bharti Corporation, registered with service tax department in August 2003 collected broadcasting service charges of Rs.936.05 crore in respect of Doordarshan commercial service and All India Radio commercial broadcasting service from 16 July 2001 to 31 March 2003 from clients. Service tax of Rs.46.80 crore due on these service charges was, however, not paid. Department too did not initiate any proceedings to recover the same.

On this being pointed out (November 2004), the Ministry stated (November 2005) that as per Board's letter dated 27 March 2003, Prasar Bharti (Doordarshan and All India Radio) was not liable to pay service tax prior to 1 April 2003.

Reply of the Ministry is not tenable as Board in its earlier circular dated 9 July 2001 had clarified that, under provisions of section 22 of Prasar Bharti Act, 1990, the Corporation, was exempted from only direct taxes since they were not borne by it from its own income, but not indirect taxes. Board in its subsequent circular dated 27 March 2003 rendered Corporation not liable to pay service tax and yet again modified its decisions through subsequent circular of 14 July 2003 making Prasar Bharti liable to pay service tax from 1 April 2003. Since specific notification under section 93 (1) or (2) of Finance Act, 1994 as amended, was not issued granting exemption to the Corporation from payment of service tax, it was recoverable for the period 16 July 2001 to 31 March 2003.

20.1.2 Management consultancy services

Section 65(65) of Finance Act 1994, envisages that management consultant is one who is engaged in providing any service, either directly or indirectly, in connection with management of any organisation in any manner and includes any person who renders any advice, consultancy or technical assistance, relating to conceptualizing, devising, development, modification, rectification or upgradation of any working system of any organization. Further, section 68 of the Act, provides that every person providing taxable service to any person shall pay service tax at the rate and within such period as may be prescribed. Interest and penalty shall also be leviable on non/delayed payment of service tax under section 75 and 76 of the Act, ibid.

M/s. Hero Cycles Ltd. and M/s. Jagatjit Industries, in Ludhiana and Jalandhar commissionerates, received Rs.14.40 crore during April 2001 to March 2004 on account of royalty for use of their trade mark by various organisations. As use of 'trade mark' fell under category of "management consultancy" the assessees were liable to pay service tax. This also found support in regional advisory committee (ST Section Madurai Commissionerate) meeting held on 29 August 2003 {2003 (111) ECR 14C} wherein it was clarified that if manufacturer gave consent to another manufacturer for use of his trade mark and realised the

amount (royalty) for the use of trade mark, it would be covered under management consultant's service and liable to service tax. No service tax was paid by the assessees. Non-payment of service tax amounted to Rs.1.04 crore besides levy of interest of Rs.23.68 lakh (upto December 2004).

On this being pointed out (December 2004), the department in one case stated (May 2005) that SCN for Rs.1.22 crore had been issued in April 2005. Reply in the second case was awaited (May 2005).

Reply of the Ministry had not been received (January 2006).

20.1.3 Clearing and forwarding agents

Under sections 66 and 67 of Finance Act, 1994 read with notification dated 11 July 1997 service provided by clearing and forwarding agent is chargeable to service tax. Clause 25 of section 65 ibid (as amended by subsequent Finance Acts) defines clearing and forwarding agent as any person who is engaged in providing any service, either directly or indirectly, connected with clearing and forwarding operations in any manner to any other person and includes consignment agents. Further, it has judicially been held in Prabhat Zarda Factory (India) Ltd. vs. commissioner {2002 (145) ELT 222 (Tri-Kolkata)} that procuring orders and passing them on to principal for executing in lieu of commission is within the scope of services of clearing and forwarding agent even if goods are not directly dealt with by them. This service is chargeable to service tax under business auxiliary services from 1 July 2003.

