PREFACE

This report for the year ended 31 March 2009 has been prepared for submission to the President of India under Article 151(1) of the Constitution of India.

Audit of Revenue Receipts – Indirect Taxes of the Union Government is conducted under the Section 16 of the Comptroller and Auditor General of India (Duties, Powers and Conditions of Service) Act, 1971.

The observations included in this report have been selected from the findings of test audit, during the year 2008-09, while conducting performance audit of custom duties from 'Natural or cultured pearls, precious or semi-precious stones, precious metals, metals clad with precious metal and articles thereof, imitation jewellery, coin (chapter 71 of Customs Tariff Heading)'.

EXECUTIVE SUMMARY

We conducted a performance audit on the levy of customs duty on 'natural or cultured pearls, precious or semi-precious stones, precious metals, metals clad with precious metal and articles thereof, imitation jewellery, coin (chapter 71 of Customs Tariff Heading)' to evaluate the adequacy of the provisions of the relevant Acts, Rules and instructions in ensuring proper assessment and collection of revenues.

The estimated duty foregone in this sector during 2005-06 to 2007-08 amounted to Rs. 68,192 crore. We found that the revenue earned from gems and jewellery by eleven audited commissionerates, during 2005-06 to 2007-08 was Rs. 2,023 crore, while the duty foregone was Rs. 20,864 crore. As against the import growth of 16 per cent, the growth in exports was only 13 per cent during the three years. Thus, despite the substantial revenue foregone and the various benefits and exemptions extended to this sector, the exports growth has not yet caught up with the rate of growth of imports. Our major findings and related recommendations are summarised in the following paragraphs:

- The Director General of Valuations (DGOV) was maintaining a database of the imports/exports of gems and jewellery which was found to be largely incomplete and could not be used as planned. The major portion of the data gap was attributable to the Diamond Plaza Customs Clearing Centre (DPCC), which handled bulk of the trade but their transactions were not entered in the database. The DPCC had also not implemented the Indian Customs Electronic Data Interchange System (ICES) used for assessments. We recommend that these two major IT systems should be kept updated and should be implemented by the DPCC, which handles the bulk of the trade.
- The goods exported by the Special Economic Zone (SEZ) units are not subjected to any physical verification. We recommend prescription of norms for physical examination of goods cleared by the SEZ units for adhering to the RBI requirements and to prevent any loss of revenue.
- There is ambiguity in the duty rate applicable for gold coins. We recommend that the ambiguity in the related notification may be clarified so that 'gold coins' can be classified as a unique item subjected to a specified rate of duty.
- The calculation of net foreign exchange (NFE) of exporters suffers from serious deficiency. The value of goods sold to Domestic Tariff Area (DTA) against foreign exchange payments are treated as exports whereas the value of goods purchased from DTA are not treated as imports. We recommend that the Government should introduce a provision in the SEZ rules to consider supplies made by DTA units to SEZ units, on foreign exchange payments, as 'imports' by SEZ units for the purpose of calculating NFE.

- The Export Oriented Units (EOUs) are obliged to achieve minimum value addition in its operations to avail benefits of duty free inputs, whereas there is no similar requirement for SEZ units. We recommend that the Government may consider prescribing similar value addition for SEZ units to bring them at par with the EOUs, thereby providing a level playing field.
- Annual Performance Report (APR) of the EOUs and SEZ units which are used for verifying whether the units have indeed achieved the required positive NFE, are not supported by any other documentation. We recommend that the department should institute a suitable control mechanism to get assurance on the reliability of the data furnished in APRs and ensure their timely submission.
- We identified several instances where exporters did not fulfil their obligations and other mandatory conditions for availing of benefit of duty free imports. Import duties of Rs. 82.78 crore forgone in these cases are to be recovered.
- We have also found instances of sale of branded jewellery without payment of applicable excise duty of Rs. 63.97 crore.

CHAPTER I
INTRODUCTION

1.1 Gems and Jewellery: the eternal fascination

Mankind has been captivated by gems and jewellery from time immemorial. India has given the world the Kohinoor and the Hope diamond, with their associated legends and fables. Today, gems and jewellery are a global industry with mining of gold, diamonds and platinum in Africa, Russia, Canada and Australia, polishing and jewellery manufacturing in Belgium, Netherlands, Israel, India, China and Turkey and retailing all over the world.

The industry contributes over 15 per cent of our total exports and employs 1.3 million people. It is second only to Information Technology (IT) related exports and contributes 3.75 per cent to our Gross Domestic Product (GDP). Gold jewellery represents about 80 per cent of the market and the balance comprises studded diamond and gemstone jewellery. While most of the gold jewellery manufactured in India is consumed in the domestic market, a major portion of rough, uncut diamonds produced in India is processed and exported as polished diamonds and finished diamond jewellery. India is the world's largest diamond processing (cutting and polishing) centre handling over 57 per cent of the world's rough diamonds by value.

1.2 The key players

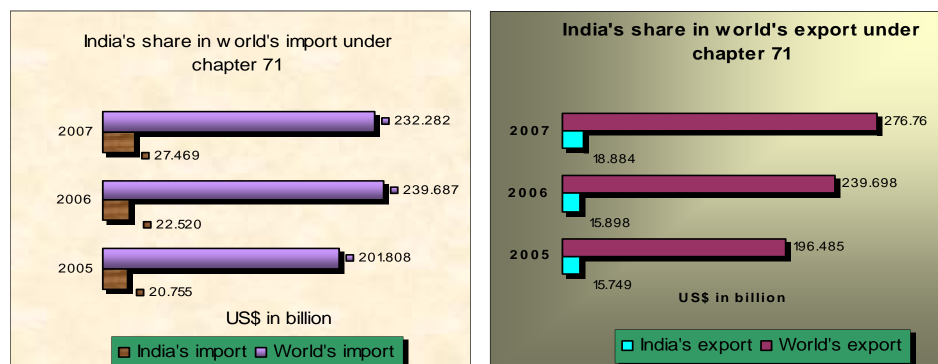
The industry is dominated by family jewellers, who constitute nearly 96 per cent of the market. Organised players such as Tata, with its Tanishq brand and Gitanjali have entered the market with branded jewellery which has a four per cent market share. The Department of Revenue under the Ministry of Finance is responsible for the tax administration of this sector. The Central Board of Excise and Customs, through its field formations spread across the country, is the main executive authority for collection of revenue. The Director General of Foreign Trade under the Ministry of Commerce implements various Export promotion schemes.

The Gems and Jewellery Export Promotion Council (GJEPC) is the apex body of the industry set-up in 1966. It is primarily involved in promoting the Indian gems and jewellery products in the international market. It also acts as trade facilitator, a nodal agency for diamond certification and organises training and research for the industry.

1.3 Major initiatives by the Government to promote the industry

This industry has been identified as a thrust sector in our Foreign Trade Policy (FTP). It falls under chapter 71 of the Customs Tariff Act, 1975 (CTA). The Government set up an Expert Committee on Gems and Jewellery in 2006 to suggest measures for making India a global hub. The committee recommended various measures for providing a competitive edge to the Indian industry which included removal of import duty on cut and polished diamonds

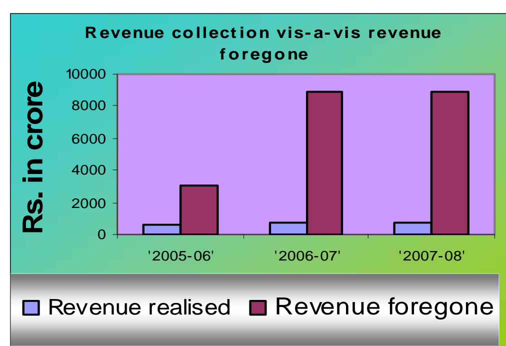
and reduction in the import duty on gold, gold items, machinery used in cutting and polishing industry etc.