M/s. New Tobacco Company Ltd. (Lessee: RDB Industries Ltd.), Kolkata, in Kolkata III commissionerate, manufacturing cigarettes and other tobacco products entered into agreements with different manufacturer/dealers of goods (principals) for procurement of orders on behalf of them from Videsh Sanchar Nigam Ltd., West Bengal State Electricity Board, etc., and passing them on to such manufacturer/dealers for execution in lieu of commissions payable by such principals. Scrutiny revealed that neither did assessee pay service tax on commission earned nor did the department demand the same. This resulted in non levy of service tax of Rs.1.02 crore during the period from 2001-02 to 2003-04. On this being pointed out (January 2005), the department contended (April 2005) that decision of the Tribunal was not relevant, since activity undertaken by assessee was that of commission agent and as per clause (2) of Board's circular dated 20 June 2003, such agents were chargeable to service tax under business auxiliary service which were exempt from service tax. Reply of the department is not acceptable since tribunal's judgment had not left any scope for doubt on classification of activities of commission agents as clearing and forwarding services. In the instant case, the assessee acting as clearing and forwarding agent had rendered services and, therefore, was liable to pay service tax from 2001-02 to 2003-04. Moreover, as per clause (3) of Board's circular of 20 June 2003, clearing and forwarding agents working on commission basis have been covered under the specific heading of clearing and forwarding service and not as claimed by the department, under the general heading of business auxiliary services which did not exist prior to July 2003. Reply of the Ministry had not been received (January 2006).

M/s. Saini Alloys Pvt. Ltd. in Noida commissionerate, collected Rs.18.19 crore as commission from customers for providing services on account of procurement of orders and promoting sales of products of those customers during the period from 2000-01 to 2003-04, but service tax of Rs.96.42 lakh due thereon was not levied. Further, interest and penalty was also to be levied on the assessee. On this being pointed out (August 2004), the Ministry

admitted the objection and stated (September 2005) that SCN for Rs.1.41 crore had been issued in January 2005.

M/s. Trumac Engineering Company, Ahmedabad and M/s. Paras Pharmaceuticals, Kalol in Ahmedabad I and III commissionerates, availed services of clearing and forwarding agents between 16 July 1997 and 16 October 1998 and paid Rs.750.38 lakh (Rs.689.23 lakh plus Rs.61.15 lakh) towards commission. During the period of agreement, service providers were required to effect sales of the goods of principal and arrange recovery of outstanding dues from customers. However, assessees neither filed ST-3A return nor paid service tax as contemplated in the rule. This resulted in non-payment of service tax to the extent of Rs.41.54 lakh including interest of Rs.4.02 lakh. On this being pointed out (August and September 2004), the Ministry admitted the objection and intimated (December 2005) issue of a show cause notice for Rs.64.58 lakh.

M/s. Tinplate Company India Ltd. (TCIL), in Jamshedpur commissionerate, entered into agreement with M/s. TISCO Ltd., Jamshedpur on 30 March 1998 appointing the assessee as consignment agent of M/s. TISCO Ltd. for consigning converted excisable goods to customers. M/s. TCIL received commission of Rs.8.97 crore against consignment of 3,58,983 tonne of products during the period April 2001 to March 2003. Service tax amounting to Rs.54.94 lakh was not paid which was recoverable with interest and penalty. On this being pointed out (June 2004), the department stated (October 2004) that service tax was not recoverable from M/s. TCIL as service was not provided by them but was recoverable from respective consignment agents. It, however intimated that demand cum SCN had been issued to M/s. TCIL. Reply of the department is not tenable as M/s. TCIL received payment for providing consignment agents services. Therefore liability to pay tax lay with M/s. TCIL. The Ministry stated (December 2005) that the assessee had paid Rs.5.64 lakh but SCN was pending decision.

20.1.4 Interconnection usage charges

Leased circuit services were brought under service tax net by Finance Act, 2001, with effect from 16 July 2001. Board clarified on 8 August 2002 that 'inter-connectivity linked charges' were charges for providing 'leased circuits', hence service tax would be leviable. On the same analogy interconnection usage charges which are recovered/collected by one operator from another operator as service revenue, for providing service of their networks, were also liable to service tax.

M/s. Hexacom India Ltd. in Jaipur I commissionerate, were engaged in activity of providing cellular mobile telephony service. Scrutiny of records revealed that bills raised by assessee on other operators viz. Bharat Sanchar Nigam Ltd., Videsh Sanchar Nigam Ltd., Reliance Infocomm Ltd., Shyam Telelinks Ltd., ESSAR, etc. on account of interconnectivity usage charges (IUC) with effect from May 2003 for providing service to consumers of those operators were without charging service tax. Since interconnect revenue was service revenue received for providing service to consumers of other operators and exhibited in profit and loss account as service revenue, service tax was required to be charged from those operators. Omission to do so resulted in non-levy of service tax amounting to Rs.1.22 crore during the period May 2003 to March 2004.

On this being pointed out (February 2005), the Ministry stated (September 2005) that it had clarified vide its letter dated 15 June 2004 that IUC will not be chargeable to service tax and other such charges would get taxed through caller charges.

Rule 6(3) of Service Tax Rules, 1994, provides that where an assessee has paid service tax in respect of a taxable service, which is not so provided by him either wholly or partially for any reason, he may adjust excess service tax so paid by him (calculated on a pro rata basis) against service tax liability for the subsequent period, if the assessee has refunded the value of taxable service and service tax thereon to the person from whom it was received.

M/s. TVS Motor Company Ltd., Hosur in Chennai III commissionerate, paid service tax of Rs.81.58 lakh for the period from November 2002 to November 2003 as recipient of service availed of from non-resident Indian on technical consultancy, engineering consultancy, marketing research etc. They found that tax of Rs.41.20 lakh had been paid in excess by oversight. Of this amount, they adjusted Rs.14.38 lakh against service tax liability during November 2003 to January 2004. In February 2004, the assessee intimated department that Rs.14.38 lakh had been adjusted and balance would be adjusted against future liability of service tax. Such *suo motu* adjustment of service tax against future liability was not correct, being not covered by rule 6(3) of Service Tax Rules, 1994, and therefore assessee should have claimed refund under section 11B of Central Excise Act, 1944.

On this being pointed out (March, April and May 2004), the Ministry admitted the objection and stated (July 2005) that SCN for Rs.41.20 lakh had been issued in May 2004.

20.6 Other cases

In 48 other cases of non/short levy of service tax the Ministry/department had accepted objections involving duty of Rs.3.52 crore and reported recovery of Rs.0.69 crore in 30 cases till January 2006.

Jayanti Prasad

New Delhi
Dated : 22 March 2006

(JAYANTI PRASAD)
Principal Director (Indirect Taxes)

Countersigned

New Delhi
Dated : 30 March 2006

(VIJAYENDRA N. KAUL)
Comptroller and Auditor General of India

20.3.2 M/s. Jay Pee Bela Plant, Rewa (formerly known as M/s. Jay Pee Bela Cement, Rewa) was registered for payment of service tax under category of goods transport operators service in Bhopal commissionerate. The assessee had goods transport operations through regional marketing offices (RMO) located at Delhi, Allahabad and Patna. Scrutiny of financial records revealed that they had received Rs.15.45 crore during December 1997 to June 1998 for providing transport services. Service tax of Rs.77.26 lakh was payable but assessee paid Rs.6 lakh only for Rewa region. Balance of Rs.71.26 lakh was recoverable with interest of Rs.35.76 lakh (till March 2001).

On this being pointed out (June 2001), the department stated (June 2005) that demand of service tax of Rs.47.40 lakh, payment of interest and penalty at appropriate rate till the date of actual payment of service tax had been confirmed (March 2005) in respect of RMO, Rewa. Case of RMO at Delhi, Allahabad and Patna was to be decided by their jurisdictional adjudication authorities as assessee had got himself registered subsequently at those places.

The Ministry admitted the objection (January 2006).

20.4 Non-recovery of service tax on services of goods transport operators

Under notification dated 5 November 1997 effective from 16 November 1997, recipients of services of goods transport operators are liable to pay service tax at the rate of five per cent of the freight charges paid to goods transport operators. In case of Laghu Udyog Bharati {1999 (112) ELT 365}, Supreme Court held that recipients of services cannot be made liable to pay service tax and the rules made in this regard are ultra vires Finance Act, 1994. In order to validate recovery of service tax from recipients, Finance Act, 1994 had been amended with retrospective effect vide section 117 of Finance Act, 2000.

By Finance Act, 2003, a new section 71A was introduced requiring service receiver/user of transport operator to file return for the relevant period (i.e. 16 November 1997 to 1 June 1998) within six months from 14 May 2003.

In case of M/s. Ruby Woollen Pvt. Ltd. {2002 (103) ECR 176 (T)}, it was held that service tax along with interest became payable retrospectively with introduction of section 116 and 117 of Finance Act, 2000.