In international trade under chapter 71, India's import for the period 2005-07 was US$ 70.74 billion (equivalent to Rs. 3,18,348 crore), which was ten per cent of the world import and the export share of US$ 50.53 billion (Rs. 2,27,389 crore) was seven per cent of the world export for the same period. Bulk of exports and imports are effected through a specialised customs clearance centre called the Diamond Plaza Customs Clearance Centre (DPCC), Mumbai.

With a view to doubling our percentage share of global exports within five years, the Government, in the Foreign Trade Policy (2004-09), announced (April 2004) special initiatives for the gems and jewellery sector. Import of gold of eight carats and above were allowed under replenishment scheme; duty free import of consumables for semi precious metals other than gold and platinum, commercial samples and re-import of rejected jewellery was allowed; and cutting and polishing of gems and jewellery was treated as manufacturing for the purpose of exemption under section 10A of the Income Tax Act. In the New Annual Supplement to FTP (2004-2009), duty free import of machinery, precious metals and gems was allowed. In the Union Budget for the year 2007-08, import duty on cut and polished diamonds was abolished, import duty on un-worked corals and rough synthetic stones was reduced and all industrial undertakings in the gems and jewellery sector were exempted from obtaining industrial licence for manufacture.

As a result of these exemptions which were given to bolster exports, the estimated duty foregone by the Government on goods of chapter 71 during 2005-06 to 2007-08 amounted to Rs. 68,192 crore.



We found that **the eleven commissionerates audited by us earned revenue of Rs. 2,023 crore from gems and jewellery during 2005-06 to 2007-08, while the duty foregone was Rs. 20,864 crore.** The revenue foregone increased by 191 per cent in the year 2007-08 over the year 2005-06, whereas the revenue earnings increased by only eight per cent during the same period. **Despite foregoing**

substantial revenue on imports and extending various benefits to this sector, the exports have not yet been able to catch up with the imports. While the imports grew by 16 per cent, the growth in exports was only 13 per cent during 2005-07. The details are shown in the table below: -

Table no 1.1
Growth of exports and imports

(Rupees in crore)

Year	Export	Growth% (Base year 2005-06)	Import	Growth% (Base year 2005-06)
2005-06	70209	--	91604	--
2006-07	72784	3.67	102250	11.62
2007-08	79763	13.61	106451	16.21
Total	**222756**		**300305**	

Source: Export Import data bank, Department Of Commerce and Receipt Budget 2007-08 and 2008-09,

According to a strategic report by the consulting firm KPMG on the jewellery industry, commissioned by GJEPC, India's growing importance in the global jewellery market is expected to increase in the future with total estimated jewellery sales of US$ 21 billion by the year 2010 and US$ 37 billion by the year 2015. Diamond jewellery consumption in India is also estimated to jump by 78 per cent in the year 2010. It is evident that the sector has tremendous potential for growth.

1.4 Why we chose the topic

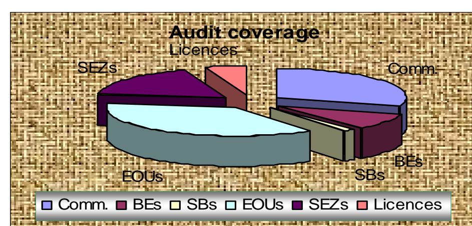
We chose the topic because the industry has a primary position in export and import activities and has tremendous potential for growth. Moreover, the Government has taken many initiatives to promote it, such as concessions, exemption, reduction of duty and has consequently foregone a large quantum of duty. We felt that all these factors made this industry a very important player in the economic activity and was suitable for a detailed study.

1.5 Audit objectives

The objectives of our audit were to ascertain whether:

- the relevant Acts, Rules and instructions issued by the Ministry of Finance/Central Board of Excise and Customs ensure proper assessment and collection of revenues,
- the internal control systems and monitoring mechanisms are effective in ensuring compliance with the provisions of the relevant Acts, rules and instructions,
- the exporter are discharging their obligation after availing of the benefits of various promotional measures and
- the export promotion schemes for this sector are being correctly administered.

1.6 Scope of audit



This performance audit was carried out in the six states of Delhi, Maharashtra, Tamil Nadu, Gujarat, Rajasthan and Karnataka, which showed highest volumes of trade for gems and jewellery. We scrutinised the records relating to imports and exports for 2005-06 to 2007-08 in 11 out of 17 commissionerates in these states. The commissionerates were selected on the basis of high volume of transactions. In these commissionerates, we selected a sample of 26,890 bills of entry (BEs), using statistical sampling technique[1], out of a total population of 1,41,527 BEs. The scrutiny of these BEs involved cross checking with 10,765 shipping bills (SBs) (total population – 4,13,494), records of 43 out of 55 Export Oriented Units (EOUs), 114 out of 292 Special Economic Zone (SEZ) units and records of 777 licences out of 3,519 licences issued under various export promotion schemes by six Regional Licensing Authorities (RLAs). In summary, a total of 19 per cent of BEs, three per cent of SBs, records of 78 per cent EOUs, 39 per cent of SEZ units and 22 per cent of licences were checked by us.

1.7 Acknowledgement

The Indian Audit and Accounts Department acknowledges the cooperation extended by the Ministry of Finance and its field formations in providing the necessary information and records during the conduct of this audit. The objectives, scope and audit methodology for the review was discussed in entry conferences held on 19 November 2008 and 7 January 2009 with Ministry of Finance and Ministry of Commerce and Industries respectively. The draft report was issued to both the ministries in December 2009. The audit findings and recommendations were discussed in an exit conference held on 15 January, 2010 with both the ministries. While the written responses to the draft review from the ministries were awaited (February 2010), the departmental responses, wherever received, have been appropriately incorporated in this report.

[1] The selection was done using the data base of import/export kept by each commissionerate. The assessees in each comissionerate were stratified on total assessable value, in a descending order. The top 25 importers were short listed. The BEs of these top 25 importers were further stratified scheme wise. From this stratified data, samples of BEs were selected using monetary unit sampling. The total number of BEs selected were restricted to one thousand per year in each commissionerate. Wherever the total number of BEs was less than 3000 in three years, the sample size for audit was kept at 50 per cent of the total transactions during three years (2005-06 to 2007-08).

CHAPTER II FINDINGS ON RULES, REGULATIONS AND SYSTEMS

2.1 In this chapter we have included audit findings and recommendations on system issues viz. inadequacies in the Acts/rules/notifications issued by the Government for export/import of products as well as the internal control mechanism, which adversely affect the collection of revenue. To highlight the issues, certain illustrative cases have been included.

2.2 Database of imported and exported goods

The Directorate General of Valuation (DGOV), Mumbai was established in the year 1997 to assist the Board in policy maters concerning valuation. To carry out this task, the DGOV had to develop a comprehensive real time electronic database of imported and exported goods which would fulfil the following objectives:-.

- The assessing officers would have instant access to the data to check for cases of undervaluation/overvaluation;
- Check abuse of export incentive schemes and valuation frauds;
- Monitor sensitive commodities which were prone to undervaluation;
- Maintain a central registry of special valuation (SVB) cases;
- Provide assistance to the Board for fixation of tariff value and transfer pricing;
- Monitoring of valuation risk component of risk management system (RMS) under Indian Customs Data Interchange System (ICES);
- Generating valuation alerts, publishing valuation bulletins and resolving valuation disputes.