Eight assessees in Chennai II, III and IV, Indore, Jaipur II, Salem, Trichy and Vadodra II commissionerates, paid freight charges to goods transport operators during the period 16 November 1997 to 1 June 1998 for hiring transport services. Service tax of Rs.1.48 crore leviable thereon was, however, not paid. Department too did not take any action for recovery. Service tax was, therefore, recoverable with interest.

On this being pointed out (between September 2000 and March 2005), the Ministry admitted the objection and stated (between August and November 2005) that service tax of Rs.46.82 lakh had been recovered with interest of Rs.3.36 lakh from three assessees.

20.5 Unauthorised adjustment of service tax

Section 83 of Finance Act 1994, provides that provisions of section 11B of Central Excise Act, 1944 in force from time to time shall apply to service tax as well. Section 11B stipulates that any person claiming refund of any duty of excise may make an application within one year.

On this being pointed out (April 2004), the Ministry admitted the objection and stated (August 2005) that SCN had been issued (October 2004) for recovery of service tax of Rs.52.33 lakh alongwith interest and penalty.

20.2.6 M/s. Tisco Ltd., in Jamshedpur commissionerate, paid foreign consultants for technical know-how, drawing and design consultancy fee amounting to Rs.4.87 crore during the period April 2002 to March 2003 but service tax amounting to Rs.24.35 lakh was not paid by the assessee.

On this being pointed out (August 2003), the Ministry admitted the objection and stated (September 2005) that service tax amounting to Rs.1.87 crore alongwith interest of Rs.19.72 lakh had been recovered.

20.2.7 M/s. Bharat Aluminium Company Ltd., Korba in Raipur commissionerate, paid Rs.9.68 crore to certain foreign consultants (agencies) against consulting charges (in foreign exchange outflow) during the financial years 2001-02 and 2002-03 on which service tax of Rs.48.40 lakh was recoverable. Service tax was, however, not paid either by assessee (receiver of taxable service) or by agencies, which had rendered taxable services.

On this being pointed out (March 2004), the Ministry admitted the objection and stated (October 2005) that SCN had been issued (February 2005).

20.2.8 M/s. S.S. Oral Hygiene Products Pvt. Ltd., in Hyderabad-IV commissionerate, engaged in manufacture of tooth paste, incurred certain expenditure in foreign currency towards technical assistance fees. Scrutiny of annual accounts for the years 2000-2001 to 2003-2004 revealed that assessee paid Rs.4.16 crore during the period from July 2001 to March 2004 to a New York based firm M/s. Colgate Palmolive Company towards fees for technical assistance provided by them by deputing technicians who rendered assistance/supervision in the manufacture of tooth paste in conformity with the standards and quality specified by the said foreign based company. Service tax amounting to Rs.25.22 lakh was neither paid by service provider/service receiver nor demanded by the department.

On this being pointed out (December 2004/April 2005), the Ministry admitted the objection and stated (September 2005) that SCN for Rs.27.53 lakh had been issued in April 2005.

20.3 Short payment of service tax

20.3.1 Notification dated 16 December 2002 exempts taxable services provided by consulting engineer to a client on transfer of technology from so much of the service tax leviable thereon under section 66 of Finance Act, 1994, as is equivalent to the amount of cess paid on the said transfer of technology under provision of section 3 of the Research and Development Cess Act, 1986.

Scrutiny of records of Gurgaon and Faridabad commissionerates, revealed that five assessees (three in Gurgaon and two in Faridabad) received services in form of technical know-how/technical assistance from foreign consultants and paid an aggregated amount of Rs.48.29 crore to service providers from 14 May 2003 to August 2004. Since assessees had already paid cess at the rate of five per cent on transfer of technology, service tax at three per cent (8 minus 5 per cent) was recoverable which worked out to Rs.1.45 crore.

On this being pointed out (August and November 2004), the Ministry admitted the objection (November 2005).

services provided by person who is non-resident or is from outside India not having any office in India.

20.2.1 Five assessees, in Chandigarh and Ludhiana commissionerates, paid sum of Rs.223.26 crore to various foreign firms towards rendering services viz. technical know-how, imported technology, technical guidance during 1998-99 to 2003-04. These services fell under the definition of consulting engineer services. No service tax was, however, paid by the assessees in terms of provision mentioned above. This resulted in non-payment of service tax amounting to Rs.13.63 crore which was recoverable with interest of Rs.3.61 crore.