The Expert Committee on Gems and Jewellery had expressed concern over the absence of reliable turnover statistics in this sector and had opined that the domestic trade was grossly under-estimated to avoid both sales tax and income tax and had recommended sharing of the trading data with other tax authorities to detect instances of tax evasion.

Given the multiple uses of the database, completeness of data was a prerequisite for doing any reliable analysis. We found that the import/export data was incomplete and could not be used as the base data for any realistic analysis. The value of imports and exports for the total transactions captured in the DGOV database for the customs tariff heading 71 was way below the actual trade figures reported by the Ministry of Commerce and Industries on the DGFT website. The figures are given in the table overleaf:-

Table no 2.1
Comparison of import/export figures

(Rupees in crore)

Year	DGOV data		DGFT data	
	Value of imports	Value of exports	Value of imports	Value of exports
2005-06	42,462	391	91,604	70,209
2006-07	53,689	189	1,02,250	72,784
2007-08	52,768	70	1,06,451	79,763

To examine the issue further, we took the data available on the DGOV database in respect of the commissionerates of Ahmedabad, Kandla and Bangalore; Air Cargo Complex, Jaipur; New Customs House (NCH), Delhi; Inland Container Depots (ICDs), Tughlakabad (TKD) and Patpadganj (PPG) and compared it with the data maintained by the respective commissionerates. There were substantial variations, as depicted below: -

Table no 2.2
Comparison of figures of DGOV and commissionerates

Year	Commissionerate and other offices	As per DGOV data		As per commissionerate data	
		No. of BEs	No. of SBs	No. of BEs	No. of SBs
2005-06	Bangalore	833	52	1,101	656
	NCH, Delhi	1,209	10	350	22,490
	ICD , TKD	32	1	108	22
	ICD, PPG	41	5	52	299
	Ahmedabad & Kandla	699	Nil	4,754	1,280
2006-07	ACC, Jaipur	3,481	Nil	4,695	19,130
	Bangalore	1,063	30	1,123	746
	NCH, Delhi	800	70	350	17,766
	ICD , TKD	61	2	794	27
	ICD, PPG	30	1	133	566
	Ahmedabad & Kandla	594	Nil	5,301	1,294
2007-08	ACC, Jaipur	2,477	Nil	5,472	21,288
	Bangalore	991	10	1,164	837
	NCH, Delhi	560	37	367	19,469
	ICD , TKD	133	Nil	834	31
	ICD, PPG	46	10	40	547
	Ahmedabad & Kandla	561	1	11,420	1,496
	Total	**13,611**	**229**	**38,058**	**1,07,944**

We observed that only 35 per cent of BEs and less than one per cent of SBs had been entered in the DGOV database. While the import data was incomplete, in the case of exports, virtually no data had been captured in the database.

The Diamond Plaza Customs Clearance Centre (DPCC) under the Commissioner of Customs, Sahar Airport, Mumbai had imported and exported goods worth Rs. 1,18,162 crore and Rs. 1,71,937 crore respectively in three years which were 36 per cent to 43 per cent of the imports and 74 per cent to 80 per cent of the exports of the entire country under chapter 71. However, the import and export data pertaining to the DPCC was not being entered in the database of DGOV.

We concluded that it was not possible to use the DGOV data for any meaningful analysis as only a small portion of the total data was being captured. Therefore, none of the objectives for setting up the DGOV database were achieved.

Recommendation No. 1

- *We recommend that the database of international trade should be kept updated, especially with the DPCC data, so that it can be utilised for the various purposes for which it has been created. This can also enable sharing of data with other tax authorities for detection of cases of duty evasion.*

2.3 Implementation of ICES in DPCC

The DPCC was set up in 1985 to facilitate expeditious clearance of consignments for import and export of diamonds, gems and jewellery. The bulk of imports and exports of the country are handled by the DPCC.

Indian Customs Electronic Data Interchange System (ICES) captures details of imports and exports in all commissisonerates. It was introduced to speed up assessments, improve transparency and to act as a repository of data. We noticed that although the DPCC had a dedicated server, the entire data relating to customs clearance of exports and imports was being kept manually. Therefore, the information relating to the bulk of the total trade for these articles was not captured in the ICES.

Consequently, the transactions at DPCC are escaping the scrutiny of the Risk Management System and Post Compliance Audit introduced by the department for examination of the high risk cargo. In our opinion, this omission of DPCC data has increased the risk of tax evasion and other un-lawful activities which where sought to be reduced by the introduction of ICES. Thus, the data in two major IT systems, ICES and DGOV database is largely incomplete primarily because DPCC has not implemented these systems.

On the matter being pointed out (July 2009), the department stated (August 2009) that the ICES could not be implemented in DPCC as it was being shifted to a new location and some changes were required in the existing software. In addition, the traders were opposed to the implementation as they felt that it would result in delays in clearance of goods, leakage of information about their imports and they would have to pay fees for the data entry at service centres.

The reply is not tenable. Due to the non-implementation of ICES at DPCC, bulk of the imports and exports of the entire country have been excluded from the ICES which defeats the very objective of the system. Issues like additional cost, confidentiality etc. have been adequately addressed in the ICES for safeguarding the interest of the importers. Moreover, the traders' data is being captured in other commissionerates and there is no justification for giving special status to the traders at DPCC and keeping their information out of the ICES.

Recommendation No. 2

- *We recommend that the department must implement the ICES in DPCC to mitigate the risk of undervaluation and overvaluation of these sensitive commodities.*

2.4 Physical examination of consignments

According to circular no. 9/2006-07 dated 1 July 2006, issued by the Reserve Bank of India (RBI), customs authorities are required to examine and certify the value of the goods exported in the guaranteed remittance (GR) form to be submitted by the exporters to their respective banks.

The Board has not fixed any norms for physical examination of goods during import or export by a SEZ unit, to adhere to the RBI requirement. We found that 10,010 consignments of total FOB value of Rs. 198.30 crore were cleared for export from SEZ Surat, during the period 2005-06 to 2007-08, without any physical examination.

On the matter being pointed (November 2008 and April 2009), Deputy Commissioner of Customs, SEZ, Surat replied (March 2009) that as per SEZ Rules 2006, export of SEZ unit need not be examined and export is on the basis of self certification.

Similarly, four SEZ units, engaged in trading activity under MSEZ, Chennai imported diamonds valued at Rs. 985.65 crore during the period 2005-06 to 2008-09. These were assessed on the basis of supplier's invoice alone.

In our opinion, the absence of any form of physical examination implies that there is no check on the risk of undervaluation/overvaluation of goods in imports/exports. The requirements of RBI are also not being fulfilled.

Recommendation No. 3

- *We recommend prescription of norms for physical examination of goods cleared by the SEZ units adhering to the RBI requirements and to prevent any loss of revenue.*

2.5 Duty rates for 'Gold coins' and 'Gold in any form'

Notification no. 62/2004-cus dated 12 May 2004 provides that the expression 'gold in any form' or 'silver in any form' shall include medallions and coins, but shall not include foreign currency coins. The notification also provides that customs duty is leviable on 'gold coins' at the rate of Rs. 100 per 10 gm (Sl. no. 1) and on 'gold in any form' at the rate of Rs. 250 per 10 gm (Sl. no. 2).

The notification is ambiguous because it gives a lower rate of duty for gold coins in comparison to 'gold in any form' whereas it also provides that gold coins are included in the term 'gold in any form'.

We found that 16,904.85 kg of gold coins with assessable value of Rs. 888.80 crore were imported through customs commissionerates at ACC, Chennai, ACC, Coimbatore, NCH Delhi, ACC, Bangalore and ACC, Mumbai, in 270 consignments, between April 2005 and November 2008 and were assessed at the rate of Rs. 100 per 10 gm. Had the duty been collected at the higher rate of Rs. 250 per 10 gm, Rs. 36.14 crore of additional revenue would have been generated.

On the matter being pointed out (July 2006, January and February 2009), customs commissionerate at Coimbatore issued (October 2006 to September 2008) SCNs for an amount of Rs. 1.67 crore but stated (November 2006 and April 2009) that duty concession was allowed correctly in terms of Sl. no. 1 of the notification read with Board's circular no. 40/2004 dated 4 June 2004,. The Supreme Court had held that when a notification contained two different rates for specific commodity, only beneficial rate would be extended and as per principles of classification, specific entry would be preferred to residuary entry for the purpose of levy of duty.

The reply underlines the ambiguity in the notification. If it had clarity, the interpretation would be self evident and it would not be necessary to resort to Supreme Court decisions and principles of classification to decide on the rate of duty.

Recommendation No. 4

- *We recommend that the ambiguity in the notification may be clarified so that 'gold coins' can be classified as a unique item subjected to a specified rate of duty.*

2.6 Procurement from domestic tariff area on payment of foreign exchange

According to Rule 53 of the SEZ Rules 2006, the units in SEZ have to achieve a positive net foreign exchange (NFE) over a period of five years from the commencement of production. The NFE is calculated by subtracting the total CIF value of imports from the total FOB value of exports by the units. The rule also specifies that one of the components of the export earnings is the value of goods sold to DTA against payment in foreign exchange.

In our opinion, if goods sold to DTA are included under exports, then the goods procured from DTA by paying foreign exchange should also be included under imports to give a realistic picture of NFE. We found that there is no such provision in the rules and, therefore, the NFE gets grossly overstated. There is also a probability that a positive NFE could actually turn to negative if DTA purchases are included in imports.

Our contention is further supported by the provision that the sale of goods by DTA units to SEZ units are treated as 'deemed exports'[2] for the former, who become eligible for matching duty free imports under the exemption remission schemes of FTP. By the same analogy, procurement from DTA by EOU/SEZ unit should also be considered as 'deemed imports' for the SEZ unit.

Two cases of overstated NFE in Mumbai SEZ are illustrated below:

M/s Jewelex International Pvt. Ltd. had total export and import of Rs. 228.44 crore and Rs.166.84 crore respectively during 2006-08 and achieved a positive

[2] According to chapter 8 of FTP 2004-2009, 'deemed exports' refers to the transaction in which goods supplied do not leave the country and payment for such supplies is received either in Indian rupees or in free foreign exchange

NFE of Rs. 61.60 crore. However, if the DTA procurement of Rs. 51.01 crore is considered as imports, the NFE works out to only Rs. 10.59 crore.

Similarly, M/s Goldiam Jewels Ltd. had a positive NFE of Rs. 6.08 crore which reduces to only rupees one crore if DTA procurement of raw material amounting to Rs. 5.08 crore is considered as imports.

Recommendation No. 5

- *We recommend that the Government should introduce a provision in the SEZ rules to consider sales by DTA units to SEZ units, on foreign exchange payments, as 'imports' by SEZ units for the purpose of calculating NFE.*

2.7 Minimum value addition prescribed for EOUs but not for SEZ units

According to paragraph 4A.2.1 of HBP, Volume-I (2004-09), an exporter of gold/platinum/silver jewellery has to achieve prescribed minimum value addition to get benefit of various schemes for exemption/remission scheme of duty. An EOU also has to achieve similar value addition.

We observed that a similar provision has not been included in SEZ Rules 2006 and FTP. Consequently, SEZ units have an undue advantage over EOU and DTA units. We found that nine SEZ units out of the 47 EOU/SEZ units audited by us under SEZ, Chennai, Cochin and Mumbai had exported without minimum value addition. They had availed of duty exemption of Rs. 89.58 lakh on imports. Had these exports been made by EOUs, they would have had to pay duty of Rs. 89.58 lakh for not achieving the prescribed value addition.

It is evident that while the units under SEZ scheme and EOUs are both involved in export oriented activity and enjoy similar benefits of duty free inputs, the absence of value addition norms for SEZ units gives them an unfair advantage over EOUs.

Recommendation No. 6

- *We recommend that the Government may consider introducing a suitable provision in the SEZ rules to prescribe a minimum value addition by the SEZ units to bring them at par with the EOUs, thereby providing a level playing field.*

2.8 Annual performance reports of exporters

According to rule 22 of SEZ Rules 2006, every unit in a SEZ has to maintain proper accounts and furnish Annual Performance Report (APR) in the prescribed format to the Development Commissioner (DC) of the SEZ duly certified by a chartered accountant (CA). There is a similar provision for EOUs in HBP, Volume I (2004-09).

The EOU/SEZ schemes rely mainly on self-certification and the rules do not require the APRs to be supported by other statutory documents like annual accounts, customs records, income tax (IT)

returns, bank realisation certificates (BRC) etc. We correlated the data furnished by the units in their certified APRs, with data available in the stock register, sale register and customs records, etc. and found discrepancies in ten units (two EOUs and eight SEZ units) under Noida SEZ and Cochin SEZ. Two EOUs under Noida and Cochin SEZ had reported inflated FOB value of exports, one SEZ unit in Noida had under reported CIF value of imports and inflated the exports and seven SEZ units under Noida had delayed submission of APRs ranging between 21 days and two years.

The APR data forms the basis for verifying whether the units have indeed achieved the required positive NFE and also as a monitoring mechanism to ensure that the units are functioning within the ambit of the applicable rules. Thus, the discrepancies in the data can distort the NFE and delays in submission of APR weakens the monitoring mechanism.

Some illustrative cases are given below:

(i) M/s Agra Products Pvt. Ltd, an SEZ unit in Noida SEZ had shown import of capital goods during the year 2007-08 as Rs. 81.22 lakh and cumulative import of capital goods as Rs. 2.61 crore in its certified APR. We found from the stock registers that the unit had actually imported capital goods of Rs. 1.21 crore in the year 2007-08 and cumulative import was Rs. 5.44 crore. Further, as against the value of exports amounting to Rs. 25.70 crore shown in APR for the year 2006-07, the actual export as per sales ledger was Rs. 25.19 crore. This has resulted in inflation of cumulative NFE by Rs. 3.34 crore.

(ii) M/s Vaibhav Gems, an EOU under Noida SEZ, had shown export of value of Rs. 236.72 crore in the APR submitted for the year 2006-07. We found from the accounts of the unit that actual export was Rs. 236.15 crore. Thus, the unit overstated the value of exports by Rs. 57.66 lakh in their APR submitted to the DC, Noida SEZ. This has resulted in inflation of NFE by Rs. 57.66 lakh.

Recommendation No. 7

- *We recommend that the department should institute a suitable control mechanism to get assurance on the reliability of the data furnished in APRs and ensure their timely submission.*

CHAPTER III
OBLIGATION OF EXPORTERS FOR AVAILING OF BENEFITS OF PROMOTIONAL MEASURES

3.1 In this and the subsequent chapters we have discussed compliance issues and their impact i.e. cases of non-compliance with the applicable Acts/rules/notifications/procedures by the executive authorities/traders.

3.2 The Government has introduced many promotional measures to increase our exports and enhance the foreign exchange earnings. The exporters are permitted to import items without paying duty or by paying reduced rates of duty. In return, they have to discharge certain obligations. Our observations in this chapter relate to cases where the exporters did not fulfil these obligations although they had imported duty free goods. Import duty is recoverable in these cases and these areas require close monitoring to ensure that importers honour their end of the bargain.