On this being pointed out (between June 2004 and December 2004), the Ministry admitted the objection (November 2005)

20.2.2 M/s. Bharat Heavy Electricals Ltd., Haridwar in Meerut I commissionerate, paid a sum of Rs.24.60 crore to foreign consultants for services in the field of management consultancy between April 2001 and March 2004. Since services were rendered in India, service tax amounting to Rs.1.46 crore was leviable. Although income tax and other taxes were deducted at source before releasing payment to foreign consultants, service tax was not recovered.

On this being pointed out (August and October 2004), the Ministry admitted the objection (November 2005).

20.2.3 Chief Engineer, National Highways, Public Works Department, Government of Karnataka, availed services falling under category of 'consulting engineers' from two foreign consultants viz. M/s. Scott Wilson Kirkpatrick and Company Ltd. U.K. and M/s. Booz Allen Hamilton Inc. U.S.A. Service charges of Rs.21.32 crore were paid during the years 1999-2000 to 2001-02. Since service had been rendered in India, service tax of Rs.1.07 crore was payable but the same was not paid.

On this being pointed out (March 2004), the Ministry while admitting objection stated (September 2005) that demands for Rs.1.24 crore had been confirmed and Rs.65.83 lakh recovered which includes Rs.25.36 lakh as interest. Report on recovery of remaining amount had not been received (January 2006).

20.2.4 M/s. L.G. Electronics Ltd., in Noida commissionerate, engaged in manufacture and marketing of various electronic house hold goods paid an amount of Rs.7.07 crore, in foreign currency, towards advertisement, publicity and sales promotion during 2003-04 but service tax amounting to Rs.56.59 lakh payable thereon was not paid.

This was pointed out (January 2005), reply of the Ministry/department had not been received (January 2006).

20.2.5 M/s. Tata Holset, Dewas, in Indore commissionerate, as part of joint venture with Holset Engineering Company Ltd., United Kingdom, received technical information and services to manufacture turbo charger. Assessee paid royalty of Rs.7.15 crore against receipt of such technical services between July 1997 and January 2004. Records further revealed that assessee was authorised by foreign service provider through an agreement that the taxes payable in India be deducted from royalty and remitted to government by the assessee. Service tax of Rs.48.59 lakh due thereon was, however, not paid which was recoverable with interest of Rs.10.14 lakh.

assistance' to buyer of plant and machinery and prior to 10 September 2004 it was leviable to service tax under 'consulting engineer's services' from 7 July 1997 as clarified by Board vide circular dated 18 December 2002.

20.1.6 Business auxiliary services

"Business auxiliary services" has been brought under service tax net with effect from 1 July 2003. Section 65(19) of Finance Act, 1994, envisages that "business auxiliary services" means any commercial concern which is engaged in providing any service to any client in relation to promotion or marketing or sale of goods, promotion or marketing of services or any customer care service, or any incidental or auxiliary support service such as billing, collection or recovery of cheque etc.

M/s. Emtici Engineering Ltd., Vallabh Vidyanagar, in Vadodara I commissionerate, entered into agreement with M/s. Eimco Elecon (I) Ltd., Vallabh Vidyanagar on 1 January 2003 (i) to provide after sales service to equipment users; (ii) enhance sales of equipments; (iii) instal and place in proper operation all new equipments sold; and (iv) make periodic visit to customer and potential customers on payment of service charges. For services rendered during July 2003 and March 2004, M/s. Eimco Elecon paid Rs.5.65 crore to service provider. However, service provider (M/s. Emtici Engineering Ltd. Vallabh Vidyanagar) neither registered themselves with jurisdictional service tax branch nor paid service tax. This resulted in non payment of service tax of Rs.45.23 lakh. On this being pointed out (January 2004), the Ministry admitted the objection (July 2005) and stated that SCN for Rs.42.23 lakh had been issued.