We must also remember that wherever an exporter imports duty free goods in excess of his entitlement, it gains an unfair advantage over the manufacturers who operate in the domestic market and pay duty on all imports.

3.3 Export obligation

3.3.1 In terms of paragraph 5.1 of FTP (2004-09) (as on 1 April 2005), an EPCG licence holder has to export goods which are equal to eight times the amount of duty saved on the import of capital goods. This is known as Export Obligation (EO). In case of small scale industrial (SSI) units, the EO is six times the amount of duty saved, provided the landed CIF value of imported capital goods does not exceed Rs. 25 lakh (Rs. 50 lakh w.e.f. 1 April 2008) and total investment in plant and machinery does not exceed the investment limit for SSI.

We found that the RLA at Surat had issued 150 EPCG licences with three per cent duty to 34 exporters who got total duty exemption of Rs. 12.83 crore. The three per cent duty rate was admissible to SSIs but the department was unable to show any records to confirm the SSI status of the exporters. The quantum of duty saved in these cases ranged from Rs. 2.63 lakh to Rs. 1.43 crore. We used the figures of the duty saved to do reverse calculation and ascertain the probable value of the goods imported by these licencees. For the calculations, we used the effective rate of duty for 2005-06 to 2007-08 on goods under Chapter 84 which was five to ten per cent. We found that the value of the capital goods imported worked out between Rs. 52 lakh and Rs. 71.59 crore, which exceeded the SSI limit of Rs. 50 lakh. Therefore, these units did not qualify as SSI and should have discharged EO of eight times, instead of six times, the duty saved. Consequently, the EO discharged was lower than the minimum obligation by Rs. 23.98 crore. The department should verify the SSI status and refix the EO where necessary and intimate us accordingly.

3.3.2 Paragraph 4.78.1 of HBP, Volume-I (as on 1 September 2004) provides that an EOU having an advance licence has to fulfil the EO stipulated in the licence, within 120 days from the date of first import. He has to submit proof to the RLA within two months of completing the exports.

We scrutinised the records of the licensing authorities at Ahmedabad, Jaipur and DC, Cochin SEZ and found that three licencees (Ahmedabad - two, Chennai-one and Jaipur-one) and two EOUs under the Cochin SEZ had failed to achieve the prescribed export obligation. Accordingly, duty of Rs. 3.54 crore (determined in proportion of the shortfall in achieving export obligation) was recoverable from these units.

One case is illustrated below:

Five advance licences were issued (November 2004 to March 2005) to M/s Hinduja Export Pvt. Ltd. and M/s Intercontinental by the RLA at Ahmedabad for duty free import of gold bars with CIF value of US$ 59.45 million (total weight 3,523.88 kg) and export of gold jewellery with FOB value of Rs. 236.56 crore (total weight 3,688.736 kg).

The licencees completed the imports during the period December 2004 to February 2005. They neither submitted the export documents within the time limit nor sought any extension. The RLA also did not initiate any penal action under the Foreign Trade (Development and Regulation) Act, 1992. The total duty of Rs. 3.52 crore foregone on the import of duty free gold bars was recoverable.

On the matter being pointed out, RLA replied (September 2008) that necessary action would be taken for recovery of customs duty.

3.3.3 As per paragraph 5.4 of FTP (2004-09) (as on 1 April 2005), EO under the EPCG scheme is to be fulfilled by the export of goods capable of being manufactured by the use of the capital goods imported under the scheme. This EO is over and above the average level of exports achieved by the exporter in the preceding three years for the same and similar products. HBP, Volume-I (2004-2009), provides that in case the exporter has supporting manufacturers, the capital goods may be installed at their premises provided their names and addresses are endorsed on the EPCG licence. The name of the supporting manufacturer should also be endorsed in the shipping bill for reckoning the exports towards the discharge of EO.

M/s. Surana Industries Ltd., Chennai, an exporter under RLA, Chennai, imported (between November 2005 and August 2007) eight wind turbine generators and accessories valued Rs. 25.59 crore. The matching EO was Rs. 21.41 crore. The licencee availed of duty exemption of Rs. 2.67 crore on the imports and exported gold medallions worth Rs. 21.78 crore through four shipments (February and March 2007). The exported items were manufactured by a supporting manufacturer. The licence was redeemed on 4 August 2008 by the RLA.

Our scrutiny revealed the following:

(a) The EO was Rs. 21.41 crore over and above Rs. 44.16 crore which was the annual average exports of the past three years, as per CA certificate dated 12 January 2008. Therefore, the total export of Rs. 21.78 crore in 2006-07 was substantially lower than the EO.

(b) M/s Surana Industries Limited, SIPCOT Industrial Complex, Gummidipoond, Chennai was mentioned as the supporting manufacturer in the EPCG licence. However, the wind turbine generators were installed at Tirunelveli although no amendment was made in the licence by the RLA for change of place of installation. Therefore, the installation of capital goods was irregular.

(c) Verification of export documents revealed that the supporting manufacturer's name was not endorsed on the shipping bills. Thus, EO reckoned for redemption of the licence was irregular.

In view of these irregularities, the duty exemption of Rs. 2.67 crore availed of by the licencee was recoverable along with interest of Rs. 1.34 crore.

3.4 Obligation to achieve value addition

In terms of paragraph 4.56 of HBP, Volume-I (as on 1 September 2004), value addition (VA) of 15 per cent in case of studded gold/ silver jewellery and seven per cent in case of plain gold/silver jewellery is essential for getting duty exemption/remission.
Paragraph 4.4.17 of FTP 2004-2009 (as on 1 September 2004) provides that public/private bonded warehouses may be set up in SEZ/DTA for import and re-export of cut and polished diamonds, subject to achievement of minimum value addition of five per cent.

We found that the prescribed percentages of value addition could not be achieved by five SEZ units, six EOUs and 11 licencees of exemption schemes operating under the RLAs at Ahmedabad and Bangalore; Development Commissioners (DC) at Chennai, Noida, Mumbai; and customs commissionerate at ACC, Jaipur. This resulted in grant of ineligible duty concession of Rs. 4.24 crore which is recoverable from the licencees/EOU/SEZ units.

A few illustrative cases are given below:

(i) RLA Ahmedabad issued (December 2004 to February 2006) eight advance authorisations to M/s Intercontinental (India) and M/s Adani Export Ltd. for import of gold bar, which were to be used for export of studded gold jewellery. The licencees imported 4,138 kg of gold bars and exported studded gold jewellery through 41 consignments during the period 2004-05 and 2005-06.

We observed that the licencees had done value addition ranging from 1.59 per cent to 3.17 per cent instead of the prescribed 15 per cent. The duty concession of Rs. 39.24 lakh is recoverable.

On the cases being pointed out (August 2008 and April 2009), RLA Ahmedabad agreed (August 2008) to take action in one case and stated (July 2009) that in the remaining cases the goods exported were medallions and coins and not studded jewellery. Reply of the RLA was not in consonance with the export obligation discharge certificates issued by him, which were available in the concerned case files and clearly mentioned that the goods exported were studded gold jewellery and not coins and medallions.

(ii) Four SEZ units falling under the jurisdiction of DC, MSEZ, Chennai imported 25,90,622.86 carats of cut and polished diamonds valued at Rs. 988.43 crore during the period 2004-05 to 2008-09. They exported processed goods valued at Rs. 1,041.71 crore. The exports included 36 consignments during the period August 2004 to March 2007 where the value addition was below the prescribed five per cent. Consequently, the duty concession of Rs. 3.50 crore on the imports used for these consignments was recoverable.

(iii) In another case of similar nature, RLA, Bangalore issued (October 2005 to October 2006) six DFRC licences to M/s Rajesh Exports for import of gold which was to be used for exporting gold jewellery. We observed that the licencee exported both plain and studded jewellery but value addition norm was uniformly applied at seven per cent. Since the norm of 15 per cent was not applied for studded jewellery, excess import entitlement of Rs. 1.74 crore was allowed. Against this, the licencee actually imported duty free gold worth Rs. 77.04 lakh on which duty of Rs. 6.61 lakh was foregone, which is recoverable.

3.5 Obligations in Letters of Permission and Letters of Approval

In terms of paragraphs 6.6 of FTP (2004-09) and rule 19 of the SEZ Rules 2006, the DC/designated officer authorises the setting up of an EOU through a letter of permission (LOP) and setting up of an unit in the SEZ through a letter of approval (LOA). Thereafter, the authorized unit executes a legal undertaking (LUT) with the DC concerned.

Our scrutiny of the records of the DCs at SEZ, Noida, Mumbai and Chennai revealed that three EOUs and four SEZ units had not fulfilled the terms and conditions of their LOP/LOA. Total duty of Rs. 7.41 crore is recoverable in addition to penal action under Foreign Trade (Development and Regulation), Act 1992.

Two cases are illustrated below:-

(i) M/s Agra Products Pvt. Ltd., a unit in SEZ, Noida was issued LOA (18 March 2002) for manufacture and export of gold/silver and imitation jewellery. As per the LOA, the unit was authorised to import capital goods with CIF value of Rs. 90 lakh which was subsequently amended (6 May 2005) to Rs. 2.50 crore. The limit was further increased to rupees three crore w.e.f. 1 August 2008.

Scrutiny of the stock register of the unit revealed that it imported capital goods worth Rs. 5.46 crore upto 2008-09, which exceeded the sanctioned limit by

Rs. 2.46 crore. Duty of Rs. 71.34 lakh foregone on the excess import of capital goods is recoverable and penal action can also be initiated.

On the matter being pointed out (July 2009), the department replied (July 2009) that requirement of capital goods was subject to enhancement/reduction as the unit is not bound to import the exact quantity as mentioned in the LOA.

The reply is not tenable because in this case the excess is very large. If the department can accept an excess import of 82 per cent, then, in our opinion, the LOA becomes a redundant document.

(ii) M/s Hope (India) Polishing, an EOU under SEZ, Mumbai was granted a LOP to import rough diamonds and thereafter manufacture and export cut and polished diamonds and it executed a LUT with DC.

Our scrutiny revealed that the unit imported cut and polished diamonds valued at Rs. 20 crore during 2005-06 to 2007-08 which were not authorised items of import as per LOP/LUT. The unit was, therefore, liable to pay duty of Rs. one crore on the import of cut and polished diamonds.

On the matter being pointed out (September 2008), the department issued (October 2009) a demand notice for the recovery of customs duty.

3.6 Obligations on the use of imported capital goods

In terms of paragraph 5.3.2 of HBP, Volume-I (2004-2009), an importer of duty free capital goods must obtain a certificate of installation and usage from the central excise authorities or an independent chartered engineer and submit to the licensing authority within six months from the date of import.

RLAs at Surat and Jaipur issued 406 EPCG licences to exporters of ‘gems and jewellery’ during the period 2004-05 to 2008-09 and duty of Rs. 28.13 crore was foregone.

Our scrutiny revealed that the requisite installation certificates for the capital goods were not furnished by the importers. Therefore, the department was required to recover the differential duty from the importers.

One case is illustrated below:

M/s Om Royal Jewellery (India) Pvt. Ltd., under the RLA, Jaipur, was issued an EPCG licence in December 2004 for import of capital goods valued at Rs. 32.71 lakh at concessional rate of duty. The licencee imported machinery worth Rs. 26.30 lakh in November 2005 and availed of duty exemption of Rs. 7.79 lakh. The licence was redeemed after export of gems and jewellery during February and March 2007. We found that the importer had not produced the required installation certificate within six months of import. The duty exemption of Rs. 7.79 lakh is recoverable.

CHAPTER IV
IMPLEMENTATION OF THE EXPORT PROMOTION SCHEMES

Since the Government is foregoing substantial amounts of duty under the export promotion schemes, it has to ensure that various conditions prescribed in the schemes are fulfilled, else import duties exempted have to be recovered. As already mentioned in the last chapter, this is also necessary to protect the interest of manufacturers operating in the domestic market and paying duty on all imports.

4.1 Limits on sub-contracted work

According to paragraph 6.14 of FTP 2004-09, EOUs can sub-contract to DTA, upto 50 per cent of the overall production of the previous year in value terms. Similarly, SEZ Rules 2006 provide that SEZ units can sub-contract upto 100 per cent of their production in the previous year to a unit in the DTA/SEZ/EOU. In both cases, permission is accorded by the customs authorities.

Our scrutiny of the records of 61 SEZ units and 18 EOUs under customs commissionerates at Chennai, NCH, Delhi and Ahmedabad revealed that during the period 2004-05 to 2008-09, four SEZ units and one EOU unit sub-contracted production to DTA units in excess of permissible limits. Duty foregone on the input materials utilised in the excess production worked out to Rs. 1.05 crore and is recoverable.

One case is illustrated below:

Customs House, Chennai permitted (valid upto April 2008) M/s Abhilasha Jewellers Pvt. Ltd., an EOU, to transfer upto 500 kg of gold bars annually from the bonded warehouse to M/s Prakash Gold Palace Pvt. Ltd., Kolkata, for conversion into gold jewellery. The unit sub-contracted for 689 kg of gold bars during the period 2007-08 which was in excess of the permission granted. It also exceeded the limit of 50 per cent of overall production of previous year by Rs. 14.38 crore. The duty concession of Rs. 19.47 lakh is recoverable along with interest.

On the matter being pointed out (January & February 2009) DC, MSEZ, Chennai replied (April 2009) that the permission for job work was amended in April 2008, enhancing the quantity of job work from 500 kg to 1,000 kg and the amendment was valid for 2007-08 also. The reply is not tenable as the amendment dated 1 April 2008 did not mention that it had retrospective effect. Hence, it was applicable only from the date of issue i.e. 1 April 2008.

4.2 Grant of replenishment licences

In terms of paragraph 4A.28 of HBP, Volume-I (2004-2009), a replenishment licence is issued for the free import of gold, platinum, related consumables, tools, machinery and equipment at the rate of one and two per cent of FOB value of exports of the preceding year. Exports of cut and polished diamonds were made eligible for this licence w.e.f. 4 April 2008.

Our scrutiny revealed that RLA, Surat issued five replenishment licences of cut and polished diamonds, during the year 2006-07, to M/s Ghaveriya Exports and four others for CIF value of Rs. 23.96 crore. As export of cut and polished diamond had not become eligible in 2006-07, the issue of these replenishment licences was irregular. The relevant import duty has to be recovered from the exporters.

RLA, Surat replied (June 2009) that excess CIF value of Rs. 19.13 lakh was adjusted in one case. Reply in the remaining cases is awaited (January 2010).

4.3 Imposition of late-cut

Paragraph 4.34 of HBP, Volume-1 (2004-2009), provides that application for 'duty free replenishment certificate (DFRC)' should be filed within six months from the date of realisation in respect of all shipments or supplies for which DFRC is being claimed. Any application received within another six months from the last date for submission may be considered after imposing a 'late cut' at the rate of ten per cent on the entitlement.