M/s. Elgi Equipments Ltd. Singanallur, in Coimbatore commissionerate, entered into agreements with M/s. Valvoline Cummins Ltd. and M/s. Chemoleum Ltd. whereby, assessee would arrange to market products of those companies through its dealer networks and would endeavor to promote sale of licensed products and arrange for regular follow-up through its personnel. The assessee also granted non-exclusive licence to the said companies for affixing or using its trade marks/brand name viz 'ELGI/AIRLUBE and also provided its marketing network for promotion of sales. Assessee received royalty of Rs.1.43 crore during 2003-04 for marketing services rendered to these companies but service tax of Rs.11.46 lakh due thereon was not paid. On this being pointed out (May June and December 2004), the Ministry stated (September 2005) that royalty received by assessee was solely consideration for use of brand name and nothing else, therefore royalty charges received by assessee attracted service tax from 10 September 2004 under the heading 'intellectual property service'. The reply is not tenable as assessee had provided marketing services and also granted trademark licence. Grant of trademark licence for compliance of quality assurance of product as provided in the agreement is 'a customer care service' provided on behalf of the companies. Customer care service is covered by definition of 'business auxiliary service'. Therefore, assessee is liable to pay service tax under 'business auxiliary service'.

20.2 Non-levy of service tax on services rendered by foreign service providers

Rule 6 of Service Tax Rules, 1994, provides that where a person liable to service tax is non-resident or is from outside India, such person shall pay service tax by demand draft alongwith the return prescribed within 30 days from date of raising bill on the client for taxable service rendered. However, vide rule 2(d) (iv) inserted with effect from 16 August 2002, person receiving taxable services in India has been made liable for payment of service tax on

Reply of the Ministry is not tenable. As IUC included charges towards interconnect link cost and set up cost which are leviable to service tax, service tax is required to be levied. Subjecting these amounts to tax subsequently through caller charges is not relevant as the point of tax becoming due would be the service provider who has provided the interconnections service.

20.1.5 Erection, commissioning and installation services

Section 65(28) of Finance Act, 1994 (as amended by Finance Act 2003) defines "commissioning and installation" as any service rendered by commissioning and installation agency in relation to commissioning and installation of plant, machinery or equipment. Service tax at the rate of eight per cent on gross amount charged by commercial concern for such service excluding cost of parts or other material if any, sold while rendering such service is leviable from July 2003 vide notifications dated 20 June 2003 and 21 August 2003.

In case of composite contact for supplying plant machinery or equipment and its commissioning and installation, service tax is payable on 33 per cent of gross amount charged from customer vide notification dated 21 August 2003.

M/s. Johnson Lifts Pvt. Ltd., in Chennai IV commissionerate, manufacturer of lifts and parts of lifts was engaged in supply, commissioning and installation of lifts on contract basis. During 2003-04, the contract receipts towards supply, commission and installation of lifts was Rs.79.73 crore. Service tax payable (eight per cent) on 33 per cent of gross contract value for the year worked out to Rs.2.10 crore. Department, however, allowed for central excise purpose, 15 per cent of contract amount as abatement towards commissioning and installation. Thus, on conservative estimate, 15 per cent of the contract amount was taken as the value of commissioning and installation i.e. Rs.11.98 crore (15 per cent of Rs.79.93 crore) for which service tax payable but not paid worked out to Rs.0.96 crore.

Assessee also purchased eight escalators and installed and commissioned them at premises of customers. Total contract receipts for these during 2003-04 were Rs.2.39 crore and service tax leviable worked out to Rs.6 lakh which also had not been paid. On this being pointed out (October and December 2004), department stated (February 2005) that since assessee manufactured lifts at customer's premises by way of supply of components and erection thereof, the said activity was manufacturing activity and not that of service under 'erection, commissioning and installation service'. Further the term 'erection' was included in the said service with effect from 10 September 2004 and Ministry also clarified in their circular of 20 June 2003 that all activities other than commissioning and installation of plant and machinery per se would not be chargeable to service tax. The reply is not tenable since as per terms of contract, construction of lift, well and related items of work were responsibilities of the customers. Since assessee had installed and commissioned the lifts, service tax was payable. Reply of the Ministry had not been received (January 2006).

M/s. Karnataka Vidyuth Karkhane, Bangalore, in Bangalore commissionerate of service tax, engaged in manufacture of plant and machinery realised Rs.293.33 lakh between July 2003 and August 2004 from various customers on account of erection, commissioning and installation of plant and machinery. Though such services were liable, service tax of Rs.23.47 lakh due thereon was not levied. On this being pointed out (October 2004), the Ministry stated (January 2006) that erection charges came into service tax net only with effect from 10 September 2004 and, hence, service tax was not leviable for the period prior to 10 September 2004. Reply of the Ministry is not tenable as erection services are in nature of 'technical