(i) We noticed that six DFRC licences were issued to M/s Triveni Gems 'N' Jewellery and five other exporters at Jaipur and Bangalore without imposing the applicable late cut of ten per cent though the applications were filed after the stipulated period. The omission resulted in grant of excess credit of Rs. 28.77 lakh, which needs to be adjusted.

(ii) Similarly, RLA Jaipur issued two DFRC licences to M/s Triveni Gems 'N' Jewellery and one other exporter for which the applications were filed after the expiry of 12 months from the last date of submission. The irregular DFRC licences granted inadmissible credit of Rs. 13.07 lakh, which needs to be adjusted.

4.4 Re-export to foreign supplier

Paragraph 4A.15 of HBP, Volume-I (2004-09), provides that in cases where an exporter receives duty free gold from a foreign supplier, converts to jewellery and exports to the same supplier, the exports should be completed within 90 days to qualify for duty exemption on the import. In cases of delay, customs duty would be recovered.

M/s Abhilasha Jewellers Pvt. Ltd., an EOU under DC, MSEZ, Chennai, imported (September 2007) 24 kg of gold bars from M/s Al Haseema Jewellers LLC., Dubai and availed of duty exemption of Rs. 2.50 lakh. It

exported (January 2008) 26.653 kg gold jewellery for FOB value of Rs. 2.54 crore. As the exports were made beyond the prescribed time limit of 90 days after import, duty concession of Rs. 2.50 lakh was recoverable.

4.5 Re-import after exhibition abroad

Gems and jewellery items taken for overseas exhibition and re-imported within 60 days from the close of exhibition are exempt from levy of basic customs duty and additional duty of customs.

Our scrutiny of the records of Air Cargo Complex, Jaipur, revealed that in seven cases, exporters re-imported gems and jewellery items with assessable value of Rs. 3.88 crore. Since the re-imports were made beyond 60 days from the dates of closure of the exhibitions, they availed of incorrect exemption of Rs 51.67 lakh which is recoverable.

4.6 Authorised export product

According to rule 34 read with rule 25 of the SEZ Rules 2006, the duty free goods admitted into a SEZ should be used for carrying out the authorised export related operations. If the goods are utilised for other purposes, duty would be charged on such goods.

M/s Chennai Chains (P) Ltd., a SEZ unit in MSEZ, Chennai was authorised (March 2003) to import rough 'agate stones' and manufacture and export 'cameos'.

Our scrutiny revealed that the unit imported 'agate stones' valued at Rs. 73.87 lakh. It manufactured and exported 'agate stone not cut to shape' during 2002-03 to 2007-08 which was not the authorised product for export. The duty foregone of Rs. 30.76 lakh is recoverable alongwith interest.

4.7 Jewellery imported for 'repair'

As per notification no. 52/2003-cus dated 31 March 2003, old jewellery imported for repair and remaking are exempt from levy of customs duty.

M/s Vaibhav Gems Ltd., Jaipur, an EOU, imported gold and platinum jewellery studded with precious and semi-precious stones with assessable value of Rs. 5.79 crore through ACC, Jaipur during the period February to April 2007. The bills of entry carried a detailed description of the jewellery but did not describe them as 'old'. There was no evidence in the case file to show that the jewellery was old. Therefore, the duty exemption of Rs. 67.47 lakh was unsupported by documents and recoverable.

4.8 Grant of duty free import

Under the FTP 2004-09, an exporter is allowed duty free import of inputs which are required for production of export products. We found that RLAs at Jaipur, Ahmedabad, Chennai, Bangalore and Mumbai SEZ had granted excess duty free import entitlement of Rs. 4.13 crore to exporters.

Some cases are illustrated below:

4.8.1 According to paragraph 4A.2 of HBP, Volume I (as on 1 April 2007), wastage of 4.5 percent in manufacture of plain silver jewellery is allowed.

Three DFIAs were issued (November 2007 to January 2008) to M/s Artistic Jewellery and M/s Alpana Gems by RLA at Jaipur for import of 5,315 kg of silver having 0.999 fineness[3].

We observed that the units exported 5,500 kg plain jewellery of 0.925 fineness. After considering the permissible wastage of 4.5 per cent, the licencees were eligible for import of 4,917 kg of silver of 0.999 fineness. This resulted in excess import authorisation of 398 kg silver of 0.999 fineness involving excess CIF value of Rs. 75.26 lakh. Therefore, the duty of Rs. 2.05 lakh on excess import of 398 kg of silver is recoverable from the licencees.

4.8.2 As per paragraph 4A.31 of HBP Volume-I (2004-09) duty free import of samples upto rupees three lakh is allowed for gems and jewellery sector.

M/s Vijay Dimon Diamond (I) Pvt. Ltd., a SEZ unit under jurisdiction of DC, SEZ Mumbai, imported samples worth Rs. 2.39 crore during the period 2005-06 to 2007-08, which was in excess of Rs. 9 lakh allowable by Rs. 2.30 crore. Thus, customs duty of Rs. 31.27 lakh is recoverable on excess import of samples.

Similarly, in another four cases, excess import entitlement of Rs. 1.09 crore to four exporters was noticed at RLA Jaipur, Chennai and Bangalore. In two other cases under RLA, Ahmedabad and Jaipur, excess import entitlement of 8,29,774.76 kg of silver and 31.19 kg of gold were allowed to four licencees. The value of the excess entitlement could not be determined in these two cases due to the absence of supporting documents.

4.9 Short levy of customs duty due to incorrect classification

In terms of section 2 of Customs Tariff Act, 1975, the rates of customs duties on imported goods are specified in the first schedule. Different rates of duties are prescribed for different commodities/group of commodities mentioned in the schedule. As per general rule 4 for interpretation of the first schedule, goods which cannot be classified based on essential character, specific description etc., are to be classified under the heading appropriate to the goods to which they are most similar.

We found a few cases of incorrect classification of goods, resulting in short levy of customs duty of Rs. 38.45 lakh which are discussed below.

(i) M/s Goldquest International Pvt. Ltd. imported 22 consignments of ‘silver medallions plated with gold’ through ACC, Chennai commissionerate, during the period May 2005 to May 2007. They had assessable value of Rs. 2.76

[3] Quantity of pure silver=Quantity of silver x fineness

crore and were classified under chapter heading 7118 as 'coins' and assessed at a concessional rate of duty under notification no. 62/2004-cus dated 12 May 2004.

We observed that the notification no. 62/2004-cus was applicable only to pure silver in any form including medallions and coins and not to silver plated with gold, which is appropriately classifiable under chapter heading 7106 which covers silver (including silver plated with gold or platinum), unwrought or in semi-manufactured forms or in powder form. Thus, this incorrect classification resulted in short levy of duty of Rs. 32.51 lakh, which is recoverable.

(ii) M/s N. K. Patel & Sons imported 32 consignments of gold and platinum for dental use, with assessable value of Rs. 58.22 lakh, through the commissionerate at ACC, Mumbai, during the period October 2005 to March 2008.

Our scrutiny revealed that the goods were classified under chapter 71 in contravention of note 3(b) of the first schedule, which specifies that dental fillings or other goods of chapter 30 are not classifiable under chapter 71. This resulted in short levy of customs duty of Rs. 5.5 lakh, which is recoverable.

4.10 Miscellaneous cases

In eight other cases, 36 units imported goods falling under chapter 71 through the commissionerates at ACC, Chennai, Jaipur, Bangalore, Mumbai and DPCC, Mumbai during January 2006 to September 2008 and claimed exemption benefit under various notifications. We found that the exemption allowed was incorrect on account of misclassification of goods, proof of re-import not submitted and same goods were assessed at different rates. Short levy of duty of Rs. 96.65 lakh due to incorrect grant of duty exemption is recoverable in these cases.

CHAPTER V
USE OF BRAND NAME

Chapter note no. 13 of chapter 71 of the CET provides that the process of affixing or embossing trade name or brand name on articles of jewellery shall amount to 'manufacture' under heading 7113.

- An article of jewellery falling under chapter heading 7113, on which brand name or trade name is indelibly affixed or embossed is chargeable to central excise duty of two per cent ad-valorem and education cess of two per cent thereon.
- Chapter note no. 12 provides that, 'brand name' or 'trade name', whether registered or not, is a name or a mark, such as symbol, monogram or label which is used to indicate a connection, in the course of trade, between a product and some person using the name or mark with or without indicating the identity of that person.
- The Board clarified that the scope of levy was only with respect to jewellery marketed and sold under such brand names as clearly understood in the trade like 'Tanishq', 'Sangini' etc.
- It was also clarified that advertising and selling of products under a brand name and also putting the same brand name or an abbreviation thereof or a mark which has a connection with such brand name on the article of jewellery would be liable to duty.

We found that two manufacturers of branded jewellery embossed abbreviations on their products and did not pay excise duty of Rs. 63.97 crore on the plea that they were not embossing their brand names on the product. The cases are detailed below.

5.1 Brand name 'Tanishq'

The well known branded jewellery, 'Tanishq' is manufactured by M/s Titan Industries Limited, Jewellery Division, Hosur (Chennai III CE commissionerate). It imports gold bars and also procures gold from RBI nominated agencies and thereafter manufactures and clears gold jewellery. It advertised and marketed its products under the registered brand name 'Tanishq', embossed it on the jewellery and paid duty at two per cent ad-valorem for clearances made upto June 2006. From July 2006, the unit stopped paying duty on the plea that it had discontinued embossing the brand name.

We found that the assessee continued to advertise and market its products under the same brand name. It replaced the emboss of 'Tanishq' with a mark 'Q', and continued to sell the jewellery through the showrooms of 'Tanishq'. The department did not take to steps to levy duty although the Board had clarified that embossing any mark which would indicate a connection between the product and a brand name i.e. Tanshiq, would render the product liable to duty. All cases prior to April 2008 have now become time-barred and the non

payment of duty for the period from September 2005 to March 2008 has resulted in loss of revenue of Rs. 53.65 crore including education cess.

On the matter being pointed out (January and February 2009), the department stated (February 2009) that the assessee had stopped embossing their brand name and instead started embossing the letter 'Q' in order to identify the goods. Therefore, the exemption availed was in order. It added (March 2009) that a protective SCN was issued in March 2009 demanding a duty of Rs. 49.83 crore for the period from September 2005 to December 2008.

The reply of the department is not tenable. The jewellery manufactured by the assessee is identified by the mark 'Q', which establishes a connection between the product and the assessee who is using that mark. Therefore, according to the clarification given by the Board, any jewellery with the mark 'Q' is connected to the brand name 'Tanishq' and liable to duty.

Moreover, while issuing the SCN, the department has verified that the assessee had sold the gold jewellery through their retail outlets 'Tanishq' with the outer packing showing the brand name 'Tanishq'.

5.2 Jewellery embossed with 'SCL'

M/s Surana Corporation Limited, falling under the jurisdiction of Chennai I CE commissionerate, manufactured and cleared gold jewellery through their showroom for domestic sales/trading. The unit imported gold and also procured from nominated agencies and traders in India. The jewellery was sold after embossing the abbreviated name of the manufacturer viz., 'SCL' which falls within the definition of 'Trade name/Brand name' as defined in the chapter notes. However, no excise duty was paid by the assessee on the pretext that this activity did not amount to manufacture.

In our opinion, the mark 'SCL' embossed on the jewellery fulfils the definition of a brand name because it establishes a connection with the user of the mark i.e. the Surana Group. Therefore, the product is branded jewellery and attracts duty at two per cent ad-valorem.

During the period 2005-06 to 2008-09 (upto September 2008), jewellery valued at Rs. 502.29 crore was manufactured and sold in the local market under the brand/trade name and the non-payment of excise duty worked out to Rs. 10.32 crore.

On the matter being pointed out (January and February 2009), the department did not accept our contention that embossing the abbreviated name 'SCL' brought the jewellers within the ambit of brand name/trade name as defined in chapter 71 and stated (February and April 2009) that identification code numbers like S1, S5, S9 etc., were written manually to identify the goldsmith.

The reply of the department is not consonant with the chapter notes and the clarification of the Board. Moreover, the website of the assessee clearly shows that the abbreviation 'SCL' is an integral part of the logo of the company and establishes a clear connection with the owner of the logo.

New Delhi	**(SUBIR MALLICK)**
Dated :	**Principal Director (Indirect Taxes)**

Countersigned

New Delhi	**(VINOD RAI)**
Dated :	**Comptroller and Auditor General of India**

Glossary of Terms and Abbreviations

Expanded form	Abbreviated form
Air Cargo Complex	ACC
Annual Performance Report	APR
Bank Realisation Certificate	BRC
Bill of Entry	BE
Central Board of Excise and Customs	Board or CBEC
Central Excise	CE
Central Excise Tariff	CET
Chartered Accountant	CA
Cost Insurance Freight	CIF
Customs Tariff Act, 1975	CTA
Customs Tariff Heading	CTH
Development Commissioner	DC
Diamond Plaza Customs Clearance Centre	DPCC
Director General of Foreign Trade	DGFT
Directorate General of Valuation (),	DGOV
Domestic Tariff Area	DTA
Duty Free Import Authorisation	DFIA
Duty Free Replenishment Certificate	DFRC
Export Obligation	EO
Export Oriented Unit	EOU
Export Promotion Capital Goods	EPCG
Foreign Trade (Development and Regulation), Act, 1992	FT (D&R) Act, 1992
Foreign Trade Policy	FTP
Free on Board	FOB
Gems and Jewellery Export Promotion Council	GJEPC
Gross Domestic Production	GDP
Hand Book of Procedures	HBP
Indian Customs Electronic Data Interchange System	ICES
Inland Container Depot	ICD
Legal Undertaking	LUT
Letter of Approval	LOA
Letter of Permission	LOP
Limited	Ltd.

Minerals and Metals Trading Corporation	MMTC
Ministry of Commerce and Industries	MOCI
Ministry of Finance	MOF
Net Foreign Exchange	NFE
New Custom House	NCH
Private	Pvt.
Quarterly Performance Report	QPR
Regional Licensing Authorities	RLAs
Reserve Bank of India	RBI
Risk Management System	RMS
Shipping Bills	SBs
Show Cause-cum-Demand Notice/Show Cause Notice	SCN
Small Scale Industry	SSI
Special Economic Zone	SEZ
Special Valuation Branch	SVB
Value Addition	VA

Export Promotion Schemes	
EOUs: Export Oriented Units	Units which undertake to export their entire production of goods and services.
EPCG: Export Promotion Capital Goods Scheme	Allows import of capital goods at concessional rate of duty against certain level of export obligation over a period of time.
DFRC: Duty Free Replenishment Certificate	Allows duty free import of inputs for exports.
DFIA: Duty Free Import Authorisation	Allows duty free import of inputs for exports.
SEZ: Special Economic Zone	A designated duty free enclave for manufacturing of goods/rendering of services to provide an internationally competitive environment for exports.